



U.S. Department of Agriculture



Office of Inspector General  
Financial and IT Operations

# Audit Report

## U.S. Department Of Agriculture Rural Development's Financial Statements for Fiscal Years 2003 and 2002

Report No. 85401-9-FM  
November 2003

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UNITED STATES DEPARTMENT OF AGRICULTURE

OFFICE OF INSPECTOR GENERAL

Washington D.C. 20250



DATE: November 7, 2003

REPLY TO

ATTN OF: 85401-9-FM

SUBJECT U.S. Department of Agriculture Rural Development's Financial Statements  
for Fiscal Years 2003 and 2002

TO: Thomas C. Dorr  
Under Secretary  
for Rural Development

ATTN: John M. Purcell  
Director  
Financial Management Division

This report presents the results of our audit of the Rural Development's financial statements for the fiscal years ending September 30, 2003 and 2002. The report contains an unqualified opinion and the results of our assessment of the Rural Development's internal control structure and compliance with laws and regulations.

Based on the information provided during the audit, we have reached management decision on the recommendation in the report. Please follow your internal procedures for forwarding documentation of final action to the Office of the Chief Financial Officer.

We appreciate the courtesies and cooperation extended to us during the audit.

/s/

RICHARD D. LONG  
Assistant Inspector General  
for Audit

# **Executive Summary**

## **U.S. Department of Agriculture Rural Development's Financial Statements for Fiscal Years 2003 and 2002 (Audit Report No. 85401-9-FM)**

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### **Purpose**

Our audit objectives were to determine whether (1) the financial statements present fairly, in all material respects, in accordance with generally accepted accounting principles, the assets, liabilities, and net position; net costs; changes in net position; budgetary resources; and reconciliation of net costs to budgetary obligations, (2) the internal control objectives were met, and (3) Rural Development complied with laws and regulations for those transactions and events that could have a material effect on the financial statements.

We conducted our audit at the Rural Development Finance Office and Centralized Servicing Center in St. Louis, Missouri, and the Rural Development National Office in Washington, D.C. We also performed site visits to selected Rural Development field offices.

### **Results in Brief**

In our opinion, the Rural Development consolidated financial statements for fiscal years 2003 and 2002, including the accompanying notes, present fairly in all material respects, the assets, liabilities, and net position of Rural Development, as of September 30, 2003 and 2002; and its net costs, changes in net position, budgetary resources, and reconciliations of net costs to budgetary obligations for the years then ended, in conformity with accounting principles generally accepted in the United States of America.

In our Report on the Internal Control Structure Over Financial Reporting, we reported that improvements are needed in the U.S. Department of Agriculture's information technology and the suspense/deposit fund reconciliation.

In our Report on Compliance with Laws and Regulations, we continued to note where further actions are necessary related to improving financial management systems.

### **Key**

#### **Recommendations**

We recommended that Rural Development establish procedures to reconcile and age the suspense accounts at a detailed transaction level and ensure the reconciliation and aging is performed timely.

#### **Agency Position**

Rural Development officials generally agreed with the findings and recommendations in this report.

## ***Abbreviations Used in This Report***

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CIO	Chief Information Officer
FFMIA	Federal Financial Management Improvement Act
FFMSR	Federal Financial Management Systems Requirements
FMFIA	Federal Managers' Financial Integrity Act
IT	Information Technology
NIST	National Institute of Standards and Technology
OIG	Office of the Inspector General
OMB	Office of Management and Budget
RUS	Rural Utilities Service

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## ***Report of the Office of Inspector General***

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**TO:** Thomas C. Dorr  
Under Secretary  
for Rural Development

We have audited the accompanying consolidated balance sheets of Rural Development as of September 30, 2003 and 2002, and the related consolidated statements of net cost, changes in net position, financing, and the combined statements of budgetary resources (hereinafter referred to as the “consolidated financial statements”) for the fiscal years then ended. The consolidated financial statements are the responsibility of Rural Development’s management. Our responsibility is to express an opinion on the consolidated financial statements based on our audit.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in Government Auditing Standards issued by the Comptroller General of the United States; and Office of Management and Budget (OMB) Bulletin No. 01-02, “Audit Requirements for Federal Financial Statements.” Those standards and OMB Bulletin No. 01-02 require that we plan and perform the audit to obtain reasonable assurance that the consolidated financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the consolidated financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall consolidated financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of Rural Development as of September 30, 2003 and 2002; and its net costs, changes in net position, reconciliation of net costs to budgetary obligations, and budgetary resources for the years then ended, in conformity with accounting principles generally accepted in the United States of America.

The information in Management Discussion and Analysis is not a required part of the consolidated financial statements, but is supplemental information required by accounting principles generally accepted in the United States of America or OMB Bulletin No. 01-09, “Form and Content of Agency Financial Statements.” We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of this information. However, we did not audit this information and, accordingly, we express no opinion on it.

We have also issued a report on Rural Development’s internal controls and a report on the mission area’s compliance with certain provisions of laws and regulations. These reports are an integral part of

an audit performed in accordance with Government Auditing Standards, and, in considering the results of the audit, these reports should be read in conjunction with this report.

This report is intended solely for the information of the management of Rural Development, OMB, and Congress, and is not intended to be and should not be used by anyone other than these specified parties.

/s/

RICHARD D. LONG  
Assistant Inspector General  
for Audit

November 7, 2003



# ***Report of the Office of Inspector General on Internal Control Structure Over Financial Reporting***

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**TO:** Thomas C. Dorr  
Under Secretary  
for Rural Development

We have audited the accompanying consolidated balance sheets of Rural Development as of September 30, 2003 and 2002, and the related consolidated statements of net cost, changes in net position, financing, and the combined statements of budgetary resources (hereinafter referred to as the “consolidated financial statements”), and have issued our report thereon dated November 7, 2003. We conducted our audit in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in Government Auditing Standards issued by the Comptroller General of the United States; and Office of Management and Budget (OMB) Bulletin No. 01-02, “Audit Requirements for Federal Financial Statements.”

In planning and performing our audit, we considered Rural Development’s internal control over financial reporting by obtaining an understanding of the internal controls, determining whether the internal controls had been placed in operation, assessing control risk, and performing tests of control in order to determine our auditing procedures for the purpose of expressing our opinion on the consolidated financial statements. We limited our internal control testing to those controls necessary to achieve the objectives described in OMB Bulletin No. 01-02 and Government Auditing Standards. We did not test all internal controls as defined by the Federal Managers’ Financial Integrity Act of 1982 (FMFIA). The objective of our audit was not to provide assurance on Rural Development’s internal control. Consequently, we do not provide an opinion on internal control over financial reporting.

Our consideration of the internal control over financial reporting would not necessarily disclose all matters in the internal control over financial reporting that might be reportable conditions. Under standards issued by the American Institute of Certified Public Accountants, reportable conditions are matters coming to our attention relating to significant deficiencies in the design or operation that, in our judgment, could adversely affect the agency’s ability to record, process, summarize, and report financial data consistent with the assertions by management in the consolidated financial statements. Material weaknesses are reportable conditions in which the design or operation of one or more internal control components do not reduce to a relatively low level the risk that misstatements, in amounts that would be material in relation to the consolidated financial statements being audited, may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. Because of inherent limitations in any internal control, misstatements due to error or fraud may occur and not be detected.



We noted certain matters described in the “Findings and Recommendations” Sections 1 and 2 involving the internal control over financial reporting and its operation that we consider to be reportable conditions. We believe that the reportable condition in Section 1 is a material weakness. This material weakness was previously identified and consequently reported in Rural Development’s FMFIA report.

### **Additional Other Procedures**

As required by OMB Bulletin No. 01-02, we considered Rural Development’s internal control over required supplemental information by obtaining an understanding of the internal control, determining whether these internal controls had been placed in operation, assessing control risk, and performing tests of controls. Our procedures were not designed to provide assurance on internal control over such required supplemental information; accordingly, we do not provide an opinion on such controls.

As further required by OMB Bulletin No. 01-02, with respect to internal control related to performance measures determined by management to be key and reported in the Management’s Discussion and Analysis, we obtained an understanding of the design of significant internal controls relating to the existence and completeness assertions. Our procedures were not designed to provide assurance on internal control over reported performance measures; accordingly, we do not provide an opinion on such controls.

This report is intended solely for the information and use of the management of Rural Development, OMB, and Congress, and is not intended to be and should not be used by anyone other than these specified parties.

/s/

RICHARD D. LONG  
Assistant Inspector General  
for Audit

November 7, 2003



# ***Report of the Office of Inspector General on Compliance with Laws and Regulations***

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**TO:** Thomas C. Dorr  
Under Secretary  
for Rural Development

We have audited the consolidated balance sheets of Rural Development as of September 30, 2003 and 2002, and the related consolidated statements of net cost, changes in net position, financing, and the combined statement of budgetary resources (hereinafter referred to as the “consolidated financial statements”), and have issued our report thereon dated November 7, 2003. We conducted our audit in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in Government Auditing Standards issued by the Comptroller General of the United States; and Office of Management and Budget (OMB) Bulletin No. 01-02, “Audit Requirements for Federal Financial Statements.”

The management of Rural Development is responsible for complying with laws and regulations applicable to it. As part of obtaining reasonable assurance about whether the consolidated financial statements are free of material misstatement, we performed tests of Rural Development’s compliance with certain provisions of laws and regulations, noncompliance with which could have a direct and material effect on the determination of the consolidated financial statement amounts, and certain provision of other laws and regulations specified in OMB Bulletin No. 01-02, including certain requirements referred to in the Federal Financial Management Improvement Act of 1996 (FFMIA). We limited our tests of compliance to the provisions described in the preceding sentence and did not test compliance with all laws and regulations applicable to Rural Development. However, providing an opinion on compliance with laws and regulations was not an objective of our audit, and accordingly, we do not express such an opinion.

The results of our tests of compliance disclosed no instances of noncompliance with other laws and regulations discussed in the second paragraph of this report, exclusive of FFMIA, that are required to be reported under Government Auditing Standards and OMB Bulletin No. 01-02. (Refer to “Findings and Recommendations,” Section 3, “Substantial Noncompliance with FFMIA Requirements.”)

This report is intended solely for the information and use of the management of Rural Development, OMB, and Congress, and is not intended to be and should not be used by anyone other than these specified parties.

/s/

RICHARD D. LONG  
Assistant Inspector General  
for Audit

November 7, 2003

# **Findings and Recommendations**

## **Section 1. Material Internal Control Structure Weaknesses Over Financial Reporting**

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Material weaknesses are reportable conditions in which the design or operation of one or more internal control components do not reduce to a relatively low level the risk that misstatements, in amounts that would be material in relation to the consolidated financial statements being audited, may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. Because of inherent limitations in any internal control, misstatements due to error or fraud may occur and not be detected. We believe that Finding No. 1 is a material weakness.

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### **Finding 1**

#### **IT Control Weaknesses Impact the Reliability of Financial Data**

As part of our financial statement audit we conducted a followup review to our prior audit<sup>1</sup> of Rural Development information technology (IT) controls. That audit disclosed, and we continue to find, material weaknesses in Rural Development's ability to effectively ensure the integrity and confidentiality of its IT resources. We believe the major cause of these material weaknesses is that the Chief Information Officer (CIO) and Information System Security Program Manager are not properly aligned within the organizational structure to effectively implement a strong security program. Further, Rural Development has had a long history of reacting to IT-related audit findings rather than instituting controls to address the systemic weaknesses in its internal control structure. As a result, there is ineffective oversight and management of its IT resources that unnecessarily expose Rural Development's critical loan portfolio data to the risk of disclosure, modification, or deletion.

We also continue to find that Rural Development is not in compliance with the Office of Management and Budget (OMB) Circular A-130, Appendix III, "Security of Federal Automated Information Resources," and Federal Information Security Management Act requirements. Rural Development has acknowledged the lack of compliance with OMB Circular A-130 as an instance of noncompliance with the Federal Financial Management Improvement Act (FFMIA).

Despite some actions to initiate the preparation of security plans, risk assessments, and certifications and accreditations of its major application and support systems, Rural Development has not completed these tasks, and in some cases has not completed them in accordance with OMB guidelines.

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<sup>1</sup> Audit Report No. 85099-2-FM, "Security Over Rural Development's Information Technology Resources Needs Improvement," dated August 5, 2002.

These documents are the foundation of a strong security program and without them Rural Development cannot be assured that all the necessary controls are in place and functioning as intended.

Material weaknesses persist in Rural Development's ability to effectively control access to its sensitive systems and data. Rural Development has not established and implemented effective internal controls to ensure that:

- User identifications belonging to former employees are timely removed;
- users have only the access needed to perform their job functions;
- remote access to Rural Development resources are properly managed and secured; and
- password settings conform to National Institute of Standards and Technology (NIST) guidance.

While Rural Development had instituted a process to circulate user lists to responsible management officials to verify access, the security staff did not include all of Rural Development systems or the level of access that each user had. Without all of the necessary data, this control is incomplete and ineffective. Without effective logical access controls, Rural Development's critical loan data is at risk of disclosure, modification, or deletion.

We also continued to identify numerous vulnerabilities in Rural Development's systems, including some that remain despite Rural Development's knowledge of the vulnerabilities through its contractors in 1997, reported by the Office of Inspector General (OIG) in 1999 and again in 2001. In spite of Rural Development management continually reporting to us that actions were taken to correct the previously identified vulnerabilities, Rural Development had not taken adequate corrective actions to correct known vulnerabilities, or established effective controls to ensure that vulnerabilities are timely identified and corrected. As a result, Rural Development's systems are unnecessarily vulnerable to exploitation.

Further, Rural Development was not following its own policies<sup>2</sup> for identifying, selecting, installing, and modifying software. Further, those same policies did not conform to departmental, NIST, and OMB guidance regarding change controls and segregation of duties. Hence, we were unable to validate that system software changes:

- Received proper authorization;
- were supported by change request documents;
- were properly tested and test results approved; or

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<sup>2</sup> "Rural Development Application Information Systems Support Handbook," dated May 1997.

- were properly monitored while being moved into the production environment.

Rural Development officials were unable to provide us a plausible explanation for this internal control weakness, but agreed that they needed to conform to proper change control procedures.

Finally, Rural Development had not ensured that all IT security controls are in place at its State and County offices. Our fieldwork in selected State and county offices across the country disclosed that Rural Development had not established controls to ensure that those offices had adequately maintained contingency planning documents, physically secured IT equipment, and ensured that all of its field employees received security awareness training. As a result, Rural Development cannot be assured that its IT resources are properly secured at its remote offices.

Despite some of its actions, it is apparent that Rural Development has not addressed the underlying cause of its poor information security by instituting a framework for proactively managing the information security risks associated with its operations. Instead, Rural Development has reacted to individual audit findings as they were reported, with little ongoing attention to the systemic causes of control weaknesses. The Department CIO's assessed Rural Development's security program at an intermediate stage noting the policies have been designed, implemented, and at least 50 percent had been tested. While we agree that Rural Development has numerous policies in place that if implemented could improve Rural Development's security posture, our detailed testing shows that Rural Development has not implemented all of its policies, or in many cases, not implemented them effectively.

OIG is in the process of reporting the results of this IT review under Audit Report No. 85099-4-FM. Recommendations to address the weaknesses identified will be addressed therein.

**Section 2. Reportable Internal Control Structure Weaknesses Over Financial Reporting**

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Reportable conditions are matters coming to our attention relating to significant deficiencies in the design or operation that, in our judgment, could adversely affect the agency’s ability to record, process, summarize, and report financial data consistent with the assertions by management in the consolidated financial statements. We believe Finding No. 2 is a reportable condition.

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**Finding 2                      Inadequate Suspense/Deposit Fund Reconciliation**

Rural Development is not properly reconciling its suspense/deposit series of Treasury Symbols to its general ledger. This occurred because Rural Development did not prioritize performing the reconciliation and aging at a detailed transaction level, nor does it have established procedures to do so. Although Rural Development allocates the cumulative suspense balances at the end of each month, its methodology does not ensure the proper accounts are identified and amounts are cleared out. (The table below illustrates 3 years of cumulative balances for Treasury Symbols 12F3875 and 12F3880). Rural Development makes a monthly net adjustment without knowing the cause of the difference or the age of the unreconciled items. As a result, differences remain that could represent potential misstatements in Rural Development’s financial statements.

Balances as Shown on Rural Development's Deposit Fund Distribution Worksheet

	<b>June 2001</b>	<b>June 2002</b>	<b>February 2003</b>	<b>July 2003</b>
<b>12F3875</b>				
<b>Beginning Balance</b>	\$ 189,074,598.08	\$ 186,741,132.68	\$ 184,390,858.59	\$ 158,168,915.34
<b>Ending Balance</b>	\$ 193,758,401.67	\$ 181,750,481.77	\$ 176,799,406.55	\$ 219,234,297.95
<b>12F3880</b>				
<b>Beginning Balance</b>	\$ 20,139,197.80	\$ 18,862,671.47	\$ 18,778,095.34	\$ 18,779,677.78
<b>Ending Balance</b>	\$ 20,125,763.28	\$ 18,840,962.15	\$ 18,788,095.34	\$ 18,777,583.72

## Recommendation No. 1

Establish and implement procedures to reconcile and age the suspense accounts at a detailed transaction level.

**Agency Response.** Rural Development indicated that a task force would be formed to determine the appropriate procedures for reconciling the deposit fund for each system. A plan with timeframes for developing the reconciliation processes will be developed by December 1, 2003. The plan will identify each system that affects the suspense accounts. Procedures will be developed and completed for each system by September 30, 2004. As procedures are completed for each system the reconciliation and aging support documentation will be reviewed to identify and clear outstanding items to the extent possible. All systems will have established procedures by September 30, 2004.

**OIG Position.** We concur with the management decision.



### **Section 3. Substantial Noncompliance with FFIA Requirements**

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Under FFIA, we are required to report whether Rural Development's financial management systems substantially comply with Federal Financial Management Systems Requirements (FFMSR), applicable Federal accounting standards, and the U.S. Government Standard General Ledger at the transaction level. To meet this requirement, we performed tests of compliance with FFIA, Section 803(a) requirements. The results of our tests disclosed instances where Rural Development's financial management systems did not substantially comply with these requirements.

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#### **Finding 3 Financial Management Systems Need Improvements**

Rural Development reported in its most recent FFIA Remediation Plan, dated August 13, 2003, that its financial management systems are not in compliance with FFMSR. We concur with that conclusion. Rural Development reported (1) its systems for servicing the Rural Utilities Service (RUS) electric and telecommunication direct loan portfolio do not comply with OMB Circular A-127, "Financial Management Systems," and (2) all financial management systems have not been certified in compliance with OMB Circular A-130, "Management of Federal Information Resources."

As a result, the RUS financial management systems do not provide adequate direct loan servicing and reporting. Also, since the financial management systems have not been certified, there is no assurance that systems have adequate security to prevent misuse or unauthorized access to or modification of information or to operate effectively and provide appropriate confidentiality, integrity, and availability.

Rural Development is in the process of incremental implementation of Rural Utilities Loan Servicing System to replace RUS legacy loan systems. Rural Development is also in the process of developing a milestone plan to more closely target the progress on the remediation of the certification of all financial management systems. The current planned completion date is September 2004.

The remediation plan also included corrective actions for performing a quality control review of Rural Development's financial statements. All corrective actions were taken to address this area as of October 2003, and therefore this is no longer an outstanding noncompliance.

Based on current corrective action plans, we are making no further recommendations in this report.

# ***Exhibit A - Consolidated Financial Statements***

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**USDA  
RURAL DEVELOPMENT**

**FISCAL YEAR 2003**

**(PREPARED BY RURAL DEVELOPMENT)**

***USDA  
RURAL DEVELOPMENT***

***CONSOLIDATED  
FINANCIAL STATEMENTS***

***FISCAL YEAR 2003 & 2002***

Rural Business-Cooperative Service

Rural Housing Service

Rural Utilities Service



Prepared by Deputy  
Chief Financial Office  
St. Louis, MO.

## MANAGEMENT'S DISCUSSION AND ANALYSIS OF RURAL DEVELOPMENT'S CONSOLIDATED STATEMENTS

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### *Mission*

This Management's Discussion and Analysis (MD & A), in conjunction with the accompanying consolidated financial statements, footnotes, and supplemental information, reflects the activities of the Rural Development mission area of the United States Department of Agriculture (USDA).

Rural Development's vision is to be a partner in helping the people of rural America develop sustainable communities. Its mission is to enhance the ability of rural communities to develop, grow, and improve their quality of life by targeting financial and technical resources in areas of greatest need through activities of greatest potential. This mission area was created by legislation signed into law on October 13, 1994.

Rural Development programs are designed to meet the diverse needs of rural communities, to help them obtain the financial and technical assistance needed to improve the quality of life in rural America, and to help individuals and businesses compete in the global marketplace. These programs consist of a variety of loan, loan guarantee, and grant programs, plus technical assistance, in the areas of business development; cooperative development; rural housing; community facilities; water and environment; electric power; and telecommunications, including distance learning and telemedicine.

The Rural Development Long Range Plan 2000-2005 defines the mission area's goals. The Plan was prepared in accordance with the requirements of the Government Performance and Results Act of 1993. It includes Rural Development's objectives as well as performance goals and results that provide a basis for measuring its success. The Plan consists of five goals, which support the United States Department of Agriculture's goal to "enhance the capacity of rural residents, communities and businesses to prosper." These goals are:

Goal 1. Good Jobs and Diverse Markets. Rural Development will improve the quality of life in rural America by encouraging the establishment and growth of rural business.

Goal 2. Quality Housing and Modern Community Facilities. Rural Development will improve the quality of life of rural residents by providing access to technical assistance, capital, and credit for quality housing and modern, essential community facilities.

Goal 3. Modern Affordable Utilities. Rural Development will improve the quality of life of rural residents by promoting and providing access to capital and credit for the development and delivery of modern affordable utility services.

Goal 4. Community Capacity Building. Rural Development will provide information, technical assistance, and, when appropriate, leadership to rural areas, rural communities and cooperatives to give their leaders the capacity to design and carry out their own rural development initiatives.

**MANAGEMENT'S DISCUSSION AND ANALYSIS OF  
RURAL DEVELOPMENT'S CONSOLIDATED STATEMENTS**

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Goal 5. Effective, Efficient Service to the Public. Rural Development will develop the staff, systems, and infrastructure needed to ensure high quality delivery of its programs to all rural residents.

***Organizational  
Structure***

Three agencies, the Rural Housing Service (RHS), Rural Utilities Service (RUS), and Rural Business-Cooperative Service (RBS) plus the Office of Community Development (OCD), which administers the Administration's rural Enterprise Zones/Enterprise communities initiative, the National Rural Development Partnership, a nationwide network of Rural Development leaders and officials committed to the vitality of rural areas, and Operations and Management constitute the Rural Development mission area.

***Loan Programs***

Rural Development loan programs, with an outstanding portfolio of approximately \$86.6 billion, are delivered through a National Office for each agency, 47 state offices, and a network of other field offices. The mission area is supported by the Office of the Deputy Chief Financial Officer in St. Louis, Missouri, which provides accounting and service support for all mission area programs, and a Centralized Servicing Center, also in St. Louis, which services the direct single-family housing portfolio. The mission area serves approximately 377,493 single family housing borrowers, 15,635 multi-family housing borrowers, 11,032 community and business borrowers, and 2,114 telecommunications, electric, cable TV, and distance learning and telemedicine borrowers.

