Congressional Budget Office
Cost Estimate

June 28, 2019

At a Glance

H.R. 3141, FHA Loan Affordability Act of 2019

As ordered reported by the House Committee on Financial Services on June 11, 2019

By Fiscal Year, Millions of Dollars	2019	2019-2024	2019-2029
Direct Spending (Outlays)	0	0	0
Revenues	0	0	0
Deficit Effect	0	0	0
Spending Subject to Appropriation (Outlays)	0	13,910	n.e.

Statutory pay-as-you-go procedures apply?	No	**Mandate Effects**	
		Contains intergovernmental mandate?	No
Increases on-budget deficits in any of the four consecutive 10-year periods beginning in 2030?	No	Contains private-sector mandate?	No

n.e. = not estimated.

The bill would

- Require the Federal Housing Administration to end a borrower's annual mortgage insurance premiums when the outstanding mortgage principal balance falls below 78 percent of the property value that was determined when the mortgage was issued
- Apply that requirement to mortgages insured after enactment of H.R. 3141

Estimated budgetary effects would primarily stem from

- Reducing the insurance premiums collected by the Federal Housing Administration and the Government National Mortgage Association

Areas of significant uncertainty include

- Accurately projecting how demand for Federal Housing Administration mortgage insurance would change under the bill

Detailed estimate begins on the next page.

See also *CBO's Cost Estimates Explained*, www.cbo.gov/publication/54437;
How CBO Prepares Cost Estimates, www.cbo.gov/publication/53519; and *Glossary*, www.cbo.gov/publication/42904.

Bill Summary

H.R. 3141 would require the Federal Housing Administration (FHA) to stop charging annual mortgage insurance premiums to borrowers whose outstanding principal balance falls below 78 percent of what the property's value was at the time of the mortgage origination (such a ratio is commonly referred to as a loan to value ratio or LTV). The changes made by the bill would affect mortgages insured by FHA after enactment of H.R. 3141.

Estimated Federal Cost

The estimated budgetary effect of H.R. 3141 is shown in Table 1. The costs of the legislation fall within budget function 370 (commerce and housing credit).

Table 1.
Estimated Increases in Spending Subject to Appropriation Under H.R. 3141

	By Fiscal Year, Millions of Dollars						
	2019	2020	2021	2022	2023	2024	2019-2024
FHA Insurance							
Estimated Authorization	0	2,260	2,590	2,950	3,160	3,410	14,370
Estimated Outlays	0	2,260	2,590	2,950	3,160	3,410	14,370
Ginnie Mae							
Estimated Authorization	0	-95	-80	-90	-95	-100	-460
Estimated Outlays	0	-95	-80	-90	-95	-100	-460
Total Changes[a]							
Estimated Authorization	0	2,165	2,510	2,860	3,065	3,310	13,910
Estimated Outlays	0	2,165	2,510	2,860	3,065	3,310	13,910

FHA = Federal Housing Administration; Ginnie Mae = Government National Mortgage Association

a. Using the fair-value approach, CBO estimates that implementing H.R. 3141 would increase costs to FHA and Ginnie Mae by $20.7 billion over the 2020-2024 period. As shown in the table, using a FCRA approach, CBO estimates that implementing H.R. 3141 would decrease offsetting collections generated by FHA and Ginnie Mae by about $ 13.9 billion over the 2020-2024 period

Basis of Estimate

For this estimate, CBO assumes that H.R. 3141 will be enacted near the end of fiscal year 2019 before fiscal year 2020 appropriations for FHA have been enacted but late enough in the year that it will not apply to mortgage guarantees made in 2019. If H.R. 3141 were enacted after 2020 appropriations were completed it would increase direct spending. For this estimate, CBO also assumes that future appropriation acts will authorize FHA to increase the amount of mortgage guarantees it provides by an amount sufficient to meet the increased demand for mortgage guarantees under the bill.

Background

FHA provides mortgage insurance for the purchase, refinance, and rehabilitation of single-family homes and charges up-front and annual premiums to mortgagors. Those premiums are classified in the budget as offsetting collections, and reduce spending subject to appropriation. Under current law, FHA requires borrowers to pay annual mortgage insurance premiums for the life of the loan for mortgages that have initial LTVs greater than 90 percent. For mortgages with initial LTVs less than 90 percent, borrowers must pay annual premiums for the first 11 years of the mortgage term.

To estimate the budgetary effects of loan guarantees, CBO uses the methodology specified in the Federal Credit Reform Act (FCRA). On that basis, CBO estimates that the net present value of the premiums collected by FHA for all mortgage guarantees under current law will exceed the cost of any default losses on the insured loans in each year. [1] Currently, CBO estimates that FHA's insurance program will have a subsidy rate of -2.69 percent in 2020. A negative subsidy occurs when the net present value of all premiums charged for a loan guarantee is greater than the estimated default costs associated with that guarantee.

The Government National Mortgage Association (Ginnie Mae) guarantees securities backed by pools of mortgages that are insured by federal agencies such as FHA. Typically, 93 percent of FHA mortgages are pooled into mortgage-backed securities (MBSs) and guaranteed by Ginnie Mae in the first few months after they are originated. In exchange for the Ginnie Mae guarantee, issuers pay a fee on the pooled mortgages that back those securities. CBO estimates that the net present value of the fees collected by Ginnie Mae will exceed the cost of any default losses on those securities in each year. Using the methodology specified in FCRA, CBO estimates that Ginnie Mae's MBS program will have a subsidy rate of -0.29 percent in 2020.

