United States Government Accountability Office

GAO

Report to the Chairman, Subcommittee on Housing and Community Opportunity, Committee on Financial Services, House of Representatives

March 2005

# HOUSING FINANCE

# Options to Help Prevent Suspensions of FHA and RHS Loan Guarantee Programs

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GAO-05-227

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# Highlights

Highlights of GAO-05-227, a report to the Chairman, Subcommittee on Housing and Community Opportunity, Committee on Financial Services, House of Representatives

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# Options to Help Prevent Suspensions of FHA and RHS Loan Guarantee Programs

## Why GAO Did This Study

In fiscal year 2004, the Department of Housing and Urban Development's Federal Housing Administration (FHA) and the Department of Agriculture's Rural Housing Service (RHS) guaranteed approximately $136 billion in mortgages for single-family homes, multifamily rental housing, and healthcare facilities under a variety of programs. In past years, both agencies have occasionally had to suspend the issuance of guarantees under some programs when they exhausted the dollar amounts of their commitment authority (which serves as a limit on the volume of new loans that an agency can guarantee) or credit subsidy budget authority (the authority to cover the long-term costs—known as credit subsidy costs—of extending these guarantees) before the end of a fiscal year. These suspensions can be disruptive to homebuyers, developers, and lenders. GAO was asked to determine (1) how often and why FHA and RHS have suspended their loan guarantee programs over the last decade, (2) how these agencies manage and notify Congress of the rate at which the authorities for these programs will be exhausted, and (3) options Congress and the agencies could exercise to help prevent future suspensions and the potential implications of these options.

www.gao.gov/cgi-bin/getrpt?GAO-05-227.

To view the full product, including the scope and methodology, click on the link above. For more information, contact David G. Wood at (202) 512-8678 or woodd@gao.gov.

## What GAO Found

On 10 occasions since 1994, FHA and RHS have suspended the issuance of loan guarantees after exhausting the commitment authority or credit subsidy budget authority for certain programs before the end of a fiscal year. Specifically, FHA suspended several programs six times and RHS suspended one program four times. The resources budgeted for these programs have not always been adequate to keep them operating for a full fiscal year due partly to difficulties in estimating demand for loan guarantees—a difficulty compounded by the process of preparing the budget request to Congress, which requires that the agencies forecast demand nearly 2 years in advance.

FHA and RHS both manage their programs on a first-come, first-served basis, a factor limiting their ability to control the rate at which they use commitment authority and obligate budget authority. However, the agencies have different requirements and approaches for estimating the rate at which they will exhaust these authorities and notifying Congress. For example, unlike RHS, FHA is statutorily required to notify Congress when it has used 75 percent of its commitment authority and when it estimates that it will exhaust this authority before the end of a fiscal year. GAO's analysis indicates that FHA's basic approach for making estimates—applying utilization rates experienced up until the time of the analysis to the remainder of the fiscal year—does not always accurately forecast whether the agency will exhaust its commitment authority. However, FHA officials and federal budget experts said that more complex methods would not necessarily produce better estimates.

Through discussions with federal agency and mortgage industry officials, GAO identified several options that Congress, FHA, and RHS could exercise to help prevent future suspensions; however, the options would also have budgetary impacts (such as increasing the budget deficit), make oversight of the programs more difficult, or impose additional administrative burdens on the agencies. For example, Congress could require FHA to provide more frequent notifications about the percentage of commitment authority the agency has used and expand this requirement to include obligations of credit subsidy budget authority. This option, which could also be applied to RHS, could give Congress additional and more timely information to consider whether to provide supplemental appropriations before the end of a fiscal year. Other options for Congress include (1) authorizing FHA to use revenues generated by some of its loan guarantee programs to cover any shortfalls in budget authority for others and (2) providing "advance funding"—budget authority made available in an appropriation act for the current fiscal year that comes from a subsequent year's appropriation—for FHA and RHS program credit subsidy costs. Further, FHA and RHS can continue to use or be given additional administrative tools—such as transferring budget authority—to help delay or prevent program suspensions.

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## Abbreviations

| | |
|---|---|
| CA | commitment authority |
| CBO | Congressional Budget Office |
| CMHI | Cooperative Management Housing Insurance |
| CSBA | credit subsidy budget authority |
| FHA | Federal Housing Administration |
| GI | General Insurance |
| HUD | Department of Housing and Urban Development |
| MMI | Mutual Mortgage Insurance |
| OMB | Office of Management and Budget |
| RHIF | Rural Housing Insurance fund |
| RHS | Rural Housing Service |
| SRI | Special Risk Insurance |
| USDA | United States Department of Agriculture |

**United States Government Accountability Office**
**Washington, D.C. 20548**

March 15, 2005

The Honorable Robert W. Ney
Chairman
Subcommittee on Housing and
Community Opportunity
Committee on Financial Services
House of Representatives

Dear Mr. Chairman:

The Department of Housing and Urban Development's (HUD) Federal Housing Administration (FHA) and the Department of Agriculture's (USDA) Rural Housing Service (RHS) administer loan guarantee programs aimed at expanding access to mortgage financing for single-family homes and facilitating the construction, purchase, and rehabilitation of multifamily rental housing and healthcare facilities.[1] These programs do not lend money directly to borrowers; instead, the federal government guarantees loans made by FHA- or RHS-approved lenders. Both agencies have periodically had to suspend the issuance of guarantees under some of these programs when they exhausted the programs' budgets before the end of a fiscal year. For example, in fiscal year 2001 FHA had to suspend its Section 221(d)(3) loan guarantee program for nonprofit multifamily housing developers because of unexpectedly high demand.[2] These suspensions can be disruptive to homebuyers, developers, and lenders because they can delay, complicate, or result in the cancellation of important financial transactions.

FHA has four funds with which it guarantees mortgages. As of September 30, 2004, the four funds had guaranteed loans with a total estimated unpaid principal balance of almost $513 billion. For budget and accounting purposes, these funds are grouped into two accounts—the Mutual Mortgage Insurance and Cooperative Management Housing

[1]A loan guarantee is a commitment by the federal government to pay part or all of a loan's principal and interest to a lender if the borrower defaults. In contrast to RHS, FHA uses the term "mortgage insurance" instead of "loan guarantee." Because "insurance" and "guarantee" have the same meaning in the context of our review, we use the term "guarantee" throughout this report.

[2]See GAO, *Multifamily Housing Finance: Funding FHA's Subsidized Credit Programs*, GAO-02-323R (Washington, D.C.: Feb. 1, 2002).

Insurance (MMI/CMHI) account and the General Insurance and Special Risk Insurance (GI/SRI) account. The MMI/CMHI account supports FHA's largest single-family mortgage insurance program and a minor multifamily program. In contrast, the GI/SRI account supports a wide range of loan guarantee programs, including programs for healthcare facilities as well as multifamily and single-family housing. RHS has one fund—the Rural Housing Insurance fund (RHIF)—and a corresponding budget account under which it guarantees mortgages for one single-family program (Section 502) and one multifamily program (Section 538). As of September 30, 2004, this fund had guaranteed loans with a total estimated unpaid principal balance of almost $14 billion.

FHA and RHS loan guarantee programs are discretionary programs that operate within constraints established through the congressional appropriations process. In developing their annual budgets, the agencies must estimate the amount of "commitment authority" and, when applicable, credit subsidy budget authority required for their loan guarantee program accounts. Commitment authority serves as a limit on the total dollar volume of new loans that an agency can guarantee.[3] Credit subsidy budget authority is the authority to incur financial obligations to cover the long-term costs, known as credit subsidy costs, of extending these guarantees.[4] Credit subsidy costs can be negative (i.e., the present value of cash inflows exceeds the present value of cash outflows) or positive (i.e., the present value of cash inflows is less than the present value of cash outflows).

[3]Although "commitment authority" is not a standard budgetary term, we are using it for ease of presentation.

[4]The credit subsidy cost is the net present value of the estimated long-term costs to the federal government of extending or guaranteeing credit, calculated over the life of the loan and excluding administrative costs. The credit subsidy costs of each program are determined by calculating a credit subsidy rate that takes into account factors such as fees, defaults, and recoveries and applying this rate to the total dollar amount of loans the agency anticipates guaranteeing. Budget authority is the authority provided by law to enter into financial obligations that will result in immediate or future outlays involving federal funds. Before an agency guarantees any loans, the Federal Credit Reform Act of 1990 (codified at 2 U.S.C. § 661 – 661f) requires that an appropriation act provide in advance either (1) new budget authority to cover the credit subsidy costs or (2) a limitation on the use of funds that are otherwise available; or for authority to otherwise be provided in an appropriation act (2 U.S.C. § 661c(b)).

The Office of Management and Budget (OMB) reviews the agencies' estimates of loan commitment authority and credit subsidy budget authority before they are finalized and included in the President's Budget request to Congress. When FHA exhausts the commitment authority for either of its accounts, it must suspend issuance of additional loan guarantees for all programs under that account until Congress provides additional authority. For FHA's programs with a positive subsidy cost, the amount of credit subsidy budget authority Congress appropriates also limits the dollar volume of new loans the agencies may guarantee.[5] For example, $5 million in credit subsidy budget authority would cover the credit subsidy costs for up to $50 million in loan guarantees for a program with a 10 percent credit subsidy rate. RHS's programs—both of which currently have positive subsidy costs—are limited by the amount of credit subsidy budget authority they receive.[6] When FHA or RHS exhausts the budget authority for its programs with positive credit subsidy costs, the agency must suspend issuance of additional loan guarantees under those programs until Congress appropriates additional budget authority.

You requested that we review issues surrounding suspensions of FHA and RHS loan guarantee programs, including ways to prevent future suspensions. Accordingly, the objectives of our review were to determine (1) since fiscal year 1994 how often and why FHA and RHS have suspended the issuance of loan guarantees due to the exhaustion of commitment authority or credit subsidy budget authority before the end of a fiscal year; (2) how FHA and RHS manage, and notify Congress of, the rate at which they use commitment authority and obligate credit subsidy budget authority; and (3) options Congress, FHA, and RHS could exercise to help prevent future suspensions of loan guarantee programs and the potential implications of these options.

To meet these objectives, we reviewed laws, regulations, and guidance governing FHA's and RHS's loan guarantee programs. We reviewed information pertaining to the agencies' suspensions of loan guarantee

[5]Only programs with positive subsidy costs require credit subsidy budget authority.

[6]For both RHS programs, the commitment authority limit is the amount of credit subsidy budget authority divided by the credit subsidy rate. RHS manages the programs on the basis of credit subsidy budget authority. The Secretary of Agriculture has limited authority to transfer budget authority from one program to another, including RHS's loan guarantee programs (7 U.S.C. § 2257). Such transfers provide RHS with additional appropriated funds to cover the credit subsidy costs of additional loan guarantees, and also proportionally increase the commitment authority limit.

programs from fiscal years 1994 through 2004. We also performed a detailed analysis of FHA monthly budget and accounting data for fiscal years 2003 and 2004. We assessed the reliability of these data and found them sufficiently reliable for the purposes of our report. In addition, we interviewed officials from FHA and RHS headquarters, OMB, the Congressional Budget Office (CBO), and housing industry groups. We conducted our work in Washington, D.C., from January 2004 through January 2005 in accordance with generally accepted government auditing standards. Our scope and methodology are discussed in greater detail in appendix I.

