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[Actions Needed to Make the Farmers Home Administration's Emergency Disaster and Emergency Livestock Credit Loan Programs More Equitable and Efficient]. CED-78-136; B-114873. August 18, 1978. 3 pp. + enclosure (15 pp.).

Report to Secretary, Department of Agriculture; by Baltas E. Birkle (for Henry Eschwege, Director, Community and Economic Development Div.).

Issue Area: Domestic Housing and Community Development (2100).
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Congressional Relevance: House Committee on Agriculture; Senate Committee on Agriculture, Nutrition, and Forestry.
Authority: Consolidated Farm and Rural Development Act, as amended (7 U.S.C. 1961). Emergency Livestock Credit Act of 1974, as amended (7 U.S.C. 1961). P.L. 95-89.

A review of the operation and administration of the Farmers Home Administration's (FmHA's) emergency disaster and emergency livestock credit loan programs in South Dakota showed that, although the programs helped eligible farmers and ranchers continue operations after physical disasters and during adverse economic conditions, FmHA needs to make the programs more equitable and efficient. The Secretary of Agriculture should direct the FmHA Administrator to adequately consider the borrowers' repayment ability in establishing repayment terms for emergency disaster loans and to reevaluate the agency's practice of providing loan guarantees only at the maximum legal limit for the emergency livestock credit program when these loans are made to refinance existing debts with participating lenders. (SC)

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UNITED STATES GENERAL ACCOUNTING OFFICE
WASHINGTON, D.C. 20548

COMMUNITY AND ECONOMIC DEVELOPMENT DIVISION

B-114873

AUGUST 18, 1978

The Honorable
The Secretary of Agriculture

Dear Mr. Secretary:

We reviewed the operation and administration of the Farmers Home Administration's (FmHA's) emergency disaster and emergency livestock credit loan programs in South Dakota. Although these programs assisted eligible farmers and ranchers with their operations after disasters or during adverse economic conditions, FmHA needs to make the programs more equitable and efficient. Our review is summarized in this letter and described in detail in the enclosure.

Our review was initiated because of congressional concerns about the adequacy and effectiveness of Federal disaster assistance programs including FmHA's emergency disaster and emergency livestock credit loan programs.

We recently issued another report which included recommendations for improvement of FmHA's emergency disaster loan program. That report, "Difficulties in Coordinating Farm Assistance Programs Operated by Farmers Home Administration and Small Business Administration" (CED-78-118, May 25, 1978), was requested by the Senate Select Committee on Small Business and the Senate Committee on Agriculture, Nutrition, and Forestry. We discussed the effectiveness of FmHA and Small Business Administration coordination in administering their farm disaster and other loan assistance programs in Florida, Georgia, Iowa, Minnesota, Mississippi, South Carolina, and Texas.

We reviewed South Dakota because many emergency disaster and emergency livestock credit loans were made in that State. In South Dakota, FmHA obligated in fiscal years 1976 and 1977 about $242 million for disaster loans--14 percent of the $1.7 billion obligated nationally--and about $47 million for livestock credit loans--7.8 percent of the $599 million obligated nationally.

CED-78-136
(06801)

Our review was conducted primarily at the FmHA national office in Washington, D.C.; the State office in Huron, South Dakota; and the county offices located in Aberdeen, Webster, and Chamberlain. We selected and reviewed a number of emergency disaster loans made in the three county offices; reviewed 13 livestock credit loans; interviewed agency officials at the national, State, and county levels; and reviewed laws, regulations, policies, procedures, and agency records. We also visited farms and interviewed borrowers and representatives of lending institutions.

For the emergency disaster loan program FmHA needs to more adequately consider borrowers' repayment ability in establishing repayment periods. To do this FmHA should exercise more care in tailoring loan repayment terms to fit the borrowers' long-term financial situations. For 22 of the 74 emergency disaster loans reviewed--about 30 percent--FmHA personnel appeared to establish loan repayment terms on the basis of the borrowers' collateral securing the loan or on their repayment ability for the crop year following the loan rather than on the borrowers' long-term repayment ability as shown in their farm and home plans.

