112029
13397

BY THE COMPTROLLER GENERAL

Report To The Congress

OF THE UNITED STATES

Ways Of Providing A Fairer Share Of Federal Housing Support To Rural Areas

Many rural American families still live in substandard conditions, although progress has been made over the last 30 years in alleviating housing shortages and improving conditions. Rural housing problems today are most acute in remote areas, among the elderly, and among those who rent.

Rural areas receive only about 20 percent of the Federal housing support available despite having one-third of the Nation's population and one-half of the substandard housing. Urban areas have benefited more.

Future progress depends on increasing the supply of mortgage credit, providing greater homeownership opportunities for moderate-income families, targeting more Federal housing funds to the neediest areas, and emphasizing programs to upgrade existing housing and develop new sites.

The Secretaries of Agriculture and Housing and Urban Development should improve Federal housing program operations in rural areas, and the Federal Farm Credit Board should act to increase the supply of housing credit.

112029

009612

CED–80–1

MARCH 28, 1980

COMPTROLLER GENERAL OF THE UNITED STATES
WASHINGTON, D.C. 20548

B-197850

CWO00001

To the President of the Senate and the
Speaker of the House of Representatives

Much progress has been made over the last 30 years in improving the quality of rural housing, but many rural families still live in substandard homes. This report points out ways that Federal agencies can improve their programs to provide a more equitable share of Federal housing support to rural areas.

We made our review to evaluate the accomplishments and shortcomings of Federal housing programs in rural America, particularly during the past 10 years. Areas of particular concern included the geographic distribution of housing assistance, gaps in program benefits, and ways to improve the programs' effectiveness in providing opportunities for rural families to obtain decent shelter.

We are sending copies of this report to the Director, Office of Management and Budget; the Secretaries of Housing and Urban Development and Agriculture; the Administrator of Veterans Affairs; and the Governor, Farm Credit Administration.

Elmer B. Staats
Comptroller General
of the United States

AGC00023
AGC00042
AGC00016
AGC00358
DLG04330

COMPTROLLER GENERAL'S
REPORT TO THE CONGRESS

WAYS OF PROVIDING A FAIRER
SHARE OF FEDERAL HOUSING
SUPPORT TO RURAL AREAS

D I G E S T

Rural families have not benefited from Federal housing programs to the same extent as urban families. Although rural areas contain one-third of the Nation's population and one-half of the substandard housing, they have received only about one-fifth of Federal housing support. (See pp. 7 and 29.)

Much progress has been made over the last 30 years in improving the quality of rural housing, and Federal programs have contributed significantly to this progress. However, housing needs in rural areas have far exceeded the level of available Federal support, and many rural families still live in substandard housing. (See pp. 7 and 9.) Housing problems today are most acute in outlying rural areas, among the elderly, and among those who rent. (See pp. 10 and 12.)

The Farmers Home Administration (FmHA) of the Department of Agriculture, Department of Housing and Urban Development (HUD), and Veterans Administration (VA) stimulate the housing industry by making home loans, providing subsidies, and/or fostering the supply of private mortgage credit. The FmHA is the principal Federal agency supporting rural housing. HUD and VA administer housing programs which have varying adaptability in rural areas.

FmHA provided about $18.7 billion in loans or grants for about 1.2 million housing units between 1950 and 1977, but about 23 percent of the units were in urban counties and an additional 35 percent were in rural counties adjacent to metropolitan areas. Although remote areas had the worst housing conditions, they received relatively little assistance. (See p. 30.)

HUD's mortgage insurance programs have not been used extensively in remote areas because

--rural financial institutions have seldom had the resources to participate,

--urban mortgage banking companies have seldom participated due to investor restrictions on loans in rural areas, and

--the agency has lacked interest in rural areas. (See pp. 31 and 36.)

Assistance provided by VA's loan guarantee program equitably paralleled the distribution of the veteran population. (See p. 33.)

WAYS FEDERAL HOUSING SUPPORT CAN BE MORE EQUITABLE

Because of low family income and inadequate public facilities, progress in reducing substandard rural housing, particularly in remote areas, depends largely on what Federal housing agencies do to reduce problems caused by the

--shortage of mortgage credit,

--rapid escalation of building costs,

--lack of an effective Federal housing strategy for remote areas,

--underuse of home repair and rehabilitation programs, and

--shortage of affordable homebuilding sites.

Availability of mortgage credit

The shortage of mortgage credit in rural areas contributes to the high incidence of substandard housing. Federal insurance and guarantee programs have not stimulated needed mortgage credit. Rural banks are small and make few home loans primarily because they have more attractive business and consumer loan opportunities. Few savings and loan associations are located in outlying areas, and mortgage banking companies seldom emphasize rural operations. (See p. 36.)

Although Federal Land Banks are not government agencies, they are authorized to make home loans to nonfarm rural families. Few such loans have been made (33,870 loans were outstanding on September 30, 1978, or 3.3 percent of all loans) because downpayment requirements are high and many bank officials resist making home loans. (See p. 41.)

Homeownership for moderate-income rural families

Purchasing a home is becoming increasingly difficult for moderate-income rural families (those earning $11,200 to $15,600 annually) due to the rapid escalation of home building costs. In 1977 the average new rural home cost about $39,000.

In parts of the Nation, a gap in program coverage exists between families eligible for FmHA mortgage interest rate subsidies and those who must pay the FmHA maximum interest rate.

For example, low-income families with adjusted annual incomes of $8,400 to $11,200 can, with FmHA interest subsidies, buy a new home costing $35,000. However, moderate-income families earning between $11,200 and $15,600 (FmHA's maximum income limit for home loans) face severe hardships in purchasing the same home. They are neither eligible for interest subsidies nor easily able to afford a mortgage at the FmHA standard interest rate for moderate-income families. (See p. 48.)

Targeting of housing assistance

Until fairly recently, FmHA provided housing assistance on the basis of demand. Beginning in fiscal year 1979, the agency decided to target its State housing allocations for disadvantaged people and distressed communities by allocating funds primarily on the basis of need.

GAO believes that little improvement will result from the new pattern of allocating funds within States. Under this strategy, equal weight is given to population, occupants of substandard housing, and per capita income. This approach favors the more densely populated counties even though per capita income is higher and housing conditions better.

For example, in fiscal year 1977 metropolitan areas of North Carolina received 20 percent of FmHA loans. In fiscal year 1979 the expected allocation under the new strategy in metropolitan areas of the State is 23.6 percent. (See p. 52.)

Housing repair and rehabilitation

Emphasis is needed on housing repair and rehabilitation to preserve existing housing and eliminate conditions detrimental to the safety or health of occupants. About half the $85 million available to FmHA for repair loans for very low-income or elderly owner-occupants went unused from 1974 to 1978. Home repair was not emphasized, according to FmHA county office officials, because too much time was required to identify needy families and explain the programs. (See p. 56.)

Building sites

Some rural residents lack decent housing because of a shortage of affordable building sites. While FmHA makes loans for site development, they have not been fully used because such loans are available only to nonprofit organizations which lack the expertise or willingness to develop sites. Small private builders, which have the expertise but lack the capital or credit, are not eligible under the law for site development funds. (See p. 58.)

RECOMMENDATIONS

The Secretaries of Agriculture and Housing and Urban Development should improve existing Federal housing program operations in rural areas, and the Federal Farm Credit Board of the Farm Credit Administration should act to increase the supply of housing credit. If implemented, these recommendations should increase the

--number of FmHA direct and guaranteed home loans for moderate-income families and the number of new housing sites in outlying areas,

--use of HUD home mortgage insurance programs by rural financial institutions, and

--volume of home loans made by Federal Land Banks.

These recommendations would also distribute more housing assistance to rural areas most in need and provide greater opportunity for rural families to repair and rehabilitate their homes. (See pp. 43 and 60.)

AGENCY COMMENTS

The Department of Agriculture, HUD, and VA agreed with most of GAO's conclusions and recommendations. (See pp. 43 and 61.)

The Federal Farm Credit Board of the Farm Credit Administration agreed to give GAO's recommendations due consideration within the scope and intent of their authority and structure. (See p. 46.)

C o n t e n t s

ABBREVIATIONS

FICB	Federal Intermediate Credit Bank
FLB	Federal Land Bank
FmHA	Farmers Home Administration
GAO	General Accounting Office
HUD	Department of Housing and Urban Development
PHA	public housing agency
SMSA	standard metropolitan statistical area
VA	Veterans Administration

CHAPTER 1

INTRODUCTION

The Housing Act of 1949 (42 U.S.C. 1441 _et seq._), amended, established a national goal that each American family have a decent and suitable living environment. That act also authorized the first Federal programs specifically for rural homeownership and housing repair.

The principal Federal agency involved in rural housing is the Farmers Home Administration (FmHA) of the Department of Agriculture. The Department of Housing and Urban Development (HUD) and the Veterans Administration (VA) administer housing programs which also apply to rural areas. To provide impetus toward the national housing goal, these three agencies assist in housing rural Americans by making loans, providing subsidies, and/or stimulating the supply of private mortgage credit. Comparative characteristics of their major programs are summarized in appendix I.

No standard definition of a "rural" area is shared by all the agencies. The Bureau of the Census traditionally has defined rural areas as open country and places having up to 2,500 residents. As defined by FmHA, "rural" means open country and towns of not more than 10,000 (except under special circumstances where the population may be as great as 20,000). HUD defines rural as counties outside a standard metropolitan statistical area (SMSA).

An SMSA is a county or group of contiguous counties which come under the economic and social influence of a city or twin cities with 50,000 or more inhabitants. The counties are metropolitan--places for nonagricultural workers to work and live. The Office of Management and Budget designates SMSA boundaries and adjusts them as population and conditions change.

"Rural," to many people, implies "agricultural." In 1970, however, only 16 percent of the rural labor force lived on farms and only 10.8 percent of that labor force were engaged in farming. Nearly as many rural residents were professional or technical workers as farmworkers.

In this study, "rural" is defined as the areas outside SMSAs. This definition is used instead of the census definition because most housing, economic, and demographic statistics are compiled on an SMSA basis. Generally, comparisons between geographic areas are practical only on that basis.

FARMERS HOME ADMINISTRATION

FmHA was established by the Farmers Home Administration Act of 1946 (7 U.S.C. 1981) and was assigned the farm loan functions previously conducted by the Farm Security Administration. The act also authorized housing loans to farmers.

FmHA's authority was expanded by the Federal Housing Act of 1961 (42 U.S.C. 1471) which made nonfarm rural residents eligible for housing loans. The Housing and Urban Development Act of 1968 (42 U.S.C. 1490a) established a loan interest supplement program to provide low-income families with interest rates as low as 1 percent. Further, the 1968 act authorized loan subsidies to build low-priced rental apartments for low-income families and the elderly.

Under the 1961 act, FmHA housing programs were extended to towns having up to 2,500 residents. Over the years this population limit was gradually increased. The Housing and Community Development Act of 1974 (42 U.S.C. 1490) included towns having up to 20,000 residents which were (1) located outside SMSAs and (2) lacked sufficient private home mortgage credit. Thus, FmHA evolved into the primary housing agency for rural America.

FmHA makes direct loans to eligible families, public agencies, and nonprofit organizations. Loans are processed by 1,896 county offices. County office personnel also counsel prospective borrowers, inspect sites, appraise properties, and service the loans. A description of FmHA's major housing programs are described in appendix II.

Home loans are made to low- and moderate-income families who cannot obtain reasonable financing from other sources. A loan is repayable in not more than 33 years, and generally no downpayment is required. Most families are eligible for only modest homes containing less than 1,300 square feet of living space. Families with adjusted annual income below $11,200 qualify for interest rate subsidies; those with adjusted incomes between $11,200 and $15,600 (higher in Alaska, Hawaii, and Guam) must pay the agency's current maximum interest rate of 10 percent. To determine eligibility, families may deduct 5 percent of total annual income and $300 for each dependent child.

The Rural Development Act of 1972 (42 U.S.C. 1487) authorized FmHA to guarantee home loans made by other public and private lenders. Currently, this program applies to families with incomes between $15,600 and $20,000 (higher in Alaska, Hawaii, and Guam).

DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT

The National Housing Act of 1934 (12 U.S.C. 1701 et seq.) established loan insurance programs under the Federal Housing Administration primarily to increase home construction and reduce unemployment during the Depression. Later, the Congress greatly increased Federal housing activities by enacting the United States Housing Act of 1937 (42 U.S.C. 1437 et seq.) and the Housing Act of 1954 (12 U.S.C. 1715), which created low-rent public housing and mortgage insurance programs for low-income families and those displaced by urban development.

In 1965 the Congress created HUD to encourage public and private agencies to cooperate in solving housing and urban development problems. Major contributions were expected from the homebuilding and mortgage lending industries.

Currently, HUD administers subsidized and unsubsidized single-family and multifamily mortgage insurance and loan programs, as well as interest rate subsidies and rent supplement programs. The principal purposes of these programs are to (1) assure decent shelter for all Americans, (2) revitalize the urban areas, (3) provide a choice of living places, and (4) enhance the capability of local governments to rejuvenate communities. The major HUD housing programs are described in appendix III.

Rural areas are eligible for HUD mortgage insurance and community development, planning, and technical assistance on the same basis as metropolitan areas, except where specific statutory limitations apply.

VETERANS ADMINISTRATION

The Servicemen's Readjustment Act of 1944 (38 U.S.C. 1801 et seq.) introduced a new form of housing assistance to benefit veterans. It authorized VA to guarantee a portion of 100-percent home mortgage loans, up to a maximum amount stipulated in the act. The guarantee, substituting for the cash downpayment required under conventional mortgages, protects the lender against loss on the guaranteed portion of the loan.

The Housing Act of 1950 (38 U.S.C. 1811) authorized VA to make direct loans in rural areas where guaranteed loan financing was not generally available. The veteran was required to show that he could not get a loan at an interest rate less than or equal to VA's authorized rate.

VA also operates a direct loan referral system for veterans in remote areas who cannot locate home financing. Under this system, when VA has approved a request for a direct loan, the application is referred to at least three lenders. If a lender accepts the application, VA than substitutes a guaranteed loan for the direct loan.

The advantages of a VA loan include no downpayment, a moderate interest rate, a long-term mortgage, and prepayment without premium or fee. No subsidies are available for veterans who cannot afford monthly mortgage payments. VA housing programs are described in appendix IV.

FARM CREDIT SYSTEM

The United States is divided into 12 farm credit districts. Each district contains a Federal Land Bank (FLB) and a number of Federal land bank associations, a Federal Intermediate Credit Bank (FICB) and a number of production credit associations, and a Bank for Cooperatives.

The 12 FLBs were organized in 1917 under the Federal Farm Loan Act of 1916 (12 U.S.C. 2001) to provide long-term farm mortgage credit. Subsequently, the banks' initial capital, advanced by the Federal Government, was repaid, and they are now cooperatively farmer owned. The banks do not lend Government funds and are self-sufficient, operating at no cost to the taxpayer.

FLBs obtain loan funds by selling securities to investors in the Nation's money markets. These securities are backed by the net worth of the FLBs and the underlying mortgages. They carry no Government guarantee.

All the stock and equity certificates of FLB associations are owned by member borrowers. Associations, in turn, purchase capital stock in the FLBs. Each association is managed by a board of directors elected by and from the membership, but voting authority is vested only in those who are agricultural mortgage borrowers.

The 12 FICBs were established under the Federal Farm Loan Act in 1923. The capital stock of the FICBs is owned by the production credit associations. The FICBs are primarily banks of discount for production credit associations and other agricultural and livestock lending institutions. Production credit associations finance on a short- and intermediate-term basis farmers, ranchers, and producers or harvesters of aquatic products.

The Banks for Cooperatives were organized in 1933 to extend credit to farm cooperatives.

The Farm Credit System includes the banks and local associations described above. Each of these institutions is an instrumentality of the United States for carrying out congressional policy and objectives. The banks are chartered by the Farm Credit Administration, an independent agency of the executive branch of the Government, and subject to regulation and supervision by the Farm Credit Administration. A Federal Farm Credit Board, appointed by the President, establishes general policy for guidance of the Farm Credit Administration.

The FLBs sought and obtained through the Farm Credit Act of 1971 (12 U.S.C. 2018) limited authority to finance rural homes for certain nonfarm families. Loans are made for up to 30 years at variable interest rates which are adjusted periodically, depending on the cost of money to the banks. The 1971 act, as it applies to housing, defines "rural" as open country or a town with less than 2,500 persons, if the town is not associated with or immediately adjacent to a larger population center.

The FICBs were also given authority, under the above act, to finance rural homes through the local production credit associations. Farm Credit Administration policy, while not excluding loans for conventional homes, emphasizes that production credit associations should provide loans for remodeling and repair of permanent homes and financing of mobile homes where the owner needs intermediate-term credit.

STATE HOUSING AGENCIES

By 1978, 40 States had created agencies to provide housing assistance for low- and moderate-income families. These agencies have a broad range of authority, including the right to issue tax-exempt securities. The proceeds of the securities are used to provide below-market interest rate financing for acquiring, developing, constructing, or rehabilitating housing. Often the agencies require mortgage insurance on their housing loans like that provided by HUD and VA. Such insurance adds security to the underlying home mortgages and aids in the sale of the agencies' securities at lower interest rates.

INTERAGENCY COOPERATION

Each Federal program is based on legislation enacted by the Congress in response to public concern about particular housing problems. The diversity of the programs limits the extent to which agencies can coordinate administrative functions. The following are examples of existing cooperation:

--VA and HUD coordinate acceptance of subdivision plans, construction inspections, and disposition of acquired properties.

--FmHA and HUD cooperate to encourage the use of HUD's rental assistance payments with FmHA's rural rental housing.

--FmHA uses HUD's minimum property standards for housing.

--FmHA uses HUD's system for obtaining credit reports on prospective homebuyers.

--As required by section 511 of the Housing and Community Development Act of 1974 (42 U.S.C. 1490), the Secretaries of Agriculture and HUD coordinate the designation of small cities in rural areas with a serious lack of mortgage credit.

SCOPE OF REVIEW

We evaluated the accomplishments and shortcomings of Federal housing programs in rural America, particularly during the past 10 years. Areas of particular concern included the geographic distribution of housing assistance, gaps in program benefits, and ways to improve the programs' effectiveness in providing opportunities for rural families to obtain decent shelter.