Spending Subject to Appropriation

CBO estimates that implementing H.R. 3141 would increase discretionary spending by reducing the offsetting collections attributed to FHA mortgage insurance by about $14.4 billion over the 2020-2024 period. The bill also would increase Ginnie Mae's offsetting collections by $460 million over that same period—leading to a net increase in discretionary spending of $13.9 billion over the 2020-2024 period.

FHA Insurance. CBO estimates that enacting H.R. 3141 would have two effects on the FHA program. First by limiting the time period that annual premiums can be charged,

1. A present value expresses a flow of past and future income or payments as a single amount received or paid at a specific time. The value depends on the rate of interest, known as the discount rate, used to translate past and future cash flows into current dollars at that time. The budgetary effects for FHA's guarantees are calculated under procedures specified in FCRA. Under FCRA, projected future cash flows are discounted to the present using interest rates on Treasury Securities.

H.R. 3141 would lower the lifetime collections of premiums that FHA would receive from many borrowers. Under current law the majority of FHA mortgages for newly purchased properties will reach an LTV of 78 percent after about 11 years and FHA guarantees of refinanced mortgages will reach that level more quickly. Accounting for the shorter period of time that such annual premiums would be charged, CBO estimates that implementing H.R. 3141 would increase FHA's mortgage insurance program's subsidy rate to -1.38 percent in 2020. Over the 2021-2024 period CBO estimates that the FHA subsidy rate would increase by a commensurate amount relative to our current law projections in each year.

Second, CBO estimates that limiting the period that FHA could charge annual premiums would increase demand for FHA mortgage insurance relative to mortgages backed by private mortgage insurance and result in a surge in refinancing of existing FHA mortgages. Using information about the change in demand for FHA guaranteed mortgages that stemmed from previous changes to annual premiums, CBO estimates that implementing H.R. 3141 would shift about $160 billion worth of mortgage volume from the private market to FHA over the 2020-2024 period. For comparison, in 2018 FHA guaranteed mortgages worth $209 billion and CBO estimates that the private market guaranteed about $280 billion worth of mortgages. Furthermore, CBO estimates there also would be a one-time increase in refinancings of FHA mortgages issued prior to enactment of H.R. 3141 so that those borrowers could receive the more favorable insurance premium treatment. Using information on refinancing practices associated with prior FHA rate changes, CBO estimates that implementing H.R. 3141 would lead to an increase in such refinancing totaling $10 billion in 2020.

Taking into account the estimated increase in both subsidy rate and volume of FHA insured mortgages, CBO estimates that implementing H.R. 3141 would decrease discretionary offsetting collections (and thus increase discretionary costs) from the FHA mortgage insurance program by about $14.4 billion over the 2020-2024 period.

Ginnie Mae. The estimated increase in FHA loan volume would increase the amount of mortgages that could be securitized by Ginnie Mae. Under H.R. 3141, CBO estimates that 93 percent of the additional FHA mortgages would be included in Ginnie Mae's MBS program. Because H.R. 3141 would not change the fees charged by Ginnie Mae, CBO's estimated subsidy rate for Ginnie Mae (-0.29 percent over the 2020-2024 period) would not change. CBO expects that Ginnie Mae would guarantee 93 percent of the $170 billion worth of additional FHA loan volume that CBO estimates would occur over the 2020-2024 period under the bill. On that basis, CBO estimates that implementing the bill would increase offsetting collections (and thus reduce discretionary costs) from Ginnie Mae's MBS program by $460 million over the 2020-2024 period.

Uncertainty

This estimate is uncertain because it is hard to predict how responsive the demand for FHA insurance would be to the changes made by H.R. 3141. If the lower premiums under the bill would increase demand for FHA mortgages by more than CBO estimates, there would be a larger increase in volume and the cost of H.R. 3141 would be lower. Conversely, if the lower premiums affected demand to a lesser extent than CBO estimates, there would be a smaller increase in volume and a higher cost to H.R. 3141.

Alternative Budgetary Treatment

The estimated cost of H.R. 3141 depends on the method used to calculate the subsidy rate for mortgages insured by FHA. Under current law, the budgetary effects of FHA's mortgage insurance program are measured in the budget according to the procedures established in FCRA. However, as required by S. Con. Res 71, the Concurrent Resolution on the Budget for Fiscal Year 2018, CBO also has prepared a cost estimate for H.R. 3141 using a fair-value approach to estimating the budgetary effect on FHA.

The fair-value approach is an alternative to the approach specified in FCRA. Both approaches rely on the same projections of future cash flows for guarantee programs, and both account for the lifetime cost of the new guarantees made in a given year (including the expected cost of losses net of fees collected). The fair-value estimates differ from FCRA estimates by recognizing that the government's assumption of financial risk has a cost that exceeds the average amount of losses that would be expected from defaults. The higher financial risk is reflected in higher fees private entities charge for similar guarantees on the basis of market prices. In practice, the main difference between FCRA estimates and fair-value estimates is the discount rate used to calculate the present value of estimated future guarantee costs and receipts. Fair-value estimates use higher discount rates that incorporate a premium for market risk.

Using the fair-value approach, CBO estimates that implementing H.R. 3141 would increase costs to FHA and Ginnie Mae by about $20.7 billion over the 2020-2024 period.

Pay-As-You-Go Considerations: None.

Increase in Long-Term Deficits: None.

Mandates: None.

Estimate Prepared By

Federal Costs: Robert Reese

Mandates: Rachel Austin

Estimate Reviewed By

Kim P. Cawley
Chief, Natural and Physical Resources Cost Estimates Unit

H. Samuel Papenfuss
Deputy Assistant Director for Budget Analysis

Theresa Gullo
Assistant Director for Budget Analysis