For the emergency livestock credit loan program, FmHA should reevaluate its practice of providing loan guarantees at the maximum percent authorized when the loans are used to refinance existing debts with the participating lenders. In such cases, FmHA should require lenders to retain a larger and more equitable share of the risks associated with such debts.

Our review of 13 emergency livestock credit loans totaling $2.2 million showed that about 79 percent of the loan proceeds--about $1.7 million--were used to refinance borrowers' debts owed to participating lenders before the guarantees. FmHA also guaranteed these loans at the highest percent authorized--either 80 or 90 percent. As a result, the lenders' potential loss was reduced from about $1.9 million before the loans were made to about $450,000 after FmHA guaranteed the loans, a decrease of $1.45 million.

We are recommending that you direct the FmHA Administrator to

--adequately consider the borrowers' repayment ability in establishing repayment terms for emergency disaster loans, and

--reevaluate the agency's practice of providing loan guarantees only at the maximum legal limit for the emergency livestock credit program when these loans are made to refinance borrowers' previous debts with participating lenders.

As you know section 236 of the Legislative Reorganization Act of 1970 requires the head of a Federal agency to submit a written statement on actions taken on our recommendations to the Senate Committee on Governmental Affairs and the House Committee on Government Operations not later than 60 days after the date of this letter and to the House and Senate Committees on Appropriations with the Department's first request for appropriations made more than 60 days after the date of this letter.

We are sending copies of this letter to the abovementioned four Committees and to the Senate Committee on Agriculture, Nutrition, and Forestry and the House Committee on Agriculture. Copies are also being sent to the Assistant Secretary for Rural Development; the Administrator, Farmers Home Administration; and the Inspector General.

We appreciate your staff's cooperation.

Sincerely yours,

for Henry Eschwege
Director

Enclosure

ACTIONS NEEDED TO MAKE THE FARMERS HOME ADMINISTRATION'S EMERGENCY LOAN PROGRAMS MORE EQUITABLE AND EFFICIENT

EMERGENCY DISASTER LOAN PROGRAM

Subtitle C of the Consolidated Farm and Rural Development Act, as amended (7 U.S.C. 1961), authorized FmHA to make emergency disaster (EM) loans in counties designated as disaster areas by the President, Secretary of Agriculture, or an FmHA State director due to property damage or severe production losses caused by natural disasters. The EM loan program's objective is to provide financial assistance to eligible farmers, ranchers, and aquaculture operators to cover losses, make major adjustments, pay operating expenses, and provide other essential needs so that sound operations can be maintained.

To be eligible for assistance, applicants must meet specific requirements. For example, an applicant, as a direct result of the disaster, must have suffered damage to his property or incurred production losses of at least 20 percent of a normal per acre production for one or more basic farm enterprises. He must also be unable to obtain sufficient credit at reasonable rates from commercial lending sources.

A number of EM loans are available to eligible applicants, depending on their needs, the adequacy of their security, and their potential repayment ability. The EM loan types and their purposes follow.

--Actual loss loans. Loans made for actual losses and expenses incurred from damaged or destroyed farm property, production enterprises, or both as a result of the disaster. Loan proceeds can be used for eligible purposes under the EM loan program.

--Major adjustment loans. Loans enabling applicants to change operations to (1) make them equivalent to operations before disasters and (2) overcome the financial difficulties caused by the disaster. Loan proceeds can be used to purchase real estate, refinance debts, and for operating purposes.

--Annual operating loans. Loans made to applicants for annual production expenses, cash payments for the use of land, buildings, and pastures, meeting family subsistence needs, and refinancing debt. Such loans may be made for the disaster year and for up to 5 successive years after the disaster year.