## Results in Brief

On 10 occasions since 1994, FHA and RHS have suspended the issuance of loan guarantees under certain programs due to the exhaustion of commitment authority or credit subsidy budget authority before the end of a fiscal year. FHA suspended the programs under its General Insurance and Special Risk Insurance account three times due to the exhaustion of credit subsidy budget authority and three times due to the exhaustion of commitment authority—most recently in January 2004. Similarly, RHS suspended its Section 502 loan guarantee program for single-family homes four times due to exhaustion of credit subsidy budget authority—most recently in August 2004. The resources budgeted for these programs have not always reflected the amounts required to keep them operating for a full fiscal year due partly to difficulties in estimating the demand for loan guarantee programs. These difficulties include the need to make budget estimates nearly 2 years in advance and fluctuations in mortgage interest rates that lead to unanticipated changes in the demand for loan guarantees. In addition, the agencies' appropriations do not always reflect estimates of program demand because of resource constraints and competing priorities within the federal budget.

FHA and RHS manage their loan guarantee programs in a similar manner but have different requirements and approaches for estimating and notifying Congress of the rates at which they use commitment authority and obligate budget authority. FHA and RHS basically manage their loan guarantee programs on a first-come, first-served basis, a factor limiting both agencies' ability to control the rate at which they use commitment authority and obligate credit subsidy budget authority. FHA is statutorily required to estimate, at least monthly, the rate at which it will use commitment authority for the remainder of any fiscal year and notify Congress (1) if an estimate indicates that the agency will exhaust its commitment authority before the end of a fiscal year or (2) when 75 percent of the authority has been used. FHA has recently complied with the 75 percent notification requirement but could not provide us with documentation of notifications prior to fiscal year 2003. Since the beginning of fiscal year 2004, FHA has also prepared daily estimates of commitment authority use and determined that none of the estimates indicated that it would exhaust its commitment authority before the end of a fiscal year. Our analysis indicates that FHA's basic approach for making estimates—applying utilization rates experienced up until the time of the analysis to the remainder of the fiscal year—does not always accurately forecast whether the agency will exhaust its commitment authority. However, FHA officials and federal budget experts said that more complex methods would not necessarily produce better estimates. FHA is not required to and does not estimate obligation rates for credit subsidy budget authority, but monitors its obligations on a daily basis. Although not subject to the same requirements as FHA, RHS estimates the rate at which it will obligate credit subsidy budget authority for its Section 502 and Section 538 programs and in recent years has notified Congress when the agency's estimates indicated that the Section 502 program would deplete its budget authority before the end of the fiscal year. Because RHS's estimation process for the Section 502 program is less formulaic and more reliant on staff judgment than FHA's, we could not replicate this approach to assess it.

Congress, FHA, and RHS could take several actions to help prevent the agencies' loan guarantee programs from exhausting commitment authority or credit subsidy budget authority before the end of a fiscal year, but some of these actions would have budgetary impacts (such as increasing the budget deficit), make oversight of the programs more difficult, or impose additional administrative burdens on the agencies. For example, Congress could

- require FHA to provide more frequent notifications about the percentage of commitment authority the agency has used and expand this requirement to include obligations of credit subsidy budget authority. This option, which could also be applied to RHS, could give Congress additional and more timely information to consider whether to provide supplemental appropriations before the end of a fiscal year.

- make FHA's commitment authority limit higher, thereby reducing the potential for program suspensions due to the exhaustion of this authority.

- combine the multifamily programs under FHA's General Insurance and Special Risk Insurance account for credit subsidy purposes, which, unless current credit subsidy rates and levels of program activity changed dramatically, would result in a single negative subsidy rate and thus eliminate the need for annual appropriations of credit subsidy budget authority. In addition, to maintain its current level of oversight, Congress would need to ensure that HUD continued providing the estimated cost of, and number of guarantees under, individual programs in its annual budget requests.
- authorize FHA to use negative subsidies generated by its General Insurance and Special Risk Insurance account programs as funding to cover any shortfalls in credit subsidy budget authority in its programs with positive credit subsidies, as proposed in legislation in 2001.
- provide "advance funding"—budget authority made available in an appropriations act for the current fiscal year that comes from a subsequent year's appropriation—for FHA and RHS credit subsidy costs.

Finally, FHA and RHS can continue to use or can be given additional administrative tools—such as transferring budget authority—to help delay or prevent program suspensions.

We are not making any recommendations in this report.

In written comments on a draft of this report, HUD agreed with our findings but cited specific difficulties with some of the options. USDA also agreed with our findings and provided technical comments, which we incorporated into this report as appropriate.

## Background

FHA and RHS operate a variety of loan guarantee programs, organized under three budget accounts, that support the financing of single-family and multifamily housing, as well as healthcare facilities (see fig. 1). The guarantees substantially reduce the financial risk for lenders in the event that borrowers default, thereby allowing lenders to make loans available to more borrowers. FHA and RHS loan guarantees for multifamily properties are often combined with other financing sources, such as low-income housing tax credits and tax-exempt bonds issued by states and localities.

**Figure 1: Major FHA and RHS Single-Family and Multifamily Loan Guarantee Programs, as of Fiscal Year 2004**

### Federal Housing Administration

**Mutual Mortgage Insurance and Cooperative Management Housing Insurance Account**

- Section 203(b) Single-family Housing
- Section 213 Cooperative Housing

**General Insurance and Special Risk Insurance Account**

**Major Multifamily and Health Care:**

- Section 221(d)(3) New Construction/Substantial Rehabilitation of Apartments with Nonprofit Sponsors
- Section 221(d)(4) New Construction/Substantial Rehabilitation of Apartments with For-profit Sponsors
- Section 223(a)(7) Refinancing of Apt. Primary Loans
- Section 232 Healthcare Facilities
- Section 232 Refinancing of Healthcare Facilities
- Section 241(a) Supplemental Loan Insurance

**Single-Family:**

- Section 203(k) Rehabilitation Mortgages
- Section 234 Condominiums
- Title I Property Improvements
- Title I Manufactured Housing
- Section 255 Home Equity Conversion Mortgage

### Rural Housing Service

**Rural Housing Insurance Fund**

- Section 502 Single-family housing
- Section 538 Multifamily housing

Sources: HUD and USDA.

FHA is the federal government's principal provider of mortgage loan guarantees and operates numerous loan guarantee programs. In fiscal year 2004, FHA guaranteed over $107 billion in loans under the MMI/CMHI account, the vast majority of which occurred within the 203(b) program. The 203(b) program provides loan guarantees for the purchase or refinancing of single-family homes.[7] The other program in the MMI/CMHI account is the Section 213 program, which guarantees mortgage loans to facilitate the construction, substantial rehabilitation, and purchase of cooperative housing projects. Because both programs currently have negative subsidy costs, neither requires credit subsidy budget authority. The MMI/CMHI account received $185 billion in commitment authority in fiscal year 2004. FHA's GI/SRI account, which received $29 billion in commitment authority in fiscal year 2004, supports an array of programs. These include programs that facilitate the development, construction, rehabilitation, purchase, and refinancing of multifamily apartments and healthcare facilities. For example, the 221(d)(4) program—FHA's largest multifamily program—guarantees loans to for-profit developers of multifamily apartments, and the 221(d)(3) program guarantees loans to nonprofit developers.[8] The GI/SRI account also includes several specialized single-family programs, such as the 203(k) (rehabilitation mortgage), Section 234 (condominiums), Title I (property improvement and manufactured housing), and Section 255 (home equity conversion mortgage) programs. In contrast to the MMI/CMHI account, several of the programs in the GI/SRI account have positive subsidy costs, which require credit subsidy budget authority. In fiscal year 2004, four GI/SRI account programs—Section 221(d)(3), Section 241, Multifamily Operating Loss, and Title I Property Improvement—received $15 million in credit subsidy budget authority.[9]

[7]HUD defines a single-family home as one containing from one to four living units. The 203(b) program and several other FHA single-family programs are open to borrowers of all income levels. However, because of its low down payment requirements (3 percent of a home's purchase price under the 203(b) program), FHA plays a major role in providing guarantees on loans to low-income families and first-time homebuyers.

[8]The other major multifamily programs under the GI/SRI account are Section 220 (construction or rehabilitation of rental housing for urban renewal and concentrated areas), Section 223(f) (refinancing or acquisition of existing rental housing), Section 232 (construction or substantial rehabilitation of nursing homes, intermediate care, board and care, and assisted living facilities), Section 232/223(f) (refinancing or acquisition of existing nursing homes, intermediate care, board and care, and assisted living facilities), and 241(a) (financing for repairs, additions, and improvements to multifamily rental housing and health care facilities with FHA-insured first mortgages or HUD-held mortgages).

[9]The number of programs that require credit subsidy budget authority and the amount of authority each program requires can vary from year to year. The credit subsidy rates that agencies use to prepare their annual budget estimates can change over time, especially as the programs or the methodology used to estimate subsidy rates change. For example, the rate for FHA's 221(d)(4) program decreased from 3.35 percent in fiscal year 2001 to negative 0.14 percent in fiscal year 2002 due primarily to FHA increasing the guarantee fee for this program.

RHS's loan guarantee programs, as a whole, are much smaller than FHA's, are targeted to rural areas, and have more income restrictions. Under its RHIF account, RHS guarantees loans through two programs—the Section 502 program and the Section 538 program. The Section 502 program serves rural residents with incomes not exceeding 115 percent of the U.S. median income who wish to purchase or refinance a single-family home.[10] In fiscal year 2004, this program received $2.7 billion in commitment authority and about $40 million in credit subsidy budget authority. The Section 538 program guarantees loans to nonprofit or for-profit developers for the construction, acquisition, and rehabilitation of multifamily rental housing in rural areas that serve households with incomes that do not exceed 115 percent of area median income. In fiscal year 2004, this program received $100 million in commitment authority and about $6 million in credit subsidy budget authority.

In formulating and executing the budgets for their loan guarantee programs, FHA and RHS must adhere to specific federal budgetary and accounting requirements. The process of preparing their annual budget request requires that FHA and RHS prepare estimates of the dollar amount of loans they anticipate guaranteeing nearly 2 years in advance. These estimates influence the amount of commitment authority and credit subsidy budget authority the agencies request and receive. The Federal Credit Reform Act of 1990 requires the President's Budget to reflect the costs of credit programs and include the planned level of new loan guarantees associated with each appropriation request.[11] Agencies therefore must calculate and estimate the long-term cost, known as the credit subsidy cost, to the federal government of extending or guaranteeing credit and the amount of new loan guarantees they plan on making. The agencies estimate these costs for each program by calculating a credit subsidy rate that takes into account factors such as fees, defaults, and recoveries, and applying this rate to the total dollar amount of loans they anticipate guaranteeing. When an agency decides to guarantee a loan, it uses this rate to determine the credit subsidy cost of doing so. Under programs requiring positive credit subsidies, the agency can issue the new guarantee only if the budget authority to cover this cost is available. In contrast, programs with negative subsidies are constrained only by

[10]RHS defines a single-family home as a property with one living unit.

