DEPARTMENT OF AGRICULTURE

Farm Service Agency

7 CFR Part 762

Rural Housing Service

Rural Business-Cooperative Service

Rural Utilities Service

Farm Service Agency

7 CFR Part 1980

RIN 0560–AF38

Implementation of Preferred Lender Program and Streamlining of Guaranteed Loan Regulations

AGENCY: Rural Housing Service, Rural Business-Cooperative Service, Rural Utilities Service, and Farm Service Agency, USDA.

ACTION: Final rule and request for comments.

SUMMARY: This action amends the regulations governing the Farm Service Agency's (FSA) guaranteed farm loan programs. It clarifies, simplifies, and streamlines the procedures to apply for, make, and service FSA guaranteed loans. This action also establishes the Preferred Lender Program.

This action also provides for an Interest Assistance Program to replace the former interest rate buydown program (IRBD). The intended effect of this rule is to clarify and simplify the rules, and to finalize the interim rule which implemented the provisions of the Omnibus Budget Reconciliation Act of 1990. As contained in the final rule, FSA grants interest assistance at a 4 percent subsidy rate in all situations that qualify for interest assistance. FSA is requesting comments on alternative methods of determining the amount of subsidy paid, including granting interest assistance at incremental rates based upon the borrower's needs.

FSA is also incorporating changes mandated by Agriculture, Rural Development, Food and Drug Administration and Related Agencies Appropriations Act, 1999, (1999 Act), signed on October 21, 1998.

DATES: This regulation is effective on February 12, 1999. Comments on the alternative interest assistance subsidy rate calculation must be received on or before April 13, 1999.

ADDRESSES: Submit written comments to the Farm Service Agency, U.S. Department of Agriculture, Farm Loan Programs Loan Making Division, Attention: Director, Room 5438–S, 1400 Independence Avenue, SW, STOP 0522, Washington, DC 20250–0522. All written comments received in connection with this rule will be available for public inspection 8:15 am—4:45 pm, Washington, DC time, except holidays, at 1400 Independence Avenue, SW, Washington, DC 20250–0522.

FOR FURTHER INFORMATION CONTACT: Steven K. Ford, Senior Loan Officer, Farm Service Agency; telephone: 202–720–3889; Facsimile: 202–690–1117; E-mail: sford@wdc.fsa.usda.gov

SUPPLEMENTARY INFORMATION:

Executive Order 12866

This rule has been determined to be significant and was reviewed by the Office of Management and Budget under Executive Order 12866.

This rule substantially streamlines FSA's procedures implementing the guaranteed loan program. By making FSA's guaranteed loan program more consistent with standard practices used within the lending industry, use by lenders will be simplified and they will be more willing to use the program. This will increase the availability of commercial credit for family size farmers.

FSA currently guarantees repayment on approximately 65,000 farm loans to 40,000 farmers. Each year, FSA receives 15,000 requests for new loans. By reducing the application burden on lenders, and making FSA rules more consistent with industry practices, we expect lenders will increase requests for loan guarantees by 25 percent, or an additional $395 million. This means an additional 3,000 farmers will be able to receive commercial credit. These farmers would otherwise have gone without credit or required assistance through FSA's direct loan programs.

Regulatory Flexibility Act

The Agency certifies that this rule will not have a significant economic effect on a substantial number of small entities and therefore is not required to perform a Regulatory Flexibility Analysis as required by the Regulatory Flexibility Act, Pub. L. 96–534, as amended (5 U.S.C. 601). An insignificant number of guaranteed loan borrowers and no lenders are small entities. This rule does not impact the small entities to a greater extent than large entities.

Environmental Impact Statement

It is the determination of FSA that this action is not a major Federal action significantly affecting the environment. Therefore, in accordance with the National Environmental Policy Act of 1969, Pub. L. 91–190, and 7 CFR part 1940, subpart G, an Environmental Impact Statement is not required.

Executive Order 12988

This rule has been reviewed in accordance with E.O. 12988, Civil Justice Reform. In accordance with that Executive Order: (1) All State and local laws and regulations that are in conflict with this rule will be preempted; (2) no retroactive effect will be given to this rule except that Agency servicing under this rule will apply to loans guaranteed prior to the effective date of the rule; and (3) administrative proceedings in accordance with 7 CFR parts 11 and 780 must be exhausted before requesting judicial review.

Executive Order 12372

For reasons set forth in the Notice to 7 CFR part 3015, subpart V (48 FR 29115, June 24, 1983) the programs and activities within this rule are excluded from the scope of Executive Order 12372, which requires intergovernmental consultation with state and local officials.

Unfunded Mandates

Title II of the Unfunded Mandates Reform Act of 1995 (UMRA), Pub.L. 104–4, requires Federal agencies to assess the effects of their regulatory actions on State, local, and tribal governments or the private sector. Agencies generally must prepare a written statement, including a cost benefit assessment, for proposed and final rules with ''Federal mandates'' that may result in expenditures of $100 million or more in any 1 year for state, local, or tribal governments, in the aggregate, or to the private sector. UMRA generally requires agencies to consider alternatives and adopt the more cost effective or least burdensome alternative that achieves the objectives of the rule.

The rule contains no Federal mandates, as defined by title II of the UMRA, for State, local, and tribal governments or the private sector. Thus, this rule is not subject to the requirements of sections 202 and 205 of UMRA.

Paperwork Reduction Act

The amendments to 7 CFR parts 762 and 1980 contained in this final rule require no revisions to the information collection requirements that were previously approved by OMB under control number 0560–0155. A proposed rule containing an estimate of the burden impact of this rule was published on September 25, 1998 [63 FR 51458—51488]. No comments regarding the burden estimates were received. Comments received relating to forms and the information collected are addressed in the discussion below.

Federal Assistance Program

These changes affect the following FSA programs as listed in the Catalog of Federal Domestic Assistance:

10.406—Farm Operating Loans
10.407—Farm Ownership Loans

Change in CFR Parts

FSA is moving its regulations governing the guaranteed farm loan program from 7 CFR part 1980, subparts A and B to 7 CFR part 762. This will better organize FSA regulations and incorporate farm loan program regulations with other FSA programs.

Discussion of the Final Rule

In response to the proposed rule published September 25, 1998, 231 respondents from 35 States and the District of Columbia commented. Most of the comments involved a number of different sections of the proposed rule. Comments were received from Agency employees, farm interest groups, lenders, lender and employee associations, individuals, and Members of Congress. The comments received on the proposed rule were overwhelmingly in support of most of the changes proposed by the Agency.

This regulation provides the features, requirements, and restrictions of the program. However, internal Agency procedures and processes were excluded. The Agency will issue a handbook and update its lender manual. These documents will, within the framework of these published regulations, more thoroughly describe processes for the Agency and lenders, identify and discuss the completion of specific Agency forms, and otherwise provide more detail than is in the **Federal Register**.

There were many comments concerning problems with program delivery. Issues included Agency employees not following or knowing regulations, slow processing, inconsistency between offices, lack of staff, and need for training. These issues will be handled internally by the Agency and are not addressed in this document.

The 1999 Act contains several revisions to the statute governing the Agency's farm loan programs. Statutory changes that impact guaranteed loan limits and borrower training requirements are discussed below in response to comments received on the proposed rule.

