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Community Developments

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Fact Sheet

Rural Housing Service Single Family Housing Guaranteed Loan Program

Community Developments Fact Sheets are designed to share information about programs and initiatives of bankers and community development practitioners. These fact sheets differ from Office of the Comptroller of the Currency (OCC) bulletins and regulations in that they do not reflect agency policy and should not be considered regulatory or supervisory guidance. Some of the information used in the preparation of this fact sheet was obtained from publicly available sources. These sources are considered reliable and current, as of May 2020, but the use of this information does not constitute an endorsement of its accuracy by the OCC.

The information in this *Community Developments Fact Sheet* is consistent with the requirements set forth by the Rural Housing Service's regulation, 7 CFR 3555, and the *Rural Housing Service's Single Family Housing Guaranteed Loan Program Technical Handbook.*

This *Community Developments Fact Sheet* explains how the Rural Housing Service (RHS) guarantees qualifying mortgages made by RHS-approved national banks and federal savings associations (collectively, banks).

Introduction

The RHS, an agency of the U.S. Department of Agriculture (USDA), offers a variety of programs to build or improve housing and essential community facilities in rural areas.

The RHS provides direct loans (made and serviced by the USDA) and guarantees mortgage loans originated and serviced by approved lenders, including banks. This fact sheet focuses on RHS-guaranteed loans to finance the purchase of single-family residences.

The RHS Single Family Housing Guaranteed Loan Program (RHS Guaranteed Loan Program) is designed to provide low- and moderate-income borrowers with an opportunity to own adequate, decent, safe, and sanitary dwellings as their primary residence in eligible rural areas.[1]

Program Basics

Under the RHS Guaranteed Loan Program, an RHS-approved lender makes the loan directly to an eligible borrower, and the RHS guarantees 90 percent of the loan. This guarantee substantially reduces the risk for lenders, encouraging them to make loans to low- and moderate-income borrowers who have little collateral.

Loans are available to eligible borrowers regardless of whether they have previously

[1] Refer to the Single Family Housing Guaranteed Loan Program website.

owned a home. The program is limited to 30-year fixed-rate mortgages.

An adjusted annual income limit that varies by property location determines whether the borrower is eligible to participate in the RHS Guaranteed Loan Program. The maximum loan amount is based on what the borrower can afford, as determined by the borrower's income and repayment ability. Housing and total debt ratios determine a borrower's repayment ability. The maximum loan amount generally cannot exceed the property's fair market value. The loan-to-value may exceed 100 percent of the fair market value of the property only if the excess is used to finance the guarantee fee. Loan proceeds may be used for the purchase or refinance of a primary residence, as well as certain other reasonable and customary expenses, repairs, or improvements.

The RHS assesses an up-front guarantee fee for all loans. As of September 12, 2019, the up-front guarantee fee is 1 percent of the loan amount.[2] This fee is charged to the lender but may be passed on to the borrower.

The RHS also charges lenders an annual fee for each guaranteed loan. As of September 12, 2019, the annual fee is 0.35 percent of the loan amount,[3] which the lender may pass on to the borrower. Lenders that pass the annual fee on to the borrower typically collect the fee as part of the monthly mortgage payment. Lenders are responsible for remitting annual fee payments to the RHS.

What Are the Benefits of the Program?

The RHS Guaranteed Loan Program gives banks the opportunity to lend to consumers with low or moderate incomes who may be having trouble obtaining mortgages. Unlike conventional mortgages, RHS-guaranteed loans have no down payment requirement, allowing a borrower to obtain financing for up to 100 percent of a home's purchase price. RHS-guaranteed loans do not require private mortgage insurance. These loans also do not require a minimum credit score, allowing lenders to accept nontraditional credit histories as evidence that the borrower has the ability and willingness to meet repayment obligations.