In addition, Rural Development guarantees loans for approximately 186,296 single-family housing, 49 multi-family housing, 3,535 business & community service, and 25 electric & cable TV borrowers.

Rural Development loan programs generally require (1) providing loans to individuals and enterprises who are at a greater risk of default, since they lack the financial resources to obtain credit in the private sector, and (2) making loans bearing an interest rate at or less than the cost of funds. Rural Development has the responsibility to protect the interest of the Government by adequately securing the loans with real estate mortgages, assignments of income, personal and corporate guarantees, and liens on revenues.

The portfolio that follows reflects a total loan portfolio balance slightly higher in fiscal year (FY) 2003 than in FY 2002. The increase in the guaranteed portfolio from \$16.0 billion to \$18.4 billion offsets the decline in Single Family Housing direct portfolio from \$15.1 billion to \$14.2 billion.

**MANAGEMENT'S DISCUSSION AND ANALYSIS OF  
RURAL DEVELOPMENT'S CONSOLIDATED STATEMENTS**

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<b>Total Loan Portfolio as of September 30, 2003 Fiscal Years 2001 Through 2003 (Dollars in Billions)</b>			
	FY 01	FY 02	FY 03
<b>Direct Loans</b>			
<b>RHS</b>			
Single Family Housing	\$15.9	\$15.1	\$14.2
Multi-Family Housing	11.9	11.9	11.8
Community Facilities/Other	1.0	1.1	1.3
<b>RUS</b>			
Water & Environmental/Other	7.6	7.9	8.0
Electric	26.5	27.0	27.7
Telecommunications	3.5	3.6	3.6
Rural Telephone Bank	1.1	1.0	0.8
<b>RBS</b>			
Business and Industry	0.7	0.8	0.8
<i>Total Direct</i>	68.2	68.4	68.2
<b>Guaranteed Loans</b>			
<b>RHS</b>			
Single/Multi-Family Housing	11.4	12.3	13.4
Community Facilities/Other	0.2	0.2	0.4
<b>RUS</b>			
Water & Environmental/Other	0.1	0.1	0.1
Electric	0.5	0.5	0.5
<b>RBS</b>			
Business and Industry	2.7	2.9	4.0
<i>Total Guaranteed</i>	14.9	16.0	18.4
<i>Total Loan Portfolio</i>	\$83.1	\$84.4	\$86.6

**MANAGEMENT'S DISCUSSION AND ANALYSIS OF  
RURAL DEVELOPMENT'S CONSOLIDATED STATEMENTS**

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***Rural Business-  
Cooperative Service***

The mission of Rural Business Cooperative Service (RBS) of USDA Rural Development is to enhance the quality of life for all rural Americans by providing leadership and supporting the rural financial and banking environments enabling local businesses and cooperatives to survive and compete in the global marketplace. RBS accomplishes this mission by guaranteeing locally financed loans, funding small micro loan programs (with local development agencies) and providing small grants that provide technical assistance to start up and expand rural business and cooperatives. RBS builds local partnerships that leverage public, private, and cooperative resources to stimulate rural economic development creating jobs and sustainable business environments.

The local RBS staff in each State Office originate and administer the RBS programs: loans, loan guarantee, grant programs, and direct technical advisory and education assistance for individual entrepreneurs, businesses and cooperatives.

Under the Business and Industry (B&I) guaranteed loan programs, RBS guarantees bank-financed debt which funds business and industrial acquisition, construction, conversion, enlargement, repair, or modernization of up to \$25 million. Eligible applicants must provide or expand jobs in rural areas and may be individuals or public, private or cooperative organizations, Indian tribes and corporate entities.

The Intermediary Relending Program (IRP) provides concessionary loans (terms: 1 percent 30 years) to cooperatives, local not-for-profit or governmental entities such as economic development authorities. The funds are loaned to small and start up businesses that are not yet eligible for traditional bank loans. The ultimate borrowers demonstrate an ability to start or expand local businesses thereby creating employment or saving existing jobs in rural communities.

The Rural Business Enterprise Grant (RBEG) Program provides grants to encourage the development of small and emerging business enterprises; the creation, expansion, and operation of rural distance learning networks; and to provide adult education or job training related to potential employment or job advancement for adult students.

The Rural Economic Development Loan (REDL) and Grant (REDG) Programs provide financial assistance to RUS borrowers to foster economic development in the RUS catchment area thereby creating new job opportunities and retaining existing employment levels.

One objective is to manage the loan portfolio in a manner that is efficient and effective.

Key Performance Indicator	FY 2003 Target	FY 2003 Actual
Delinquency rate - excluding bankruptcy cases (Guaranteed Loans only)	6%	8.29%

**MANAGEMENT'S DISCUSSION AND ANALYSIS OF  
RURAL DEVELOPMENT'S CONSOLIDATED STATEMENTS**

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The goal to create “Good Jobs and Diverse Markets” is specific to the programs administered by RBS.

A second objective is to create or save jobs as well as to increase the availability and quality of jobs in rural areas.

Key Performance Indicators	FY 2003 Target	FY 2003 Actual
Create or save jobs		
B&I Guaranteed Loans	22,894	23,244
IRP Loans	30,600	30,394
RBEG	17,206	22,231
REDL	2,400	1,853
REDG	844	1,032
* Two other programs: The Rural Business Opportunity Grant Program and The Renewable Energy Systems and Energy Efficiency Improvements Grant Program together contributed jobs in FY 2003	0	9,857*
Total	73,944	88,611

In FY 2003 RBS approved REDL projects with high impacts on community services and economic development, but with fewer than anticipated jobs created in the current year.

***Rural Housing Service***

The RHS mission is to improve the quality of life in rural America and help build competitive, vibrant rural communities through its community facilities and housing programs. The goal for the RHS as stated in its Long-Range/Strategic Plan is to improve the quality of life of rural residents by providing access to technical assistance, capital and credit for quality housing and modern, essential community facilities.

Single Family  
Housing Programs

RHS provides financing, with no down payment and at favorable rates and terms, either through a direct loan with RHS or a loan from a private financial institution which is guaranteed by RHS. The direct Single Family Housing (SFH) program is the largest component of the rural housing portfolio. Direct SFH loans are made to families or individuals with very low and low incomes to buy, build, improve, repair, and/or rehabilitate rural homes. These loans are repayable over 33 years at an effective interest rate as low as 1 percent annually. RHS provides low interest loans and grants to enable very low income rural homeowners to remove health and safety hazards in their homes and to make homes accessible for people with disabilities.



**MANAGEMENT'S DISCUSSION AND ANALYSIS OF  
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The field offices handle the direct SFH loan application process and some servicing functions, and the Centralized Servicing Center handles most phases of direct loan servicing, from risk management to borrower assistance. RHS also provides escrow accounts for property taxes and insurance for its home loan borrowers.

Guaranteed loans make up the remaining portion of the SFH portfolio. A loan may be guaranteed for an amount not to exceed 90 percent of the loan amount. Guaranteed loans are available for low- and moderate-income families. These loans are repaid over 30 years with the interest rates negotiated between the borrower and the lender. The guaranteed loan program reflects the RHS commitment to achieve maximum leveraging of the federal loan funds.

The following table reflects one of the key performance indicators for the single family housing program objective of improving the quality of life for the residents of rural communities by providing access to decent, safe, affordable housing. The program provides the 100 percent loan-to-value financing needed to place qualified applicants in modest single family homes. Their quality of life is improved through the advantages of homeownership, which is the American Dream.

Key Performance Indicator	FY 2003 Target	FY 2003 Actual
Number of rural households receiving financial assistance to purchase a home of their own.	45,700	44,130

The number of households receiving financial assistance to purchase a home of their own is less than the projected target. The goal was not met due to rapidly rising housing costs that resulted in fewer homes being financed with the available dollars.

Another key performance indicator for RHS is reflected below and supports the objective to manage the loan portfolio in a manner that is efficient and effective. The indicator reflects how well the accounts are monitored and supervised. By providing effective loan servicing supervision through both the local offices and the Centralized Servicing Center, borrowers who, without proper counseling and assistance, would have faced blemished credit reports and even foreclosure are able to remain in their homes thus avoiding a diminished quality of life.

For FY 2005, RHS is changing its goal to compare its performance with the FHA portfolio.

Key Performance Indicator	FY 2003 Target	FY 2003 Actual
First year delinquency rate (Direct Loans only)	3.3 %	2.6 %

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Multi-Family  
Housing Programs

The Multi-Family Housing program finances farm labor housing, rural rental housing, and cooperative housing for low income and elderly people in rural communities of under 10,000 population. Farm labor housing loans and grants enable farmers, public or private nonprofit organizations, and units of state and local governments to develop or rehabilitate farm labor housing for seasonal and year round workers. These loans are generally repayable over 33 years at an interest rate of as low as 1 percent annually.

Rural rental housing loans enable developers to provide housing for the elderly, disabled individuals, and families who cannot afford the purchase price and maintenance costs of their own houses. In addition, grants are provided to public nonprofit organizations to assist rental property owners and co-ops to repair and rehabilitate their units.

The Multi-Family Housing program has established the following performance indicator to illustrate how they are meeting the objective of managing the MFH loan portfolio in a manner that is efficient and effective. When delinquency and losses are minimized, more affordable housing is available for eligible rural residents which helps to meet the RHS goal of providing more quality housing to improve the lives of rural residents.

Key Performance Indicator	FY 2003 Target	FY 2003 Actual
Number of projects with accounts more than 180 days past due	140	142

RHS' objective to improve the quality of life for the residents of rural communities by providing access to decent, safe, sanitary and affordable housing is reflected in the performance indicators below. By providing rental assistance, RHS is directing resources to those rural communities and customers with the greatest need.

Key Performance Indicators	FY 2003 Target	FY 2003 Actual
Total number of units funded for new construction (FY)	3,800	4,173
Total number of units funded for rehabilitation (FY)	8,300	10,313
Number of rental assistance units renewed (tenants do not lose subsidy)	41,500	42,034
Number of tenant households living in affordable, decent, safe, and sanitary housing	435,246	465,757

Community Facilities  
Programs

Rural Development strives to improve the quality of life of rural residents by providing access to modern, essential community facilities such as fire stations, health care clinics and child care facilities. RHS continues to offer both direct and guaranteed loans which are made available to public entities such as municipalities, counties, and special purpose districts as well as nonprofit corporations and tribal governments. These loans are repayable up to 40 years. Recipients must demonstrate that they are unable to obtain capital from commercial sources.

**MANAGEMENT'S DISCUSSION AND ANALYSIS OF  
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A key performance indicator is reflected below and supports the RHS objective to manage the loan portfolio in a manner that is efficient and effective. The indicator reflects how well the accounts are monitored and supervised. When delinquency and losses are minimized, the facilities are in a better position to assist the rural residents they are servicing thus improving the quality of life for their customers. This goal was achieved by RHS.

Key Performance Indicator	FY 2003 Target	FY 2003 Actual
Delinquency rate for CF customers	2%	2%

***Rural Utilities Service***

The RUS mission is to serve a leading role in improving the quality of life in rural America by administering its electric, telecommunications (including distance learning and telemedicine), and water and environmental programs in a service-oriented, forward-looking and financially responsible manner. The RUS programs leverage scarce federal funds with private capital for investing in rural infrastructure, technology, and the development of human resources. Financial assistance is provided to rural utilities, municipalities, commercial corporations, public utility districts, Indian Tribes, and cooperative, nonprofit, limited-dividend, or mutual associations. These entities are obligated to serve the public welfare and, in many instances, are subject to state regulatory oversight.

**Electric Program**

As restructuring of the electric industry advances toward a more competitive environment, Rural Development is ensuring the continued availability of reliable, high-quality electric service at a reasonable cost to rural consumers. The electric program provides financing and technical assistance to upgrade, expand, and maintain the vast rural American electric utility infrastructure. Electric borrowers have received more than \$70.4 billion in loans and loan guarantees as of September 30, 2003. Another \$53 million was refinanced during FY 2003.

Rural Development's goal of improving the quality of life of rural residents by promoting and providing access to capital and credit for the development and delivery of modern affordable utility services is reflected in their objectives and performance indicators.

Key Performance Indicators	FY 2003 Target	FY 2003 Actual
Number of rural electric systems upgraded	187	187
Number of residential consumers benefiting from system improvements (millions)	2.9	2.8
Electric loans to borrowers serving persistent poverty counties	87	70
Electric loans to borrowers serving persistent out-migration counties	86	145

## **MANAGEMENT'S DISCUSSION AND ANALYSIS OF RURAL DEVELOPMENT'S CONSOLIDATED STATEMENTS**

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Two performance measures were met or exceeded. It was projected that we would make loans to 87 borrowers who provide service to a county that is considered to be a persistent poverty county, however, the actual number was 70. As mandated by Congress, all loans are approved on a first-come-first-served basis. In FY 2003, we followed our required procedures of processing loans on a first-come-first-served basis and at the end of the fiscal year we had 70 loans that were approved for borrowers who serve persistent poverty counties.

Loans are primarily used to finance the acquisition, construction, improvement, or replacement of facilities for the distribution of electric power. The guaranteed loan program is used to finance generation, transmission, and distribution facilities. Repayment of loans is secured through liens on the assets of borrowers, long-term power arrangements, and RUS oversight of borrower activities. Loan maturity dates are selected by the borrowers and generally run for the life of the facility, but no more than 35 years. The typical distribution borrower applies for a new loan about every 3 to 5 years to finance system upgrades and expansion.

Municipal rate loans are used to finance electric distribution and sub-transmission facilities. The interest rate is based on competitive rates available in the municipal bond market for similar maturities. The majority of borrowers are required to seek supplemental financing for 30 percent of their capital requirements from a private lender without a federal guarantee. Borrowers may choose from several maturities that will determine the interest rate, which changes quarterly. Certain borrowers are eligible for a capped municipal rate, which cannot exceed 7 percent. Interest rates are set when funds are actually advanced.

Hardship loans can also be used to finance electric distribution and sub-transmission facilities. These loans are made to applicants that have rates that are above state averages (rate disparity) and that serve consumers with below average per capita and household incomes. On a case by case basis, hardship loans may be offered if the RUS administrator determines that the borrower has suffered a severe, unavoidable hardship, such as a natural disaster. Hardship loans carry a statutory interest rate of 5 percent.

Treasury rate loans are used to finance electric distribution and sub-transmission facilities. RUS administers the direct Treasury rate loan program substantially the same as it administers the municipal rate loan program, with the primary distinction being one of the interest setting methodologies. Interest rates for the Treasury rate program are the prevailing cost of money to the U.S. Treasury for comparable terms.

Loan guarantees may be made for generation, transmission, or distribution facilities. The electric program approves guaranteed loans made through the FFB, National Rural Utilities Cooperative Finance Corporation (CFC), and the National Bank for Cooperatives (CoBank). The FFB interest rate is the prevailing cost of money to the U.S. Treasury for comparable terms, plus one-eighth of 1 percent. Interest rates for private lenders are the current competitive rate.

**MANAGEMENT'S DISCUSSION AND ANALYSIS OF  
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Telecommunications Program

In order meet the goal of increasing economic opportunity in rural America, USDA annually finances the deployment of a seamless, nation-wide telecommunications network. Without access to advanced telecommunications networks, rural America will suffer the consequences in the form of declining educational opportunities, inadequate health care, depressed economies, and high unemployment.

Since private capital for the deployment of broadband services in rural areas is not sufficient, incentives offered by Rural Development's RUS are more important than ever before. Providing rural residents and businesses with barrier-free access to the benefits of today's technology will bolster the economy and improve the quality of life for rural residents, and ultimately, increase not only economic opportunity in rural America, but to the Nation as a whole.

The RUS Telecommunications Program contains three major components: 1) loans for infrastructure improvement and expansion; 2) loans and grants for distance learning and telemedicine initiatives in rural areas; and 3) loans and grants specifically targeted for the deployment of broadband service in small towns and communities. Utilizing advanced telecommunications services, combined, these programs provide USDA with a powerful tool in building strong rural economies and increasing educational and health care services in rural communities across the U.S.

Key Performance Indicators	FY 2003 Target	FY 2003 Actual
Number of new subscribers receiving service	190,000	86,390
Number of subscribers with improved service	495,000	379,380
Leveraging of telecommunications financial assistance (private investment to RUS and RTB funding)	\$5:1	\$3.85 : 1

Neither target was met for number of improved and new subscribers. These targets were derived using past year's experience and by developing a per subscriber relationship to the amount of loan funds available in the year. While the actual amount of funds loaned in FY 2003 was near the anticipated amount used in developing the target, average amount of investment per subscriber increased substantially. This is a probable result of increased investment in system upgrades, replacements, and improvements versus actual loan funds for new subscribers. Since the calculation is based on the average for the previous year, a variance from year to year can be expected.

The leveraging performance indicator was not met. This indicator measures the extent to which borrowers are investing in plant with funds other than RUS funds. During the past year, a higher portion of funding was invested in plant from RUS and other government funds than from other sources. Several factors may contribute to this, including favorable terms associated with government loans (i.e., lower interest rates and longer maturities) and a desire to increase cash reserves through a conservative cash management approach (resulting in fewer dollars invested from general funds).

**MANAGEMENT'S DISCUSSION AND ANALYSIS OF  
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The Distance Learning and Telemedicine program continues its charge to wire our schools and improve health care delivery in rural America. This program is having a profound impact in rural America by assisting rural schools and learning centers in gaining access to improved educational resources, and by assisting rural hospitals and health care centers in gaining access to improved medical care. Building on advanced telecommunications infrastructure, telemedicine projects are providing new and improved health care services and benefits to rural residents, many in medically underserved areas by linking to urban medical centers for clinical interactive video consultation, distance training of rural health care providers, and access to medical expertise and library resources. Distance learning projects provide funding for computers and Internet hookups in schools and libraries and promote confidence in, and understanding of, the world-wide-web and its benefits to students and young entrepreneurs.

Key Performance Indicators	FY 2003 Target	FY 2003 Actual
Number of schools receiving distance learning facilities	800	590
Number of healthcare providers receiving telemedicine facilities	425	188
Leveraging of telemedicine and distance learning financial assistance (private investment to RUS funding)	\$:8:1	\$:8:1

Neither target was met for number of schools and health care providers receiving distance learning facilities. The primary reason is that the program only approved \$20.7 million in loans, leaving approximately \$279 million in unused lending authority.

The Farm Security and Rural Investment Act of 2002 (2002 Farm Bill) established a new loan and loan guarantee program "Access to Broadband Telecommunications Services in Rural Areas." This program is designed to provide funding for the cost of constructing, improving, and acquiring facilities and equipment for broadband service in rural communities of 20,000 inhabitants or less. Direct loans are made at the cost of money to the Treasury for the life of the facilities financed. Loans may be made at 4 percent to extremely rural communities where broadband service does not currently exist. Loan guarantees bear an interest rate set by the private lender consistent with the current applicable market rate for a loan of comparable maturity and are made for no more than 80 percent of the principal amount.

Key Performance Indicator	FY 2003 Target	FY 2003 Actual
Number of new subscribers receiving service through the Broadband loan program	1,834,779	2,849

The number of new Broadband subscribers was not met. This program was implemented January 30, 2003. As this is a new program with significantly different regulatory and statutory requirements from its predecessor "pilot program," eligible applicants need sufficient time to prepare and submit

## MANAGEMENT'S DISCUSSION AND ANALYSIS OF RURAL DEVELOPMENT'S CONSOLIDATED STATEMENTS

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applications in accordance with the new rules and regulations. Initially, many of the first applications received were determined to be incomplete because the applicants did not follow the new procedures. The application deadline for this year's funding was July 31, 2003. As such, the majority of the applications were not received until late July. Therefore, processing delays resulted from the delay in submission of applications and the initial delays in processing applications that were incomplete. Only two loans totaling approximately \$55 million were approved during FY 2003. The target was based on full utilization of approximately \$1.45 billion in loans.

The building and delivery of advanced telecommunications networks is having a profound effect on our Nation's economy, its strength, and its growth. Broadband networks in small, rural towns will facilitate economic growth and provide the backbone for the delivery of increased educational opportunities over state-of-the-art telecommunications networks. While rural America can be defined by various statistics – number of counties: 2,300; or percentage of landmass 80 percent -- the most important statistic is that rural America is home to 55 million people. Just as our citizens in our cities and suburbs benefit from access to broadband services, so should our rural residents. In rural America, access to broadband plays a vital role in solving the problems created by time, distance, location, and lack of resources. The promise of broadband is not just "faster access:" It means:

- New educational opportunities through distance learning – enabling rural students to take virtual field trips to places all over the world, from historic Williamsburg to the Louvre;
- Life saving medical treatment over telemedicine networks – allowing for specialists to guide surgeries hundreds of miles away; and
- Economic growth and new markets -- where businesses prosper and grow locally, while competing nationally and globally over high-speed networks and inter-connecting with suppliers, manufacturers, and consumers to optimize business strategies.

Today's advanced telecommunications networks will allow rural communities to become platforms of opportunity for new businesses to compete locally, nationally, and globally and ensure that no rural resident – from students to parents and teachers, from patients to doctors, or from consumers to entrepreneurs – will be left behind in this new century.

### Water and Environmental Programs

Water and Waste Disposal loans and grants are provided to rural communities for the development, replacement, or upgrading of water and environmental facilities. Direct loans are repayable up to 40 years. Water and Waste Disposal borrowers have received a total of \$29.5 billion in direct loans, loan guarantees, and grants as of September 30, 2003. During FY 2003, \$779 million in direct loans was approved, \$3.6 million in loans was guaranteed, and \$638 million in grants were awarded.

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One of the objectives of the Water and Environmental Program is to provide rural residents with modern and affordable water and waste disposal services. Another objective is to direct program resources to those rural communities with the greatest need. This includes rural communities that are poverty-stricken as a result of out-migration, natural disasters or economic stress due to Federal actions.

Key Performance Measures	FY 2003 Target	FY 2003 Actual
Loans to develop or expand rural water systems to provide quality drinking water in compliance with the Safe Drinking Water Act	510	518
Loans to develop or expand rural waste disposal systems to provide quality waste disposal service in compliance with State and Federal environmental standards	273	321
Direct program resources to persistent poverty counties (number and amount in millions)	114 \$180	174 \$176
Special initiatives – (number of projects and amount of funding in millions):		
EZ/EC	27 (\$26)	26 (\$39)
Colonias	32 (\$20)	27 (\$24)
Alaskan Village	23 (\$20)	32 (\$29)
Guaranteed Loans	6 (\$2)	4 (\$4)

The target for direct program resources to persistent poverty counties was exceeded for the number of loans by more than 50 percent but the dollar fell short of the goal by about two percent. Although the average cost of projects in persistent poverty counties was below expectations, overall the goal was met.

The target for the number of EZ/EC projects fell short by one; however, the dollar amount exceeded the goal by 50 percent. The average EZ/EC project cost exceeded expectations limiting the number of projects that could be funded with available resources.

The target for the number of Colonias' projects fell short by five; however, the dollar amount exceeded the goal by 20 percent. The average Colonias' project cost exceeded expectations limiting the number of projects that could be funded with available resources.

The target number for the guaranteed loans fell short by two; however, the dollar amount exceeded the goal by 100 percent. The demand for guaranteed loans is limited by our inability to effectively finance exempt bonds.