When South Dakota was declared a disaster area in 1976, the interest rate on actual loss loans, other than for personal residences and property, was 5 percent for the total loan. Public Law 95-89, enacted on August 4, 1977, however, reduced the actual rate to 3 percent on the first $250,000 for actual loss loans. The rate remained at 5 percent on loss loans above $250,000. The interest rate reduction was retroactive for actual loss loans made for disasters after July 1, 1976. The interest rate on EM major adjustment and annual operating loans is the prevailing rate on similar loans as determined by the Secretary of Agriculture. The interest rate in effect for these loans during our review was 8 percent.

All EM loans reviewed were a result of drought conditions which caused farmers to suffer production losses. We did not review actual loss loans from disasters damaging personal residences or property; therefore, all actual loss loans discussed in this enclosure were made at interest rates of 3 percent for the first $250,000 and 5 percent on amounts above $250,000.

Repayment terms for EM loans vary according to the type of loan, the type of collateral used, and the borrowers' ability to repay. To determine the borrowers' repayment ability, a farm and home plan is prepared for each applicant. This plan includes a financial statement with details of the projected income from crops and livestock and the associated estimated expenses. The plan also shows the borrower's estimated living expenses and anticipated future borrowing.

Repayment terms for actual loss loans are to be based on applicants' repayment ability and the collateral used to secure the loans. FmHA regulations state that these loans will generally be repaid within a period not to exceed 7 years with a possible 5-year extension on the final year's installment. Longer repayment terms may be approved, however, if justified. If longer terms are justified, the repayment terms will not exceed 20 years, and real estate will generally be required to secure the loan.

Repayment terms for major adjustment loans will be based on the borrowers' ability to repay and the use made of the loan proceeds. FmHA regulations state that these loans will generally be repaid within a period not to exceed 7 years with a possible 5-year extension on the final year's installment when the loan funds are used for operating purposes. If the loans are used to purchase real estate, however, repayment may be scheduled in accordance with the useful life of the real estate--not to exceed 40 years. Annual operating loans are scheduled for repayment when the principal income from the year's operations is normally received or when the sale of livestock is expected. Generally, these loans are scheduled for repayment within 1 year.

FmHA instructions state that borrowers should graduate to other sources of credit when able. EM loan borrowers will be reviewed periodically to determine if they can graduate to other sources of credit. For nonreal estate loans, FmHA reviews borrowers' financial situations 5 years after the loans are made and every other year thereafter. For real estate loans, financial situations are reviewed 10 years after the loans and every other year thereafter.

NEED TO ADEQUATELY CONSIDER BORROWERS' REPAYMENT ABILITY IN ESTABLISHING REPAYMENT TERMS

FmHA regulations state that loans for actual losses to crops and livestock will be repaid according to the borrowers' reasonable repayment ability as determined by their farm and home plans. The regulations state that these loans generally will be repaid within a period not to exceed 7 years with a possible 5-year extension on the final year's installment. Under special conditions, repayment may be scheduled not to exceed 20 years if borrower needs are justified. If longer terms are justified, real estate will generally be needed to secure the loan. The regulations do not require that all actual loss loans have either 7-or 20-year terms but rather establishes these terms as outside limits. Other periods may be used if warranted by the borrowers' repayment ability.

Our review of repayment terms was limited to actual loss loans secured by real estate because (1) all borrowers qualified for these loans before qualifying for major adjustment and operating loans and (2) more flexibility was given county personnel in establishing repayment terms for loans secured with real estate than for those secured without real estate.

Personnel in the three FmHA county offices did not always adequately consider the borrowers' repayment ability in establishing repayment terms for real estate-secured, actual loss loans. As a result, some borrowers were given longer terms and smaller annual payments than needed while others were given shorter terms and larger an[illegible] payments than they appeared able to meet.

We reviewed 74 of 367--about 20 percent--of the actual loss loans secured with real estate. We found that in 22 of the 74 cases--about 30 percent--the county personnel did not adequately consider borrowers' long-term repayment ability. These cases instead appeared to base repayment terms on collateral used in securing the loans or on repayment ability for only the crop year following the loans.