Lenders may use all eligible assistance programs to enhance the borrower's ability to afford the loan (e.g., mortgage credit certificates and Section 8 Homeownership Voucher). The RHS has no limits on the dollar amount of gifts, grant fund programs, or down payment assistance that is used in connection with the guaranteed loan. Concessions provided by a seller or other interested third party are limited to 6 percent of the property's sale price, unless otherwise provided by the RHS,

If the bank originates a mortgage under the RHS Guaranteed Loan Program and otherwise complies with the RHS regulation, RHS-guaranteed mortgages are considered qualified mortgages.[4] Under Regulation Z, which implements the Truth in Lending Act, a bank can receive a conclusive presumption of compliance, or a safe harbor, for qualified mortgages because they are presumed to meet the Regulation Z ability to repay standards.[5]

[2] Refer to the [Fiscal Year 2020 Conditional Commitment Notice].

[3] Ibid.

[4] Refer to 7 CFR 3555.109.

[5] Refer to 12 CFR 1026.43(e)(1) and 84 Fed. Reg. 37155, footnote 20 (July 31, 2019).

How Can Banks Participate?

A lender must meet certain requirements to be approved to participate in the RHS Guaranteed Loan Program. Banks should review the application and eligibility information in the *RHS Single Family Housing Guaranteed Loan Program Technical Handbook (Lender's Handbook).*

The RHS may approve federally supervised lenders, including banks supervised by the Office of the Comptroller of the Currency (OCC), to participate in the program if they submit documentation to the RHS showing their ability to originate, underwrite, and service single-family home loans and meet other requirements.

A bank may demonstrate its ability to originate and underwrite loans by submitting the appropriate documentation to the RHS, including

- a summary of residential mortgage lending activity.
- written criteria outlining its policies and procedures for originating, underwriting, and closing residential mortgage loans.
- evidence of an experienced loan underwriter on staff.

A bank may demonstrate its ability to service loans by submitting appropriate documentation to the RHS, including

- written servicing policies and procedures.
- a written plan if the bank contracts for escrow services.
- evidence that the bank has serviced single-family residential mortgage loans in the year before applying to participate in the RHS Guaranteed Loan Program.

A bank that does not intend to service the RHS-guaranteed loans it originates must certify that it will contract its servicing with a USDA-approved lender that meets the criteria to participate in the program as a servicer.

How Do Individuals Qualify?

In addition to meeting certain underwriting requirements, borrowers must certify to the bank that they are unable to obtain a traditional conventional mortgage without the RHS guarantee.

Income Limits

At the time of loan approval, the household's adjusted income must not exceed the applicable moderate-income limit.

Lenders must obtain and maintain documentation of three borrower income categories: annual income, adjusted annual income, and repayment income.

Annual income: Annual income includes all the income of adult household members regardless of whether they are a party to the loan (household income). Annual income includes all current verified income, either part time or full time, received by the borrower and all other adult members of the household—subject to the exclusions in the *Lender's Handbook*. Annual income also includes income of less than 12 months' duration, such as seasonal income, commissions, overtime bonuses, and unemployment income.[6] After total annual

[6] Income of less than 12 months' duration is computed as the estimated annual amount of such income for the upcoming 12 months.

income is determined, eligible adjustments are subtracted to derive adjusted annual income.

Adjusted annual income: Adjusted annual income is used to determine program eligibility. A household's adjusted annual income is calculated as annual income minus eligible deductions listed in the *Lender's Handbook*. The household income must not exceed the adjusted annual income limit based on its household size for the state and county where the property is located. The adjusted annual income limit is 115 percent of the area's median income. Visit the [USDA Income and Property Eligibility]() website to determine adjusted annual income eligibility.

Repayment income: Repayment income is the amount of stable and dependable income from all sources that parties to a loan are expected to receive. Repayment income is used to calculate housing and total debt ratios and determine the borrower's ability to repay the loan in addition to the borrower's other recurring debt. The repayment income calculation may differ from the annual income calculation because some household members may not be a party to the loan, or because some income sources may not be deemed stable and dependable by the lender. It is common for annual income to be higher than repayment income. Also, repayment income includes some income sources excluded for the purpose of adjusted income.

Debt Ratios

The RHS uses two ratios to determine the repayment ability of the borrower:

- **Principal, interest, real estate taxes, homeowner's insurance (PITI):** Typically, PITI must not exceed 29 percent of the borrower's gross monthly repayment income. The RHS may allow exceptions if certain compensating factors exist.
- **Total debt (TD):** TD consists of PITI plus other monthly debt repayments. Typically, TD must not exceed 41 percent of the borrower's gross monthly repayment income. The RHS may allow exceptions if certain compensating factors exist.

