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

RESOURCES, COMMUNITY,
AND ECONOMIC DEVELOPMENT
DIVISION

August 26, 1985

B-219568

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The Honorable Douglas K. Bereuter
House of Representatives

Dear Mr. Bereuter:

Subject: Processing Time for Farmers Home Administration's Operating Loans in Minnesota During Fiscal Year 1984 (GAO/RCED-85-142)

As requested in your May 30, 1984, letter and modified in subsequent discussions with your office, this report provides information on the processing time for the Farmers Home Administration's (FmHA) fiscal year 1984 operating loans in Minnesota. FmHA operating loans provide short-to-intermediate term (up to 7 years to repay) credit for operating expenses--such as seed, fertilizer, equipment, and livestock--to operators of family-size farms who cannot obtain credit elsewhere. The operating loan program is the largest FmHA farmer loan program providing about 60,000 operating loans nationwide for approximately $2.1 billion in fiscal year 1984. FmHA made about 59,000 of these operating loans for about $2 billion (over 98 percent) as insured (direct) loans. Private lenders made the remainder under FmHA guarantees.

This report discusses the results of our work in Minnesota. In summary, we found the following:

--FmHA does not have formal criteria for timely loan processing, although FmHA officials said that about 60 days was a reasonable processing time for typical operating loans. Loans having unusual processing problems would take longer.

--The average (mean) processing time for operating loans in Minnesota was about 72 days and the median processing time for our sample was 57 days.

--FmHA officials attribute the length of time taken to process loans to such reasons as incomplete documentation by the farmer, heavy workload in the county offices during the peak operating loan season early in the year, time and effort required to assess financial viabiility of

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marginally creditworthy FmHA applicants, and special processing problems such as the need to clear title defects when real estate is offered as collateral.

--FmHA closed about 58 percent of the operating loans (1,984 of 3,449) before planting time and approved another 24 percent (830) by then (thus providing the farmers the opportunity to obtain credit needed for planting crops). Only about 3 percent (124) of the loans were not closed or approved before planting time because of temporary funding delays attributable to FmHA.

--FmHA's files contained no information, such as letters of complaint or records of visits or telephone calls, showing that the time it took to process loans had an adverse effect on the borrowers during 1984.

The following sections of this report provide information on our objectives, scope, and methodology; background on FmHA's operating loan program; and the results of our work.

OBJECTIVES, SCOPE, AND METHODOLOGY

As initially agreed with your office, our overall objective was to evaluate the timeliness of the FmHA operating loan process. Our specific objectives were to determine (1) the criteria for timely loan processing, (2) the actual processing time and the reasons for the length of time between the various processing steps, (3) the effects of any delays on the farmers, and (4) alternatives available for improving the process. Because Minnesota had the third highest operating loan activity in the nation, we selected it as the first of several states in which we would evaluate the timeliness of the fiscal year 1984 operating loan process. We chose the 1984 loan process to evaluate because it had been most recently completed at the time our work was performed, between October 1984 and May 1985.

During our review both the Administration and the Congress initiated actions affecting the ongoing fiscal year 1985 operating loan program which, in turn, affected the relevance of our examination of the timeliness of FmHA's 1984 program. For example, the Administration took steps to (1) provide additional loan funding, (2) hire additional FmHA staff and utilize staff from other U.S. Department of Agriculture (USDA) agencies to process 1985 loans, and (3) encourage state governments and Farm Credit System lenders to help FmHA process 1985 loan applications. In addition, bills were introduced in the Congress requiring FmHA to hire additional personnel and urging it to use other USDA personnel and resources to expeditiously process loan applications.

Because of the 1985 actions that affected the relevance of our 1984 program evaluation and the lack of both FmHA loan processing time criteria and file evidence of the loan processing time's adverse effect on FmHA borrowers during 1984, we agreed with your office to terminate our work. We agreed, however, to provide you with information we gathered on Minnesota's 1984 operating loan process.

Because of the decision to terminate our review, we did not fully determine the reasons for the length of time between the various loan processing steps, the effects of any delays on the farmers, and alternatives available for improving the process. Our review was conducted in accordance with generally accepted government auditing standards.

To develop information on loan processing time criteria, we reviewed FmHA regulations and held discussions with FmHA officials at the national, state, district, and county office levels. Because of the decision to terminate our review, we limited our work on determining the reasons for the length of time between the various processing steps to discussions with FmHA officials in the National Office and the Minnesota state, district, and county offices. For that same reason, we did not discuss loan processing procedures or the timeliness of the loan process, including processing-time criteria, with FmHA borrowers, other lenders, or other creditors such as seed and fertilizer companies.

