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RURAL HOUSING SERVICE

Progress on GAO Recommendations and Preliminary Observations on Loan Guarantee Risk Management

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GAO-15-625T

GAO Highlights

Highlights of GAO-15-625T, a testimony before the Subcommittee on Housing and Insurance, Committee on Financial Services, House of Representatives

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Why GAO Did This Study

RHS, an agency within USDA, administers a number of direct loan, loan guarantee, and grant programs that support affordable housing and community development for rural residents. According to USDA financial and budget data, RHS manages a portfolio of almost $120 billion in housing loans and loan guarantees and administers more than $1 billion in rental assistance payments each year. GAO issued three reports since March 2011 on RHS housing assistance programs (see GAO-11-329, GAO-12-554, and GAO-12-624) and has ongoing work in this area.

This testimony is based on those three reports and ongoing GAO work. It discusses (1) prior GAO findings on the extent to which the housing programs of RHS and HUD overlap and related implications for program collaboration and consolidation; (2) the status of GAO recommendations on the rental housing assistance program and farm labor housing loan and grant program; and (3) preliminary observations from the ongoing review of risk-management practices for the single-family loan guarantee program. To update the status of recommendations, GAO reviewed RHS policies, procedures, and reports. For its ongoing work, GAO reviewed federal requirements and leading practices for risk management and compared them with RHS policies, procedures, and practices. GAO also interviewed RHS officials.

GAO makes no new recommendations in this testimony, but may consider making additional recommendations once its ongoing work is complete.

View GAO-15-625T. For more information, contact Mathew Scirè at (202) 512-8678 or sciremj@gao.gov.

What GAO Found

Overlap in housing assistance programs—particularly those of the Department of Agriculture's (USDA) Rural Housing Service (RHS) and the Department of Housing and Urban Development (HUD)—highlight opportunities for increased collaboration and consolidation. GAO's August 2012 report found overlap in the products offered and populations (income groups) and geographic areas served by RHS and HUD single-family mortgage guarantee programs. GAO also found selected multifamily housing programs served similar purposes. The report made three recommendations to RHS. RHS generally agreed with the recommendations and implemented one by formalizing collaborative efforts with other federal agencies on single-family housing programs. However, RHS and other federal housing agencies have not yet taken other recommended steps to build on interagency efforts—for example, by evaluating specific opportunities for consolidating similar housing programs, including those that would require statutory changes.

RHS generally agreed with and has addressed some of GAO's prior recommendations for the rental assistance and farm labor housing programs, but others require further attention. Specifically, RHS implemented three of the seven recommendations GAO made in May 2012 to enhance the agency's efforts to identify and reduce improper rental assistance payments. Additional steps are needed to implement the remaining recommendations, which address shortcomings in the way RHS estimates and reports on improper payments. RHS also addressed three of the seven recommendations GAO made in March 2011 on oversight of the farm labor housing program. Further actions are required to implement the other four, which address weaknesses in RHS controls for ensuring tenant eligibility, among other issues.

Ongoing GAO work indicates that aspects of RHS's risk management for the single-family mortgage guarantee program broadly align with federal requirements, while others are not fully consistent with requirements and leading practices. For example, RHS has policies and procedures for a number of risk-management functions addressed in Office of Management and Budget guidance (such as determining borrower creditworthiness and overseeing lenders). However, GAO's ongoing work indicates that, contrary to federal internal control standards, RHS does not have written policies and procedures for a committee responsible for evaluating credit quality issues and addressing them through policy changes. Also, certain benchmarks RHS uses to help assess the performance of its guaranteed portfolio have limitations that diminish their value for assessing risk and are not fully consistent with leading practices for successful performance measures. These shortcomings may limit the effectiveness of RHS's risk-management efforts.

Chairman Luetkemeyer, Ranking Member Cleaver, and Members of the Subcommittee:

I am pleased to be here today to discuss our work on the Rural Housing Service (RHS), a component of Rural Development within the Department of Agriculture (USDA). Among other responsibilities, RHS provides housing assistance to low- and moderate-income rural Americans through a number of direct loan, loan guarantee, and grant programs. These programs support homeownership, promote the development and rehabilitation of rental properties, and help make rents affordable. According to RHS financial and budget data, the agency manages a portfolio of almost $120 billion in single- and multifamily housing loans and loan guarantees and administers more than $1 billion in rental assistance payments each year.

RHS is one of several federal agencies—including the Departments of Housing and Urban Development (HUD), Veterans Affairs (VA), and Treasury—with programs or activities that support housing. For example, HUD insures mortgages for single- and multifamily properties through the Federal Housing Administration (FHA) and administers rental assistance programs. The fragmented and overlapping nature of federal housing assistance stems partly from distinctions between urban and rural areas that existed when federal housing programs were created. However, the rural America of today is different than when the federal government first began to provide housing assistance to rural residents in the 1930s. Today's constrained budget environment makes it especially important that federal housing programs adapt to changing conditions, reduce waste, and effectively manage risk in order to deliver housing assistance as efficiently and effectively as possible.

My testimony today is based primarily on three reports we issued between March 2011 and August 2012, as well as an ongoing study that we are conducting at the request of this Subcommittee.[1] (For a list of recommendations from the three issued reports and their status,

[1]See GAO, *Rural Housing Service: Opportunities Exist to Strengthen Farm Labor Housing Program Management and Oversight*, GAO-11-329 (Washington, DC.: Mar. 30, 2011); *Rural Housing Service: Efforts to Identify and Reduce Improper Rental Assistance Payments Could be Enhanced*, GAO-12-624 (Washington, D.C.: May 31, 2012); and *Housing Assistance: Opportunities Exist to Increase Collaboration and Consider Consolidation*, GAO-12-554 (Washington, D.C.: Aug. 16, 2012).

see app. I.) This body of work addresses both program-specific issues and broader issues affecting multiple housing programs. I will discuss (1) our prior findings on the extent to which there is overlap in the single- and multifamily housing programs of RHS and HUD, including geographic areas served, and related implications for program collaboration and consolidation; (2) the status of our recommendations on RHS's Section 521 Rental Assistance Program and Section 514 and 516 Farm Labor Housing Loan And Grant Program; and (3) preliminary observations from our ongoing assessment of risk management practices for RHS's Section 502 Single Family Housing Guaranteed Loan Program.