In reviewing borrower repayment terms, the 22 loans we questioned were those cases where FmHA gave 20-year terms when 7 years or less appeared more appropriate or where FmHA gave 7-year terms when 20-year terms appeared to be more appropriate. We also found that FmHA provided 7-year or 20-year repayment terms for all 367 borrowers. We believe, however, that because these periods are only outside limits, some repayment terms for unquestioned loans should be scheduled for less than 7 years. Other repayment terms should be between 7 and 20 years, depending on the borrowers' repayment ability.

The table following shows (1) actual loss loans--in three counties we reviewed--made through December 1977 as a result of the 1976 drought, (2) repayment terms for those loans with real estate for security, and (3) results of our comparison of debt repayment terms and repayment ability for selected loans secured with real estate.

	Chamberlain	Aberdeen	Webster
Actual loss loans:	131	221	146
Real estate-secured loans:			
20-year terms	80	25	14
7-year terms	1	144	103
Real estate-secured loans examined:			
20-year terms	30	5	1
7-year terms	1	19	18
Results of examination:			
20-year terms provided and 7 years or less more appropriate	5	1	1
7-year terms provided and 20 years more appropriate	0	5	10

The table shows that the county office in Chamberlain scheduled 80 of 81 actual loss loans secured with real estate for 20-year repayment terms, while the county offices in Aberdeen and Webster scheduled only a small percentage of these loans for 20-year repayment terms. We asked the FmHA county and State officials why most of the Chamberlain office actual loss loans secured with real estate were scheduled for 20-year repayment terms, while Aberdeen and Webster office loans had very few scheduled for 20-year repayment terms. We were told that Chamberlain is located in the western part of the State and that part of the State was affected more by the drought than the eastern part where Aberdeen and Webster are located. As a result, borrowers at the Chamberlain office needed longer repayment terms.

Although it appeared that a number of borrowers at the Chamberlain office needed 20-year terms to repay their loans, our review of 30 loans showed that 5--about 17 percent--could have been repaid with terms of 7 years or less, as the following example illustrates.

In May 1977 FmHA made an actual loss loan and a major adjustment loan to a victim of the 1976 drought. The actual loss loan was for $35,000 at 5 percent 1/ to be repaid in 20 years. The major adjustment loan was for $90,000 at 8 percent to be repaid in 40 years. Required loan payments for principal and interest were $1,151 and $4,735, respectively, due in January 1978, and annual principal and interest payments of $2,809 and $7,549, respectively, beginning in January 1979, continuing for the balance of the repayment periods. This drought victim also had other annual debt payments of $16,857, making the total payments due after the 1977 crop year $22,743. After the 1978 crop year, the total annual payment due will be $27,215 until 1997 when the 20-year note payment of $2,809 will be completed. The borrower's farm and home plan projects as available $73,450 for annual debt payments. Based on this information, it appears reasonable that larger annual payments could be made. Loan terms of 7 years on both loans would have required an annual payment of $6,049 on the $35,000 5-percent loan and $17,287 on the $90,000 8-percent loan. With 7-year terms, the borrower's total annual debt payments would increase to $40,193--well within the available projected $73,450 for annual debt payments.

In Aberdeen and Webster, 247 of 286 actual loss loans secured with real estate--about 86 percent--were scheduled for 7-year repayment terms. Our review of 37 of these loans, however, showed that 15 loans--about 41 percent--appeared to warrant 20-year terms. In addition, two of the six loans reviewed which were scheduled for 20-year repayment terms should have been scheduled for 7 years or less.