The 1999 Act also eased the debt forgiveness restrictions which were mandated by the Federal Agriculture Improvement and Reform Act of 1996 (1996 Act). Previously, any FSA borrower receiving debt forgiveness would be ineligible for additional FSA credit. The 1999 Act provides that a borrower may have received debt forgiveness on three occasions prior to or on April 4, 1998, and still be determined eligible for guaranteed credit. Borrowers receiving debt forgiveness on more than three occasions, or any debt forgiveness after April 4, 1996, will be ineligible for FSA guaranteed loans.

The 1996 Act provided an additional exception to the debt forgiveness provision. A borrower who received debt write down, as compared with other types of debt forgiveness, previously could receive an annual operating loan. The 1999 Act expanded this exception to include borrowers who are current on confirmed bankruptcy reorganization plans. These changes have been incorporated into the final regulation at § 762.120.

Appraisals

One hundred and nine comments were received concerning raising the threshold for requiring a certified general appraiser from $100,000 to $250,000. Nine comments objected to the change, 94 supported it, and six requested clarification or modifications. Those supporting the change cited reduced costs, shortened application process and compliance with their regulatory requirements as reasons. The concern, expressed by all of those opposed to the change, is that relaxing the policy will adversely affect the quality of the appraisals. Most of the commenters objecting to the change stated that many of the appraisals currently received from certified general appraisers are not correct and do not adhere to Uniform Standards of Professional Appraisal Practice (USPAP). Another concern was that less qualified licensed appraisers (previously used for transactions up to $100,000) were more experienced with residential rather than agricultural appraising and not qualified to perform the more complicated appraisals of agriculture property.

On transactions of $250,000 or less, the proposed rule provided that the Agency would determine if the appraiser possessed adequate experience and training to estimate the value of the type property in question. It also required appraisals to be completed in accordance with USPAP. The Agency desires to comply with industry standards, and with the controls in place, is convinced that relaxing the policy will not adversely affect appraisal quality. Therefore, the Agency has decided to leave the threshold at $250,000, as in the proposed rule with minor editorial changes in § 762.127(d)(3) to clarify that the entire appraisal process, not just the report, will be completed in accordance with USPAP. The Agency has requested and the Office of Management of Budget (OMB) has granted an exception from OMB circular A–129 for this purpose.

Three comments requested additional clarification of what is an acceptable appraiser. The proposed rule stated that the lender must demonstrate to the Agency's satisfaction that the appraiser possesses sufficient experience or training to estimate values. As proposed, the lender could provide any documentation considered appropriate to demonstrate this expertise. The level of expertise could vary by region and complexity of agriculture. The Agency did not want to dictate and limit what could be used to demonstrate appraiser competency. However, a revision has been made to § 762.127(d)(2)(i) to require the appraisal expertise to be in appraising agricultural property. Additional guidance consistent with this standard will be placed in the agency handbook and lender manual.

Several comments noted an inconsistency between the proposed rule and the preamble. The preamble incorrectly stated that the appraiser must use all three approaches to value, while the regulation required that appraisal reports comply with USPAP standards. The final rule at § 762.127(d)(3) should eliminate any confusion concerning this matter. It states that real estate appraisals must be completed in accordance with USPAP.

Two respondents suggested we permit only the original appraiser to update an appraisal. One of the comments went on to say USPAP requires that the original appraiser be involved in an update. These suggestions were not adopted because the Agency believes that the requirement that appraisals be performed in accordance with USPAP adequately covers the respondents' concern. The agency handbook and lender manual will include clarification and guidance of the standard published in this final rule.

Two comments objected to approving a loan subject to an adequate appraisal. Eighty-five respondents supported this change. A concern appears to be that the lender may ignore the conditions of approval and close the loan without adequate security. The Agency would then refuse to issue the guarantee. The

Agency has determined that the benefits of a simplified application process outweigh the minimal risk to the lender that the Agency would so act and will not adopt this suggestion.

Another comment suggested an estimate of value be included with the application. This will be included on the application form.

One respondent suggested the regulation include the specific items needed in a chattel appraisal. The regulation states that lenders may use the Agency's form or any other form containing at least the same information. The Agency feels this adequately identifies the information required for a valid appraisal.

Two comments were received suggesting outside chattel appraisers be required for refinancing bank debt. Another comment suggested bank loan officers not be permitted to perform real estate appraisals over $100,000. Since the regulation permits the Agency to determine if the appraiser possesses adequate experience or training, the Agency feels safeguards are adequate to assure valid appraisals by lenders. Therefore, these suggestions are not being adopted.

Packager Requirements

Ninety-seven comments were opposed to the proposal to restrict lender use of loan packagers. Many of the comments preferred to address excessive fees by simplifying the paperwork requirements and making packaging services unnecessary. Six comments suggested varying levels of restrictions or clarification such as limiting the fee to a certain percentage of the loan, prohibiting packager use entirely, or clarification of how any limitations would be enforced. Although the Agency feels that the proposed rule change reduced paperwork requirements, it agrees that packagers do provide a valuable service to some farmers and any arbitrary limitations would not be warranted. Therefore, the use of packagers will not be prohibited or restricted in the final rule.

Loan Limits

Twenty-eight comments were received indicating the maximum guarantee loan limits of $300,000 for Farm Ownership (FO) loans and $400,000 for Operating loans (OL) were too low. Numerous suggestions to raise or modify the limits were provided. Loan limits are established by statute and the Agency has no authority to raise them. However, the 1999 Act did modify the loan limits and provided for a maximum of $700,000 total guaranteed FO and OL indebtedness. This will permit an applicant to receive a total of $700,000 guaranteed OL and FO loans. The $200,000 Direct FO and OL limitations remain in place. The result is that in some situations, the borrowing limit may be $900,000. The revised limitation was incorporated into § 762.122.

One comment was received concerning the need to conform approval authorities with other FSA regulations. This suggestion will be implemented administratively.

Loan Restrictions

One comment suggested that lenders be permitted to advance funds to purchase cooperative membership stock outside the guarantee. There is nothing in existing or proposed regulations that would prevent a lender from financing stock purchases with unguaranteed funds. Therefore, no change to the regulation is needed.

One comment was received concerning joint ventures, suggesting a relaxing of the requirement that members of an entity must operate the farm. The proposal is that the applicant only need take an active role in management. The Agency is unable to adopt this suggestion as §§ 302 and 311 of the CONACT requires that the members holding a majority interest in the entity must operate the farm. However, the Agency has clarified the regulation to say only the members holding a majority interest must operate the farm. See § 762.120(e) and (f).

One respondent suggested limiting the size of the farm dwelling to be financed with a guarantee. Such a restriction would be arbitrary and contrary to the Agency's policy of reducing regulatory limitations. The Agency is not directly supervising the loan, does not wish to become actively involved in the loan applicant's management decisions and is not in a position to dictate the maximum size of a dwelling. The lender is required to place limits on borrower expenditures to prevent the buildup of excessive debt, with the resulting inability to repay the loan. The suggestion was not adopted.

One comment stated that the guaranteed program is designed for row crop loans and does not fully address the needs of livestock producers. No specific examples were provided. The Agency does not agree with this comment because livestock issues are specifically discussed throughout the regulation.

This same individual objected to the lender certification requirements. Since the Agency is unable to identify the specific objectionable requirements the commentor is referring to, the Agency is unable to address this comment.

One comment was received requesting that ''bridge'' loans made by the lender while waiting for a final decision from the Agency can be included under the guarantee, once it is approved. This practice, although not prohibited by regulation, is strongly discouraged. There could be a question of the need for a guarantee if the lender was willing to close the loan without one. However, if the lender is willing to assume the risk of making a bridge loan prior to any Agency decision to guarantee the permanent loan, the final rule does not prohibit including such debt under the guarantee. This will be further discussed in the agency handbook and lender manual.

