Farm Credit Administration

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Informational Memorandum

April 10, 2007

To: Chief Executive Officer
All Farm Credit System Institutions

From: Andrew D. Jacob, Director
Office of Regulatory Policy

Subject: Clarification of 12 C.F.R. § 613.3030 – Rural Home Financing

This Informational Memorandum (IM) discusses the definition of "moderately priced" housing for rural home financing that is contained in § 613.3030(a)(4) of the Farm Credit Administration's regulation. The attached Frequently Asked Questions (FAQs) document addresses specific issues relating to the regulatory definition of moderately priced housing, what is necessary to identify moderately priced housing values, and what data is acceptable to establish those values.

Farm Credit System (System) institutions are authorized by sections 1.11(b) and 2.4(b) of the Farm Credit Act of 1971, as amended, (the Act) to provide rural housing financing for dwellings that are single-family, owner-occupied, and moderately priced for the rural area in which they are located. Section 613.3030(a)(4) defines moderately priced as:

> (i) Satisfies the criteria in section 8.0 of the Act pertaining to rural home loans that collateralize securities that are guaranteed by the Federal Agricultural Mortgage Corporation (Farmer Mac);[1] or
>
> (ii) Is otherwise determined to be moderately priced for housing values for the rural area where it is located, as documented by data from a credible, independent, and recognized national or regional source, such as a Federal, state, or local government agency, or an industry source. Housing values at or below the 75th percentile of values reflected in such data will be deemed moderately priced.

System institutions have reported difficulties applying our regulatory definitions for moderately priced rural home values. Several System institutions explained that it is often too costly or impractical to find credible, independent sources of data to determine moderately priced

[1] Section 8.0 of the Act identifies eligible rural homes for Farmer Mac credit enhancements as those dwellings valued at or below $100,000 (as adjusted for inflation)—excluding land value—and located in a rural area with a population of 2,500 or less. Currently, the adjusted Farmer Mac rural housing value limit is $247,184.

housing values. As a result, many System institutions have chosen to use the Farmer Mac rural housing value limit as their moderately priced limit, even though some have found it does not allow them to adequately serve the market for what they consider moderately priced housing in their local territories.

There are significant differences in housing values across the country, making it increasingly difficult for System institutions to use a nation-wide number like the Farmer Mac rural housing value limit, without unduly restricting their ability to provide rural home financing in some areas. Because of the limitations of a single nation-wide number, data gathered using the criteria in § 613.3030(a)(4)(ii) may be a more appropriate means for establishing values on a localized basis. However, we recognize that it may be difficult for System institutions to obtain credible, independent data for determining the 75th percentile of housing values in their lending territory. There is also considerable evidence that the cost of new home construction is higher than the price of existing, comparable dwellings, impacting the System's ability to provide rural home financing for new construction. Further, we recognize the difficulty in applying the Farmer Mac dwelling-only limit in an established marketplace based on combined house/land values and loan limits (i.e., realtors' expectations, appraisals, secondary market purchasers, data sources).

The attached FAQs provide guidance for determining moderately priced housing values and how to address difficulties associated with using the national Farmer Mac rural housing value limit and determining the 75th percentile value. We encourage System institutions to implement this guidance, where applicable, to fully use the authorities granted by Congress and serve rural homeowners across the full spectrum of the rural marketplace as allowed by Statute. Specifically, we encourage System institutions to develop housing programs that help creditworthy individuals of all income levels, particularly low- to moderate-income households, to purchase homes in rural areas.

Please contact Barry Mardock, Office of Regulatory Policy, at (703) 883-4456 or mardockb@fca.gov, if you have questions regarding this IM or the FAQs document.

Attachment

Rural Home Financing
Frequently Asked Questions

1. For what homes may System institutions provide financing to nonfarm rural residents?

Farm Credit banks and associations are permitted to finance single-family, moderately priced homes located in rural areas (areas with a population of 2,500 or less). Single-family homes that may be financed include detached houses and townhouses. System institutions may not finance multiple-family housing.

2. Are System institutions limited to financing the purchase of nonfarm rural homes?

No. System institutions may also use their rural housing lending authority to finance the construction, remodel, repair or refinance of a rural home. Construction lending may include both building the house and buying a vacant lot, if zoned for residential use.

3. What types of refinancing may System institutions offer to rural homeowners?

System institutions may refinance existing mortgages on homes that are owner-occupied, single-family, moderately priced, and located in a rural area. System institutions may also provide equity loans or revolving credit lines for improvements or repairs to single-family, moderately priced rural homes.

