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USDA Rural Housing Programs: An Overview

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USDA Rural Housing Programs: An Overview

Summary

Title V of the Housing Act of 1949 authorized the Department of Agriculture (USDA) to make loans to farmers to enable them to construct, improve, repair, or replace dwellings and other farm buildings to provide decent, safe, and sanitary living conditions for themselves or their tenants, lessees, sharecroppers, and laborers. USDA was also authorized to make grants or combinations of loans and grants to those farmers who could not qualify to repay the full amount of a loan, but who needed the funds to make the dwellings sanitary or to remove health hazards to the occupants or the community.

While the act was initially targeted toward farmers, over time the act has been amended to enable USDA to make housing loans and grants to rural residents in general. Currently, the USDA housing programs are administered by the Rural Housing Service (RHS). The housing programs are generally referred to by the section number under which they are authorized in the Housing Act of 1949, as amended.

The rural housing programs include loans for the purchase, repair, or construction of single-family housing; loans and grants to remove health and safety hazards in owner-occupied homes; loans and grants for the construction and purchase of rental housing for farmworkers; loans for the purchase and construction of rental and cooperative housing for the elderly and for rural residents in general; rental assistance payments to make rental housing more affordable; interest subsidies to make homeownership loans more affordable and to enable production of rental housing that is affordable for the target population; and loans for developing building sites upon which rural housing is to be constructed.

In the 109th Congress, H.R. 5039 has been introduced to provide for the revitalization of rural rental housing stock under the Section 515 housing program. On April 25, 2006, a hearing was held on this bill by the Subcommittee on Housing and Community Opportunity of the House Financial Services Committee. Also pending in the 109th Congress is H.R. 3715, which would amend the Internal Revenue Code of 1986 to provide that the gain from the sale of certain federally or state-assisted multifamily rental housing would not be counted as income, provided that the property were sold to an entity that agreed to maintain the affordability and use restrictions on the property for 30 years. Both bills attempt to address longstanding concerns that owners of some RHS-financed multifamily housing may prepay their loans and convert their properties to uses other than rental occupancy by low- and moderate-income families. Keeping federally assisted housing available for use by low- and moderate-income occupants is referred to as housing preservation.

This report will be updated as deemed necessary.

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USDA Rural Housing Programs: An Overview

Introduction

Title V of the Housing Act of 1949 authorized the Department of Agriculture (USDA) to make loans to farmers to enable them to construct, improve, repair, or replace dwellings and other farm buildings to provide decent, safe, and sanitary living conditions for themselves or their tenants, lessees, sharecroppers, and laborers.¹ USDA was also authorized to make grants or combinations of loans and grants to those farmers who could not qualify to repay the full amount of a loan, but who needed the funds to make the dwellings sanitary or to remove health hazards to the occupants or the community.

While the act was initially targeted toward farmers, over time the act has been amended to enable USDA to make housing loans and grants to rural residents in general. Currently, the USDA housing programs are administered by the Rural Housing Service (RHS). The housing programs are generally referred to by the section number under which they are authorized in the Housing Act of 1949, as amended.

In the 1970s, there was concern that owners of some RHS-financed multifamily housing were prepaying their loans and converting the property to uses other than rental occupancy by low- and moderate-income families. Keeping federally assisted housing available for use by low- and moderate income occupants is referred to as housing preservation. In prior years, preservation related more to maintaining or improving the physical standards of the housing, but, since the late 1970s, preservation has related more to simply keeping the property available for use by the target population for whom it was initially constructed. Funding housing preservation, in both senses of the word, continues to be a concern for Congress.

Partly because housing projects for the elderly are more acceptable to communities than low-income projects in general, a relatively large number of projects funded through the Section 515 rural rental program are elderly projects. Occupants who were in their 60s upon initial occupancy may have aged 10, 20, or 30 years. Such occupants may have need for different services, and these have to be financed. Laws have changed regarding building accessibility requirements, and repairs must be made to meet those requirements. These also need to be financed.

¹ P.L. 81-171, Oct. 25, 1949, 42 U.S.C. 1471, et. seq.

When the majority of the Section 514 and 515 projects were originally financed, the owners were required to maintain a reserve of 10% of the project costs for future repairs and replacements. While 10% seemed adequate 30 years ago, many owners now find that these reserves are not adequate to finance needed repairs and replacements. This suggests a need for a change in law or regulation, but in the meantime, the projects may need additional loans to finance repairs.

In response to this need, P.L. 109-97 included \$9 million for the cost of a demonstration program for the preservation and revitalization of Section 515 housing. The Administration's FY2007 budget proposal, however, would not fund this program in FY2007, and would transfer any balances to the multifamily housing rural voucher program. Language would provide that, subject to authorization, these funds could also be used for preservation and revitalization of Section 515 multifamily rental housing properties.