Our review was made at the Washington, D.C., headquarters of the Farmers Home Administration; the Department of Housing and Urban Development; the Farm Credit Administration; the Veterans Administration; and at selected field offices of those agencies in Alabama, Colorado, Indiana, Kentucky, Maine, and North Carolina. We also visited FmHA county offices which serve 18 counties in the six States.

These States were selected because they contain one or more typical rural housing problems, such as a high percentage of substandard homes, a high percentage of rural poor, large areas remote from metropolitan service areas, or high construction costs. In addition, these States contain a significant number of homes financed with FmHA loans. We selected the 18 counties in the six States so as to obtain a mix of remote rural locations and areas near metropolitan centers.

We interviewed Federal, State, and county officials of the above agencies; State housing officials; local planning officials; bankers; and builders. We examined legislation and administrative regulations, procedures, and program records. We also toured single-family homes and rental housing projects financed by FmHA.

CHAPTER 2

FURTHER IMPROVEMENTS NEEDED

TO UPGRADE RURAL HOUSING

Although significant improvements in rural housing quality have been achieved, many rural families live in substandard housing today. Rural areas contain about one-half of the Nation's substandard housing but only one-third of the population. About three-fourths of the rural substandard housing is located in more remote or difficult-to-reach communities. These areas are plagued by a high incidence of poverty, rising homeownership costs, and a lack of volume homebuilders. Among substandard housing occupants, a high proportion are elderly and half are renters.

A national housing goal of 26 million new or rehabilitated units, established in 1968 for the 10-year period ended June 1978, fell about 5 million units short. While goals for new rural housing were less definitive, apparently only one-half of 1.5 million units targeted for low- and moderate-income families were built.

HOUSING GOALS AND OBJECTIVES

The Housing and Urban Development Act of 1968 required production targets to help meet the national goal of decent housing for all. The objective was to build or rehabilitate 26 million housing units by 1978. Because the Nation was treated as one housing market, there was no urban-rural apportionment of the targets.

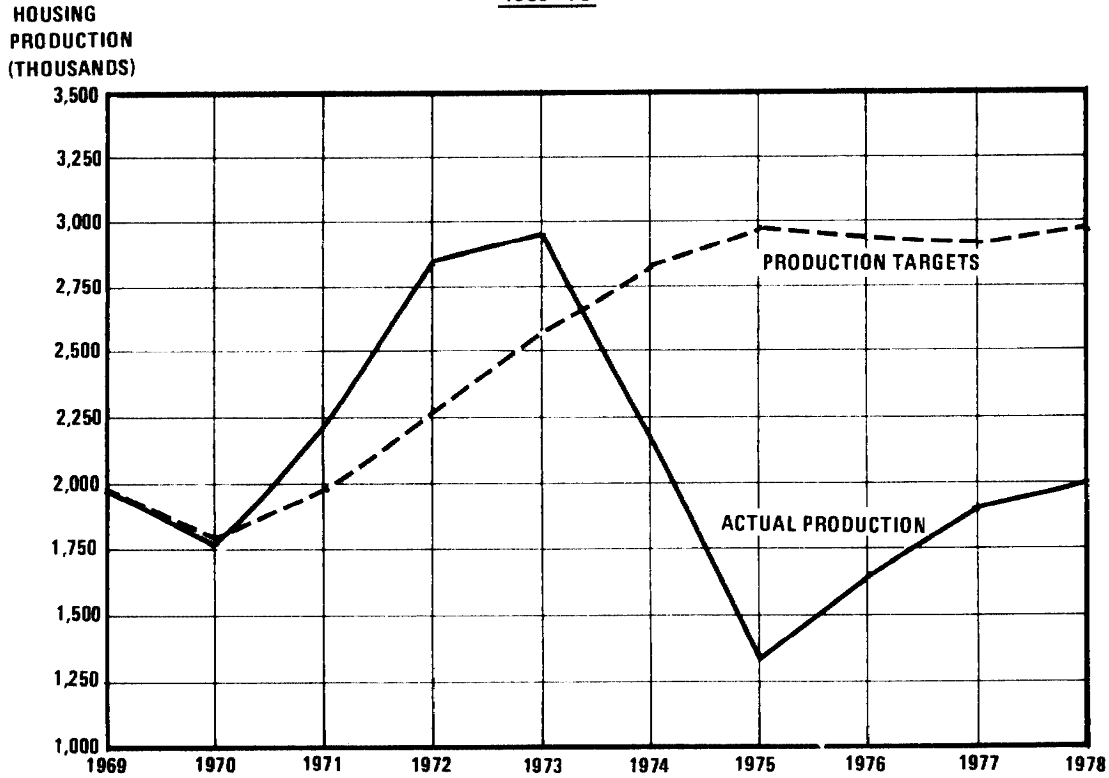
The Rural Development Act of 1972 directed the Secretary of Agriculture to establish rural housing goals as part of overall development plans. The housing goal established, however, was only a general statement calling for equal access to standard-quality housing in rural and metropolitan areas.

During the 10-year period an estimated 21 million housing units were produced nationally, about 5 million units short of the target.

Overall, production targets were exceeded in the first 5 years. By June 30, 1973, about 11.7 million units were produced, exceeding the 10.5-million target. However, production in the last 5 years of the period fell short of the targets. In 1975, for example, the targeted production was 2.95 million units, but only about 1.3 million were produced. The graph on page 8 compares targeted and actual production of housing units nationwide. (Production for 1977 and 1978 was estimated based on preliminary data.)

COMPARISON OF ACTUAL AND TARGETED PRODUCTION

1969 - 78



TRENDS IN RURAL HOUSING CONDITIONS

The incidence of rural substandard housing declined from 59 percent of occupied units in 1950 to about 8 percent in 1975. During this period nearly 7 million substandard rural homes were eliminated while the supply of adequate units increased by about 15 million. Construction accounted for much of the progress, but migration to the cities also played a major role in upgrading rural housing quality. When farm population dropped from 23 million in 1950 to 9.7 million in 1970, millions of substandard rural homes were abandoned or destroyed.

The number of substandard rural homes, defined as homes that lack complete plumbing or are dilapidated, decreased nearly 79 percent from about 9 million in 1950 to about 1.9 million in 1975. The following table shows the trend.

Trends in Rural Substandard Housing 1950-1975

	1950	1960	1970	1975
	(000 omitted)			
Lacking complete plumbing	8,947	4,678	2,387	1,331
Dilapidated with complete plumbing (note a)	133	207	497	593
Total	9,080	4,885	2,884	1,924

a/Estimated by the Economics, Statistics, and Cooperatives Service of the Department of Agriculture.

The Annual Housing Survey of 1976, conducted by the Department of Commerce and sponsored by HUD, showed that rural housing conditions further improved in 1976 but still lagged behind improvements in urban housing. While occupied rural housing increased to 23,553,000 units, those which lacked complete plumbing declined to 1,265,000. The number of dilapidated units is not shown in the annual surveys, but other selected defects are counted to compare the conditions of rural and urban housing, as shown in the following table. The defects cannot be totaled because more than one structural deficiency may be reported for the same unit.

Percent of Occupied Housing Units with Selected Defects in 1976

Defect	Metropolitan	Rural
Lacks some or all plumbing:	1.3	5.4
Lacks bathroom	1.1	5.1
Lacks piped-in water	0.2	2.0
Lacks complete kitchen	1.0	3.0
Water leaks:		
Through the roof	5.3	7.2
In basements	18.6	28.1
Open cracks or holes in interior ceilings and walls	5.4	5.3
Holes in interior floors	1.6	1.9
Signs of mice or rats	9.1	15.8

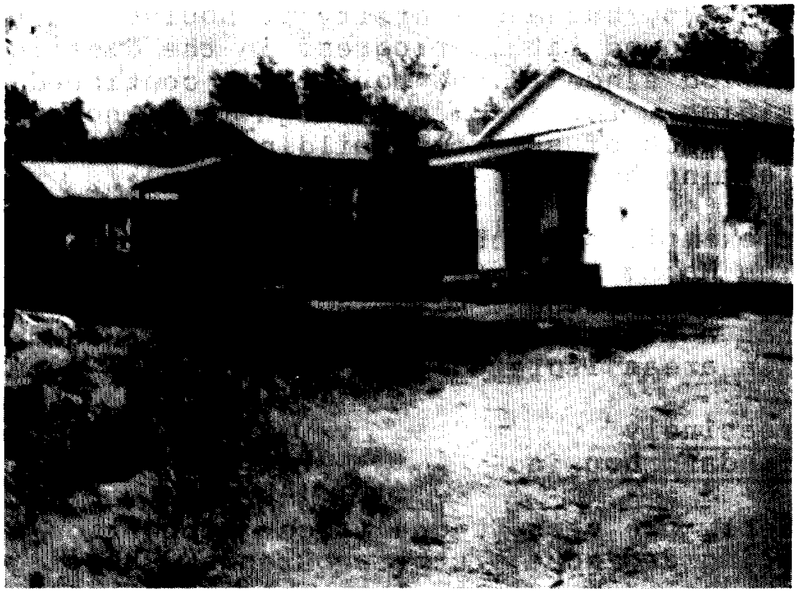
Remote areas show little housing improvement

Although rural residents made significant progress toward adequate housing, not all areas shared equally in the gain. Rural poverty and poor housing persist in large areas of the country. Per capita income is low, and essential public facilities and services are inadequate. About three-fourths of the substandard rural housing is located in remote and more difficult-to-reach communities containing less than 2,500 people. The photographs on page 11 show occupied substandard homes in remote areas.

The following table shows the distribution of substandard housing by community size.

Distribution of Substandard Housing by Size of Town in 1975

Population	Percent
Under 2,500	74.9
2,500 to 4,999	6.0
5,000 to 9,999	6.9
10,000 to 24,999	7.4
25,000 and over	4.8
Total	100.0



OCCUPIED SUBSTANDARD HOUSES IN RURAL
CHAMBERS COUNTY, ALABAMA

OCCUPIED SUBSTANDARD HOUSE IN NORTHAMPTON
COUNTY, NORTH CAROLINA

The problems found in the Kentucky River Area Development District, a planning region composed of eight counties containing only five communities of 1,000 or more population, exemplify those of remote areas. In 1970 about 107,245 people resided in 29,675 homes, of which 52.4 percent were substandard. Due to growth in the coal-mining industry, population increased to 119,286 in 1975, but a University of Louisville housing needs analysis showed little progress in the district during the 5-year period since 14,492 households continued to need housing subsidies. Low incomes, a high incidence of elderly residents, and lack of suitable building sites were principal problems affecting housing in this area.

Another example of problems in remote areas can be found in Maine. The Maine Human Services Council estimated that 76 percent of homes without plumbing were located in rural areas and that a high proportion of the substandard housing was located in areas isolated from even a small community.

Elderly increasingly occupy substandard housing

The elderly are occupying a larger proportion of the Nation's housing and more of the substandard housing in both rural and metropolitan areas. The table on page 13 shows these increases.

Providing housing for the elderly is difficult because they often have declining incomes, reduced physical strength, and less mobility. Many elderly persons find single-family homes expensive, difficult to maintain, or too isolated. Adequate rental apartments are scarce in rural areas and often too expensive or inconvenient to needed services.

Renters occupy half of substandard rural housing

In 1976 about 52 percent of all occupied substandard rural housing was rented. This percentage has increased from about 44 percent in 1950. Three factors contributing to the problem were:

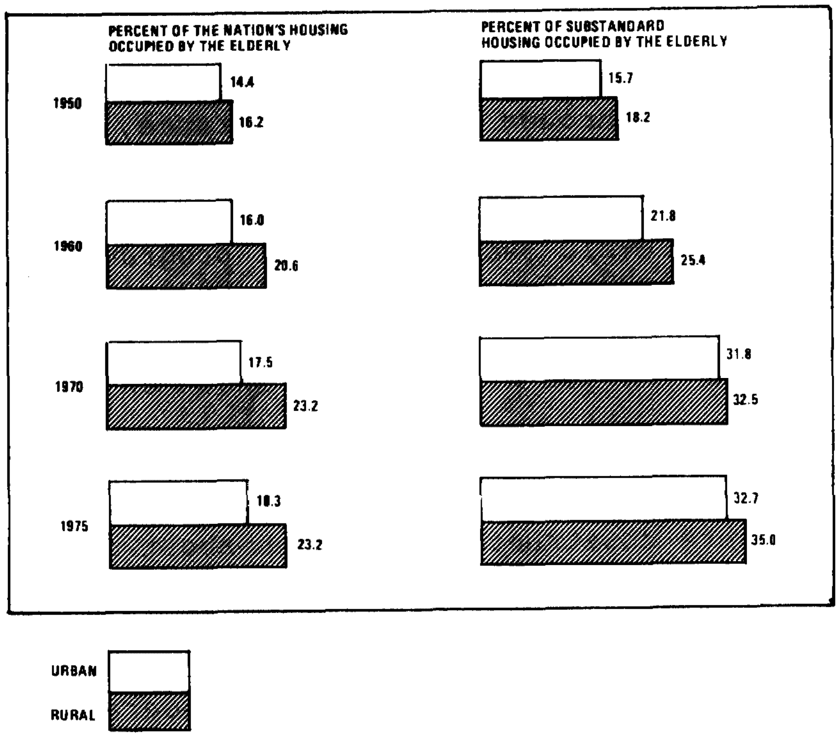
--Age--About 48 percent of the occupied units were 37 years old or older.

--Condition--About 10.8 percent of the units lacked complete plumbing.

--Renter income--About 50 percent of the occupants had incomes of less than $7,000.

TRENDS IN HOUSING OCCUPIED BY THE ELDERLY

1950 - 75



Between 1970 and 1976 rural rental housing increased by nearly 754,000 units. This increase was due primarily to (1) a growing number of elderly residents, (2) rising single-family housing costs, and (3) a halt in rural outmigration.

FEDERAL CONTRIBUTIONS TO RURAL HOUSING PRODUCTION

About 23 percent, or 3.1 million, of the 13.5 million rural housing units constructed from 1950 through 1976 were federally supported through mortgage insurance, guarantee, direct loan, or subsidy programs. The annual level of Federal support fluctuated between 12.3 percent in 1964 and 33.9 percent in 1970. These fluctuations generally paralleled national home construction levels because Federal programs rely on private builders and lenders. The graph on page 15 shows the annual level of Federal support for rural home production from 1950 through 1976. Photographs of rural housing units supported by FmHA and HUD programs are shown on pages 16 to 19.

Although HUD was the major source of Federal support for rural housing production before 1973, since then FmHA has predominated. During the 1950s and 1960s about 8.9 million rural housing units were constructed, of which about 1.9 million received Federal support. About 54 percent of the units received HUD support. HUD support peaked in 1970 and 1971 at about 100,000 units each year but has since declined to about 40,000 units in 1976. The graph on page 20 shows the levels of support for rural housing by the three Federal agencies--FmHA, HUD, and VA--and the Federal Land Banks from 1969 through 1976.

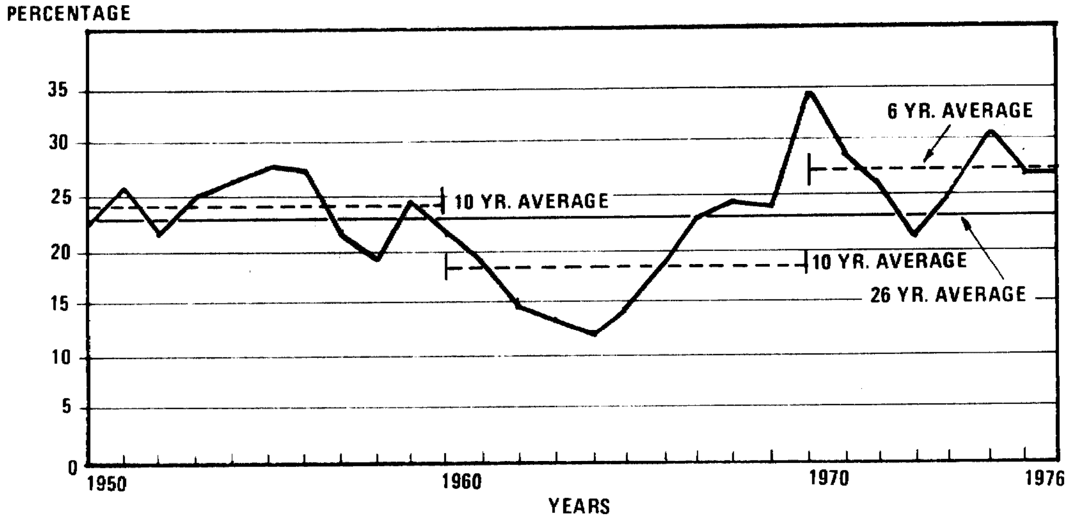
FmHA, HUD, and VA officials told us that the changes in agency support over the 10-year period can be attributed to the following factors:

--FmHA loans have more liberal terms, including no downpayment and interest rates as low as 1 percent.

--FmHA has 1,896 county offices and is much more accessible to rural builders than HUD and VA, which have offices in metropolitan areas.

--Construction cost increases have reduced the ability of rural families to buy homes without some type of subsidy.

