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United States General Accounting Office  
Washington, DC 20548

Resources, Community, and  
Economic Development Division

B-285596

June 7, 2000

The Honorable Robert E. Andrews  
House of Representatives

Subject: Rural Housing Service: Update of Data on High-Interest Direct Loans

Dear Mr. Andrews:

You asked us to update the data we presented in December 1994 on the number of borrowers who pay above-market interest rates on direct single-family housing loans made by the U.S. Department of Agriculture's (USDA) Rural Housing Service (RHS).<sup>1</sup> Specifically, you asked us to determine whether a significant number of borrowers continue to pay above-market interest rates on such loans.

RHS makes both direct and guaranteed housing loans to rural Americans who generally cannot obtain credit elsewhere. The agency's direct loan program is designed to promote homeownership for rural households with low and very low incomes by providing direct mortgage loans for single-family housing, and depending on the borrowers' incomes, interest subsidies to lower the monthly mortgage payments. The direct loans are meant to provide temporary credit—borrowers are required to graduate from the direct loan program when their incomes are sufficient for them to afford private credit. The guaranteed loan program is designed primarily to assist rural households with moderate incomes. In guaranteeing a single-family housing loan, RHS agrees, in the event that a borrower defaults, to reimburse a commercial lender for an amount up to 90 percent of the principal advanced to the borrower. Because qualifying for private credit without a government guarantee is more difficult than qualifying with a guarantee, movement from a direct loan to a guaranteed loan is a logical progression for borrowers whose financial condition has improved but is still not sufficient to qualify for nonguaranteed private credit. However, RHS is statutorily prohibited from refinancing direct single-family housing loans using the guaranteed program.

In our 1994 report, we found that as of September 30, 1994, 92,000 nonsubsidized direct single-family loans were held by borrowers who were paying interest rates of 9.5 percent or higher on an outstanding principal balance of \$2.2 billion. The prevailing rate for the guaranteed loan program at the time of our 1994 report was 9.5 percent. About 13,000 of these direct loans were carrying interest rates of 13 percent or higher. As of

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<sup>1</sup>See *Shift to Guaranteed Program Can Benefit Borrowers and Reduce Government's Exposure* (GAO/RCED/AIMD-95-63, Dec. 21, 1994).

May 31, 2000, over 65,000 nonsubsidized direct single-family loans were still being held by borrowers who were paying interest rates of 9.5 percent or higher on an outstanding principal balance of almost \$1.5 billion. About 9,100 of these direct loans carry rates of 13 percent or higher. An additional 11,500 borrowers receive \$50 or less in interest subsidies each month but still pay an effective interest rate of 9.5 percent or higher. These borrowers could also benefit from refinancing using the guaranteed program. Table 1 compares data on direct loans for the two periods.

**Table 1: Data on RHS' Direct Single-Family Housing Loan Program, September 30, 1994, and May 31, 2000**

Date	Total outstanding principal balance	Total number of direct loans	Portion of loans with interest subsidy	Number of nonsubsidized loans at 9.5% or higher	Outstanding principal balance of loans at 9.5% or higher	Number of nonsubsidized loans at 13% or higher
Sept. 30, 1994	\$18.6 billion	765,000	About two-thirds	92,000	\$2.2 billion	13,000
May 31, 2000	\$16.5 billion	552,000	Under half	65,000	\$1.5 billion	9,100

Source: Data for 1994 are from GAO's Dec.21, 1994, report (GAO/RCED/AIMD-95-63) and data for 2000 are from RHS.

A significant number of borrowers continue to hold RHS single-family direct loans with interest rates at or above the 9.5-percent guaranteed rate that was prevailing at the time of our 1994 report. Under today's prevailing guaranteed rate of 8.75 percent, the number of borrowers that would be eligible to refinance their loans using the guaranteed loan program would be even greater.

**Agency Comments**

We provided a copy of this report to RHS for its review and comment. The RHS Deputy Administrator for Single-Family Housing said that the report accurately reflects data on the single-family housing direct loan portfolio. He observed that the ability to refinance direct loans with high interest rates through the guaranteed loan program would be of significant benefit to RHS customers holding such loans. He also noted that moving customers from the direct loan program to private-sector financing would be consistent with RHS' statutory mandate and would help to ensure the customers' continued success with homeownership.

**Scope and Methodology**

To obtain information for this report, we met with officials from RHS' Single-Family Housing Direct Loan and Guaranteed Loan Divisions. We also obtained current loan data from RHS' Centralized Servicing Center in St. Louis, Missouri.

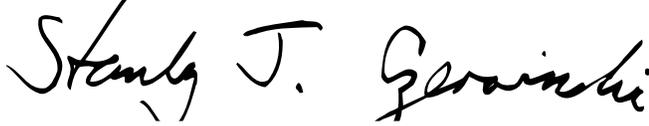
We performed our work in June 2000 in accordance with generally accepted government auditing standards.

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We are sending copies of this report to interested congressional committees and the Honorable Dan Glickman, Secretary of Agriculture. We will also make copies available to others upon request.

Please call me on (202) 512-7631 if you or your staff have any questions.

Sincerely yours,

A handwritten signature in black ink that reads "Stanley J. Czerwinski". The signature is written in a cursive style with a large, stylized 'S' and 'C'.

Stanley J. Czerwinski  
Associate Director, Housing and Community  
Development Issues

(385867)

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