To conduct our previously issued work, we relied on several analytical methods, including analyzing RHS budget, financial, and program data; reviewing RHS policies and procedures and comparing them to federal requirements; and comparing the geographic locations and populations benefiting from RHS programs to those benefiting from other selected housing agency programs. We also interviewed RHS and other government officials and industry representatives. Our prior reports each include a detailed description of our scope and methodology. To update the status of our prior recommendations, we reviewed updated RHS policies, procedures, and reports. For this testimony, we also reviewed information on RHS's estimates of improper rental assistance payments reported in fiscal years 2013 and 2014. To conduct our ongoing work, we reviewed federal requirements and leading practices for risk management and compared them with RHS policies, procedures, and practices. We also interviewed RHS officials. We performed the work on which this testimony is based in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

Background

The federal government plays a major role in supporting housing. Federal housing assistance includes, but is not limited to, the following categories:

- Homeownership programs, often called single-family housing programs, provide mortgage insurance, loan guarantees, and direct loans to support the purchase or refinance of a home, as well as grants or loans for home repairs or modifications.

- Rental housing programs, often called multifamily programs, provide loans, interest rate subsidies, loan guarantees, tax incentives, or a combination of these to promote the development and rehabilitation of privately owned rental properties.

- Rental assistance programs, which make rents affordable to eligible households by paying the difference between the unit's rent and 30 percent of a household's adjusted income. These programs include (1) tenant-based rental assistance that provides vouchers for eligible tenants to rent privately owned apartments or single-family homes and can be applied to different properties if tenants move, and (2) project-based rental assistance that is attached to specific properties and available to tenants only when they are living in units at these properties.

In the 1930s, when most rural residents worked on farms and rural areas generally were poorer than urban areas, Congress authorized separate housing assistance for rural areas and made USDA responsible for administering it. Specifically, in 1937 the Bankhead-Jones Farm Tenant Act authorized USDA to provide long-term, low-interest loans to farm tenants and sharecroppers so that they could purchase and repair farms, including homes on farms. The Housing Act of 1949 authorized new rural lending programs through USDA and made farm owners eligible for assistance for dwellings and other farm buildings. Amendments added in 1961 made nonfarm properties eligible for single-family loans and created the farm labor housing program. A 1962 amendment created the rural rental housing program.

The housing programs that RHS currently administers include, but are not limited to, the following:

- The Section 502 Single Family Housing Guaranteed Loan Program (single-family guarantee program) provides guarantees on mortgage loans to households with low and moderate incomes in rural areas.[2]

- The Section 521 Rental Assistance Program (rental assistance program) provides rental subsidies to help very low- and low-income

[2]To be eligible for an RHS-guaranteed single-family mortgage, the borrower's income must not exceed 115 percent of the area median income.

rural tenants afford decent rental housing.[3] The properties in which the tenants live were created through other RHS programs that provide low-interest loans for the development of multifamily housing.

- The Section 514 and 516 Farm Labor Housing Loan and Grant Program (farm labor housing program) provides direct loans and grants for the development of on-farm and off-farm housing for farmworker tenants. The farm labor housing program is the only RHS program that does not have to meet rural eligibility criteria—that is, it funds properties in both urban and rural areas.

Opportunities Exist to Increase Collaboration and Consider Consolidation of RHS and HUD Programs

Our prior work assessing fragmentation, overlap, and duplication in selected housing programs concluded that increased collaboration or even consolidation of certain housing programs (including RHS programs) could make the programs and program administration more effective.

In an August 2012 report, we found that overlap exists between selected single-family federal housing programs—particularly those of RHS and HUD—in the products offered and populations (income groups) and geographic areas they served.[4] For instance,

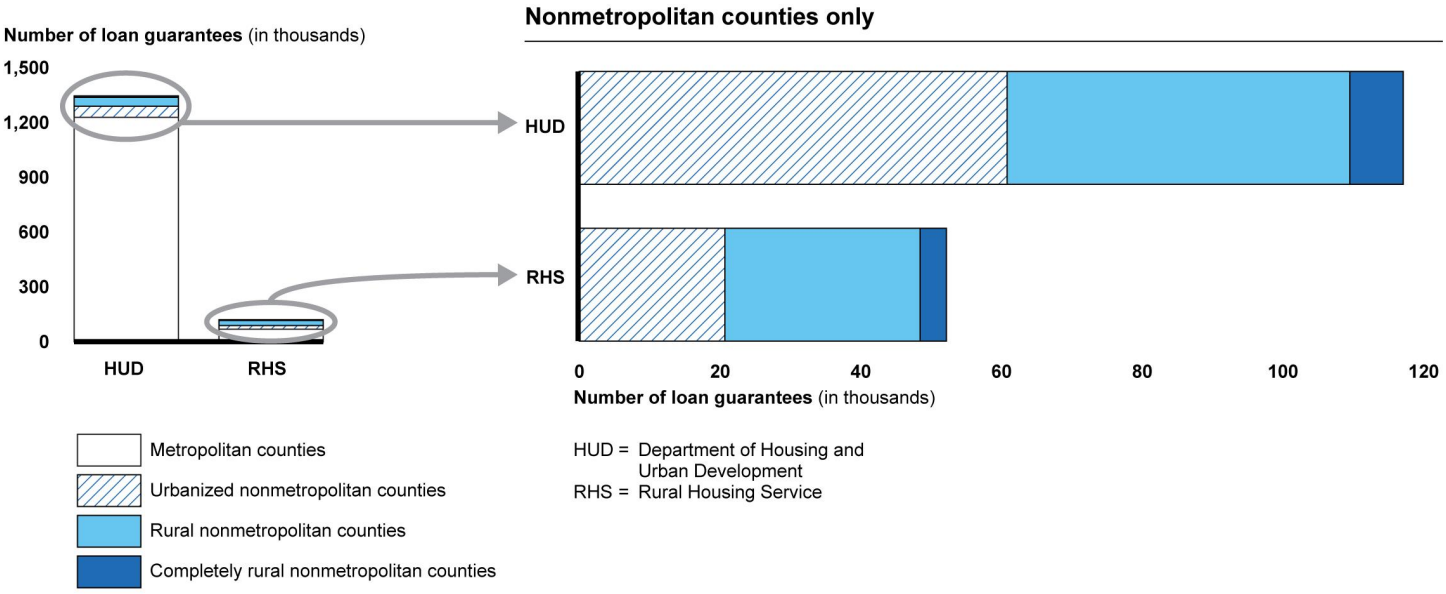
- RHS, HUD, and VA all guarantee single-family mortgage loans for homeowners.
- According to fiscal year 2009 loan data, 74 percent of HUD borrowers fell into the low- to moderate- income category and therefore met the income eligibility requirement for the RHS single-family guarantee program in fiscal year 2009.
- Also according to fiscal year 2009 data, HUD served a larger number of low- and moderate-income households in nonmetropolitan counties, including those parts of the county considered by USDA's

[3]Very low income is defined as below 50 percent of the area median income; low income is from 50 to 80 percent of area median income.

