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FARMERS HOME ADMINISTRATION

Appeals of Farm and Housing Loan
Decisions

Statement of
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Before the
Subcommittee on Agricultural Credit
Senate Committee on Agriculture, Nutrition, and Forestry
and the
Government Information, Justice, and Agriculture Subcommittee
House Committee on Government Operations



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Mr. Chairmen and Members of the Subcommittees:

We are pleased to be here today to discuss the Farmers Home Administration's (FmHA) appeals process for individuals dissatisfied with FmHA loan decisions. Our testimony today is based primarily on our April 1991 report,¹ which discusses (1) the status of FmHA farmer loan program and rural housing loan program appeals; (2) the timeliness of holding appeal hearings and implementing appeal decisions; and (3) the results of appeals broken down by whether appellants were minorities or nonminorities. Additionally, as you requested, we will comment on the methodology used by the U.S. Department of Agriculture's (USDA) Office of Inspector General (OIG) in a recent study that evaluated the quality of hearing officers' decisions on appeals.

Our April report focused on the 1,369 appeals of farmer program and rural housing program loan decisions that were filed by individuals in Arkansas, Mississippi, and Texas from the start of the current appeals process in July 1988 through December 1989. In summary, we found that as of April 1990:

- About 62 percent of the appeals filed in the three states received an FmHA hearing, 25 percent were concluded or withdrawn without a hearing, and 13 percent had hearings pending.

- FmHA hearing officers' decisions reversed or modified the prior FmHA loan decisions in about half the cases. Decisions were reversed because, among other things, FmHA county officials (1) used outdated or otherwise inaccurate appraisals of the land or farm equipment that was used as collateral

¹Farmers Home Administration: Information on Appeals of Farm and Housing Loan Decisions (GAO/RCED-91-106, Apr. 9, 1991).

to secure a loan or (2) improperly serviced borrowers' loans, such as failing to issue timely or accurate delinquency notices.

-- Most appeals took longer to receive a hearing than the FmHA-established standard of 45 days. In fact, on average, 4 months passed before hearing officers reviewed farmer program loan appeals and 2-1/2 months before they reviewed rural housing program loan appeals.

-- Overall, the data for the three states indicate comparable reversal rates of the prior loan decisions for minorities and nonminorities.

The OIG reported in March 1991 that, among other things, about half of 60 hearing officers' appeal decisions it reviewed were questionable.² This report was based, in part, on a judgmental sample of appeals that were decided from June 1989 to December 1989. For this hearing, we did not have time to completely review the OIG's scope and methodology, but because the OIG used a judgmental sample, we can conclude that no statistically supportable conclusions can be drawn about the quality of all hearing officers' appeal decisions made during the period the OIG reviewed. The results of the OIG's study apply only to the 60 cases reviewed.

BACKGROUND

FmHA, an agency of USDA, makes farm ownership, operating, and emergency loans and rural housing loans to individuals who cannot obtain credit elsewhere at reasonable rates and terms. FmHA also

²Farmers Home Administration Administrative Appeal Procedures (USDA/OIG Audit Report 04600-13-At, Mar. 27, 1991).

services these loans, including assisting in developing farm financial plans, collecting loan payments, and restructuring delinquent debt.

The FmHA county office is the focal point for individuals to apply for and to receive approval of farmer program and rural housing loans. The FmHA county office is also responsible for servicing loans, including visiting borrowers and assisting them as needed. FmHA district directors provide guidance and supervision to county supervisors in making and servicing loans and are responsible for rural housing loan foreclosure decisions.

FmHA loan applicants or existing borrowers can appeal most adverse loan decisions made through the county offices and by district directors. Examples of appealable decisions include denial of loan eligibility and denial of loan servicing to restructure delinquent debt. If a hearing officer reverses a loan decision, FmHA is required to withdraw the adverse decision and reconsider the application. This does not necessarily mean that the appellant will receive the loan-making or loan-servicing action that was originally denied; it only requires that FmHA reconsider the loan application.

