

Comments to the  
Rural Housing Service of the  
United States Department of Agriculture

Regarding Loan Servicing Request for Information

Notice ID: 12SAD225RFI-1

by National Consumer Law Center  
(on behalf of its low-income clients)

and

National Housing Law Project

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We are writing on behalf of the National Consumer Law Center and the National Housing Law Project in response to the United States Department of Agriculture's request for input from the public on the vendor solicitation proposal.

Since 1969, the nonprofit National Consumer Law Center® (NCLC®) has used its expertise in consumer law and energy policy to work for consumer justice and economic security for low-income and other disadvantaged people in the United States. NCLC's expertise includes policy analysis and advocacy; consumer law and energy publications; litigation; expert witness services, and training and advice for advocates. NCLC works with nonprofit and legal services organizations, private attorneys, policymakers, and federal and state government and courts across the nation to stop exploitative practices, help financially stressed families build and retain wealth, and advance economic fairness.

The National Housing Law Project's (NHLP) mission is to advance housing justice for poor people and communities. We achieve this by strengthening and enforcing the rights of tenants and homeowners, increasing housing opportunities for underserved communities, and preserving and expanding the nation's supply of safe and affordable homes. NHLP is considered one of the national experts on USDA's rural development programs, long advocating for equal access to these programs on behalf of low-income individuals and families eligible for and residing within USDA's Rural Development's multifamily and single-family programs.

The servicing of USDA Direct Loans presents an array of unique challenges. The program rules are highly complex. The borrower populations face persistent obstacles in their struggle to maintain homeownership. The vendor solicitation proposal outlined in the June 13, 2025 Direct Loan RFI, suggests that the agency is considering a significant, yet unclear outsourcing of USDA Direct Loan servicing.

These comments describe how the vendor solicitation proposal will exacerbate the chronic problems that Direct Loan borrowers already face. Because of the Direct Loan program's basic structure, any large-scale outsourcing of servicing is simply not feasible. For the reasons outlined below, the proposal described in the RFI will not save the government money. It will not promote efficiencies. It will lead to unnecessary loss of revenue. Given the complexity of the Direct Loan program and the high risk of default in the borrower population, it is highly unlikely that any vendor will find the venture profitable without significantly harming the health of the Direct Loan fund and borrowers. Rural homeowners, the beneficiaries that Congress intended for the program, will be worse off.

Our major concerns with the RFI include the following:

- The RFI is vague and confusing as to which servicing activities it proposes to assign to the vendor (*See Part 1, below*).

- The RFI fails to warn vendors about the particular vulnerabilities of the borrower population and the obstacles these present for servicing (Part 2).
- The RFI does not disclose facts about the extensive delinquency rates and long-standing arrearages that exist in the Direct Loan portfolio (Part 2).
- The RFI omits any coherent analysis of the essential role that the Government plays in the Direct Loan program and how this would impact a contracting servicer (Part 3).
- The RFI does not adequately describe the complexities of the Direct Loan statutory and regulatory scheme and the challenges these present for staffing, training, and the development of servicing platforms (Parts 4-6).
- The RFI fails to address the impact of outsourcing on the constitutional due process rights of Direct Loan borrowers (Part 3).
- The RFI fails to address the role of the USDA National Appeals Division in oversight of Direct Loan servicing (Part 3).
- The RFI ignores the substantial litigation risk that outsourcing will create both for the Government and the servicer, given the likelihood of systemic violations of federal and state servicing and foreclosure laws (Parts 3-6).
- The RFI does not take into account the loss in future revenue from repayments on the Direct Loans due to unnecessary foreclosures that will flow from mismanagement of payment subsidies, loss mitigation, and recapture (Parts 4, 6).
- The RFI fails to propose any minimum servicing standards that a vendor must meet (Part 7).
- The RFI does not consider how the accelerated loss of homeownership in rural areas from poor servicing of Direct Loans will further the downward economic spiral in these localities.
- The RFI does not consider how the loss of Social Security, VA, and tax benefits due to deteriorated Direct Loan servicing impacts the elderly, disabled, and poorest families in rural areas.