[11]2 U.S.C. § 661c(a).

commitment authority, which limits the amount of financial risk the federal government assumes each year.

FHA and RHS receive their commitment authority limit and appropriations of credit subsidy budget authority on a somewhat different basis. Although FHA, as required, estimates its commitment authority and credit subsidy needs for each loan guarantee program under the MMI/CMHI and GI/SRI accounts, it requests and receives these authorities on an account, rather than a program, basis. Congress has generally not specified a level of commitment authority or credit subsidy budget authority for each program. In addition, FHA routinely requests and receives a commitment authority limit that exceeds the dollar amount of loans it has estimated it will make, a practice that helps prevent exhaustion of commitment authority before the end of a fiscal year. In contrast, RHS receives credit subsidy budget authority on a program basis. That is, the Section 502 program and Section 538 program receive separate appropriations of credit subsidy budget authority. For both of these programs, the commitment authority limit is the amount of credit subsidy budget authority divided by the credit subsidy rate.

## Difficulties in Estimating Demand Underlie FHA and RHS's 10 Suspensions of Loan Guarantee Programs Since 1994

On 10 occasions since 1994, FHA and RHS have suspended the issuance of loan guarantees under certain programs because the programs effectively exhausted their commitment authority or credit subsidy budget authority before the end of a fiscal year.[12] Specifically, FHA suspended programs six times and RHS four times. Several factors contributed to these suspensions, including unforeseeable fluctuations in mortgage interest rates that led to changes in the demand for loan guarantees. Further, the need to make budget estimates nearly 2 years in advance compounds the difficulty of predicting demand. As a result, and because of resource constraints and competing priorities within the federal budget, the resources appropriated for these programs have not always reflected the amounts required to keep them operating for an entire fiscal year.

[12]Completely exhausting its credit subsidy budget authority could cause an agency to violate the Anti-Deficiency Act. Among other things, the act states that an officer or employee of the United States government may not make or authorize an expenditure or obligation exceeding an amount available in an appropriation (31 U.S.C. § 1341). Therefore, the agencies suspend these programs before the balance of their budget authority reaches zero.

## FHA Suspended Guaranteed Loan Programs Six Times Over the Past Decade

As shown in table 1, FHA has suspended the issuance of loan guarantees under certain programs six times since 1994 after effectively exhausting the commitment authority or credit subsidy budget authority for these programs before the end of the fiscal year.[13] For example, from fiscal year 1994 through fiscal year 2004, FHA suspended the programs with positive subsidy costs under its GI/SRI account three times—in February 1994, July 2000, and April 2001—after effectively exhausting the credit subsidy budget authority under this account.[14]

**Table 1: Summary of FHA and RHS Suspensions, Fiscal Years 1994-2004**

| Date | What was suspended | Programs remained suspended until |
|---|---|---|
| **FHA** | | |
| February 1994[a] | GI/SRI programs with positive subsidy costs | OMB released the agency's third quarter allotment of credit subsidy budget authority in April 1994.[b] |
| July 26, 2000 | GI/SRI programs with positive subsidy costs | the start of the next fiscal year. |
| April 2001[a] | GI/SRI programs with positive subsidy costs | the start of the next fiscal year. |
| September 16, 2003 | All GI/SRI programs | Congress approved a $2 billion supplemental appropriations bill (Emergency Supplemental Appropriations Act, 2003, Pub. L. No. 108-83, Title III, § 3606, 117 Stat. 1038 (Sept. 30, 2003)) and enacted a continuing appropriation for fiscal year 2004 (Pub. L. No. 108-84, 117 Stat. 1042 (Sept. 30, 2003)). |
| December 2003[a] | All GI/SRI programs | Congress provided additional commitment authority in a subsequent continuing resolution (Pub. L. No. 108-185, 117 Stat. 2684 (Dec. 16, 2003)). |
| January 14, 2004 | All GI/SRI programs | Congress approved the Consolidated Appropriations Act, 2004 (Pub. L. No. 108-199, 118 Stat. 3 (Jan. 23, 2004)). |

[13] We use the phrases "suspended the issuance of loan guarantees" and "program suspension" interchangeably throughout the report.

[14] In contrast, FHA did not suspend the programs under its MMI/CMHI account during the period covered by our review. However, in fiscal year 2003, FHA determined that there was a possibility that it would exhaust the commitment authority for this account before the end of the year. In August 2003, to help address this situation, FHA permanently changed the recording of its loan commitments from a date earlier in the loan guarantee process to the date on which FHA actually guarantees the loans.

(Continued From Previous Page)

| Date | What was suspended | Programs remained suspended until |
|---|---|---|
| **RHS** | | |
| Fiscal year 1995[a] | Section 502 program | the start of the next fiscal year. |
| Fiscal year 1996[a] | Section 502 program | the start of the next fiscal year. |
| August 27, 2003 | Section 502 program | the start of the next fiscal year. |
| August 24, 2004 | Section 502 program | the start of the next fiscal year. |

Sources: FHA and RHS.

[a]The agencies were unable to provide us with more specific dates for these suspensions.

[b]In fiscal year 1994, OMB allotted FHA's credit subsidy budget authority on a quarterly basis.

FHA has also suspended all of the programs under the GI/SRI account three times after effectively exhausting the account's commitment authority. On September 16, 2003, FHA suspended the issuance of loan guarantees under the GI/SRI account until Congress raised the commitment authority limit in a supplemental appropriations act. The other two suspensions occurred while the agency was operating under a series of continuing resolutions in early fiscal year 2004.[15] The first suspension occurred in early December 2003, when FHA exhausted the $3.8 billion in commitment authority provided in the first of these resolutions. FHA lifted the suspension after receiving an additional $3.9 billion under a subsequent resolution in mid-December 2003 but suspended the programs again after exhausting this amount on January 14, 2004. FHA restarted the programs approximately 2 weeks later, after Congress passed the Consolidated Appropriations Act, 2004.[16]

[15]A continuing resolution provides temporary appropriations and can provide commitment authority to continue the operation of federal agencies and programs if the agencies' annual appropriations bills have not been enacted.

[16]Pub. L. No. 108-199, 118 Stat. 3 (Jan. 23, 2004).

## RHS Suspended Its Section 502 Program Four Times during the Past Decade

RHS has suspended its Section 502 program four times since 1994—in fiscal years 1995, 1996, 2003, and 2004—after effectively exhausting its credit subsidy budget authority.[17] However, in some cases, RHS was able to take actions that delayed or mitigated the impact of the suspensions on borrowers and lenders. For example, in early August 2003, RHS transferred $3.6 million in budget authority from the Section 523 (Mutual and Self-help Technical Assistance) grant program to the Section 502 program in order to delay suspension of the program.[18] This transfer enabled the Section 502 program to guarantee an additional $297 million in loans and delayed suspension of the program until August 27. Also, during the 4-week suspension period, RHS continued to accept and approve loan guarantee applications submitted by lenders and committed to issuing the guarantees as soon as it received its next appropriation. Further, in March 2004, RHS anticipated that the Section 502 program would exhaust its credit subsidy budget authority early in the fourth quarter. In June, RHS increased the program's guarantee fee and transferred a total of $7 million in budget authority from the Section 504 (Natural Disaster), 514 (Farm Labor Housing), 515 (Multifamily Housing), 516 (Rural Housing Assistance), and 538 programs to the Section 502 program.[19] The increase in the guarantee fee enabled RHS to issue an additional $100 million in loan guarantees, and the transfers enabled RHS to issue an additional $531 million in loan guarantees. Although these actions delayed suspension of the program, RHS eventually had to suspend the program on August 24, 2004. During this suspension period, RHS again accepted and approved loan guarantee

[17] In contrast, RHS did not suspend its Section 538 program before the end of a fiscal year during the period covered by our review. However, according to RHS officials, the program has never received appropriations—and therefore has not issued loan guarantees—during the first quarter of a fiscal year. This has occurred because since the program's inception in 1996, the federal government has operated in the beginning of each fiscal year under continuing resolutions, which appropriate budget authority based on appropriations received in the first quarter of the previous year (zero in the case of the Section 538 program).

[18] The Secretary of Agriculture has the authority under 7 U.S.C. § 2257 to transfer up to 7 percent of the budget authority appropriated for any program to another (subject to the availability of budget authority in the former program). The Secretary of HUD does not have similar authority.

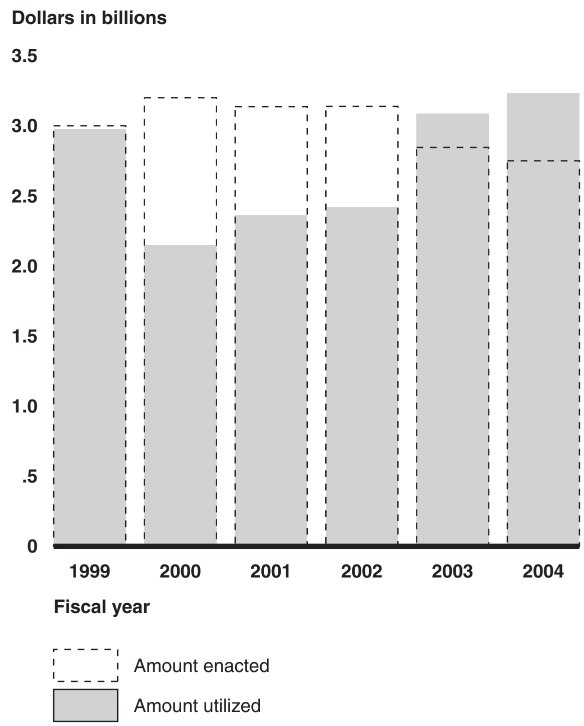
[19] A guarantee fee is paid by the borrower as part of the cost of securing the loan guarantee. Before fiscal year 2005, RHS was permitted to increase or decrease the guarantee fee throughout the year, subject to statutory limitations. The fiscal year 2005 appropriations act required that the fee be set at 2 percent, and therefore RHS currently does not have administrative flexibility to change the fee.

applications submitted by lenders and committed to issuing the guarantees as soon as it received its next appropriation.