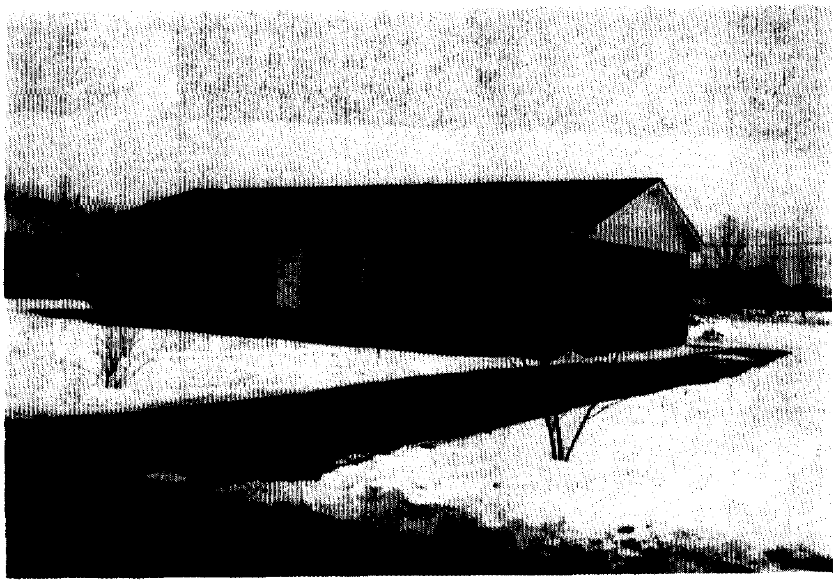
CONTRIBUTION OF FEDERAL PROGRAMS
TO RURAL HOUSING PRODUCTION
AS A PERCENT OF TOTAL CONSTRUCTION



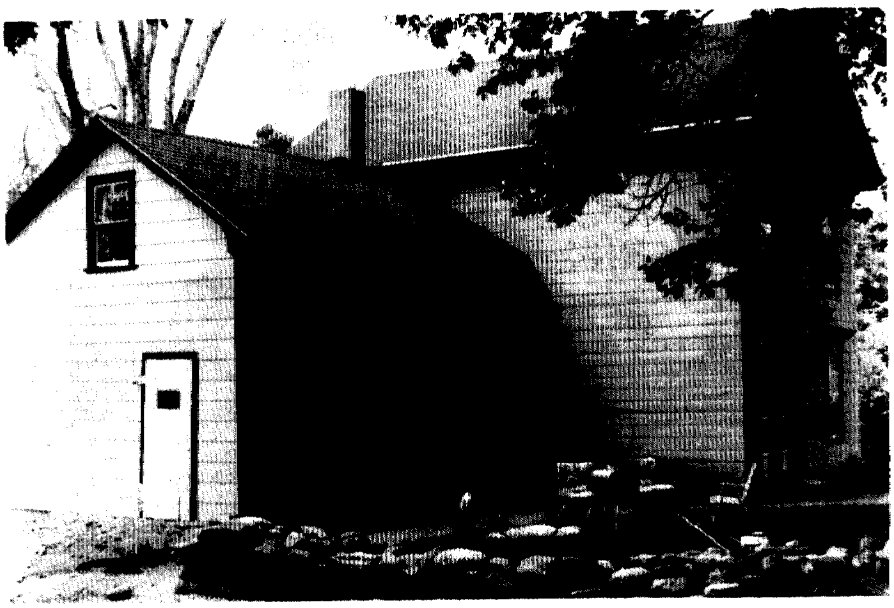
FORMER SUBSTANDARD RESIDENCE OF AN FmHA BORROWER IN CHAMBERS COUNTY, ALABAMA

NEW FmHA-FINANCED HOME OF BORROWER PREVIOUSLY RESIDING IN HOUSE SHOWN ABOVE

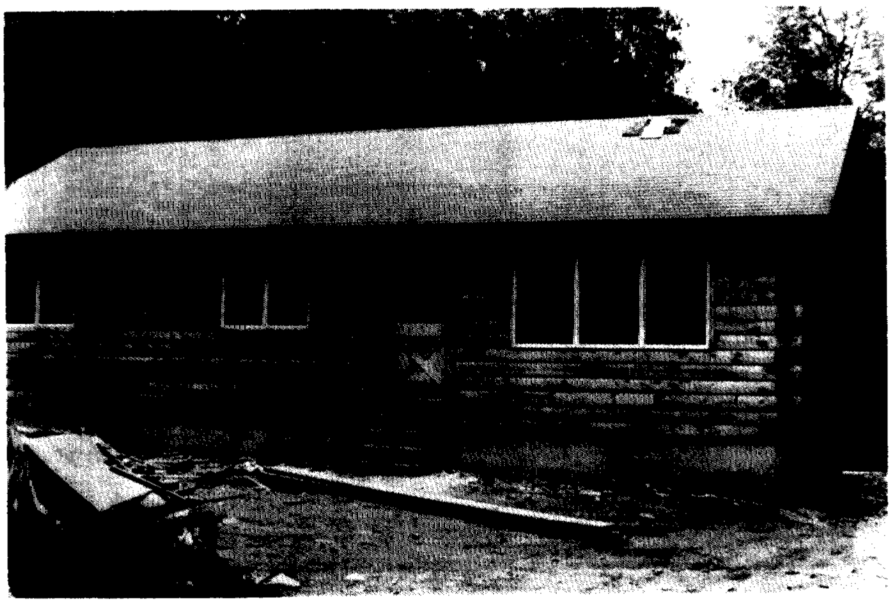
FmHA-FINANCED SUBDIVISION IN
VIGO COUNTY, INDIANA



FmHA-FINANCED HOME IN OLDHAM COUNTY, KENTUCKY



HOUSE PURCHASED AND REPAIRED IN PENOBSCOT COUNTY, MAINE, WITH AN FmHA LOAN



FmHA-FINANCED LOG HOUSE BEING CONSTRUCTED BY OWNER IN PENOBSCOT COUNTY, MAINE

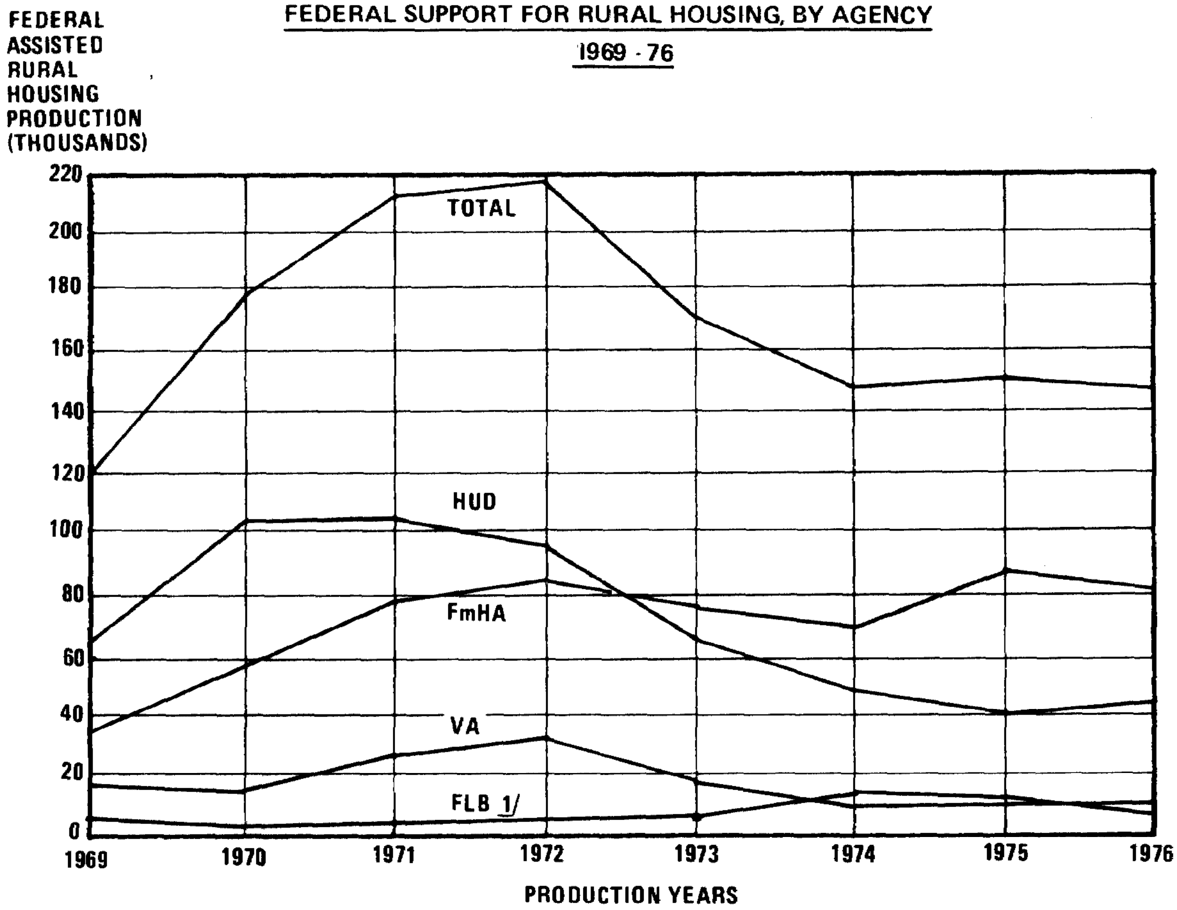
FmHA-FINANCED HOUSING PROJECT FOR THE ELDERLY IN OTERO COUNTY, COLORADO

FmHA-FINANCED AND HUD SECTION 8- ASSISTED MULTIFAMILY HOUSING PROJECT IN CLINTON COUNTY, INDIANA

HUD PUBLIC HOUSING PROJECT IN NORTHAMPTON COUNTY, NORTH CAROLINA

FEDERAL SUPPORT FOR RURAL HOUSING, BY AGENCY

1969 - 76



1/ Federal Land Banks are not Federal agencies but are included because they are federally chartered and hold limited authority to extend rural housing credit.

HOUSING PRODUCTION FOR LOW- AND MODERATE-INCOME FAMILIES

The Housing and Urban Development Act of 1968 estimated that, during the 10-year target period (1968-78), 6 million new and rehabilitated housing units were needed for low- and moderate-income families requiring Federal assistance. The act, however, did not apportion the units among the agencies nor did it establish annual production targets.

In 1970 the Second Annual Report on the National Housing Goals, required by the act, assigned 25 percent of the 6 million units, or 1.5 million units, to FmHA and the remaining 4.5 million to HUD. Since FmHA was the major source of federally subsidized housing in rural areas, the 1.5 million units were apportioned essentially to low- and moderate-income rural families.

The 4.5 million units assigned to HUD were not divided between urban and rural areas. Later, however, the Housing and Community Development Act of 1974 required that rural areas receive 20 to 25 percent of the HUD subsidy program funds.

Major FmHA and HUD programs provided funds for about 1.06 million new units in rural areas during the 10 years; thus, production fell short of the 1.5-million-unit target. During that period FmHA provided assistance for about 753,000 new or rehabilitated units while expending almost all funds appropriated for this effort. During the 9-year period ended in 1977, HUD provided about 304,000 new or rehabilitated units for low- and moderate-income rural families, as shown below.

HUD program	Units
Section 235 single-family home ownership	56,000
Section 221 single-family home ownership	5,000
Section 236 rental housing	58,000
Section 221 rental housing	87,000
Section 8 rental assistance	13,000
Low-rent public housing	85,000
Total	304,000

Since 1974, the Section 8 Lower Income Leased Housing Program has been the principal source of HUD subsidies to lower income families. About 146,900 rural families were receiving assistance at the end of 1977. Of these, about 13,000 rural families were living in program-constructed housing, and 133,900 were in existing housing. The section 8 program was apportioned to rural areas in accordance with the Housing and Community Development Act of 1974.

During fiscal year 1978 FmHA initiated a rental assistance program similar to the HUD section 8 program. Eligible families are those living in FmHA-financed rental housing who earn less than $11,200 annually. The program was to assist about 20,000 families during the first year.

ECONOMIC PROBLEMS PERPETUATE HOUSING CONDITIONS

Substandard rural housing is perpetuated by economic problems over which Federal housing agencies have little control but which they must consider when designing and operating their programs. Included are problems such as (1) low family income, (2) rising costs of homeownership, and (3) lack of volume homebuilders.

Rural income levels low

Family income is probably the most important factor in obtaining adequate housing. Rural families have lower income levels than urban families and therefore have more trouble affording decent housing. The following table compares the 1976 income levels of rural and urban families.

Selected Rural and Urban Income Characteristics

	Rural	Urban		
		Total	Central city	Suburbs
	(000 omitted)			
Number of families:				
Owner-occupants	17,009	30,895	11,349	19,546
Renters	6,544	19,557	11,581	7,976
Total	23,553	50,452	22,930	27,522
Median annual family income:				
Owner-occupants	$11,900	$16,200	$14,300	$17,300
Renters	$ 7,100	$ 8,600	$ 7,500	$10,200
Percent of households with annual incomes below $7,000:				
Owner-occupants	28.5	17.6	21.8	15.1
Renters	49.4	41.3	47.1	32.9
All occupants	34.3	26.8	34.6	20.2
Percent of households with annual income below $15,000:				
Owner-occupants	63.5	45.7	53.0	41.4
Renters	85.0	78.3	82.0	73.0
All occupants	69.5	58.3	67.7	50.6

As shown above, rural families have median incomes that are even lower than those of central city residents.

Two and one-half times family income is generally considered by housing and lending industries as a measure of an affordable mortgage. Based on this criterion, about 70 percent of rural households could not afford a mortgage greater than $37,500.

During the past few years the cost of new homes increased steadily nationwide. In the 1960s family incomes kept pace with housing costs but lagged well behind during the 1970s. The following table illustrates the increased ratio of new housing prices to family income.

Year	Median family income	Median sales price	Sales-price-to-income ratio
1972	$11,100	$27,600	2.50
1973	12,100	32,500	2.70
1974	12,800	35,900	2.80
1975	13,700	39,300	2.90
1976	14,500	44,200	3.05
1977	16,000	48,800	3.05

Rural housing costs higher

Construction costs per square foot are generally higher for rural than urban homes. Since rural homes are smaller than urban houses, the cost per square foot is a better comparison of housing costs than sales price. The following table compares increases in urban and rural housing costs nationwide.

Single Family Houses Sold
1973-1977

Year	Area	Square footage per unit		Cost per square foot	
		Median	Average	Median	Average
1973	Urban	1,625	1,760	$17.15	$17.55
	Rural	1,380	1,490	17.05	17.95
1974	Urban	1,665	1,785	18.75	18.85
	Rural	1,405	1,545	19.60	19.55
1975	Urban	1,630	1,735	20.55	20.90
	Rural	1,365	1,490	21.45	21.80
1976	Urban	1,675	1,775	22.25	22.65
	Rural	1,425	1,560	22.85	23.05
1977	Urban	1,705	1,795	24.70	25.40
	Rural	1,440	1,565	25.10	25.10

In some rural areas housing costs are higher than the national average. For example, in 1978 throughout most of Maine, the cost of building a home was about $35 a square foot; in Colorado the cost was about $36. Housing officials in these States attributed the higher costs to the price of land and the cost of its development.

Homeownership costs, including utilities, are also increasing nationwide. The following Consumer Price Index data shows the inflationary spiral of such costs compared to the 1967 base period. As can be seen, most costs have about doubled since 1967.

	1967	1973	1976	Oct. 1978
All housing	100	135.0	177.2	209.5
Rental	100	124.2	144.7	167.4
Homeownership	100	146.7	191.7	237.0
Fuel and utilities	100	126.9	182.7	220.1
Furnishings and operations	100	124.9	168.5	181.9

Heating costs particularly affect rural homeowners. Between 1973 and 1977 about 61 percent of rural homes were constructed to use electric heat due to lack of gas facilities or the inability of utility companies to accept new customers. Costs vary by region, but heating with electricity is generally more expensive than gas. During 1977, for example, heating a modest home in Kentucky cost about $34 more a month using electricity than gas. In Colorado electric heating cost $20 more per month. More rigid thermal standards have been implemented by FmHA to help overcome problems associated with rising heating costs.

Few volume rural homebuilders

Rural housing construction is characterized by the lack of economically efficient builders. The building industry comprises many small companies which are generally under-organized, highly transitory, and inhibited by inefficient operations and seasonal conditions. Many rural builders construct houses as a secondary occupation.

The 1977 Alabama State housing plan showed that, unlike large companies, rural builders operate on a unit basis, largely using manual operations which often waste labor and materials. The resultant inefficiency and increasing costs of land, labor, and materials often discourage construction of houses affordable by low- or moderate-income families. Volume builders, because of inconvenience and high overhead costs, generally resist expanding their operations into outlying areas.

FUTURE DEMAND FOR NEW RURAL HOUSING MAY NOT BE MET

Demand for new rural housing may not be met unless production is increased beyond that of the past 10 years. The average annual housing demand from 1976 to 1985 is an estimated 895,000 units, but the annual supply in the previous decade averaged only 622,200 units.

The proportion of the Nation's population residing in rural areas declined in the past due to rural-to-urban migration. According to a 1976 study by the Department of Agriculture, this migration apparently stopped between 1970 and 1973 and may have reversed. The study pointed out that in the first years of the 1970s, rural counties experienced average annual immigration of 353,000. It is unknown if this population shift will be long term, but according to the study, rural households will probably account for one-third of the Nation's estimated 86.5 million households by 1985. The graph on page 27 compares past rural housing production levels with projected demand.

The demand for new housing units is governed by the formation of households and replacement of units lost through demolition or casualty. Of the projected demand for 9 million rural units in the 1976-85 decade, over 67 percent is for household formation. The number of households actually formed, however, will be affected by the availability of housing units. If units are available at reasonable cost, creation of households may be encouraged. Conversely, a shortage of units may limit formations.

As shown by the graph on page 27, projected demand apparently does not exceed capacity to supply rural housing before 1980. Production needed after 1980 may be more difficult to meet. A major issue identified by Agriculture's study is the capacity of the economy to generate capital to sustain the rising levels of rural housing demand.

The affordability of rural housing may also be a major problem because, as discussed previously, in the 1970s prices of homes nationwide increased faster than household incomes. From 1970 to 1975 the cost of new single-family homes increased 58 percent while median income increased only 44 percent. Continuation of this trend in rural areas could reduce housing demand, increase average aging of housing, and slow the improvement of housing quality.