### **1. Introduction: The RFI is vague and confusing about the vendor's role.**

The RFI is strikingly unclear about the scope of the proposed vendor's authority. At certain points the proposal describes the vendor's tasks as providing support for the USDA's own servicing. Under this approach it appears that the vendor would perform

limited support tasks under the supervision of a “Federal oversight staff.”<sup>1</sup> Elsewhere, the RFI proposes what appears to be a complete outsourcing of Direct Loan servicing to a vendor.<sup>2</sup> Under this much broader delegation the vendor assumes responsibility for the entire range of Direct Loan servicing activities described in USDA regulations and handbooks. These include providing “first line service” to all Direct Loan borrowers, processing all communications with the borrowers, managing payment systems, escrow accounts, payment subsidies, loss mitigation, Treasury offsets, and dispute resolution.<sup>3</sup>

Adding to the confusion, the RFI suggests that the vendor’s role would be limited to activities that are not deemed “inherently governmental.”<sup>4</sup> The text gives only a few examples of “inherently governmental” tasks. These include responding to communications from Congressional staff and credit reporting.<sup>5</sup> However, elsewhere the same document lists responding to Congressional inquiries and credit reporting as tasks the vendor will have full authority to perform.<sup>6</sup> Throughout, the RFI makes little or no attempt to identify specific regulatory and handbook servicing functions that it deems to fall within or outside of the “inherently governmental” nomenclature. Traditional governmental functions are inextricably intertwined with all aspects of servicing Direct Loans. Therefore, the “inherently governmental” distinction the RFI attempts to make is confusing rather than helpful.

If the USDA is proposing a full-scale outsourcing of Direct Loan servicing obligations defined by its regulations and handbooks, it should say so. If USDA is proposing a limited outsourcing, it needs to make this clear and specify what those limitations are.

The Direct Loans exist as part of a government program. As we describe below in Part 3, the RFI glosses over the fact that Direct Loans are inherently part of a long-standing government program. A wholesale outsourcing of Direct Loan servicing is not only contrary to the structure Congress created, it is also impractical. Large scale outsourcing will trigger confusion, inefficiencies, and unnecessary expenditures. The consequences will be harmful to the government and to borrowers. The arrangement would also pose significant financial risks for the vendor.

## **2. USDA direct loans serve a distinct population of low-income borrowers.**

USDA section 502 direct borrowers are unlike any other group of homeowners whose mortgage loans are now being serviced in the United States. The Direct Loan eligibility requirements make this population distinct.

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<sup>1</sup> RFI, p. 6.

<sup>2</sup> *Id.*, pp. 8, 10.

<sup>3</sup> *Id.*, pp. 8-9.

<sup>4</sup> *Id.*, p. 5.

<sup>5</sup> *Id.*, p. 10.

<sup>6</sup> *Id.*, pp. 6, 8.

First, Direct Loan borrowers have low incomes. Several federal programs insure or guarantee mortgage loans for borrowers and properties that meet certain qualifications. This is true for the GSEs, FHA, VA, and the USDA (through its guaranteed home loan program). However, these programs do not exclusively serve borrowers whose incomes fall below a fixed level. USDA Direct Loan borrowers must have incomes that fall below a “low income” threshold.<sup>7</sup> Borrowers considered “very low income” are specifically defined as eligible for Direct Loans.<sup>8</sup> Direct Loan guidelines define “very low income” as less than 50% of the area median income based on family size.<sup>9</sup>

Second, to qualify for a Direct Loan potential borrowers must have been unable to obtain credit from other sources on terms and conditions they can reasonably be expected to fulfil.<sup>10</sup> Applicants for Direct Loans must submit documentation to establish this eligibility requirement.<sup>11</sup> If the applicant can obtain similar financing from other sources, the applicant is ineligible. Thus, by explicit program directive, Direct Loans are the home purchase option of last resort for low-income homeowners.

Third, the property qualifying for the Direct Loan must be in a rural area.<sup>12</sup> USDA defines rural areas as locations on open land or in towns with a population of 10,000 or less. A rural area can also include towns and cities with populations up to 20,000 that are outside of a Metropolitan Statistical Area and have a serious lack of mortgage credit for lower- and moderate-income families.<sup>13</sup>

These characteristics of Direct Loan borrowers present unique challenges for a servicer. Direct Loan borrowers inevitably face financial stressors that are more frequent and more severe than do borrowers under any other government-related insured or guaranteed loan program. They often face significant financial literacy barriers. In addition, Direct Loan borrowers tend to live in areas where job opportunities have eroded, and transportation and communication barriers are persistent.