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***Office of Community  
Development***

Rural Development is dependent on the ability and skills of its staff for the effective delivery of its programs of technical assistance. The staff must be adequately trained and have the resources needed if it is to accomplish its job. Rural Development will utilize a management approach and encourage a workplace environment that ensures all customers and employees are treated fairly, equitably, and with dignity and respect.

Key Performance Indicators	FY 2003 Target	FY 2003 Actual
Ratio of non-EZ/EC grants to EZ/EC grants invested in EZ/EC communities	7:1 or greater	16.58:1
Number of jobs created in EZ/EC & REAP communities	1000	7,015

***Future Opportunities  
and Challenges***

Rural Development is subject to many of the changes occurring in society as a whole and was impacted by the events of September 2001. Other societal changes will potentially impact Rural Development programs and its operations in the future. Some opportunities and challenges resulting from these changes are summarized in the following areas:

**Technology**

Within Rural Development, initiatives such as the Data Warehouse provide employees with faster and easier access to data that crosses all business lines. Rural Development is supporting USDA eGovernment efforts and is participating in the eGrants and eLoans initiatives. Rural Development will interface with the eGrants storefront and accept grant applications submitted via the internet. Rural Development also currently offers via the internet in excess of 136 forms to the public. These forms can be completed online and electronically submitted to field service centers for processing. Rural Development is also promoting web-based business applications such as the capability to advertise and sell single family housing properties via the internet. This capability is being extended to the Farm Service Agency in the advertisement and sale of farm properties. Multi-Family Housing project management tenant data can now be entered via the internet and rental properties are being advertised via the internet to the public. Under development is an initiative to provide a web-based automated underwriting system to guaranteed loan lenders to allow them to more efficiently review and approve loan applications for Rural Development Single Family Housing Guaranteed loans.

Rural Development is currently developing tactical business plans for all major loan programs that will outline how current business processes will be transformed in order to electronically deliver programs directly to the public.

Rural Development is working with the Department of Agriculture, the Farm Service Agency, and the National Resource Conservation Service to deploy the secure technical infrastructure necessary to support the delivery of programs to

**MANAGEMENT'S DISCUSSION AND ANALYSIS OF  
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	<p>the public including authenticating customers. The initiative to provide communities with the telecommunication infrastructure to access the technologies we make available to them is virtually complete and authentication processes are being expanded to support trusted partner relationships.</p> <p>These initiatives will impact Rural Development's future policies and regulations, automated systems, and organizational structure.</p>
OMB Circular A-76 Competitive Sourcing	<p>Rural Development competitive sourcing goals for FY 2003 are on track. The Mission area met the fifteen percent goal established by the Department by September 30, 2003 and will study an additional ten percent of its commercial functions in FY 2004.</p>
Budget and Performance Integration	<p>Budget and Performance Integration is the fifth government-wide initiative in the President's Management Agenda. The initiative intends to provide a greater focus on performance, and to formally integrate the review of performance with budget decisions. This will require identifying high quality outcome measures, accurately monitoring the performance of programs, and measuring the total cost of programs.</p>
Pilot Loan Asset Sales	<p>Rural Development, along with the Farm Service Agency, should conduct a review and develop a pilot asset sale. The sale should include both performing and non-performing loans with a loan mix that results in the greatest budgetary savings for the Federal government. The total proceeds from the pilot loan sale should have a net savings, after factoring the cost of running the sale, of \$5 million. Work on this should begin in 2003 so that the actual sale can take place in early 2004.</p>
Market Globalization	<p>The advent of electronic commerce offers a great opportunity to rural businesses to participate in the global market, especially for the small entrepreneur or cooperative whose business is operating in a niche market. Electronic commerce eliminates factors such as geographical distance and small customer base which have historically limited the growth potential of rural businesses and communities.</p>
Farm Bill	<p>Passage of the Farm Security and Rural Development Act of 2002 had a broad impact on Rural Development programs and policies. The bill created a variety of new energy related and telecommunication programs and changed existing programs. This provides both an opportunity and a challenge to implement the provisions in a timely fashion to benefit the residents of rural America.</p>
Homeland Security	<p>The events of September 2001 had a significant impact on the citizens of the United States including Rural America. It resulted in a reevaluation of how we do business and how we would continue to do business in a time of national emergency.</p>
Diversity	<p>The racial and ethnic backgrounds of our rural customers and our employees will continue to become more diverse. Rural Development gives priority to ensuring all customers, including employees, are treated with dignity and respect. This priority must continue if Rural Development is to ensure its programs are delivered equitably and its workforce recognizes the value of a diverse staff.</p>

**MANAGEMENT'S DISCUSSION AND ANALYSIS OF  
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***Highlights of Rural  
Development's Financial  
Position***

The accompanying financial statements include the combined financial information for rural housing, rural utilities, and rural business and cooperative development programs.

**Limitations on Financial  
Statements**

These consolidated financial statements have been prepared to report the financial position and results of operations of the entity, pursuant to the requirements of the Chief Financial Officers Act of 1990. While the statements have been prepared from the books and records of the entity in accordance with the formats prescribed by the Office of Management and Budget, the statements are in addition to the financial reports used to monitor and control budgetary resources which are prepared from the same books and records. The statements should be read with the realization that they are a component of the U.S. Government, a sovereign entity. One implication of this is that liabilities cannot be liquidated without legislation that provides resources to do so.

***Entity's Systems, Controls  
And Legal Compliance***

The purpose of the Federal Managers' Financial Integrity Act (FMFIA) is to promote the development of systematic and proactive measures to ensure management accountability for the effectiveness and efficiency of program operations.

**Section 2**

Section 2 of the law focuses on the assessment of the adequacy of management controls to manage the risk associated with a given program and to provide reasonable assurance that obligations/costs comply with applicable laws and regulations; that Federal assets are safeguarded against fraud, waste and mismanagement; and that transactions are properly recorded and accounted for.

A material weakness identifies an instance in which the management controls are not sufficient to provide the level of assurance required by Section 2 and requires major milestones for corrective action. Such a weakness may significantly impair the fulfillment of an agency component's mission; deprive the public of needed services; violate statutory or regulatory requirements, significantly weaken safeguards against waste, loss, unauthorized use or misappropriation of funds, property, or other assets; or result in a conflict of interest.

For FY 2003, Rural Development is reporting three open material weaknesses. The weaknesses are related to: (1) weaknesses continue to exist in Rural Development's IT networks, (2) lack of adequate oversight and internal controls which has led to abuse by Multi-Family Housing program participants; and (3) weak access controls jeopardize the integrity and confidentiality of Rural Development's critical data.

Since the major portion of the corrective actions are in place for the above weaknesses, the impact on Rural Development operations and the public is reduced to the extent that these material weaknesses are not sufficiently serious

**MANAGEMENT'S DISCUSSION AND ANALYSIS OF  
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to prevent Rural Development from providing reasonable assurance that the mission area complies with Section 2 of the FMFIA.

Section 4

Section 4 of the law relates to the review of financial accounting systems to ensure conformance with certain principles, standards, and other Federal requirements. A financial system nonconformance is an instance in which the financial system does not conform to the requirements of Section 4. A nonconformance also requires major milestones for corrective action.

For FY 2003, we report that our financial management/accounting systems do not comply with Office of Management and Budget (OMB) Circular A-127, Financial Management System, requirements. The following is the basis for that conclusion: systems for servicing the RUS electric and telecommunication direct loan portfolio do not comply with OMB Circular A-127 as they are inefficient, labor intensive, and lack automated controls. All financial management systems have not been certified in compliance with OMB Circular A-130, Management of Federal Information Resources; and the Credit Reform processes and procedures need enhancements to estimate and re-estimate the cost of loans and loan guarantees.

**U.S. DEPARTMENT OF AGRICULTURE  
RURAL DEVELOPMENT  
CONSOLIDATED BALANCE SHEET  
AS OF SEPTEMBER 30, 2003 AND 2002**  
(In Millions)

<b>ASSETS (Note 2)</b>	<u>2003</u>	<u>2002</u>
Intragovernmental:		
Funds Balance with Treasury (Note 3)	\$ 9,593	\$ 8,783
Accounts Receivable (Note 5)	<u>62</u>	<u>5</u>
Total Intragovernmental	9,655	8,788
Cash and Other Monetary Assets (Note 4)	76	71
Accounts Receivable (Note 5)	1	2
Loans Receivable and Related Foreclosed		
Property, Net (Note 6)	56,306	57,944
General Property, Plant and Equipment, Net (Note 7)	47	32
Other (Note 8)	<u>37</u>	<u>36</u>
Total Assets	<u>\$ 66,122</u>	<u>\$ 66,873</u>
<b>LIABILITIES (Note 9)</b>		
Intragovernmental:		
Debt (Note 10)	\$ 49,869	\$ 49,892
Resources Payable to Treasury (Note 1Q)	7,704	8,281
Other (Note 12)	<u>480</u>	<u>772</u>
Total Intragovernmental	58,053	58,945
Accounts Payable	79	85
Loan Guarantee Liability (Note 6)	727	507
Debt Held by the Public (Note 10)	80	84
Stock Payable to RTB Borrowers (Note 11)	1,309	1,343
Other (Note 12)	<u>195</u>	<u>180</u>
Total Liabilities	\$ 60,443	\$ 61,144
Commitments and Contingencies (Note 13)		
<b>NET POSITION</b>		
Unexpended Appropriations	\$ 5,700	\$ 5,362
Cumulative Results of Operations	<u>(21)</u>	<u>367</u>
Total Net Position	<u>\$ 5,679</u>	<u>\$ 5,729</u>
Total Liabilities and Net Position	<u>\$ 66,122</u>	<u>\$ 66,873</u>

**The accompanying notes are an integral part of these statements.**

**U.S. DEPARTMENT OF AGRICULTURE  
RURAL DEVELOPMENT  
CONSOLIDATED STATEMENT OF NET COST  
FOR THE YEARS ENDED SEPTEMBER 30, 2003 AND 2002  
(In Millions)**

**Costs: (Note 14)**

<b>Program Costs:</b>	<u>2003</u>	<u>2002</u>
Intragovernmental Gross Costs	\$ 3,409	\$ 3,558
Less: Intragovernmental Earned Revenue (Note 15)	322	297
Intragovernmental Net Costs	<u>3,087</u>	<u>3,261</u>
Gross Costs with the Public:		
Grants and Payments	1,530	1,443
Loan Subsidy Costs	855	(374)
Other	2,265	3,077
Total Gross Costs with the Public	<u>4,650</u>	<u>4,146</u>
Less: Earned Revenues from the Public (Note 15)	3,998	4,047
Net Costs with the Public	<u>652</u>	<u>99</u>
<b>NET COST OF OPERATIONS</b>	<u>\$ 3,739</u>	<u>\$ 3,360</u>

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**The accompanying notes are an integral part of these statements.**

**U.S. DEPARTMENT OF AGRICULTURE  
RURAL DEVELOPMENT  
CONSOLIDATED STATEMENT OF CHANGES IN NET POSITION  
FOR THE YEARS ENDED SEPTEMBER 30, 2003 AND 2002  
(In Millions)**

	<u>2003 Cumulative Results of Operations</u>	<u>2003 Unexpended Appropriations</u>	<u>2002 Cumulative Results of Operations</u>	<u>2002 Unexpended Appropriations</u>
Beginning Balances	\$ 367	\$ 5,362	\$ (430)	\$ 5,256
Prior Period Adjustments (Note 16)	<u>0</u>	<u>0</u>	<u>11</u>	<u>0</u>
Beginning Balances, as Adjusted	367	5,362	(419)	5,256
Budgetary Financing Sources:				
Appropriations Received		3,211		2,930
Appropriations Transferred-in/out		18		8
Other Adjustments (rescissions, etc)	(15)	(66)		(53)
Appropriations Used	2,825	(2,825)	2,783	(2,779)
Transfers-in/out Without Reimbursement	446		1,364	
Other Budgetary Financing Sources	0		(104)	
Other Financing Sources:				
Imputed Financing from Costs Absorbed by Others	<u>95</u>		<u>103</u>	
Total Financing Sources	3,351	338	4,146	106
Net Cost of Operations	<u>3,739</u>		<u>3,360</u>	
Ending Balances	<u>\$ (21)</u>	<u>\$ 5,700</u>	<u>\$ 367</u>	<u>\$ 5,362</u>

**The accompanying notes are an integral part of these statements.**





**U.S. DEPARTMENT OF AGRICULTURE  
RURAL DEVELOPMENT  
COMBINED STATEMENT OF BUDGETARY RESOURCES  
FOR THE YEAR ENDED SEPTEMBER 30, 2003 AND 2002  
(In Millions)**

	<b>2003</b>	<b>2003 Non-Budgetary Credit Program Financing Accounts</b>	<b>2002</b>	<b>2002 Non-Budgetary Credit Program Financing Accounts</b>
	<u>Budgetary</u>	<u>Accounts</u>	<u>Budgetary</u>	<u>Accounts</u>
Status of Budgetary Resources:				
Obligations Incurred: (Note 17)				
Direct	\$ 4,872	\$ 10,064	\$ 5,242	\$ 10,160
Reimbursable	487	0	481	0
Subtotal	<u>5,359</u>	<u>10,064</u>	<u>5,723</u>	<u>10,160</u>
Unobligated Balance:				
Apportioned	317	1,043	207	274
Unobligated Balance Not Available	1,981	348	1,280	802
Total Status of Budgetary Resources	<u><u>7,657</u></u>	<u><u>11,455</u></u>	<u><u>7,210</u></u>	<u><u>11,236</u></u>
Relationship of Obligations to Outlays:				
Obligated Balance, Net, Beginning of Period	6,773	13,157	6,729	10,232
Obligated Balance, Net, End of Period:				
Accounts Receivable	(94)	(4)	(25)	0
Unfilled Customer Orders from Federal Resources	0	(714)	0	(666)
Undelivered Orders	6,599	15,105	6,360	13,823
Accounts Payable	411	2	438	0
Outlays:				
Disbursements	4,954	8,434	5,422	7,053
Collections	(6,382)	(4,471)	(5,877)	(3,635)
Subtotal	<u>(1,428)</u>	<u>3,963</u>	<u>(455)</u>	<u>3,418</u>
Less: Offsetting Receipts	790	0	356	0
Net Outlays	<u><u>\$ (2,218)</u></u>	<u><u>\$ 3,963</u></u>	<u><u>\$ (811)</u></u>	<u><u>\$ 3,418</u></u>

See required supplementary information at the end of these footnotes for a breakdown by major budget account.

**The accompanying notes are an integral part of these statements.**

**U.S. DEPARTMENT OF AGRICULTURE  
RURAL DEVELOPMENT  
CONSOLIDATED STATEMENT OF FINANCING  
FOR THE YEARS ENDED SEPTEMBER 30, 2003 AND 2002**  
(In Millions)

	<u>2003</u>	<u>2002</u>
<b>Resources Used to Finance Activities:</b>		
Budgetary Resources Obligated		
Obligations Incurred	\$ 15,423	\$ 15,883
Less: Spending Authority from Offsetting Collections and Recoveries	11,513	9,950
Obligations Net Offsetting Collections and Recoveries	<u>3,910</u>	<u>5,933</u>
Less: Offsetting Receipts	790	356
Net Obligations	<u>3,120</u>	<u>5,577</u>
Other Resources		
Imputed Financing from Costs Absorbed by Others	95	103
Net Other Resources Used to Finance Activities	<u>95</u>	<u>103</u>
<b>Total Resources Used to Finance Activities</b>	<b>3,215</b>	<b>5,680</b>
<b>Resources Used to Finance Items Not Part of the Net Cost of Operations:</b>		
Change in Budgetary Resources Obligated for Goods, Services and Benefits Ordered But Not Yet Provided	1,472	2,775
Resources That Fund Expenses Recognized in Prior Periods	344	371
Budgetary Offsetting Collections and Receipts That Do Not Affect Net Cost of Operations		
Credit Program Collections Which Increase Liabilities for Loan Guarantees or Allowances for Subsidy	(10,399)	(8,292)
Other	(790)	(356)
Resources That Finance the Acquisition of Assets	9,994	8,780
Other Resources or Adjustments to Net Obligated Resources That Do Not Affect Net Cost of Operations	<u>0</u>	<u>(11)</u>
<b>Total Resources Used to Finance Items Not Part of the Net Cost of Operations</b>	<b><u>621</u></b>	<b><u>3,267</u></b>
<b>Total Resources Used to Finance the Net Cost of Operations</b>	<b>2,594</b>	<b>2,413</b>
<b>Components of the Net Cost of Operations That Will Not Require or Generate Resources in the Current Period:</b>		
Components Requiring or Generating Resources in Future Periods:		
Increase in Annual Leave Liability	0	0
Upward/Downward Reestimates of Credit Subsidy Expense	418	(461)
Increase in Exchange Revenue Receivable From the Public	0	(35)
Other	<u>0</u>	<u>27</u>
Total Components of Net Cost of Operations That Will Require or Generate Resources in Future Periods	418	(469)
Components Not Requiring or Generating Resources:		
Depreciation and Amortization	4	2
Other	<u>723</u>	<u>1,414</u>
Total Components of Net Cost of Operations That Will Not Require or Generate Resources	<u>727</u>	<u>1,416</u>
<b>Total Components of Net Cost of Operations That Will Not Require or Generate Resources in the Current Period</b>	<b><u>1,145</u></b>	<b><u>947</u></b>
<b>Net Cost of Operations</b>	<b><u>\$ 3,739</u></b>	<b><u>\$ 3,360</u></b>

**The accompanying notes are an integral part of these statements.**

**RURAL DEVELOPMENT  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS  
AS OF SEPTEMBER 30, 2003**

**NOTE 1: SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES**

**A. Basis of Presentation**

These financial statements have been prepared to report the financial position and results of operations of the USDA Rural Development mission area, as required by the Chief Financial Officers Act of 1990. The financial statements have been prepared from the books and records in accordance with the Office of Management and Budget (OMB) Bulletin 01-09, *Form and Content of Agency Financial Statements*, and the accounting policies which are summarized in this note. These statements are, therefore, different from the financial reports, also prepared pursuant to OMB directives, that are used to monitor and control the use of budgetary resources.

The amounts in the fiscal year (FY) 2002 column of the Consolidated Statement of Financing have been reclassified due to evolving changes in the guidance for this statement. This reclassification will facilitate a meaningful comparison between FY's 2003 and 2002.

Certain items in the prior year have been reclassified to conform to the current presentation.

**B. Reporting Entity**

As of September 30, 2003, the mission area provides credit for housing, rural development, and rural utilities within the U.S. Department of Agriculture (USDA). When it began in 1935, under the name of the Resettlement Administration, the Agency's original function was to make loans and grants to depression-stricken families and help them regain self-sufficiency in making their living on family farms. In 1937, the Farm Security Administration (FSA) was created as successor to the Resettlement Administration. Its primary responsibilities were to make farm rehabilitation and farm ownership loans to farmers unable to borrow from usual sources of credit.

In 1946, Congress passed the Farmers Home Administration Act and the name "FHA" was adopted. The Act gave FHA the authority to administer farm ownership loans, farm operating loans, a limited water facilities loan program, and the emergency crop and feed loan program. FHA was also authorized to insure and guarantee loans made by banks, other agencies, private citizens, as well as to make direct Government loans.

During the 1960's, pursuant to the Housing Act of 1949, FHA was given the authority to administer direct and insured loans to repair or purchase new or existing housing to very low-income and low-income rural residents who could not obtain credit elsewhere. These loans provided rural residents with modest, safe, and sanitary single family dwellings at affordable rates and terms. In addition, FHA was granted authority to administer rental and cooperative housing loans, farm labor housing loans, and rural housing site loans to rural areas.

The agency was commonly known as "FHA" until April 1974 when USDA formally adopted "FmHA" as the agency's abbreviation. This was done to easily distinguish Farmers Home Administration from other agencies that have the same initials, such as the Federal Housing Administration and Federal Highway Administration.

The Rural Electrification Administration (REA) was established under the Rural Electrification Act of 1936 as a credit agency within the USDA which assisted rural electric and telephone utilities in obtaining the financing required to provide electric and telephone service in rural areas.

In 1971, the Rural Telephone Bank (RTB) was established within REA to provide a supplemental source of financing for rural telephone systems. In 1987, the program was further expanded to provide zero-interest loans and grants to its borrowers for the purpose of rural development.

In 1992, the Rural Development Agency (RDA) was established by the Food, Agriculture, Conservation and Trade (FACT) Act. RDA was a separate agency within the Department of Agriculture which provided funding for loans, grants, and loan guarantees for community development in rural areas. The Health and Human Services Act of 1986 authorized further rural development lending by instituting the Intermediary Relending Program. Under this program, RDA provided loans to public or private nonprofit organizations for the purpose of relending for business or community development in rural areas.

On October 13, 1994, the President signed the Federal Crop Insurance Reform and Department of Agriculture Reorganization Act of 1994, Public Law No. 103-354. The law permitted the reorganization of the Department, including the establishment of a subcabinet position, the restructuring of headquarter agencies and offices, continued reductions in the number of USDA personnel, and consolidation and closure of field office locations. This streamlining of the Department permitted USDA to deliver programs and services to the public in an efficient and cost-effective manner.

The Secretary of Agriculture abolished the position of Under Secretary of Agriculture for Small Community and Rural Development and the agencies of FmHA, RDA, and REA. At the same time, all activities related to farm loans were transferred to the Farm Service Agency. Of the subcabinet positions ordered by the Secretary, the Under Secretary of Agriculture for Rural Economic and Community Development was established. This name was later shortened to Rural Development during FY 1996. The following is a description of the services and activities over which the mission area has jurisdiction:

#### Rural Housing Service (RHS)

RHS is responsible for housing loan programs and grants formerly performed by FmHA and rural community facility loan programs formerly performed by RDA. Other related functions include hazard waste management allocated grants and the salaries and expenses account.

#### Rural Utilities Service (RUS)

RUS is responsible for electric and telephone loan programs, Rural Telephone Bank activities, and distance learning and medical link grants formerly performed by REA. RUS is also responsible for rural water and waste disposal loans and grants and other grants which include solid waste management and emergency community water assistance formerly performed by RDA. Other related functions include the Appalachian Regional Commission and Economic Development

Administration allocated grants, local television loan program, high energy cost grants, and the salaries and expenses account.

#### Rural Business - Cooperative Service (RBS)

RBS is responsible for business and industry loan programs, assistance programs for cooperatives, and activities of the Agricultural Cooperative Service, all of which were formerly performed by RDA. RBS is also responsible for rural economic development loans and grants formerly performed by REA. Other related functions include rural business enterprise and rural technology and cooperative development grants, and the salaries and expenses account.

The mission area is responsible for 109 accounting entities of various compositions and sizes which are used to make various loans and grants. As of September 30, 2003 and 2002, loan and grant obligations in the amount of \$13.1 billion and \$13.2 billion were incurred, respectively.