As in prior years, the FY2007 budget requests no funding for the Section 515 program. It may be argued that there would be a net loss of affordable rental housing in rural areas whenever owners prepay their loans and find other uses for the property instead of continuing its use as low-income rental property. This may be one of the reasons that Congress has continued to fund the program, though the funding has been at significantly lower levels than in the past. (See **Table 1b.**)

A bill, H.R. 5039, that has recently been introduced in the 109th Congress would amend the Housing Act of 1949 to direct USDA to carry out a revitalization program for Section 515 projects. Owners would be given financial incentives to continue using their property as low- to moderate-income rental, but prepayment of the loans would also be permitted if certain requirements are met.

Descriptions of the rural housing programs are presented below in the order of the sections under which they are authorized in the Housing Act of 1949. Note that most of the programs involve direct loans from USDA, while others involve USDA-insured loans from private lenders. USDA is one of the few government agencies that makes direct loans to borrowers. The report concludes with a discussion of current legislative issues. Tables are presented that show funding for various rural housing programs since FY1980.

Single-family Housing Loans (Section 502)

Section 502 of the Housing Act of 1949 gave USDA authority to make housing loans to farm owners to construct or repair farm dwellings and other buildings, for themselves or their tenants, lessees, sharecroppers, and laborers. The act was amended in 1961 to make nonfarm rural residents eligible for the Section 502 loans.² Amendments by the Housing and Urban Development Act of 1965 authorized the purchase and repair of previously occupied dwellings, as well as the purchase of building sites.³ Amendments in 1968 enabled borrowers to receive interest credits

² P.L. 87-70, sec. 801, June 30, 1961, 42 U.S.C. 1472.

³ P.L. 89-117, sec. 1001, Aug. 10, 1965, 42 U.S.C. 1479.

to reduce the interest rate to as low as 1%.⁴ The Housing and Urban Development Act of 1970 enabled Section 502 loans to be made for homes on leased land, as long as the remaining term of the lease extends beyond the repayment period of the loan.⁵

In 1977, Section 502 was amended to authorize USDA to guarantee loans made by private lenders to above-moderate-income borrowers in rural areas.⁶ Funding for guaranteed loans was discontinued in 1983. The Housing and Community Development Act of 1987 directed USDA to carry out a three-year demonstration program, under which moderate-income borrowers may obtain guaranteed loans under Section 502 for the purchase of single-family homes.⁷ A permanent guaranteed loan program was authorized in 1990 by the Cranston-Gonzalez National Affordable Housing Act.⁸

Under the present Section 502 program, borrowers may obtain loans for the purchase or repair of new or existing single-family housing in rural areas. Borrowers may either obtain direct loans from USDA or obtain loans from private lenders that are guaranteed by USDA.

Borrowers with income of 80% or less of the area median may be eligible for the direct loans, and may receive interest credit to reduce the interest rate to as low as 1%. The loans are repayable over a 33-year period. In a given fiscal year, at least 40% of the units financed under this section must be made available only to very low-income families or individuals.⁹ The loan term may be extended to 38 years for borrowers with incomes below 60% of the area median.

Borrowers with income of up to 115% of the area median may obtain USDA-guaranteed loans from private lenders. Guaranteed loans may have up to 30-year terms. Priority is given to first-time homebuyers, and USDA may require that borrowers complete a homeownership counseling program.

In recent years, Congress and the Administration have been increasing the funding for the guaranteed loans and decreasing funding for the direct loans.

About 98% of the Section 502 loans are used for home purchases. The homes to be financed must be “modest” in cost and design, and must be located in rural areas serviced by the Agriculture Department. To be eligible for a Section 502 loan, a borrower must have the means to repay the loan but be unable to secure reasonable credit terms elsewhere.

⁴ P.L. 90-448, sec. 1001, Aug. 1, 1968, 42 U.S.C. 1490a.

⁵ P.L. 91-609, sec. 802, Dec. 31, 1970, 42 U.S.C. 1479.

⁶ P.L. 95-128, sec. 502, Oct. 12, 1977, 42 U.S.C. 1472, 42 U.S.C. 1487, 42 U.S.C. 1490a.

⁷ P.L. 100-242, sec. 304, Feb. 5, 1988, 42 U.S.C. 1472.

⁸ P.L. 101-625, sec. 706, Nov. 28, 1990, 42 U.S.C. 1472.

⁹ Defined as those having incomes below 50% of the median income for the area.

Modernizing Rural Homes (Section 504)

For farmers without sufficient income to qualify for a Section 502 loan, Section 504 of the Housing Act of 1949 authorized loans, grants, or combinations of loans and grants to make farm dwellings safe and sanitary or to remove health hazards.¹⁰ Low-income nonfarm homeowners became eligible for the program in 1961.¹¹ Eligibility was extended to leasehold property in 1970.¹² The 1983 Housing Act made the program available to very low-income homeowners only.¹³ The act also eliminated congressionally mandated loan and grant limits for individual homeowners and gave USDA the authority to set those limits.