Our work to develop actual loan processing time was designed to produce results that could be projected statewide. We randomly selected 8 county offices (Warren, Crookston, Mahnomen, Ivanhoe, Slayton, Redwood Falls, Austin, and Brainerd) and 160 insured (direct) operating loan applications, 20 within each county office, to measure the loan processing time from the date FmHA received the applications until it closed the loans and the farmers received the money. We focused our attention on insured loans made directly by FmHA because of the relatively small number of guaranteed loans made nationwide (less than 2 percent) and the difference in the guaranteed-loan process due to the involvement of a private lender. The processing time and associated sampling errors were calculated at the 95-percent confidence level.

BACKGROUND

FmHA makes direct loans (government-funded) and guarantees some loans made by private lenders primarily to family farmers[1] who are unable to obtain credit from other lenders at reasonable rates and terms. As such, FmHA serves as a "lender of last resort" to farmers and is the federal government's primary

[1]A family farm is one that can be operated and managed by one family, which performs a substantial portion of the labor. The farm business may be conducted by an individual, partnership, corporation, or cooperative.

source of farm credit. Its history of financial and technical assistance goes back to the 1930's when its original function was to help needy farm families reestablish themselves on a self-supporting basis during and after the Depression. Since that time the Congress has expanded FmHA's programs to include housing, community facilities, and business and industrial development in rural areas. However, FmHA's main purpose continues to be a source of credit for building stronger family farms. Statutory authority for FmHA's lending programs is provided by the Consolidated Farm and Rural Development Act, as amended (Public Law 87-128, August 8, 1961, last amended by Public Law 98-258, April 10, 1984).

In addition to farm operating loans, FmHA has farmer programs for

--farm ownership loans to buy, improve, or refinance farm real estate;

--emergency loans to help farmers recover from losses inflicted by natural disasters (such as drought, floods, and hailstorms) and by economic conditions beyond the farmers' control; and

--other purposes, such as recreation, improvement of soil and water resources, and land purchases by Indian tribal organizations.

Farmer program loans made during fiscal year 1984 were as follows:

Table 1

Farmer Program Loans in Fiscal Year 1984

	Number of loans	Amount (millions)
Farm operating loans	60,167	$2,071.2
Farm ownership loans	8,717	700.7
Emergency loans	34,997	1,051.6
Economic emergency loans[a]	5,770	599.3
Soil and water loans	771	12.5
Indian tribe land acquisition loans	3	2.6
Total	110,425	$4,437.9

[a]The Economic Emergency Loan Program has not been authorized for years subsequent to fiscal year 1984.

Source: U.S. Department of Agriculture, Farmers Home Administration, A Brief History of Farmers Home Administration, February 1985.

Organizational responsibilities for FmHA farmer program loans

FmHA's organization for managing and conducting its farmer program loans consists of its National Office in Washington, D.C.; its Finance Office in St. Louis, Missouri; and a system of 46 state, 270 district, and 1,945 county offices serving the rural counties and parishes in the 50 states plus the Pacific Trust Territory, American Samoa, Guam, Puerto Rico, and the Virgin Islands. The National Office develops plans, policies, and procedures for use on a nationwide basis for making and servicing farmer program loans. It also monitors, inspects, and evaluates the administration of these loan programs as executed by the state, district, and county offices. The Finance Office maintains the necessary obligation and corresponding fund controls related to disbursing loan funds to FmHA borrowers.

FmHA state offices provide overall direction of FmHA program operations within the state, and district offices supervise the operations within their areas. County offices serve one or more counties or parishes and have the major responsibility for executing farmer program loans--accepting loan applications and approving, closing, and servicing these loans. FmHA also uses County Committees--made up of three local residents who are appointed by the FmHA state director with recommendations from the FmHA county supervisor and who know local farming and credit conditions--to determine applicants' eligibility for farmer program loans. The

County Committee members serve 3-year terms, two of the three must be farmers, and none can be FmHA borrowers except in certain emergency situations.

Operating loan program

Farm operating loans can be used to pay for items needed for a successful operation. These items include livestock, poultry, farm and home equipment, feed, seed, fuel, fertilizer, chemicals, hail and other crop insurance, food, clothing, medical care, and hired labor. In addition, funds can be used for minor improvements to buildings and real estate, to develop water systems, or to refinance certain debts.