One comment suggested that the lender should certify at loan closing that no material adverse change has occurred in the operation since the request for guarantee was submitted. The existing regulation requires this certification to reveal changes since the conditional commitment was issued. The Agency agrees with this suggestion and adopted it in the final rule.

Five comments suggested removing the prohibition of additional guaranteed OLs after a borrower has received loans for 15 years. This requirement is statutory and cannot be eliminated without legislative action.

One comment suggested the Agency treat a husband and wife applicant as an individual, rather than a joint operation. The Agency agrees that this can be burdensome for some lenders. However the Agency desires to maintain continuity with its direct loan programs and will reevaluate this issue as the direct loan program regulations are revised.

One respondent suggested that veterans preference for funding be expanded. The Agency feels the current policy, which was not changed in this rule, is appropriate.

Conflict of Interest

One comment indicated that the conflict of interest changes will permit a loan to be made where a conflict of interest exists. This is not correct. The lender is required to provide information concerning ownership or business relationships, and the Agency will determine if these relationships are sufficiently likely to result in a conflict. The Agency revised § 762.110(f) to say relationships, rather than conflicts will be reported to the Agency.

Another respondent suggested specifying a penalty for the lender if a relationship is not reported, but is later identified. A specific penalty is not being adopted for not reporting conflicts. Such situations are case specific and depending on the severity of the situation, such a violation will be handled with regulations already in place. Additional guidance will be provided in the agency handbook and lender manual.

Interest Assistance

There were seven comments requesting an extension of interest assistance beyond the 7 or 10 years, making the argument that the limits are arbitrary and will result in failure. While the Agency sympathizes with the plight of individuals in need of a subsidy which is expiring, the Agency's mission is one of temporary assistance to farm families. In addition, the interest assistance program is the most expensive of the Agency's guaranteed farm loan programs and limits must be placed to control costs. This recommendation was not adopted.

One respondent requested that interest assistance be available for existing guaranteed loans. The Agency agrees that this would be ideal, and this is currently not prohibited by regulation. However, the interest assistance program is very expensive and funding for paying a subsidy on existing loans is not available. Including this option for all guaranteed loans would result in a dramatic increase in costs for the entire guarantee program or reduce the number of applicants that could receive credit. Therefore, the Agency will not adopt this recommendation.

Additional public comments received concerning the interest assistance program interim rule are discussed below.

Preferred and Certified Lender Programs

The Agency received 131 comments concerning various aspects of the preferred lender program (PLP) and certified lender programs (CLP). Comments from almost all of the respondents supported the introduction of PLP and the minor modifications made to the existing CLP.

The proposed rule provided that lenders could request either PLP or CLP status. One comment suggested that lenders be permitted to operate under both the CLP and PLP if they desired. For administrative simplification and clarity, it is desirable for each lender to operate under only one status. PLP lenders will be able to receive 95 percent guarantees when refinancing Agency direct farm loans or when the borrower will be participating in the Agency's down payment loan program. The Agency did not adopt the suggestion to allow lenders to request both PLP and CLP status.

The proposed rule provided that the Agency will determine which branches of the lender have the necessary experience and ability to participate in CLP or PLP. Comments from 82 respondents suggested that it would be more expedient if the applying institution designate those branches it wishes to be considered for certification, followed by Agency approval or disapproval. The Agency intended this in the proposed rule. The proposed rule provided that lenders desiring PLP or CLP status address, in their request, the State in which they desire status. One comment suggested that applicants specify the county or parish in which they desire status, to assure consistency with the requirement that an office be located near enough to the collateral's location to efficiently discharge loan making and servicing responsibilities. In response to these comments the Agency has included a provision in § 762.106(a)(1)(i) that lenders requesting PLP or CLP status indicate the branch offices they want considered for status.

The proposed rule provided that lenders desiring PLP or CLP status must send their request to the Agency State office for the State in which the lender's headquarters are located. One comment suggested that the lender send the request to the Agency state office for each State in which the lender intends to make guaranteed loans. This suggested change was based upon the fact that banking laws, security requirements, and other lending procedures vary from one State to another and each Agency State office is independently responsible for maintaining credit quality and consistency within the State. The Agency recognizes the administrative need to coordinate among various Agency State offices; however, the Agency believes it would be unnecessarily burdensome to require a lender to apply for status at several Agency offices. The administrative details of coordinating requests that cover several States will be addressed in the agency handbook and lender manual. The Agency did not adopt the suggested change.

Three comments suggested the Agency centralize the processing of CLP and PLP loan making and servicing activities, pointing out that centralization would promote uniformity. The proposed and final rule purposely does not specify where the Agency will process guarantee applications. This will allow the Agency administrative flexibility to configure operations in the most effective manner.

One comment expressed concern about the ''10 loan [sic] in 2 year requirement'' under the CLP. The proposed rule continued existing Agency policy at 7 CFR § 1980.190(b)(1)(vii) and required, for CLP eligibility, that a lender have closed a minimum of ten Agency guaranteed loans or lines of credit and have closed a total of five Agency loans in the past 2 years. The Agency developed these requirements to assure that CLP lenders have a reasonable amount of experience with the guaranteed program. The Agency believes that these requirements are reasonable and will not change them.

The proposed rule provided that, to be eligible for PLP status, a lender must have made at least 20 PLP, CLP, or approved lender program (ALP) loans, or a combination of these type loans within the past 5 years. The ALP is another level of lender status and is being discontinued with this rule. This requirement was established at a level designed to permit the Agency to grant PLP status to one percent of the 2,500 lenders that make guaranteed farm loans each year. Clarification or reconsideration of this requirement was requested by 98 respondents. Several respondents expressed concern that criteria that limited the program to only 25 lenders was too restrictive. Most commenters suggested that the Agency clarify that 20 individual loans, as opposed to 20 borrowers, be the criteria. Comments from two respondents suggested that the 20 should refer to borrowers. Another respondent suggested that either all guaranteed loans or just PLP and CLP loans be considered, suggesting that ALP doesn't show any better quality than a loan from a standard lender. Other comments suggested that all guaranteed loans be considered. Three respondents suggested that the number of loans be eliminated as an eligibility criteria or alternate criteria be considered. One respondent suggested that agricultural banks (as defined by either the Federal Reserve or FDIC) be PLP lenders based on the lenders call report data. The respondent pointed out that call report data is the proven result of the quality of the lender's credit management system. The Agency considered the various comments and determined that criteria that restrict PLP status to one percent of the 2,500 lenders that make guaranteed farm loans each year is too restrictive. The Agency also agrees that all FSA guaranteed loans that a lender has made should be considered.

The Agency wants to establish the PLP eligibility criteria at a level where the lenders have demonstrated adequate recent experience with the guaranteed program while not being too restrictive. The Agency modified § 762.106(c)(3) to provide that the lender will have made a minimum number of guaranteed loans within the previous 3 years as set out in a separate published notice. As the Agency and lenders become accustomed to these PLP process, the volume requirements may be changed. These changes will be established in a **Federal Register** notice.