4. How may System institutions determine what is moderately priced for a rural area?

There are two basic definitions of the term moderately priced:

(a) A home valued at or below the Farmer Mac rural housing value limit of $100,000 (adjusted for inflation), excluding the value of the land on which it sits. This adjusted housing limit is $247,184 for 2007.

(b) A home that is determined to be moderately priced for the rural area where it is located, as documented by data from a credible, independent, and recognized national or regional source, such as a federal, state, or local government agency, or an industry source.

Housing values at or below the 75th percentile of values in such data are deemed moderately priced. Examples of the 75th percentile calculation are included in an attached *Appendix*.

5. May System institutions finance rural homes above the 75th percentile?

Yes. The 75th percentile is merely the point where values are deemed by the regulation to be moderately priced. System institutions may finance existing or planned rural housing that exceeds the 75th percentile of housing values in a rural area if they determine that the housing in question is moderately priced for the rural area where it is located, using data from credible, independent, and recognized national or regional sources. For example, an applicant may receive financing to build a new house that exceeds the 75th percentile value for existing homes in a rural area if the System institution obtains new home sales data or construction costs data that show the planned house is moderately priced for rural homes that are existing, planned or recommended for the rural area.

6. What measure of inflation is used to adjust the Farmer Mac rural housing value limit?

Farmer Mac annually adjusts its housing limit for inflation using the October-to-October percentage change in the average house price published in the Monthly Interest Rate Survey from the Federal Housing Finance Board (regulator for the Federal Home Loan Banks). Another government sponsored enterprise (GSE) regulator, the Office of Federal Housing Enterprise Oversight, which oversees Fannie Mae and Freddie Mac, uses this same factor to adjust the Conforming Loan Limit (CLL), which serves as a cap on the mortgages these housing GSEs are allowed to purchase.

7. Are System institutions required to use the Farmer Mac land value limit with the rural housing value limit?

No. Although Farmer Mac places a limit on the value of the land associated with a rural dwelling (50 percent of the total appraised value of the combined property), System institutions do not have to use that limit. However, rural housing loans made by System institutions with land values exceeding the Farmer Mac limit would not be eligible for sale into the Farmer Mac secondary market or for Farmer Mac credit enhancements.

8. May housing market data be segmented when determining moderately priced values?

Yes. It may be appropriate to segment housing market data for new construction of single-family homes to arrive at moderately priced values. For example, a rural area might have smaller, older existing houses that are not of the same character and size of recently built homes or those planned for the area. This may require segmenting the data into new and existing homes to determine the moderate price of newer housing. It may also be necessary if the cost of new home construction is higher than the price of existing, comparable dwellings in the institution's territory.

9. Are there specific requirements for the size of the area or the number of values used when evaluating market data?

No; however, data should represent a cross section of homes, not just the upper or lower end of the distribution, and include enough housing values to accurately reflect the housing market in the identified rural area. It would not be appropriate to identify and gather data from too small of an area, such as a subdivision, where values would not be representative of (nor considered moderately priced) homes in the rural area.

10. May System institutions use housing data from towns with populations over 2,500 when developing an analysis of moderately priced rural housing?

Yes, in some situations it may be permissible. FCA regulations require institutions to use data from credible, independent, and recognized national or regional sources, such as a federal, state, or local government agency, or industry sources. Accordingly, System institutions must make a good faith effort to use data that appropriately represents values for the rural area where they may provide nonfarm rural home financing. When it is not feasible to remove data associated with towns, villages, and cities over 2,500 due to prohibitive costs or limitations in the data source, System institutions may use the best data available for the institution's territory after removing the data on large, readily identifiable urban areas. For example, if an institution found that the most representative data source for home values in its territory was a regional source, but the institution could not reasonably eliminate the data from areas over 2,500, it would not be restricted from using this data source. System institutions may not provide rural housing financing in towns with populations over 2,500.

11. May System institutions use the Conforming Loan Limit to identify moderately priced housing values?

Yes, in some situations it may be appropriate. The CLL is a national value representing the maximum mortgage amount that housing GSEs are permitted to buy, not the sales price of homes being financed. FCA regulations require institutions to use data from credible, independent, and recognized national or regional sources, such as a federal, state, or local government agency or an industry source. The CLL is calculated using data collected by a Federal agency so it is considered an allowable data source. However, the CLL may or may not be the most representative data available for an institution to use when determining moderately priced housing in its territory. In order for an institution to use the CLL, it would be necessary for the institution to provide reasonable support that using the CLL (or a calculated value, based on the CLL) would result in financing moderately priced homes in its territory. The CLL for single-family mortgages in 2007 was set at $417,000 except for Alaska, Hawaii, Guam and the Virgin Islands, which had a 50 percent higher limit.