## Difficulties in Estimating Program Demand Contributed to the Exhaustion of Commitment and Budget Authority before the End of a Fiscal Year

Due partly to difficulties in estimating the demand for loan guarantee programs, the resources budgeted for these programs have not always reflected the amounts required to keep them operating for a full fiscal year. Estimating demand for budget purposes is difficult for several reasons. A primary reason is that demand for loan guarantees is highly responsive to interest rates, which are volatile and difficult to forecast. For example, due in part to the decline in mortgage interest rates in fiscal year 2003, the number of FHA single-family refinancing loans was 60 percent higher than in fiscal year 2002. According to FHA officials, they could not have anticipated the interest rate change or reflected it in their fiscal year 2003 budget. As a result, FHA used its commitment authority faster than anticipated and effectively exhausted the authority for the GI/SRI account 2 weeks before the end of the fiscal year. Similarly, according to RHS officials, low interest rates in fiscal year 2003 resulted in significantly higher demand for Section 502 loan guarantees (and a corresponding increase in the use of commitment authority) compared with the previous 3 years (see fig. 2). Because RHS based its fiscal year 2003 budget estimate primarily on actual demand levels from these prior years, the amount the agency requested and was appropriated for the Section 502 program was not adequate to fund the program for the entire fiscal year, resulting in suspension of the program in late August 2003.

Figure 2: Amount of Commitment Authority Enacted and Used for RHS's Section 502 Program, Fiscal Years 1999–2004




Source: RHS.

In addition, FHA and RHS have implemented program and policy changes that were not foreseen or whose specific effects could not be known at the time the agencies developed their budgets. For example, in response to a statutory change that occurred after HUD submitted its fiscal year 2004 budget request, FHA increased its individual loan limits for multifamily housing in high-cost areas during the second and third quarters of fiscal year 2004.[20] FHA officials told us that while they expected that these changes would result in higher utilization of commitment authority, they could not have factored them into the department's budget request. Additionally, in the beginning of fiscal year 2003—well after federal

[20]The FHA Multifamily Loan Limit Adjustment Act of 2003 (Pub. L. No. 108-186, Title III, § 302, 117 Stat. 2692 (Dec. 16, 2003)) increased the maximum mortgage amount for individual FHA-insured mortgages for multifamily housing located in high-cost areas.

agencies had developed their budgets for that year—the administration established a goal to increase the number of minority homeowners by at least 5.5 million families by 2010. To help achieve this goal, RHS, among other things, lowered its guarantee fee, conducted outreach with minority lenders, and promoted credit counseling and homeownership education. According to RHS, these actions helped increase loan volume under the Section 502 program to an historic high but could not have been taken into account in preparing the agency's fiscal year 2003 budget.

Compounding the difficulty in predicting demand is the federal budget process, which requires that FHA and RHS submit to OMB estimates of the dollar amount they anticipate guaranteeing in a given year nearly 2 years in advance. The agencies' estimates influence the amount of commitment authority and credit subsidy budget authority the agencies request and receive through the budget process. Because these estimates are prepared so far in advance, they cannot be made with a high level of certainty. Further, the agencies' appropriations do not always reflect estimates of program demand because of resource constraints and competing priorities within the federal budget.

## FHA and RHS Manage Their Programs in a Similar Manner but Estimate and Notify Congress of the Rate at Which They Will Exhaust Commitment and Budget Authority Differently

FHA and RHS basically manage their loan guarantee programs on a first-come, first-served basis, a factor limiting both agencies' ability to control the rate at which they use commitment authority and obligate credit subsidy budget authority. FHA is required to estimate, at least monthly, the rate at which it will use commitment authority for the remainder of any fiscal year and notify Congress (1) if an estimate indicates that the agency will exhaust its commitment authority before the end of a fiscal year or (2) when 75 percent of the authority has been used.[21] FHA has recently complied with the 75 percent notification requirement, but could not provide us with documentation of notifications prior to fiscal year 2003. FHA has also prepared the estimates on a daily basis since the beginning of fiscal year 2004 and determined that none of the estimates indicated that it would exhaust its commitment authority before the end of a fiscal year. Our analysis indicates that FHA's basic approach for making estimates does not always accurately forecast whether the agency will exhaust its commitment authority; however, FHA officials and federal budget experts said that more complex methods would not necessarily produce better

[21] 12 U.S.C. § 1721 note.

estimates. Although not subject to the same requirements as FHA, RHS periodically estimates the rate at which it will obligate credit subsidy budget authority for its Section 502 and Section 538 programs and in recent years has notified Congress when the agency's estimates indicated that the Section 502 program would deplete its budget authority before the end of the fiscal year.

## FHA and RHS Manage Their Loan Guarantee Programs on a First-Come, First-Served Basis

FHA and RHS basically manage their loan guarantee programs on a first-come, first-served basis, a factor that limits control over the rate at which they use commitment authority and obligate credit subsidy budget authority. More specifically, according to FHA and RHS officials, neither agency prioritizes or rejects eligible applications as long as sufficient commitment and budget authority are available because they have determined that, with few exceptions, they lack the authority to do so.[22] The agencies do not, for example, try to reduce their utilization or obligation rates by placing a higher priority on smaller loans than larger loans. FHA officials told us that even if they had this authority, they would not want to be in the position of judging whether loans under one program should be guaranteed before loans under another program or choosing between eligible loans under the same program. Consequently, all FHA programs (those with positive and negative subsidy costs) under the same account provide loan guarantees until the account's commitment authority is exhausted, or, for programs with positive subsidy costs, until either the account's commitment authority or credit subsidy budget authority is exhausted.

FHA and RHS implement the first-come, first-served approach somewhat differently. Although FHA makes loan guarantees through its single-family and multifamily housing field offices, it does not allocate commitment authority and credit subsidy budget authority to these offices in advance of using and obligating the authorities. In contrast, under its Section 502 program, RHS first allocates the budget authority to its state offices based on a formula. Each state office then obligates the budget authority on a first-come, first-served basis. RHS also maintains a central reserve that can

[22]For its Section 502 program, RHS gives preference to first-time homebuyers or veterans, their spouses, or children of deceased veterans when there is a shortage of budget authority and there is more than one request for a loan guarantee (see 7 C.F.R. § 1980.353). For its Section 538 program, RHS gives priority to projects in smaller rural communities, in the neediest communities, or located in Empowerment Zones/Enterprise Communities or on tribal lands (see 7 C.F.R. § 3565.5).

be used to supplement funding to state offices that run out of budget authority before the end of the fiscal year. In addition, RHS may redistribute budget authority from state offices that have more than necessary to state offices with shortfalls. For its Section 538 program, RHS obligates budget authority on a first-come, first-served basis without first allocating the funds to its state offices. Appendix II provides additional information on FHA's and RHS's processes for making loan guarantees.

## FHA Has Specific Estimation and Notification Requirements for Utilization of Commitment Authority and Relies Primarily on a Straightforward Estimation Process to Satisfy These Requirements

FHA is required by statute to estimate, on at least a monthly basis, the rate at which it will use commitment authority for the remainder of the fiscal year and to notify Congress (1) when 75 percent of the authority has been used or (2) if estimates indicate that the authority will be exhausted before the end of the year. These notifications help Congress to determine whether supplemental authority may be needed to prevent a suspension of the programs due to the exhaustion of commitment authority. These requirements do not pertain to FHA's credit subsidy budget authority.

To determine when it has reached the 75 percent level, FHA continuously monitors the amount of commitment authority used under its loan guarantee programs. FHA currently relies on several unintegrated data systems to monitor its authority balances. An FHA official receives end-of-day activity reports from all guaranteed lending programs on commitment authority utilization and credit subsidy budget authority obligations and manually enters the data into a spreadsheet on a daily basis. By the end of calendar year 2006, FHA expects to complete the implementation of a new subsidiary ledger accounting system that, according to FHA officials, will replace the spreadsheet and provide them with real-time utilization and obligation data.

Although FHA notified Congress, as required, when it had used 75 percent of its commitment authority in fiscal years 2003 and 2004, it could not provide us with documentation of notifications prior to fiscal year 2003. Specifically:

- In June 2003, FHA notified Congress that it had used 75 percent of the commitment authority under the MMI/CMHI account and that it anticipated using 75 percent of the commitment authority under the GI/SRI account within a few weeks.

- In January 2004, FHA notified Congress that while it did not anticipate exhausting the commitment authority provided under a continuing resolution, it had used 75 percent of the commitment authority under the MMI/CMHI account.

- In July 2004, FHA notified Congress that the agency estimated it would use 75 percent of the commitment authority under the GI/SRI account within a few weeks and that while the utilization rate was slightly lower than the rate necessary to exhaust the commitment authority before the end of the fiscal year, there was a possibility of a shortfall.

FHA has estimated the rates of future use of commitment authority on a daily basis since fiscal year 2004, essentially using a "straight-line" method that applies the utilization rate experienced up until the time of the analysis to the remainder of the fiscal year.[23] To supplement the straight-line estimates, FHA officials indicated that they also use their judgment and experience to factor in market and economic variables, such as interest rates. Although FHA provided us with examples of its straight-line estimates, it did not maintain records of its more comprehensive estimates, which incorporated judgments about these other variables. FHA officials told us that none of these more comprehensive estimates made after the agency had received its fiscal year 2004 appropriation clearly indicated that either the MMI/CMHI or the GI/SRI account would exhaust its commitment authority before the end of the fiscal year.[24] The officials said that they do not make similar estimates of obligation rates for credit subsidy budget authority but indicated that they monitor actual obligations on a daily basis and monitor anticipated obligations by periodically querying the FHA field offices that process loan guarantees.

Although a straight-line estimation analysis has its limitations, FHA officials told us they do not believe that a more complex method for making estimates—one that might systematically account for the effects of additional variables—would necessarily result in more accurate estimates because of the inherent unpredictability of the demand for loans. They also said that it would be difficult to develop such a method. Officials from OMB, CBO, and housing industry groups agreed that it is difficult to

[23]FHA officials told us that prior to fiscal year 2004, they made estimates using a similar method but on a less frequent basis. FHA could not provide us with documentation of these estimates.

[24]As noted previously, FHA operated under a series of continuing resolutions for almost the first 4 months of fiscal year 2004.

estimate the rate at which commitment authority will be used and that a more complex method may not yield better estimates.

While FHA maintains data on its utilization of commitment authority, it could not provide us with complete records of its straight-line estimates. In the absence of these estimates, we analyzed FHA's data on commitment authority utilization and found that a basic straight-line method cannot always accurately predict whether the agency will exhaust its commitment authority before the end of a fiscal year.[25] As shown in table 2, by the end of March 2003—halfway through the fiscal year—FHA had used less than half of its commitment authority (45.5 percent) under the GI/SRI account. Assuming the same utilization rate for the second half of the year (i.e., 45.5 percent over 6 months), we estimated that FHA would have used 91 percent of its commitment authority by the end of the fiscal year. However, in actuality, FHA used 91 percent of its commitment authority by the end of August—earlier than it might have estimated based on a straight-line analysis—and was forced to suspend the issuance of loan guarantees under this account in the middle of September. Even if FHA had conducted this analysis at the end of June, it would have estimated that it would use less than 100 percent of its commitment authority by the end of the fiscal year.