[4]GAO-12-554.

Economic Research Service to be rural or completely rural (see fig. 1).[5]

Figure 1: Number of Single-Family Loan Guarantees Servicing Low- and Moderate-Income Borrowers, Fiscal Year 2009



Source: GAO analysis of agency data. | GAO-15-625T

Note: Low- and moderate-income borrowers are those with incomes at or below 115 percent of area median income.

HUD and VA single-family programs are not restricted geographically. In contrast, eligible areas for RHS programs are "rural," as defined by

[5]RHS had a higher proportion of guarantees in nonmetropolitan counties than HUD had in those areas. Our analysis categorized areas on a rural-urban continuum that USDA's Economic Research Service developed (counties are categorized by degree of rurality). The rural-urban continuum codes form a classification scheme that distinguishes metropolitan counties by the population of their metropolitan area, and nonmetropolitan counties by degree of urbanization and adjacency to a metropolitan area or areas. A county may include both RHS eligible and ineligible areas.

statute.[6] However, in our August 2012 report, we found that RHS can operate in virtually all areas of the United States, and 37 percent of the population as of 2011 was eligible for rural housing programs on the basis of geography alone.[7] Over the years, we have found that the methods for identifying eligible areas results in similar areas being treated differently. For example, in our August 2012 report, we reiterated a finding from a 2004 report that the definition of rural used to determine eligibility for rural housing programs can lead to similar areas receiving different eligibility determinations.[8] Our 2004 report recommended that Congress consider certain changes to the definition to better ensure that RHS made more consistent eligibility determinations for rural housing programs.[9] We maintain that these changes would improve the consistency with which RHS determines eligibility for such programs. In addition, the changes would help target the programs to more rural areas—for instance, by

[6]Section 520 of the Housing Act of 1949, as amended, defines rural for most RHS housing programs. The definition is largely based on population, but also considers other factors, such as proximity to metropolitan areas and access to mortgage credit. Currently, rural areas are any open country or any place, town, village, or city that is not part of or associated with an urban area and that (1) has a population not in excess of 2,500 inhabitants; or (2) has a population in excess of 2,500 but not in excess of 10,000 if it is rural in character; or (3) has a population in excess of 10,000 but not in excess of 20,000, and (A) is not contained within a standard metropolitan statistical area, and (B) has a serious lack of mortgage credit for lower- and moderate-income families, as determined by the Secretaries of USDA and HUD. Any area classified as “rural” or a “rural area” prior to October 1, 1990, and determined not to be “rural” or a “rural area” as a result of data received from or after the 1990, 2000, or 2010 decennial census, and any area deemed to be a “rural area” for purposes of title V of the Housing Act of 1949, as amended, under any provision law at any time during the period beginning January 1, 2000, and ending December 31, 2010, shall continue to be so classified until receipt of data from the 2020 decennial census, if such area has a population in excess of 10,000 but not in excess of 35,000, is rural in character, and has a serious lack of mortgage credit for lower- and moderate-income families.

[7]At the time we conducted this analysis, the statutory definition of rural was more restrictive in certain ways than the current definition.

[8]GAO, *Rural Housing: Changing the Definition of Rural Could Improve Eligibility Determinations*, GAO-05-110 (Washington, D.C.: Dec. 3, 2004).

[9]In GAO-05-110, we suggested that Congress consider (1) including density measures, rather than the metropolitan statistical area (MSA) criterion, in the statute to better reflect where people live; (2) phasing out grandfathering of communities; and (3) eliminating the “lack of credit” requirement. Although Congress considered these changes in an oversight hearing held in March 2005, it did not implement any of the suggested changes to the definition of rural.

eliminating “grandfathered” eligibility for places that had become part of metropolitan areas.

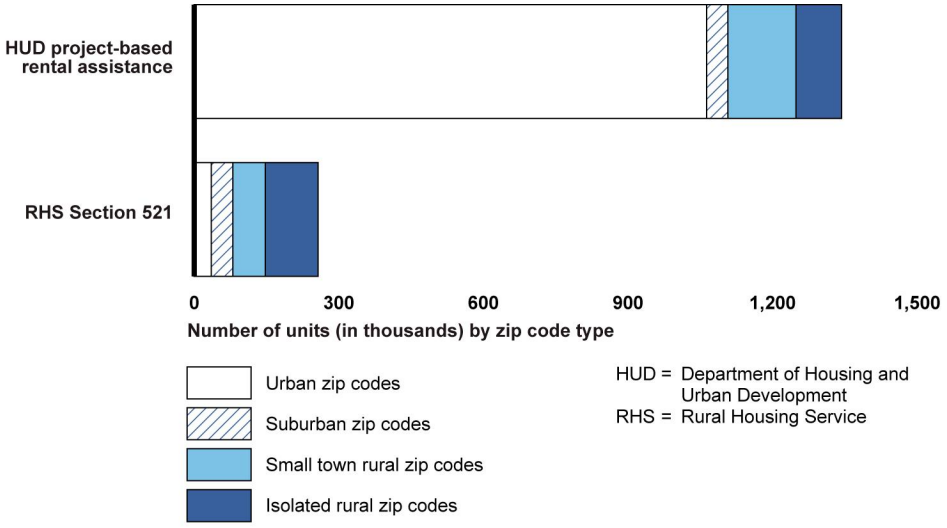
Agencies have started to work on better coordinating their single-family programs. In February 2011, the administration announced a task force to evaluate the potential for coordinating or consolidating homeownership loan programs at HUD, USDA, and VA. But, in our August 2012 report, we found that opportunities existed to increase collaboration among the agencies and potentially realize efficiencies. The single-family task force’s efforts as of 2012 had not yet incorporated key collaborative practices we identified in previous work.[10] We concluded that practices, such as identifying goals and resources and defining strategies and outcomes, would be important as the task force moved forward. We recommended that HUD, USDA, and VA, and the Director of the Office of Management and Budget (OMB) take steps to establish a more rigorous approach to collaboration. For example, as a first step, agencies could define and articulate goals or common outcomes for their collaborative efforts. HUD, USDA, and VA generally agreed with the recommendation; however, HUD and OMB stated that actions should wait until after the housing markets stabilized. In 2014, representatives from HUD, USDA, VA, and other agencies addressed our recommendation by signing a Joint Federal Housing Agencies Working Group Organization Charter. The charter stated that the purpose of the working group included promoting coordination and consistency in federal housing programs. It also set membership rules, voting procedures, and meeting schedules.