12. How often must a moderately priced housing limit be calculated or updated?

An institution’s moderately priced housing limit should be updated to reflect significant market changes in the value of single-family homes. A new or updated limit is not required for normal market fluctuations, but an institution must decide if market changes in the rural area are significant enough to warrant a new or updated calculation. Institutions must account for both positive and negative market changes. Rather than calculating a new limit, an institution may choose to update its rural housing limit by using an annual inflation adjustment factor, such as the one used by Farmer Mac, or a local or regional housing price index to update its limit--whichever index better reflects the marketplace for rural homes in its territory. However, frequent changes from one index to another would not be appropriate.

Attachment (Appendix)

Rural Home Financing
APPENDIX – Examples of the 75th Percentile Calculation

1. Calculating the 75th Percentile Rural Home Price Limit from a List of Home Values.

In this example, there is a list of 24 rural home values from a local multiple-listing service for a specific rural area with a population of 2,500 or less. The 75th percentile home value is that value which has 25 percent of the home values larger than it and 75 percent of the home values smaller than it. The 75th percentile home value is determined by first multiplying the number of homes by 75%, i.e., 24 * 75% = 18. The home value associated with the 18th home is $475,000 (dwelling and land), which would automatically be considered moderately priced for rural home loan purposes in this area, as well as all homes under $475,000.

Single Family Home Sales
Rural Area, USA

Sales Price	Home No.
$168,700	1
$187,450	2
$191,250	3
$202,300	4
$203,150	5
$214,500	6
$227,150	7
$252,700	8
$322,700	9
$333,700	10
$359,650	11
$417,000	12
$422,000	13
$425,000	14
$450,000	15
$458,000	16
$469,000	17
$475,000	18
$519,000	19
$530,000	20
$595,000	21
$810,000	22
$945,000	23
$1,005,000	24

Source: FCA, ORP, August 2006.

2. Calculating the 75th Percentile Rural Home Value Limit from a Distribution of New Home Values report completed by the U.S. Census Bureau.

In this example, a distribution of new home sales was obtained from a report prepared quarterly by the U.S. Census Bureau. The first column indicates the value ranges in dollars; the second column lists the number of homes for each value range; the third column contains the cumulative number of homes for all values up to and including the range in the corresponding row; and the fourth column contains the cumulative percentage of homes.

The 75th percentile home value from a distribution of home values can be determined by the following formula:

Q3 = LQ3 + (.75*N - FLQ3)/FQ3)*IQ3

Where:

Q3 = the third quartile (or 75th percentile), which is the home value that has one fourth of the home values larger than it and three fourths of the home values smaller than it.

LQ3 = the lower range in which the third quartile falls.

N = the number of home values.

FLQ3 = cumulative number of homes less than the lower range in which the third quartile falls.

FQ3 = the number of homes in the range in which the third quartile falls.

IQ3 = the dollar range in which the third quartile falls.

First determine the value range where the third quartile falls. For 838 home sales, N=838 and .75*N = .75*839 = 629.25 or 629 when rounded to the nearest whole number. The remaining values are as follows:

LQ3 = $300,000
FLQ3 = 544
FQ3 = 131
IQ3 = $99,999 (i.e., $399,000 - $300,000)

Then, Q3 = $300,000 + (.75 * 839 - 544) / 131 * $99,999 = $365,076.

Thus, the 75th percentile home value from this distribution of new home sales would be $365,076.

Sales Range in Dollars	No. Homes*	Cumulative No. of Homes*	Cumulative Percentage of Homes
<$125,000	54	54	6%
$125,000 to $149,999	82	136.49	16%
$150,000 to $199,999	173.42	310	37%
$200,000 to $249,999	128	438	52%
$250,000 to $299,999	106	**544**	65%
$300,000 to $399,999	**131**	675	80%
$400,000 to $499,999	65	740	88%
$500,000 to $749,000	63	804	96%
>$750,000	36	839	100%
Total (N)	**839**		
LQ3 =	**$300,000**		
FLQ3 =	**544**		
FQ3 =	**131**		
IQ3 =	**$99,999**	**= $399,999 - $300,000**	
Q3 =	**$365,076**	**= $300,000 + (.75 * 839 - 544) / 131 * $99,999**	

* Units are thousands of homes. Components may not add to total because of rounding.

Source: U.S.Census Bureau, New Residential Sales, Quarterly Sales by Price and Financing, Table Q1.