Established by the Agricultural Credit Act of 1987, FmHA's National Appeals Staff assumed responsibility for the appeals process on July 12, 1988. From that date through December 31, 1989, the staff--which operates independently of FmHA officials making program decisions--received 1,369 appeals in the three states we reviewed. The appeals staff does not investigate allegations of discrimination; these are handled by FmHA's Equal Opportunity Staff, which investigates such allegations and refers cases that merit further review to USDA's Office of Advocacy and Enterprise.

STATUS OF LOAN-DECISION APPEALS

Of the 1,369 appeals filed in Arkansas, Mississippi, and Texas from July 12, 1988, to December 31, 1989, two-thirds involved FmHA farmer program loan decisions and one-third involved rural housing program loan decisions. The status of appeals falls into one of three categories: (1) hearings are held and decisions are either issued or pending, (2) hearings are pending, and (3) appeals are concluded or withdrawn without a hearing. On the latter, appeals were generally concluded by hearing officers or withdrawn by appellants because appellants failed to appear at the scheduled hearing or because appellants and FmHA reached agreement on the issue prior to the hearing.

As of April 1990, about 64 percent of the 918 farmer loan program appeals had been heard by hearing officers, who reversed or modified prior loan decisions in about half of the cases in which a decision was issued. Of those cases not heard by a hearing officer, 21 percent were concluded or withdrawn without a hearing and 15 percent had hearings pending.

Of the 451 rural housing loan program appeals, 58 percent had been heard by hearing officers, who reversed or modified about 46 percent of the cases in which a decision was issued. Of those cases not heard by a hearing officer, 34 percent were concluded or withdrawn and 8 percent were still pending.

Attachments I and II show the status and results of farmer loan program and rural housing loan program appeals filed in the three states we examined from July 12, 1988, to December 31, 1989.

REASONS FOR LOAN-DECISION APPEALS

We reviewed 70 judgmentally selected appeals of farmer program and rural housing program loan decisions to determine the reasons

for these appeals. As noted in our April 1991 report, the results of our work on this review is not projectible. The 45 appeals of FmHA farmer program loan decisions were filed because of appellants' (1) dissatisfaction with FmHA appraisals of loan security property, which could affect the amount of debt reduction borrowers may receive in the agency's servicing of delinquent loans; (2) belief that FmHA had incorrectly considered the farm production or financial information submitted in their applications for a loan or for loan servicing; (3) objection to FmHA's denial of loan servicing based on their failure to submit a servicing application within the 45-day time period specified in the Agricultural Credit Act of 1987; and (4) disagreement with FmHA's decision that they lacked farming experience and thus were ineligible for a loan.

The 25 appeals of rural housing program decisions were filed to (1) prevent loan foreclosures, (2) seek a reduction in loan payments, or (3) contest FmHA's decisions to deny loans based on appellants' poor credit histories or inability to repay the loan.

REASONS FOR LOAN-DECISION REVERSALS

Hearing officers reversed or modified farmer program loan decisions for various reasons, including the following: (1) county offices used appraisals that were outdated, did not properly consider the condition of the property or equipment reviewed, or did not properly consider comparable properties; (2) county offices could not support their assertion that borrowers had not acted in "good faith" in meeting the terms of their loan agreements with FmHA; (3) county offices used inaccurate income, expense, production, or asset values in evaluating the reasonableness of appellants' projections of farm production and finances; (4) county offices or county committees had not followed FmHA regulations or procedures in reaching loan decisions; or (5) county offices or county committees had failed to recognize that appellants' farm

experiences or training were adequate to qualify them for loans. Also, in some cases appellants presented new information at the appeal hearing, which resulted in hearing officers' reversing or modifying the prior loan decisions.

Hearing officers reversed or modified rural housing program loan decisions for various reasons, including that (1) county offices had not followed FmHA regulations or procedures in servicing appellants' loans, e.g., delinquency notices were not issued at required time intervals or contained inaccurate amounts, and (2) county offices had not properly considered appellants' credit histories in their loan decisions, e.g., information on credit reports did not establish a pattern of poor debt repayment.