As part of any RFI directed at a potential servicer, USDA needs to disclose the current default rates for its Direct Loan portfolio. A potential servicer needs to know the risks and challenges it would face in servicing these loans. For example, advocates in Maine reported to us that USDA recently referred approximately 500 Direct Loans for foreclosure in the state. Many of these had substantial delinquencies, with arrearages extending back five, ten, and even fifteen years. Arrearages such as these are unique in the servicing industry.

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<sup>7</sup> 7 C.F.R. § 3550.53(a) (referencing 42 U.S.C. § 1473a(b)(2)(A) which defines term to mean less than 80% of the median income for locality based on family size).

<sup>8</sup> 7 C.F.R. §§ 3550.51, 3550.53 (referencing 42 U.S.C. § 1473a(b)(2)(B)).

<sup>9</sup> *Id.*

<sup>10</sup> 7 C.F.R. §§ 3550.51, 3550.53(h).

<sup>11</sup> USDA Direct Loan Single Family Housing Loans and Grants – Field Office Handbook HB – 1-3550 § 4.16, at p. 4-16.

<sup>12</sup> 7 C.F.R. §§ 3550.10, 3550.56(a) Handbook HB-1-3550.1 § 5.3, p. 5-4.

<sup>13</sup> Handbook HB-1-3550.1 § 5.3, at p. 5-4.

### 3. Unique obligations arise when the U.S. Government is the direct owner of a loan.

Regardless of the entity chosen to service a USDA Direct Loan, the United States remains the loan's owner. For example, in a judicial proceeding to foreclose on a Direct Loan the United States must be named as the foreclosing party. The servicer acts solely as agent for the government. When a servicer takes on the responsibilities of agent for the government, its role is fundamentally different from that of any other servicer. The RFI largely ignores the significance of the role of United States as owner of the loans to be serviced.

As one appellate court noted, a USDA section 502 Direct Loan, "once made, creates a statutory entitlement and a property interest protected by the due process clause of the Fifth Amendment."<sup>14</sup> In its interactions with Direct Loan borrowers the USDA must comply with the constitutional due process obligation to provide notice and an opportunity to be heard when its decisions impact the participant's rights.<sup>15</sup> Acting through a servicer does not change this fact. Notices of adverse actions, such as the acceleration of a loan or the denial of a borrower's request for moratorium relief must comply not only with all applicable federal and state laws, but also with constitutional due process standards.

These due process protections do not come into play in the servicing of any other category of residential mortgage loan in the United States. Private parties hold the mortgage loans under the other federally insured programs, such as FHA, VA, and the USDA guaranteed loan programs. Despite the FHFA receivership over the GSEs, courts have held that due process protections do not apply in the servicing of GSE loans.<sup>16</sup> Yet, courts have consistently ruled that the USDA loans at issue in the RFI, as held directly by the United States, create constitutionally protected property interests for borrowers.<sup>17</sup>

A second important area where direct loans differ from all other mortgage loans is the availability of a formal administrative review procedure.<sup>18</sup> The USDA National Appeals Division ("NAD") functions similarly to other administrative hearing procedures

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<sup>14</sup> Johnson v. U.S.D.A., 734 F.2d 774, 782 (11th Cir. 1984).

<sup>15</sup> Johnson v. U.S.D.A., 734 F.2d 774, 782 (11th Cir. 1984); U.S. v. Henderson, 707 F.2d 853, 857-58 (5th Cir. 1983) (notice of acceleration must accurately inform borrowers of legal rights under direct loan program); Ramey v. U.S.D.A., 2020 WL 1844192 (S.D.W. Va. Apr. 10, 2020); Rau v. Cavanaugh, 500 F. Supp. 204, 206 (D.S.D. 1980).

<sup>16</sup> Compare Montilla v. Fed. Natl. Mtge. Assn., 999 F.3d 751 (1st Cir. 2021) (because Fannie Mae and Freddie Mac are not government actors subject to Fifth Amendment due process clause, they may proceed with nonjudicial foreclosure under Rhode Island law) and Johnson v U.S.D.A., 734 F.2d 774 (11th Cir. 1984) (foreclosure of USDA section 502 Direct Loan constitutes state action, granting class relief against use of Alabama non-judicial foreclosure procedure to foreclose section 502 loans); Rau v. Cavanaugh, 500 F. Supp. 204 (D.S.D. 1980) (non-judicial foreclosure conducted under South Dakota law did not adequately protect Direct Loan borrower's due process rights).