Information on borrowers' farm and home plans showed that the county personnel do not always consider borrowers' long-term repayment ability but base repayment ability instead on available cash to borrowers for the crop year following the loan. In some cases, borrowers may have loans requiring full repayment during the crop year following the EM loan. This payment would be used by county personnel in computing repayment terms. Because loan payments would decrease repayment ability, county personnel may give borrowers 20-year repayment terms on EM loans. Because loan payments would not be due in subsequent years, however, borrowers would have more cash available to repay EM loans

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1/ Although this rate was reduced to 3 percent as a result of Public Law 95-89, the 5-percent rate was in effect when the county personnel computed repayment ability.

in subsequent years. As a result, borrowers may not need 20-year repayment terms but may be able to repay EM loans in 7 years or less.

In other cases only interest on EM loans is paid for the first year. Principal and interest payments are paid in subsequent years. The borrowers' overall payments are, therefore, lower for the first year and repayment terms may be met while payments will be higher in subsequent years and borrowers may be unable to meet repayment terms. Some borrowers may, therefore, need longer than 7 years to repay EM loans, as the following example illustrates.

In March 1977 FmHA made an actual loss, a major adjustment, and an annual operating loan to a victim of the 1976 drought. The actual loss loan was for $46,000 at 5 percent to be repaid in 7 years, the major adjustment loan was for $35,000 at 8 percent for 7 years, and the annual operating loan for $27,200 at 8 percent for 1 year. Required interest payments on the actual loss and major adjustment loans were $2,300 and $2,611, respectively, due in J[illegible]y 1978. Full payment of about $29,400 was due on the a[illegible] operating loan after the 1977 crop year. In January [illegible]79 annual payments of principal and interest on the actual loss and major adjustment loans will be $7,800 and $7,098, respectively. Annual payments on these loans will decrease about $600 a year from 1979 until 1984 when the balance of the principal and interest is due--about $19,320 on the actual loss loan and about $15,120 on the major adjustment loan. This borrower also has other annual debt payments of $1,258, making total payments due after the 1977 crop year of $35,570. After the 1978 crop year, his total annual debt payment will be about $16,160, decreasing by about $600 a year until 1984 when the balance of the actual loss and major adjustment loans is due.

The borrower's farm and home plan projects about $39,000 available for debt payment after the 1977 crop year, including the proceeds of $27,200 from the annual operating loan. Beginning with crop year 1978, only about $12,000 will be available for debt payment--about $4,000 less than his required annual debt payments. Had the borrower been given 20-year terms on the actual loss and major adjustment loans, his annual payments would have been about $3,600 on the actual loss loan and about $3,625 on the major adjustment loan. This would have reduced his total annual payments due after the 1978 crop year from $16,160 to about $8,500--within the $12,000 projected as available for debt payments.

We believe that the EM program would provide greater benefits if loan payments were tailored to fit borrowers' financial situations. Repayment terms should be established based on long-term repayment ability as shown in farm and home plans and not solely on the cash available for the following crop year or on whether the borrower has real estate.

EMERGENCY LIVESTOCK (EL) CREDIT LOAN PROGRAM

The Emergency Livestock Credit Act of 1974, as amended, (7 U.S.C. note prec. 1961 (1976)), authorized FmHA to guarantee loans made by legally organized lending agencies to farmers and ranchers primarily engaged in agricultural production and who have substantial operations in breeding, raising, fattening, or marketing livestock to permit them to maintain their operations during temporary adverse economic periods. The program which was to expire July 25, 1975, initially authorized FmHA to guarantee loans up to $250,000 and pay up to 80 percent of the principal and interest of any losses sustained by the lenders in case borrowers default. In June 1975 the program was extended through December 31, 1976, and FmHA was authorized to guarantee loans up to $350,000, paying up to 90 percent of any losses sustained by the lenders in case borrowers default. In October 1976 the program was extended through September 30, 1978, and in August 1978 it was extended through September 30, 1979.