#### **C. Budgets and Budgetary Accounting**

The Federal Credit Reform Act of 1990 contained in the Omnibus Budget Reconciliation Act of 1990 requires substantial changes to the accounting system and in budget presentation for the loan programs previously under the ten revolving/credit funds. The ten funds are: (1) Rural Housing Insurance Fund, (2) Rural Water and Waste Disposal Loan Fund, (3) Rural Business and Industry Loan Fund, (4) Rural Community Facility Loan Fund, (5) Rural Development Insurance Fund, (6) Rural Development Loan Fund, (7) Rural Electrification and Telephone Revolving Fund, (8) Rural Communications Development Fund, (9) Rural Economic Development Subaccount, and (10) Rural Telephone Bank. The loan portfolio created in these funds prior to FY 1992 is maintained in the liquidating accounts. While no new loans or administrative expenses can be charged to the liquidating accounts, it represents the largest portion of the loan portfolio. Three additional accounts were created to cover loans made in FY 1992 and thereafter, as follows:

- The program account represents all subsidy costs and administrative expenses related to direct and guaranteed loan commitments made after FY 1991. Subsidy costs reflect the cost to the government for the credit program on a net present value basis. Administrative expenses are not included in the subsidy cost. The program account receives a current definite appropriation authority for obligations of subsidy payments and administrative expenses, and a permanent indefinite appropriation authority for reestimates of subsidy.
- The direct loan financing account records the obligations and cash flows associated with direct loan obligations made after FY 1991. Annually, Congress adopts an appropriation bill limiting the dollar amount of obligations for new loan making. New loans are also limited by a corresponding apportioned program subsidy. The direct loan financing account's loan disbursements are financed through subsidies received from the program accounts and Treasury borrowings. However, the total disbursements cannot exceed the appropriated amount, as previously allowed under revolving accounts.
- The guaranteed loan financing account records the cash flows associated with guaranteed loan commitments made after FY 1991. Congress' annual appropriation bill limiting guaranteed loan commitments and their corresponding apportioned program subsidies serve to limit the dollar

amount of obligations for new guaranteed loan commitments. Tracked cash flows include payments of default claims, receipts of fees on guaranteed loan commitments, collections on defaulted guaranteed loans and subsidy payments, and the reserve maintained to cover default payments. The disbursements for defaulted loans from the guaranteed financing account are financed through subsidies received from the program accounts, interest earned on the subsidy, and Treasury borrowings.

#### **D. Basis of Accounting**

Aided by studies and recommendations from the Federal Accounting Standards Advisory Board (FASAB), the Director of OMB and the Comptroller General published specific standards which constitute generally accepted accounting principles for the Federal Government and its component entities. This comprehensive set of accounting principles and standards must be followed by Federal entities. For those transactions deemed not addressed by FASAB pronouncements, accounting principles and standards published by authoritative standard-setting bodies and other authoritative sources shall be considered, depending upon their relevance in a particular set of circumstances.

Pre-Credit Reform and Post-Credit Reform nonfederal transactions are recorded on a cash accounting basis, except for the accrual of interest related to borrower loans; Federal transactions are recorded on an accrual accounting basis. Under the cash method, revenues are recognized when cash is received and expenses are recognized when they are paid. Budgetary accounting is also necessary to facilitate compliance with legal constraints and controls over the use of Federal funds.

All significant interfund and intrafund balances and transactions have been eliminated in the consolidation except for those Credit Reform transactions impacting the Statements of Budgetary Resources and Financing as currently required.

During FY's 2003 and 2002, no new Statements of Federal Financial Accounting Standards (SFFAS) were implemented due to the fact that either none were applicable or no changes were required.

#### **E. Revenues and Other Financing Sources**

##### Revolving/Credit Funds:

Beginning in FY 1992, the Balanced Budget Act of 1990, Title XIII of the Omnibus Budget Reconciliation Act of 1990, provided Credit Reform procedures which affected the financing of the revolving funds. Under Credit Reform, an appropriation is received in the year of loan-making sufficient to cover the subsidy cost of providing the loan. The subsidy cost is defined as the net present value, at the time of disbursement, of the difference between the Government's estimated cash disbursements for that loan and the Government's estimated cash inflows resulting from that loan (e.g., repayments of principal and interest, and other payments adjusted for estimated defaults, prepayments, fees, penalties, and other recoveries). Consequently, the implementation of Credit Reform has resulted in authorized appropriations which provide for estimated future losses as opposed to reimbursement for losses appropriations which provided for past losses actually sustained prior to FY 1992. In addition to subsidy appropriations, the other sources of funding for the revolving funds include borrowings from Treasury and borrower loan repayments.

General Funds:

Appropriations are provided by Congress on both an annual and multi-year basis to fund certain general funds and other expenses such as personnel and compensation and fringe benefits, rents, communications, utilities, other administrative expenses, and capital expenditures. The current budgetary process does not distinguish between capital and operating expenditures. For budgetary purposes, both are recognized as a use of budgetary resources as paid; however, for financial reporting purposes under accrual accounting, operating expenses are recognized currently while expenditures for capital and other long-term assets are capitalized and are not recognized as expenses until they are consumed during normal operations. Appropriations for general fund activities are recorded as a financing source when expended. Unexpended appropriations are recorded as Net Position.

**F. Fund Balance with Treasury**

All receipts and disbursements are processed by the U.S. Treasury which, in effect, maintains the appropriate bank accounts.

**G. Escrow Disbursement Account**

With the implementation of the Centralized Serving Center on October 1, 1996, the Rural Housing Service began collecting escrow payments (i.e., insurance and taxes) from new Single Family Housing borrowers. Existing borrowers, which were delinquent and required servicing actions, must also submit these escrow payments. These payments are deposited with the Trustee, Firststar Bank, a subsidiary of U.S. Bank. As Trustee, they are required to invest these funds and disburse them as stipulated in the Trust Agreement. As of September 30, 2003 and 2002, the balance in this account was \$76 million and \$71.1 million, respectively. This amount has been included in the Consolidated Balance Sheet on the Cash and Other Monetary Assets (**Note 2**) and Other Liabilities (**Note 12**) lines. It has also been included on the Cash line (**Note 4**).

**H. Direct Lending Activities**

Appropriated authority is received to make direct loans. These loans represent actual cash disbursements to borrowers which require repayment. Direct loans are only made if a borrower cannot secure adequate credit from other sources at reasonable rates and terms. Federal law provides for multiple servicing actions to assist financially troubled borrowers. The maintenance of detailed loan records consistent with the terms and conditions agreed upon with the borrower is required. The most significant of these actions include:

Interest Credit Program:

The interest credit program provides for contractual agreements with single family and rural rental housing borrowers to reduce the borrowers' effective interest rate to as low as 1 percent. Single family housing borrowers currently receiving interest credit will continue to receive it for the initial loan and any subsequent loan as long as they are eligible and remain on interest credit. Borrowers' incomes will be reviewed annually to determine whether eligibility for this payment subsidy is still warranted.

Payment Assistance:

This is a type of payment subsidy for single family housing borrowers who have never received interest credit or who have ceased receiving interest credit and at a later date again qualify for a payment subsidy. Borrowers' incomes will be reviewed annually to determine whether eligibility for this payment subsidy is still warranted.

For FY's 2003 and 2002, interest credit and payment subsidy granted under this program is approximately \$1.1 billion and \$1.1 billion, respectively.

Moratorium:

A moratorium is a period of up to 2 years during which scheduled payments are deferred for payment at a later date. Borrowers may apply for a postponement of payments if, due to circumstances beyond their control, they are unable to continue making scheduled payments on the loan without unduly impairing their standard of living. As of September 30, 2003 and 2002, the number of borrowers with a moratorium in effect were 2,037 and 1,594, respectively.

Delinquency Workout Agreements:

Borrowers with past due accounts may be offered the opportunity to avoid liquidation by entering into an agreement with RHS that specifies a plan for bringing the account current. To receive a delinquency workout agreement, the following requirements apply:

- A borrower who is able to do so will be required to pay the past-due amount in a single payment.
- A borrower who is unable to pay the past-due amount in a single payment must pay monthly all scheduled payments plus an agreed upon additional amount that brings the account current within 2 years or the remaining term of the loan, whichever is shorter.
- If a borrower becomes more than 30 days past due under the terms of a delinquency workout agreement, RHS may cancel the agreement.

As of September 30, 2003 and 2002, the number of borrowers which had received delinquency workout agreements were 5,452 and 5,241, respectively.

**I. Guaranteed Lending Activities**

Other lending activities include the guaranteed loans for single family housing, multi-family housing, and community programs. The term "guarantee" means "to guarantee the repayment of loans originated, held, and serviced by a private financial agency or other lender approved by the Secretary of Agriculture." Rural Development provides financial assistance to borrowers by guaranteeing loans made by federal or state chartered banks, savings and loan associations, cooperative lending agencies, or approved lending institutions who perform all loan servicing activities. Generally, the guaranteed loan program allows Rural Development to guarantee up to 90 percent of the money loaned by a financial institution (lender) to borrowers in rural areas or to businesses who employ people in rural areas.

Some guaranteed loans may be sold in the secondary market by the lender to an institution (referred to as a holder). However, all servicing responsibilities remain with the lender. Payments by the borrower are forwarded on a pro rata basis to the holder. If the holder does not receive



payments on the note within 60 days of an installment due date, the holder can demand the Rural Development purchase the holder's share of the loan. When the loan is purchased, Rural Development assumes the rights of the holder and is entitled to the pro rata share of any payments made by the borrower to the lender. All guaranteed loans which are repurchased are treated as an asset (loans receivable) in the portfolio **(Note 6)**.

Lenders are required to inform Rural Development on the loan status of community and business program borrowers as of December 31 and June 30, and single family housing borrowers on a quarterly basis unless the loan is in default which requires more frequent reporting. If a borrower defaults on the loan, the lender is responsible for liquidating the collateral. After the proceeds of the sale have been applied to the outstanding balances, Rural Development is liable for losses under the terms of the guarantee.

Rural Development also provides financial assistance in the form of loan guarantees to rural electric and telephone utilities. Guaranteed loans are accounted for as contingent liabilities **(Note 6)**.

#### **J. Loans Receivable and Related Foreclosed Property, Net**

Loans are accounted for as receivables after funds have been disbursed. They are carried at their principal amount outstanding **(Note 6)**, and accrue interest daily based on the contractual interest rate. When a loan becomes nonperforming (in excess of 90 days delinquent or when borrowers enter into troubled debt restructuring arrangements), all interest previously accrued on the loan is reversed for financial reporting purposes, and interest income on the nonperforming loan is then recognized only to the extent of the collections received. Nonperforming loans are reclassified as performing and accrue interest when they become current or less than 90 days delinquent. In addition, interest income recognition subsequent to troubled debt restructuring arrangements is generally limited to actual cash interest received from these borrowers.

Direct loans obligated prior to October 1, 1991, are reported at the present value method. The provision calculation for FY 2003 is based upon the weighted-average subsidy rate of financing account cohorts which have been substantially disbursed. In the case of most loan programs, substantially disbursed will be 90 percent. This methodology was used during FY 2003 and is different from that which was employed during FY 2002. The provision calculation for FY 2002 is based upon projected cash flows discounted at the weighted-average rate of the outstanding Treasury and Federal Financing Bank borrowings made prior to FY 1992.

The liability for loan guarantees and for guaranteed loans obligated prior to October 1, 1991, are reported at present value which is the same methodology used by the direct loan programs for FY 2003. For the FY 2002 financial statements, the provision calculation is based upon future cash flows discounted at the average interest rate of the U.S. Treasury interest-bearing debt. The estimate is reported as an expense, and a corresponding accrual for estimated losses on loan guarantees is reported as a liability on the Consolidated Balance Sheet.

The projected cost of direct loan and guaranteed loan defaults (for loans obligated prior to October 1, 1991) will not necessarily reflect Rural Development's future appropriation requests. To the extent that revolving fund revenues are not sufficient to fund future costs, financing will have to

be obtained from future appropriations, or other congressionally-approved sources. For direct loans obligated on or after October 1, 1991, Rural Development recognizes these as assets at the present value of their estimated net cash inflows. The difference between the outstanding principal of the loans and the present value of their net cash inflows is recognized as a subsidy cost allowance. For guaranteed loans obligated on or after October 1, 1991, the present value of estimated net cash outflows of the loan guarantees is recognized as a liability.

#### **K. Investments**

In FY 1987, a loan asset sale was conducted as required in the Omnibus Budget Reconciliation Act of 1986. As a result of these sales, residual investments were maintained in the securities. A description of these investments is included in **Note 8**.

#### **L. Property, Plant and Equipment (PP&E)**

The land, buildings, and equipment in the current operating environment is provided by the General Services Administration, who charges a Standard Level Users Charge that approximates the commercial rental rates for similar properties. Under Credit Reform, all equipment purchases are made through the Salaries and Expense fund. See **Note 7** for the capitalization thresholds of the various classes of PP&E.

#### **M. Internal Use Software**

Internal Use Software is classified as "general property, plant and equipment" as defined in the Statement of Federal Financial Accounting Standard (SFFAS) #6, Accounting for Property, Plant and Equipment. See **Note 7** for further information.

Costs of internal use software are accounted for in accordance with SFFAS #10, Accounting for Internal Use Software. SFFAS #10 requires the capitalization of the cost of internal use software whether it is commercial off-the-shelf, contractor-developed, or internally-developed which solely meets internal or operational needs.

SFFAS #10 provides for the capitalization of costs incurred during the software development phase and the expensing of costs incurred during the preliminary design and post-implementation/operational phases for software having a useful life of at least 2 years. The capitalization threshold is \$100,000.00.

Costs incurred prior to the initial application of this standard, whether or not capitalized, should not be adjusted to the amounts that would have been capitalized, had this Standard been in effect when those costs were incurred.

#### **N. Liabilities**

Liabilities represent the amount of monies or other resources that are likely to be paid as the result of a transaction or event that has already occurred. However, no liability can be paid absent an appropriation. Where an appropriation has not been enacted, liabilities are considered not covered by budgetary resources. There is no certainty that appropriations will be enacted. Also, liabilities arising from other than contracts can be abrogated by the Government, acting in its sovereign capacity.

#### **O. Borrowings/Interest Payable to the Treasury**

Borrowings payable to the Treasury result from the Secretary of Agriculture's authority to make and issue notes to the Secretary of the Treasury for the purpose of discharging obligations for the revolving funds. These revolving funds make periodic principal and interest payments to Treasury in accordance with established agreements.

#### **P. Federal Employee's Compensation Act (FECA)**

This Act established the Federal Employees' Compensation Special Benefit Fund. This Fund pays for income lost and medical costs for federal civilian employees injured on the job, employees who have incurred a work-related occupational disease and beneficiaries of employees whose death is attributable to a job-related injury or occupational disease.

This Fund pays benefits on behalf of Federal entities as costs are incurred and bills (charges back) the Federal entity annually (August 15) for the costs incurred during the previous fiscal year ended June 30 (July 1 - June 30). Federal entities fund the FECA payments through appropriations or operating revenues. For appropriated funds, the payment is due at the beginning of the second fiscal year after receipt of the bill (approximately 15 months). These liabilities due to the Fund are recorded by Federal entities as unfunded (if annual appropriations are used) at the time of receipt of the bill. Generally, Federal entities with no-year appropriations should recognize a funded liability and the funding availability at the time of the receipt of the chargeback from the Department of Labor (DOL).

Annually, Federal entities are also allocated a portion of the long term FECA actuarial liability attributable to the entity. The liability is calculated to estimate the expected liability for death, disability, medical and miscellaneous costs for approved compensation cases. The liability amounts and the calculation methodologies are provided by DOL to the Federal entities by October 31 for the previous fiscal year ended September 30.

On or before August 15 of each year, DOL submits a yearly billing (chargeback) report to Federal entities. The report is entitled Notification of Workers' Compensation Cost Incurred on Your Behalf (annual chargeback report) and covers the preceding July 1 through June 30 fiscal year. Additionally, each entity receives a quarterly Detailed Chargeback Report. The quarterly report provides a detailed listing of amounts paid by the FECA fund during the previous quarter. The current year FECA expense and total liability are calculated using information contained in these reports.

#### **Q. Resources Payable to Treasury**

Prior to FY 1999, Rural Development consolidated all unobligated net resources of loans obligated prior to FY 1992 as either a Receivable from Appropriations (negative equity) or Resources Payable to Treasury (positive equity). All other capital accounts were transferred to these accounts.

Beginning in FY 1999, agencies can no longer accrue a Receivable from Appropriations, as required in Statement of Federal Financial Accounting Standard #7, Accounting for Revenue and Other Financing Sources, unless prior approval is received from OMB and Treasury. As a result, all unobligated net

resources of loans obligated prior to FY 1992 are now consolidated as a negative Resources Payable to Treasury.

The FY 2003 financial statements include formal budget reestimates for all programs as of September 30, 2002, with the exception of the Rural Telephone Bank direct loan program, the Section 502 Single Family Housing direct loan program, and the Section 515 Multi-Family Housing direct loan program which were included in the FY 2002 financial statements. Also included in FY 2003 financial statement reporting, reestimates were estimated as of September 30, 2003, for all major loan programs.

The FY 2002 financial statements include formal budget reestimates for the Rural Telephone Bank direct loan program, the Section 502 Single Family Housing direct loan program, and the Section 515 Multi-Family Housing direct loan program as of September 30, 2002. The statements also include formal budgetary reestimates for all other programs as of September 30, 2001. Additionally, for financial statement reporting, reestimates were estimated as of September 30, 2002, for all other major loan programs.

#### **R. Contingencies**

The Rural Development mission area is a party in various legal actions and claims through the normal course of its operations. In the opinion of management and the USDA Office of the General Counsel, the ultimate resolution of these legal actions and claims will not materially affect the financial position or results of operations (**Note 13**).

#### **S. Capital Stock Class A**

Rural Development owns all Class A stock on behalf of the United States Government and any cash dividends are paid to the U.S. Treasury. Public Laws 92-12 and 97-98 authorized Congress, in FY's 1971 through 1991, to appropriate no more than \$30 million per year for the purchase of RTB Class A stock, a nonvoting class of stock. Class A stock has a guaranteed annual dividend of 2 percent of the total funds received. The law provides that Congress annually appropriate funds until such purchases approximate \$600 million. The total amount of RTB Class A stock appropriations received is \$592.1 million and no future appropriations are anticipated. Beginning in 1996, RTB is required to repurchase this stock from Rural Development; however, in accordance with Public Law 105-86, the maximum Class A stock that may be retired is 5 percent. According to enabling legislation and amendments, the Bank will be converted to independent status when 51 percent of the Class A stock issued to the United States has been fully redeemed and retired. On September 30, 2003 and 2002, in accordance with Bank Board resolutions 2003-2 and 2002-4, the eighth and seventh redemptions of Class A stock, in the amounts of \$21.5 million and \$22.7 million occurred, leaving balances of \$408.7 million and \$430.2 million outstanding, respectively which has been eliminated in the consolidation.

#### **T. Unexpended Appropriations**

Unexpended Appropriations include the undelivered orders and unobligated balances of the general funds and the program accounts which receive Congressional appropriations through the budgetary process. As appropriated funds incur obligations, the obligated amount is recorded as an undelivered order. Undelivered orders are reduced by either an expenditure or an obligation cancellation. Appropriated funds which are not obligated are

treated as unobligated amounts. At the end of the fiscal year, certain multi-year appropriations which have unobligated balances remain available for obligation in future periods. Unobligated appropriations are returned to the U.S. Treasury when their period of availability expires.

#### **U. Intragovernmental Financial Activities**

The Rural Development mission areas is an integral part of the operations of the U.S. Department of Agriculture (USDA) and may thus be subject to financial and managerial decisions and legislative requirements which are beyond the control of the Agency's management. Consequently, day-to-day operations may not be conducted as they would if Rural Development were a separate and independent entity.

Beginning in FY 1998, USDA has provided mission areas with an allocation of departmental nonreimbursed appropriated costs to include in their financial statements. These costs affect the Statement of Net Cost, Statement of Changes in Net Position, and the Statement of Financing.

The consolidated financial statements are not intended to report the mission area's proportionate share of the Federal deficit or of public borrowing, including interest thereon. Financing for budget appropriations could derive from tax revenues or public borrowing or both; the ultimate source of this financing, whether from tax revenues or public borrowing, has not been specifically allocated to Rural Development.

The majority of employees participate in the Civil Service Retirement System (CSRS), to which Rural Development makes matching contributions equal to 7 percent of pay. Rural Development does not report CSRS assets, accumulated plan benefits, or unfunded liabilities, if any, applicable to its employees. Reporting of such amounts is the responsibility of the Office of Personnel Management.

On January 1, 1987, the Federal Employees Retirement System (FERS) went into effect pursuant to Public Law 99-335. Most employees hired after December 31, 1983, are automatically covered by FERS and Social Security. Employees hired prior to January 1, 1984, could elect to either join FERS and Social Security or remain in CSRS. A primary feature of FERS is that it offers a savings plan to which the agencies automatically contribute 1 percent of pay and matches any employee contribution up to an additional 4 percent of pay.

Annual leave is accrued as it is earned and the accrual is reduced as leave is taken. Each year, the balance in the accrued annual leave account is adjusted to reflect current pay rates. To the extent current or prior year appropriations are not available to fund annual leave earned but not taken, funding will be obtained from future financing sources. Sick leave and other types of nonvested leave are expensed as taken.

**NOTE 2: NON-ENTITY ASSETS**

*Amounts are presented in millions.*

	<u>2003</u>	<u>2002</u>
<b><u>With the Public</u></b>		
Cash and Other Monetary Assets	\$ 76	\$ 71
Total Non-Entity Assets	76	71
Total Entity Assets	66,046	66,802
Total Assets	<u>\$66,122</u>	<u>\$66,873</u>

See **Note 1G** for a description of Cash and Other Monetary Assets.

Non-Entity Assets represent assets that are "not for use" by Rural Development.

**NOTE 3: FUND BALANCE WITH TREASURY**

*Amounts are presented in millions.*

<b>Fund Balances:</b>	<u>2003</u>	<u>2002</u>
Revolving Funds	\$ 3,153	\$ 2,678
Appropriated Funds	6,442	6,109
Other Fund Types	(2)	(4)
Total	<u>\$ 9,593</u>	<u>\$ 8,783</u>

**Status of Fund Balance with Treasury:**

Unobligated Balance:		
Available	\$ 896	\$ 847
Unavailable	57	944
Unavailable - Restricted	1,747	93
Obligated Balance Not Yet Disbursed	6,892	6,903
Clearing Account Balances	1	(4)
Total	<u>\$ 9,593</u>	<u>\$ 8,783</u>

Represents the undisbursed account balances with the U.S. Treasury as reported in the mission area's records.

The amounts included on the Unavailable - Restricted line are limited in their future use and are not apportioned for current use. These amounts represent the expired authority in fixed year Grant and Program accounts (fixed year's prior to FY 2003) and are only available for restoration of funds. After the fifth year of expiration, all funds are returned to Treasury as required except those entities having extended authority.

**NOTE 4: CASH AND OTHER MONETARY ASSETS**

*Amounts are presented in millions.*

	<u>2003</u>	<u>2002</u>
Cash	\$ 76	\$ 71
Total Cash and Other Monetary Assets	<u>\$ 76</u>	<u>\$ 71</u>

See **Note 1G** for a description of this Cash. As discussed in **Note 2**, this Cash is unavailable for Agency use.