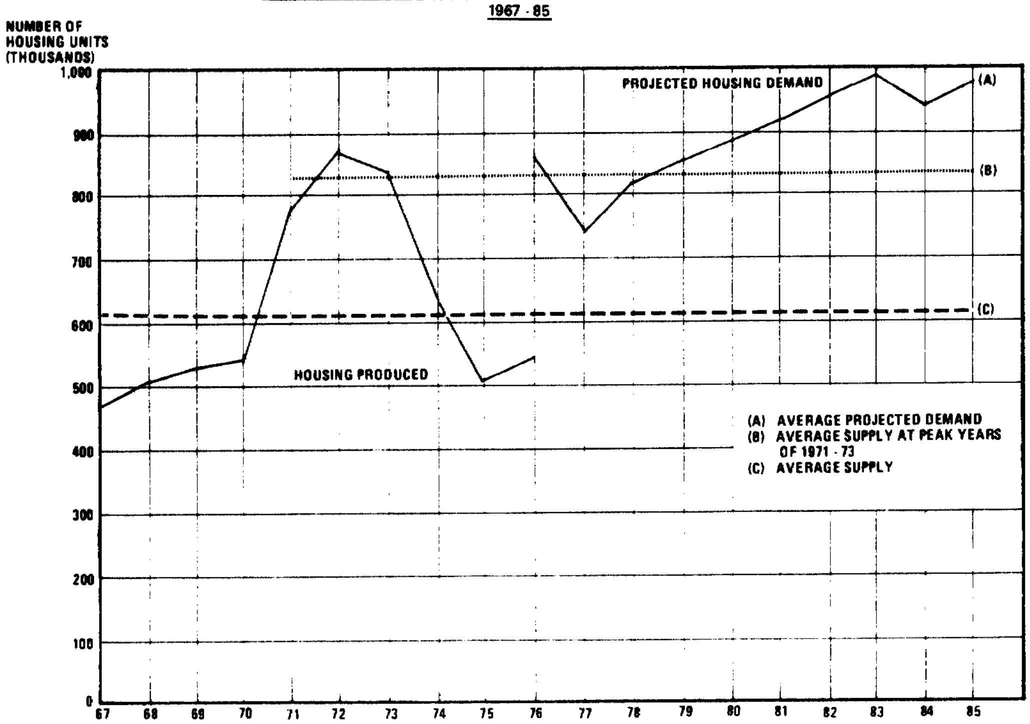
CONCLUSIONS

The condition of rural housing has significantly improved over the last 30 years, and Federal housing programs have contributed to this improvement. However, many rural families remain in substandard housing. Rural areas have about one-third the Nation's population but one-half the substandard housing. About three-fourths of this housing is located in outlying and difficult-to-reach areas. These areas are plagued by low incomes and inadequate public facilities and services.

Because of the economic problems in rural areas, such as low family income and high homeownership costs, future rural housing improvement depends largely on Federal housing agencies'

RURAL HOUSING PRODUCTION COMPARED WITH PROJECTED DEMAND

1967 - 85



taking steps to improve the effectiveness of their programs, particularly in view of the expected increase in demand for rural housing.

The demand for rural housing in the decade ending in 1985 is estimated at 895,000 units a year. The level of production required does not appear to be beyond construction capacity before 1980. After 1980 meeting rural housing demand may be more difficult because of problems such as shortages of (1) rural mortgage credit, (2) housing assistance for low- and moderate-income families, particularly in remote areas, and (3) affordable building sites.

CHAPTER 3

RURAL FAMILIES RECEIVE LESS

FEDERAL HOUSING SUPPORT THAN URBAN FAMILIES

Rural families have not benefited from Federal housing programs to the same extent as urban families. Only about 20 percent of Federal housing support went to rural areas although housing deprivation there was more acute. Federal support of rural housing generally decreases as the distance from urban centers increases. Factors contributing to this include

- --an FmHA program which applies about one-fourth of its support to metropolitan counties,
- --HUD programs which were designed for urban areas with little consideration of rural financial needs or resources, and
- --State housing agencies which support primarily urban housing because rural financial institutions often decline to participate and cooperating urban financial institutions confine loan activity to more urban areas.

DISTRIBUTION OF MAJOR FEDERAL HOUSING SUPPORT

Federal support to rural areas consists primarily of direct loans or subsidies to low- and moderate-income families residing in less remote areas. The following table shows the urban-rural distribution of the major housing programs operated by FmHA, HUD, and VA, based on SMSA boundaries. Federal support includes guaranteed and insured mortgages, direct loans, and contributions for low-rent public housing.

Estimated Urban-Rural Distribution
of Major Federal Housing Support

Agency and program	Period of operation	Units Total	Units Urban	Units Rural	Percent rural
Department of Housing and Urban Development:					
Single-family mortgage insurance	1934-77	12,266,222	10,426,288	1,839,934	15.0
Rental housing mortgage insurance	1935-77	2,398,879	2,036,408	362,471	15.1
Low-income public housing	1937-77	1,367,958	1,016,393	351,565	25.7
Veterans Administration:					
Guaranteed home loans	1944-77	9,672,969	8,145,607	1,527,362	15.8
Direct home loans	1950-77	328,865	91,227	237,638	72.3
Farmers Home Administration:					
Single-family direct loans	1950-77	1,077,579	247,843	829,736	77.0
Rental housing direct loans	1963-77	117,633	19,527	98,106	83.4
Total		27,230,105	21,983,293	5,246,812	19.3

The distribution of Federal housing support between rural and urban areas can also be demonstrated by comparing per capita outlays (new commitments, guarantees, insurance, and appropriations) for housing. In the peak building year of 1972, per capita Federal outlays in urban areas were $127 but were only $61 in rural areas. In 1975, a year of low building activity, per capita urban outlays were $85 and rural outlays were $50.

FmHA SUPPORT NOT CONCENTRATED IN REMOTE RURAL AREAS

Since 1965 FmHA has significantly increased housing support to low- and moderate-income families. Distribution of the support, however, was similar to that in other Federal programs in that much of the housing was constructed around urban areas. We estimate the 23 percent of FmHA single-family home loans made between 1950 and 1977 were for housing in metropolitan counties. In addition, rural counties adjacent to metropolitan areas received a large proportion of the support. For example, in the six States we visited, 35 percent of the single-family home loans made during fiscal year 1977 were in counties adjacent to metropolitan counties. FmHA officials told us that many of these loans had been made for homes in bedroom communities and to families who were prior residents of the urban center. They also pointed out that expansion of rural areas to include places with populations of 10,000 to 20,000 outside SMSAs, which occurred by law in 1974, increased development near urban centers.

FmHA assistance has been concentrated in urban areas and counties adjacent to urban counties because demand-oriented program management relied on builders and realtors to refer clients rather than reaching out to those in more remote areas. Builders and realtors tend to concentrate in areas with access to suitable building sites, ready labor and materials supply, and adequate public facilities. Thus, the more accessible rural communities contain much of the FmHA-financed housing, and the programs have had little impact on reducing substandard housing in outlying areas.

HUD SUPPORT PRIMARILY URBAN

Various HUD studies have concluded that the major HUD programs were designed for urban areas with too little consideration of rural financial needs or resources. HUD support was distributed primarily on demand, and little attempt was made to increase demand through advertising or outreach. For example, during 1977 no insured loans were made in many remote Kentucky counties. HUD has but one program specifically for rural areas, the 203(i) program which began in 1954. This program reduces some of the requirements placed on insurance of housing mortgages in built-up urban areas. Fewer than 100,000 loans have been insured under the program.

During 1978 the Secretary of HUD organized a task force to study the delivery of HUD services to rural areas. The task force concluded that additional outreach and further analysis of program delivery were needed. As a result, the States of North Carolina and Washington were chosen to participate in a 2-year study of methods to make programs more accessible and extend the capacity of rural communities to use them.

Mortgage insurance programs little used in rural areas

Only about 15 percent of housing covered by HUD mortgage insurance was located in rural areas. According to HUD officials, these programs are not used extensively in rural areas due to (1) limited access to financial institutions or limited capacity of private developers and (2) complex program regulations. HUD local offices are in metropolitan areas, and service to remote areas is difficult. Builders and lenders often must mail applications to a HUD office hundreds of miles away.

The use of single-family HUD mortgage insurance in rural areas has declined since 1973. The growth of FmHA programs during the period probably contributed to the decline. The following schedule shows this decreasing activity.

Year	Number of HUD-insured single-family mortgages	Percentage rural
1970	471,981	13.2
1971	565,417	15.0
1972	427,858	14.1
1973	240,004	13.4
1974	195,850	8.8
1975	255,061	8.3
1976	250,808	7.4
1977	321,118	8.0

HUD's rental housing mortgage insurance programs were also little used in rural areas because, according to HUD officials and various studies, (1) rental housing in rural areas was not considered a desirable alternative to single-family homes, (2) lack of demand prevented construction of rental units in economically sized developments, (3) few builders or developers in rural areas had the expertise to comply with HUD's administrative requirements, and (4) many rural communities lacked suitable sites and adequate public facilities, such as water and sewers, to support rental housing developments.

Remote areas lack public housing

As of December 31, 1977, an estimated 25.7 percent of the 1,367,958 units supported under HUD's Low-Rent Public Housing Program was in rural areas but only 5 percent was in towns of fewer than 2,500 people. According to public housing officials many rural counties had no public housing because they lacked sponsors to organize public housing agencies. HUD officials told us that communities were responsible for initiating discussions, and little attempt was made to sell the program in rural areas.

STATE HOUSING SUPPORT GROWING BUT PRIMARILY URBAN

State housing agencies are playing a growing role in the support of housing for low- and moderate-income families through selling tax-exempt notes and bonds. Four of six States we visited have housing agencies, and most of their funds flow to metropolitan areas.

By September 1977, housing agencies in 34 States had issued bonds for over $10 billion to finance about 400,000 housing units. They used several financing methods including direct loans, mortgage purchases, loans to commercial lenders, and construction loans. In the States visited, most loans were made for units in metropolitan areas because, according to State housing officials, (1) rural financial institutions often declined to participate and (2) the loans were generally covered by mortgage insurance and processed by those lenders familiar with Federal housing programs. For example, the Kentucky Housing Corporation made single-family housing loans to families with adjusted annual incomes not in excess of $15,000 through financial institutions designated as mortgage originators. As of April 30, 1978, they had financed the purchase of 8,023 single-family homes and 2,361 rental units. About 7,000 of the single-family homes and 1,961 of the rental units were in metropolitan areas which contained only 45 percent of the population.

VA HOUSING SUPPORT CONSISTENT WITH DISTRIBUTION OF VETERAN POPULATION

About 18 percent of VA housing support (15.8 percent of VA single-family guaranteed mortgages and 72.3 percent of direct loans) assisted rural veterans. This geographic distribution of support appears consistent with the distribution of the veteran population. In fiscal year 1978 the distribution of the veteran population and designated loan areas was as follows:

Loan program authorized	Counties where programs are authorized	Veteran population in the counties	Percentage of veterans in the counties
Rural areas:			
Direct loan	2,105	4,465,525	15.4
Partial direct and partial guarantee	254	1,563,935	5.4
Urban areas:			
Guarantee	735	22,942,410	79.2
Total	3,094	28,971,870	100.0

VA support of total rural home construction declined from 15.4 percent in 1955 to about 2 percent in 1976. Local VA officials said that the probable cause of the decreased activity was rising home building costs. Also, we noted that many veterans were using the FmHA home loan program.

To assist veterans in credit deficient areas, VA is authorized to make direct home loans. However, to reduce the necessity for direct loans, VA operates a loan referral program. Approved direct loan applications are referred by the receiving VA office to at least three financial institutions within a 100-mile radius of the property to be purchased. The referral is made from a list compiled and maintained by the local VA office, including all Federal savings and loan associations, mortgage bankers, and other lending associations whose deposits are insured by the Federal Savings and Loan Insurance Corporation. These institutions are located or lend money within the local VA office service areas. If a financial institution or mortgage company approves the loan, VA guarantees it rather than making a direct loan.

Of the six States visited, the VA referral system essentially eliminated the need to make direct loans in four States and reduced the need in the others.

In commenting on our report (see app. V), VA stated that our report adequately describes its guaranteed and direct home loan programs.

CONCLUSIONS

The distribution of Federal housing support between rural and urban areas has not been consistent with the relative need. Generally, Federal support for housing decreases as the distance from urban centers increases.

FmHA has provided significant support for rural housing. However, much of the housing was constructed around urban areas because program management was demand oriented and relied on builders and realtors to refer clients rather than reaching out to the more remote areas which had the greatest need.

HUD housing programs have been less successful in rural areas because the major programs were designed for urban areas and are often beyond rural financial or administrative resources.

Single-family and rental housing mortgage insurance programs have not been used extensively due to (1) limited resources of rural financial institutions or limited capacity of private rural developers and (2) complex program regulations. Low-rent public housing has not been used successfully by many rural communities because they lack sponsors to organize public housing agencies.

VA single-family housing support has been more successful in rural areas because the agency is authorized to make direct loans in credit deficient areas. Overall, VA support appears consistent with the distribution of the veteran population.

State housing agencies are playing a growing role in housing support for low- and moderate-income families, but to date most support has flowed to urban areas. The State agencies have been less successful in rural areas because (1) rural financial institutions often declined to participate and (2) the loans were generally covered by Federal mortgage insurance and processed by urban lenders familiar with Federal housing insurance programs.

CHAPTER 4

NEED TO INCREASE THE SUPPLY

OF RURAL MORTGAGE CREDIT

Families in remote areas have inadequate access to mortgage credit because local financial institutions make few home loans. Because credit is essential for home construction or improvement, lack of credit contributes to the high incidence of substandard housing in rural areas.

Rural banks have not met the need for housing credit because they are small and are called upon to supply a wide range of credit needs. Alternative loan opportunities often provide a higher return to the banks. Savings and loan associations are not numerous in remote areas and provide only a small number of housing loans. They generally require mortgage terms which are more restrictive than urban associations.

To stimulate housing construction in remote areas, home loans need to be long term with low downpayments and reasonable interest rates. Urban families with greater access to financial institutions have more opportunities to obtain mortgage credit on favorable terms. Thus, they have a significant advantage over rural families in obtaining housing.

To overcome the shortage of local credit, rural areas need to attract mortgage loan funds from urban capital markets. The new FmHA guarantee program will probably not accomplish this objective because it relies mainly on local lenders. The program, however, could be revised so that loan applications from remote areas are referred to financial institutions--particularly urban ones--willing to make loans.

Federal Land Banks, while not Government agencies, could, through their extensive network of local offices and direct access to money markets, extend greater amounts of housing credit in rural areas within the authority they hold. The decision to do so rests substantially with the farmer owners of those institutions who determine lending policies and practices. In our opinion, an increase in FLB housing loans would not significantly affect their providing adequate credit to commercial farmers.

Legislation is being considered by the Congress to increase the supply of mortgage credit for rural housing. This legislation would create a rural development bank to assist rural communities by making funds available for various purposes. Under various conditions the bank would make or guarantee housing or purchase loans extended by rural financial institutions to residents of rural areas.

RURAL BANKS HAVE LIMITED LENDING CAPABILITIES

Rural banks have not met the need for housing credit because low asset levels, based on deposits from the local economy, restrict lending capability. In 1975 the per capita assets of banks in the most rural counties averaged only $3,303 compared with $6,834 in the largest metropolitan counties. In addition, they are called upon to supply a wide range of credit, including loans for farm property, farm and business operation, and consumer goods. Thus, they often cannot make large numbers of home loans.

Rural banks generally require downpayments of 20 to 50 percent for the limited number of home loans they make. Such large downpayments limit the families who can qualify for loans; young, newly formed households are usually most affected. While they may have sufficient steady incomes to afford loans, young families often have not saved enough for downpayments.

The length of the mortgage life also affects affordability. Rural banks generally require shorter amortization periods than do urban banks or savings and loan associations. Repayment periods of 15 years or less are common, and more than 20 years is rare. Interest rates charged by rural and urban banks are similar.

SAVINGS AND LOAN ASSOCIATIONS NOT NUMEROUS IN RURAL AREAS

About 800 of the Nation's 2,400 rural counties had no savings and loan association in 1975. Where these lenders are accessible, buyers generally look to savings and loan associations for mortgage credit because they make long-term loans at reasonable interest rates and with low downpayments. Nationally, associations are by far the largest source of single-family mortgage credit.

Rural associations offer less attractive mortgage terms than urban associations. Downpayment requirements are generally higher and repayment periods are shorter. While interest rates are similar, the shorter repayment period results in higher monthly payments for borrowers; thus, fewer rural families can afford the loans.

In 1975 only about 0.2 percent of housing loans held by savings and loan associations were for homes in counties most rural in character. Housing loans held by associations in counties with no towns having over 2,500 residents were $52 per capita compared with $1,456 for associations in large metropolitan counties with populations of at least 1 million.

LITTLE ACTIVITY BY MORTGAGE COMPANIES IN RURAL AREAS

Mortgage banking officials told us that mortgage companies do not emphasize operations outside urban areas because investors often place restrictions on rural loans.

Mortgage companies make original mortgage loans which they later sell to third parties but continue to service for a fee. Consequently, not many mortgages are held by the companies in their own portfolios.

FEW INSURED OR GUARANTEED LOANS MADE IN RURAL AREAS

Rural commercial banks and savings and loan associations make little use of Federal mortgage insurance or guarantee programs. This fact affects the ability of rural families to purchase or build homes. HUD's single-family house mortgage insurance program requires a downpayment of 3 percent of the first $25,000 borrowed and 5 percent of the remainder. VA-guaranteed loans require no downpayments. Also, mortgages federally insured or guaranteed have terms of up to 30 years, reducing monthly payments. However, few rural families have been able to take advantage of these favorable terms. The following table compares the use by urban and rural financial institutions of federally supported mortgage loan programs.

Percentage of Family Housing Loans Federally Insured or Guaranteed as of December 31, 1975

Type of loan by institution	Population of metropolitan counties: Over a million	Population of metropolitan counties: 50,000 to 1 million	Population of rural counties: 2,500 to 50,000	Population of rural counties: All rural
Banks:				
Insured by HUD	6.6	4.2	2.7	2.9
Guaranteed by VA	4.8	3.4	1.2	0.5
Savings and loans:				
Insured by HUD	7.2	6.4	4.5	1.8
Guaranteed by VA	9.0	7.3	5.0	2.4

The primary reason cited by rural lenders for not making federally insured or guaranteed home loans is the involved administrative requirements. Paperwork is extensive and is generally designed for large volume builders and lenders in urban areas that often employ specialists to prepare the documents. Rural institutions seldom have the loan volume to justify such employment.

The administrative requirements may not be the only reason rural institutions do not invest assets in housing loans. Rural institutions often invest available funds for shorter periods and at higher interest rates than allowed by HUD and VA.

OPPORTUNITIES TO INCREASE THE AVAILABILITY OF MORTGAGE CREDIT IN RURAL AREAS

Need to revise the FmHA Guaranteed-Loan Program

Without revision, it is unlikely that the FmHA Guaranteed-Loan Program will significantly increase mortgage credit in remote areas because it contends with similar administrative and economic obstacles, such as limited participation by local financial institutions, which hindered the use of HUD insurance and VA guarantee programs. In addition, the loan terms required under the guarantee program are not compatible with requirements of Federal Land Banks, a possible source of loan funds under the guarantee program.