Since the program's inception in fiscal year 1975--through fiscal year 1977--FmHA guaranteed 7,190 loans for about $951.6 million. As of September 9, 1977, 5,500 of these loans were still active with a balance of about $550 million. Demand for new loan guarantees has slowed down. Only 1,173 loans were guaranteed during fiscal year 1977 compared with 3,021 and 2,996 loans, during fiscal years 1975 and 1976, respectively. FmHA had paid loss claims to lenders under 128 guaranteed loans for about $4.4 million as of September 9, 1977. The rate of loss claims accelerated during fiscal year 1977 even though this amount was less than 1 percent of the total obligations.

Under this program, loans may be made to individuals, partnerships, and corporations that are established farmers and ranchers in the United States and are unable to obtain credit from commercial sources. Borrowers must be primarily engaged in breeding, raising, fattening, or marketing their beef or dairy cattle, swine, sheep, goats, chickens, or turkeys.

Loan funds may be used for essential livestock operations, including

--replacing livestock,

--providing feed,

--paying the usual charges for grazing permits and for the use of land and buildings,

--providing farm machinery,

--moving livestock, and

--building or repairing pens and fences.

Loan funds may also be used to refinance debts incurred for livestock operations when (1) such refinancing is absolutely essential for borrowers to remain in business, (2) lenders would not refinance loans without guarantees, and (3) lenders are not currently refinancing similar loans to others without such guarantees. When refinancing occurs, the lenders are required to certify that the above conditions have been met before FmHA will guarantee loans.

LOANS USED FOR REFINANCING PREVIOUS LOANS WITH LENDER SHOULD BE GUARANTEED FOR LESS THAN 90 PERCENT

In South Dakota FmHA guaranteed 612 loans for about $74.9 million through fiscal year 1977. All 13 loans we reviewed--about $2.2 million--were guaranteed at the highest percent authorized--either 80 or 90 percent. The loan funds were used primarily to refinance borrowers' existing debts with lenders who received the guarantees. As a result the lenders' exposure to losses was reduced substantially on previous loans. A national office official stated that, to his knowledge, all EL loans have been guaranteed for the maximum percent authorized.

For the 13 loans reviewed, the following table shows

--the amount of the guaranteed loan,

--the percent guaranteed,

--the borrower's existing debts with the participating lender before the guarantee,

--the amount of borrower's existing debt refinanced with the guarantee to the participating lender, and

--the lender's reduction in exposure.

Amount of EL loan	Guarantee	Borrower's debts to participating lender before guarantee	Borrower's debts refinanced with guaranteed loan	Lender's reduction in exposure
$ 60,000	90%	$ 47,711	$ 47,711	$ 41,711
21,000	90	21,000	21,000	18,900
220,600	90	137,600	137,600	115,540
178,800	90	129,800	129,734	111,854
150,000	90	133,000	133,000	118,000
200,000	90	52,000	52,000	32,000
85,000	90	96,000	85,000	76,500
350,000	90	304,520	304,500	269,500
137,500	90	74,000	61,493	47,743
350,000	90	343,606	341,000	306,000
250,000	80 (note a)	397,000	250,000	200,000
103,300	80 (note a)	96,304	96,304	75,644
62,000	80 (note a)	66,122	50,000	37,600
$2,168,200		$1,8[illegible],663	$1,709,342	$1,450,992

a/ These loans were guaranteed before June 1975 when FmHA could guarantee loans for up to 80 percent.

As the table shows, all 13 guaranteed loans reviewed were used to refinance all or most of the borrowers' existing debts with participating lenders, and all 13 loans were guaranteed at the highest percent authorized, even though FmHA can make guarantees for a lower percent.

Of about $2.2 million guaranteed for the 13 loans, about $1.7 million--about 79 percent--was used to refinance borrowers' debts which existed with participating lenders before the guarantees. As a result, the lenders' exposure to potential loss was reduced from about $1.9 million before the EL loan guarantees to about $450,000 after the guarantees--a decrease of about $1.45 million. In December 1975, for example, FmHA issued a 90-percent

guarantee to a lender for a $350,000 loan to a borrower. Before the guaranteed loan, the borrower owed the lender $304,520. After the guarantee was made, $304,500 of the loan proceeds were used to refinance the existing debt owed the lender, thereby reducing the lender's exposure to loss by $269,500.