**NOTE 5: ACCOUNTS RECEIVABLE, NET**

*Amounts are presented in millions.*

	<u>2003</u>		
	<u>Accounts Receivable, Gross</u>	<u>Allowance for Uncollectible Accounts</u>	<u>Accounts Receivable, Net</u>
<b><u>Intragovernmental</u></b>			
A/R Revenue, Refund, Reimbursements	\$ 62	\$ 0	\$ 62
Total Intragovernmental Accounts Receivable	62	0	62
<b><u>With the Public</u></b>			
Audit Receivable	1	0	1
Total Accounts Receivable	<u>\$ 63</u>	<u>\$ 0</u>	<u>\$ 63</u>
	<u>2002</u>		
	<u>Accounts Receivable, Gross</u>	<u>Allowance for Uncollectible Accounts</u>	<u>Accounts Receivable, Net</u>
<b><u>Intragovernmental</u></b>			
A/R Revenue, Refund, Reimbursements	\$ 5	\$ 0	\$ 5
Total Intragovernmental Accounts Receivable	5	0	5
<b><u>With the Public</u></b>			
A/R Revenue, Refund, Reimbursements	1	0	1
Audit Receivable	1	0	1
Total Accounts Receivable	<u>\$ 7</u>	<u>\$ 0</u>	<u>\$ 7</u>

As of September 30, 2003 and 2002, the establishment of an allowance for uncollectible amounts was deemed unnecessary.

## **NOTE 6. LOANS RECEIVABLE AND RELATED FORECLOSED PROPERTY, NET**

### **Balance Sheet Review**

#### Direct Loans

Direct loan obligations or loan guarantee commitments made pre-1992 and the resulting direct loans or loan guarantees are reported at net present value.

Direct loan obligations or loan guarantee commitments made post-1991, and the resulting direct loan or loan guarantees, are governed by the Federal Credit Reform Act of 1990 as amended. The Act requires agencies to estimate the cost of direct loans and loan guarantees at present value for the budget. Additionally, the present value of the subsidy costs (i.e. interest rate differentials, interest subsidies, delinquencies and defaults, fee offsets and other cash flows) associated with direct loans and loan guarantees are recognized as a cost in the year the loan or loan guarantee is disbursed. The net present value of loans or defaulted guaranteed loans receivable at any point in time is the amount of the gross loan or defaulted guaranteed loans receivable less the present value of the subsidy at that time.

The net present value of loans receivable is not necessarily representative of the proceeds that might be expected if these loans were sold on the open market.

Loans receivable and related foreclosed property, net balances at the end of FY 2003 were \$56 billion compared to \$58 billion at the end of FY 2002. Defaulted guaranteed programs were \$187 million and \$79 million at the end of FY's 2003 and 2002, respectively. Table 1 below illustrates the overall composition of the Rural Development loan portfolio by mission area and loan program for FY 2003.

During the fiscal year, the gross outstanding balance of the direct loans obligated post-1991 is adjusted by the value of the subsidy cost allowance held against those loans. Current year subsidy expense, modifications, and reestimates all contribute to the change of the subsidy cost allowance throughout the year. The subsidy cost allowance moved from \$3.8 billion to \$4.2 billion during FY 2003, an increase of \$400 million. During FY 2002, the allowance decreased \$491 million. Table 2 shows the reconciliation of subsidy cost allowance balances from FY 2002 to FY 2003.

Total direct loan subsidy expense for FY 2003 is a combination of subsidy expense for new direct loans disbursed in the current year, modifications to existing loans, and interest rate and technical reestimates to existing loans. Total direct loan subsidy expense in FY 2003 was \$629 million compared to \$-68 million in FY 2002, an increase of \$697 million. This increase is largely due to the Housing and Electric loan programs. Table 3 illustrates the breakdown of total subsidy expense for FY's 2003 and 2002 by program.

Direct loan volume increased from \$4.6 billion in FY 2002 to \$5.5 billion in FY 2003. This increase was largely due to a \$927 million increase in Electric loans disbursed in FY 2003. Volume distribution between programs is shown in Table 4.



**Table 1****Total Credit Program Receivables and Related Foreclosed Property (in millions)****FY 2003**

<b>Direct Loans</b>	<b>Loans Receivable, Gross</b>	<b>Interest Receivable</b>	<b>Foreclosed Property</b>	<b>Present Value Allowance</b>	<b>Value of Assets</b>
<b>Obligated Pre-1992</b>					
Housing Loans	13,885	117	30	(5,760)	8,272
Electric Loans	15,262	6	0	(1,935)	13,333
Telecommunications Loans	1,843	1	0	(147)	1,697
Rural Telephone Bank	476	1	0	12	489
Rural Development *	2,463	25	0	(396)	2,092
Development Loan Funds	58	0	0	(29)	29
Other Programs	4	0	0	0	4
<b>Pre-1992 Total</b>	<b>33,991</b>	<b>150</b>	<b>30</b>	<b>(8,255)</b>	<b>25,916</b>
<b>Obligated Post-1991</b>					
Housing Loans	12,144	53	30	(1,872)	10,355
Community Facility Loans	1,290	15	1	(108)	1,198
Electric Loans	12,413	198	0	(1,113)	11,498
Telecommunications Loans	1,737	1	0	(46)	1,692
Rural Telephone Bank	328	0	0	(2)	326
Water and Environmental Loans	5,565	49	0	(809)	4,805
Development Loan Funds	347	2	0	(150)	199
Business & Industry Funds	105	0	0	(39)	66
Economic Development	74	0	0	(10)	64
<b>Post-1991 Total</b>	<b>34,003</b>	<b>318</b>	<b>31</b>	<b>(4,149)</b>	<b>30,203</b>
<b>Total Direct Loan Receivables</b>	<b>67,994</b>	<b>468</b>	<b>61</b>	<b>(12,404)</b>	<b>56,119</b>
<b>Defaulted Guaranteed Loans</b>					
<u>Pre-1992</u>					
Rural Development Insurance Fund	4	1	0	0	5
<u>Post-1991</u>					
Community Facilities	0	0	0	0	0
Business & Industry	189	3	0	(10)	182
<b>Total Defaulted Guaranteed Loans</b>	<b>193</b>	<b>4</b>	<b>0</b>	<b>(10)</b>	<b>187</b>
<b>Total Loans Receivable and Related Foreclosed Property, Net</b>					<b>56,306</b>

\* Prior to Credit Reform, Water and Environmental, Business and Industry and Community Facilities were combined under one Treasury symbol and fund.

**FY 2002**

<b>Direct Loans</b>	<b>Loans Receivable, Gross</b>	<b>Interest Receivable</b>	<b>Foreclosed Property</b>	<b>Present Value Allowance</b>	<b>Value of Assets</b>
<b>Obligated Pre-1992</b>					
Housing Loans	14,957	108	39	(5,178)	9,926
Electric Loans	17,337	42	0	(1,682)	15,697
Telecommunications Loans	2,076	5	0	(245)	1,836
Rural Telephone Bank	680	2	0	53	735
Rural Development *	2,802	30	0	(12)	2,820
Development Loan Funds	61	0	0	(20)	41
Other Programs	7	0	0	(2)	5
<b>Pre-1992 Total</b>	<b>37,920</b>	<b>187</b>	<b>39</b>	<b>(7,086)</b>	<b>31,060</b>
<b>Obligated Post-1991</b>					
Housing Loans	12,055	51	32	(2,059)	10,079
Community Facility Loans	1,135	13	3	(112)	1,039
Electric Loans	9,696	4	0	(536)	9,164
Telecommunications Loans	1,533	2	0	(24)	1,511
Rural Telephone Bank	334	0	0	(11)	323
Water and Environmental Loans	5,055	55	0	(754)	4,356
Development Loan Funds	335	2	0	(150)	187
Business & Industry Funds	113	2	0	(34)	81
Economic Development	77	0	0	(12)	65
<b>Post-1991 Total</b>	<b>30,333</b>	<b>129</b>	<b>35</b>	<b>(3,692)</b>	<b>26,805</b>
<b>Total Direct Loan Receivables</b>	<b>68,253</b>	<b>316</b>	<b>74</b>	<b>(10,778)</b>	<b>57,865</b>
<b>Defaulted Guaranteed Loans</b>					
<u>Pre-1992</u>					
Rural Development Insurance Fund	12	0	0	(9)	3
<u>Post-1991</u>					
Community Facilities	4	0	0	0	4
Business & Industry	180	0	0	(108)	72
<b>Total Defaulted Guaranteed Loans</b>	<b>196</b>	<b>0</b>	<b>0</b>	<b>(117)</b>	<b>79</b>
<b>Total Loans Receivable and Related Foreclosed Property, Net</b>					<b>57,944</b>

\* Prior to Credit Reform, Water and Environmental, Business and Industry and Community Facilities were combined under one Treasury symbol and fund.

**Table 2****Schedule for Reconciling Subsidy Cost Allowance Balances (Post-1991 Direct Loans)  
(in millions)**

<b>Beginning Balance, Changes, and Ending Balance</b>	<b>FY 2003</b>	<b>FY 2002</b>
<b>Beginning Balance of the subsidy cost allowance</b>	3,800	4,291
Add: Subsidy expense for direct loans disbursed during the year by component		
Interest rate differential costs	113	337
Default costs (net of recoveries)	29	25
Fees and other collections	(32)	(76)
Other subsidy costs	225	46
<b>Total of the above subsidy expense components</b>	<b>335</b>	<b>332</b>
Adjustments		
Fees received	13	11
Loans written off	(81)	(117)
Subsidy allowance amortization	(87)	(407)
Other	(115)	90
<b>Ending balance of the subsidy cost allowance before reestimates</b>	<b>3,865</b>	<b>4,200</b>
Add or subtract subsidy reestimates by component		
Interest rate reestimate	135	188
Technical/default reestimate	159	(588)
<b>Total of the above reestimate components</b>	<b>294</b>	<b>(400)</b>
<b>Ending balance of the subsidy cost allowance</b>	<b>4,159</b>	<b>3,800</b>

**Table 3**

**Direct Loan Subsidy Expense by Program and Component**  
(in millions)

CURRENT REPORTING YEAR	Subsidy Expense for New Direct Loans Disbursed					Reestimates			GRAND TOTAL
	Interest Differential	Defaults	Fees and Other Colls	Other	Total	Interest Rate	Technical	Total	
<b>Direct Loan Programs</b>									
Housing Loans	11	23	(32)	231	233	4	(192)	(188)	<b>45</b>
Community Facility Loans	18	1	0	(1)	18	1	(8)	(7)	<b>11</b>
Electric Loans	(19)	4	0	(2)	(17)	94	359	453	<b>436</b>
Telecommunications Loans	2	0	0	0	2	6	30	36	<b>38</b>
Rural Telephone Bank	1	0	0	0	1	0	(6)	(6)	<b>(5)</b>
Water and Environmental Loans	85	1	0	(3)	83	39	(36)	3	<b>86</b>
Development Loan Funds	12	0	0	0	12	(6)	3	(3)	<b>9</b>
Business & Industry Funds	0	0	0	0	0	(3)	10	7	<b>7</b>
Economic Development	3	0	0	0	3	0	(1)	(1)	<b>2</b>
<b>Total Subsidy Expense, Direct Loans</b>	<b>113</b>	<b>29</b>	<b>(32)</b>	<b>225</b>	<b>335</b>	<b>135</b>	<b>159</b>	<b>294</b>	<b>629</b>

PRIOR REPORTING YEAR	Subsidy Expense for New Direct Loans Disbursed					Reestimates			GRAND TOTAL
	Interest Differential	Defaults	Fees and Other Colls	Other	Total	Interest Rate	Technical	Total	
<b>Direct Loan Programs</b>									
Housing Loans	220	13	(75)	51	209	(47)	(422)	(469)	<b>(260)</b>
Community Facility Loans	18	1	(1)	0	18	3	(15)	(12)	<b>6</b>
Electric Loans	(2)	2	0	(2)	(2)	209	(117)	92	<b>90</b>
Telecommunications Loans	4	0	0	0	4	3	(5)	(2)	<b>2</b>
Rural Telephone Bank	1	0	0	0	1	1	(3)	(2)	<b>(1)</b>
Water and Environmental Loans	82	1	0	(3)	80	22	(27)	(5)	<b>75</b>
Development Loan Funds	16	0	0	0	16	0	(2)	(2)	<b>14</b>
Business & Industry Loans	(6)	8	0	0	2	(3)	4	1	<b>3</b>
Economic Development	4	0	0	0	4	0	(1)	(1)	<b>3</b>
<b>Total Subsidy Expense, Direct Loans</b>	<b>337</b>	<b>25</b>	<b>(76)</b>	<b>46</b>	<b>332</b>	<b>188</b>	<b>(588)</b>	<b>(400)</b>	<b>(68)</b>

**Table 4****Total Amount of Direct Loans Disbursed (Post-1991) (in millions)**

<b>Direct Loans</b>	<b>Current Year</b>	<b>Prior Year</b>	<b>Current Year Over (Under) Prior Year</b>
Housing Loans	1,163	1,207	(44)
Community Facility Loans	228	201	27
Electric Loans	3,007	2,080	927
Telecommunications Loans	300	368	(68)
Rural Telephone Bank	56	60	(4)
Water and Environmental Loans	754	643	111
Development Loan Funds	26	34	(8)
Business & Industry Loans	2	36	(34)
Economic Development	11	17	(6)
<b>Total Direct Loans Disbursed</b>	<b>5,547</b>	<b>4,646</b>	<b>901</b>

**Guaranteed Loans**

Rural Development offers both direct and guaranteed loan products which are administered in coordination with conventional agricultural lenders for up to 90 percent of the principal loan amount. Under the guaranteed loan programs, the lender is responsible for servicing the borrower's account for the life of the loan. The agency, however, is responsible for ensuring borrowers meet certain qualifying criteria to be eligible and monitoring the lender's servicing activities. Borrowers interested in guaranteed loans must apply to a conventional lender, which then arranges for the guarantee with the agency. Guaranteed loans are reflected on the balance sheet in two ways: estimated losses on loan credit guarantees must be valued and carried as a liability and guaranteed loans purchased from third party holders are carried at net realizable value in loans receivable and related foreclosed property, net.

Guaranteed loans outstanding at the end of FY 2003 remained comparable to the FY 2002 portfolio. At the end of FY 2003 and FY 2002, there was \$18.4 billion in outstanding principal (face value) and \$16 billion in outstanding principal (guaranteed). Table 5 shows the outstanding balances by loan program.

During the fiscal year, the value of the guaranteed loans is adjusted by the value of the loan guarantee liability held against those loans. Current year subsidy expense and reestimates all contribute to the change of the loan guarantee liability through the year. The loan guarantee liability is a combination of the liability for losses on pre-1992 guarantees and post-1991 guarantees. The total liability moved from \$507 million to \$727 million during FY 2003, an increase of \$220 million. The post-1991 liability moved from \$477 million to \$724 million, an increase of \$247 million. Table 6 shows the reconciliation of loan guarantee liability post-1991 balances and the total loan guarantee liability.

Total guaranteed loan subsidy expense for FY 2003 is a combination of subsidy expense for new guaranteed loans disbursed in the current year and the interest rate and technical reestimates to existing loans. Total guaranteed loan subsidy expense in FY 2003 was \$226 million compared to \$-28 million in FY 2002, an increase of \$254 million. This increase was due to Housing and the Business and Industry guaranteed programs. Table 7 illustrates the breakdown of total subsidy expense for FY 2003 and FY 2002 by loan program.

Guaranteed loan volume (face value) increased from \$3.4 billion in FY 2002 to \$3.8 billion in FY 2003. Volume distribution between program is shown in Table 8.

**Table 5**

***Loan Guarantees Outstanding (in millions)***

	Pre-1992 Outstanding Principal, Face Value	Post-1991 Outstanding Principal, Face Value	Total Outstanding Principal, Face Value	Pre-1992 Outstanding Principal, Guaranteed	Post-1991 Outstanding Principal, Guaranteed	Total Outstanding Principal, Guaranteed
<b>Guaranteed Loans (FY 2003)</b>						
Housing Loans	11	13,420	13,431	10	12,078	12,088
Community Facility Loans	0	373	373	0	319	319
Electric Loans	293	224	517	293	224	517
Business and Industry Loans	51	4,031	4,082	39	2,975	3,014
Water and Environmental	0	29	29	0	23	23
Other Programs	4	0	4	3	0	3
<b>Total Guarantees Disbursed</b>	<b>359</b>	<b>18,077</b>	<b>18,436</b>	<b>345</b>	<b>15,619</b>	<b>15,964</b>
<b>Guaranteed Loans (FY 2002)</b>						
Housing Loans	16	13,602	13,618	14	12,242	12,256
Community Facility Loans	0	301	301	0	249	249
Electric Loans	317	199	516	317	199	516
Business and Industry Loans	80	3,883	3,963	57	2,863	2,920
Water and Environmental	0	30	30	0	24	24
Other Programs	4	0	4	3	0	3
<b>Total Guarantees Disbursed</b>	<b>417</b>	<b>18,015</b>	<b>18,432</b>	<b>391</b>	<b>15,577</b>	<b>15,968</b>

**Table 6a**

Liability for Loan Guarantees (Present value method for Pre-1992 guarantees)  
(in millions)

	FY 2003			FY 2002		
	Liabilities for Losses on Pre-1992 Guarantees Present Value	Liabilities for Loan Guarantees on Post-1991 Guarantees Present Value	Total Liabilities for Loan Guarantees	Liabilities for Losses on Pre-1992 Guarantees Present Value	Liabilities for Loan Guarantees on Post-1991 Guarantees Present Value	Total Liabilities for Loan Guarantees
<b>Liability for Loan Guarantees</b>						
Housing Loans	0	399	399	3	327	330
Community Facility Loans	0	1	1	0	5	5
Electric Loans	0	0	0	24	0	24
Business and Industry Loans	3	324	327	3	145	148
Water and Environmental	0	0	0	0	0	0
Other Programs	0	0	0	0	0	0
<b>Total Liabilities for Loan Guarantees</b>	<b>3</b>	<b>724</b>	<b>727</b>	<b>30</b>	<b>477</b>	<b>507</b>

**Table 6b**

*Schedule for Reconciling Loan Guarantee Liability*  
(in millions)

Beginning Balance, Changes, and Ending Balance	FY 2003	FY 2002
<b>Beginning Balance of the loan guarantee liability</b>	<b>477</b>	<b>587</b>
Add: Subsidy expense for guaranteed loans disbursed during the year by component		
Interest supplement costs	6	18
Default costs (net of recoveries)	172	93
Fees and other collections	(109)	(47)
Other subsidy costs	0	0
Total of the above subsidy expense components	69	64
Adjustments		
Fees received	57	62
Interest supplements paid	0	0
Claim payments to lenders	(146)	(114)
Interest accumulation on the liability balance	31	(2)
Other	79	(28)
Ending balance of the loan guarantee liability before reestimates	567	569
Add or subtract subsidy reestimates by component		
Interest rate reestimate	26	(122)
Technical/default reestimate	131	30
Total of the above reestimate components	157	(92)
<b>Ending balance of the loan guarantee liability</b>	<b>724</b>	<b>477</b>

**Table 7**

**Guaranteed Loan Subsidy Expense by Program and Component  
(in millions)**

CURRENT REPORTING YEAR	Subsidy Expense for New Guaranteed Loans Disbursed					Reestimates			GRAND TOTAL
	Interest Supplement	Defaults	Fees and Other Colls	Other	Total	Interest Rate	Technical	Total	
<b>Guaranteed Loan Programs</b>									
Housing Loans	6	130	(98)	0	38	13	58	71	<b>109</b>
Community Facility Loans	0	0	(1)	0	(1)	0	(2)	(2)	<b>(3)</b>
Electric Loans	0	0	0	0	0	0	0	0	<b>0</b>
Business and Industry Loans	0	42	(10)	0	32	13	75	88	<b>120</b>
<b>Total Subsidy Expense, Guaranteed Loans</b>	<b>6</b>	<b>172</b>	<b>(109)</b>	<b>0</b>	<b>69</b>	<b>26</b>	<b>131</b>	<b>157</b>	<b>226</b>
PRIOR REPORTING YEAR	Subsidy Expense for New Guaranteed Loans Disbursed					Reestimates			GRAND TOTAL
	Interest Supplement	Defaults	Fees and Other Colls	Other	Total	Interest Rate	Technical	Total	
<b>Guaranteed Loan Programs</b>									
Housing Loans	18	56	(38)	0	36	(45)	(47)	(92)	<b>(56)</b>
Community Facility Loans	0	0	0	0	0	(2)	6	4	<b>4</b>
Electric Loans	0	0	0	0	0	0	0	0	<b>0</b>
Business and Industry Loans	0	37	(9)	0	28	(75)	71	(4)	<b>24</b>
<b>Total Subsidy Expense, Guaranteed Loans</b>	<b>18</b>	<b>93</b>	<b>(47)</b>	<b>0</b>	<b>64</b>	<b>(122)</b>	<b>30</b>	<b>(92)</b>	<b>(28)</b>

**Table 8**

**Guaranteed Loans Disbursed (in millions)**

	Current Year		Prior Year	
	Principal, Face Value Disbursed	Principal, Guaranteed Disbursed	Principal, Face Value Disbursed	Principal, Guaranteed Disbursed
<b>Guaranteed Loans</b>				
Housing Loans	2,992	2,693	2,449	2,205
Community Facility Loans	138	117	59	49
Electric Loans	0	0	54	54
Business and Industry Loans	654	513	839	658
Water and Environmental	3	2	9	7
<b>Total Guaranteed Loans Disbursed</b>	<b>3,787</b>	<b>3,325</b>	<b>3,410</b>	<b>2,973</b>



## **Credit Program Discussion and Descriptions**

Rural Development offers direct and guaranteed loans through credit programs in the mission area through the Rural Housing Service (RHS), the Rural Business-Cooperative Service (RBS), and the Rural Utilities Service (RUS).

### ***The Rural Development mission area***

Each year, Rural Development programs create or preserve tens of thousands of rural jobs and provide or improve the quality of rural housing. To leverage the impact of its programs, Rural Development is working with state, local and Indian tribal governments, as well as private and nonprofit organizations and user-owned cooperatives. Rural Development programs are administered through the three services.

Through its loan and grant programs, RHS provides affordable housing and essential community facilities to rural communities. Programs also help finance new or improved housing for moderate, low, and very low-income families each year. RHS programs also help rural communities to finance, construct, enlarge or improve fire stations, libraries, hospitals and medical clinics, industrial parks, and other community facilities.

RBS' goal is to promote a dynamic business environment in rural America. RBS works in partnership with the private sector and community based organizations to provide financial assistance and business planning. It also provides technical assistance to rural businesses and cooperatives, conducts research into rural economic issues, and provides cooperative educational materials to the public.

RUS helps to improve the quality of life in rural America through a variety of loan programs for electric energy, telecommunications, and water and environmental projects. RUS programs leverage scarce Federal funds with private capital for investing in rural infrastructure, technology and development of human resources.

Rural Development agencies are able to provide certain loan servicing options to borrowers whose accounts are distressed or delinquent. These options include reamortization, restructuring, loan deferral, lowering interest rate, acceptance of easements, and debt write-downs. The choice of servicing options depends on the loan program and the individual borrower.