Under current regulations, rural homeowners with incomes of 50% or less of the area median may qualify for USDA direct loans to repair their homes. Loans are limited to \$20,000, and have a 20-year term at a 1% interest rate. Owners who are aged 62 or more may qualify for grants of up to \$7,500 to pay for needed home repairs. To qualify for the grants, the elderly homeowners must lack the ability to repay the full cost of the repairs. Depending on the cost of the repairs and the income of the elderly homeowner, the owner may be eligible for a grant for the full cost of the repairs, or for some combination of a loan and a grant that covers the repair costs. The combination loan and grant may total no more than \$20,000.

Construction Defects/Underserved Areas (Section 509)

Section 504 of the Housing and Community Development Act of 1977 added Section 509(c) to the Housing Act of 1949.¹⁴ Under Section 509(c), USDA is authorized to receive and resolve complaints concerning construction of Section 502 housing by contractors. If a contractor refuses or is unable to honor a warranty, the borrower may be eligible for a grant for the cost of correcting the defects. The borrower must begin the process within 18 months of the completion of the home. Related costs, such as temporary living expenses, may be included in the grant.

The Cranston-Gonzalez National Affordable Housing Act amended Section 509 by adding subsection (f).¹⁵ In each fiscal year, USDA is required to designate 100 counties and communities as “targeted underserved areas” that have severe unmet housing needs. The USDA must set aside 5% of each fiscal year’s lending authority under Sections 502, 504, 515, and 524, and reserve it for assistance in targeted underserved areas. Colonias, however, are given priority for assistance with the

¹⁰ 42 U.S.C. 1474.

¹¹ P.L. 87-70, sec. 801, June 30, 1961, 42 U.S.C. 1474.

¹² P.L. 91-609, sec. 802, Dec. 31, 1970, 42 U.S.C. 1474.

¹³ P.L. 98-181, sec. 504, Nov. 30, 1983, 42 U.S.C. 1474.

¹⁴ P.L. 95-128, Oct. 12, 1977, 42 U.S.C. 1479.

¹⁵ P.L. 101-625, sec. 709(b), Nov. 28, 1990, 42 U.S.C. 1479.

reserved funds.¹⁶ The USDA must also set aside sufficient Section 521 rental assistance that may be used with the Section 514 and Section 515 programs. (See Section 521, discussed below.)

Under the Housing Application Packaging Grant (HAPG) program, nonprofit organizations, community development organizations, state or local governments, or their agencies may receive grants from USDA to help interested parties prepare applications for USDA housing loans in targeted underserved areas and colonias.

Housing for Farm Laborers (Sections 514 and 516)

The Housing Act of 1961 added Section 514 to the Housing Act of 1949.¹⁷ Under Section 514, loans are made to farm owners, associations of farm owners, or nonprofit organizations to provide “modest” living quarters, basic household furnishings, and related facilities for domestic farm laborers. The loans are repayable in 33 years and bear an interest rate of 1%. To be eligible for Section 514 loans, applicants must be unable to obtain financing from other sources that would enable the housing to be affordable by the target population.

Individual farm owners, associations of farmers, local broad-based nonprofit organizations, federally recognized Indian tribes, and agencies or political subdivisions of local or state governments may be eligible for loans from USDA to provide housing and related facilities for domestic farm labor. Applicants who own farms or who represent farm owners must show that the farming operations have a demonstrated need for farm labor housing, and the applicants must agree to own and operate the property on a nonprofit basis. Except for state and local public agencies or political subdivisions, the applicants must be unable to provide the housing from their own resources and unable to obtain the credit from other sources on terms and conditions that they could reasonably be expected to fulfill. The applicants must be unable to obtain credit on terms that would enable them to provide housing to farm workers at rental rates that would be affordable to the workers. The USDA state director may make exceptions to the “credit elsewhere” test when (1) there is a need in the area for housing for *migrant* farm workers and the applicant will provide such housing, and (2) there is no state or local body or nonprofit organization that, within a reasonable period of time, is willing and able to provide the housing.

Applicants must have sufficient capital to pay the initial operating expenses. It must be demonstrated that, after the loan is made, income will be sufficient to pay operating expenses, make capital improvements, make payments on the loan, and accumulate reserves.

¹⁶ Colonia are defined as any identifiable community that (1) is in the state of Arizona, California, New Mexico, or Texas; (2) is within 150 miles of the border between the United States and Mexico (except for metropolitan areas with populations exceeding 1 million); (3) is designated as a colonia by the state or county in which it is located; (4) is determined to be a colonia on the basis of objective criteria such as a lack of a potable water supply, inadequate sewage systems, and a shortage of decent, safe and sanitary housing; and (5) was in existence and recognized as a colonia prior to Nov. 28, 1990.