Two types of operating loans are available through FmHA--insured (direct) loans made directly by FmHA and FmHA-guaranteed loans made by private lenders. Over 98 percent of the fiscal year 1984 operating loans were insured loans--59,202 loans for about $2 billion. The interest rate for insured loans is based on the federal government's cost of borrowing and was set at a standard 10.25 percent in fiscal year 1984. For applicants with limited resources who cannot repay an insured loan at the standard interest rate, a lower interest rate--7.25 percent in fiscal year 1984--is available. Interest rates for guaranteed loans are negotiated between the lender and the borrower, are higher than for insured loans, and approximate or are slightly above the market rate. Operating loan limits during fiscal year 1984 were $200,000 for insured loans and $400,000 for guaranteed loans.

Eligibility requirements

According to FmHA regulations, operating loan applicants may include individuals, corporations, cooperatives, and partnerships that will conduct family-size farming or ranching operations. An individual must meet the following eligibility requirements:

--have farm experience or training and possess the character, industry, and managerial ability to carry out the operation;

--possess the legal capacity to incur the obligations of the loan;

--be unable to obtain sufficient credit elsewhere at reasonable rates and terms;

--be a citizen of the United States or a resident alien who has been legally admitted into and has permanent residence in the United States;

--be an owner or tenant operating a family farm after the loan is closed;

--need to rely on farm income and any other income to provide a level of living comparable to that considered reasonably adequate for the area; and

--try honestly to carry out the terms and conditions of the loan.

In addition to meeting the eligibility requirements for individuals, if members, stockholders, or shareholders of a partnership, corporation, or cooperative are related by blood or marriage, at least one stockholder, shareholder, or partner must operate the farm. In the case of an entity whose members are not related by blood or marriage, a majority of the members must operate the farm. In either case, the members, stockholders, or partners cannot, as individuals, have an individual FmHA farm ownership, soil and water, recreation, or operating loan and cannot be members or have an interest in another entity that has one of those loans.

Operating loan process

The operating loan process consists primarily of five steps: (1) application receipt, (2) eligibility determination, (3) loan approval, (4) check processing, and (5) loan closing and funds disbursement. The process's complexity and completion time vary considerably among different borrowers, depending on such factors as FmHA's previous experience with the borrower, the borrower's financial condition, and the intended use of the loan proceeds. We developed the following description of the process through review of FmHA regulations and work standards and discussions with FmHA county supervisors in Minnesota.

Application receipt--When an applicant for an operating loan comes into the FmHA county office to apply, the county supervisor explains the program and the information that the applicant must furnish. The applicant is given the necessary forms to complete and return to the county supervisor. As a minimum, these forms include the Application for FmHA Services and the Farm and Home Plan--a financial statement showing financial condition, debt repayment plan, recommended management improvements, and projected expenses and income. When the completed forms are returned, the county supervisor reviews them for completeness and assists the applicant in completing them, if necessary.

Eligibility determination--The County Committee certifies an applicant's eligibility in accordance with the eligibility requirements previously discussed. The County Committee reviews the application and may interview the applicant or visit the farm before making its decision. County Committees do not determine loan feasibility or have loan approval authority. These functions are the responsibility of FmHA, generally the county supervisor.

County Committees meet periodically, as needed, to review applications. Generally, they meet every 2 weeks during the peak operating loan processing season and review several applications during a single meeting.

Loan approval--Loans cannot be approved before the County Committee determines eligibility; however, county supervisors may perform some of the following required functions while awaiting the eligibility determination. Depending on the circumstances, such as knowledge of the applicant and/or previous loan experience, the county supervisor may

--visit the applicant's farm to observe the operation and/or appraise loan collateral,

--check at the county courthouse for recorded loans to the applicant or liens or judgments against the applicant, and

--check with the applicant's creditors concerning amounts owed and payment history.

If the County Committee determines that the applicant is eligible for FmHA assistance, the county supervisor will schedule a meeting with the applicant to review the application and the Farm and Home Plan. A major part of this review is a cash flow analysis based on the applicant's plan of operation for the coming year. In addition, before loan approval the county supervisor must decide whether the proposed loan complies with established policies and all pertinent regulations. Among other things, the county supervisor must determine that

--funds are requested for authorized purposes,
--the proposed loan is sound,
--the security is adequate, and
--necessary FmHA supervision is planned.

If the county supervisor decides to approve the loan, he/she signs the Request for Obligation of Funds and sends a copy to FmHA's Finance Office in St. Louis, Missouri, to serve as the basis for check issuance.

Check processing--The Finance Office reviews the Request for Obligation of Funds for the approved loan, processes the loan check, and mails the check to the county office. (FmHA changed this process to an electronic fund transfer system in fiscal year 1985 as discussed on page 13.)