One comment requested clarification of the rating service acceptable to the Agency for determining an acceptable level of financial soundness for Farm Credit System institutions. Instead of defining a particular rating or rating service, the Agency has determined a more appropriate requirement is that the lender not be under any regulatory enforcement action based upon financial condition. The Agency's National office will work with the financial institution regulators to assure that lenders holding CLP or PLP status are financially sound. Section 762.106(b)(6) has been modified to include this requirement.

The Agency received 82 comments requesting clarification or parameters as to what elements comprise a satisfactory credit management system. The comments pointed out that more specific criteria that the lender must address would help promote uniformity and assure that objective criteria are considered when the Agency evaluates the lender's credit management systems. The respondents suggested that the Agency use a methodology similar to that contained in bank and thrift regulators manuals. The Agency does not want to unnecessarily limit a PLP lender in the methods used to administer their credit transactions, therefore the Agency has not added additional specificity or regulatory requirements for a satisfactory credit management system. However, the Agency agrees that additional guidance of what should be addressed in the lender's credit management system would result in more uniformity and it will provide such guidance in the agency handbook and lender manual. In addition, § 1980.106(d)(4) has been modified to state that any lending criteria not specifically addressed in the lender's credit management system will be governed by the CLP requirements.

One respondent stated that requiring that the PLP lender show a consistent practice of submitting applications that are detailed with complete information that supports the loan proposal is subjective, and questioned how to ensure consistency across State lines. The Agency will gather and review information from all of the States in which the lender wishes to do business. The process by which this information will be gathered will be addressed in the agency handbook and lender manual.

The Agency proposed that a PLP lender have a history of using the guaranteed programs for new loans instead of refinancing the lender's existing debts. Comments from 93 respondents addressed this requirement. Comments from seven respondents supported this requirement or suggested that the restriction be expanded. One comment suggested that the Agency disallow all refinancing of existing debt, another suggested the Agency limit the guarantee to 80 percent in all cases of refinancing, another suggested that refinancing not be allowed under CLP or PLP, and another recommended that PLP be ''limited to lenders with a past history of promoting new credit and willing to continue activity promoting new credit.'' Comments from 88 respondents either opposed the requirement or suggested that the requirement was too ambiguous and counterproductive. These comments pointed out that the requirement was not amenable to a bright line of interpretation and that the Agency had provided little rationale for imposing the criteria. They commented that this burdensome requirement would cause some lenders to not participate in the program and could adversely impact borrowers. The Agency agrees that the requirement is ambiguous, of limited value, is burdensome and would cause some lenders not to participate. The requirement has been removed.

Three comments suggested that the Agency pre-approve all Farm Credit System lenders for CLP or PLP. Because each separate Farm Credit System entity will need to select which status they desire and meet those eligibility criteria, the Agency cannot adopt this recommended change.

One respondent suggested that applicants for CLP and PLP status should be required to have fulfilled obligations regarding graduation and market placement. Since the Agency is responsible for these programs and cannot transfer these obligations to a lending institution. The Agency did not adopt the suggested additional eligibility requirement.

One respondent suggested that the Agency revoke CLP or PLP status if the lender does not make 40 percent of the guaranteed operating loans and 25 percent of the guaranteed farm ownership loans to beginning farmers. While the Agency agrees with the need to encourage lending to beginning farmers and does target guarantee funds for that purpose, the Agency does not feel revocation of lender status would be a reasonable method of encouragement; therefore the Agency did not adopt this suggestion.

Lender Eligibility

One respondent suggested that standard eligible lenders be approved for 5 years, rather than demonstrating eligibility for each guarantee request submitted. The Agency did not change the requirements from existing practice and does not contemplate that a standard eligible lender will need to provide all evidence demonstrating eligibility with each guarantee request. The Agency did not adopt the multi-year eligibility suggestion for standard eligible lenders. However, the language in the introductory paragraph of § 762.105(a) is clarified so that the lender must demonstrate eligibility and provide evidence when the Agency requests.

One comment suggested that the Agency use the terminology ''standard lender'' rather than ''standard eligible lender'' to simplify reference and that the Agency add an abbreviation for ''standard lender.'' Another comment suggested the terminology should be ''eligible lender.'' Since the use of terminology and an abbreviation is within the Agency's discretion, FSA decided that its own terminology is reasonably descriptive and did not to adopt either recommendation for publication.

One respondent suggested that the Agency require lenders to have agricultural loan experience. The respondent was concerned that without this requirement, the lenders may not have the necessary experience to properly make and service agricultural loans. The Agency generally agrees with this concern, and has added clarifying language to § 762.105(b)(1) to require that the lender must have experience in making and servicing agricultural loans.

One respondent suggested that the Agency require that lenders have a permanent presence in the State where they originate loans. The Agency believes that the eligibility requirement contained in the proposed rule concerning lender locations is adequate to assure good loan servicing and did not revise the rule.

The Agency received two comments requesting that the Agency clarify or remove the requirement that a lender be in ''good standing'' with all applicable State or Federal regulatory agencies. The Agency agrees that this requirement was ambiguous and removed it.

Two comments suggested that a ''maximum loss rate'' eligibility requirement for standard eligible lenders be established. The Agency did not establish a ''maximum loss rate'' for Standard Eligible Lenders; however, in response to these comments, it added a requirement in § 762.105(b)(2) that the lender must not have losses or deficiencies in processing and servicing guaranteed loans above a level which would indicate an inability to properly process and service a guaranteed loan.

One respondent recommended that the Agency establish a method to remove standard eligible lenders from the guaranteed loan program when the lender does not perform in accordance with its agreements. The Agency may revoke a lender's PLP or CLP status for failure to meet a regulatory requirement, but the Agency has no comparable ''penalty'' for standard eligible lenders. The Agency may recommend that a lender be debarred or suspended from participation in all Government programs, but cannot merely revoke participation in the Agency's guaranteed programs. The Agency agrees with the concern and § 762.105 allows the Agency to determine that a lender may no longer participate in the guaranteed farm loan programs. This provides a less severe penalty than debarment or suspension, which would restrict participation in all Government programs. Additional guidance will be provided in the agency handbook and lender manual.

One respondent suggested that lenders notify the Agency when the lender assigns responsibilities to other than the authorized designee and that the Agency should reconsider the lender's CLP or PLP status at that time. The commenter noted that CLP loan making and servicing quality often deteriorate when the lender changes their ''authorized designee''. The purpose in revising the regulation was to reasonably increase lender loan making and servicing flexibility. Therefore, the Agency chose not to adopt the suggestion.

One respondent recommended that consideration be given to allowing standard eligible lenders make farm ownership loans. The proposed and final regulation allows all lenders, regardless of status, to make either operating loans or farm ownership loans.

The agency received 161 comments concerning the Agency's consideration of allowing certain non-traditional financial entities to make guaranteed loans. The respondents in 156 comments opposed the expansion of lender eligibility criteria, citing concerns that unregulated lenders such as machinery manufacturers and agricultural supply firms lack credit expertise and have an inherent conflict when they are trying to provide financing for a sale. Two commenters suggested that eligibility should be expanded based on financial strength, while one commenter suggested that it would be ''beneficial'' to expand eligibility to some mortgage or insurance companies. One respondent suggested that the guarantee program eligibility be expanded to authorize guarantees for farmers when the individual is a retiring farmer selling land to a beginning farmer. The general tenor of the comments was that a lender must have experience in making and servicing agricultural loans and have the capability to make and service the loan for which a guarantee is requested. The Agency agrees and has decided not to expand the eligibility to nontraditional lenders.