¹⁷ P.L. 87-70, sec. 804, June 30, 1961, 42 U.S.C. 1484.

In 1964, the 1949 Housing Act was amended to add Section 516.¹⁸ The Section 516 program permitted qualified nonprofit organizations, Indian tribes, and public bodies to obtain grants for up to two-thirds of the development cost of farm labor housing. Applicants must demonstrate that there is a need for such housing, and that there is reasonable doubt that the housing would be built without USDA assistance. Grants may be used simultaneously with Section 514 loans if the necessary housing cannot be provided by financial assistance from other sources. The section was amended in 1970 to permit grants of up to 90% of the development cost of the housing.¹⁹ The 1983 Housing Act provides that in decisions on approving applications under these two sections, USDA shall consider only the needs of farm laborers and make the determination without regard to the extent or nature of other housing needs in the area.²⁰ The act also requires that, in a given fiscal year, up to 10% of the funds available under Section 516 shall be made available to assist eligible nonprofit agencies in providing housing for domestic and migrant farm workers.²¹

Nonprofit organizations, Indian tribes, and local or state agencies or subdivisions may qualify for Section 516 grants to provide low-rent housing for farm labor. The organizations must be unable to provide the housing from their own resources, and be unable to secure credit (including Section 514 loans) on terms and conditions that the applicant could reasonably be expected to fulfill. Applicants must contribute at least 10% of the total development costs from their own resources or from other sources, including Section 514 loans. The housing and related facilities must fulfill a “pressing need” in the area, and there must be reasonable doubt that the housing can be provided without the grant.

The Housing and Community Development Act of 1987 redefined “domestic farm labor” to include persons (and the family of such persons) who receive a substantial portion of their income from the production or handling of agricultural or aquacultural products.²² They must be U.S. citizens or legally admitted for permanent residence in the U.S. The term includes retired or disabled persons who were domestic farm labor at the time of retiring or becoming disabled. In selecting occupants for vacant farm labor housing, USDA is directed to use the following order of priority: (1) active farm laborers, (2) retired or disabled farm laborers who were active at the time of retiring or becoming disabled, and (3) other retired or disabled farm laborers.

Farm labor housing loans and grants to qualified applicants may be used to buy, build, or improve housing and related facilities for farm workers, and to purchase and improve the land upon which the housing will be located. The funds may be used to install streets, water supply and waste disposal systems, parking areas, and

¹⁸ P.L. 88-560, sec. 503, Sept. 2, 1964, 42 U.S.C. 1486.

¹⁹ P.L. 91-609, sec. 801(d)(4), Dec. 31, 1970.

²⁰ P.L. 98-181, sec. 510, Nov. 30, 1983.

²¹ P.L. 98-181, sec. 513, Nov. 30, 1983.

²² P.L. 100-242, sec. 305, Feb. 5, 1988.

driveways, as well as for the purchase and installation of appliances such as ranges, refrigerators, and clothes washers and dryers. Related facilities may include a maintenance workshop, recreation center, small infirmary, laundry room, day care center, and office and living quarters for a resident manager.

Section 514 loans are available at 1% interest for up to 33 years. Section 516 grants may not exceed the lesser of (1) 90% of the total development cost of the project, or (2) the difference between the development costs and the sum of (a) the amount the applicant can provide from its own resources, and (b) the maximum loan the applicant can repay given the maximum rent that is affordable to the target tenants.

Rural Rental Housing (Section 515)

The Senior Citizens Housing Act of 1962 amended the Housing Act of 1949 by adding Section 515.²³ The law authorized USDA to make loans to provide rental housing for low- and moderate-income elderly families in rural areas. Amendments in 1966 removed the age restrictions and made low- and moderate-income families, in general, eligible for tenancy in Section 515 rental housing.²⁴ Amendments in 1977 authorized Section 515 loans to be used for congregate housing for the elderly and handicapped.²⁵

Loans under Section 515 are made to individuals, corporations, associations, trusts, partnerships, and public agencies. The loans are made at a 1% interest rate and are repayable in 50 years. Except for public agencies, all borrowers must demonstrate that financial assistance from other sources will not enable the borrower to provide the housing at terms that are affordable to the target population.

The Housing and Community Development Act of 1987 amended the Housing Act of 1949 to state that occupancy of Section 515 housing, which has been allocated for low-income housing tax credits (LIHTC),²⁶ may be restricted to those families whose incomes are within the limits established for the tax credits.²⁷ If, however, USDA finds that some of the units have been vacant for at least six months and that their continued vacancy will threaten the financial viability of the project, then higher-income tenants will be authorized to occupy the units.