Our August 2012 report also found overlapping purposes in selected RHS, HUD, and Treasury multifamily programs, but differing products, areas served, and delivery methods. For example, RHS, HUD, and Treasury provide financing for development and rehabilitation of multifamily housing for low- and moderate-income households, but RHS-financed properties were more concentrated in rural areas, while properties financed through HUD and Treasury programs were more concentrated in urban and suburban areas. But for rental assistance programs, while RHS had a much higher proportion of assisted units in small town rural zip codes and isolated rural zip codes (rural zip codes) than HUD had in those areas, HUD had a greater number of assisted

[10]See GAO, *Results-Oriented Government: Practices That Can Help Enhance and Sustain Collaboration among Federal Agencies*, GAO-06-15 (Washington, D.C.: Oct. 21, 2005).

units in rural zip codes than RHS.[11] Specifically, as of 2012, HUD provided assistance to 235,828 units in rural zip codes and RHS to 176,957 (see fig.2).[12]

Figure 2: Number and Location of Selected Rental Assistance Units as of 2012



Source: GAO analysis of agency data. | GAO-15-625T

Note: Data on HUD programs are as of February 2012. Data on the RHS program are as of May 2012.

We also found that agencies had been working to coordinate multifamily programs. More specifically, HUD, USDA, and Treasury had been working to consolidate and align requirements in rental housing programs through the Interagency Rental Policy Working Group established by the White House's Domestic Policy Council in 2010. Although the working group's efforts were consistent with many key collaborative practices, our August 2012 report found that the group had not taken full advantage of opportunities to reinforce agency accountability for collaborative efforts or

[11]As we previously noted, project-based rental assistance is attached to specific properties and available to tenants only when they are living in units at these properties. RHS rental assistance is largely project-based.

[12]For this analysis, we compared the locations of all properties financed through the selected HUD, USDA, and Treasury programs using the USDA (Economic Research Service) categorization of zip codes—urban, suburban, small town rural, and isolated rural.

expanded the scope of its evaluation to include proposals that would require statutory action.[13] We recommended that the Rental Policy Working Group take steps to document collaborative efforts in strategic and annual plans to help reinforce agency accountability for these efforts. As of May 2015, this recommendation has not been implemented, and RHS indicated that it was seeking ways to formally document the results of interagency collaboration.

We also found that consolidation of similar RHS and HUD housing programs may offer an effective means for achieving long-term cost savings. We first suggested in 2000 that Congress consider requiring USDA and HUD to examine the benefits and costs of merging programs serving similar markets and providing similar products.[14] In our August 2012 report, we found that in subsequent years, certain aspects of the RHS and HUD homeownership programs grew more alike (for example, as RHS shifted from single-family direct loans toward loan guarantees). However, we indicated that the current statutory framework imposed additional challenges on the agencies' ability to consolidate similar programs. For example, HUD has noted that without legislative changes, any efforts to merge the programs likely would result in a more cumbersome delivery system. Thus, any evaluations of which programs, products, systems, and processes to retain, revise, consolidate, or eliminate would involve complex analyses, trade-offs, and difficult policy decisions. We concluded that the single-family task force offered opportunities for these agencies to identify potential areas for consolidation or greater coordination and which actions would require statutory change. We recommended that to build on efforts already under way to coordinate, consolidate, or improve housing programs, and help inform Congress's decision-making process, HUD, Treasury, USDA, and VA should evaluate and report on the specific opportunities for consolidating similar housing programs, including those that would require statutory changes. HUD, USDA, and VA generally agreed with the recommendation. However, the recommendation has yet to be implemented.

[13]For additional information on efforts of the working group, see GAO, *Managing for Results: Implementation Approaches Used to Enhance Collaboration in Interagency Groups*, GAO-14-220 (Washington, D.C.: Feb. 14, 2014).

[14]See GAO, *Rural Housing: Options for Optimizing the Federal Role in Rural Housing Development*, GAO/RCED-00-241 (Washington, D.C.: Sept. 15, 2000).

Additional Actions Are Needed to Address GAO Recommendations on Improper Rental Assistance Payments and Oversight of Farm Labor Housing

In our prior work on RHS's rental assistance and farm labor housing programs, we concluded that RHS could take additional steps to enhance program oversight and efficiency.[15] Our May 2012 report on improper rental assistance payments made seven recommendations to RHS, three of which are implemented. In a March 2011 report on oversight of the farm labor housing program, we made seven recommendations to RHS, three of which are implemented. Further actions are needed to address the remaining recommendations. The following discussion addresses selected recommendations from these reports. (See app. I for a full list of the recommendations from these reports and their status.)

Improper Rental Assistance Payments

In our May 2012 report, we found that RHS had made annual estimates of improper payments in its rental assistance program and taken steps to reduce such payments.[16] RHS generates these estimates as part of annual improper payment audits. From fiscal years 2007 through 2010, RHS reduced its reported error rate (total amount improperly paid divided by program outlays) from 3.95 percent (representing $35 million in errors) to 1.48 percent (representing $15 million in errors). RHS's error rates reported in fiscal years 2013 and 2014 were 1.79 and 1.99 percent, respectively.