## Rural Development List of Programs

### **Rural Housing Service**

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Home Ownership Direct Loans  
Home Ownership Guaranteed Loans  
Home Improvement and Repair Direct Loans  
Home Ownership and Home Improvement and Repair Nonprogram Loans  
Rural Housing Site Direct Loans  
Farm Labor Housing Direct Loans  
Rural Rental and Rural Cooperative Housing Loans  
Rental Housing Guaranteed Loans  
  
Multi-family Housing - Nonprogram - Credit Sales  
Community Facilities Direct Loans  
  
Community Facilities Guaranteed Loans

### **Rural Business-Cooperative Service**

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Business and Industry Direct Loans  
Business and Industry Guaranteed Loans  
Intermediary Relending Program Direct Loans  
Rural Economic Development Direct Loans

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### **Rural Utilities Service**

Water and Environmental Direct Loans  
  
Water and Environmental Guaranteed Loans  
Electric Direct Loans  
  
Electric Guaranteed Loans  
Telecommunications Direct Loans  
Rural Telephone Bank  
Federal Financing Bank-  
Telecommunications Guaranteed  
Distance Learning and Telemedicine  
Direct Broadband Telecommunications Services

**Table 9a**

<b>Program Characteristics - Direct</b>			
<b>Major Programs (Direct)</b>	<b>Repayment Period</b>	<b>Interest Rate</b>	<b>Unique Servicing Option</b>
Housing Single-Family	Maximum 30-38 years/program	Current	Payment assistance - payment moratoriums - loan reamortization
Rural Rental/Rural Cooperative	1997 and prior - 50 years Subsequent - 50 year amortization with 30 year repayment and balloon	Current	Payment assistance - rental assistance to tenants
Community Facility	Maximum 40 years	4.5% to current	Workout agreements - loan reamortization
Water & Environmental	Useful life not to exceed 40 years	< or equal 5% to current	Principal payment deferrals - loan reamortization - loan transfers
Electric	Maximum 35 years	Current	Payment deferrals - loan reamortization - discounted loan prepayments Loans prior to 11/93 received interest rates from 2-5%.
Telecommunications	Expected composite life (depreciated life plus 3 years)	5-7%	Payment extension
Rural Telephone Bank	Expected useful life not to exceed 35 years	Current or 5%	Payment extension
Development Loans Intermediary Relending	Maximum 30 years	1%	Payment moratoriums
Business and Industry	Maximum 7-30 years per program	Current	Loan reamortization - loan transfer

**Table 9b**

<b>Program Characteristics - Guaranteed</b>			
<b>Major Programs (Guaranteed)</b>	<b>Repayment Period</b>	<b>Interest Rate</b>	<b>Unique Servicing Option</b>
Housing Single-Family	Maximum 30 years	Lender	Maximum 90% guarantee - Lender pays 2% fee - Loans may be sold to third party
Rental Housing	Maximum 40 years	Lender	
Community Facilities	Maximum 40 years	Lender	Maximum 90% guarantee - Lender pays 1% fee - Loans may be sold to third party
Electric	Maximum 35 years	Lender	100% Guarantee
Business & Industry	Maximum 7- 30 years per program	Lender	Guarantee maximum 60-80% - Lender pays 2% fee
Water and Environmental	Maximum 40 years	Lender	Rates will be negotiated between the lender and the borrower. They may be fixed or variable rates.

## Discussion of Administrative Expenses, Subsidy Costs, and Subsidy Rates

### *Administrative Expenses*

Consistent with the Federal Credit Reform Act of 1990 as amended, subsidy cash flows exclude direct Federal administrative expenses. Administrative expenses for FY 2003 are shown in Table 10.

**Table 10**

#### ***Administrative Expenses (in millions)***

##### ***FY 2003***

<b>Direct Loan Programs</b>	<b>Amount</b>	<b>Guaranteed Loan Programs</b>	<b>Amount</b>
<b>Total</b>	256	<b>Total</b>	155

##### ***FY 2002***

<b>Direct Loan Programs</b>	<b>Amount</b>	<b>Guaranteed Loan Programs</b>	<b>Amount</b>
<b>Total</b>	178	<b>Total</b>	131

### *Reestimates, Default Analysis, and Subsidy Rates*

The Federal Credit Reform Act of 1990 as amended governs the proprietary and budgetary accounting treatment of direct and guaranteed loans. The long-term cost to the government for direct loans or loan guarantees is referred to as "subsidy cost". Under the Act, subsidy costs for loans obligated beginning in FY 1992 are recognized at the net present value of projected lifetime costs in the year the loan is disbursed. Subsidy costs are revalued annually. Components of subsidy include interest subsidies, defaults, fee offsets, and other cash flows.

Based on a sensitivity analysis conducted for each cohort or segment of a loan portfolio, the difference between the budgeted and actual interest for both borrower and Treasury remain the key components for the subsidy formulation and reestimate rates of many USDA direct programs. USDA uses the government-wide interest rate projections provided by the Office of Management and Budget in order to do its calculations and analysis.

Rural Development's cashflow models are tailored for specific programs based on unique program characteristics. The models utilized are guaranteed, housing, and a model which encompasses the remaining direct programs. During FY 2003, the actual budgetary reestimates as of September 30, 2002, were recorded with the exception of the Electric Municipal loan program which was not accomplished during the fiscal year and the reestimates for Single-Family Housing (Section 502), Multi-Family Housing (Section 515), and Rural Telephone Bank which were recorded in the FY 2002 Financial Statements. Estimates for FY 2003 activity using an approximator method were recorded for all major loan programs.

The FY 2002 Financial Statements shown under the prior reporting period included estimates for all major programs using the approximator method. Actual budgetary reestimates as of September 30, 2002, were recorded for the aforementioned programs and the remaining programs that had not been reestimated using September 30, 2001, actual cohort data.

For the FY 2002 data, the Single Family Housing model was expanded to incorporate additional data and program characteristics, resulting in refined

reestimate amounts with the FY 2002 data reflecting further reduction of subsidy expense compared to FY 2003. The electric program's key sensitivity elements may include interest rate and loan terms. The average borrower interest rates have declined in some programs, which have resulted in subsidy expense increases between the FY 2003 and the FY 2002 reporting periods.

In FY 2003 and FY 2002, Rural Development guaranteed loan programs recorded prior year actual budgetary reestimates and current year activity estimates for material programs. A key sensitivity element in the guaranteed programs is defaults. The material programs, Single Family Housing and Business and Industry, experienced losses in excess of the budgeted projections.

Subsidy rates are used to compute each year's subsidy expenses as disclosed in tables 3 and 7. The subsidy rates disclosed below pertain only to the FY 2003 cohorts. These rates cannot be applied to the direct and guaranteed loans disbursed during the current reporting year to yield the subsidy expense. The subsidy expense for loans reported in the current year could result from disbursements of loans from both current year cohorts and prior year cohorts. The subsidy expense reported in the current year also include reestimates.

**Table 11****Subsidy Rates for Direct Loans (percentage)**

<b><u>FY 2003</u></b>						<b><u>FY 2002</u></b>					
	Interest		Fees and Other		Total		Interest		Fees and Other		Total
	Differential	Defaults	Collect.	Other			Differential	Defaults	Collect.	Other	
<b>Direct Loan Program</b>						<b>Direct Loan Programs</b>					
Section 502 Single-Family Housing	-12.90	2.68	0.00	29.59	19.37	Section 502 Single-Family Housing	13.20	1.31	-7.15	5.80	13.16
Section 504 Housing Repair Credit Sales Section 203 (SFH)	28.98	2.27	0.00	-0.23	31.02	Section 504 Housing Repair Credit Sales Section 203 (SFH)	29.96	2.30	-5.98	5.85	32.13
Section 514 Farm Labor Housing	-16.51	1.17	0.00	5.76	-9.58	Section 514 Farm Labor Housing	-20.20	4.55	-10.51	21.34	-4.82
Section 515 Rural Rental Housing	48.64	0.07	0.00	0.31	49.02	Section 515 Rural Rental Housing	46.94	0.08	-2.51	2.80	47.31
Section 523 Self-Help Housing Land Dev.	-13.18	0.03	0.00	59.78	46.63	Section 523 Self-Help Housing Land Dev.	50.56	-0.03	-30.91	22.70	42.32
Section 524 Housing Site Development	1.15	3.72	0.00	-0.46	4.41	Section 524 Housing Site Development	3.54	1.03	-9.14	9.65	5.08
Credit Sales Section 209 (MFH)	-4.02	3.92	0.00	1.19	1.09	Credit Sales Section 209 (MFH)	-1.75	1.77	-9.64	10.17	0.55
Modular Housing Loans	-13.12	0.03	0.00	59.77	46.68	Modular Housing Loans	50.52	-0.02	-1.96	-6.37	42.17
Community Facilities	21.03	-0.10	0.00	-3.01	17.92	Community Facilities	17.94	0.03	-1.64	1.35	17.68
Distance Learning and Telemedicine	6.80	0.20	0.00	-0.76	6.24	Distance Learning and Telemedicine	4.53	1.18	0.00	-0.28	5.43
Broadband	0.41	0.00	0.00	-1.56	-1.15	Broadband	0.00	0.01	0.00	-0.08	-0.07
Water and Environmental Disposal	0.00	5.21	0.00	-0.05	5.16	Water and Environmental Disposal	0.00	0.01	0.00	-0.08	-0.07
Electric Hardship	11.77	0.10	0.00	-0.53	11.34	Electric Hardship	6.96	0.12	0.00	-0.20	6.88
Electric Municipal	5.84	0.00	0.00	-0.13	5.71	Electric Municipal	2.92	0.03	0.00	0.03	2.98
FFB Electric	4.46	0.00	0.00	-0.43	4.03	FFB Electric	-0.15	0.03	0.00	0.03	-0.09
Electric Treasury	-1.26	0.04	0.00	-0.60	-1.82	Electric Treasury	-1.12	0.03	0.00	-0.04	-1.13
Telephone Hardship	0.00	0.03	0.00	-0.07	-0.04	Telephone Hardship	-0.06	0.03	0.00	-0.01	-0.04
Telephone Treasury	1.71	0.00	0.00	0.00	1.71	Telephone Treasury	2.27	0.03	0.00	0.02	2.32
FFB Telephone	0.00	0.02	0.00	0.03	0.05	FFB Telephone	0.00	0.04	0.00	0.06	0.10
Rural Telephone Bank Intermediary Relending Program	-1.09	0.13	0.00	-1.40	-2.36	Rural Telephone Bank Intermediary Relending Program	-0.92	0.11	0.00	-0.04	-0.85
Rural Economic Development	2.21	0.02	0.00	-0.85	1.38	Rural Economic Development	2.29	0.02	0.00	-0.17	2.14
Business and Industry	48.32	0.00	0.00	-0.06	48.26	Business and Industry	43.22	0.00	0.00	-0.01	43.21
	22.46	0.05	0.00	-1.15	21.36		24.91	0.05	0.00	-0.80	24.16
	0.00	0.00	0.00	0.00	0.00		-30.79	58.98	0.00	0.28	28.47

**Table 12****Subsidy Rates for Loan Guarantees (percentage)**

<b><u>FY 2003</u></b>						<b><u>FY 2002</u></b>					
	Interest		Fees and Other		Total		Interest		Fees and Other		Total
	Supplement	Defaults	Collect.	Other			Supplement	Defaults	Collect.	Other	
<b>Guaranteed Loan Programs</b>						<b>Guaranteed Loan Programs</b>					
Section 502 Single-Family Housing	0.00	2.72	-2.00	0.00	0.72	Section 502 Single-Family Housing	0.00	3.28	-2.00	0.00	1.28
Section 502 Single Family Housing - Refinance	0.00	0.68	-0.50	0.00	0.18	Section 502 Single Family Housing - Refinance	0.00	0.00	0.00	0.00	0.00
Section 538 Multi-Family Housing	8.22	0.00	-3.72	0.00	4.50	Section 538 Multi-Family Housing	8.82	2.24	-7.13	0.00	3.93
Community Facilities	0.00	0.28	-0.82	0.00	-0.54	Community Facilities	0.00	0.12	-0.80	0.00	-0.68
Electric	0.00	0.08	0.00	0.00	0.08	Electric	0.00	0.08	0.00	0.00	0.08
Business and Industry	0.00	5.45	-1.48	0.00	3.97	Business and Industry	0.00	5.22	-1.48	0.00	3.74
NAD Bank	0.00	6.15	-1.59	0.00	4.56	NAD Bank	0.00	5.28	-1.60	0.00	3.68

## **Other Disclosures**

### **Foreclosed Property**

Property is acquired largely through foreclosure and voluntary conveyance. Acquired properties associated with loans are reported at their market value at the time of acquisition. The projected future cash flows associated with acquired properties are used in determining the related allowance (at present value).

For FY's 2003 and 2002, Rural Housing Service properties consisted primarily of 952 and 1,114 rural single-family dwellings, respectively. The average holding period for single-family housing properties in inventory for FY's 2003 and 2002 was 22 months and 20 months, respectively. The approximate number of borrowers for which foreclosure proceedings were in process at the end of FY's 2003 and 2002 was 20,000 and 22,000, respectively. Certain properties can be leased to eligible individuals.

### **Commitments to Guarantee**

As of September 30, 2003 and 2002, there were approximately \$2.1 billion and \$2.0 billion in commitments to extend loan guarantees, respectively.

### **Non-performing Loans**

Rural Development's loan interest income on non-performing receivables is calculated but the recognition of revenue is deferred. Non-performing receivables are defined as receivables that are in arrears by 90 or more days.

### **Interest Credit**

Approximately \$18.6 billion and \$19.1 billion of the Rural Housing Service unpaid loan principal as of September 30, 2003 and 2002, respectively, was receiving interest credit. If those loans receiving interest credit had interest accrued at the full-unreduced rate, interest income would have been approximately \$1.1 billion and \$1.1 billion higher for FY's 2003 and 2002, respectively. At the end of FY's 2003 and 2002, the Rural Development portfolio contained approximately 96 thousand and 104 thousand restructured loans with an outstanding unpaid principal balance of \$5.9 billion and \$6.2 billion, respectively.

**NOTE 7: GENERAL PROPERTY, PLANT AND EQUIPMENT, NET**

*Amounts are presented in millions.*

This equipment generally represents computer hardware, software, and other office equipment used in the Rural Development mission area's network of offices. Refer to **Notes 1L and 1M** for further information. The capitalization threshold for personal property was changed from \$5,000 to \$25,000 effective October 1, 2002.

2003						
Classes	Cost	Accumulated Depreciation	Book Value	Estimated Useful Life*	Method of Depreciation**	Capitalization Threshold
<b>Personal Property</b>						
Equipment	\$ 11	\$ 6	\$ 5	1-5	SL	\$ 25,000
Internal Use Software	32	5	27	2-15	SL	\$ 100,000
Internal Use Software in Development	15	0	15	2-15	SL	\$ 100,000
Total	<u>\$ 58</u>	<u>\$ 11</u>	<u>\$ 47</u>			

2002						
Classes	Cost	Accumulated Depreciation	Book Value	Estimated Useful Life*	Method of Depreciation**	Capitalization Threshold
<b>Personal Property</b>						
Equipment	\$ 11	\$ (4)	\$ 7	1-5	SL	\$ 5,000
Internal Use Software	17	(2)	15	2-15	SL	\$ 100,000
Internal Use Software in Development	10	0	10	2-15	SL	\$ 100,000
Total	<u>\$ 38</u>	<u>\$ (6)</u>	<u>\$ 32</u>			

\* Range of Service Life

\*\* SL - Straight Line

**NOTE 8: OTHER ASSETS**

*Amounts are presented in millions.*

	2003	2002
With the Public		
Investment in Loan Asset Sale Trust*	\$ 35	\$ 35
Other	2	1
Total Other Assets	<u>\$ 37</u>	<u>\$ 36</u>

\* In FY 1987, a loan asset sale was conducted as required in the Omnibus Budget Reconciliation Act of 1986 (Public Law 99-509). As a result of these sales, the Rural Development Insurance Fund (RDIF) and the Rural Housing Insurance Fund (RHIF) maintain investments in the Class C securities of the Community Program, Loan Trust, 1987A, and the Rural Housing Trust, 1987-1, respectively. These investments represent a residual security in the respective Trust and entitles Rural Development to residual cash flows resulting from loan repayments not required to pay trust security holders or to fund required reserves. Rural Development intends to retain the RDIF and RHIF Class C investments into the foreseeable future.



**NOTE 9: LIABILITIES NOT COVERED BY BUDGETARY RESOURCES**

*Amounts are presented in millions.*

	<u>2003</u>	<u>2002</u>
<b><u>Intragovernmental</u></b>		
Unfunded FECA Liability	\$ 6	\$ 5
<b>Total Intragovernmental</b>	<u>6</u>	<u>5</u>
<b><u>With the Public</u></b>		
Federal Employee and Veterans' Benefits	34	31
Unfunded Annual Leave	26	34
Contingent Liability	8	0
<b>Total Liabilities Not Covered by Budgetary Resources</b>	<u>74</u>	<u>70</u>
<b>Total Liabilities Covered by Budgetary Resources</b>	<u>60,369</u>	<u>61,074</u>
<b>Total Liabilities</b>	<u>\$ 60,443</u>	<u>\$ 61,144</u>

See **Note 1P** for a discussion of FECA.  
See **Note 1U** for a discussion of Annual Leave.

Liabilities not covered by budgetary resources represent liabilities for which Congressional action is required before budgetary resources could be provided.

**NOTE 10: DEBT**

*Amounts are presented in millions.*

	<u>2002 Beginning Balance</u>	<u>Net Borrowing</u>	<u>2002 Ending Balance</u>	<u>Net Borrowing</u>	<u>2003 Ending Balance</u>
<b><u>Agency Debt</u></b>					
Held by the Public	\$ 2	\$ 0	\$ 2	\$ 0	\$ 2
Notes Payable	85	(3)	82	(4)	78
<b>Total Agency Debt</b>	<u>87</u>	<u>(3)</u>	<u>84</u>	<u>(4)</u>	<u>80</u>
<b><u>Other Debt</u></b>					
Debt to the Treasury	25,650	1,863	27,513	(344)	27,169
Debt to the Federal Financing Bank (FFB)	25,220	(2,841)	22,379	321	22,700
<b>Total Other Debt</b>	<u>50,870</u>	<u>(978)</u>	<u>49,892</u>	<u>(23)</u>	<u>49,869</u>
<b>Total Debt</b>	<u>\$ 50,957</u>	<u>\$ (981)</u>	<u>\$ 49,976</u>	<u>\$ (27)</u>	<u>\$49,949</u>

	<u>2003</u>	<u>2002</u>
<b><u>Classification of Debt</u></b>		
Intragovernmental Debt	\$ 49,869	\$ 49,892
Debt Held by the Public	80	84
<b>Total Debt</b>	<u>\$ 49,949</u>	<u>\$ 49,976</u>

Borrowings from the FFB are either in the form of Certificates of Beneficial Ownership (CBO) or loans executed directly between the borrower and FFB with Rural Development unconditionally guaranteeing repayment. Borrowings from private investors are in the form of CBO's. CBO's outstanding with the FFB and private investors are generally secured by unpaid loan principal balances. CBO's outstanding are related to Pre-Credit Reform loans and are no longer used for program financing.

FFB CBO's are repaid as they mature and are not related to any particular group of loans. Borrowings made to finance loans directly between the borrower and FFB mature and are repaid as the related group of loans become due. Interest rates on the related group of loans are equal to interest rates on FFB borrowings, except in those situations in which an FFB-funded loan is restructured and the terms of the loan are modified. For FY's 2003 and 2002, there were approximately \$47 million and \$79 million of FFB loans repriced or refinanced, respectively.

In conjunction with certain RUS troubled debt restructurings, Rural Development has assumed notes payable to non-federal entities for FY's 2003 and 2002, approximating \$79 million and \$82 million, respectively for debt previously guaranteed. A substantial portion of these balances are owed to the National Rural Utilities Cooperative Finance Corporation, a private lender to rural electric borrowers. The notes bear interest at rates ranging from 7.13 to 10.70 percent, and mature through the year 2027.

Supplemental information associated with debt follows:

**Amounts are presented in millions.**

	<u>2003</u>	<u>2002</u>
<b><u>Interest Payable, Federal</u></b>		
Federal Financing Bank	\$ 170	\$ 196
U.S. Treasury	1	3
Total	<u>\$ 171</u>	<u>\$ 199</u>

These interest payable amounts associated with borrowings from the Treasury and the FFB are included in the table at the beginning of this note.

	<u>2003</u>	<u>2002</u>
<b><u>Interest Expense, Federal</u></b>		
Federal Financing Bank	\$ 1,616	\$ 1,829
U.S. Treasury	1,570	1,494
Total	<u>\$ 3,186</u>	<u>\$ 3,323</u>

**NOTE 11: STOCK PAYABLE TO RTB BORROWERS**

*Amounts are presented in millions.*

	<u>2003</u>	<u>2002</u>
<b><u>With the Public</u></b>		
B Stock Payable	\$ 572	\$ 792
C Stock Payable	737	551
Total	<u>\$1,309</u>	<u>\$ 1,343</u>

These liabilities are long-term in nature.

**Capital Stock Class B:**

Class B stock, a voting class of stock, is issued only to borrowers of RTB, in proportion to actual loan advances. RTB requires borrowers to purchase Class B stock in the amount of 5 percent of advanced loan amounts. Class B stock is nontransferable, except in connection with a transfer of ownership, approved by RTB, of all or part of a RTB loan. A borrower may exchange Class B stock for Class C stock: 1) upon retiring all debt with RTB; or 2) effective November 9, 1999, prior to retiring all debt on a proportionate basis equal to the percentage of each note repaid. Otherwise, the borrower retains possession of the stock.

**Capital Stock Class C:**

Class C stock, a voting class of stock, is issued only to RTB borrowers, or to corporations and public entities eligible to borrow from RTB under Section 408 of the Rural Electrification Act of 1936, as amended, or by organizations controlled by such borrowers, corporations, and public entities.

For further details regarding Class B & C Stock, see **Note 9, Capital Stock**, in the Rural Telephone Bank Financial Statements which are issued under separate cover.

**NOTE 12: OTHER LIABILITIES**

*Amounts are presented in millions.*

	<b>2003</b>		
	<b>Non-Current</b>	<b>Current</b>	<b>Total</b>
<b><u>Intragovernmental</u></b>			
Employer Contributions & Payroll Taxes Payable	\$ 0	\$ 2	\$ 2
Unfunded FECA Liability	0	6	6
Liability for Deposit Funds & Suspense Accounts	0	(2)	(2)
Other	0	9	9
Payable to Treasury General Fund	0	465	465
Total Intragovernmental	<u>0</u>	<u>480</u>	<u>480</u>
Accrued Funded Payroll and Benefits	0		
Dividends Payable	0	28	28
Liability for Deposit Funds & Suspense Accounts	0	79	79
Unfunded Annual Leave	0	26	26
Contingent Liability	0	8	8
Other	18	36	54
Total Other Liabilities	<u>\$ 18</u>	<u>\$ 657</u>	<u>\$ 675</u>
	<b>2002</b>		
	<b>Non-Current</b>	<b>Current</b>	<b>Total</b>
<b><u>Intragovernmental</u></b>			
Employer Contributions & Payroll Taxes Payable	\$ 0	\$ 2	\$ 2
Unfunded FECA Liability	0	5	5
Liability for Deposit Funds & Suspense Accounts	0	(4)	(4)
Other	0	17	17
Payable to Treasury General Fund	0	752	752
Total Intragovernmental	<u>0</u>	<u>772</u>	<u>772</u>
Accrued Funded Payroll and Benefits	0	(1)	(1)
Dividends Payable	0	22	22
Liability for Deposit Funds & Suspense Accounts	0	72	72
Unfunded Annual Leave	0	34	34
Other	17	36	53
Total Other Liabilities	<u>\$ 17</u>	<u>\$ 935</u>	<u>\$ 952</u>

These liabilities are covered by Budgetary Resources.

**NOTE 13: COMMITMENTS AND CONTINGENCIES**

**COMMITMENTS**

Rural Development has commitments under cancelable leases for office space. The majority of buildings in which Rural Development operates are leased by the General Services Administration (GSA). GSA charges rent which is intended to approximate commercial rental rates.