<sup>17</sup> Johnson v. U.S.D.A., 734 F.2d 774, 782 (11th Cir. 1984); Rau v. Cavanaugh, 500 F. Supp. 204, 206 (D.S.D. 1980) (benefits under Direct Loan program cannot be terminated without due process safeguards)

<sup>18</sup> 42 U.S.C. § 1480(g); 7 C.F.R. § 3550.4; Handbook HB-1-3550.1 § 1.9 – 1.11.

that allow an aggrieved participant in a government program to seek review of an adverse agency decision. The Social Security Administration, for example, offers a similar option for review of agency decisions by a hearing officer. For USDA Direct Loans, appeals must be processed in accordance the NAD Rules of Procedure.<sup>19</sup> The NAD appeals system implements the judicial directive to ensure that borrowers' property interests arising from participation in the Direct Loan program are not impaired without notice and an opportunity to be heard before a neutral third party.<sup>20</sup>

Direct Loan borrowers must be notified of appeal and review options when an adverse decision affects their rights under the program.<sup>21</sup> Appealable decisions include determinations of the borrower's monthly payment amount, a denial of a request for moratorium relief, a loan acceleration, or a foreclosure.<sup>22</sup> The hearing officer's decision must be based on a documented agency record that is provided to the borrower before the hearing.<sup>23</sup> Appeal decisions are subject to a USDA Director review and further judicial review after the final Director determination.<sup>24</sup> USDA reviews involve not only the option for a hearing on the record before a hearing officer, but also mediation and other less formal reviews.<sup>25</sup>

USDA decisions affecting borrowers in the Direct Loan program are also subject to review under the Administrative Procedure Act ("APA").<sup>26</sup> Under the APA courts can review a federal agency decision and set it aside as arbitrary and capricious or contrary to law.

In addition to the constitutional and administrative review protections, USDA regulations impose duties on the servicer of a Direct Loan. Compliance with USDA regulatory requirements is a condition to foreclosure of a direct loan.<sup>27</sup> A servicer's noncompliance with Direct Loan regulations can be asserted as a defense to a judicial foreclosure or raised as a ground to oppose a non-judicial foreclosure. For example, a

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<sup>19</sup> 7 C.F.R. part 11.

<sup>20</sup> *Johnson v. U.S.D.A.*, 734 F.2d 774, 782 (11th Cir. 1984) (granting relief based on court's view that the USDA system for appeals in effect at the time did not provide for neutral decision maker required by due process).

<sup>21</sup> Handbook HB-1-3550.1 Ch. 1, Appendix 1-B, 1-C.

<sup>22</sup> 7 C.F.R. § 11.3(a).

<sup>23</sup> 7 C.F.R. § 11.10(c).

<sup>24</sup> 7 C.F.R. § 11.9 (Director Review); 7 C.F.R. § 11.13 (judicial review).

<sup>25</sup> Handbook HB-1-3550.1 § 1.11.

<sup>26</sup> *Wood v. United States Dept. of Agric. Rural Hous. Serv.*, 2020 WL 1521801, at \*7 (S.D.W. Va. Mar. 30, 2020); *United States v. Brown*, 2014 WL 657518, at \*1 (E.D. Pa. Feb. 20, 2014) ("The Administrative Procedures Act (APA) applies to the decision to foreclose, as foreclosure by a federal agency under the National Housing Act is typically treated as an administrative decision.").

<sup>27</sup> *United States v. Brewer*, 1996 WL 34494311, at \*5 (D. Vt. Sept. 18, 1996); *United States v. Gomiller*, 545 F. Supp. 17, 21 (N.D. Miss. 1981).

servicer's failure to give a required notice or to consider the borrower for a moratorium could significantly impair USDA's foreclosure remedies.<sup>28</sup>

Finally, as an agency of the United States, USDA has access to two powerful offset remedies for collection of debts owed to it under the Direct Loan program. The agency routinely uses both.<sup>29</sup> One is the ability to offset USDA debts against funds that borrowers receive from the federal government.<sup>30</sup> These include Social Security retirement and Veterans benefits. The other is an offset against tax refunds due to a borrower from the IRS. Tax intercepts can include earned income tax credit benefits payable to low-income families.<sup>31</sup> Low-income rural borrowers rely heavily on government benefit programs and tax refunds that are subject to these offsets.