TIMELINESS OF APPEALS PROCESS

FmHA regulations state that an appeal hearing should normally be held within 45 days after the appeals staff receives an appeal. However, we found that about 8 out of every 10 appeals that resulted in hearings exceeded that standard. In fact, on average, farmer program loan appeals took 4 months for a hearing and rural housing loan appeals took 2-1/2 months.

FmHA National Appeals Staff officials attributed delays in hearing appeals to a backlog of appeals at the inception of the process, before there were enough trained hearing officers. To expedite the handling of appeals, FmHA took several actions, such as increasing the number of hearing officers and requiring hearings to be held at central locations so that hearing officers could review more cases in less time. Also, FmHA state officials were required to identify cases in which incorrect loan decisions may have been made.

The Director of the National Appeals Staff told us she believed that these actions, together with a reduction in the

number of new appeals, had resulted in appeal hearings generally being held within 45 days of filing. However, the National Appeals Staff had not compiled data to substantiate her belief.

Timeliness of starting actions on appeal decisions

On average, FmHA county offices began actions to implement hearing officers' decisions on farmer program appeals within 26 days of the decision date and on rural housing program cases within 20 days. We considered implementation action to have started when the county office contacted the appellant to provide notice that FmHA was reconsidering the loan or loan-servicing application.

In response to a March 1991 request from Chairman Conrad, we recently started a review focusing on the final resolution of farmer program appeal cases in which loan decisions have been overturned through the appeals process. As a part of this effort, we plan to compile information from a national statistical sample of overturned cases to determine, among other things, how FmHA implemented the reversed and modified decisions and the timeliness of its actions.

RESULTS OF LOAN-DECISION APPEALS BY MINORITIES AND NONMINORITIES

Of the loan appeals covered by our review, minorities filed 350 and nonminorities filed 1,019. Minorities and nonminorities filed appeals in about the same proportion as each group received FmHA farmer program and rural housing program loans. Generally, statistical data on the status and results of appeals is comparable for minorities and nonminorities.

Hearing officers issued decisions on about 52 percent of the minority appeals, compared with 58 percent of the nonminority appeals. In these decisions, they reversed or modified about 43

percent of the prior loan decisions for minorities and about 50 percent for nonminorities. Attachment III shows the status and results of minority and nonminority appeals in the three states we examined.

COMMENTS ON OIG'S SAMPLING METHODOLOGY

The OIG's March 1991 report questioned, among other things, about half of the 60 hearing officers' decisions that it judgmentally selected for review. The OIG judgmentally selected four decisions that were made from June 1989 to December 1989 by each of 15 hearing officers. Because the OIG judgmentally selected decisions, no statistically supportable conclusions can be drawn about the extent to which those decisions represent the quality of all National Appeals Staff decisions or even the decisions made by the 15 hearing officers.³ The results of the OIG's study apply only to the 60 cases reviewed.

Had the OIG selected appeals for review using probability sampling, it could have obtained an unbiased estimate of the proportion of all hearing officers' decisions that were questionable, as well as a measure of the precision of that estimate. There are several different ways to select a probability sample, which depends on the use of random selection rather than judgmental selection, such as selecting decisions randomly from among all decisions or randomly selecting hearing officers and then randomly selecting decisions made by those officers.

Generally speaking, the more precise the estimate desired, the more time-consuming and costly the probability sampling strategy. We did not analyze the costs of employing probability sampling

³Due to time constraints, our analysis was limited to examining the sampling methodology the OIG used to select hearing officers' decisions for review. We did not examine the OIG's scope and methodology in conducting the entire study.

techniques in the OIG's study. As a result, we are not in a position to say that the OIG should have used probability sampling in designing its audit. At a minimum, however, we believe the OIG's audit report should have more clearly identified the limitations of their study; specifically, that there is no statistical assurance the results apply to any cases other than those reviewed.

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Mr. Chairmen, this completes my prepared statement. I would be happy to respond to any questions.