Loan closing and funds disbursement--When the county office receives the check, it notifies the applicant and makes an appointment for loan closing. Before or at loan closing, the applicant signs a financing statement, which the county office sends to the county courthouse for recording; a security agreement; and a promissory note. The applicant then receives the check for the approved loan amount. At the county supervisor's discretion, the borrower may be required to deposit the operating loan proceeds into a supervised bank account to ensure that loan funds are used only for approved purposes. In setting up the supervised bank account, the borrower, FmHA, and the bank execute a deposit agreement, which provides, among other things, that checks the borrower draws on the account be countersigned by FmHA.

FmHA DOES NOT HAVE FORMAL CRITERIA FOR TIMELY LOAN PROCESSING

FmHA has not established calendar-day criteria for the time it should take to process an operating loan from the date the application is received until the loan is closed and funds received by the borrower.[2] The FmHA Acting Assistant Administrator for Farmer Programs in the National Office told us that a reasonable processing time for typical operating loans was about 60 calendar days, but loans having unusual processing problems would take longer. District directors and county supervisors in Minnesota generally agreed that about 60 days was a reasonable processing time for typical operating loans. However, the Acting Assistant Administrator believed that criteria based on calendar days would not be appropriate for the following reasons:

--Farmers do not always submit all of the required information in the initial application package, thus requiring additional time for follow-up discussions and documentation. In addition, because of the large number of applicants, often a waiting period exists for an appointment to see the county supervisor.

--FmHA applicants have marginal creditworthiness, as evidenced by their inability to obtain private financing. Consequently, considerable time and effort are often required to assess financial viability and to structure a loan package that will enable the farmer to stay in business.

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[2]FmHA regulations do have a calendar-day criterion for one of the intermediate steps--County Committee determination of eligibility--to be completed within 30 days after receipt of a completed application. However, this time frame is not firm because if this determination cannot be made within 30 days, the regulations specify that the applicant be notified in writing of the circumstances causing the delay and the approximate time needed to make a decision on eligibility.

--Some loans have special processing requirements, such as executing subordination agreements with other lenders and clearing title defects in instances where real estate is offered as collateral. These actions take considerable time and, in many cases, are beyond the control of FmHA.

The Chief, Loan Processing Branch of the Farm Real Estate and Production Division in FmHA's National Office told us that a better measurement of processing time than a calendar-day time frame would be to determine whether the farmer had received the loan funds when needed. For example, an operating loan for planting crops would be needed by planting time. If a farmer received an operating loan by then, the farmer's needs would be met. According to the FmHA official, operating loans for other purposes, such as the purchasing of livestock or equipment, may not be as time critical as an operating loan for planting crops.

LOAN PROCESSING TIME AND REASONS FOR LENGTH OF TIME BETWEEN PROCESSING STEPS

On the basis of a random sample (160) of Minnesota's 4,435 operating loan applications during fiscal year 1984, we have determined that 78 percent (3,449) of the applications resulted in operating loans. The average (mean) processing time for those applications resulting in loans was about 72 days with time frames ranging from under 30 days to over 120 days. FmHA's Acting Assistant Administrator for Farmer Programs and other officials indicated that the same reasons held true for the length of time between steps in the loan process as for the inappropriateness of setting calendar-day criteria for the processing time.

Loan Processing Time

As stated above, our random sample indicated that 78 percent of Minnesota's 1984 operating loan applications resulted in operating loans. Of the remaining 22 percent (986), 8 percent (381) had been withdrawn, 8 percent (343) had been rejected, and 6 percent (262) were still pending at the time of our review. The average (mean) processing time for the projected number of applications that resulted in loans was about 72 days. (The median processing time for our sample was 57 days.)

In comparison to the 60 days that the FmHA officials in the National Office, the Minnesota district directors, and county supervisors said was a reasonable processing time for typical operating loans, about 49 percent (1,701) of the projected 3,449 loans were closed within 60 days; and about 51 percent (1,748) took more than 60 days.

Table 2 groups the processing time for the projected completed operating loans in fiscal year 1984.

Table 2

Processing Time for Projected Completed Operating Loans

Processing time (days)	Loans			
	Number	Percent	Cumulative number	Cumulative percent
30 or less	150	4	150	4
31-45	551	16	701	20
46-60	1,000	29	1,701	49
61-75	602	17	2,303	66
76-90	238	7	2,541	73
91-105	374	11	2,915	84
106-120	293	9	3,208	93
More than 120	241	7	3,449	100
Total	3,449	100		

FmHA closed about 58 percent (1,984) of the loans in time for crop planting, the farmers' major reason for obtaining loans. Another 24 percent (830) were approved but not yet closed before planting time, which, according to the Minnesota county supervisors, generally begins during the last week in April or the first week in May. A number of the district directors and county supervisors that we visited told us that a farmer with an approved loan could generally get credit from seed, fertilizer, and fuel suppliers until the loan was closed.