However, we also found that RHS's reported error rates might understate the magnitude of the problem for several reasons, including the following:

[15]See GAO-12-624 and GAO-11-329. RHS generally agreed with the recommendations we made in these reports.

[16]An improper payment is defined by statute as any payment that should not have been made or that was made in an incorrect amount (including overpayments and underpayments) under statutory, contractual, administrative, or other legally applicable requirements. Our report focused on RHS's compliance with requirements contained in the Improper Payments Information Act of 2002 [Pub. L. No. 107-300, 116 Stat. 2350 (2002)], the Improper Payments Elimination and Recovery Act of 2010 [Pub. L. No. 111-204, 124 Stat. 2224 (2010)], and associated OMB guidance. After the issuance of our report, Congress enacted the Improper Payments Elimination and Recovery Improvement Act of 2012 [Pub. L. 112-248, 126 Stat. 2390 (2013)], which required agencies to make additional efforts to identify, recover, and prevent improper payments.

- RHS had not estimated improper payments due to unreported tenant income because it lacked the authority to match data on tenant income against federal wage and benefits databases.

- RHS had not estimated improper payments made on the behalf of deceased tenants because it had not completed steps to gain access to the Social Security Administration's (SSA) Death Master File, which could be used to match data to detect such payments.[17]

- In 2008, RHS began excluding improper payments of less than $100 from estimated error rates. However, RHS did not submit this change to OMB, which is responsible for approving agency methodologies for estimation.

Our May 2012 report also found that RHS had not fulfilled all OMB reporting requirements for improper payments. For example, USDA's Performance and Accountability Reports (1) did not contain a description of steps the agency took to ensure managers were accountable for reducing and recovering improper payments; and (2) did not fully discuss whether the agency had the internal controls, human capital, information systems, and other infrastructure to reduce improper payments.

To address limitations in RHS's detection and estimation of improper payments, in our May 2012 report we suggested that Congress consider amending the Social Security Act to grant RHS access to the National Directory of New Hires database (New Hires database) for purposes of verifying tenant incomes.[18] Although USDA drafted legislation to obtain this access, and a bill was introduced in the 113th Congress (2013–2014) to provide access, these proposals were not enacted.[19] We continue to believe that providing RHS with this access would strengthen the accuracy and integrity of RHS's payment process.

[17]The Death Master File is a national database of deceased individuals who had Social Security numbers and whose deaths were reported to SSA.

[18]The Department of Health and Human Services maintains this national database, which compiles information reported by employers to state workforce agencies and information from federal agencies. It contains information on newly hired employees, quarterly wage information for each job held by an employee, and unemployment insurance information on individuals who have received or applied for unemployment.

[19]See *Housing Assistance Eligibility Verification Act of 2013* [H.R. 2729, 113th Cong. (2013)].

In addition, we recommended that USDA do the following:

- Draft proposed legislation to grant RHS access to SSA benefits data for income verification purposes. USDA has not yet drafted this legislation. USDA officials told us that they wanted to obtain access to the New Hires database before pursuing access to the SSA benefits data.

- Complete steps to use SSA's Death Master File to identify improper payments made on behalf of deceased tenants. RHS officials told us in March 2015 that they now conduct prepayment checks against the Death Master File to avoid making improper payments to deceased tenants and that they planned to use the file to help detect improper payments in future audits.

- Submit RHS's methodology for estimating improper payments, including the use of the $100 exclusion threshold, to OMB for review. As of March 2015, RHS officials said they had prepared a draft request to USDA's Office of the Chief Financial Officer to request an OMB review of the methodology. However, RHS has yet to submit the methodology to OMB for review.

Our May 2012 report also made two recommendations to address shortcomings in RHS's reporting on improper payments. First, we recommended that RHS complete steps to ensure agency manager accountability for reducing and recovering improper payments and include a discussion of these steps in USDA's Performance and Accountability Reports. RHS addressed this recommendation in USDA's fiscal year 2012 Annual Financial Report (AFR)—the report in which USDA now reports improper payment information. Second, we recommended that RHS discuss internal controls, human capital, information systems, and other infrastructure in USDA's Performance and Accountability Reports. However, RHS has not included this discussion in the AFRs. In March 2015, RHS officials told us that the discussion was not applicable to the rental assistance program because the improper payments stem from the actions of private property managers (who request RHS rental subsidies on behalf of tenants), not from insufficient RHS resources for internal controls and infrastructure. We disagree that RHS internal controls and resources are not applicable to the rental assistance program because RHS has processes, people, and data that it uses to prevent and detect improper payments. We maintain that RHS should provide the required discussion in the AFR to better inform Congress and OMB of its capability to reduce improper payments.

Oversight of Farm Labor Housing Program

In a March 2011 report, we found that RHS could strengthen its management processes in several areas to more effectively implement and oversee the farm labor housing program. As the only federally assisted source of housing for farmworkers, the program plays an important role in constructing and rehabilitating housing. However, we concluded that a number of RHS management processes hindered the agency's ability to provide farmworkers with access to decent and safe housing and ensure compliance with program requirements, as follows:

- The enforcement mechanisms RHS used may not be effective in bringing borrowers—that is, the recipients of the program's loans and grants—into compliance in a timely manner.[20] Forms of borrower noncompliance varied in severity—from mortgage default or health and safety violations on a property to failure to submit annual budget documentation.[21] We concluded that some RHS enforcement actions were too mild (servicing letters), and others too severe (acceleration of the loan payments) to have the intended effect of returning borrowers to compliance. We recommended that RHS implement enforcement actions that could be tailored to the severity of the borrower's noncompliance. The agency agreed with this recommendation and published a proposed rule to establish civil money penalties as a "mid-level" enforcement mechanism. But according to USDA, a regulatory change is needed before Rural Development can use the services of USDA Administrative Law Judges to adjudicate civil money penalty cases.

- Although RHS staff must ensure that borrowers (or their management agents) verify tenants' income levels, the processes RHS used for verifying income were inconsistent among state offices that help

[20]The farm labor housing program may award both loan and grant funds to one recipient. Therefore, we refer to recipients as borrowers, as RHS does in its management handbooks and regulations.