[25]Because FHA does not have a systematic process for taking other variables into account, we performed this analysis assuming that the agency would use commitment authority for the remainder of the fiscal year at the same rate experienced previously in the year, without considering other variables.

**Table 2: Actual and Straight-Line Estimated Commitment Authority Utilization under FHA's GI/SRI Account, Fiscal Year 2003**

| | 1st Quarter | | | 2nd Quarter | | | 3rd Quarter | | | 4th Quarter | | |
|---|---|---|---|---|---|---|---|---|---|---|---|---|
| | Oct. | Nov. | Dec. | Jan. | Feb. | Mar. | Apr. | May | June | July | Aug. | Sept. |
| Actual cumulative percentage of commitment authority used at month end | 4.4 | 7.9 | 22.1 | 30.0 | 37.4 | 45.5 | 54.5 | 64.5 | 72.8 | 80.7 | 91.0 | 104.0 |
| Projected percentage of commitment authority used at fiscal year end (straight-line estimates based on above) | 52.7 | 47.4 | 88.4 | 90.0 | 89.7 | 91.0 | 93.4 | 96.8 | 97.0 | 96.9 | 99.2 | N/A |

Source: GAO analysis of FHA data.

Note: In early fiscal year 2003, FHA operated under a series of continuing resolutions that gave the agency sufficient commitment authority to operate its loan guarantee programs until it received the $23 billion in commitment authority that was provided in the Consolidated Appropriations Resolution, 2003 (Pub. L. No. 108-7, 117 Stat. 11, 496 (Feb. 20, 2003)). However, for our purposes, we calculated the utilization rates and projections for October through June as if FHA had received the $23 billion at the beginning of the fiscal year. FHA used 104 percent of this $23 billion in commitment authority after Congress raised the commitment authority limit in a supplemental appropriations act on September 30, 2003, which allowed FHA to issue additional loan guarantees up to $25 billion under its GI/SRI account.

Further, as shown in table 3, straight-line calculations can also overestimate utilization. Specifically, an analysis conducted at the end of March 2004, when FHA had used 52.5 percent of the commitment authority under the GI/SRI account, would have projected that FHA would exhaust the authority before the end of the fiscal year and that almost 105 percent of its commitment authority would be needed in order to prevent a suspension. However, FHA actually used only 95.2 percent of its total commitment authority by the end of the fiscal year.

**Table 3: Actual and Straight-Line Estimated Commitment Authority Utilization under FHA's GI/SRI Account, Fiscal Year 2004**

| | 1st Quarter | | | 2nd Quarter | | | 3rd Quarter | | | 4th Quarter | | |
|---|---|---|---|---|---|---|---|---|---|---|---|---|
| | Oct. | Nov. | Dec. | Jan. | Feb. | Mar. | Apr. | May | June | July | Aug. | Sept. |
| Actual cumulative percentage of commitment authority used at month end | 9.9 | 19.0 | 24.8 | 33.0 | 41.6 | 52.5 | 57.3 | 64.2 | 71.5 | 78.2 | 85.9 | 95.2 |
| Projected percentage of commitment authority used at fiscal year end (straight-line estimates based on above) | 118.2 | 113.8 | 99.3 | 99.0 | 99.9 | 104.9 | 98.2 | 96.3 | 95.3 | 93.8 | 93.7 | N/A |

Source: GAO analysis of FHA data.

Note: In early fiscal year 2004, FHA operated under a series of continuing resolutions that provided $7.6 billion in commitment authority. However, for our purposes, we calculated the utilization rates and projections for October through July as if FHA had received the $25 billion in commitment authority that was provided in the Consolidated Appropriations Act, 2004, at the beginning of the fiscal year. On August 9, 2004, Congress provided an additional $4 billion in commitment authority. (Pub. L. No. 108-301, 118 Stat. 1102 (Aug. 9, 2004)). The table does not reflect this increase.

Variations in utilization rates are a fundamental reason why FHA faces difficulty in estimating its use of commitment authority for the entire year. For example, in fiscal year 2003, FHA's monthly utilization rates ranged from 3.5 percent in November to 14.2 percent in December. In addition, the widely varying size of multifamily projects adds to the difficulty in projecting volume, and a single large project can significantly change a utilization rate.

## RHS Does Not Have Estimation and Notification Requirements but Has Relied on a Complex Estimation Process to Notify Congress of the Rate at Which it Obligates Budget Authority

Although not subject to the same requirements as FHA, RHS, as a matter of policy, monitors its obligations of credit subsidy budget authority on a daily basis and has recently notified Congress when it appeared that its Section 502 program would exhaust its credit subsidy budget authority before the end of a fiscal year.[26] In August 2003, RHS notified Congress that credit subsidy budget authority for the Section 502 program would soon be exhausted and that the agency was exercising its authority to transfer budget authority between programs to help cover the expected shortfall. Similarly, in early 2004, RHS officials notified Congress that credit subsidy budget authority for the Section 502 program might be exhausted by July 2004 because of a strong demand for housing that would most likely remain constant or increase. Then, in June 2004, RHS notified Congress that credit subsidy budget authority for the Section 502 program would be exhausted early in the fourth quarter and that in order to continue guaranteeing loans, RHS would (1) increase the guarantee fee—effectively decreasing the subsidy rate and allowing the agency to guarantee more loans—and (2) exercise its authority to transfer budget authority. In contrast, RHS officials told us that in August 2004 they estimated that the Section 538 program would exhaust its credit subsidy budget authority by September 15, but did not notify Congress of this situation. However, the program was able to operate until the end of the fiscal year.

In contrast to FHA, RHS's estimation process is less formulaic, more reliant on staff judgment, and performed less frequently. To estimate when the Section 502 program may exhaust its budget authority, RHS officials told us they analyze obligation data and external variables at least monthly. RHS officials explained that, depending on current program performance and time elapsed into the fiscal year, they may base the estimate on obligation rates from a specific prior year or an average of several prior years and on differences in obligations from the previous year(s) to the current year. RHS officials emphasized that they also use their experience and judgment to incorporate market and economic information, such as interest rates and data on new housing starts, into formulating the estimates. Because RHS's estimation process (1) can differ from one estimate to another, (2) relies heavily on program officials' interpretations of external variables, and (3) does not include documentation of all the data used and assumptions made in reaching the estimates, we could not replicate this

[26] In contrast to FHA, RHS has a single accounting system to monitor obligations of credit subsidy budget authority for both of its programs.

process to assess it. However, RHS provided us the results of an estimate from April 2004, which accurately predicted that the Section 502 program would exhaust its budget authority before the end of the fiscal year.

Because RHS's Section 538 program is relatively small—it guaranteed 42 loans in fiscal year 2003—RHS officials told us they are able to estimate whether the credit subsidy budget authority for the program will be sufficient for the entire fiscal year by surveying RHS's state offices and participating lenders about anticipated demand for loan guarantees.

## Congress, FHA, and RHS Could Exercise Options to Help Prevent Suspensions, but Options Would Have Other Implications

Through discussions with FHA, RHS, OMB, CBO, and housing industry officials, and a review of relevant literature, we identified options—some of which would require statutory changes—that could provide better warning of future suspensions of loan guarantee programs or help prevent them altogether. For example, by requiring FHA to provide more frequent notifications concerning its commitment authority balances and creating notification requirements for FHA and RHS concerning their balances of credit subsidy budget authority, Congress could gain additional and more timely information to consider whether supplemental appropriations would be needed to prevent program suspensions. Congress could also provide FHA higher annual limits on commitment authority to minimize the likelihood that the agency would exhaust this authority before the end of a fiscal year. To help prevent program suspensions due to the exhaustion of credit subsidy budget authority, Congress could (1) combine multifamily programs with negative and positive subsidy costs under the GI/SRI account to eliminate the need for credit subsidy appropriations, (2) authorize FHA to use negative subsidies to cover any shortfalls in credit subsidy budget authority, or (3) make budget authority from the subsequent year's appropriation available in the current year. Finally, the agencies can continue to use or be given additional administrative tools to help delay or prevent program suspensions due to exhaustion of credit subsidy budget authority. However, each of the options we identified would have legal, budgetary, administrative, or oversight implications, and their specific impacts would depend on how they were structured and implemented.

### Expanding FHA Notifications on the Use of Commitment Authority

As noted previously, FHA is currently required to notify its authorizing and appropriations committees when it has used 75 percent of the commitment authority for the MMI/CMHI and GI/SRI accounts. (In contrast to FHA, RHS—which manages its programs based on credit subsidy budget authority—does not have a notification requirement.) Congress could require FHA to provide additional notifications before and after the agency has reached the 75 percent level—for example, when the agency has used specified percentages of commitment authority or at certain points in the fiscal year.

More frequent notifications would provide additional and more timely information to Congress on the status of commitment authority balances for FHA's MMI/CMHI and GI/SRI accounts. For example, in June 2003, FHA, as required, notified Congress that it would soon use 75 percent of the commitment authority in its GI/SRI account. However, this was the only notification Congress received prior to FHA's suspension of the GI/SRI account programs in mid-September. Had FHA been required to provide an additional notification when it reached, for example, the 90 percent level, Congress would have been notified in August—when there was a strong possibility that the programs would need to be suspended—giving Congress timelier information to consider providing supplemental commitment authority that could have prevented the suspension.

FHA could implement this option with little administrative effort because it already maintains the data on its commitment authority balances that would be needed to meet expanded notification requirements.

## Expanding Notifications to Include Obligations of Credit Subsidy Budget Authority by FHA and RHS

As discussed previously, the exhaustion of credit subsidy budget authority before the end of a fiscal year has resulted in FHA and RHS suspending the issuance of loan guarantees. Currently, neither agency is required to notify Congress of the status of its balances of credit subsidy budget authority. Congress could require FHA and RHS to provide such notifications—for example, when they have obligated specified percentages or at certain points in the fiscal year. These notifications would apply only to FHA's GI/SRI account and RHS's Section 502 and 538 programs, which require credit subsidy budget authority.

Requiring these notifications would provide Congress with more information to use in considering if supplemental appropriations would be needed to prevent program suspensions. FHA and RHS could implement this option with little administrative effort because they already maintain the data on their balances of credit subsidy budget authority that would be needed to meet the notification requirements.