²³ P.L. 87-723, sec. 4(b), Sept. 28, 1962, 42 U.S.C. 1485.

²⁴ P.L. 89-754, sec. 804, Nov. 3, 1966.

²⁵ P.L. 95-128, sec. 508, Oct. 12, 1977.

²⁶ For background on the LIHTC, see CRS Report RS22389, *An Introduction to the Design of the Low-Income Housing Tax Credit*, by Pamela J. Jackson.

²⁷ P.L. 100-242, sec. 306, Feb. 5, 1988. LIHTC provides a 10-year reduction in tax liability for owners of low-income rental housing based on the development costs of low-income apartments. In general, apartments financed using LIHTC cannot be rented to anyone whose income exceeds 60% of area median gross income.

Rental Assistance and Interest Subsidy (Section 521)

In 1968, Section 521 was added to the Housing Act of 1949.²⁸ Section 521 established an interest subsidy program under which eligible low- and moderate-income purchasers of single-family homes (under Section 502) and nonprofit developers of rental housing (under Section 515) may obtain loans with interest rates subsidized to as low as 1%.

Section 521 was amended in 1974 to authorize USDA to make rental assistance payments to owners of USDA-financed rental housing (Sections 515 or 514) to enable eligible tenants to pay no more than 25% of their income in rent.²⁹ Amendments in the 1983 Housing Act provide that rent payments by eligible families would equal the greater of (1) 30% of monthly adjusted family income, (2) 10% of monthly income, or (3) for welfare recipients, the portion of the family's welfare payment that is designated for housing costs.

The rental assistance payments, which are made directly to the borrowers, make up the difference between the tenants' payments and the USDA-approved rent for the units. Borrowers must agree to operate the property on a limited profit or nonprofit basis. The term of the rental assistance agreement is 20 years for new construction projects and five years for existing projects. Agreements may be renewed for up to five years. An eligible borrower who does not participate in the program may be petitioned to participate by 20% or more of the tenants eligible for rental assistance.

Self-help Housing (Section 523)

The Housing and Urban Development Act of 1968 added Section 523 to the Housing Act of 1949.³⁰ Under Section 523, nonprofit organizations may obtain two-year loans to purchase and develop land that is to be subdivided into building sites for housing to be built by the mutual self-help method (groups of low-income families who are building their own homes). The interest rate is 3% for these loans. Applicants must demonstrate a need for the proposed building sites in the locality.

Sponsors may also obtain technical assistance (TA) grants to pay for all or part of the cost of developing, administering, and coordinating programs of technical and supervisory assistance to the families who are building their own homes. Each family is expected to contribute at least 700 hours of labor in building homes for each other. Participating families generally have low income and are unable to pay for homes built by the contract method.

Applicants must demonstrate that (1) there is a need for self-help housing in the area, (2) the applicant has or can hire qualified people to carry out its responsibilities under the program, and (3) funds for the proposed TA project are not available from other sources.

²⁸ P.L. 90-448, sec. 1001, Aug. 1, 1968.

²⁹ P.L. 93-383, sec. 514, Aug. 22, 1974.

³⁰ P.L. 90-448, sec. 1005, Aug. 1, 1968.

The program is generally limited to very low- and low-income families. Moderate-income families may be eligible to participate, provided they are unable to pay for a home built by the contract method.

TA funds may not be used to hire construction workers or to buy real estate or building materials. Private or public nonprofit corporations, however, may be eligible for two-year site loans under Section 523. The loans may be used to purchase and develop land in rural areas. The land is subdivided into building sites and sold on a nonprofit basis to low- and moderate-income families. Generally, a loan will not be made if it will not result in at least 10 sites. The sites need not be contiguous.

Sites financed through Section 523 may only be sold to families who are building homes by the mutual self-help method. The homes are usually financed through the Section 502 program.

Developing Building Sites (Section 524)

In 1979, Section 524 was added to the Housing Act of 1949.³¹ Under Section 524, nonprofit organizations and Indian tribes may obtain direct loans from USDA to purchase and develop land that is to be subdivided into building sites for housing low- and moderate-income families. The loans are made for a two-year period.

Sites financed through Section 524 have no restrictions on the methods by which the homes are financed or constructed. The interest rate on Section 524 site loans is the Treasury cost of funds.

Housing Preservation Grants (Section 533)

The Rural Housing Amendments of 1983 amended the Housing Act of 1949 by adding Section 533.³² This section authorizes USDA to make grants to organizations for (1) rehabilitating single-family housing in rural areas that is owned by low- and very low-income families, (2) rehabilitating rural rental properties, and (3) rehabilitating rural cooperative housing that is structured to enable the cooperatives to remain affordable to low- and very low-income occupants. The grants were made for the first time in FY1986.