National and State office officials told us that they believe lenders would be unwilling to accept guarantees for less than 90 percent and would force borrowers to liquidate to pay debts rather than accept less than the maximum percent authorized. The officials believe the guarantee program would not have been useful if FmHA had attempted to get lenders to retain more of the exposure to potential loss which existed before the guarantees.

We contacted five lenders in Aberdeen, South Dakota, all of whom previously had or presently have guarantees, and asked them if they were willing to accept guarantees for less than 90 percent. These lenders generally responded that although they preferred 90-percent guarantees they were willing to accept guarantees for less than 90 percent, stipulating that circumstances would affect each case. They did state, however, that if 90-percent guarantees were not available, they would generally be willing to accept guarantees for less.

We believe that FmHA should reevaluate its practice of automatically guaranteeing EL loans for the maximum percent authorized when the loans are used to refinance borrowers' previous debts with the participating lenders. We believe that because the lenders allowed borrowers to accumulate these debts, FmHA should negotiate with the lenders to guarantee these loans at a lesser percentage so that the lenders retain a larger and more equitable share of the risks associated with such debts.

CONCLUSIONS

The EM and EL loan programs helped eligible farmers and ranchers continue operations after physical disasters and during adverse economic conditions; however, FmHA needs to make the programs more equitable and efficient.

The EM program would provide greater benefits to borrowers if more care were exercised in tailoring loan payments to borrowers' long-term financial situations. Repayment terms should be established based on the borrowers' long-term repayment ability as shown in farm and home plans. Terms should

not be based solely on borrowers' available cash for the following crop year or on whether real estate is available for loans. FmHA personnel should also establish repayment terms for other than only 7 or 20 years if warranted by borrowers' repayment ability.

For the EL credit loan program, FmHA should reevaluate its practice of automatically guaranteeing these loans for only the maximum authorized percent when loan proceeds are basically for refinancing borrowers' previous debts with participating lenders. Because the lenders allowed borrowers to accumulate these debts, FmHA should require these lenders to retain a larger and more equitable share of the debt-associated risks. Although FmHA officials believe that lenders will not accept guarantees for less than the maximum allowed, our discussions with lenders disclosed that the lenders might accept guarantees at a lesser percentage.

RECOMMENDATIONS

We recommend that the Secretary of Agriculture direct the FmHA Administrator to

--adequately consider the borrowers' repayment ability in establishing repayment terms for EM loans, and

--reevaluate the agency's practice of providing loan guarantees only at the maximum legal limit for the EL credit loan program when these loans are made to refinance borrowers' prior debts with participating lenders.

OBSERVATIONS

Our review of the EM loan program disclosed that FmHA county personnel are processing EM loan applications much faster since an FmHA Administrator's notification on loan processing. The staff time spent processing these loans, however, has limited FmHA's ability to adequately service its entire loan portfolio. Although our audit work in these areas was limited and we are not making any recommendations at this time, we believe the information should be considered by FmHA management in monitoring agency programs.

EM loan processing time

On July 7, 1977, the FmHA Administrator notified all FmHA State directors that EM loan applications were not being processed promptly. To reduce the time between the date of applications and loan closings, the Administrator directed that applications should be approved, if possible,

within 30 days after they are received in the county office. Our review of loans processed in the Aberdeen and Webster offices showed that county personnel have been processing EM loans more promptly since the notification but not within 30 days as directed by the FmHA Administrator.

Before July 7, 1977, the Aberdeen and Webster offices had completed 203 and 141 EM loans, respectively, under the 1976 disaster declaration for South Dakota. Averages of 85 and 104 days, respectively, were required to process EM loan applications through approval. The total processing time, from applications through closings, averaged 116 and 163 days, respectively. Despite the rather lengthy time to process these loans, borrowers we questioned told us that the loan processing times caused them little or no financial hardship.