FmHA approved the remaining 18 percent (635) of the loans after planting time. Of the 18 percent, about 47 percent of the borrowers (298) did not apply until after or less than 60 days before planting time. Unusual processing problems, such as the need to clear title defects on real property used as collateral, delayed about 23 percent (144). About 11 percent (69) were for purposes other than planting crops.

Temporary funding shortages that could be considered an FmHA-caused delay caused the remaining 19 percent (124) of the approvals after planting time--about 3 percent of the total 3,449 loans. Loans cannot be processed through the approval stage unless funds are available either at the county office if funds are allocated to that level or at the state office if funds are pooled at the state level. If funds are not available at the state office, the National Office has to allocate additional funds to the state. In fiscal year 1984, the Minnesota state office allocated loan funds to its county offices. To provide more even distribution of loan funds in fiscal year 1985, most state offices, including Minnesota, pooled their loan funds at the state level rather than allocate them to their county offices.

Loan processing segments

FmHA county office personnel record significant steps in the loan process on FmHA form 1905-4, Application and Processing Card--Individual. According to the dates recorded on these cards, the average processing time of 72 days can be broken down into four major segments as follows:

Table 3

Processing Time for Major Processing Segments

Segment	Average Days
Application receipt to eligibility determination	11
Eligibility determination to loan approval	28
Loan approval to date of check	20
Date of check to loan closing	13
Total	72

Reasons for length of time between processing steps

The FmHA Acting Assistant Administrator for Farmer Programs, the Minnesota Farmer Programs Chief, and a number of the Minnesota district directors and county supervisors that we visited attributed the length of time between the processing steps to such reasons as (1) incomplete loan application documentation on the part of the farmer, (2) heavy workload in the county offices during the operating loan season, (3) time and effort required to assess financial viability of marginally creditworthy FmHA applicants, and (4) special processing problems such as clearing title defects when real estate is offered as collateral. These are some of the same reasons why these officials believed that processing time criteria based on calendar days would not be appropriate.

NO ADVERSE EFFECT OF LOAN PROCESSING TIME IDENTIFIED IN FmHA FILES

We found no documentation in the FmHA loan files of adverse effect on the FmHA borrowers because of the time it took to process 1984 operating loans in Minnesota. In reviewing the loan files from our random sample of 160 applications in 8 county offices, we found no letters of complaint nor any indication in the running records of meetings, phone calls, etc. that the borrowers, creditors, or others were dissatisfied with the timeliness of the loan process. (FmHA is required to maintain such documentation in case of appeals, legal suits, and supervisory reviews.) In addition, FmHA county supervisors told us that during 1984 they were able to process the loans and provide the money when the farmers needed it. As previously discussed, about 82 percent (2,814) of the loans were closed or approved by planting time.

FmHA ACTIONS TO REDUCE PROCESSING TIME

The Acting Assistant Administrator for Farmer Programs stated that, in addition to Congressional and Administration actions, FmHA had taken some action and had others under consideration to reduce loan processing time. He said that one action already taken has the Finance Office transfer loan funds electronically instead of mailing checks to the county office. He estimated that this should reduce this segment of processing time to 7 days or less in 1985 (as compared to the 20 days that we calculated for Minnesota in 1984), with further improvements coming with experience. He said that another action under consideration was to eliminate certain steps--such as the need for eligibility determinations--in the loan application process for the established FmHA borrowers who have good farm management practices and are current on their loans. (We calculated 11 days for eligibility determination in Minnesota in 1984.) He added that changes in FmHA regulations and perhaps in legislation may be required to implement this action as well as others being considered.

AGENCY COMMENTS

We obtained agency comments on the results of our work. The agency generally agreed with the information contained in the report. The comments provided were mostly technical in nature and have been incorporated where appropriate. In addition, FmHA told us that it is pursuing a more active guaranteed loan program, which should reduce the workload of the county offices in processing insured (direct) loans. We were further informed that FmHA is installing multifunction, computerized work stations in its county offices, which should help reduce loan processing time.

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As arranged with your office, we are sending copies of this report to the Secretary of Agriculture, the Administrator of the Farmers Home Administration, and other interested parties.

Sincerely yours,

J. Dexter Peach
Director