Applicants must have a staff or governing body with either (1) the proven ability to perform responsibly in the field of low-income rural housing development, repair, and rehabilitation; or (2) the management or administrative experience that indicates the ability to operate a program providing financial assistance for housing repair and rehabilitation.

The homes must be located in rural areas and be in need of housing preservation assistance. Assisted families must meet the income restrictions (income of 80% or

³¹ P.L. 91-152, sec. 413(f)(1), Dec. 24, 1969.

³² P.L. 98-181, sec. 522, Nov. 30, 1983.

less of the median income for the area), and must have occupied the property for at least one year prior to receiving assistance. Occupants of leased homes may be eligible for assistance if (1) the unexpired portion of the lease extends for five years or more, and (2) the lease permits the occupant to make modifications to the structure and precludes the owner from increasing the rent because of the modifications.

USDA is authorized to provide grants to eligible public and private organizations. The grantees may in turn provide homeowners with direct loans, grants, or interest rate reductions on loans from private lenders to finance the repair or rehabilitation of their homes. A broad range of housing preservation activities are authorized: (1) the installation and/or repair of sanitary water and waste disposal systems to meet local health department requirements; (2) the installation of energy conservation materials such as insulation and storm windows and doors; (3) the repair or replacement of heating systems; (4) the repair of electrical wiring systems; (5) the repair of structural supports and foundations; (6) the repair or replacement of the roof; (7) the repair of deteriorated siding, porches, or stoops; (8) the alteration of a home's interior to provide greater accessibility for any handicapped member of the family, and (9) the additions to the property that are necessary to alleviate overcrowding or to remove health hazards to the occupants. Repairs to manufactured homes or mobile homes are authorized if (1) the recipient owns the home and site, and has occupied the home on that site for at least one year, and (2) the home is on a permanent foundation or will be put on a permanent foundation with the funds to be received through the program. Up to 25% of the funding to any particular dwelling may be used for improvements that do not contribute to the health, safety, or well-being of the occupants; or materially contribute to the long-term preservation of the unit. These improvements may include painting, paneling, carpeting, air conditioning, landscaping, and improving closets and kitchen cabinets.

USDA is also authorized to make Section 533 grants to organizations that will rehabilitate rental and cooperative housing. This part of the law, however, had never been implemented because USDA had not issued the regulations. Thus, the Congress, in 1987, passed legislation that directed USDA to issue the necessary regulations.³³ The final regulations were published in 1993.³⁴

Guaranteed Loans for Rental Housing (Section 538)

The Section 538 program was added in 1996.³⁵ Under this program, borrowers may obtain loans from private lenders to finance multifamily housing, and USDA guarantees to pay for losses in case of borrower default. Section 538 guaranteed that loans may be used for the development costs of housing and related facilities that (1) consist of five or more adequate dwelling units, (2) are available for occupancy only by renters whose income at time of occupancy does not exceed 115% of the median income of the area, (3) would remain available to such persons for the period of the loan, and (4) are located in a rural area.

³³ P.L. 100-242, sec. 310, Feb. 5, 1988.

³⁴ 58 *Federal Register* 21894, April 26, 1993.

³⁵ P.L. 104-120, Mar. 28, 1996.

Eligible lenders include the following: (1) any lender approved by the Federal National Mortgage Association (Fannie Mae), the Federal Home Loan Mortgage Corporation (Freddie Mac), or the Federal Housing Administration (FHA), and currently active in their multifamily housing guaranteed lending programs; (2) state or local housing finance agencies; (3) members of the Federal Home Loan Bank System; and (4) other lenders that demonstrate to USDA that they have knowledge and experience with multifamily lending. In any case, the lenders must apply to USDA for permission to participate in the program. Eligibility must be verified every year.

Eligible borrowers include public agencies, Indian tribes, individuals, general partnerships (if formed for a term at least equal to the loan term), limited partnerships, for-profit corporations, nonprofit corporations, limited liability companies, and trusts. In addition, borrowers must meet the following requirements: (1) be a creditworthy single-asset entity³⁶ or have received prior written approval from USDA; (2) not be in default under any other agency housing program, or have performed well for six months in an approved workout plan; (3) be able to and intend to operate and maintain the project in accordance with program requirements; (4) be in legal and regulatory compliance with respect to any federal debt; (5) be a U.S. citizen or legal resident, a U.S.-owned corporation, or a limited liability corporation (LLC) or a partnership where the principals are U.S. citizens or permanent legal residents. Borrowers must contribute initial operating capital equal to at least 2% of the loan amount.