## Establishing a Higher Limit on FHA Commitment Authority

The amount of commitment authority for FHA's loan guarantee programs is set in annual appropriations acts and serves as a limitation on the volume of loans the agency can guarantee. For programs under FHA's MMI/CMHI account, this limitation exists even though they generate substantial negative subsidies. As noted previously, for the programs with positive subsidy costs under the GI/SRI account, the volume of loans FHA can guarantee is also limited by annual appropriations of credit subsidy budget authority. FHA's annual budget requests and enacted levels of commitment authority for its MMI/CMHI and GI/SRI accounts reflect commitment authority limits that usually exceed the dollar volume of loans the agency estimates it will actually guarantee. According to FHA officials, the "cushion" between the enacted commitment authority limit and FHA's estimate of guarantees is intended to minimize the possibility of FHA exhausting its authority before the end of the fiscal year. The enacted commitment authority limits are increased periodically to reflect growth in the loan guarantee programs over time but do not always reflect changes in FHA's estimates from year to year. As a result, the difference between the enacted commitment authority limits and FHA's estimates—what FHA refers to as "standby authority"—has varied considerably. For example, from fiscal years 1999 through 2004, the enacted commitment authority limits exceeded FHA's estimates by anywhere from 5 to 49 percent for the MMI/CMHI account and 0 to 94 percent for the GI/SRI account. To overcome the inherent difficulties in forecasting program demand and to help ensure that FHA's commitment authority limit is high enough to prevent program suspensions, Congress could enact total commitment authority limits that exceed FHA's estimates by at least a minimum level.

With a higher commitment authority limit, it is possible that FHA would guarantee a higher volume of loans—thereby assuming a greater insurance risk—than it would otherwise. In that event, loan programs with negative subsidy costs, such as FHA's 203(b) program, would, all other things being equal, increase the amount of negative subsidies available to offset FHA's budget but also increase the agency's exposure to risk. In contrast, loan volume for programs with positive subsidy costs under FHA's GI/SRI account would continue to be limited by the annual credit subsidy appropriation and so would not be affected by this option. Depending on the level of additional loan guarantee activity resulting from a higher limit, FHA may also require supplemental administrative resources to process, review, and manage additional loan guarantees.[27]

## Combining Multifamily Programs under FHA's GI/SRI Account for Credit Subsidy Purposes

Currently, several multifamily, healthcare, and single-family programs make up FHA's GI/SRI account, and programs may have a positive or negative credit subsidy rate. Under the Federal Credit Reform Act of 1990, the President's Budget must reflect the costs of loan guarantee programs and must include the amount of new loan guarantees planned.[28] Federal agencies must therefore prepare a budget estimate for each loan guarantee program which represents the amount of credit subsidy budget authority the program would require or the amount of negative subsidy the program would generate. For example, for fiscal year 2004, FHA estimated that it would need approximately $8 million in credit subsidy budget authority for three multifamily programs under the GI/SRI account. FHA also estimated that the remaining six multifamily programs under the account would generate approximately $79 million in negative subsidies. As proposed by the Millennial Housing Commission in 2002, HUD could combine all nine of these programs for credit subsidy purposes, which, unless current credit subsidy rates and levels of program activity changed dramatically, would result in a single negative credit subsidy rate and thus eliminate the need for annual appropriations of credit subsidy budget authority.[29]

Currently, negative subsidies generated by some of FHA's multifamily programs are considered as offsetting receipts in the agency's annual budgets.[30] Using some of the negative subsidies to, in effect, pay for the positive subsidies required for other GI/SRI programs would reduce the offset, all other things being equal. The elimination of credit subsidy appropriations under a combined multifamily program could compensate for the reduced offset. However, because the programs with positive

[27]FHA's appropriations for the MMI/CMHI and GI/SRI accounts typically include limited additional budget authority for administrative expenses that becomes available if guaranteed loan commitments exceed specified levels on or before April 1.

[28]2 U.S.C. § 611c(a).

[29]The Millennial Housing Commission, established at the request of Congress in 2000, studied the federal role in meeting the nation's housing challenges and issued a report in 2002 recommending a variety of reforms to federal housing programs, among other things.

[30]Offsetting receipts are collections that are deducted from gross budget authority and outlays by agency, rather than added to receipts.

subsidies would no longer be constrained by appropriations of budget authority, they could experience more activity and higher resulting costs than they would otherwise, thus increasing the budget deficit (all other things being equal). Because FHA already estimates credit subsidy rates for each multifamily program to comply with Federal Credit Reform Act requirements, limited additional administrative effort would likely be required to merge these rates into a single rate.

This option would require congressional action and pose several challenges to Congress and FHA. For example, to the extent that the option may be inconsistent with Federal Credit Reform Act requirements, Congress would have to provide FHA a limited exception to these requirements. Further, congressional oversight would be affected because combining the programs would eliminate the need for credit subsidy budget authority. Therefore, congressional appropriators would only be able to control the size of the programs through limits on commitment authority. Additionally, to maintain its current level of oversight, Congress would need to ensure that HUD continued providing the estimated cost of, and number of guarantees under, individual programs in its annual budget requests. This option would also require FHA to alter its accounting and record keeping systems to accurately track the budget activity for the combined programs.

## Authorizing Use of Negative Subsidies to Cover Shortfalls in Credit Subsidy Budget Authority for FHA

In recent years, negative subsidies generated by the single-family and multifamily programs under FHA's GI/SRI account have exceeded the account's positive subsidy requirements (i.e., credit subsidy costs) by over $200 million per year. A bill introduced in April 2001 would authorize FHA to use negative credit subsidies from its GI/SRI account programs to cover the credit subsidy costs of making loan guarantees if FHA exhausted the original appropriation of credit subsidy budget authority before the end of a fiscal year.[31]

If this option were implemented, it would be unlikely—given the current credit subsidy rates and level of activity for each program—that FHA would have to suspend the issuance of loan guarantees for GI/SRI account

[31]Specifically, H.R. 1481, 107th Cong. (2001) provided that the amount of negative credit subsidy from any of the programs under the General Insurance Fund or the Special Risk Insurance Fund would be considered as new budget authority provided in advance in an appropriations act for that fiscal year and that it would be available for covering the costs of making guarantees under any program funded by the GI/SRI account.

programs due to the exhaustion of credit subsidy budget authority. The proposal would require Congress to amend section 519 of the National Housing Act (codified at 12 U.S.C. § 1735c) to allow the use of negative subsidies as budget authority for programs with positive subsidy costs, which could result in these programs experiencing more activity and higher resulting costs than they would otherwise, thus increasing the budget deficit (all other things being equal). From a budgeting perspective, this option would prevent these subsidies from being used as offsetting receipts in HUD's overall budget. As a result, additional appropriations or cuts in HUD's other discretionary spending might be required to compensate for the elimination of the offset. Further, the amount of negative subsidies that CBO estimated FHA would need to cover shortfalls in credit subsidy budget authority would be charged against FHA's overall budget authority in the current fiscal year.

## Appropriating Advanced Funding for Credit Subsidy Costs at FHA and RHS

To help ensure that FHA and RHS programs with positive subsidy costs would not be suspended due to exhaustion of credit subsidy budget authority, Congress could also provide "advance funding" for FHA and RHS program credit subsidy costs. Advance funding authorizes agencies, if necessary, to charge obligations in excess of the specific amount appropriated for that year to the next fiscal year's appropriation. Congress could stipulate in the agencies' annual appropriations acts that an additional amount of budget authority would automatically be made available to cover additional credit subsidy costs in the current fiscal year if the original appropriation of credit subsidy budget authority were exhausted.[32] For example, Congress could specify this amount as a fixed sum or a percentage of the original appropriation.

If FHA or RHS were to obligate any of these additional amounts, the amounts would be charged to the agencies' appropriations of credit subsidy budget authority for the subsequent fiscal year. All other things being equal, this would reduce the amount of budget authority available in the subsequent year.

[32]For FHA's GI/SRI account programs and RHS's Section 502 program, the credit subsidy budget authority available in any fiscal year includes current year appropriations plus any unobligated budget authority from prior fiscal years.

## Continuing or Expanding Currently Permitted Practices at FHA and RHS, Such As Increasing Fees or Transferring Budget Authority

FHA and RHS have existing tools that they can and have used to help delay or prevent program suspensions. For example, FHA and RHS establish application or guarantee fees for their loan guarantee programs and have the discretion to change them during the fiscal year. All other things being equal, raising fees lowers the credit subsidy rate for the affected program and allows the agencies to cover the credit subsidy costs for more loan guarantees. For example, in June 2004, RHS increased its loan guarantee fee by 25 basis points (0.25 percent) on all Section 502 guaranteed loans. RHS indicated that the fee increase allowed it to reduce its credit subsidy rate and thereby cover the credit subsidy costs for more than 1,000 additional loan guarantees. Additionally, and as discussed previously, RHS has limited authority to transfer budget authority to cover resource shortfalls. RHS used this authority in fiscal years 2003 and 2004, when it transferred funds from various loan and grant programs to cover the credit subsidy costs for the Section 502 program. FHA does not have, but could be given, similar authority by Congress.

The agencies cannot transfer budget authority or change fees without significant administrative effort. According to FHA officials, changing application fees requires them to promulgate regulations, while increasing guarantee fees requires them to develop and place a notice in the *Federal Register*. Furthermore, increasing fees makes loan guarantees less affordable for borrowers. Finally, administrative transfers of budget authority cannot be made without budget authority being available elsewhere in an agency's budget and requires concurrence by OMB.

# Agency Comments

We provided a draft of this report to HUD and USDA for their review and comment. HUD provided comments in a letter from the Deputy Assistant Secretary for Finance and Budget (see app. IV). HUD agreed with our findings but said it saw difficulties with each of the options we presented for helping to prevent program suspensions. HUD cited specific difficulties with some of the options. For example, HUD questioned the option to expand FHA notifications on the use of commitment authority, saying we presumed that Congress did not act to prevent the suspension of the GI/SRI account programs in fiscal year 2003 because it did not receive timely notifications. Our draft report did not make this presumption. Nevertheless, we clarified the final report to emphasize that had FHA been required to provide an additional notification once there was a strong possibility that the programs would need to be suspended, Congress would have had timelier information to consider providing additional commitment authority.

HUD also commented that the option to combine multifamily programs under FHA's GI/SRI account for credit subsidy purposes is inconsistent with the Federal Credit Reform Act, which requires that credit subsidy rates be determined for each program. Our draft report indicated that this option would require congressional action. We added language to our final report to recognize that this could involve giving FHA a limited exception to Federal Credit Reform Act requirements to the extent that the option may be inconsistent with these requirements. Also, as our draft report stated, to maintain its current level of oversight, Congress would need to ensure that HUD continued providing the estimated cost of, and number of guarantees under, individual programs in its annual budget requests.

HUD said that the option for appropriating advance funding for credit subsidy costs was a one-time-only solution because program activity in the year from which funding was advanced would be at risk for suspension due to inadequate credit subsidy budget authority. We disagree that the option would only be a one-time solution, because any year from which funding was advanced could likewise receive an advance from the subsequent fiscal year to avoid program suspensions, if necessary.

USDA agreed with our findings and provided technical comments, which we incorporated into this report as appropriate.

As agreed with your office, unless you publicly announce its contents earlier, we plan no further distribution of this report until 30 days from the date of the letter. At that time, we will send copies to other interested Members of Congress and congressional committees and to the Secretaries of HUD and USDA. We will also make copies available to others upon request. In addition, the report will be available at no charge on the GAO Web site at http://www.gao.gov.

Should you or your staff have any questions or comments on matters discussed in this report, please contact me at (202) 512-8678 or woodd@gao.gov or Steve Westley at (202) 512-6221 or westleys@gao.gov. Major contributors to this report are listed in appendix V.