As of September 30, 2003 and 2002, there were approximately \$2.1 billion and \$2.0 billion in commitments to extend loan guarantees, respectively.

As of September 30, 2003 and 2002, there were no obligations due to cancelled appropriations for which there is a contractual commitment for payment.

**CONTINGENCIES**

The Rural Development mission area is subject to various claims and contingencies related to lawsuits. No amounts have been accrued in the Financial Statements for claims where the amount or probability of judgment is uncertain.

For cases in which payment has been deemed probable and for which the amount of potential liability has been estimated, \$8 million and \$0 million have been accrued in the Financial Statements as of September 30, 2003 and 2002, respectively.

Although overall the existing multiple family housing portfolio is in fair to good condition, Rural Development National Office officials, during a FY 2000 Management Control Review determined that adequate funds had not been accrued to address future maintenance costs. A conservative estimate is that in the next 5 years, approximately 4,250 properties and 85,000 apartment units, will physically deteriorate to the point where safety and sanitation will necessitate a general modernization program to maintain their marketability and ultimately compete for tenants. The cost is expected to reach into the hundreds of millions of dollars.

**NOTE 14: SUPPORTING SCHEDULE FOR THE STATEMENT OF NET COST**

*Amounts are presented in millions.*

2003

	<u>Mortgage Credit</u>	<u>Housing Assistance</u>	<u>Area &amp; Regional Development</u>	<u>Energy Supply &amp; Conservation</u>	<u>Agricultural Research &amp; Services</u>	<u>Consolidated Total</u>
<b>Costs:</b>						
Program Costs:						
<b>Intragovernmental Gross Costs</b>	\$ 1,028	\$ 13	\$ 643	\$ 1,725	\$ 0	\$ 3,409
Less: Intragovernmental Earned Revenue (Note 15)	<u>101</u>	<u>1</u>	<u>141</u>	<u>79</u>	<u>0</u>	<u>322</u>
Intragovernmental Net Costs	927	12	502	1,646		3,087
<b>Gross Costs with the Public</b>						
Grants and Payments	1	793	732	0	4	1,530
Loan Subsidy Costs	153	2	225	474	0	854
Other	<u>1,222</u>	<u>28</u>	<u>603</u>	<u>413</u>	<u>0</u>	<u>2,266</u>
Total Gross Costs with the Public	1,376	823	1,560	887	4	4,650
Less: Earned Revenues from the Public (Note 15)	<u>1,482</u>	<u>0</u>	<u>607</u>	<u>1,909</u>	<u>0</u>	<u>3,998</u>
Net Costs with the Public	(106)	823	953	(1,022)	4	652
<b>NET COST OF OPERATIONS</b>	<u>\$ 821</u>	<u>\$ 835</u>	<u>\$ 1,455</u>	<u>\$ 624</u>	<u>\$ 4</u>	<u>\$ 3,739</u>

**NOTE 14: SUPPORTING SCHEDULE FOR THE STATEMENT OF NET COST**

*Amounts are presented in millions.*

	2002					
	<u>Mortgage Credit</u>	<u>Housing Assistance</u>	<u>Area &amp; Regional Development</u>	<u>Energy Supply &amp; Conservation</u>	<u>Agricultural Research &amp; Services</u>	<u>Consolidated Total</u>
<b>Costs:</b>						
Program Costs:						
<b>Intragovernmental Gross Costs</b>	\$ 1,172	\$ 13	\$ 730	\$ 1,643	\$ 0	\$ 3,558
Less: Intragovernmental Earned Revenue <b>(Note 15)</b>	<u>118</u>	<u>0</u>	<u>114</u>	<u>65</u>	<u>0</u>	<u>297</u>
Intragovernmental Net Costs	\$ 1,054	\$ 13	\$ 616	\$ 1,578	\$ 0	\$ 3,261
<b>Gross Costs with the Public</b>						
Grants and Payments	2	728	710	0	3	1,443
Loan Subsidy Costs	(486)	2	51	59	0	(374)
Other	<u>3,458</u>	<u>23</u>	<u>(669)</u>	<u>265</u>	<u>0</u>	<u>3,077</u>
Total Gross Costs with the Public	2,974	753	92	324	3	4,146
Less: Earned Revenues from the Public <b>(Note 15)</b>	<u>1,634</u>	<u>0</u>	<u>683</u>	<u>1,730</u>	<u>0</u>	<u>4,047</u>
Net Costs with the Public	1,340	753	(591)	(1,406)	3	99
<b>NET COST OF OPERATIONS</b>	<u>\$ 2,394</u>	<u>\$ 766</u>	<u>\$ 25</u>	<u>\$ 172</u>	<u>\$ 3</u>	<u>3,360</u>

OTHER DISCLOSURES

FUNCTION LEVEL TITLE	SUBFUNCTION LEVEL TITLE	BUDGET SUB-FUNCTION CODE	ACTIVITY INCLUDED IN FINANCIAL STATEMENTS PROGRAMS (where applicable)	LOAN/GRANT PROGRAMS INCLUDED IN BUDGET SUBFUNCTION CODE
National Defense	Department of Defense - Military	051	Other	Armament Retooling and Support
Energy	Energy Supply & Conservation	271, 272	Rural Utilities Service	Rural Electric and Telecommunication
National Resources	Water Resources Conservation & Land Management Pollution Control & Abatement	301 302 304	Other	Hazardous Waste Disposal
Agriculture	Agricultural Research and Services	352	Rural Business and Cooperative Services	Conservation loans
Commerce & Housing	Mortgage Credit	371	Rural Housing Service	Single Family Housing (Direct & Guaranteed) Multi-Family Housing (Direct & Guaranteed)
Community & Regional Development	Area & Regional Development	452	Rural Housing Service  Rural Business and Cooperative Service  Rural Utilities Service	Rural Community Facility (Direct and Guaranteed)  Rural Business and Industry (Direct and Guaranteed) Rural Economic Development (Loans and Grants) Rural Development Loan Funds  Rural Water and Environmental (Direct and Guaranteed) Rural Telephone Bank Distance Learning and Telemedicine
Income Security	Housing Assistance	604	Rural Housing Service	Domestic Farm Labor Grants Very Low-Income Housing Repair Grants Construction Defects Rental Assistance Program Other Housing Grants

USDA and the individual agencies preparing their own Financial Statements are required to prepare the Statement of Net Cost at the subfunction level. The Statement of Net Cost, as prepared by the Department of Treasury for the U.S. Government, shows these activities at the function level.



**NOTE 15: EARNED REVENUES**

*Amounts are presented in millions.*

	2003				
	<u>Mortgage Credit</u>	<u>Housing Assistance</u>	<u>Area &amp; Regional Development</u>	<u>Energy Supply &amp; Conservation</u>	<u>Total</u>
<b><u>With the Public</u></b>					
Interest Revenue	\$ 1,482	\$ 0	\$ 607	\$ 1,909	\$ 3,998
Other					
Total	<u>\$ 1,482</u>	<u>\$ 0</u>	<u>\$ 607</u>	<u>\$ 1,909</u>	<u>\$ 3,998</u>
<b><u>Intragovernmental</u></b>					
Interest Revenue from Treasury	\$ 93	\$ 0	\$ 139	\$ 78	\$ 310
Other	7	1	3	1	12
Total	<u>\$ 100</u>	<u>\$ 1</u>	<u>\$ 142</u>	<u>\$ 79</u>	<u>\$ 322</u>
Total Earned Revenues	<u><u>\$ 1,582</u></u>	<u><u>\$ 1</u></u>	<u><u>\$ 749</u></u>	<u><u>\$ 1,988</u></u>	<u><u>\$ 4,320</u></u>

**NOTE 15: EARNED REVENUES**

*Amounts are presented in millions.*

	2002				
	<u>Mortgage Credit</u>	<u>Housing Assistance</u>	<u>Area &amp; Regional Development</u>	<u>Energy Supply &amp; Conservation</u>	<u>Total</u>
<b><u>With the Public</u></b>					
Interest Revenue	\$ 1,634	\$ 0	\$ 683	\$ 1,730	\$ 4,047
Other	0	0	0	0	0
Total	<u>\$ 1,634</u>	<u>\$ 0</u>	<u>\$ 683</u>	<u>\$ 1,730</u>	<u>\$ 4,047</u>
<b><u>Intragovernmental</u></b>					
Interest Revenue from					
Treasury	\$ 114	\$ 0	\$ 112	\$ 65	\$ 291
Other	4	0	2	0	6
Total	<u>\$ 118</u>	<u>\$ 0</u>	<u>\$ 114</u>	<u>\$ 65</u>	<u>\$ 297</u>
Total Earned Revenues	<u><u>\$ 1,752</u></u>	<u><u>\$ 0</u></u>	<u><u>\$ 797</u></u>	<u><u>\$ 1,795</u></u>	<u><u>\$ 4,344</u></u>

## Other Disclosures

### Credit Reform

The amount of subsidy expense on post-1991 direct loans equals the present value of estimated cash outflows over the life of the loan less the present value of cash inflows, discounted at the interest rate of marketable Treasury securities within a similar maturity term. A major component of subsidy expense is the interest subsidy cost/interest differential. This is defined as the excess of the amount of direct loans disbursed over the present value of the interest and principal payments required by the loan contracts, discounted at the applicable Treasury rate. One of the components of interest subsidy cost/interest differential is interest revenue. This interest revenue is earned from both federal and non-federal sources. For a further discussion of present value refer to **Note 1J**.

### Exchange Transactions With Non-Federal Sources

When a new direct loan program becomes a reality, the applicable public law normally addresses interest rates to be charged to borrowers in some fashion. Public laws can be specific, state a minimum and/or maximum rate, or be in general terms. The following general discussion about borrower interest rates is in relation to loan programs within each of our mission areas.

**Rural Housing Service:** The two largest loan programs (single-family housing and rural rental & cooperative housing) have a statutory basis for rates that is not less than the current average market yield on outstanding U.S. marketable obligations of comparable maturities. This rate has been determined to be the 25-year Treasury rate.

**Rural Business-Cooperative Service:** The main loan program (business and industry) has a statutory basis for a rate which is not less than the Treasury rate determined by considering 1) current average market yield on outstanding U.S. marketable obligations of comparable maturities, 2) comparable private market rates, 3) Secretary of Agriculture's insurance plus an additional charge to cover losses.

**Rural Utilities Services:** Water and Environmental loans have a statutory basis for a rate which has a range between less than or equal to 5 percent to not greater than the current market yield for outstanding municipal obligations of comparable maturities adjusted to the nearest 1/8 of 1 percent. Telephone cost-of-money loans have a statutory basis for a rate equal to the current cost-of-money to the Federal Government for loans of a similar maturity, but not to exceed 7 percent. Electric municipal rate loans have a statutory basis for a rate equal to the current market yield on outstanding municipal obligations, subject to a 7 percent maximum, with remaining periods to maturity similar to the term selected by the applicant. Telephone and Electric hardship rate loans have a statutory basis for a rate of 5 percent. The rate on telephone and electric loans purchased by the Federal Financing Bank, shall be the rate applicable to similar loans being made or purchased by the Federal Financing Bank.

**Exchange Transactions With Federal Sources**

As the discussion in **Note 1B** attests, the history of Rural Development is one of financial and technical assistance to rural America. Rural Development serves as a temporary source of supervised credit until borrowers are able to qualify for private sector resources. As the lender of last resort, Rural Development is unable to recoup all the costs associated with its loan making and loan servicing activities. The main reason is that the costs associated with borrowings from Treasury to make loans exceeds the interest income received from borrowers plus any interest income earned from Treasury.

**NOTE 16: PRIOR PERIOD ADJUSTMENTS**

*Amounts are presented in millions.*

	<u>2003</u>	<u>2002</u>
Property	\$ 0	\$ (1)
FECA Actuarial	0	12
Total	<u>\$ 0</u>	<u>\$ 11</u>

**NOTE 17: APPORTIONMENT CATEGORIES OF OBLIGATIONS INCURRED**

*Amounts are presented in millions*

	<u>2003</u>		
	<u>Direct</u>	<u>Reimbursable</u>	<u>Total</u>
Category A	\$ 10,358	\$ 0	\$ 10,358
Category B	4,578	487	5,065
Total Obligations Incurred	<u>\$ 14,936</u>	<u>\$ 487</u>	<u>\$ 15,423</u>
	<u>2002</u>		
	<u>Direct</u>	<u>Reimbursable</u>	<u>Total</u>
Category A	\$ 11,498	\$ 0	\$ 11,498
Category B	3,904	481	4,385
Total Obligations Incurred	<u>\$ 15,402</u>	<u>\$ 481</u>	<u>\$ 15,883</u>

**NOTE 18: AVAILABLE BORROWING AUTHORITY, END OF PERIOD**

As of September 30, 2003 and 2002, the amount of available borrowing authority was \$15.0 billion and \$13.2 billion, respectively.

**NOTE 19: TERMS OF BORROWING AUTHORITY USED**

**Requirements for repayments of borrowings:** Borrowings are repaid on SF 1151, Nonexpenditure Transfer Authorization, as maturity dates become due. For liquidating accounts, maturity dates are one working day prior to the anniversary date of the note. For financing accounts, maturity dates are based on the period of time used in the subsidy calculation, not the contractual term of the agency's loans to borrowers. This period of time used in the subsidy calculation will normally be longer than the contractual term of the agency's loans to borrowers.

**Financing sources for repayments of borrowings:** Included are reestimates and cash flows (i.e., borrower loan principal repayments), appropriations received in liquidating accounts for "cash needs", residual unobligated balances, where applicable, and other Treasury borrowings.

**Other terms of borrowing authority used:** In general, borrowings are for periods of between one year and approximately fifty years depending upon the loan program/cohort. Interest rates on borrowings in the liquidating accounts were assigned on the basis of the Treasury rate in effect at the time of the borrowing. Interest rates on borrowings in the financing accounts are assigned on the basis of the Treasury rate in effect during the period of loan disbursements. Some individual loans are disbursed over several quarters or years. Consequently, several interest rates can be applicable to an individual loan. Thus, a single weighted average interest rate is maintained for each cohort and is adjusted each year until the disbursements for the cohort have been made. Each year, the current average annual interest rate is weighted by current year disbursements and merged with the prior years weighted average to calculate a new weighted average.

Prepayments can be made on Treasury borrowings in the liquidating and financing accounts without penalty; however, they cannot be made on Federal Financing Bank Certificates of Beneficial Ownership in the liquidating accounts without penalty.

**NOTE 20: ADJUSTMENTS TO BEGINNING BALANCE OF BUDGETARY RESOURCES**

Amounts are presented in millions.

	2003		2002	
	Unobligated	Obligated	Unobligated	Obligated
Beginning balances	\$ 2,563	\$ 19,930	\$ 1,829	\$ 16,887
Adjustments	0	0	(58)	74
Beginning balances, as adjusted	\$ 2,563	\$ 19,930	\$ 1,771	\$ 16,961
<b>Explanation:</b>				
Obligation accrued in 2001 but not recorded in budgetary accounts until 2002			(68)	68
Reclassification due to changes in Parent/Child reporting			5	6
Unobligated balance not included in FY 2001 but included in amount brought forward for FY 2002			5	N/A
			\$ (58)	\$ 74

**NOTE 21: PERMANENT INDEFINITE APPROPRIATIONS**

***Existence, purpose, and availability of permanent indefinite appropriations:***

Permanent indefinite appropriations are mainly applicable to liquidating accounts which have the ability to apportion them and for reestimates related to upward adjustments of subsidy in the program accounts. These appropriations become available pursuant to standing provisions of law without further action by Congress after transmittal of the Budget for the year involved. They are treated as permanent the first year they become available, as well as in succeeding years. However, they are not stated as specific amounts but are determined by specified variable factors, such as "cash needs" for the liquidating accounts and information about the actual performance of a cohort or estimated changes in future cash flows of the cohort in the program accounts.

The period of availability for these appropriations are as follows: Annual authority is available for obligation only during a specified year and expires at the end of that time. Multi-year authority is available for obligation for a specified period of time in excess of one fiscal year. No-year authority remains available for obligation for an indefinite period of time, usually until the objectives for which the authority was made available are achieved.

Annual and multi-year authority expire for the purpose of incurring new obligations. However, the authority is available for adjustments to obligations and for disbursements that were incurred or made during the period prior to expiration, but not recorded. Unless specifically authorized in law, the period that the expired authority is available for adjustments to obligations or for disbursements is five fiscal years (beginning with the first expired year). At the end of the fifth expired year, the authority is "cancelled". Thereafter, the authority is not available for any purpose.

**NOTE 22: LEGAL ARRANGEMENTS AFFECTING USE OF UNOBLIGATED BALANCES**

The availability/use of budget authority (i.e., unobligated balances) for obligation and expenditure are limited by purpose, amount, and time.

- **Purpose** - Funds may be obligated and expended only for the purpose authorized in appropriation acts or other laws.
- **Amount** - Obligations and expenditures may not exceed the amounts established in law. Amounts available are classified as either definite (i.e., not to exceed a specified amount) or indefinite (i.e., amount is determined by specified variable factors).
- **Time** - The period of time during which budgetary resources may incur new obligations is different from the period of time during which the budgetary resources may be used to disburse funds.

The time limitations on the use of unobligated balances are the same as those previously discussed in the last two paragraphs of the permanent indefinite appropriations footnote disclosure.

Any information about legal arrangements affecting the use of unobligated balances of budget authority will be specifically stated by program and

fiscal year in the appropriation language or in the alternative provisions section at the end of the Appropriations Act.

**NOTE 23: EXPLANATION OF DIFFERENCES BETWEEN THE STATEMENT OF BUDGETARY RESOURCES (SBR) AND THE BUDGET OF THE UNITED STATES GOVERNMENT**

The 2005 Budget of the United States Government, with the Actual Column completed for FY 2003, has not yet been published as of the date of these financial statements. The Budget is currently expected to be published and delivered to Congress in early February 2004. The Budget will be available from the Government Printing Office.

The 2004 Budget of the United States Government, with the Actual Columns completed for FY 2002, was published in February 2003 and reconciled to the SBR. No reporting errors were found. However, legitimate differences did occur as described in the table below. The legitimate differences represent:

- Expired budgetary authority available for upward adjustments of obligations, which is excluded from the President's Budget "actual" column per OMB Circular No. A-11, but is included in the SBR.
- Shared accounts which represent designated fund account symbols by USDA to receive and subsequently obligate and disburse and allotments treated as nonexpenditure transactions. These accounts retain the fund account symbol identified with the original appropriation from which monies were advanced.
- Amounts due to rounding.

**Reconciliation Between FY 2002 Statement of Budgetary Resources and the President's Budget**

*Amounts are presented in millions.*

Applicable Line From SBR	Amount from SBR	Applicable Line From President's Budget	Amount from President's Budget	Legitimate Differences	Reporting Errors
Total Budgetary Resources (line 7)	\$18,446	Total budgetary resources available for obligation	\$18,183	T - \$263 E - 262 S - 1	None
Total Status of Budgetary Resources (line 11)	\$18,446	Total new obligations, Unobligated balance expiring/withdrawn, Unobligated balance carried forward, end of year, and Unobligated balance available, end of year	\$18,189	T - \$257 E - 262 R - (6) S - 1	None
Outlays (line 15)	\$2,963	Outlays	\$2,962	T - \$ 1 R - (1) S - 2	None

**LEGEND**

T = Total Amount  
E = Expired Budgetary Authority

R = Rounding  
S = Shared Accounts

**NOTE 24: EXPLANATION OF RELATIONSHIP BETWEEN LIABILITIES NOT COVERED BY BUDGETARY RESOURCES ON THE BALANCE SHEET AND THE CHANGE IN COMPONENTS REQUIRING OR GENERATING RESOURCES IN FUTURE PERIODS ON THE STATEMENT OF FINANCING**

	<u>2003</u>	<u>2002</u>
Current Year Liabilities Not Covered by Budgetary Resources, as Disclosed in Note 9	\$ 74	\$ 70
Prior Year Liabilities Not Covered by Budgetary Resources	(70)	(74)
Increase (Decrease) in Liabilities Not Covered by Budgetary Resources	4	(4)
Upward/Downward Reestimates of Credit Subsidy Expense	418	(461)
Increase in Exchange Revenue Receivable from the Public	0	(35)
Other	(4)	31
Components Requiring or Generating Resources in Future Periods, as Reported on the Statement of Financing	<u>\$ 418</u>	<u>\$ (469)</u>

For FY 2002, the \$31 million amount reported as "Other" above is different from the \$27 million amount reported as "Other" on the Statement of Financing due to the inclusion of \$(4) million amount reported above on the line titled, Increase (Decrease) in Liabilities Not Covered by Budgetary Resources, in the overall computation.

For FY 2003, the \$(4) million amount reported as "Other" above is different from the amount reported as "Other" on the Statement of Financing due to the inclusion of \$4 million amount reported above on the line titled "Increase (Decrease) in Liabilities Not Covered by Budgetary Resources, in the overall computation.

The subsidy reestimates are recognized expenses even though budgetary resources will be provided in a subsequent period. These credit subsidy reestimates are reported as liabilities covered by budgetary resources since the budget authority to fund the reestimates is permanent and indefinite and no further congressional action is required to provide the resources.

**NOTE 25: DESCRIPTION OF TRANSFERS THAT APPEAR AS A RECONCILING ITEM ON THE STATEMENT OF FINANCING**

- The Appalachian Regional Commission (ARC) invests in the basic building blocks of sustainable economic development in the 406 counties (13-State Region) which comprise the Appalachian Region. ARC has allocated funds to Rural Development to provide accounting services. As of September 30, 2003 and 2002, the amount of this reconciling item is \$15.5 million and \$17.1 million, respectively.
- The Economic Development Administration's (EDA) Assistance Program provides grants for public works facilities, other financial assistance, and planning and coordination assistance needed to alleviate conditions of substantial and persistent unemployment and underemployment in economically distressed areas and regions. EDA has allocated funds to Rural Development to provide accounting services. As of September 30, 2003 and 2002, the amount of this reconciling item is \$5.9 million and \$1.1 million, respectively.