The Rural Development Act of 1972 authorized FmHA to guarantee commercial home loans in order to stimulate the supply of private mortgage credit in rural areas. According to State FmHA officials, the original program was not successful because the allowable interest rate was limited to that on FmHA direct loans. The FmHA interest rate was generally less than that charged by rural financial institutions. The program's lack of success was demonstrated during fiscal years 1976 and 1977 when only 75 loans were guaranteed by FmHA in the entire Nation.

The Housing and Community Development Act of 1977 made two major changes in the guarantee programs:

--Where previously only moderate-income families (earning $11,200 to $15,600 annually) were eligible, now families earning more than the moderate-income standard are eligible.

--The allowable interest rate is now negotiable between the borrower and lender but cannot exceed prevailing rates in the locality.

Loan guarantee terms not compatible with requirements of Federal Land Banks

The terms of the guarantee program are not compatible with loan terms required by FLBs. Two basic conflicts are involved:

--FLB loan regulations usually require variable interest rates while FmHA regulations require fixed rates.

--FLBs, as provided by law and design of the farm owners, require an effective downpayment of 20 percent to ensure the system does not engage in "soft" credit; FmHA regulations allow a minimum downpayment of 3 percent of the first $25,000 borrowed and 5 percent of the remainder.

Unless these conflicts are resolved, the FLBs cannot participate in the guarantee program, and thus a potential source of mortgage credit will not be available to rural families.

Need to attract capital to remote areas

Remote areas need to attract mortgage funds from capital surplus areas because of the shortage of savings and bank deposits. Additional mortgage funds could be attracted to these areas if FmHA referred rural families seeking guaranteed home loans to urban financial institutions willing to provide credit.

Urban families are often referred to credit sources by builders and realtors that arrange conditional lines of credit or maintain knowledge of the sources. Due to the distance from capital markets, rural builders and realtors are less likely to have such sources.

A system used by VA, with good results in the States visited, refers direct loan applications received from veterans in remote areas to urban financial institutions willing to make VA-guaranteed loans. FmHA could operate a similar system with the guarantee program.

FLBs could provide more rural housing credit

FLBs have made minimal contributions to rural housing. They occupy a unique position among rural financial institutions and have the potential to expand rural home lending.

FLBs were established because farmers could not obtain farm mortgage credit at affordable terms. Downpayment requirements at rural banks were high and the repayment periods short. These terms prevented many families from owning their own farms.

The cooperative farmer-owned FLB system is a response to those needs, and generations of farm families have benefited from FLB loans. The FLBs have responded further and make mortgage loans to part-time farmers and to a limited extent to certain rural residents. The institutions, however, are farmer-owned cooperatives designed to meet farm mortgage needs and rural home lending is a secondary consideration.

Home loan volume small

Since eligibility was extended to nonfarm rural residents in 1971, the FLBs have made about 9,000 home loans a year. The combined housing loan portfolio of the 12 district banks, as of September 30, 1978, was 33,870, accounting for 3.3 percent of the value of all loans outstanding. About one-third of the home loans outstanding were made by the Columbia, South Carolina, bank, which serves North Carolina, South Carolina, Georgia, and Florida.

Home loans are made at the discretion of local Associations. FLB officials told us that many farm-oriented local officials have not perceived a need for additional nonfarm rural housing credit. They added that other Association officials, alarmed by "leapfrog" housing development of agricultural land, resist further expansion of housing credit.

The banks do not extensively advertise home loan availability among nonfarm residents; advertising is generally restricted to farm publications. District banks provide some advertising material to local Associations for use as they deem appropriate.

Need for more favorable loan terms

Many rural families cannot obtain an FLB home loan because of high downpayment requirements. The Farm Credit Act of 1971 restricts loans to no more than 85 percent of appraised home value. This was by design to maintain a quality of housing loan comparable to that of agricultural mortgage loans. Since the borrower must also purchase equity certificates in the local Association equal to 5 percent of the loan amount, the net loan can be no more than 80 percent of the home value. Thus, the effective downpayment required on a $40,000 home would be $8,000, which precludes large numbers of rural families from using the banks' services. By comparison, the minimum downpayment for such a loan under the HUD-insured program would be only $1,500.

During our review we discussed with FLB officials the restriction that home loans be no more than 85 percent of appraised home value. Also, in a draft of this report sent to the Federal Farm Credit Board on September 27, 1979, we suggested that the Board propose to the Congress legislation to amend the Farm Credit Act of 1971 to reduce the equity requirement so that FLBs can serve more families.

In commenting on our draft report (see app. VI), the Board stated that legislation recently recommended to the Congress by the Board includes raising the 85 percent lending limit for loans supported by Government guarantee. The Board pointed out that, if passed by the Congress, the new provision would apply to rural home loans as well as agricultural loans. The Board further stated, however, that the peculiar posture of rural home lending in the FLBs, and the adamant posture of the user-owners against engaging in soft credit, present immediate limitations to extensive use of that authority in the rural housing area.

Since the Board has proposed the legislative change we suggested, this report contains no recommendation in this area. We believe that the legislation, if passed, could help increase the availability of mortgage credit in rural areas.

CONCLUSIONS

Rural families, particularly those in outlying areas, have inadequate access to home mortgage credit. Rural banks are small and reluctant to make long-term housing loans because they have other, more lucrative business opportunities. Savings and loan associations are scarce in rural areas, and available institutions often require mortgage terms more restrictive than those in urban areas. Neither rural banks nor savings and loan associations make much use of Federal mortgage insurance or guarantee programs. Since adequate credit is essential for home construction or improvement, lack of credit contributes to the high incidence of substandard rural housing.

The availability of rural mortgage credit can be expanded by:

--Revising the FmHA guaranteed-loan program to provide for referring loan applications from remote areas to urban financial institutions willing to make guaranteed loans.

--Allowing more flexible loan terms under the guaranteed-loan program to encourage participation by Federal Land Banks.

--Increasing home loan activity of Federal Land Banks by educating bank management concerning the need to make additional loans.

RECOMMENDATIONS TO THE SECRETARY OF AGRICULTURE

We recommend that to increase the availability of mortgage credit in rural areas the Secretary of Agriculture direct the FmHA Administrator to:

- --Establish a loan referral or clearinghouse procedure through the guarantee program for families in outlying areas who cannot obtain local loans even with an FmHA guarantee. Loan applications should be referred to urban mortgage companies or financial institutions willing to make loans.

- --Revise the guaranteed-loan program to permit variable interest rate loans needed to obtain home loans from FLBs.

RECOMMENDATIONS TO THE SECRETARY OF HUD

We recommend that to increase the availability of home loans on reasonable terms, the Secretary of HUD, in connection with the 2-year study of methods to improve HUD program accessibility in rural areas, devise and test incentives to

- --increase the use of HUD home mortgage insurance programs by rural financial institutions and

- --expand the operations of urban financial institutions into remote areas.

RECOMMENDATION TO THE FEDERAL FARM CREDIT BOARD OF THE FARM CREDIT ADMINISTRATION

We recommend that the Board, to take advantage of the direct access to urban money markets available to the Federal land bank system, emphasize to FLBs the importance of adequate home mortgage credit to orderly development and to the well-being of all rural residents.

AGENCY COMMENTS AND OUR EVALUATION

The Department of Agriculture, HUD, and the Federal Farm Credit Board generally agreed with our findings and recommendations.

Department of Agriculture

In response to our recommendation (see app. VII) that FmHA establish a loan referral or clearinghouse procedure for families in outlying areas who cannot obtain local loans even with an FmHA guarantee, the Department agreed that additional mortgage funds need to be attracted to rural areas. They believe, however, that efforts should be expanded to encourage rural lenders to participate in the secondary market. They believe this would permit rural borrowers to obtain credit within a reasonable distance of their residences and that the location of the lender is essential during loan making and servicing.

As discussed on page 37, many rural areas lack adequate financial services. Many such areas have no savings and loan associations and only small commercial banks. Further, our discussions with rural financial officials disclosed few were interested in engaging in secondary market activities. Also, VA has successfully placed home loans for veterans residing in remote areas with lenders in the more urban areas, as discussed on page 33. VA officials did not indicate to us that the location of the lender presented unusual loan-making or loan-servicing problems under its program.

The Department agreed with our recommendation to revise the FmHA guaranteed-loan program to permit variable interest rate loans needed to obtain home loans from Federal Land Banks. It said that a variable interest rate for the guaranteed rural housing loan program was being considered. The Department pointed out that this change will facilitate participation in the Federal Land Bank housing loan program. However, the Department believes the change will not attract much additional investment capital because secondary money markets primarily use fixed interest rate loan instruments.

In this regard, it should be noted that since the Federal Land Banks hold home loans in their own portfolio, the loan instruments need not be designed for the secondary market. Should other financial institutions or mortgage companies agree to participate in the FmHA guarantee program, the mortgage instruments can be written with fixed interest rates to accommodate their needs.

<u>HUD</u>

HUD agreed with our recommendations (see app. VIII) that, in connection with its study of methods to improve HUD program accessibility in rural areas, it should devise and test incentives to

--increase the use of HUD home mortgage insurance programs by rural financial institutions and

--expand the operations of urban financial institutions into remote areas.

HUD stated that it is deeply concerned with the problems of rural areas and has taken steps to establish demonstrations which will test the effectiveness of our recommended actions. In connection with a rural assistance initiative which it has undertaken, HUD said it was hopeful many lenders, now reluctant to deal directly with HUD, will participate in this demonstration. HUD also pointed out that it has met with the Federal National Mortgage Association to discuss joint efforts to improve the availability of mortgage credit in rural areas and is studying ways the section 235 interest subsidy program can be better utilized in rural areas.

In addition, HUD said it has directed development of a demonstration program of outreach and delegated loan processing. This program is aimed at the more sophisticated urban lender which, in order to participate in the delegated processing program, must take steps to make mortgage insurance financing available in certain areas selected by HUD not now active in the mortgage insurance programs.

In commenting on our report, HUD also stated that it might be useful to distinguish between mortgage insurance programs which are generally used to facilitate homeownership by moderate-income households and housing assistance programs which provide rental or interest subsidies to primarily low-income households. HUD believes the distinction might be useful because

--our conclusion that 20 percent of Federal housing support goes to rural areas includes the full range of mortgage insurance programs, direct loans, and rental assistance programs designed for different income groups;

--Federal housing assistance specifically for low-income households is over 25 percent, since 24 percent of HUD's section 8 funds and 25 percent of HUD's low rent public housing funds are allocated to nonmetropolitan areas; and

--over 90 percent of FmHA housing assistance goes to nonmetropolitan areas.

We believe that an analysis of the distribution of all major Federal housing support programs is useful because it identifies where Federal housing resources have been applied, indicates geographic gaps in individual program coverage, and leads to identification of problems in program design. Such an analysis shows, as discussed on page 30, that rural families have not benefited from Federal housing programs to the same extent as urban families and that Federal support of rural housing generally decreases as the distance from urban centers increases. Further, although each program may serve somewhat different income groups, we believe this difference should not in itself mean that certain programs are or are not applicable to rural areas because rural residents, although having lower incomes generally than urban residents, comprise different income groups.

In this regard, it should also be noted that a distinction by type of housing program and agency is made in the table on page 30. This table illustrates that rural distribution of major Federal housing support ranges from a low of about 15 percent for HUD's single-family and rental housing mortgage insurance programs to a high of about 83 percent for FmHA's rental housing direct loan program.

HUD also said it believed our report would be strengthened by specifying the definitions we used to determine substandard housing. It pointed out that it was unclear what defects were included in the "dilapidation" category. HUD defined substandard as "physically inadequate," which includes "lacking complete plumbing" or up to 16 other specifically enumerated defects collected by the Annual Housing Survey. Using that list of defects, the 1977 survey shows that nonmetropolitan areas contain 41 percent of all units with physical inadequacies, according to HUD.

Our analysis of trends in rural substandard housing contained on page 9 was based on historical definitions used by the Department of Commerce. As discussed on page 9, the Annual Housing Surveys mentioned by HUD do not show the number of dilapidated units but use specific defects to indicate housing conditions. As also discussed on that page, the survey defects cannot be totaled because more than one structural deficiency may be reported for the same unit.

Federal Farm Credit Board

The Federal Farm Credit Board agreed to give our recommendation due consideration and stated rural home lending will be given positive direction within the scope and intent of the Board's authority as structured.

In commenting on our report, the Board stated it had reservations as to whether the FLBs could be equitably included in the report since they believe their structure, management, lending objectives, and independence from Government are totally different from the agencies around which the substance of the report was developed. Their reservations were based on the following reasons.

--FLBs are cooperative lending institutions owned and operated by the farmowners who use them; they are not Government agencies. They do not lend Government funds and operate at no cost to the taxpayer.

--FLBs are basically agricultural mortgage lenders. However, limited home loan authority was voluntarily sought by the banks in recognition of a need for rural homeowners to have better access to mortgage credit. The scope of lending was aimed at middle-income owners with moderate-priced homes, and there was no intent to engage in subsidized or soft housing credit.

--Elected boards of directors of local FLBs establish credit standards and the scope of lending involvement.

The Board stated it would not object to being included under the broad mantle of "Federal housing support institutions" if certain editorial comments, which they furnished, were included in the report to help improve the communication to the reader. The Board believed the revisions were necessary to clearly identify the distinctions of structure and operation which set the FLBs apart from Government agencies.

We agree and have incorporated most of the Board's editorial comments in this report. We believe also that FLBs, while not a Government agency, do represent an opportunity to increase the supply of housing credit in rural areas.

Also, it should be noted that the FLBs are federally chartered institutions originally created by the Congress to meet a shortage of farm mortgage credit which in many ways parallels today's home mortgage credit problems. Just as agriculture has changed since the FLBs were created, so have the needs of rural residents.

The Farm Credit Act of 1971 designed a new charter for FLBs. The importance of home mortgage credit was recognized by the Congress which established that up to 15 percent of outstanding credit could be for nonfarm rural homes. Thus far, the FLBs have not made extensive use of this authority as discussed on page 41. The proposed Farm Credit Act Amendments of 1979, which would allow FLBs to make loans for more than 85 percent of the appraised value of farmland when these loans are guaranteed by FmHA, indicate further efforts to recognize the needs of nonfarm rural residents.

CHAPTER 5

OPPORTUNITIES FOR FmHA TO IMPROVE

THE OPERATIONS OF RURAL HOUSING PROGRAMS

FmHA can improve the effectiveness of its housing programs so that (1) families in remote areas, which have the highest incidence of substandard housing, can be better served and (2) a more equitable share of Federal housing support can be provided to rural areas. Specifically, the housing needs of moderate-income families have not been adequately met, housing resources have not been distributed to those most in need, available home repair programs have been underused, and few housing sites have been developed.

FmHA housing assistance can be improved by:

--Increasing home affordability for moderate-income families through the graduated-mortgage-payment plans, which have initial lower monthly payments than those required for FmHA nonsubsidized home loans.

--Targeting assistance within the States based on (1) the proportion of occupied substandard housing, (2) the proportion of rural population, and (3) per capita income. In addition, county level housing goals should be established to indicate work priorities needed to achieve program objectives.

--Making small private builders eligible for FmHA site development loans.

--Reaching out to locate families who need repair, rehabilitation, or homeownership programs. Through cooperative agreements, local public service organizations could assist FmHA.

HOMEOWNERSHIP FOR MODERATE-INCOME RURAL FAMILIES IS A GROWING PROBLEM

Home purchase is becoming more difficult for moderate-income rural families (those earning between $11,200 and $15,600) due to rapid escalation of home building costs. In some parts of the Nation, a significant gap exists between the maximum income needed by families to obtain an FmHA-subsidized loan and the minimum income needed to afford a modest home at the FmHA maximum interest rate. For example, to obtain an FmHA loan of $30,000 at the maximum interest rate of 8.75 percent, 1/a family would need an adjusted income of about $15,400; with interest subsidies an adjusted income between $7,200 and $11,200 is sufficient. Families earning between $11,200 and $15,400 face severe hardships in purchasing the home.

A similar problem existed for low-income families who could not afford a home loan at the lowest interest rate of 1 percent. However, in October 1979, legislation was enacted which authorized a Homeownership Assistance Program. This program is designed to make homeownership possible for rural families who otherwise cannot afford an FmHA interest credit loan. FmHA subsidizes costs of mortgage principal and interest, taxes, insurance, utilities, and maintenance which exceed 25 percent of adjusted income. The subsidy is adjusted periodically as the borrower's income changes. Also, the program requires recapture of subsidies if the home is sold for a profit. About 16,000 low-income families were expected to purchase homes under the program in the first year; however, at the time of our review, the Congress had not appropriated funds for the program.

Under the FmHA section 502 program, loans for homeownership are made to low-income families whose mortgage payments and ownership expenses do not exceed 20 percent of their adjusted income. To assist low-income families, loans can be made at interest rates as low as 1 percent. For moderate-income families, no specific income to homeownership expense ratio is used; however, home purchase price and costs of interest, taxes, and insurance are major factors determining the family income level needed for loan repayment.

FmHA recognized the problem faced by moderate-income families and, in May 1978, raised the maximum income limit for interest-credit home loans from $10,000 to $11,200. While this action eased the problem, it did not eliminate it. For example, in Maine a modest new home costs about $40,000. As a result, families with incomes of $11,200 to $15,600 face difficulty qualifying for a loan because mortgage and ownership expenses are excessive. In parts of Indiana and Kentucky, modest new homes cost about $30,000. Families with incomes over $15,200 can generally obtain FmHA financing, but those families with incomes between $11,200 and $15,200 face difficulty finding an affordable new home. In Alabama prices range between $23,000 and $28,000; thus, most moderate-income families could afford a home.

1/The maximum interest rate was increased to 10 percent in 1979.

Housing construction and operating costs for the same basic home differ throughout the Nation because the costs of land, land development, labor, utilities, and taxes vary. For example, real estate taxes for a modest new home in the Northeast approach $900 a year; in the South the taxes are about $250. Costs also vary because building methods differ. Homes in the North are usually constructed with basements because of the depth of the frostline, but in the South a crawl space is adequate.