USDA pursues offsets for debts owed for existing loans in default and for loans that went through foreclosure leaving a deficiency claim.<sup>32</sup> The offsets can have a lifelong, devastating impact on families. It is highly unlikely that any private mortgage servicing company has experience with the federal offset program. The RFI proposal would likely lead to an inexperienced entity playing a key role in running a program capable of causing devastating harm to low-income rural families.

#### **4. The complexity of the Direct Loan payment subsidy program**

The USDA Direct Loan program includes a system of ongoing payment subsidies for borrowers.<sup>33</sup> No other mortgage loan program relies on a similar system. The amount of subsidy a Direct Loan borrower receives depends on household income. The goal is to set the borrower's monthly payment at an affordable level by calculating the borrower's actual monthly payment as a percentage of income.<sup>34</sup> The subsidy pays the portion of the contractually due payment that the borrower cannot afford, while the borrower pays the rest. The system is similar to those used to set rent levels in federally subsidized rental housing programs.

A servicer of Direct Loans would be under a duty to calculate each borrower's monthly payment level on an ongoing basis for the life of a loan. The servicer would have to set up an annual income review for each borrower.<sup>35</sup> For each review the servicer must examine the income of all household members.<sup>36</sup> This involves the solicitation of

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<sup>28</sup> Ramey v. U.S.D.A., 2020 WL 1844192 (S.D.W. Va. Apr. 10, 2020); United States v. Brewer, 1996 WL 34494311, at \*5 (D. Vt. Sept. 18, 1996).

<sup>29</sup> 7 C.F.R. § 3550.10 (defining "offset").

<sup>30</sup> 7 C.F.R. § 3550.210 (c).

<sup>31</sup> 7 C.F.R. § 3550.210 (a).

<sup>32</sup> 7 C.F.R. §§ 3550.211(a), 3550.252(g).

<sup>33</sup> 7 C.F.R. §§ 3550.68 (noting the subsidies can be in one of three forms: interest credit, payment assistance method 1, and payment assistance method 2).

<sup>34</sup> 7 C.F.R. §§ 3550.53(a); 3550.54; Handbook HB-2-3550-2 § 4.7, at p. 4-15.

<sup>35</sup> 7 C.F.R. §§ 3550.157(a)(1); Handbook HB-2-3550-2 § 4.7, at p. 4-15.

<sup>36</sup> Handbook HB-2-3550-2 § 4.7, at p. 4-16.



documentation of each individual's current income.<sup>37</sup> Documentation must be in the form of paystubs or evidence of self-employment income.<sup>38</sup> After determining income, the servicer applies a series of deductions, such as for dependents, child care costs, medical expenses, and expenses related to elderly or disabled household members.<sup>39</sup> Whenever any household member experiences a change of income, the servicer must perform an interim review.<sup>40</sup> As a loss mitigation option the servicer must also review borrowers facing foreclosure for a revision of the payment subsidy.<sup>41</sup>

## 5. Payment Subsidy Recapture

As described above, payment subsidy is a unique feature of the USDA Direct Loan program. The obligation to repay the subsidy is also unique to the program. Direct Loan borrowers must repay all or part of the subsidies that lowered their payments over the life of the loan.<sup>42</sup> Repayment is generally due when the loan is paid off or when the borrower ceases to occupy the property. However, the full recapture debt also comes due upon a foreclosure.<sup>43</sup> The formula for calculating the recapture amount is complex. The calculation takes into account the current property valuation, appreciation since the loan was taken out, and the value of capital improvements made since loan origination.<sup>44</sup>

The subsidy recapture amount can be significant, often exceeding the amount of the original loan principal. Direct Loan borrowers are often surprised when they learn that they owe the debt, and at the extent of their indebtedness.<sup>45</sup> A Direct Loan servicer would be responsible for collecting the recapture debt. Collection options include the drastic remedies of federal benefits offsets and seizure of tax refunds.