APPEALS OF FmHA FARMER PROGRAM LOAN DECISIONS,
JULY 12, 1988-DECEMBER 31, 1989

	<u>Arkansas</u>	<u>Mississippi</u>	<u>Texas</u>	<u>Total</u>
Decision category:				
Loan-making	30	35	95	160
Loan-servicing	<u>233</u>	<u>226</u>	<u>299</u>	<u>758</u>
Total	<u>263</u>	<u>261</u>	<u>394</u>	<u>918</u>
Appeal results: ^a				
Hearing held	154	150	282	586
Appeal concluded/withdrawn	62	41	86	189
Hearing not held	<u>47</u>	<u>70</u>	<u>26</u>	<u>143</u>
Total	<u>263</u>	<u>261</u>	<u>394</u>	<u>918</u>
Appeal decisions: ^a				
FmHA upheld	62	79	122	263
FmHA reversed	79	46	123	248
FmHA modified	2	3	7	12
Decision not finalized	<u>11</u>	<u>22</u>	<u>30</u>	<u>63</u>
Total	<u>154</u>	<u>150</u>	<u>282</u>	<u>586</u>

^aAs of April 30, 1990.

Source: Based on information obtained from FmHA offices in Arkansas, Mississippi, and Texas and from the National Appeals Staff.

APPEALS OF FmHA RURAL HOUSING PROGRAM LOAN DECISIONS,
JULY 12, 1988-DECEMBER 31, 1989

	<u>Arkansas</u>	<u>Mississippi</u>	<u>Texas</u>	<u>Total</u>
Decision category:				
Loan-making	60	77	29	166
Loan-servicing	<u>67</u>	<u>161</u>	<u>57</u>	<u>285</u>
Total	<u>127</u>	<u>238</u>	<u>86</u>	<u>451</u>
Appeal results: ^a				
Hearing held	79	124	61	264
Appeal concluded/withdrawn	39	91	23	153
Hearing not held	<u>9</u>	<u>23</u>	<u>2</u>	<u>34</u>
Total	<u>127</u>	<u>238</u>	<u>86</u>	<u>451</u>
Appeal decisions: ^a				
FmHA upheld	40	63	30	133
FmHA reversed	36	51	25	112
FmHA modified	0	2	1	3
Decision not finalized	<u>3</u>	<u>8</u>	<u>5</u>	<u>16</u>
Total	<u>79</u>	<u>124</u>	<u>61</u>	<u>264</u>

^aAs of April 30, 1990.

Source: Based on information obtained from FmHA offices in Arkansas, Mississippi, and Texas and from the National Appeals Staff.

APPEALS OF FmHA LOAN DECISIONS BY MINORITIES AND NONMINORITIES
IN THREE STATES, JULY 12, 1988-DECEMBER 31, 1989

Decision category:	<u>Farmer program</u>		<u>Housing program</u>	
	<u>Minority</u>	<u>Nonminority</u>	<u>Minority</u>	<u>Nonminority</u>
Loan-making	33	127	75	91
Loan-servicing	<u>80</u>	<u>678</u>	<u>162</u>	<u>123</u>
Total	<u>113</u>	<u>805</u>	<u>237</u>	<u>214</u>
Appeal results: ^a				
Hearing held	67	519	133	131
Appeal concluded/withdrawn	20	169	89	64
Hearing not held	<u>26</u>	<u>117</u>	<u>15</u>	<u>19</u>
Total	<u>113</u>	<u>805</u>	<u>237</u>	<u>214</u>
Appeal decisions: ^a				
FmHA upheld	31	232	73	60
FmHA reversed	28	220	47	65
FmHA modified	2	10	2	1
Decision not finalized	<u>6</u>	<u>57</u>	<u>11</u>	<u>5</u>
Total	<u>67</u>	<u>519</u>	<u>133</u>	<u>131</u>

^aAs of April 30, 1990.

Source: Based on information obtained from FmHA offices in Arkansas, Mississippi, and Texas and from the National Appeals Staff.

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