Several respondents suggested that the Agency not require lenders to provide information to consumer and commercial credit reporting agencies. The comments noted that this requirement is inconsistent with standard practices of many lenders. Rather than requiring lenders to provide the information, the Agency will provide the information on guaranteed loan extension to credit reporting agencies, as required by the Debt Collection Improvement Act of 1996. The proposed lender requirement was removed.

Percent of Guarantee and Maximum Loss

The proposed regulation provided that all guarantees issued to PLP lenders would be at 80 percent, unless the loan was eligible for a 95 percent guarantee. Comments from 15 respondents suggested that PLP guarantees should be at a higher percentage, arguing that lenders would not use the PLP if only an 80 percent guarantee was available and it is inconsistent for the Agency to penalize the program's best performing lenders with a lower percent of guarantee. The Agency should encourage its best lenders to be active. The Agency agrees with these comments. Loss rates for CLP lenders have been lower than those for other lenders and the Agency expects this to continue under the PLP program. In addition, since the PLP will take less time to process, the Agency's administrative cost savings will be greater if more lenders participate in the PLP. Also, the statutory language prescribing the percent of guarantees for CLP and PLP lenders is identical. For these reasons, the Agency has revised § 762.129(c) to authorize up to a 90 percent guarantee for PLP lenders.

Loan Approval and Issuing the Guarantee

Eight respondents suggested that the 14 day automatic approval for PLP should be removed, arguing that it is unreasonable, a bad business practice, and not in the best interest of the Government. The Agency is sympathetic to these arguments, but disagrees with them. The review of PLP applications will be significantly reduced from present guarantee application review requirements and the Agency has management methods and responsibilities to assure that the PLP loans are timely reviewed. The automatic approval is statutorily mandated and will not be modified in the final rule. One comment suggested that, at a minimum, the automatic PLP approval requirement be changed to 14 business days, citing concern for Agency office coverage. Because calendar days are also statutorily mandated, this suggestion was not adopted.

Two respondents recommended requiring applications be submitted by certified mail to document the beginning of the 14 day time period. The Agency chose not to impose this additional burden; however, the Agency will send the lender a letter confirming receipt of the application and indicating the date of receipt. Section 762.130(a)(3) has been added to include this procedure.

Two respondents suggested the Agency clarify what happens in cases where the Agency has asked for additional information or clarification. The Agency is committed to providing a response to the lender within 14 days of receipt of a complete application. However, in some situations, it will be impossible for the Agency to satisfy its environmental responsibilities based on the information supplied with a PLP application. In those situations, the Agency will notify the lender within the 14 day time period of the additional information that is needed to complete the Agency's environmental review, and that the 14 day automatic approval is suspended until this information is received. After the Agency receives this additional information, another 14 day approval period will start. The Agency does not anticipate this additional information will be required in a large number of cases. Section 762.130(a)(2)(ii) has been revised to provide for this procedure.

One respondent suggested the 14 day processing timeframe for CLP be removed. Since this is a statutory requirement at § 339(c)(4)(C) of the CONACT, no modification was made in response to the comment.

Another respondent requested that the Agency ensure that all approvals are made within 14 days. Since the Agency's methods to ensure that all approvals are timely issued is an administrative matter, this issue will be addressed in the agency handbook. No changes were made in the regulation as a result of this comment.

Insurance and Farm Inspection Requirements

One comment suggested that the lender be required to obtain an assignment of crop insurance and be shown as loss payee. This requirement can be addressed, as necessary, as part of collateral requirements in the agency's conditional commitment for guarantee. This will be further clarified in the Agency handbook and lender manual.

Security Requirements

One respondent suggested that the requirement that a lien be taken on all ''significant nonessential assets'' is contradictory to the requirement that the lender is responsible for ensuring that adequate security is obtained. A lien on nonessential assets is often unnecessary for security purposes, and does not improve the quality of the loan. The Agency agrees with the comment and removed the requirement. If the Agency determines, on a case by case basis, that a lien on a nonessential asset is needed, to assure that the loan has adequate security that requirement may be included as a condition for issuing the guarantee. Additional guidance will be provided in the agency handbook and lender manual.

One respondent requested the Agency amend the proposed rule to allow individual principals to own collateral where the borrower is a legal entity. The proposed rule at § 1980.126 did not specify who has to own the collateral, therefore no change was made in § 762.126 to address this comment.

One respondent suggested limiting real estate financing to no more than 90 percent of the appraised value. While the Agency recognizes the risk of 100 percent financing, and that additional collateral should be taken when available to adequately secure the debt, the Agency does not want to prohibit lenders from providing credit to otherwise viable operations, because of tight collateral margins. This suggestion was not adopted, however the agency handbook and lender manual will provide guidance on this issue.

One respondent recommended that the Agency should clearly specify that a line of credit used for the purchase of feeder livestock must always be secured by a first lien on the livestock. The regulation states at § 762.126(e)(3) that junior liens on livestock will not be relied upon for security unless the lender is involved in multiple loans to the same borrower and also has first lien on the collateral. This requirement adequately addresses the respondent's concern in that it will assure a first lien on livestock except in very limited situations. The suggestion to add an additional regulatory requirement was therefore not adopted.

One respondent requested the regulation be clarified regarding acceptable differentiation on identifiable livestock. The final regulation, in § 762.126(c) explains that, for security to be identifiable, the lender must be able to distinguish the collateral item and adequately describe it in the security instrument. This requirement applies to all security, including livestock. The Agency does not believe additional regulatory clarification is necessary, however, additional guidance will be provided in the agency handbook and lender manual.

Line of Credit

The proposed rule allows lenders to advance funds from a line of credit for a borrower to make term debt payments on capital items. Comments were received from 109 respondents concerning this proposed change, with 98 comments supporting the change because it will conform the guaranteed program more closely to current industry practices. Eight respondents recommended the Agency not allow lenders to advance funds from a line of credit for a borrower to make term debt payments on capital items. Two comments were concerned that this use would reduce the number of loans the Agency could guarantee as each borrower's lending needs would increase. The other opposing respondents argued that advancing for term payments was not prudent lending, and should be restricted. One respondent suggested that the Agency restrict payments on non-agricultural and real estate debts. The Agency considered the comments and determined that the practice of making term payments on capital items cannot be deemed imprudent lending, because that practice is customary in much of the agriculture lending industry. While the Agency recognizes that this additional authorized purpose may marginally impact funding availability, the advantages of a less restrictive program that will benefit more borrowers outweigh that concern. The Agency determined that an overall limitation on non-agricultural and real estate debts was too restrictive, however the Agency addressed the concern by clarifying in § 762.121 that the debt be for authorized FO loan or OL purposes.

One respondent recommended that the Agency eliminate the line of credit program and allow the lender to renew loans annually without submitting a complete new application. The Agency could not discern an advantage for the lenders or borrowers from the suggested change and so chose not to implement this recommendation.

One respondent suggested that the Agency authorize revolving lines of credit for capital purchases and term loans. The Agency chose not to implement this recommendation because it is concerned that adequate controls cannot be effectively implemented to assure proper supervision of major financial planning decisions.

Interest Rates, Terms, Charges, and Fees

The Agency provided the interest rate may not exceed the rate the lender charges its average farm customer. Two comments recommended that the Agency remove restrictions on the interest rate or allow a more reasonable range of interest rate. One comment recommended that the interest rate ceiling should be the rate paid by the average farm customer in the same interest rate program. The comment explained that a lender may have many rate options that are based on the risk profile of the borrower and other factors, and it would be more acceptable to limit the rate on guaranteed loans to no greater than some specific spread over the lender's index rate. The comment argued that the proposed regulation may not permit lenders to price to market in many instances. Because the Agency believes that the interest rate limitation is a reasonable, understandable restriction, and that the guarantee reduces the lender's credit risk in loans, the Agency did not adopt the proposal.