The graph on page 51 illustrates the relationship between housing costs and income needed for mortgage repayment. Expenses were estimated as follows:

--An interest rate of 1 percent, the lowest possible rate, was used for interest-credit loans, and 8.75 percent was used for market rate loans.

--Repayment period was 33 years.

--Mortgage payment, interest, taxes, and insurance equal 20 percent of adjusted family income.

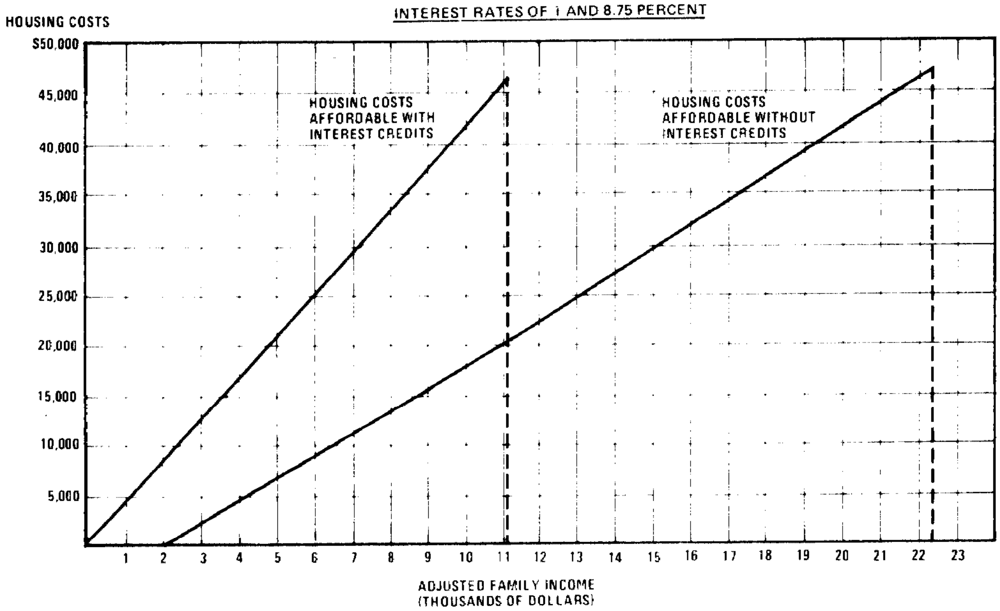
--Insurance and taxes were established at $1.23 for each $100 of value as used in the October 27, 1977, Department of Agriculture Housing Program Strategy Study.

As shown in the graph, with an interest-credit loan a family earning $11,200 can purchase a modest new home priced up to $47,000 if it has a good credit history and no unusually high debts. A family with an adjusted income of $15,600 is limited to a home costing $31,000. To afford a $47,000 home loan without interest credits, a family would need an adjusted annual income of $22,400. Thus, in high-cost areas moderate-income families can be precluded from purchasing a new home while low-income families are not.

FmHA could increase the affordability of homes for moderate-income rural families by adopting a graduated payments system for its loans. Under such a system, buyers' monthly payments start lower than those required under a regular home loan. Monthly payments increase over a number of years and then level out for the remaining repayment period. In effect, the buyer borrows extra money during the early years of the mortgage to reduce initial monthly payments. This additional loan is added to the outstanding mortgage balance and repaid by increasing payments in later years.

HUD insures graduated payment mortgages under its section 245 program. Five plans which are available to prospective homeowners differ in the following ways:

COMPARISON OF ANNUAL INCOME REQUIRED
TO PURCHASE A HOUSE AT FmHA
INTEREST RATES OF 1 AND 8.75 PERCENT



--The rate at which the monthly payments increase ranges from 2 to 7.5 percent per year.

--The number of years over which payments increase is either 5 or 10 years.

The graph on page 53 compares payments on a 30-year mortgage of $35,000 at an 8.75-percent interest rate under regular payment method with those required under one of HUD's graduated plans, where monthly mortgage payments increase 3 percent a year for 10 years before leveling out for the remainder of the repayment period.

A graduated mortgage is designed to assist prospective homeowners with insufficient incomes, but who expect their incomes to increase substantially over the next 5 to 10 years, to meet regular mortgage payments. At an FmHA market interest rate of 8.75 percent, a family needs an annual adjusted income of $15,200 or more to qualify for a $30,000 home loan; but under a graduated payment plan, a family with income of $13,450 could qualify to buy the same house. Increased affordability under a 3-percent, 10-year graduated payment plan is illustrated by the graph on page 54.

Graduated payment plans can contribute to homeownership assistance for moderate-income rural families because many FmHA loan applicants are young, newly formed families with reasonable expectation of increasing income.

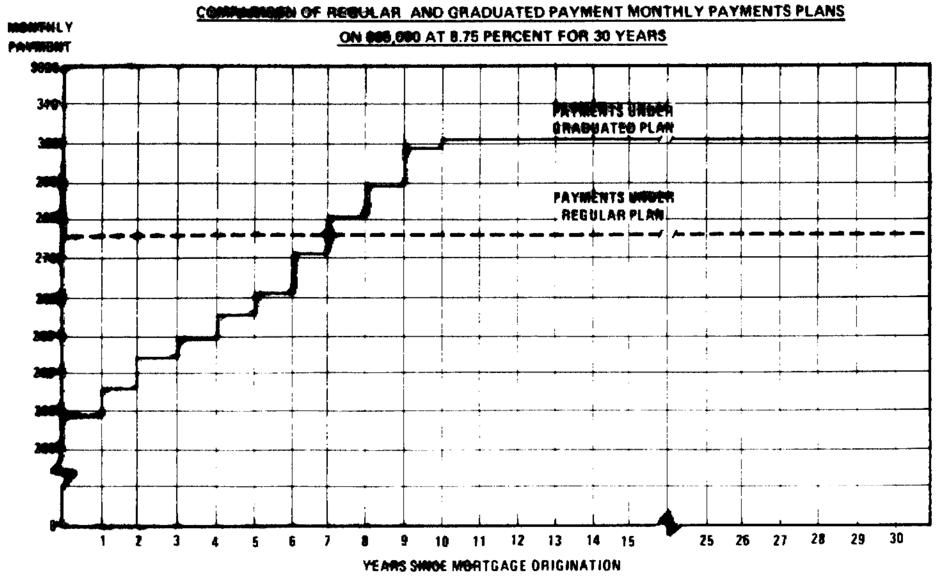
NEED TO BETTER TARGET HOUSING ASSISTANCE

If FmHA housing programs are to effectively reach needy families in remote areas, these families must be identified. A new FmHA strategy devised to better equate housing assistance to need may not be effective because it favors the more metropolitan areas while housing needs of families in remote areas are not adequately considered.

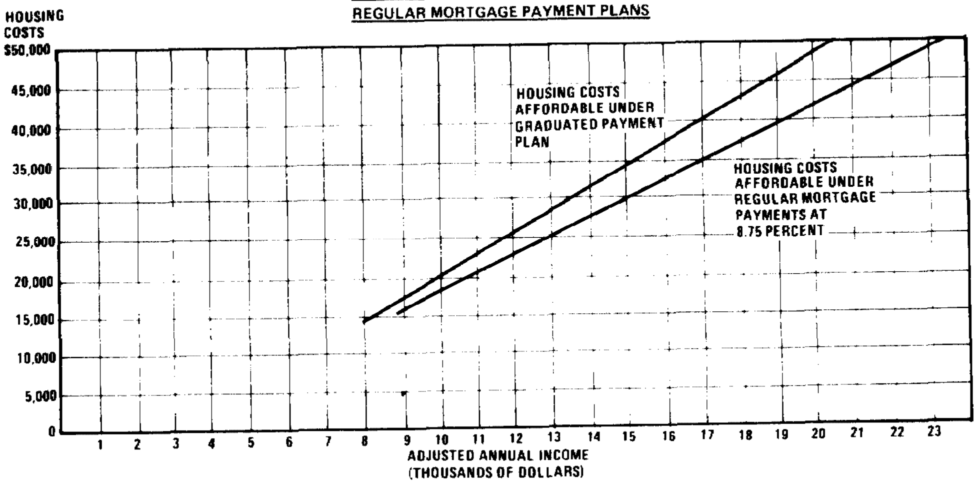
Beginning in fiscal year 1979, FmHA decided to target program resources within States to assist disadvantaged people and distressed communities by allocating housing funds primarily on the basis of need. Under the new policy, each State must develop a plan giving priority to the neediest families and most distressed communities. State plans are not expected to be completed until sometime in fiscal year 1980.

To help identify target areas, FmHA headquarters prepared an approach for use by the States which assigns a share of the housing funds to each county within a State based on equal weighting of rural population, per capita income, and the number of people in substandard housing. This approach, however, is not likely to result in a significant shift in the level of

COMPARISON OF REGULAR AND GRADUATED PAYMENT MONTHLY PAYMENTS PLANS
ON $65,000 AT 8.75 PERCENT FOR 30 YEARS



COMPARISON OF HOUSING COSTS AFFORDABLE UNDER GRADUATED AND REGULAR MORTGAGE PAYMENT PLANS



assistance previously provided to outlying areas. The following table compares, for two States, allocations previously made to those that can be expected under the new approach.

County type	Kentucky Actual allocation FY 1977	Kentucky Expected allocation FY 1979	North Carolina Actual allocation FY 1977	North Carolina Expected allocation FY 1979
	(percent)			
Metropolitan	13.8	14.2	20	23.6
Rural--adjacent to metropolitan	29.0	26.8	45	39.1
Rural--remote	57.2	59.0	35	37.3
Total	100.0	100.0	100	100.0

As shown in the table, little increase in funding for remote rural areas can be expected under the new approach.

The use of absolute numbers to measure population and occupants of substandard housing favors more densely populated metropolitan and adjacent counties. The measure of per capita income favors remote rural counties. Since all three factors are weighted equally, metropolitan and adjacent counties are likely to be apportioned a large share of assistance. To target a greater share of program funding to outlying counties, different index factors or weighting is needed. For example, the percentage rather than the number of families in substandard housing could be used.

Targeting of funds to outlying areas does not guarantee that rural families will be adequately assisted. Actual needs and desires of families must be considered to deliver needed program assistance to them. A thorough understanding and evaluation of area housing conditions and family needs, however, are often not available. According to State housing officials, recent housing studies made in conjunction with local housing plans are often superficial, outdated, and incomplete because they are prepared by regional planning agencies or consulting firms with limited financing and staff.

The delivery of adequate FmHA assistance to outlying families depends on (1) identifying eligible families through outreach, (2) assessing family needs for housing repair, rehabilitation, or ownership programs, (3) establishing county-level housing goals to meet assessed needs, and (4) measuring success by attainment of housing goals established.

MORE EMPHASIS NEEDED ON HOUSING REPAIR AND REHABILITATION

FmHA needs to emphasize its housing repair and rehabilitation programs to help preserve housing stock and eliminate conditions affecting the safety or health of rural families. About 4.4 million owner-occupied rural housing units have one or more structural deficiencies, and 900,000 of these units are substandard. An estimated 3.4 million of the units are occupied by low- and moderate-income families. Despite the magnitude of the problem, funds available under the FmHA section 504 emergency repair program were underused. Few home improvement loans were made under the section 502 program because, according to FmHA, such loans require an inordinate amount of the county supervisor's time to identify needy families and explain the programs.

About half the funds available for the section 504 repair program between 1974 and 1978 went unused even though there were many potential applicants. Under this program, 20-year loans at a 1-percent interest rate were available to very low-income or elderly owner-occupants to eliminate health or safety hazards. These repairs were not necessarily all those required to bring the home up to standard condition.

We estimate that during 1975 about 568,000 rural families were potential beneficiaries of the section 504 program because they (1) occupied substandard housing and (2) had incomes of less than $5,000 a year. Yet, less than half the funds available during fiscal years 1974-78 were obligated. However, FmHA officials stated that the 504 program was receiving more emphasis at this time.

Repair Loans Under Section 504

Fiscal year	Funds Available	Funds Obligated	Percent unobligated	Number of loans
	(000 omitted)			
1974	$10,000	$ 4,430	55.7	2,635
1975	20,000	4,816	75.9	2,554
1976	25,000	8,289	66.8	3,799
1977	15,000	7,886	47.4	3,505
1978	14,970	11,941	20.2	4,823
Total	$84,970	$37,362	56.0	17,316

Beginning in fiscal year 1977, repair grants were made available under section 504 to elderly persons who could not afford to repay loans even at the 1-percent interest rate. Appropriations totaling $14 million for 5,598 grants were fully expended in fiscal years 1977 and 1978.

FmHA officials told us that the section 504 program formerly was not emphasized because county supervisors did not have time to identify potential beneficiaries and explain the program. We noted, however, that the program was particularly adaptable to cooperative agreements with local public service organizations having daily contact with needy families. For example, in Maine FmHA entered into a cooperative agreement with the Maine Human Services Council to identify and assist potential section 504 applicants. The council provided 13 technicians to locate eligible families, explain available programs, and help complete FmHA applications. In other States visited, few county supervisors had agreements with service organizations to publicize the programs.

The following table compares the use of loan funds in Maine with that of the Nation. Usage in excess of the State allocation is possible because FmHA's national office redistributes unused funds.

Fiscal year	Percent of allocation used	
	Maine	Nation
1976	97.6	33.2
1977	67.0	52.6
1978	221.1	79.8

Repair loans were also available under FmHA's section 502 program, but, according to FmHA officials, few were made. Under this program loans with interest rates as low as 1 percent are available to lower income families. The loans were limited to $7,000, 1/ with a maximum repayment period of 25 years. For families who could afford the FmHA market interest rate, repair loans had no maximum amount but were effectively limited by the requirements that the home be modest in design, size, and cost. All loans made under section 502 must be used for repairs to bring the homes up to standard condition.

In 1974 FmHA revised its policy to place stronger emphasis on assisting families of greatest need. An objective established that 40 percent of the section 502 loans would be for purchase or repair of older homes. For fiscal years 1976-78 an additional objective required 10 percent of the loans to be for repair only. Information was not available to determine how many older homes were purchased and repaired; however, the repair objective was not met, as shown in the following table.

1/FmHA is currently revising the 502 incentive repair program to permit loans up to $9,000. The regular 502 repair program will be available at 1 percent and has no dollar limit.

Fiscal year	Number of section 502 loans for repair	Repair loans as percent of all section 502 loans
1976	2,555	1.8
1977	2,035	1.7
1978	2,302	2.1

Although a national objective established that 50 percent of program funds would be used for purchase or repair of older homes, this objective was not divided into county-level goals. Therefore, county officials placed little emphasis on achieving this objective. The practice of allocating 50 percent of funds for purchase and repair of older homes is no longer an administrative goal.

NEED TO INCREASE THE DEVELOPMENT OF BUILDING SITES

Homes for low- and moderate-income families are not being built in some rural areas because of a shortage of affordable building sites. The FmHA program, which makes loans to develop affordable sites, including water and sewer lines, has not developed many sites, and appropriations for fiscal years 1974 through 1978 were consistently underused. Appropriations for fiscal years 1979 and 1980 were reduced below the prior levels but fully obligated. Appropriations were consistently underused because

--nonprofit organizations, which are eligible for assistance, lacked the expertise or willingness to develop sites and

--profit-oriented builders, which have the expertise, are not eligible for program assistance.

A major component of the increase in the price of modest housing is the cost of land and its development. In some areas, land prices rose two to four times more rapidly than home prices and accounted for about 25 percent of building costs.

Some land in remote areas is not level and can be used for housing only after extensive development. For example, only a small amount of land in Appalachia has less than a 15-percent slope, and level land is either precariously situated in a flood plain or prohibitively expensive. Costs of $15,000 to $20,000 are not uncommon for a developed lot in such areas. When housing prices are set to cover land and development costs, homes are beyond the financial reach of most low- and moderate-income families.

Inadequate rural water and sewer facilities are also problems hindering large-scale site development. For example, in Kentucky and Indiana some counties and towns have no public systems while others are being used to capacity. In the Penobscot Valley Regional Planning District in Maine, virtually all land with water and sewer service has been developed. Alternatives to public systems, such as private wells and septic tanks, are costly and often unacceptable because of soil conditions. The installation of utilities is often beyond the financial ability of either private developers or local communities.

FmHA site development loans are required by law to be made to nonprofit organizations at 3 percent interest for self-help groups and at FmHA's maximum rate for sites sold to low- and moderate-income families. The following table compares the funds available and obligated in the past 7 fiscal years under this program.

Fiscal year	Funds Available	Funds Obligated	Percent unobligated
	(000 omitted)		
1974	$ 5,900	$ 1,837	68.9
1975	3,900	2,347	39.8
1976	5,383	1,190	77.9
1977	4,125	2,099	49.1
1978	4,394	2,923	33.5
1979	3,000	3,000	0.0
1980	1,000	1,000	0.0
	$27,702	$14,396	48.0

Based on our discussions with FmHA officials, we believe that the lack of program demand and reduction in funds available were not indicative of need but rather of a shortage of nonprofit organizations with the expertise and willingness to develop sites. On the other hand, many small private builders, which cannot participate in this program, had the expertise but lacked the capital or credit.

According to FmHA State and county officials, site development by small private rural builders would increase if credit was available. Also, low-interest-rate loans to private builders could help reduce building costs.

CONCLUSIONS

FmHA has not effectively delivered housing assistance to remote areas with the highest level of substandard housing. Program support was provided primarily on demand, and little has been done to promote available programs. Builders and realtors in more urban areas were relied upon to provide clientele and distribute assistance geographically.

Moderate-income rural families, as well as low-income families, face increasing difficulty obtaining a single-family home due to rapid escalation of homebuilding costs. Young, newly formed families are often most affected because they have not accumulated enough savings to make a substantial downpayment.

Uneven topography and inadequate water and sewer facilities make development of housing sites in remote areas at best expensive and sometimes impossible. As a result, few new homes affordable by low- and moderate-income families are built.

FmHA funds to purchase and develop housing sites for low-income families are underused. Loans, by law, are available only to nonprofit organizations, few of which have the expertise or willingness to develop housing sites. Private builders, which have the expertise, lack capital or credit. A viable method to increase development of rural housing sites for low- and moderate-income families is to make small private builders eligible for FmHA site development loans.