**NOTE 26: INCIDENTAL CUSTODIAL COLLECTIONS**

*Amounts are presented in millions.*

	<u>Custodial Activity</u>	
	<u>2003</u>	<u>2002</u>
<b><u>Sources of Collections</u></b>		
Soil Conservation Service Loan Collections	<u>\$ 1</u>	<u>\$ 1</u>
Total Revenue Collected	<u>\$ 1</u>	<u>\$ 1</u>
<b><u>Disposition of Collections</u></b>		
Amount Transferred to Treasury Receipt Accounts	<u>\$ 1</u>	<u>\$ 1</u>
Total Disposition of Revenue	<u>\$ 1</u>	<u>\$ 1</u>
Net Custodial Activity	<u>\$ 0</u>	<u>\$ 0</u>

**REQUIRED SUPPLEMENTARY INFORMATION**

*Amounts are presented in millions.*

	<b>2003 Budgetary</b>				
	<b>Rural Community Advancement Program</b>	<b>Rural Electrification/ Telecommunication Funds</b>	<b>Rural Telephone Bank Funds</b>	<b>Rural Housing Funds</b>	<b>Rental Assistance Programs</b>
Budgetary Resources:					
Budget Authority:					
Appropriations Received	\$ 1,404	\$ 193	\$ 7	\$ 797	\$ 788
Borrowing Authority	0	0	0	0	0
Net Transfers	23	22	(22)	1	0
Unobligated Balance:					
Beginning of Period	180	90	945	63	4
Spending Authority from Offsetting Collections:					
Earned					
Collected	495	3,350	247	1,779	0
Receivable from Federal Sources	0	0	56	0	0
Change in Unfilled Customer Orders Without Advance from Federal Sources					
	0	0	0	0	0
Subtotal	495	3,350	303	1,779	0
Recoveries of Prior Year Obligations	23	4	14	88	1
Permanently Not Available	(624)	(2,093)	(10)	(1,267)	(67)
<b>Total Budgetary Resources</b>	<b>\$ 1,501</b>	<b>\$ 1,566</b>	<b>\$ 1,237</b>	<b>\$ 1,461</b>	<b>\$ 726</b>

**REQUIRED SUPPLEMENTARY INFORMATION***Amounts are presented in millions.*

	<b>2003 Budgetary</b>				
	<b>Rural Community Advancement Program</b>	<b>Rural Electrification/ Telecommunication Funds</b>	<b>Rural Telephone Bank Funds</b>	<b>Rural Housing Funds</b>	<b>Rental Assistance Programs</b>
Status of Budgetary Resources:					
Obligations Incurred:					
Direct	\$ 1,252	\$ 1,191	\$ 35	\$ 1,200	\$ 724
Reimbursable	0	0	0	0	0
Subtotal	<u>1,252</u>	<u>1,191</u>	<u>35</u>	<u>1,200</u>	<u>724</u>
Unobligated Balance:					
Apportioned	169	0	0	14	0
Unobligated Balance Not Available	80	375	1,202	247	2
Total Status of Budgetary Resources	<u>\$ 1,501</u>	<u>\$ 1,566</u>	<u>\$ 1,237</u>	<u>\$ 1,461</u>	<u>\$ 726</u>
Relationship of Obligations to Outlays:					
Obligated Balance, Net, Beginning of Period	\$ 2,682	\$ 380	\$ 117	\$ 412	\$ 2,789
Obligated Balance, Net, End of Period:					
Accounts Receivable	0	0	(57)	0	0
Unfilled Customer Orders from Federal Resources	0	0	0	0	0
Undelivered Orders	2,757	269	82	243	2,747
Accounts Payable	78	115	28	116	46
Outlays:					
Disbursements	1,076	1,182	29	1,164	720
Collections	(496)	(3,350)	(247)	(1,778)	0
Subtotal	<u>580</u>	<u>(2,168)</u>	<u>(218)</u>	<u>(614)</u>	<u>720</u>
Less: Offsetting Receipts	37	70	4	673	0
Net Outlays	<u>\$ 543</u>	<u>\$ (2,238)</u>	<u>\$ (222)</u>	<u>\$ (1,287)</u>	<u>\$ 720</u>

**REQUIRED SUPPLEMENTARY INFORMATION***Amounts are presented in millions.*

	<b>2003 Budgetary</b>			
	<b>Rural Housing Grants</b>	<b>Salaries &amp; Expense</b>	<b>Other</b>	<b>Total</b>
Budgetary Resources:				
Budget Authority				
Appropriations Received	\$ 114	\$ 146	\$ 96	\$ 3,545
Borrowing Authority	0	0	0	0
Net Transfers	(2)	0	60	82
Unobligated Balance:				
Beginning of Period	42	45	118	1,487
Spending Authority from Offsetting Collections:				
Earned				
Collected	0	491	20	6,382
Receivable from Federal Sources	0	(4)	17	69
Change in Unfilled Customer Orders				
Without Advance from Federal Sources	0	0	0	0
Subtotal	0	487	37	6,451
Recoveries of Prior Year Obligations	4	50	9	193
Permanently Not Available	(12)	(18)	(10)	(4,101)
Total Budgetary Resources	<u>\$ 146</u>	<u>\$ 710</u>	<u>\$ 310</u>	<u>\$ 7,657</u>

**REQUIRED SUPPLEMENTARY INFORMATION***Amounts are presented in millions.*

	<b>2003 Budgetary</b>			
	<b>Rural Housing Grants</b>	<b>Salaries &amp; Expense</b>	<b>Other</b>	<b>Total</b>
Status of Budgetary Resources:				
Obligations Incurred:				
Direct	\$ 122	\$ 186	\$ 162	\$ 4,872
Reimbursable	0	487	0	487
Subtotal	<u>122</u>	<u>673</u>	<u>162</u>	<u>5,359</u>
Unobligated Balance:				
Apportioned	24	3	107	317
Unobligated Balance Not Available	0	34	41	1,981
Total Status of Budgetary Resources	<u>\$ 146</u>	<u>\$ 710</u>	<u>\$ 310</u>	<u>\$ 7,657</u>
Relationship of Obligations to Outlays:				
Obligated Balance, Net, Beginning of Period	\$ 134	\$ 126	\$ 133	\$ 6,773
Obligated Balance, Net, End of Period:				
Accounts Receivable	0	(1)	(36)	(94)
Unfilled Customer Orders from Federal Resources	0	0	0	0
Undelivered Orders	168	109	224	6,599
Accounts Payable	2	23	3	411
Outlays:				
Disbursements	82	622	79	4,954
Collections	0	(491)	(20)	(6,382)
Subtotal	<u>82</u>	<u>131</u>	<u>59</u>	<u>(1,428)</u>
Less: Offsetting Receipts	0	0	6	790
Net Outlays	<u>\$ 82</u>	<u>\$ 131</u>	<u>\$ 53</u>	<u>\$ (2,218)</u>

**REQUIRED SUPPLEMENTARY INFORMATION***Amounts are presented in millions.***2003 Non-Budgetary Credit Program Financing Accounts**

	<b>Rural Community Advancement Program</b>	<b>Rural Electrification/ Telecommunication/ Funds</b>	<b>Rural Telephone Bank Funds</b>	<b>Rural Housing Funds</b>	<b>Rental Assistance Programs</b>
Budgetary Resources:					
Budget Authority:					
Appropriations Received	0	0	0	0	0
Borrowing Authority	\$ 994	\$ 4,418	\$ 169	\$ 1,673	\$ 0
Net Transfers	0	0	0	0	0
Unobligated Balance:					
Beginning of Period	243	362	17	431	0
Spending Authority from Offsetting Collections:					
Earned					
Collected	1,032	1,256	94	2,029	0
Receivable from Federal Sources	3	0	0	0	0
Change in Unfilled Customer Orders					
Without Advance from Federal Sources	(5)	(5)	1	54	0
Subtotal	1,030	1,251	95	2,083	0
Recoveries of Prior Year Obligations	136	32	32	78	0
Permanently Not Available	(378)	(746)	(116)	(528)	0
Total Budgetary Resources	<u>\$ 2,025</u>	<u>\$ 5,317</u>	<u>\$ 197</u>	<u>\$ 3,737</u>	<u>\$ 0</u>

**REQUIRED SUPPLEMENTARY INFORMATION***Amounts are presented in millions.***2003 Non-Budgetary Credit Program Financing Accounts**

	<b>Rural Community Advancement Program</b>	<b>Rural Electrification/ Telecommunication Funds</b>	<b>Rural Telephone Bank Funds</b>	<b>Rural Housing Funds</b>	<b>Rental Assistance Programs</b>
Status of Budgetary Resources:					
Obligations Incurred:					
Direct	\$ 1,640	\$ 5,307	\$ 196	\$ 2,758	\$ 0
Reimbursable	0	0	0	0	0
Subtotal	<u>1,640</u>	<u>5,307</u>	<u>196</u>	<u>2,758</u>	<u>0</u>
Unobligated Balance:					
Apportioned	355	0	0	683	0
Unobligated Balance Not Available	30	10	1	296	0
Total Status of Budgetary Resources	<u>\$ 2,025</u>	<u>\$ 5,317</u>	<u>\$ 197</u>	<u>\$ 3,737</u>	<u>\$ 0</u>
Relationship of Obligations to Outlays:					
Obligated Balance, Net, Beginning of Period	\$ 2,932	\$ 8,315	\$ 1,091	\$ 551	\$ 0
Obligated Balance, Net, End of Period:					
Accounts Receivable	(3)	0	0	0	0
Unfilled Customer Orders from Federal Resources	(306)	(62)	(20)	(271)	0
Undelivered Orders	3,223	9,561	1,189	831	0
Accounts Payable	0	2	0	0	0
Outlays:					
Disbursements	1,526	4,095	84	2,617	0
Collections	(1,032)	(1,256)	(94)	(2,029)	0
Subtotal	<u>494</u>	<u>2,839</u>	<u>(10)</u>	<u>588</u>	<u>0</u>
Less: Offsetting Receipts	0	0	0	0	0
Net Outlays	<u>\$ 494</u>	<u>\$ 2,839</u>	<u>\$ (10)</u>	<u>\$ 588</u>	<u>\$ 0</u>

## REQUIRED SUPPLEMENTARY INFORMATION

Amounts are presented in millions.

<u>2003 Non-Budgetary Credit Program Financing Accounts</u>				
	<u>Rural Housing Grants</u>	<u>Salaries &amp; Expense</u>	<u>Other</u>	<u>Total</u>
Budgetary Resources:				
Budget Authority				
Appropriations Received	\$ 0	\$ 0	\$ 0	\$ 0
Borrowing Authority	0	0	122	7,376
Net Transfers	0	0	0	0
Unobligated Balance:				
Beginning of Period	0	0	23	1,076
Spending Authority from Offsetting Collections:				
Earned				
Collected	0	0	60	4,471
Receivable from Federal Sources	0	0	1	4
Change in Unfilled Customer Orders				
Without Advance from Federal Sources	0	0	3	48
Subtotal	0	0	64	4,523
Recoveries of Prior Year Obligations	0	0	68	346
Permanently Not Available	0	0	(98)	(1,866)
Total Budgetary Resources	<u>\$ 0</u>	<u>\$ 0</u>	<u>\$ 179</u>	<u>\$ 11,455</u>



**REQUIRED SUPPLEMENTARY INFORMATION***Amounts are presented in millions.***2003 Non-Budgetary Credit Program Financing Accounts**

	<b>Rural Housing Grants</b>	<b>Salaries &amp; Expense</b>	<b>Other</b>	<b>Total</b>
Status of Budgetary Resources:				
Obligations Incurred:				
Direct	\$ 0	\$ 0	\$ 163	\$ 10,064
Reimbursable	0	0	0	0
Subtotal	<u>0</u>	<u>0</u>	<u>163</u>	<u>10,064</u>
Unobligated Balance:				
Apportioned	0	0	5	1,043
Unobligated Balance Not Available	0	0	11	348
Total Status of Budgetary Resources	<u>\$ 0</u>	<u>\$ 0</u>	<u>\$ 179</u>	<u>\$ 11,455</u>
Relationship of Obligations to Outlays:				
Obligated Balance, Net, Beginning of Period	\$ 0	\$ 0	\$ 268	\$ 13,157
Obligated Balance, Net, End of Period:				
Accounts Receivable	0	0	(1)	(4)
Unfilled Customer Orders from Federal Resources	0	0	(55)	(714)
Undelivered Orders	0	0	301	15,105
Accounts Payable	0	0	0	2
Outlays:				
Disbursements	0	0	112	8,434
Collections	0	0	(60)	(4,471)
Subtotal	<u>0</u>	<u>0</u>	<u>52</u>	<u>3,963</u>
Less: Offsetting Receipts	0	0	0	0
Net Outlays	<u>\$ 0</u>	<u>\$ 0</u>	<u>\$ 52</u>	<u>\$ 3,963</u>

**REQUIRED SUPPLEMENTARY INFORMATION***Amounts are presented in millions.*

	<b>2002 Budgetary</b>				
	<b>Rural Community Advancement Program</b>	<b>Rural Electrification/ Telecommunication Funds</b>	<b>Rural Telephone Bank Funds</b>	<b>Rural Housing Funds</b>	<b>Rental Assistance Programs</b>
Budgetary Resources:					
Budget Authority					
Appropriations Received	\$ 2,582	\$ 86	\$ 11	\$ 837	\$ 763
Borrowing Authority	0	1	0	0	0
Net Transfers	460	103	(23)	(4)	0
Unobligated Balance:					
Beginning of Period	98	3	772	156	9
Spending Authority from Offsetting Collections:					
Earned					
Collected	428	2,858	220	1,866	0
Receivable from Federal Sources	0	0	0	0	0
Change in Unfilled Customer Orders					
Without Advance from Federal Sources	0	0	0	0	0
Subtotal	428	2,858	220	1,866	0
Recoveries of Prior Year Obligations	32	20	8	24	0
Permanently Not Available	(1,853)	(1,839)	(10)	(1,491)	(63)
Total Budgetary Resources	<u>\$ 1,747</u>	<u>\$ 1,232</u>	<u>\$ 978</u>	<u>\$ 1,388</u>	<u>\$ 709</u>

**REQUIRED SUPPLEMENTARY INFORMATION***Amounts are presented in millions.*

	<b>2002 Budgetary</b>				
	<b>Rural Community Advancement Program</b>	<b>Rural Electrification/ Telecommunication Funds</b>	<b>Rural Telephone Bank Funds</b>	<b>Rural Housing Funds</b>	<b>Rental Assistance Programs</b>
Status of Budgetary Resources:					
Obligations Incurred:					
Direct	\$ 1,567	\$ 1,143	\$ 33	\$ 1,324	\$ 705
Reimbursable	0	0	0	0	0
Subtotal	<u>1,567</u>	<u>1,143</u>	<u>33</u>	<u>1,324</u>	<u>705</u>
Unobligated Balance:					
Apportioned	71	0	0	21	3
Unobligated Balance Not Available	109	89	945	43	1
Total Status of Budgetary Resources	<u>\$ 1,747</u>	<u>\$ 1,232</u>	<u>\$ 978</u>	<u>\$ 1,388</u>	<u>\$ 709</u>
Relationship of Obligations to Outlays:					
Obligated Balance, Net, Beginning of Period	\$ 2,377	\$ 572	\$ 123	\$ 539	\$ 2,738
Obligated Balance, Net, End of Period:					
Accounts Receivable	0	0	0	0	0
Unfilled Customer Orders from Federal Resources	0	0	0	0	0
Undelivered Orders	2,599	278	95	270	2,741
Accounts Payable	84	103	21	142	48
Outlays:					
Disbursements	1,229	1,314	31	1,427	654
Collections	(428)	(2,858)	(220)	(1,866)	0
Subtotal	<u>801</u>	<u>(1,544)</u>	<u>(189)</u>	<u>(439)</u>	<u>654</u>
Less: Offsetting Receipts	54	26	3	269	0
Net Outlays	<u>\$ 747</u>	<u>\$ (1,570)</u>	<u>\$ (192)</u>	<u>\$ (708)</u>	<u>\$ 654</u>

**REQUIRED SUPPLEMENTARY INFORMATION***Amounts are presented in millions.*

	<b>2002 Budgetary</b>			
	<b>Rural Housing Grants</b>	<b>Salaries &amp; Expense</b>	<b>Other</b>	<b>Total</b>
Budgetary Resources:				
Budget Authority				
Appropriations Received	\$ 105	\$ 150	\$ 84	\$ 4,618
Borrowing Authority	0	0	0	1
Net Transfers	0	0	52	588
Unobligated Balance:				
Beginning of Period	39	53	29	1,159
Spending Authority from Offsetting Collections:				
Earned				
Collected	0	497	8	5,877
Receivable from Federal Sources	0	(23)	12	(11)
Change in Unfilled Customer Orders				
Without Advance from Federal Sources	0	0	0	0
Subtotal	0	474	20	5,866
Recoveries of Prior Year Obligations	5	174	4	267
Permanently Not Available	0	(28)	(5)	(5,289)
Total Budgetary Resources	<u>\$ 149</u>	<u>\$ 823</u>	<u>\$ 184</u>	<u>\$ 7,210</u>

**REQUIRED SUPPLEMENTARY INFORMATION***Amounts are presented in millions.*

	<b>2002 Budgetary</b>			
	<b>Rural Housing Grants</b>	<b>Salaries &amp; Expense</b>	<b>Other</b>	<b>Total</b>
Status of Budgetary Resources:				
Obligations Incurred:				
Direct	\$ 107	\$ 296	\$ 67	\$ 5,242
Reimbursable	0	481	0	481
Subtotal	<u>107</u>	<u>777</u>	<u>67</u>	<u>5,723</u>
Unobligated Balance:				
Apportioned	42	3	67	207
Unobligated Balance Not Available	0	43	50	1,280
Total Status of Budgetary Resources	<u>\$ 149</u>	<u>\$ 823</u>	<u>\$ 184</u>	<u>\$ 7,210</u>
Relationship of Obligations to Outlays:				
Obligated Balance, Net, Beginning of Period	\$ 107	\$ 123	\$ 150	\$ 6,729
Obligated Balance, Net, End of Period:				
Accounts Receivable	0	(6)	(19)	(25)
Unfilled Customer Orders from Federal Resources	0	0	0	0
Undelivered Orders	132	96	149	6,360
Accounts Payable	2	35	3	438
Outlays:				
Disbursements	75	624	68	5,422
Collections	0	(497)	(8)	(5,877)
Subtotal	<u>75</u>	<u>127</u>	<u>60</u>	<u>(455)</u>
Less: Offsetting Receipts	0	0	4	356
Net Outlays	<u>\$ 75</u>	<u>\$ 127</u>	<u>\$ 56</u>	<u>\$ (811)</u>

**REQUIRED SUPPLEMENTARY INFORMATION***Amounts are presented in millions.***2002 Non-Budgetary Credit Program Financing Accounts**

	<b>Rural Community Advancement Program</b>	<b>Rural Electrification/ Telecommunication Funds</b>	<b>Rural Telephone Bank Funds</b>	<b>Rural Housing Funds</b>	<b>Rental Assistance Programs</b>
Budgetary Resources:					
Budget Authority:					
Appropriations Received	\$ 0	\$ 0	\$ 0	\$ 0	\$ 0
Borrowing Authority	1,531	4,969	174	1,302	0
Net Transfers	0	0	0	0	0
Unobligated Balance:					
Beginning of Period	113	6	5	478	0
Spending Authority from Offsetting Collections:					
Earned					
Collected	738	976	49	1,804	0
Receivable from Federal Sources	(319)	(90)	(16)	(213)	0
Change in Unfilled Customer Orders					
Without Advance from Federal Sources	311	68	19	217	0
Subtotal	730	954	52	1,808	0
Recoveries of Prior Year Obligations	80	34	22	69	0
Permanently Not Available	(123)	(278)	(35)	(844)	0
Total Budgetary Resources	<u>\$ 2,331</u>	<u>\$ 5,685</u>	<u>\$ 218</u>	<u>\$ 2,813</u>	<u>\$ 0</u>

**REQUIRED SUPPLEMENTARY INFORMATION***Amounts are presented in millions.***2002 Non-Budgetary Credit Program Financing Accounts**

	<b>Rural Community Advancement Program</b>	<b>Rural Electrification/ Telecommunication/ Funds</b>	<b>Rural Telephone Bank Funds</b>	<b>Rural Housing Funds</b>	<b>Rental Assistance Programs</b>
Status of Budgetary Resources:					
Obligations Incurred:					
Direct	\$ 2,088	\$ 5,323	\$ 201	\$ 2,381	\$ 0
Reimbursable	0	0	0	0	0
Subtotal	<u>2,088</u>	<u>5,323</u>	<u>201</u>	<u>2,381</u>	<u>0</u>
Unobligated Balance:					
Apportioned	140	0	0	113	0
Unobligated Balance Not Available	103	362	17	319	0
Total Status of Budgetary Resources	<u>\$ 2,331</u>	<u>\$ 5,685</u>	<u>\$ 218</u>	<u>\$ 2,813</u>	<u>\$ 0</u>
Relationship of Obligations to Outlays:					
Obligated Balance, Net, Beginning of Period	\$ 2,319	\$ 6,208	\$ 1,001	\$ 487	\$ 0
Obligated Balance, Net, End of Period:					
Accounts Receivable	0	0	0	0	0
Unfilled Customer Orders from Federal Resources	(311)	(68)	(19)	(217)	0
Undelivered Orders	3,244	8,382	1,110	768	0
Accounts Payable	0	0	0	0	0
Outlays:					
Disbursements	1,402	3,205	86	2,244	0
Collections	(738)	(976)	(49)	(1,804)	0
Subtotal	<u>664</u>	<u>2,229</u>	<u>37</u>	<u>440</u>	<u>0</u>
Less: Offsetting Receipts	0	0	0	0	0
Net Outlays	<u>\$ 664</u>	<u>\$ 2,229</u>	<u>\$ 37</u>	<u>\$ 440</u>	<u>\$ 0</u>

## REQUIRED SUPPLEMENTARY INFORMATION

Amounts are presented in millions.

2002 Non-Budgetary Credit Program Financing Accounts

	<u>Rural Housing Grants</u>	<u>Salaries &amp; Expense</u>	<u>Other</u>	<u>Total</u>
Budgetary Resources:				
Budget Authority				
Appropriations Received	\$ 0	\$ 0	\$ 0	\$ 0
Borrowing Authority	0	0	127	8,103
Net Transfers	0	0	0	0
Unobligated Balance:				
Beginning of Period	0	0	10	612
Spending Authority from Offsetting Collections:				
Earned				
Collected	0	0	67	3,634
Receivable from Federal Sources	0	0	(56)	(694)
Change in Unfilled Customer Orders				
Without Advance from Federal Sources	0	0	51	666
Subtotal	<u>0</u>	<u>0</u>	<u>62</u>	<u>3,606</u>
Recoveries of Prior Year Obligations	0	0	6	211
Permanently Not Available	0	0	(16)	(1,296)
Total Budgetary Resources	<u>\$ 0</u>	<u>\$ 0</u>	<u>\$ 189</u>	<u>\$ 11,236</u>



**REQUIRED SUPPLEMENTARY INFORMATION***Amounts are presented in millions.***2002 Non-Budgetary Credit Program Financing Accounts**

	<b>Rural Housing Grants</b>	<b>Salaries &amp; Expense</b>	<b>Other</b>	<b>Total</b>
Status of Budgetary Resources:				
Obligations Incurred:				
Direct	\$ 0	\$ 0	\$ 167	\$ 10,160
Reimbursable	0	0	0	0
Subtotal	<u>0</u>	<u>0</u>	<u>167</u>	<u>10,160</u>
Unobligated Balance:				
Apportioned	0	0	21	274
Unobligated Balance Not Available	0	0	1	802
Total Status of Budgetary Resources	<u>\$ 0</u>	<u>\$ 0</u>	<u>\$ 189</u>	<u>\$ 11,236</u>
Relationship of Obligations to Outlays:				
Obligated Balance, Net, Beginning of Period	\$ 0	\$ 0	\$ 217	\$ 10,232
Obligated Balance, Net, End of Period:				
Accounts Receivable	0	0	0	0
Unfilled Customer Orders from Federal Resources	0	0	(51)	(666)
Undelivered Orders	0	0	319	13,823
Accounts Payable	0	0	0	0
Outlays:				
Disbursements	0	0	116	7,053
Collections	0	0	(68)	(3,635)
Subtotal	<u>0</u>	<u>0</u>	<u>48</u>	<u>3,418</u>
Less: Offsetting Receipts	0	0	0	0
Net Outlays	<u>\$ 0</u>	<u>\$ 0</u>	<u>\$ 48</u>	<u>\$ 3,418</u>