[21]We previously reported that penalties in federal award programs should correspond to performance. See GAO, *Grants Management: Enhancing Performance Accountability Provisions Could Lead to Better Results*, GAO-06-1046 (Washington, D.C.: Sept. 29, 2006).

implement the program.[22] For example, some state offices used third-party income verification systems, such as a wage matching system, while other states did not have access to these verification tools. We recommended that USDA seek legislative authority to gain access to the New Hires database for data matching purposes and noted that we first recommended granting such access in 2004.[23] USDA agreed with our 2011 recommendation and, as discussed previously, proposed legislation to obtain this access. Although the legislative proposals have not been enacted, we maintain that providing RHS access to the database would improve management of the program.

- Although borrowers must verify the legal residency of tenants, we found inconsistencies in the methods RHS used to ensure borrower compliance.[24] The Citizenship and Immigration Services division of the Department of Homeland Security operates the Systematic Alien Verification for Entitlements (SAVE) program, which provides an online service for verifying legal residency documentation. This service is available, upon request, to all federal, state, and local benefit-granting agencies. As part of supervisory reviews of borrowers, we found that staff from some RHS state offices used SAVE to check whether borrowers were verifying residency status, while staff from several other offices either did not or were unaware of the program. We recommended that to better ensure that requirements for tenant eligibility were met, RHS should require staff to use the SAVE program to verify tenants' residency status during supervisory reviews. As of April 2015, RHS had not implemented this recommendation.

[22]Although state office responsibilities may vary, these offices typically accept, review, and service loans; monitor budgets; conduct fiscal and physical inspections; and engage in limited policy making and oversight of local field offices. The state office also ranks, scores, and forwards eligible applications it receives for funding to the national office. According to RHS's asset management handbook, field office staff are to provide consistent, effective oversight of properties financed by RHS to ensure that they are operated in accordance with applicable regulatory and administrative requirements.

[23]GAO, *Rural Housing Service: Updated Guidance and Additional Monitoring Needed for Rental Assistance Distribution Process*, GAO-04-937 (Washington, D.C.: Sept. 13, 2004).

[24]Only U.S. citizens or permanent residents are eligible for RHS farm labor housing units.

Preliminary Observations on Risk Management of RHS's Single-Family Loan Guarantee Program

As requested by this Subcommittee, we are conducting ongoing work on RHS that focuses on RHS's methods of estimating credit subsidy costs and risk-management practices for its single-family guarantee program.[25] In relation to risk management, we have been examining the extent to which RHS's practices are consistent with key federal requirements, including those in OMB Circular A-129 (Policies for Federal Credit Programs and Non-Tax Receivables) and federal internal control standards.[26] Overall, our work as of May 2015 indicates that while aspects of RHS's risk-management practices broadly align with selected federal requirements, other aspects are not fully consistent with requirements and leading practices. Our preliminary observations are summarized below.

RHS has policies, procedures, and practices for a number of risk-management functions addressed in OMB Circular A-129. Examples include the following:[27]

- RHS has procedures for determining borrower creditworthiness, including an automated underwriting system that helps lenders determine whether applicants qualify for an RHS-guaranteed mortgage. The procedures also require RHS field staff to perform several steps. For example, RHS field staff must review every loan application and associated loan documentation (such as the property appraisal) before the lender closes the loan.[28] If the documentation is satisfactory, RHS issues a conditional commitment to guarantee the loan, which may require the lender to satisfy certain conditions before proceeding to loan closing. Once the lender closes the loan and submits the closing package to RHS, RHS field staff must conduct a

[25]The credit subsidy cost for loan guarantees is the net present value of the difference between projected cash flows to and from the government over the lifetime of the loans.

[26]GAO, *Standards for Internal Control in the Federal Government*, GAO/AIMD-00-21.3.1 (Washington, D.C.: November 1999).

[27]While we are not testing RHS's compliance with the policies and procedures as part of our ongoing review, we are reviewing audits by USDA's Office of the Inspector General that have included compliance testing and are reviewing information on RHS's actions to address the Inspector General's recommendations.

[28]Lenders must submit more documentation to RHS for loans that are manually underwritten than for those underwritten using the automated system and for which the system provided an "accept" decision.

final review to determine whether the lender met the conditions before issuing the loan guarantee.

- RHS has policies and procedures for overseeing lenders that underwrite or service RHS-guaranteed mortgages. For example, lenders must meet eligibility standards prescribed in regulation and apply to RHS for approval. RHS procedures require RHS field and contractor staff to conduct periodic desk or on-site reviews of lenders and servicers, and RHS has developed risk-based criteria to guide the selection of lenders and servicers for review. RHS staff must prepare written reports on their findings, and the lenders and servicers must respond in writing to any report recommendations. RHS also has documented procedures for reviewing lender loss claims on guaranteed loans that have defaulted.

- RHS has established a risk appetite—the amount and type of risk an organization is willing to accept in pursuit of its objectives—for the single-family guarantee program. According to RHS officials, the program's risk appetite is expressed primarily through the goal of making each annual cohort of loan guarantees "subsidy-neutral," while keeping guarantee fees at a level affordable to low- and moderate-income households. In the budgetary context, subsidy-neutral means that, initially, the present value of lifetime estimated cash inflows (for example, guarantee fees) equals the present value of lifetime estimated cash outflows (for example, loss claims).[29]

Our ongoing work indicates that RHS also has been making a number of enhancements to its risk-management practices. Chief among these is the development of an econometric model intended to support analysis of RHS's guaranteed portfolio and help estimate credit subsidy costs for the single-family guarantee program. According to RHS officials, the model will help the agency better estimate the effects of market and policy changes on portfolio performance and improve management of program risks. RHS expects that development of the model will be completed in December 2015. RHS also has proposed regulations that would strengthen its authority to require lenders to indemnify (compensate) RHS for loss claims on defaulted loans that were not properly underwritten. Current regulations authorize RHS to seek indemnification within 24 months of loan closing when RHS concludes that the lender did not

[29]Actual subsidy costs may differ from the initial estimates.

comply with the agency's underwriting standards. In March 2015, RHS issued a proposed rule that, among other things, would increase the indemnification period to 5 years.[30] Additionally, Rural Development is exploring the appointment of a Chief Risk Officer, in response to a congressional report directive and consistent with OMB Circular A-129 requirements.[31]

Based on our ongoing work, we have found elements of RHS's risk management that are not fully consistent with federal requirements and leading practices, which may limit the effectiveness of RHS's overall risk-management efforts. Examples include the following:

- **Limitations in performance benchmarks.** While RHS uses a number of benchmarks to assess the performance of its guaranteed portfolio, two key benchmarks have limitations that diminish their usefulness. In particular, these benchmarks are not fully consistent with certain attributes of successful performance measures—such as objectivity and reliability—that we identified in prior work.[32] According to RHS officials, since 2004, they have compared the overall delinquency and foreclosure rates for RHS's portfolio with corresponding rates for FHA's insured portfolio of 30-year fixed-rate mortgages.[33] RHS has established performance goals stating that RHS should be within a specified range of FHA's delinquency and foreclosure rates at the end of each fiscal year. Although RHS generally has met these goals, using FHA's performance as a benchmark may not provide objective and reliable information for risk management. The weakness in the benchmark is two-fold. First, a simple comparison of two portfolios ignores potential differences in their composition—for example, in the age and geographic distribution of loans—that may influence loan performance and make

[30]See 80 Fed. Reg. 11950 (Mar. 5, 2015). In cases in which RHS determines that fraud or misrepresentation occurred in the origination of the loan, the existing regulation authorizes RHS to seek indemnification regardless of when the loan was closed. The proposed rule would clarify that RHS could seek indemnification in those cases regardless of when the loan was closed or when the default occurred.

[31]See H.R. Rep. No. 468, 113th Cong., 2nd Sess. at 37-38 (2014).

[32]GAO, *Tax Administration: IRS Needs to Further Refine Its Tax Filing Season Performance Measures*, GAO-03-143 (Washington, D.C.: Nov. 22, 2002).

[33]RHS generally guarantees only 30-year fixed-rate mortgages, while FHA guarantees 15-year and 30-year fixed-rate and adjustable-rate mortgages.

comparisons of the portfolios invalid.[34] Second, it implies that FHA has been effectively managing its risk. However, FHA has at times exhibited shortcomings in this area. For example, in a 2006 report, we found that FHA had not developed sufficient standards and controls to manage risks associated with the substantial proportion of FHA-insured loans with down-payment assistance.[35]

- **Lack of formal procedures for a key committee.** RHS does not have written procedures for a key part of its risk-management structure. Specifically, since 2009 RHS has had a Credit Policy Committee that, according to RHS officials, meets regularly to detect, discuss, and analyze credit quality issues and address them through policy changes. According to federal internal control standards, agencies should have effective control activities, including policies and procedures, to help mitigate risks and should document significant events. However, the Credit Policy Committee operates without policies and procedures describing its purpose, scope, membership, or decision-making process. RHS also has not defined the roles and responsibilities of committee members and does not prepare minutes of meeting discussions and results.

- **Key relationships not documented.** RHS has not documented the relationships between the agency components that have risk-management functions and responsibilities. OMB Circular A-129 states that federal credit agencies should codify clearly defined lines of authority and communication. RHS's risk-management structure is decentralized and complex. According to RHS officials, it involves staff in 47 state offices; the Centralized Servicing Center and National Financial and Accounting Operations Center in St. Louis, Missouri; and USDA headquarters. Although RHS has basic organizational charts for these components of the risk-management structure, it has not documented the lines of authority or communication among them.

[34]For example, if a portfolio were concentrated in a strong housing market or included a high proportion of recent loans that had had little time to default, it would have a lower foreclosure rate than a portfolio with the opposite characteristics, all other things being equal. Therefore, not accounting for the different composition of the two portfolios could lead to incorrect conclusions about how well the portfolios were being managed.

[35]GAO, *Mortgage Financing: Additional Action Needed to Manage Risks of FHA-Insured Loans with Down Payment Assistance*, GAO-06-24 (Washington, D.C.: Nov. 9, 2005).

As we complete our ongoing work, we will determine whether additional actions are needed by RHS to rectify these issues. We will consider making recommendations, as appropriate, in our final report.

In conclusion, our reviews of RHS housing assistance programs since 2011 have identified a number of areas in which RHS could strengthen its program oversight and enhance collaboration and consolidation efforts. RHS has made progress in implementing some of our recommendations, but additional actions are needed to address others. Additionally, our ongoing work has identified shortcomings in certain aspects of RHS's risk management for the single-family guarantee program. To operate as efficiently and effectively as possible, it will be important for RHS to sustain the improvements it has made, implement outstanding audit recommendations, and address any future recommendations we may make in a timely manner.

Chairman Luetkemeyer, Ranking Member Cleaver, and Members of the Subcommittee, this concludes my prepared statement. I would be happy to respond to any questions that you may have at this time.

GAO Contact and Staff Acknowledgments

For further information about this testimony, please contact me at 202-512-8678 or sciremj@gao.gov. Contact points for our Offices of Congressional Relations and Public Affairs may be found on the last page of this statement. Individuals making key contributions to this testimony include Steve Westley, Assistant Director; Melissa Kornblau, Analyst-in-Charge; Alexandra Martin-Arseneau; Andy Finkel; John McGrail; Marc Molino; Barbara Roesmann; and Julie Trinder-Clements.

Appendix I: Content and Status of Relevant GAO Recommendations

The following table summarizes the status of our prior recommendations to USDA from our August 2012, May 2012, and March 2011 reports that discuss RHS housing assistance programs. We classify each recommendation as either open (the agency has either not taken or completed steps to implement the recommendation) or implemented. The recommendations are listed by report.