According to FmHA officials, the time required to process these loans in the two county offices was lengthy because

--some applicants failed to provide all the data required when they filed their applications,

--some applicants were slow to provide FmHA with abstracts of title and other related data needed to close loans,

--some applicants filed loan applications early and requested that they not be processed until they were needed several months later (average processing times were based on the elapsed days between the dates applications were filed and the loans were closed),

--considerable time was required to inventory and appraise security, and

--considerable time was required to prepare and legally record appropriate security documents.

We also reviewed 17 loans in the county offices located in Aberdeen and Webster which were processed since the July 7, 1977, notification and found that the average processing time for these loans from receipt of application to approval and from application to closing had decreased dramatically. Application-to-approval time was 42 days in Aberdeen and 52 days in Webster. At the time of our review, only 5 of these approved loans had been closed and the processing time from receipt of application to loan closing averaged 64 days and 62 days, respectively.

We did not determine if the faster loan processing time was due to the FmHA Administrator's notice or for some other reason, such as less applications to process. We believe, however, that FmHA management should monitor the loan processing time in other county offices to determine if its loan processing time has decreased significantly and the reasons for this reduction.

Staffing requirements

FmHA officials told us that the high volume of EM loans processed during 1976 and 1977 reduced the resources needed for servicing EM loans and loans made under other FmHA programs. Although not yet apparent, failure to service accounts during 1976 and 1977 may cause higher delinquency rates and a number of loan foreclosures over the next several years. According to these FmHA officials, a shortage of staff will cause loan servicing to be limited to those loans with existing or potential problems while other loans will receive little servicing. These officials stated that although they have started limited servicing of EM loans, this servicing consists primarily of inventorying security for chattel-secured loans.

According to FmHA officials, adequate servicing consists of actions that must be taken to collect loan indebtedness and to provide borrowers with adequate supervision and management assistance to successfully continue farming operations. They stated that proper servicing will reduce delinquency rates and eliminate many farm operation failures. As a minimum these officials told us that servicing for loans secured with chattels should consist of annual farm visits to inventory security and inspect farm operations, to review security agreements, the status of loans, and the borrowers' operating plans for the next year. For loans secured with real estate, FmHA officials stated that minimum servicing consists of obtaining new financial statements from borrowers every 2 years in addition to annual farm visits that may be necessary. According to these officials, some borrowers require three farm visits annually plus meetings one or more times in the county office to provide adequate supervision and management assistance (servicing), while much less is required for other borrowers.

The following table shows the number and amounts of loans made and the staffing levels for FmHA in South Dakota from fiscal year 1975 through 1977.

Fiscal year	Loans made	Amount (millions)	Number of employees: Permanent	Temporary	Total (note a)
1975	4,876	$118.8	144	6	150
1976	4,400	136.5	156	0	156
1977	10,038	349.2	164	10	174

a/ These employee totals represent the number employed at the end of each fiscal year. Additional employees may have worked other months of the year and would, therefore, not show up in the yearend totals.

Since fiscal year 1975, the number of loans has more than doubled while the permanent staff level has increased by only 20. Although the number of temporary staff was only 10 at the end of fiscal year 1977, 36 temporary employees were hired during various times that year to assist in processing EM loans. The increase in loan volume is primarily due to increases in EM loans which accounted for about 7,000 of the 10,000 loans made in fiscal year 1977.

Because of large increases in EM loans made by FmHA during the past few years and the relatively constant number of permanent employees in South Dakota, the lack of adequate staff to service loans could create a problem that FmHA should address. We believe FmHA should closely monitor its loan servicing, especially in those States where high volumes of EM loans have been made and the staff size has remained fairly constant, so that increases in delinquencies and foreclosures can be identified early and corrective actions can be taken.