Sincerely yours,

David G. Wood

David G. Wood
Director, Financial Markets
and Community Investment

# Scope and Methodology

To determine how often and why FHA and RHS have suspended their loan guarantee programs due to the exhaustion of commitment authority or credit subsidy budget authority before the end of a fiscal year, we reviewed relevant agency and housing industry notices, budget data, and correspondence relating to program suspensions since fiscal year 1994. We also interviewed cognizant agency and housing industry officials.

To determine how FHA and RHS manage, and notify Congress of, their use and obligation of these authorities, we reviewed laws, regulations, and guidance governing the agencies' approval, monitoring, and estimation processes and the agencies' procedures for informing Congress of the status of their loan guarantee programs. We also interviewed agency officials responsible for these tasks and obtained information on the information systems they use to administer their loan guarantee programs. Finally, to assess FHA's approach for estimating utilization of commitment authority, we analyzed FHA monthly budget and accounting data for fiscal years 2003 and 2004. We conducted a straight-line analysis for each month within that time frame that assumed that the agency would use commitment authority for the remainder of the fiscal year at the same rate experienced previously in the year.

To identify options that Congress, FHA, and RHS could exercise to help prevent the agencies from suspending their loan guarantee programs before the end of a fiscal year and the likely implications of these options, we interviewed budget, legal, and housing finance specialists from OMB and CBO; housing industry officials from the National Association of Home Builders, the Mortgage Bankers Association, and the National Association of Realtors; and we conducted a literature review to identify relevant studies and legislation. To determine and illustrate the potential implications of these options, we obtained these officials' views on the effects of various alternatives and analyzed agency budget and accounting data.

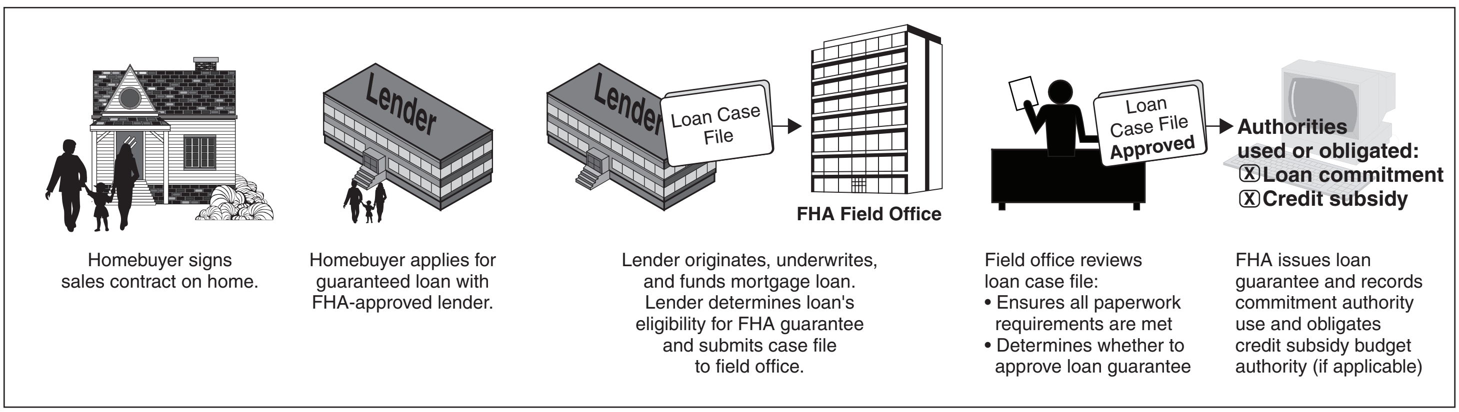
We assessed the reliability of the data used in our analyses by (1) reviewing existing information about the systems and the data, (2) interviewing agency officials knowledgeable about the data, and (3) examining the data elements (fields) used in our work by comparing known and/or anticipated values. When inconsistencies were found, we discussed our findings with agency officials to understand why inconsistencies could exist. We determined that the data were sufficiently reliable for the purposes of this report.

We conducted our work in Washington, D.C., between January 2004 and January 2005 in accordance with generally accepted government auditing standards.

# FHA and RHS Loan Guarantee Processes

FHA's loan guarantee processes are different for its single-family and multifamily programs. As shown in figure 3, for FHA's single-family programs, an FHA-approved lender determines a borrower's (homebuyer's) eligibility for an FHA loan guarantee. If the lender determines that the homebuyer and the property being financed are eligible, the loan case file is sent to an FHA field office for review. If the field office approves and issues the loan guarantee, FHA then records the amount of commitment authority used and, when appropriate, obligates credit subsidy budget authority.

**Figure 3: Loan Guarantee Process for FHA Single-Family Programs**

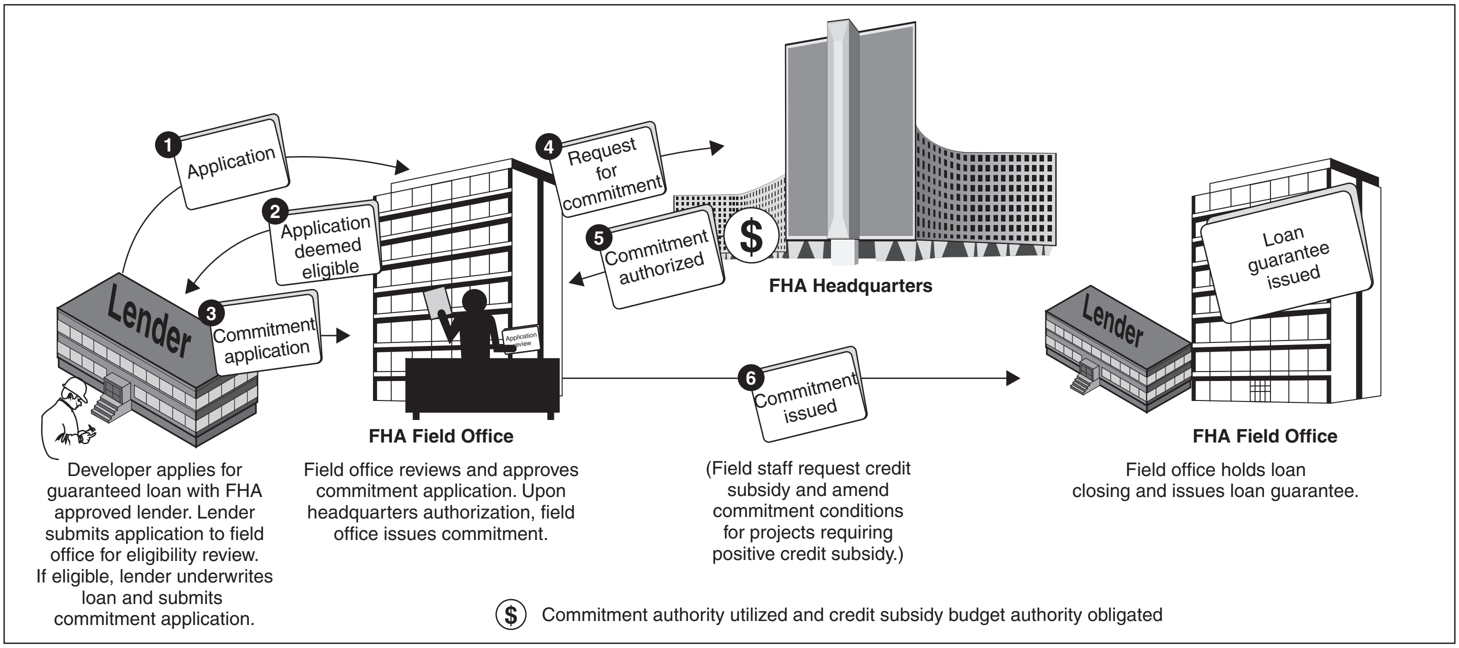



Sources: GAO (analysis); Nova Development (images).

Note: Origination refers to accepting mortgage applications, obtaining employment verifications and credit histories on applicants, ordering appraisals, and performing other tasks that precede the loan underwriting process, while underwriting refers to a risk analysis that uses information collected during origination to decide whether to approve a loan.

For FHA's multifamily programs, the process begins when a borrower (developer) applies for a loan from an FHA-approved lender, who in turn submits a loan guarantee application to an FHA field office for review (see fig. 4). If the field office determines that the borrower and the property being financed are eligible, then the lender underwrites the loan and submits an application for commitment—the formal agreement by the government to guarantee the loan once the lender fulfills certain conditions—to the field office. If the field office approves the application, FHA then records the amount of commitment authority used and, when appropriate, obligates credit subsidy budget authority upon headquarters authorization, after which the field office issues the commitment.

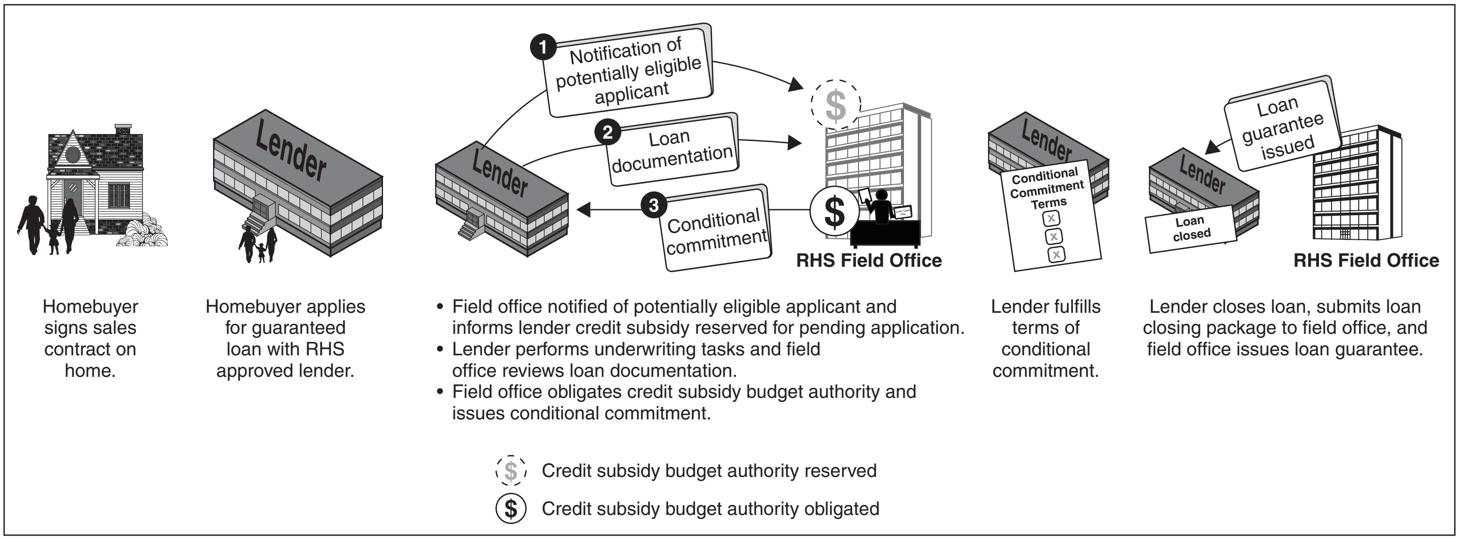
Figure 4: Loan Guarantee Process for FHA Multifamily Programs




Sources: GAO (analysis); Nova Development (images).