The eligible uses of loan proceeds include new construction; moderate or substantial rehabilitation and acquisition when related to the rehabilitation; acquisition of existing buildings for special needs; acquisition and improvement of land; development of essential on- and off-site improvements; development of related facilities; on-site management and maintenance offices; appliances; parking development and landscaping; limited commercial space costs; professional and application fees; technical assistance and packaging fees to and by nonprofit entities; board of director education fees for cooperatives; interest on construction loans; relocation assistance when applicable; developers fees; and refinancing applicant debt when authorized in advance to pay for eligible purposes prior to loan closing and approved by RHS. The program may not be used for transient or migrant housing, health care facilities, or student housing. Unless granted an exception by USDA, refinancing is not an authorized use of funds.

The interest rates on Section 538 loans must be fixed. The maximum allowable interest rate is as specified in each year's Notification of Funding Availability (NOFA). In order to help the Section 538 program serve low- and moderate-income tenants, however, at least 20% of Section 538 loans made each year must receive interest credit subsidy sufficient to reduce the effective interest rate to the Applicable Federal Rate (AFR) defined in Section 42(I)(2)(D) of the Internal Revenue Code.³⁷

³⁶ A single-asset entity is one that owns no assets other than the proposed project.

³⁷ The AFR is available at [<http://ftp.fedworld.gov/pub/irs-utl/afrs.pdf>], or in the *Wall Street Journal* on the third Wednesday of each month, labeled the "Long Term Monthly Rate."

Current Legislation

As noted in the introduction, in the 1970s there was concern that owners of some USDA-financed multifamily housing were prepaying their loans and converting the property to uses other than rental occupancy by low- and moderate-income families. As of November 1, 2003, USDA's portfolio of Section 515 loans encompassed 15,899 properties with 434,296 apartments.³⁸ Since at least 1979, there has been congressional interest in ensuring that these properties remain available and affordable to low-income rural residents. It is an issue that has yet to be resolved to the satisfaction of all interested parties. A couple of bills have been introduced in the 109th Congress that seek to address the issue.

H.R. 5039, the Saving America's Rural Housing Act of 2006. As introduced on March 29, 2006, H.R. 5039 would amend the Housing Act of 1949 to direct USDA to carry out a revitalization program for Section 515 projects. It would be a program under which property owners would request participation. On April 25, 2006, hearings were held on H.R. 5039 by the House Committee on Financial Services Subcommittee on Housing and Community Opportunity.

For participating properties, USDA would prepare and approve a long-term viability plan, which would include a comprehensive needs assessment of an eligible project over the next 20 years, and a financial plan that reviews the financial stability of the project. The financial plan might include loan restructuring and rent adjustments as needed, while providing the owner with a rate of return comparable to that received on comparable commercial multifamily housing projects — and while ensuring affordable rents to eligible households. Owners who agree to a financial restructuring plan would enter into long-term use agreements with USDA, under which the property would continue to be used as low-income rental housing for the greater of 20 years or the remaining loan term. Renters would pay a minimum monthly rent of \$25 and a maximum rent of 30% of adjusted income.

USDA would be directed to develop a plan to administer requests from owners to prepay Section 515 loans and to provide tenant protection vouchers to families residing in the properties. The vouchers could also be used toward home purchase.

Prepayments would be permitted for Section 515 loans entered into before December 15, 1989, provided that (1) the borrower has not been provided assistance to extend low-income use of the project, (2) the loan was not restricted by servicing actions, and (3) the project was no longer subject to use restrictions. During the 75-day period after the owner notified USDA of its intention to prepay the loan, the owner would be unable to sell the property, except to a purchaser who agrees to purchase the property at market rates, and to continue the property for low-income use for 20 years. USDA would be directed to establish and maintain a database of persons who have expressed interest in purchasing such properties at market price and maintaining them for use as affordable housing.

³⁸ Rural Rental Housing — Comprehensive Property Assessment and Portfolio Analysis, Final Study Report, Prepared for the USDA by ICF Consulting, Nov. 2004.

H.R. 3715, the Affordable Housing Preservation Tax Relief Act of 2005. As introduced on September 8, 2005, H.R. 3715 would amend the Internal Revenue Code of 1986 to provide that the gain from the sale of certain federally or state-assisted multifamily rental housing would not be counted as income, provided that the property were sold to an entity that agreed to maintain the affordability and use restrictions on the property for 30 years. Federally assisted property would include housing financed under the Section 221(d)(3) and Section 236 programs of the Department of Housing and Urban Development and the Section 514 and Section 515 programs of USDA. This bill was referred to the House Ways and Means Committee; no further action has yet occurred.