Opportunities for FmHA to improve the effectiveness of its rural housing programs include:

--Increasing home affordability for moderate-income families through graduated mortgage payment plans.

--Distributing a greater share of assistance to disadvantaged families and distressed communities by better targeting of housing funds within States.

--Preserving more housing and eliminating conditions affecting safety or health by placing greater emphasis on housing repair and rehabilitation.

--Increasing the number of affordable housing sites for low- and moderate-income families by making site development loans to small private builders.

RECOMMENDATIONS TO THE SECRETARY OF AGRICULTURE

We recommend that to provide greater homeownership opportunities for moderate-income rural families and increase the availability of affordable homebuilding sites, the Secretary direct the FmHA Administrator to:

--Test graduated loan repayment plans for moderate-income families, thereby reducing monthly payments made in the early years of the loan. Upon conclusion of the test, determine whether to implement the plans nationwide.

--Propose to the Congress legislation to amend section 524 of the Housing Act of 1949 to allow small, profit-oriented builders to participate in FmHA's rural site development program.

We recommend that to better target and distribute housing assistance to families most in need, the Secretary also direct the FmHA Administrator to require:

--Field offices to develop county-level plans which target housing resources to outlying areas with the greatest need. The plans should specify goals and objectives for each housing program and emphasize matching the type of assistance to family need.

--County offices to reach out to remote areas to identify families with great needs and explain how FmHA programs can help. County offices could negotiate cooperative agreements with community service organizations for outreach assistance.

--Housing program results to be compared with planned goals.

AGENCY COMMENTS AND OUR EVALUATION

The Department of Agriculture generally agreed with our recommendations or stated they would give them careful study.

Concerning our recommendation to test graduated loan repayment plans for moderate-income families, the Department stated it will take the recommendation under advisement. It said such plans require careful study because the proposed graduated payment method will exceed the level payments method after 6 years, and that fact could lead to loan-servicing problems since expenses are increasing more rapidly than income.

HUD had insured about 117,000 units under five different graduated payment plans as of July 1979. It should be noted, however, that they are intended only to facilitate early homeownership for families that expect their incomes to rise substantially over the next few years. Careful evaluation of loan applicants is required to ensure that such plans are used by eligible families with such income expectations. Many FmHA applicants are young, newly formed households with reasonable expectations of rising incomes, and graduated payment plans could assist in early homeownership for many of them.

It should also be noted that the graduated loan repayment plan referred to by FmHA is only one of several currently used by HUD. As discussed on pages 50 and 52, other plans offer different terms altering the period when the amount of payment increases.

In response to our recommendation that the Department propose to the Congress legislation allowing participation by small profit-oriented builders in FmHA's site development program, it said that previous efforts to include private enterprises as eligible applicants were not successful. The Department also stated that building site loan demand has grown tremendously in the last 2 years, and demand exceeds appropriations for fiscal years 1980 and 1981. Also, FmHA officials told us that they plan to ask for $7 million for this program for fiscal year 1981.

Although we agree that examples of well-organized and effective site development projects sponsored by nonprofit groups can be found, we continue to believe that it is unlikely that nonprofit groups can effectively use large amounts of funds for building sites in remote areas and that another effort to include private enterprise should be made.

In response to our recommendation to develop county-level plans which target housing resources to the areas of greatest need, the Department stated it was currently completing State management plans which outline areas of need and assistance. These plans will be used by FmHA district offices, which are aligned with most substate planning districts, in determining housing needs. It said the district offices are assisting county offices to develop work plans but are concerned that county plans are premature, if at all practical.

FmHA has, from time to time, adopted various national goals intended to better distribute housing support to the areas of greatest need. For the most part, these efforts have had little impact on county-level work priorities. We believe specific objectives on targeting housing resources to the outlying areas with the greatest need are needed at the county level to encourage and measure success of the various programs and to indicate areas where additional management attention is required.

In commenting on our recommendation that county offices reach out to remote areas to identify families with great needs, the Department stated it agreed further outreach was needed. It said, however, that most county offices are not properly staffed to carry out such a function.

We agree that many FmHA county offices are not staffed to carry out extensive outreach services. As pointed out on page 57, however, we believe many opportunities exist for FmHA county personnel to obtain outreach services from other public and private organizations in the counties. The first step should be maximum use of cooperative agreements with these groups, which generally place fewer administrative demands on FmHA personnel than inhouse efforts.

The Department also suggested a number of editorial changes in our draft report, most of which have been incorporated in this report.

SPONSORS

gency

Nonprofit	Co-operative	Political Subdivision		UNIQUE CHARACTERISTICS
				Can not own adequate housing or get reasonable credit elsewhere
				Owner must occupy unit
				Only to the elderly
X	X	X		
X		X		Not to exceed 90 percent of costs
X	X			50 years to repay on Senior Citizen projects
X		X		Land and housing costs not eligible
X				3 percent interest on direct loans for self-help sites
				For outlying areas
				Anyone displaced by Urban Renewal qualifies for special terms
	X			Anyone displaced by Urban Renewal given preference
				90 percent financing of limited-profit sponsors
	X			Program suspended as of 1/5/73
	X			
				Annual grants to retire mortgage debts of local housing authorities

DESCRIPTION OF FmHA HOUSING PROGRAMS

SECTION 502 PROGRAM

The Housing Act of 1949, and subsequent amendments, authorized direct loans for modest-sized homes under section 502 (42 U.S.C. 1471) to low- and moderate-income families who cannot acquire reasonable commercial financing.

Section 502 is FmHA's basic homeownership program under which loans are made to build or purchase homes or to rehabilitate owner-occupied dwellings. The Housing and Urban Development Act of 1968 added the interest-credit provision which allows an interest rate as low as 1 percent to low-income families. As of May 1978 the maximum income eligibility limit for interest credit was $11,200 per year (higher in Alaska, Hawaii, and Guam).

The Rural Development Act of 1972 authorized loan guarantees. Currently, families with incomes between $15,600 and $20,000 (higher in Alaska, Hawaii, and Guam) are eligible.

Between 1950 and 1977, FmHA made 1,150,223 single-family housing loans totaling about $16.8 billion.

SECTION 504 PROGRAM

The Housing Act of 1949 authorized direct loans and grants to very-low-income families and the elderly for eliminating safety or health hazards under section 504 (42 U.S.C. 1474).

Section 504 loans are made to install plumbing, kitchen facilities, screens, storm windows, and insulation or to improve housing quality. Loans carry a 1-percent interest rate for up to 20 years. The maximum loan amount is $5,000. Grants are made to the very-low-income elderly who do not have the repayment ability to obtain loans.

By the end of fiscal year 1977, FmHA had made 45,921 loans and 11,746 grants totaling about $75.1 million.

SECTION 515 PROGRAM

The Housing Act of 1949 and subsequent amendments authorized loans to finance rental housing for low- and moderate-income families and persons 62 or older.

Under section 515 (42 U.S.C. 1485), loans are made for the amount of development costs or the project's security value, whichever is less, up to a maximum of $1,500,000. The maximum repayment period is 50 years. Profit-oriented borrowers must pay FmHA's maximum interest rate; nonprofit or limited-profit sponsors can qualify for interest credit. Loans are also made to rural cooperatives to develop rental housing.

Through fiscal year 1977, FmHA made 8,041 loans totaling about $1.75 billion for projects containing 117,633 rental units.

SECTIONS 523 AND 524 PROGRAMS

The Housing Act of 1949, as amended by the Housing and Urban Development Act of 1968, authorized short-term housing site development loans to nonprofit organizations for the benefit of low- and moderate-income families.

Under section 523 (42 U.S.C. 1490c), 2-year loans to a maximum of $100,000 are made to develop sites to be used for self-help projects and may carry a 3-percent interest rate.

Technical assistance for self-help is authorized under section 523 (42 U.S.C. 1490c) for those families providing a major portion of the labor to construct their homes. Mortgage funds, including interest credits, are available under the section 502 program. Grants are also available to public and private nonprofit groups for organizing and assisting families using the self-help approach. The grants can be used to purchase equipment, train family members, and hire construction supervisors.

Under section 524 (42 U.S.C. 1490d), loans at FmHA's maximum interest rate are made to nonprofit organizations, public agencies, and cooperatives for developing sites to be sold to low- and moderate-income families.

From 1970 through 1977, FmHA made 110 site development loans amounting to about $12 million. In addition, 156 self-help technical assistance grants were made for about $27 million.

DESCRIPTION OF HUD's MAJOR

HOUSING ASSISTANCE PROGRAMS

SECTIONS 203(b) and (i) PROGRAMS

The National Housing Act of 1934 authorized one- to four-family home mortgage insurance under sections 203(b) and (i) (12 U.S.C. 1709) to encourage capital investment in the home mortgage market. Commercial lenders are insured against loss for up to 97 percent of the property value and for terms of up to 30 years. The loans may finance homes in both urban and rural areas, except farm homes. Less rigid construction standards are permitted in rural areas. The interest rate is based on HUD's current market rate.

By September 30, 1977, about 10 million units had been insured for about $125 billion under section 203(b). An additional 80,000 units had been insured in remote areas for $600 million under section 203(i).

SECTION 235 PROGRAM

The Housing and Urban Development Act of 1968 amended the National Housing Act by adding section 235 (12 U.S.C. 1715z), which authorized mortgage insurance and interest subsidy for low- and moderate-income home buyers. Families with adjusted incomes of less than 95 percent of the area median income are eligible to purchase new or substantially rehabilitated single-family housing.

Monthly payments by HUD to the lender reduce interest costs to as low as 4 percent if the homeowner cannot afford a market-rate mortgage. The homeowner must contribute 20 percent of adjusted income to monthly mortgage payments and must make a downpayment of 3 percent of the purchase price. The mortgage limit is $32,000, except in high-cost areas where it is $38,000. The limits are increased to $38,000 and $44,000 when the home is for five or more persons. As of September 1977, about 487,000 units had been insured for $8.6 billion.

SECTION 221(d)(2) PROGRAM

The Housing Act of 1954 amended the National Housing Act by adding section 221(d)(2) (12 U.S.C. 1715l), which authorized mortgage insurance to increase homeownership opportunities for low- and moderate-income families, especially those displaced by urban renewal. Lenders are insured against loss on loans to finance the purchase, construction, or rehabilitation of low-cost, one- to four-family housing. Maximum insurable loans range from $31,000 to $42,000 for single-family homes with higher limits for two- to four-family housing. Through September 1977 about 837,000 units had been insured for about $11 billion.

SECTION 207 PROGRAM

The National Housing Act of 1934, as amended, authorized the insurance of mortgages under section 207 (12 U.S.C. 1713) to facilitate the production of good quality housing that would serve the needs of a broad cross section of the rental housing market at reasonable rents.

The section 207 program is HUD's basic nonsubsidized rental housing program under which the agency insures privately financed mortgage loans for constructing and/or rehabilitating economically sound multifamily rental projects. Eligible mortgagors include investors, builders, developers, and others who meet HUD requirements. The maximum insured loan amount, in most cases, is limited to 90 percent of the project's estimated value. Through June 1977 about 283,000 units had been insured for $3.9 billion.

SECTION 221(d)(3) AND SECTION 221(d)(4) PROGRAMS

The Housing Act of 1954 amended the National Housing Act by adding the section 221 (12 U.S.C. 1715(l)) program designed to meet the needs of low- and moderate-income families, as well as families displaced by urban renewal or government action.

Under these programs HUD is authorized to insure loans to construct or substantially rehabilitate multifamily rental or cooperative housing projects. Currently, the principal differences between the two programs are that:

--HUD insures 100 percent of project value under section 221(d)(3) but only 90 percent under 221(d)(4).

--Nonprofit, limited-dividend, or cooperative organizations may qualify for the 221(d)(3) program while 221(d)(4) mortgages are reserved for profit-oriented sponsors.

Formerly, projects financed under section 221(d)(3) could qualify for below-market interest rates (as low as 3 percent) and for rent supplements. These Federal payments reduced rents for disadvantaged low-income persons. Below market interest rates and rent supplements are no longer available for new projects insured under these programs. The rent supplement program was suspended under the housing subsidy moratorium of January 5, 1973. Units financed under both programs now qualify for assistance under the section 8 program, currently the major Federal program to subsidize the rent of lower income families.

Through June 1977 the section 221(d)(3) program had insured 132,858 units for about $1.8 billion and section 221(d)(4) program had insured 381,731 units for about $4.7 billion.

SECTION 236 PROGRAM

The Housing and Urban Development Act of 1968 (42 U.S.C. 1441a) amended the National Housing Act by adding the section 236 (12 U.S.C. 1715z-1) program to provide low- and moderate-income multifamily rental housing units.

HUD was authorized to insure privately financed mortgage loans to construct or substantially rehabilitate multifamily housing projects and to pay, on behalf of the mortgagors, the mortgage insurance premiums and interest over 1 percent on the mortgage loans.

On January 5, 1973, HUD suspended the section 236 program; however, considerable expenditures under the program will continue for many years because many units are already in operation. HUD estimates that interest reduction payments on existing projects could amount to about $10.3 billion over the remaining lives of these project mortgages. Beginning in 1974 HUD paid additional subsidies to cover the difference between tenant contributions and project operating costs. Cumulative activity through June 1977 was about 460,000 units insured for $7.9 billion.

SECTION 202 PROGRAM

The Housing Act of 1959 authorized direct loans under section 202 (12 U.S.C. 1701q) to provide housing and related facilities for the elderly or handicapped. Long-term loans are made to finance private, nonprofit sponsors of rental or cooperative housing. Until the program was revised in 1974, the interest rate was 3 percent. The current rate is based on the average rate paid on Federal obligations during the preceding fiscal year. Also, a minimum of 20 percent of the units in a project must be reserved for households participating in the section 8 rental assistance program.

Mortgage insurance for similar housing is available under section 231 (12 U.S.C. 1715v). Through fiscal year 1977 about 97,000 units had been approved under section 202 for about \$2.2 billion, and through June 1977 about 53,000 units had been insured under section 231 for about \$783 million.

SECTION 8 PROGRAM

The Housing and Community Development Act of 1974 (42 U.S.C. 1437f) amended the Housing Act of 1937 (42 U.S.C. 1401) and added, under section 8, a new lower income housing assistance program. Section 8 provides financial assistance to lower income families, enabling them to lease existing, newly constructed, or substantially rehabilitated housing.

Under section 8, HUD makes payments under annual contribution contracts to public housing agencies that assist in developing or operating housing for lower income families. Also, HUD contracts directly with owners who lease housing units to eligible families.

Program eligibility depends on family size and income compared with the median income in the area. Lower income families pay between 15 and 25 percent of their incomes for rent. At least 30 percent of the assisted units are to be initially occupied by very-low-income families. The Federal subsidy is equal to the difference between contract rent, including utilities, and the amount an eligible family can afford.

As of September 30, 1977, about 946,000 units have been approved for Federal subsidy, but only 295,000 were occupied.

LOW-INCOME PUBLIC HOUSING

The Housing Act of 1937 (42 U.S.C. 1437 *et seq.*), amended by the Housing and Community Development Act of 1974 (42 U.S.C. 5301 *et seq.*), authorized Federal aid for public housing agencies (PHAs).

PHAs are established by local governments to build, acquire, manage, or lease housing units for low-income residents. HUD furnishes technical and professional assistance to plan, develop, and manage the projects and makes loans for project planning and annual contributions for debt service of PHA obligations. Operating subsidies are also made to help cover maintenance and operating costs.

As of June 30, 1977, about 1 million rental units were available, and another 61,346 were under construction or rehabilitation.

SECTION 245 PROGRAM

Under section 245 of the National Housing Act of 1934, as added by section 308 of the Housing and Community Development Act of 1974 (12 U.S.C. 1715Z-10), HUD insures mortgages to facilitate early homeownership for families that expect their incomes to rise substantially over the next few years. These graduated payment mortgages allow homeowners to make smaller payments in the early years and gradually increase the size of payments in later years. Five different payment plans are available, varying in duration and rate of increase. As of July 1979 about 117,000 units had been insured.

DESCRIPTION OF VA HOUSING PROGRAMS

GUARANTEE LOAN PROGRAM

The Servicemen's Readjustment Act of 1944 (38 U.S.C. 1801 et seq.) authorized the guarantee of home mortgages to help veterans finance reasonably priced homes. VA guarantees loans made by private lenders at an established VA interest rate for up to 30 years and 32 days. The guarantee is limited to 60 percent of the mortgage, up to a maximum of $25,000. The veteran must be able to afford the loan at the stated terms.

Through December 1977 about 9.7 million loans totaling $71.3 billion had been guaranteed.

DIRECT LOAN PROGRAM

The Housing Act of 1950 (38 U.S.C. 1811) authorized direct home loans to veterans. Loans for a maximum of $33,000 for up to 30 years and 32 days at the VA-established interest rate are made to veterans in areas where guaranteed private loan financing is not available. By the end of 1977, VA had made 328,865 direct loans totaling about $3.3 billion.

APPENDIX V

Office of the
Administrator
of Veterans Affairs

Washington, D.C. 20420

Veterans
Administration

OCTOBER 25 1979

SERVING THE VETERAN FOR FIFTY YEARS 1930 1980 VETERANS ADMINISTRATION

Mr. Gregory J. Ahart
Director, Human Resources Division
U. S. General Accounting Office
Washington, DC 20548

Dear Mr. Ahart:

Your September 27, 1979 draft report, "Ways A More Equitable Share of Federal Housing Support Can Be Provided To Rural Areas," has been reviewed by my staff and we found that it adequately describes our guaranteed and direct home loan programs. We were pleased to note that you found the Veterans Administration's (VA) housing operations in rural areas are well administered, that support is consistent with the geographic distribution of the veteran population, the VA's referral system largely eliminates the need for make direct loans, and that the Farmers Home Administration would benefit by operating a system similar to ours.

We appreciate the opportunity to review this report.

Sincerely,

MAX CLELAND
Administrator

Farm Credit Administration

490 L'Enfant Plaza
Suite 4000
Washington DC 20578
(202) 755-2195

October 12, 1979

Mr. Henry Eschwege, Director
U. S. General Accounting Office
Washington, DC 20548

Dear Mr. Eschwege:

The proposed draft of the GAO report entitled, "Ways a More Equitable Share of Federal Housing Support Can Be Provided to Rural Areas," was reviewed with the Federal Farm Credit Board at its meeting the past week. The Board had several observations which are presented herewith.