The recapture debt can impact all aspects of servicing a Direct Loan. For example, federal and state laws require that servicers provide borrowers with ongoing account statements and, upon request, payoff statements. By law, periodic account statements and payoff statements must itemize the outstanding debt in specific ways. Accounting for the recapture claim in these communications presents a significant challenge. Servicers who do not accurately communicate amounts owed can face

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<sup>37</sup> Handbook HB-2-3550-2 § 4.8, at p. 4-33.

<sup>38</sup> *Id.* pp. 4-33 – 4-37.

<sup>39</sup> 7 C.F.R. § 3550.54 (b) and (c); Handbook HB-2-3550-2 § 4.9.

<sup>40</sup> 7 C.F.R. § 3550.157(a)(3).

<sup>41</sup> 7 C.F.R. § 3550.204.

<sup>42</sup> 7 C.F.R. § 3550.162; Handbook HB-2-3550-2 ch 2 § 5.

<sup>43</sup> 7 C.F.R. § 3550.162(a),(b).

<sup>44</sup> Handbook HB-2-3550-2 § 2.23.

<sup>45</sup> *Allen v U.S.D.A.*, 698 F. Supp. 669, 672 (S.D. Miss. 1988) (direct loan borrowers could not challenge obligation to pay subsidy recapture based on claim they had not been adequately informed of obligation); *In re Robles Lugo*, 2022 WL 2068720, at \*3 (Bankr. D.P.R. June 8, 2022) (direct loan subsidy recapture is secured claim against the property, borrower's lack of understanding of the claim not a basis to challenge it).

statutory penalties and other legal claims. Similarly, pre-foreclosure notices required under state laws typically require a specific itemization of the outstanding debt. Errors in these notices can make a foreclosure vulnerable to challenge.<sup>46</sup> A servicer unfamiliar with the complexities of the Direct Loan program is likely to run afoul of an array of state and federal laws that regulate routine servicing and foreclosure.

The payment subsidy and recapture aspects of the Direct Loan program present distinct challenges for a servicing platform. The RFI is unclear about whose platform the vendor would use. USDA acknowledges that its current servicing software platform for Direct Loans is outdated and needs to be replaced.<sup>47</sup> It is highly likely that a vendor would have to develop a unique new platform designed for the intricacies of Direct Loan servicing. The RFI glosses over the need for this significant investment on the part of a contracting servicer.

## **6. Implementation of moratorium relief and other loss mitigation options**

Beginning with the 2008 foreclosure crises, the major institutional owners, guarantors, and insurers of home mortgage loans substantially revised their loss mitigation guidelines. This was true for the GSEs, FHA, VA, and USDA guaranteed loan programs. The industry's across-the-board changes included flexible new options for loan modifications. The goal of these modifications was to reinstate defaulted loans with terms that allowed for affordable payments for the remainder of the loan term. The formulae for these modifications have evolved since the foreclosure crisis, but affordable modification options have now become embedded as important features in all of today's loss mitigation protocols, with the exception of the USDA Direct Loan program.

Unlike the rest of the industry, the Direct Loan program's loss mitigation structure has remained essentially unchanged for decades. The system relies on a very limited number of tools, and these are unique to the Direct Loan program. The payment subsidy option, if implemented properly, helps to lower borrowers' payments when they experience income reductions. As described above, effective management of payment subsidies requires significant servicer resources and expertise.

Aside from payment subsidies and repayment plans, the centerpiece of loss mitigation for Direct Loans has always been the "moratorium" on payments.<sup>48</sup> The moratorium is a suspension of the borrower's payment obligation for up to two years. By federal statute, USDA must make moratorium relief available to borrowers who experience a temporary reduction of income or increased expenses due to circumstances beyond their control.<sup>49</sup>

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<sup>46</sup> 42 U.S.C. § 1475(b); *United States v. Buskell*, 2014 WL 1765386 (E.D. Pa. May 2, 2014) (USDA must provide pre-foreclosure notices required under Pennsylvania law to the extent the state law requirements are more favorable to the borrower than any USDA provisions).

<sup>47</sup> USDA-OIG Rural Development's Financial Statement for Fiscal Years 2023-2024 Audit Report 85401-0015-11 (Nov. 2024), pp. 17-18.

<sup>48</sup> 42 U.S.C. § 1475; 7 C.F.R. § 3550.207.