Table 1a. Funding for Selected Rural Housing Programs, FY1980-FY2007
(\$ in millions)

Fiscal Year	Section 502 Direct	Section 502 Guaranteed	Section 504 Loans	Section 504 Grants	Section 514	Section 516
1980	2,805.6	18.9	21.9	24.0	24.6	22.3
1981	2,577.9	5.8	17.9	22.7	18.5	10.5
1982	2,476.4	na	10.0	13.6	1.9	14.9
1983	2,137.1	na	7.1	12.5	4.0	7.5
1984	1,844.9	na	7.2	12.5	5.5	9.8
1985	1,789.9	na	7.9	12.5	17.6	11.2
1986	1,155.7	na	7.0	13.9	10.4	10.8
1987	1,144.2	na	5.9	12.5	10.7	7.1
1988	1,270.9	na	7.6	12.5	11.4	11.2
1989	1,266.8	na	11.3	12.5	11.4	9.4
1990	1,310.8	na	11.6	12.6	11.3	10.8
1991	1,2691.7	38.4	11.2	12.8	13.8	10.4
1992	1,253.8	214.4	11.3	12.8	15.9	13.5
1993	1,291.3	539.8	11.8	14.3	16.3	15.9
1994	1,656.8	725.9	25.2	27.5	15.7	40.6

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Fiscal Year	Section 502 Direct	Section 502 Guaranteed	Section 504 Loans	Section 504 Grants	Section 514	Section 516
1995	931.3	1,048.8	29.5	27.8	15.1	11.0
1996	1,016.4	1,700.0	35.1	25.7	15.0	10.0
1997	706.4	2,000.0	30.9	17.6	15.0	8.4
1998	1,007.8	2,822.5	30.3	25.7	14.6	10.0
1999	922.9	2,977.0	25.5	21.3	20.0	13.1
2000	1,140.9	2,150.5	27.4	30.4	28.8	19.3
2001	1,074.7	2,341.6	30.8	33.7	33.2	9.9
2002	1,080.6	2,418.7	32.0	31.2	47.3	14.5
2003	1,038.2	3,086.7	32.1	33.7	55.9	7.0
2004	1,351.5	3,233.4	33.6	32.4	24.1	6.8
2005	1,140.7	3,045.5	34.7	31.6	32.9	30.4
2006*	1,129.3	3,782.3	34.7	30.1	38.1	13.9
2007**	1,237.5	3,564.2	36.3	29.9	41.6	13.9

Source: Prepared by the Congressional Research Service based on documents from the U.S. Department of Agriculture.

na = program was not authorized in the years shown.

* USDA estimate based on amount appropriated.

** USDA Budget request.

Table 1b. Funding for Selected Rural Housing Programs, FY1980-FY2007
(\$ in millions)

Fiscal Year	Section 515	Section 521	Section 523 Self-Help Housing Grants	Section 524 Site Loans	Section 533	Section 538
1980	881.3	393.0	6.2	0.8	na	na
1981	864.8	423.0	13.1	0.5	na	na
1982	953.7	403.0	4.7	0	na	na
1983	802.0	398.0	10.2	0.3	na	na
1984	919.0	123.7	5.0	0.2	na	na
1985	903.0	111.0	9.4	0	na	na
1986	652.3	168.3	5.1	0	19.1	na
1987	554.9	275.3	7.6	0.2	19.1	na
1988	554.9	275.3	5.7	0	19.1	na
1989	554.9	275.4	8.3	0.4	19.1	na
1990	571.0	296.4	5.3	0.1	19.1	na
1991	576.3	311.1	12.0	0.6	23.0	na
1992	573.9	319.8	7.8	0.4	23.0	na
1993	573.9	404.0	16.9	0.6	23.0	na
1994	512.4	446.7	11.9	0.1	23.0	na
1995	183.3	523.0	12.9	0	22.0	na

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Fiscal Year	Section 515	Section 521	Section 523 Self-Help Housing Grants	Section 524 Site Loans	Section 533	Section 538
1996	151.0	540.5	12.9	0.6	11.0	23.7
1997	152.5	520.2	26.2	0.1	7.6	51.8
1998	149.4	541.4	26.7	0.4	11.1	78.7
1999	114.4	583.4	26.2	3.1	7.2	74.8
2000	113.8	639.6	28.0	0.6	5.5	99.7
2001	114.1	685.7	17.6	3.7	7.4	101.8
2002	118.4	701.0	26.5	0.5	8.6	99.4
2003	115.0	723.7	40.0	1.2	10.3	102.0
2004	115.9	580.6	35.3	3.2	9.3	99.4
2005	99.2	592.0	42.1	0.4	8.8	97.2
2006**	99.0	653.1	34.1	5.0	10.5	99.0
2007***	0	486.3	37.6	5.0	9.9	198.0

Source: Prepared by the Congressional Research Service based on documents from the U.S. Department of Agriculture.

na = program was not authorized in the years shown.

* \$12,000 was provided for sites in South Dakota.

** USDA estimate based on amount appropriated.

*** USDA Budget request