Credit History

Borrowers generally must have a verifiable credit history that indicates a reasonable ability and willingness to meet debt obligations. If a borrower has a history of "significant derogatory credit," such as a foreclosure or bankruptcy within the 36 months before applying for the loan, the lender may consider such extenuating circumstances during underwriting.

Borrowers who do not have a traditional credit history may still be eligible for loan consideration. In such cases, lenders may use alternative methods as evidence of a borrower's ability and willingness to pay, such as a nontraditional mortgage credit report or multiple independent verifications of trade references.

When relying on a nontraditional credit history, a lender must develop a borrower's credit profile based on at least two trade lines. The lender may rely on two trade lines when one of them is 12-month verification of rent. When there is no documentation of rent history, the borrower must provide at least three trade lines.

Nontraditional trade lines must have a 12-month history and cannot have been closed more than six months before the loan application's submission. Examples of acceptable trade lines include

- rental or housing payment.
- utility payment records.
- insurance payments.
- payments to a retail store.

Nontraditional trade lines may not be used to offset derogatory references in traditional credit information.

Property Eligibility

A residence to be purchased and financed under the RHS Guaranteed Loan Program must be located in an eligible rural area as defined by the RHS.[7] Lenders can use the RHS website to determine property eligibility. Guaranteed loans are for single-family primary residences. Properties that include buildings or land specifically used for agricultural business or other income-producing activities are ineligible.

Existing homes must meet the U.S. Department of Housing and Urban Development's (HUD) minimum property standards for one- to four-unit dwellings. Condominium units are eligible if they are in condominium projects that meet the requirements of 7 CFR 3555, as well as the condominium standards established by HUD, the U.S. Department of Veterans Affairs, Fannie Mae, or Freddie Mac. New construction also is eligible, and the RHS may issue a loan note guarantee before construction begins. Guidelines on new construction are in the *Lender's Handbook*.

Charges and Fees

The RHS allows a lender to charge reasonable lender fees (such as an origination fee) if the charges and fees do not exceed those the lender charges to other applicants for similar types of loan transactions. An RHS guaranteed loan must meet, among other things, the point and fee limits under Regulation Z to be considered a qualified mortgage.[8]

Other Considerations

Indemnification

If the RHS determines that a lender did not originate a loan in accordance with RHS requirements, and the RHS pays a loss claim under the guarantee as a result of the originating lender's nonconforming action or failure to act, the RHS may require the originating lender to indemnify the RHS for the loss and may revoke the originating lender's status as an eligible lender.

Federal Home Loan Bank Mortgage-Backed Security Program

The Federal Home Loan Bank (FHLB) of Chicago issues securities backed by government-insured or government-guaranteed mortgages originated by FHLB member financial institutions, including loans made under the RHS Guaranteed Loan Program. The secondary market conduit product, Mortgage Partnership Finance government mortgage-backed securities, can provide lenders, particularly smaller institutions that lack direct access to the secondary mortgage market, with a source of liquidity.

Community Reinvestment Act

Generally, RHS-guaranteed loans originated for low- and moderate-income borrowers' purchase of homes located in a bank's

[7] See RHS eligibility maps for areas that are eligible for the loan guarantee.

[8] Refer to 12 CFR 1026.43(e)(3).

assessment area(s) would be considered under the applicable lending test.[9] Because the RHS income levels generally differ from the Community Reinvestment Act (CRA) income levels, banks should compare the borrower income limits with the income limits defined under the CRA.[10]

OCC Resources

- *Community Developments Fact Sheet*, "FHLB Government Mortgage-Backed Security Program: Facilitating Secondary Market Access"
- OCC Community Affairs Contacts

[9] Refer to 12 CFR 25.22 and 25.26(b)-(c) (national banks) and 12 CFR 195.22 and 195.26(b)-(c) (federal savings associations).

[10] Refer to 12 CFR 25.12(m) (national banks) and 195.12(m) (federal savings associations).