<sup>49</sup> *Id.*

Effective implementation of the Direct Loan moratorium program requires that a servicer perform specified tasks set out in USDA guidance. First and foremost, the servicer must understand when moratorium relief will be helpful for a particular borrower and offer the option.<sup>50</sup> Moratorium eligibility criteria are specific to USDA Direct Loans.<sup>51</sup> These criteria include a complex test to assess changes in borrower income, and have been the subject of litigation.<sup>52</sup> Once a servicer has approved a moratorium it must monitor the borrower's continuing eligibility for up to two years and terminate the moratorium when appropriate.<sup>53</sup> When a moratorium terminates, the servicer must assess the borrower's repayment ability and calculate a reamortization of the loan.<sup>54</sup>

Non-compliance with moratorium requirements and failure to implement loss mitigation reviews generally is a defense to a foreclosure of a Direct Loan. If a servicer mishandles loss mitigation, USDA will be unable to enforce mortgages through foreclosure.<sup>55</sup>

## 7. Minimum Servicing Standards

A key component of any outsourcing of Direct Loan servicing must be a set of clear minimal standards for servicing. The RFI does not set out clear standards. Any proposal should include, at a minimum:

- Clear, accurate, and consistent communications with borrowers and authorized third parties about all aspects of the servicing of the loan, including:
  - Loan status
  - P&I payments and other amounts due
  - Application of payments
  - Subsidy determinations
  - Options available to borrowers with financial hardships
  - Borrower's rights
  - Subsidy recapture
  - Loan/payment history
  - Referrals to the Treasury Offset Program

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<sup>50</sup> Handbook HB-2-3550-2 § 5.5 p. 5-13 “Although some borrowers may be knowledgeable enough to request a moratorium, more typically the Servicing Office will recognize that a borrower is a candidate for a moratorium and propose it to the borrower.”

<sup>51</sup> Handbook HB-2-3550-2 § 5.5 pp. 5-13 and 5-14.

<sup>52</sup> Ramey v. U.S.D.A., 2020 WL 1844192 (S.D.W. Va. Apr. 10, 2020); United States v. Shields, 733 F. Supp 776 (D. Vt. 1989); United States v. Gomiller, 545 F. Supp.17 (N.D. Miss. 1981).

<sup>53</sup> Handbook HB-2-3550-2 § 5.5 p. 5-14.

<sup>54</sup> Handbook HB-2-3550-2 § 5.5 p. 5-15. In 2022 USDA amended the moratorium regulation in order to facilitate the reamortization of a direct loan at the conclusion of a moratorium. 7 C.F.R. § 3550.207(c). The amendment leaves significant decisions about the impact of reamortization, including the option to forgive accrued unpaid interest, to the USDA, or to its servicer.

<sup>55</sup> Ramey v. U.S.D.A., 2020 WL 1844192 (S.D.W. Va. Apr. 10, 2020); United States v. Brewer, 1996 WL 34494311, at \*5 (D. Vt. Sept. 18, 1996).

- Accuracy in all calculations, including:
  - Subsidy determinations
  - Subsidy recapture
  - Escrow account analysis
  - Reinstatement quotes
  - Payoff statements
  - Application of payments
  - Application of TOP receipts
  
- Timeliness in completing servicing tasks and responding to inquiries and updates about borrower accounts, including:
  - Prompt pick-up/response times for calls from borrowers and authorized third parties
  - Prompt responses to emails and other correspondence, including adherence to timelines for Requests for Information and Notices of Error
  - Prompt processing and application of funds received
  - Prompt recordation of lien releases/reconveyances upon payment of all amounts due
  
- Adherence to applicable laws and regulations, including:
  - Due process requirements
  - Notice requirements
  - Moratorium and reamortization rules
  - Protections regarding Treasury Offset Program referrals
  - Subsidy determinations
  - Subsidy recapture

## **8. Conclusion**

The vendor solicitation proposal will exacerbate the chronic problems that Direct Loan borrowers already face. The proposal will not save the government money and will instead lead to a loss of revenue. Because of the Direct Loan program's basic structure, any large-scale outsourcing of servicing is simply not feasible. Given the complexity of the Direct Loan program and the high risk of default in the borrower population, it is highly unlikely that any vendor will find the venture profitable while meeting minimum servicing standards. Rural homeowners, the beneficiaries that Congress intended for the program, will be worse off. Instead of outsourcing, USDA and Congress should commit further resources to improving staffing levels and training.