Considering that the Federal land banks are not Government agencies, are cooperative lending institutions owned and operated by the farm owners who use them, do no loan government funds and operate at no cost to the taxpayer, it was the view of the Board that it is out of character to include FLBs under the broad mantle of "Federal Housing Support" institutions. Although deemed inconsistent to do so, the Board would not object to this blanket reporting provided each of the sections of the report referencing the FLBs clearly identifies the distinctions of structure and operation which sets the FLBs completely apart from the agencies.

There are several significant characteristics in the FLB rural home lending authority which the Board wishes to emphasize. The FLBs are basically agricultural mortgage lenders. In recognition of a need at times in some parts of the country for rural home owners to have better access to mortgage credit, the FLBs voluntarily sought limited authority in 1971 to make rural home loans. The scope of lending was deliberately aimed at middle-income owners with moderate priced homes. The intent was to maintain a quality of housing loan comparable to that of FLB agricultural mortgage loans. There was no intent that the FLB would engage in subsidized or soft housing credit. Thus, the analyses made in the GAO review and the conclusions reached are less pertinent when caste in this environment.

Administratively, there are also some significant features about the FLBs which must be recognized. The farmer user-owners take great pride in their having achieved self-sufficient, government free status. This was recognized by Congress in the Farm Credit Act of 1971 and the Farm Credit Administration was directed to encourage farmer-rancher-borrower participation in the management, control, and ownership of a permanent

APPENDIX VI

system of credit for agriculture (Sections 1.1 and 1.2 of the Farm Credit Act of 1971). Because the FLBs are basically agricultural mortgage lenders and since the rural home lending authority was sought as an accommodation lending, the utilization of the authority is optional with the associations and the banks. The elected boards of directors of those institutions make this determination, establish the credit standards and the scope of involvement desired. This again places GAO analyses and conclusions at some odds with the actual posture of the FLBs.

In consideration of the above, the Federal Farm Credit Board has reservations as to whether the FLBs can be equitably included in the report since their structure, management, lending objectives and independence from Government are totally different from the agencies around which the substance of the report is developed. Should you elect to include the FLBs in the report, we have enclosed editorial comments which we believe would help you to improve the communication to the reader.

In any event, the Board will give your recommendations due consideration. Rural home lending will be given positive Federal Board direction within the scope and intent of the authority as structured. The legislation recently recommended to Congress by the Board includes a raising of the 85 percent lending limit with respect to loans supported by Government guarantee. If passed by Congress, this would apply to rural home loans as well as agricultural loans. However, the peculiar posture of rural home lending in the FLBs and the adamant posture of the user/owners against engaging in soft credit present immediate limitations to an extensive use of that authority in the rural housing area.

It is hoped the foregoing will assist in getting the FLB rural home lending operations in a better perspective. The opportunity to review the draft is appreciated and if we can be of further assistance, please contact us.

Sincerely,

Donald E. Wilkinson

Donald E. Wilkinson
Governor

Enclosure

DEPARTMENT OF AGRICULTURE
OFFICE OF THE SECRETARY
WASHINGTON, D.C. 20250

19 NOV 1979

Mr. Henry Eschwege
Director, Community and
Economic Development Division
U. S. General Accounting Office
Washington, DC 20548

Dear Mr. Eschwege:

The General Accounting Office in Draft Report entitled "Ways A More Equitable Share of Federal Housing Support Can Be Provided to Rural Areas" made recommendations on pages 63 and 85 that the Secretary of Agriculture direct the Farmers Home Administration (FmHA) to place special emphasis on some existing loan programs and outreach activities. These are addressed along with comments to enhance the report.

Specifically, GAO recommends that the Secretary of Agriculture direct Farmers Home Administration to:

1. Establish a loan referral or clearinghouse procedure through the guarantee program for families in outlying areas who are unable to obtain local loans even with a FmHA guarantee. Loan applications should be referred to urban mortgage companies or financial institutions willing to make loans.

We concur additional mortgage funds need to be attracted to rural areas. However, we feel efforts should be expanded to encourage rural lenders to participate in the secondary market. This permits rural borrowers to obtain credit within a reasonable distance of their residences. The location of the lender is essential during loan making and servicing, as are the efforts to attract more mortgage funds to rural areas.

2. Revise the guarantee loan program to permit variable interest rate loans needed to obtain home loans from Federal Land Banks.

We concur with this recommendation. Currently, a variable interest rate for the guaranteed rural housing loan program is being considered. We believe it will not attract much additional investment capital, as secondary money markets primarily use fixed interest rate instruments. It will facilitate participation in Federal Land Bank Housing loan program.

3. Test graduated loan repayment plans for moderate income families which reduces the monthly payments made in the early years of the loan. Upon conclusion of the test determine whether to implement the plans on a nationwide basis.

We will take this recommendation under advisement. The proposed graduated payment method indicates payments will exceed the level payment method after 6 years. This could lead to massive servicing problems as expenses are increasing more rapidly than incomes. This plan requires careful study.

4. Propose to the Congress legislation to amend Section 524 of the Housing Act of 1949 to allow participation by small profit-oriented builders in FmHA's rural site development program.

The building site loan program has grown tremendously in the last two years to where extreme demand exceeds appropriations and personnel for Fiscal Years 1980 and 1981. Also, efforts to change the law have been initiated to include private enterprises as eligible applicants but failed.

5. Field offices to develop county level plans which target housing resources to the outlying areas with the greatest need. The plans should contain specific goals and objectives for each housing program and emphasize matching the type of assistance to family need.

We are currently completing State Management plans which outline the areas of need and assistance needed. These plans will be used by the District Offices, which are aligned with most sub-state planning districts, in determining housing needs. District Offices are assisting county offices develop work plans. Any county plans are probably premature, if at all practical.

6. County offices to perform outreach in the outlying areas to identify families with great needs and explain how FmHA programs can be of assistance. In this effort, county offices could negotiate cooperative agreements with community service organizations for outreach assistance.

We agree further outreach is needed. However, we believe most county offices are not properly staffed to carry out such a function. Currently, close coordination of FmHA programs with state and sub-state planners is underway to identify and develop financial needs of each community.

FmHA offers the following comments to improve the report:

1. Page ii -- The location of FmHA financed housing in urban and adjacent counties is in some measure attributed to the legislated authority in the Housing and Development Act of 1974. Also, the distribution of the population and substandard housing should be considered.

2. Page iii -- Shortage of mortgage credit can be related to appropriation levels agreed upon by the Executive and Legislative Branches.

3. Pages iv, 65 -- Several places throughout the report it is indicated that households in the $11,200 to $15,600 income group have difficulty in purchasing houses. This is true but it should not be directed to FmHA loan activity, as all of our appropriated loan funds in the $11,200 to $15,600 adjusted income levels have always been used. More analysis and information is required to address this situation in smaller income increments. The gap of affordability widens above $11,200 each year, thus indicating a real need for interest subsidy.

4. Pages v, 65 -- Targeting through the reallocation of funds among states drastically affected some states in Fiscal Year 1979. The second phase of reallocation within states will further involve priorities currently being developed.

5. Page v -- Housing repair and rehabilitation program will be increased through more fully utilizing the 504 program. However, emphasizing these programs at the sacrifice of maintaining a high level of new construction through the 502 program will result in the long run in a shortage of housing. Also, this will tend to drive up the price of existing housing beyond the reach of FmHA clientele.

6. Page 2 -- A rural definition that corresponded to FmHA's would be helpful in analyzing and implementing the results.

7. Pages 11, 28, 29 -- Implying FmHA is responsible for meeting only 50 percent of the 1968 - 1978 goal is misleading. In actuality, FmHA has obligated 92.4% of its housing appropriations during this period. Some programs have exceeded appropriations, as shown in Table 1. Recently, the guaranteed program has limited complete obligation of 502 appropriations while the demand for insured 502 loans far exceeds available funds. Thus, achievement of the goal was more likely directly affected by the amount of funds appropriated.

8. Page 18 -- It should be shown that 62.5 percent of the non-metro substandard housing is inhabited by families with less than $5,000 incomes. Thus, a program alternate other than the 502 subsidized program (i.e., HOAP) is needed to assist these families.

9. Page 31 -- "According to USDA, 2 1/2 times family income is generally considered an affordable mortgage". This should be deleted as a guideline of this type is prohibited by FmHA.

10. Page 32 -- Suggest table be modified as shown. This illustrates that FmHA cannot serve low income families without additional subsidies.

Year	Median Family Income	FmHA Adjusted Income	Median Sales Price	Average Initial New 502 Housing Loan	Sales* Price to Income Ratio
1972	$11,100	$5,471	$27,600	$15,483	2.50
1973	12,100	6,218	32,500	17,067	2.70
1974	12,800	7,321	35,900	19,706	2.80
1975	13,700	7,750	39,300	21,932	2.90
1976	14,500	8,270	44,200	23,267	3.05
1977	16,000	9,505	48,800	25,066	3.05

11. Pages 32, 33 -- Rural housing costs per square foot are higher. It should also be noted that FmHA units are smaller and costs for sewer, water, etc., will increase the cost per square foot in smaller units.

12. Page 34 -- To alleviate some of the problems associated with rising heating costs, more rigid thermal standards have been implemented by FmHA.

13. Pages 34, 35 -- Our experience has shown small low volume builders can construct homes at a lower cost than volume builders in rural areas.

14. Pages 35, 36 -- Future demand should address the impact inflation has upon low income groups' ability to purchase homes without assistance. Also, the increased demand for housing suggests that new construction is as important as rehabilitation of existing units.

15. Page 39 -- A housing demand and condition is addressed here which can only be met through increased appropriations and staff rather than only agency efforts.

16. Page 40 -- "A FmHA program which applies about one-fourth of its support to metropolitan counties". This reflects in part our mandate to serve these rural areas as defined by Congress.

17. Page 49 -- The conclusion that "much of the housing was constructed in and around urban areas" is misleading. It should read "constructed around urban areas because this was the location of demand and homeownership affordability rather than in the remote areas". A program such as HOAP would assist us in serving these remote areas.

18. Page 65 -- The question of affordability throughout the report refers to the assumption that no applicant can afford more than 20 percent of adjusted income for PITI. This is a criteria for interest credit and not a repayment ability criteria.

19. Pages 66, 76 -- As outreach is discussed in your report, consideration needs to be given to the requirements of funds and staff to achieve this outreach. A suggestion by Congress or GAO that FmHA should do more outreach requires careful evaluation. The Section 525 program was legislated for outreach in 1974 but emphasis has been shifted to counseling through the appropriation process. Some FmHA offices could do a better job of working with local organizations. The National Office plans to encourage and improve coordination with local organizations.

20. Page 67 -- HOAP update: Congress has not appropriated funds at this time.

21. Page 76 -- The delivery of adequate assistance will occur through the priorities now being established by the Agency. These criteria are outlined in your report.

22. Page 77 -- Update: The section 504 program is receiving more emphasis at this time. This can be noted by the trend shown in Table 1 where 87 percent of the funds were obligated in 1978.

23. Page 79 -- We are presently revising the 502 Incentive Repair Program to permit loans up to $9,000. Also, the regular 502 program is available with 1 percent interest and no dollar limit.

24. Page 80 -- Allocating 50 percent of the funds for purchasing and repairing older homes is no longer an administrative goal.

6

25. Page 84 -- The word "incidence" is misleading; it should read "level".

26. Page 90 -- Correction. (1) Borrowers are of three types, profit, limited profit, and nonprofit; and (2) 50 year amortization is no longer restricted to only senior citizens.

TABLE 1

Low and Moderate Income Appropriation (A) and Obligation (0)

Year	502	504	515	515	516	Total
			PROGRAM TITLE Millions			
1969						
A	485.0	18.0	25.0	15.0	4.2	547.2
0	480.4	5.8	17.3	3.5	5.0	512.0
1970						
A	1,125.0	10.0	28.0	15.0	2.5	1,180.5
0	756.3	5.2	28.4	1.5	2.1	793.5
1971						
A	1,420.0	10.0	37.0	10.0	2.5	1,479.5
0	1,362.3	5.5	26.8	.5	.7	1,395.8
1972						
A	1,555.0	10.0	35.0	10.0	2.5	1,612.5
0	1,561.2	5.3	40.1	2.7	6.7	1,616.0
1973						
A	2,059.0	10.0	70.0	10.0	2.5	2,151.5
0	1,735.7	4.6	105.1	10.2	1.7	1,857.3
1974						
A	1,985.0	10.0	144.0	10.0	7.5	2,156.5
0	1,589.8	4.4	173.3	10.0	10.1	1,787.6
1975						
A	2,073.0	20.0	146.0	10.0	5.0	2,254.0
0	1,926.6	4.8	292.4	8.1	5.0	2,236.9
1976						
A	3,229.0	25.0	625.0	12.5	10.7	3,902.2
0	2,899.9	8.3	500.0	10.1	10.7	3,429.0
1977						
A	2,637.0	20.0	545.0	10.0	7.5	3,219.5
0	2,568.7	12.9	545.0	5.3	7.3	3,139.2
1978						
A	2,675.0	24.0	690.0	10.0	7.8	3,406.8
0	2,690.9	20.9	676.0	10.0	7.8	3,405.6
TOTALS						
A	19,243.0	157.0	2,345.0	112.5	52.7	21,910.2
0	17,571.8	77.7	2,404.4	61.9	57.1	20,172.9
Percent O/A	91%	49%	103%	55%	108%	92%

DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT
WASHINGTON, D.C. 20410

November 1, 1979

OFFICE OF THE ASSISTANT SECRETARY FOR
HOUSING-FEDERAL HOUSING COMMISSIONER

IN REPLY REFER TO:

Mr. Henry Eschwege
Director, Community and Economic
Development Division
U.S. General Accounting Office
Washington, D.C. 20548

Dear Mr. Eschwege:

Secretary Landrieu has asked me to respond to your letter of September 27, 1979, transmitting a draft of the proposed report to the Congress entitled: "Ways a More Equitable Share of Federal Housing Support Can be Provided to Rural Areas."

We have reviewed the report and its recommendation that, to increase the availability of home loans on reasonable terms, the Secretary of HUD, in connection with the two-year study of methods to improve HUD program accessibility in rural areas, devise and test incentives to:

(1) Increase the use of HUD home mortgage insurance programs by rural financial institutions; and

(2) Expand the operations of urban financial institutions into outlying rural areas.

I agree with these recommendations and have already taken the steps to establish demonstrations which will test the effectiveness of such actions.

A Departmental Rural Assistance Initiative has been undertaken to identify the best methods, within existing authorities, to encourage use of HUD-insured mortgage financing as well as HUD's assisted housing and community development programs. In the North Carolina initiative, our Greensboro Area Office, by my directive, has undertaken a program of delegated processing aimed specifically at rural lenders. I am hopeful that many lenders who are now reluctant to deal directly with the HUD Office will participate in this rural initiative demonstration. My staff has also met with the staff of the Federal National Mortgage Association (FNMA) to discuss what joint efforts must be taken to improve

2

the availability of mortgage credit in rural areas. It is our belief that rural lenders must have an extensive knowledge of the secondary market, since many lenders do not have the necessary capital to undertake extensive lending without such markets.

The Office of Housing has also directed the development of a demonstration program of outreach and delegated processing. This program is aimed at the more sophisticated urban lender which, in order to participate in the delegated processing program, must take steps to make mortgage insurance financing available in certain areas selected by HUD not now active in the mortgage insurance programs.

I have also asked my staff to study ways in which our interest subsidy program, Section 235, can be better utilized in rural areas.

In assessing federal housing support to rural areas, it might be useful to note a distinction between mortgage insurance programs which are generally used to facilitate homeownership by moderate income households, and housing assistance programs which provide rental or interest subsidies to primarily low income households. The GAO conclusion, i.e., that 20 percent of federal housing support goes to rural areas, includes the full range of mortgage insurance programs, direct loans, and rental assistance programs designed for different income groups. In contrast, federal housing assistance specifically for low income households is over 25 percent, since 24 percent of HUD's Section 8 funds and 25 percent of HUD's Low Rent Public Housing funds are allocated to non-metropolitan areas, and over 90 percent of the Farmers Home administration's housing assistance goes to non-metropolitan areas.

Moreover, the report would be strengthened by the specification of definitions used to determine substandard housing. The GAO report states that one-half of "substandard" housing defined as "lacking complete plumbing" and "dilapidated with complete plumbing" is located in non-metropolitan areas. We are unclear what defects are included in the "delapidation" category. HUD defines substandard as "physically inadequate," which includes "lacking complete plumbing" or up to sixteen other specifically enumerated defects collected by the Annual Housing Survey (AHS). Using HUD's list of defects, the 1977 AHS data shows that non-metropolitan areas contain 41.0% of all units with physical inadequacies.

We are deeply concerned with the problems of rural areas. I appreciate the opportunity to comment on this General Accounting Office audit report and to inform you of the actions already taken to improve the availability of mortgage credit in rural areas.

Sincerely,

Lawrence Simons

Lawrence B. Simons
Assistant Secretary

(382120)

☆U.S. GOVERNMENT PRINTING OFFICE : 1980-620-386/111

Single copies of GAO reports are available free of charge. Requests (except by Members of Congress) for additional quantities should be accompanied by payment of $1.00 per copy.

Requests for single copies (without charge) should be sent to:

U.S. General Accounting Office
Distribution Section, Room 1518
441 G Street, NW.
Washington, DC 20548

Requests for multiple copies should be sent with checks or money orders to:

U.S. General Accounting Office
Distribution Section
P.O. Box 1020
Washington, DC 20013

Checks or money orders should be made payable to the U.S. General Accounting Office. NOTE: Stamps or Superintendent of Documents coupons will not be accepted.

<u>PLEASE DO NOT SEND CASH</u>

To expedite filling your order, use the report number and date in the lower right corner of the front cover.

GAO reports are now available on microfiche. If such copies will meet your needs, be sure to specify that you want microfiche copies.

AN EQUAL OPPORTUNITY EMPLOYER

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

OFFICIAL BUSINESS
PENALTY FOR PRIVATE USE, $300

POSTAGE AND FEES PAID
U. S. GENERAL ACCOUNTING OFFICE

U.S.MAIL

SPECIAL FOURTH CLASS RATE
BOOK