RHS also has separate loan guarantee processes for its Section 502 and Section 538 programs. For the Section 502 program, as shown in figure 5, a borrower (homebuyer) applies for a guaranteed loan through an RHS-approved lender. RHS is notified and reserves the required amount of credit subsidy budget authority. The RHS field office then reviews the loan documentation and, if the documentation meets RHS's requirements, obligates credit subsidy budget authority, and issues a commitment.

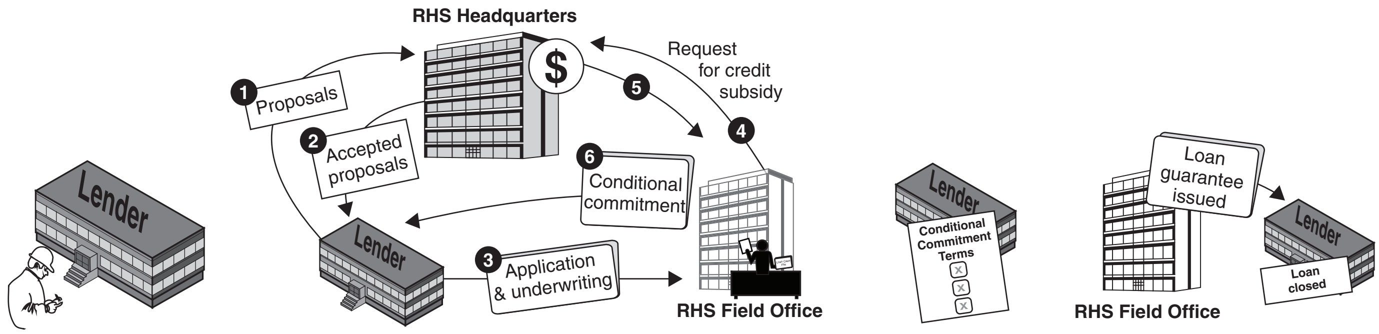
Figure 5: Loan Guarantee Process for RHS Section 502 Program




Sources: GAO (analysis); Nova Development (images).

As shown in figure 6, for loans guaranteed under the Section 538 program, a borrower (developer) applies for a guaranteed loan through an RHS-approved lender. RHS selects proposals based on eligibility requirements and has a field office review the underwriting. The field office then forwards a request for credit subsidy budget authority to headquarters, which obligates the authority.

**Figure 6: Loan Guarantee Process for RHS Section 538 Program**




Developer applies for guaranteed loan with RHS-approved lender.

- Headquarters receives proposals. Selected proposals continue with application process.
- Field office processes applications, reviews lender's underwriting, and forwards request for credit subsidy to headquarters.
- Headquarters obligates credit subsidy budget authority. Field office issues conditional commitment.

Lender fulfills terms of conditional commitment.

Field office issues loan guarantee and lender closes loan.

$ Credit subsidy budget authority obligated

Sources: GAO (analysis); Nova Development (images).

Note: Starting in fiscal year 2005, loan applications are accepted and processed by the field offices. Lenders no longer send applications to headquarters.

# Applicability of Options to Past Program Suspensions

The usefulness of options for delaying or preventing suspensions of FHA's and RHS's guaranteed loan programs can be considered in light of whether they would have been applicable to past suspensions. (See table 4.) As previously noted, the expanded notification options would have provided additional information on the status of resources for FHA and RHS guaranteed lending programs and would thus have been applicable to most of the suspensions since fiscal year 2000. Providing a higher limit on commitment authority would have increased the amount of commitment authority available to FHA and, as a result, would have been applicable to the suspension of programs under FHA's GI/SRI account in fiscal years 2003 and 2004 due to the exhaustion of commitment authority. The option that would combine the multifamily programs under FHA's GI/SRI account for credit subsidy purposes would likely eliminate the need for appropriations of credit subsidy budget authority and therefore would have been applicable to the suspension of GI/SRI account programs due to the exhaustion of budget authority in fiscal years 2000 and 2001. The option that would permit the use of negative subsidies to cover shortfalls in credit subsidy budget authority would have been applicable to the same suspensions. In addition, the option that would appropriate advance funding for credit subsidy costs would have been applicable to the suspension of programs under FHA's GI/SRI account in fiscal years 2000 and 2001 and the suspension of RHS's Section 502 program in fiscal years 2003 and 2004—all of which were due to the exhaustion of credit subsidy budget authority. Further, the option to continue or expand currently permitted practices, such as increasing fees or transferring budget authority, would have been applicable to or was actually used to delay the same four suspensions. For example, RHS used its authority to increase fees to delay suspension of the Section 502 program in fiscal years 2003 and 2004. FHA could have taken similar steps to help avoid or delay the suspension of programs under its GI/SRI account in fiscal years 2000 and 2001. Finally, RHS used its authority to transfer budget authority to delay the suspension of its Section 502 program in fiscal years 2003 and 2004. If FHA had the authority to transfer budget authority, this option would have been applicable to its fiscal year 2000 and 2001 suspensions.

**Table 4: Applicability of Options to Past Program Suspensions, Fiscal Years 2000–2004**

| | Program suspensions due to exhaustion of commitment authority (CA) or credit subsidy budget authority (CSBA) | | | | | |
|---|---|---|---|---|---|---|
| | FHA GI/SRI account programs | | | | RHS Section 502 program | |
| Options | FY 2000 (CSBA) | FY 2001 (CSBA) | FY 2003 (CA) | FY 2004[a] (CA) | FY 2003 (CSBA) | FY 2004 (CSBA) |
| Require more notification on CA | | | ✔ | | | |
| Require notification on CSBA | ✔ | ✔ | | | ✔ | ✔ |
| Provide a higher limit on CA | | | ✔ | ✔ | | |
| Combine multifamily programs under FHA's GI/SRI account for credit subsidy purposes | ✔ | ✔ | | | | |
| Authorize use of negative subsidies to cover shortfalls in CSBA | ✔ | ✔ | | | | |
| Appropriate advance funding for credit subsidy costs | ✔ | ✔ | | | ✔ | ✔ |
| Continuing or expanding currently permitted practices such as increasing fees or transferring budget authority | ✔ | ✔ | | | ✔ | ✔ |

Source: GAO.

Note: ✔ indicates "applicable."

[a]As noted previously, FHA suspended the programs under its GI/SRI account twice in early fiscal year 2004 when it was operating under a series of continuing resolutions. Under the continuing resolutions, FHA was required to notify Congress about the status of its commitment authority balances on a daily or weekly basis.

# Comments from the Department of Housing and Urban Development

U.S. DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT
WASHINGTON, DC 20410-8000

ASSISTANT SECRETARY FOR HOUSING-
FEDERAL HOUSING COMMISSIONER

MAR 0 4 2005

Mr. David G. Wood
Director
Financial Markets and Community Investments
United States Government Accountability Office
Washington, DC 20548

Dear Mr. Wood:

We appreciate the opportunity to comment on the draft GAO Report _Options to Help Prevent Suspensions of FHA and RHS Loan Guaranteed Programs_. Our comments will address the broad issues covered by the report and the options that the report presents for consideration by the Congress.

The Department shares the Congress' and GAO's concern that suspension of the FHA mortgage insurance programs due to the exhaustion of either the commitment limitations or credit subsidy is disruptive to the mortgage finance markets and the FHA borrower constituency. Specifically to avoid this type of disruption, FHA utilizes all available tools to estimate its projected needs however, as noted by GAO, these estimates, because of the requirements of the budget cycle, are prepared nearly two years in advance of the relevant program activity and therefore changing economic conditions can have significant impact on their accuracy. FHA also closely monitors the usage of both the commitment limitation and credit subsidy and reports to Congress immediately upon reaching specific levels of use or estimating that available levels may be insufficient to accommodate program demand. In spite of the Department's efforts, program activity has been suspended several times in recent years due to the exhaustion of commitment authority or credit subsidy.

Therefore, GAO has made several suggestions for actions by Congress that could possibly reduce the likelihood of such program suspensions occurring in the future. While the Department appreciates the GAO's effort to explore possible methods for avoiding program disruptions, we do see difficulties with each of the suggested alternatives.

Expanding FHA Notifications on the Use of Commitment Authority. The GAO cites as a specific example fiscal year 2003 where FHA, as required by law, notified Congress in June that it would soon exhaust 75 percent of its available commitment authority. GAO suggests that a subsequent notification in August that FHA had used 90 percent of its limitation might have been helpful. While, we agree that additional notifications concerning the use of the commitment level would constitute negligible administrative burden, we question the presumption that the Congress did not take action to increase the commitment level because of the lack of timely notice of the pace of usage.

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Establishing a Higher Limit on FHA Commitment Authority. The GAO suggests that Congress could enact a commitment limitation so large as to virtually assure that it would never be breached. We agree that this alternative would largely eliminate the possibility of a program suspension due to the exhaustion of commitment authority.

Combining Multifamily Programs under FHA's GI/SRI Account for Credit Purposes. This proposal is inconsistent with Credit Reform which requires that credit subsidy be determined and recorded at the lowest possible level.

Authorizing Use of Negative Subsidies to Cover Shortfalls in Credit Subsidy Budget Authority for FHA. As the GAO notes, the negative subsidies generated by FHA are currently considered offsetting receipts. These receipts significantly exceed the credit subsidy currently required by FHA programs. Therefore, if all negative subsidy generated by FHA were restricted to this use, this alternative would severely and artificially restrict the Department's available budget authority. Conversely, if only the portion required to cover the anticipated positive credit subsidy needs were set aside, the program would still be subject to suspension if that level were reached.

Appropriating Advanced Funding for Credit Subsidy Costs at FHA and RHS. This is only a single time solution because the year from which the funding was borrowed would be at risk for suspension due to inadequate credit subsidy.

Continuing or Expanding Currently Permitted Practices at FHA and RHS such as increasing Fees or Transferring Budget Authority. GAO notes that FHA does not have the authority to transfer Budget Authority but could possibly reduce credit subsidy utilization per case by raising fees or premiums. We agree that this could possibly extend the coverage of available credit subsidy by some amount.

Again, the Department appreciates the opportunity to comment on the draft report and will be pleased to work with the GAO and the Congress on any proposals which will allow the FHA to operate more effectively.

Sincerely,

Sandra L. Allison
for Margaret A. Young
Deputy Assistant Secretary
For Finance and Budget

# GAO Contacts and Staff Acknowledgments

## GAO Contacts

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