One respondent recommended that the Agency clarify what penalties will be imposed upon a lender that charges more than the rate charged to their average customer. A lender that charges more than the rate charged to their average customer is in violation of the terms of the lender's agreement and subject to revocation of PLP or CLP status under § 762.106(g). A standard eligible lender in violation of the terms of the lender's agreement could be prohibited from making additional loans under § 762.105(b)(2). In addition, the

Agency may contest the guarantee under § 762.103(a) if the lender misrepresents the interest rate charged. Because these penalties were already contained in the regulation, the Agency did not add any clarifying language to the regulation in response to this comment.

One comment recommended creating incentives for lenders who seek low cost funding sources, limit spreads and guide borrowers toward the use of long term fixed rate loans. The Agency fully supports the goal of providing competitive as well as fixed rates to guarantee borrowers, the advantages to financially stressed producers are well documented. Many lenders are able to provide such rates through participation in the secondary market and such activity is encouraged by the Agency. The comment did not provide specific suggestions, but encouraged the Agency to study these issues further. The Agency agrees that this issue warrants further study.

One respondent recommended that the 7 year limitation on operating loans be removed because it is unrealistic for a young farmer to completely pay for cattle and machinery in 7 years. Section 316(b) of the CONACT requires that guarantees on all operating loans be repaid in a term not to exceed 7 years; therefore, the Agency did not adopt the recommendation. The regulation at § 762.124(d) does provide that repayment schedules may include unequal or balloon installments if needed to establish a new enterprise.

The proposed rule stated that crops, livestock, or livestock products produced are not sufficient collateral for loans with balloon installments. Two comments recommended that breeding livestock should be acceptable collateral. The Agency agrees with this recommendation and has modified the rule accordingly.

One respondent recommended that balloon installments must be secured by real estate. The Agency did not adopt this recommendation because it would be too restrictive.

Two respondents recommended that balloon installments should be authorized for FO loans. The final rule modified § 762.124 to provide that balloon installments are authorized for any loan issued under a loan guarantee.

One respondent recommended that balloon installments should not be authorized because the use of balloon payments will cause excessive future servicing requirements and future losses. The Agency does not agree with the rationale for limiting balloon installments and believes there will be situations where a balloon payment is prudent, such as when reduced installments are needed to establish a new enterprise, develop a farm, or recover from a disaster or an economic reversal. Therefore, the Agency did not change the rule.

Year 2000 Compliance

The proposed rule stated the Agency was considering adding a requirement that lenders have computer systems which are year 2000 compliant and requested comments on this requirement. The Agency received seven comments opposing this requirement and five comments in support. Comments pointed out that lenders were already addressing the issue internally and regulators are closely monitoring this problem. Regulators already require lenders to have a year 2000 action plan and have been incorporating this into lender reviews. Therefore, the Agency did not adopt this requirement, however, lenders are encouraged to ensure their systems are compliant.

Application and Forms

The proposed rule reduced application requirements to minimize burden on all lenders applying for guarantees. Eliminating the need for the lender to submit copies of all leases and contracts, and the need to submit detailed legal documentation for all entity loan applicants were adopted. The rule also permitted the agency to approve a loan subject to an acceptable appraisal. The Agency received 90 comments supporting its reduced application requirements.

The agency received one comment requesting articles of incorporation or partnership agreements be submitted as part of a complete application and one comment requesting the application provide information on entity members. The comment requesting entity legal documents indicated concerns that the Agency's approval official would not be familiar with the entity's structure. The lender's loan narrative submitted with each application will contain sufficient description of the entity's structure, owners, and roles of the entity members; therefore, no changes are being made regarding entity information.

One comment requested the Agency specify the items which must be contained in a line of credit agreement. In response to this comment and to reduce the burden, the Agency removed the requirement in the proposed § 1980.110(b)(5) that a loan agreement be submitted to the Agency. The information generally included in a loan agreement is adequately addressed in the loan narrative.

Two comments were received regarding credit reports. One comment requested all lenders submit credit reports or certify to credit history. The Agency does not believe this is necessary and has proposed no changes. Credit reports will be required for all loans and CLP lenders may certify to satisfactory credit history. Any unusual items will be addressed in the lender's loan narrative. One comment also requested that commercial credit reports not be required for small, closely held farm entities. The Agency does not specify when a commercial credit report is required. We believe this is best addressed on a case by case basis between the Agency's responsible office and the lender. No changes are being made regarding credit reports.

Financial and Production History

The proposed rule reduced the amount of financial and production history required to be gathered and analyzed by lenders. The Agency reduced the history from 5 years to 3 years on loans above $50,000, eliminated history requirements for loans under $50,000, and permitted CLP lenders to base cash flows on financial history rather than requiring production history. In addition to the 90 comments supporting reduced application requirements, 17 comments specifically supported reducing the financial history requirement from 5 years to 3 years.

The Agency received ten comments requesting the proposed requirement be strengthened. Four comments requested 3 years of production history be required in all cases; three comments requested 5 years of financial and production history be required in all cases; and three comments requested the Agency require 5 years financial and production history if the loan purpose is for refinancing debt. Two comments suggested the lender's file contain production and financial history. Comments requesting additional financial and production history cited concerns over credit quality; specifically, the ability of Agency loan officers to determine whether the loan applicant's cashflow projection was reasonable.

The Agency has considered the credit quality concerns and continues to believe that 3 years financial and production history is sufficient to arrive at reasonable cashflow projections. In addition, CLP and PLP lenders have already demonstrated the ability to properly process a loan application and should not be required to submit financial and production history. Therefore, the suggestions are not being adopted.

Regarding small loans, the risk of loss on loans under $50,000 is much smaller and does not warrant the same amount of documentation. Also, under past procedures, lenders often could not justify making small loans under the guaranteed program because of the excessive administrative costs to gather and process the required information. However, operations requesting these loans are likely to be smaller, and the lender typically can estimate the feasibility using industry standards. Therefore, the Agency is not making any changes from the proposed rule regarding financial and production history.

PLP Application

The Agency proposed that a complete application will consist of at a least (1) an application form, (2) a loan narrative, and (3) any other items agreed to during the approval of the PLP lender's status. The Agency received two comments requesting PLP lenders be required to submit a cashflow and one comment requesting the Agency to require PLP lenders to certify their cashflow is based on past history. Feasibility of the loan applicant's request will be addressed in the lender's loan narrative. Furthermore, as part of the request for PLP status, a lender will describe their application requirements and underwriting standards. The PLP lender will certify that each application is processed as proposed in their application for status; therefore, the proposed requirements are sufficient.

The Agency received one comment requesting the Agency clarify what is required of PLP. PLP lenders will be required to submit an application form and loan narrative to the Agency. The particular items the lender maintains in their file will vary depending on that lender's procedures and will be defined during application for PLP status. Therefore, it would not be appropriate for the Agency to further define the requirement in the **Federal Register**.

Small Loan Applications

In the proposed rule, the Agency substantially reduced the amount of documentation required for loans under $50,000. This was directed by 333A(g)(1) of the CONACT. The Agency received 96 comments supporting the abbreviated application requirements for loans under $50,000.