Table 1: Status of Recent GAO Recommendations Concerning RHS, May 2015

Product	Recommendation	Status
GAO-12-554: Housing Assistance: Opportunities Exist to Increase Collaboration and Consider Consolidation, (August 2012)		
	To enhance task force efforts to evaluate the potential for coordination or consolidation of single-family housing programs and activities, the Secretaries or other designated officials of HUD, USDA, and VA, and the Director of OMB should take steps to establish a more rigorous approach to collaboration. For example, as a first step, agencies could define and articulate goals or common outcomes and identify opportunities that can be addressed or problems solved through their collaborative efforts. Enhancing the task force's efforts also could entail establishing and implementing a written agreement; specifying roles and responsibilities; establishing mechanisms to monitor, evaluate, and report on results; and reinforcing accountability for collaborative efforts.	Implemented
	To further improve HUD, USDA, and Treasury's efforts through the Rental Policy Working Group to consolidate and align certain requirements in multifamily housing programs, the Rental Working Group should take steps to document collaborative efforts in strategic and annual plans to help reinforce agency accountability for these efforts.	Open
	To build on task force and working group efforts already underway to coordinate, consolidate, or improve housing programs, and help inform Congress's decision-making process, the Secretaries or other designated officials of HUD, Treasury, USDA, and VA should evaluate and report on the specific opportunities for consolidating similar housing programs, including those that would require statutory changes.	Open
GAO-12-624: Rural Housing Service: Efforts to Identify and Reduce Improper Rental Assistance Payments Could be Enhanced, (May 2012)		
	To help estimate, reduce, and recover improper payments in the Section 521 rental assistance program, the Secretary of Agriculture should draft proposed legislation for congressional consideration that would grant RHS access to SSA benefits data for purposes of verifying tenant incomes.	Open
	To help estimate, reduce, and recover improper payments in the Section 521 rental assistance program, the Secretary of Agriculture should submit RHS's methodology for estimating improper payments, including use of the $100 exclusion threshold, to OMB for review.	Open
	To help estimate, reduce, and recover improper payments in the Section 521 rental assistance program, the Secretary of Agriculture should consider examining payment processing errors as part of the next improper payments audit to provide more current information on whether these errors are significant.	Implemented
	To help estimate, reduce, and recover improper payments in the Section 521 rental assistance program, the Secretary of Agriculture should, in conducting the annual improper payments audit, either count all payments made on behalf of tenants with signed but undated Tenant Certification forms as improper or revise the audit procedure to classify such payments as proper when an acceptable certification date can be imputed from other documents.	Implemented

Product	Recommendation	Status
	To help estimate, reduce, and recover improper payments in the Section 521 rental assistance program, the Secretary of Agriculture should complete steps to use SSA's Death Master File—potentially utilizing the batch-processing option offered through Treasury's 'Do Not Pay" web portal—to identify improper payments made on behalf of deceased tenants and use this capability in conducting the annual improper payments audit and for ongoing oversight of program payments.	Open
	To help estimate, reduce, and recover improper payments in the Section 521 rental assistance program, the Secretary of Agriculture should complete steps to ensure that RHS managers are held accountable for reducing and recovering improper payments in the rental assistance program and include a discussion of the accountability steps in USDA's Performance and Accountability Reports.	Implemented
	To help estimate, reduce, and recover improper payments in the Section 521 rental assistance program, the Secretary of Agriculture should include a discussion in USDA's Performance and Accountability Reports of whether RHS has the internal controls, human capital, information systems, and other infrastructure to reduce improper rental assistance payments to targeted levels.	Open
GAO-11-329: Rural Housing Service: Opportunities Exist to Strengthen Farm Labor Housing Program Management and Oversight, (March 2011)		
	To better ensure that Farm Labor Housing (FLH) funds obligated but unliquidated are efficiently used to provide farm labor housing, the Secretary of Agriculture should direct the Administrator of RHS to issue guidance on obligation expiration dates and make all RHS staff in the state and local offices aware of the guidance and how to implement it.	Implemented
	To help ensure that reliable program costs are estimated in future years, the Secretary of Agriculture should direct the Administrator of RHS, on an annual basis, to work with budget staff to investigate key assumptions, including comparing these assumptions to actual program performance, in order to explain unusual fluctuations impacting the credit subsidy rate used in budget formulation.	Open
	To better ensure that requirements for tenant eligibility are met across the FLH portfolio, the Secretary of Agriculture should direct the Administrator of RHS to seek legislative authority to gain access to the Department of Health and Human Services' National Directory of New Hires and make this information available to RHS so that they can assess the accuracy of tenant income documentation during supervisory reviews and other oversight activities.	Implemented
	To better ensure that requirements for tenant eligibility are met across the FLH portfolio, the Secretary of Agriculture should direct the Administrator of RHS to require its loan servicers to use the Systematic Alien Verification and Entitlements program administered by the Department of Homeland Security to verify tenant's residency status during supervisory reviews.	Open
	To help resolve identified borrower noncompliance in a timely manner, the Secretary of Agriculture should direct the Administrator of RHS to implement enforcement mechanisms that can be tailored to the severity of the borrower noncompliance, such as the civil money penalty enforcement provision in its program regulations.	Open
	To better determine and track compliance across the portfolio, the Secretary of Agriculture should direct the Administrator of RHS to implement mechanisms to improve the specificity and timely reporting of its compliance review information—such as findings data and performance grade data in the Multi-Family Housing Information System.	Implemented
	The Secretary of Agriculture should direct the Administrator of RHS to better utilize available data on demand for the FLH program—such as systematically reviewing local market analyses, further analyzing occupancy data on a statewide, regional, or national level, and retaining and analyzing application information—to help target available funding to areas of greatest need.	Open

Appendix II: Accessible Data

Data Table for Figure 1: Number of Single-Family Loan Guarantees Servicing Low- and Moderate-Income Borrowers, Fiscal Year 2009

Number of loan guarantees (in thousands) servicing nonmetropolitan counties

	Metropolitan counties	Urbanized nonmetropolitan counties	Rural nonmetropolitan counties	Completely rural nonmetropolitan counties
HUD (< or = 115%)	1228.46	60.798	48.701	7.588
RHS guaranteed	68.222	20.679	27.756	3.734

Source: GAO analysis of agency data. GAO-15-625T.

Note: Low- and moderate-income borrowers are those with incomes at or below 115 percent of area median income.

Abbreviations: HUD = Department of Housing and Urban Development, RHS = Rural Housing Service.

Data Table for Figure 2: Number and Location of Selected Rental Assistance Units as of 2012

Number of units (in thousands) by zip code type

	Urban zip codes	Suburban zip codes	Small town rural zip codes	Isolated rural zip codes
HUD project-based rental assistance	1063.3	44.135	141.078	94.75
RHS Section 521	35.316	44.833	67.437	109.52

Source: GAO analysis of agency data. GAO-15-625T.

Note: Data on HUD programs are as of February 2012. Data on the RHS program are as of May 2012.

Abbreviations: HUD = Department of Housing and Urban Development, RHS = Rural Housing Service.

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