The Agency received four comments requesting the $50,000 threshold be increased. While the Agency does have some administrative latitude to increase this threshold, the CONACT clearly identifies $50,000 as Congress' intended level. After the Agency has more experience and historical data to analyze the impact of reduced documentation requirements on its small loans, the level may be increased beyond $50,000.

The Agency received four comments requesting lenders be able to determine whether a sufficiently strong equity position exists to require an appraisal. The proposed § 1980.127(b)(2) stated that the Agency determined whether a strong equity position exists. This requirement was removed from § 762(b)(2). As with most other requirements, the lender is expected to make the initial determination subject to Agency approval. On a case-by-case basis, if the Agency disagrees with the lender's recommendation, they can require an appraisal as an approval condition.

The Agency received three comments requesting clarification that a lender's cash flow budget may be abbreviated. The Agency agrees with this comment and clarified in the definition of cash flow budget at § 762.102(b) that cash flow budgets for loans under $50,000 are not required to have income and expenses itemized by categories.

The Agency received three comments requesting it include the ability to require lenders with excessive losses or poor performance to submit full documentation required on loans above $50,000. The comments were concerned about potential lender abuse with no Agency authority to require needed documentation. The Agency agrees with these comments and included the authority in § 762.110(a)(4) to require lenders with losses in excess of the maximum CLP loss rate to submit those additional items required of loans above $50,000.

The proposed rule stated the Agency expects lenders to utilize the same level of documentation and evaluation as they require for their nonguaranteed loans under $50,000. The Agency received one comment requesting banks be required to submit their written policies for approval before the loan is made. While the Agency understands the potential for lenders to perform lesser evaluation for Agency guaranteed loans under $50,000 than it does for its nonguaranteed loans, it believes sufficient safeguards are already in place to prevent this from becoming a major problem. Lenders will be aware of the requirement through the lender manual and training. Lenders who do not perform the same level of evaluation may have a loss claim under the guarantee adjusted or denied. Therefore, this recommendation was not adopted.

The Agency received one comment requesting additional information requirements be reduced, not just the application form. The Agency already had language to reduce information required on the application by eliminating financial and production history and verifications of debt and income. The Agency feels the remaining requirements for information are necessary for adequate oversight and program administration. No further changes are being made.

The Agency received one comment requesting lenders be prohibited from making two $50,000 loans to same borrower in order to circumvent the threshold. The Agency agrees. The regulation as proposed did not prevent this circumstance. The Agency revised the language in section § 762.110 to apply the $50,000 to any one package of loan guarantee proposals.

Forms

Four comments requested the Agency automate forms or allow applications to be filed electronically. Several private companies provide financial software packages which print Agency application forms. Many Agency forms are now available through the Agency internet site. In addition, the Agency is working on the problem of applying through the Internet. At this time, many of the Agency's local offices do not have the ability to receive electronic applications. As our automation system is updated we will pursue electronic applications.

Eligibility

The Agency received one comment requesting the Agency revise its loan applicant eligibility criteria to require loan applicants to have been truthful and not have provided false or misleading information. The comment expressed concerns that the Agency has no way to deny loan guarantees to these loan applicants. The Agency agrees with this comment and has included the eligibility condition in § 762.120(f).

The Agency received one comment requesting delinquent IRS debt be included in the requirement that a borrower cannot be delinquent on Federal Debt. This exception to the definition of a Federal Debt is permitted by 31 U.S.C. 3720B(a). Rather than administratively modify the definition of Federal Debt, the Agency considers delinquent IRS debt as part of its creditworthiness determination and also in the cash flow budget used to determine feasibility.

Family Farm Definition

Four comments suggested the Agency remove its requirement that a loan applicant has been a family farmer, or that the Agency provide a uniform definition of family farmer. Two comments recommended simply ensuring the loan applicants were producers of agricultural products. Any modification of the family farmer definition should be consistent between the Agency's direct and guaranteed programs; therefore, these comments will be addressed when the Agency revises its direct program regulations.

Financial Feasibility

The Agency received one comment that financial feasibility requirements be clarified to state that in cases of startup or expansion, factors beyond financial history should be considered. This was included under projecting yields, but not for other projections in cash flows. This was an oversight and the Agency has added the ability to use other sources to develop a cashflow projection when actual history is not available or not appropriate to § 762.125(a)(5).

Advancing Funds

The Agency received one comment recommending that the lender be required to only advance funds when needed by the borrower. The commenter was concerned that some lenders advance more funds than needed by the borrower at that time, thereby accruing excessive interest charges. While the Agency understands this does occur in isolated cases, the problem should be worked out between the lender and the borrower. The Agency believes it is the borrower's responsibility as manager of the farm operation to decide when funds are needed. Furthermore, identifying what amount is excessive would be unreasonably burdensome for the Agency and the lender. No changes were made regarding advancing of funds.

Environmental

The Agency received 82 comments requesting clarification of the impact on a lender of finding a previously undetected environmental hazard, particularly whether the guarantee will be put in jeopardy. The proposed regulations require the lender to perform a due diligence investigation for any guarantee request involving real estate. Unless the lender fails to perform the due diligence investigation, or the Agency can demonstrate that the lender was negligent in performing the investigation, the guarantee will not be in jeopardy. Further clarification may be incorporated into Agency environmental regulations, agency handbook, and lender manual, see also the discussion below concerning the use of the American Society of Testing Materials (ASTM) transaction screen questionnaire.

The Agency received 72 comments requesting reduced environmental review for small loans or expressing concern with the cost associated with the reviews. In addition, the Agency received one comment requesting the lender be required to provide evidence of environmental compliance with a small loan application. The environmental statutes governing Farm Loan Programs do not permit the Agency to differentiate its review based solely on the amount of the transaction. However, the Agency believes loan requests under $50,000 involving real estate will normally not require a complicated environmental review. These loans are typically made to smaller operations and do not involve extensive land development or large animal populations. The Agency intends to simplify its environmental review process as it revises its environmental regulations.

The Agency received two comments requesting the ASTM transaction screen questionnaire not be required. In considering this requirement, the Agency believed a standard for due diligence needed to be identified. In our research, the Agency selected ASTM as the most widely accepted industry standard for a due diligence investigation. The Agency also recognizes that many lenders already have adopted investigation forms and procedures comparable with the ASTM form. To permit lenders to use their own forms and processes, the proposed rule stated the Agency will accept any similar documentation to the ASTM transaction screen questionnaire. The Agency believes this provides sufficient flexibility.

The Agency received one comment requesting clarification of lender and Agency environmental responsibilities. Section 762.128 provides that lenders will assist in the environmental review process by providing environmental information, and enumerates the specific requirements and documentation expectations. Any remaining investigation or determination is the Agency's responsibility. There are many environmental laws applying to Agency loans. Only those which require direct input from the lender have been addressed in the these regulations. Rather than duplicate the requirements for Agency review, the environmental regulations governing the Agency's review are presently published in 7 CFR part 1940 subpart G. The agency handbooks will clarify the procedures for the Agency's review.

The Agency received one comment requesting that compliance with wetlands and HEL be included as an eligibility requirement. This requirement is already part of 7 CFR part 1940, subpart G. To avoid duplication and potential conflicts between regulations, the Agency has decided to reference the environmental regulations rather than repeat the requirements in these regulations.

Lender's Debt Instruments

The Agency proposed removing the requirement that a lender's promissory note not contain a ''payment on demand'' clause. The Agency received two comments requesting this restriction be retained. This long standing requirement was intended to ensure lenders clearly establish the payment schedule on the promissory note. In evaluating debt instruments, the Agency found that many contained industry accepted language which ensured the lender's ability to accelerate a note in the event the collection of the loan was impaired. Many Agency offices interpreted this language to be in violation of the regulations when the note satisfied the intent of the regulations. The Agency therefore clarified its intent by stating the lenders note must clearly state the principal and interest repayment schedule, but the regulation does not prohibit demand clauses.

Loan Underwriting

The Agency requested comments on its underwriting standards, particularly whether the Agency should adopt more comprehensive criteria. The Agency received 16 comments on its underwriting criteria. Seven comments suggested the Agency remove its requirement for a 1.10 term debt and capital lease coverage ratio (TDCLCR), with one commenter offering the alternative of incorporating exception authority. Comments stated that during years of depressed prices, disasters, or other unforseen problems a 10 percent margin was not possible to project. The Agency adopted the 10 percent margin as a provision for future capital replacement as required by § 339(b) of the CONACT. Approving a loan to an operation unable to project a 10 percent margin would be imprudent lending and surely result in higher default rates for the program. The Agency continues to believe that a TDCLCR of 1.10 is necessary, particularly in the absence of any other criteria to measure financial feasibility.

One comment recommended the Agency implement a credit scoring system and several comments suggested the Agency incorporate additional financial ratios into its decision. While the Agency is aware of the merits of incorporating financial ratios or a credit scoring system, further analysis is needed before implementing such a change. The Agency will continue to study improved methods to underwrite its loans.

The Agency received 82 comments requesting clarification of its positive cash flow definition. While the Agency did not add more detail to this already extensive definition, it added a definition of the cash flow budget in § 762.102 to provide a mechanism for achieving a positive cash flow.

Loan Servicing Comments

The comments received regarding loan servicing were overwhelmingly in support of most of the changes proposed by the Agency. Most of the comments received were from lenders that participate in the Agency's guaranteed loan program, Agency field office personnel, or associations that represent the interests of those groups. The lending community unanimously supported the Agency's efforts to revise its guaranteed lending regulations, as did the large majority of Agency personnel and others who commented. However, there were some proposals, such as mandatory lender buyback of loans sold on the secondary market, that caused extensive concern. Numerous other comments were made requesting clarification, pointing out potential problems with the proposed rule or expressing personal opinion on a particular issue. The following is a discussion of specific comments, grouped into main subject areas, with Agency information providing clarification of some comments, adoption of others, and explanations for those that are not being incorporated into the final rule.

Mandatory Repurchase

The secondary market repurchase requirements proposed in § 1980.144 generated many comments. Of the 231 total comments received on the proposed rule, 105 expressed vehement opposition to the Agency proposal to require mandatory lender buyback of loans sold on the secondary market. The overwhelmingly negative comments were provided by farmer associations, secondary market purchasers, lenders and lender associations, including the American Bankers Association (ABA) and the Independent Bankers Association of America (IBAA). The proposed change was supported by two Agency employees, two Agency employee associations, and one bank.

Most of the 105 negative comments indicated that the requirement seems to punish all participating lenders for the errors of a few. In summary, these comments said that this policy would cause irreparable harm to the fledgling secondary market for FSA guaranteed loans, and that lenders would be discouraged from making long term fixed rate loans. The commenters almost all agreed that it is essential for many banks to sell fixed rate loans because they do not have the ability to match loan funding to the loan term unless they structure the loans to be sold in the secondary market. By selling the loan, the bank is better able to match its interest rate risk. Also, by removing the loans from their books, they obtain liquidity to make more loans. According to the ABA, requiring the lender to buy the loan back is tantamount to restructuring them as full recourse loans. As a result, the ABA and IBAA are concerned that bank regulators may hold the full capital charge against these loans, thereby increasing the cost of capital for banks and causing higher interest rates for borrowers. Liquidity planning would be more difficult because banks would be uncertain of funding capacity if they must maintain reserves to potentially buy back loans that were sold.

As a result of these comments, the Agency has eliminated mandatory repurchase of loans sold, and addressed problems with repurchased loans in other ways. First, delinquent account servicing regulations in § 762.143(b)(2) now spell out that the lender consider repurchasing the guaranteed portion of the loan sold on the secondary market. Second, § 762.144(b)(1) requires the lender to consider the request according to the servicing actions that are necessary on the loan, and encourages lenders to repurchase the loan upon the holder's request. Third, direct consequences of a lender's failure to comply with § 762.144(c) were added at § 762.160(a)(2). This states that if the lender does not comply with requirements to reimburse the Agency for the repurchase within 180 days, the Agency will not execute the Assignment of Guarantee, and will prohibit the sale of future loans on the secondary market. Provisions were included for waiver of this prohibition if the lender is in compliance with an Agency approved liquidation plan. The 180 day liquidation or reimbursement requirement in §§ 762.144(c)(7)(ii) and 762.144(c)(7)(iii) were proposed in § 1980.144(c)(6) and no negative comments were received. Finally, the Agency has clarified proposed § 1980.106(g)(2)(ix) by requiring in § 762.106(g) that consistent deficiencies in servicing loans sold on the secondary market will be considered when reviewing PLP or CLP status as part of the assessment of the lender's abilities. The agency handbook will provide guidelines for implementing this requirement, such as considering whether those repurchases resulted in increased losses or servicing problems for the borrowers.

Reporting Requirements

Comments were received requesting the Agency specify the lender's reporting requirements in the lenders agreement. The lenders agreement for guaranteed loans currently references the Code of Federal Regulations (CFR) for all reporting requirements. The Agency recognizes that there are older loans with specific reporting requirements that may differ from the CFR, but they represent a very small portion of the existing portfolio. Several years ago it was recognized that different lender designations had different reporting requirements in the respective lender's agreements, that were inconsistent with regulations. It was because of this inconsistency that a change was made to have the new lender's agreement for guaranteed loans refer to the CFR. The comment is not being adopted.

A comment was received requesting that the Agency reduce lender status reporting from semi-annual to annual. The Department of Treasury requires the Agency to report the condition of its loan portfolio on a semi-annual basis. In the recent past, the Agency was able to reduce the burden of its guaranteed loan status report by allowing multiple loans to be included on one report and automating its input at the local level. The Agency will continue to explore areas where it can reduce reporting burdens; however, the comment cannot be adopted and the semi-annual status requirement has not been revised.

Servicing Actions

Numerous comments were received on the Agency's various proposals to authorize lenders to conduct servicing actions on their guaranteed loans. One comment felt that lenders should conduct all servicing actions and, to enforce this, suggested that the Agency provide for revocation of preferred or certified status when a lender assigns or contracts for applications or servicing with an outside agent. The Agency did not adopt this comment. Part of the reason for this rule is that the lending industry, especially in agriculture, is changing. For the Agency to continue to encourage lenders to provide credit to family farmers and ranchers, it is critical that the Agency also change and adapt with the industry. The rule will maintain the provisions that exist today in that a lender has authority to contract with outside agents to service guaranteed loans. However, under the guarantee, the lender remains accountable for any actions of its agents or assignees that are inconsistent with the loan requirements, regulations and statutes.

Another comment was made requesting that lender servicing authorities be decided on a case by case basis, rather than basing this on the particular lender designation (Preferred Lender Program (PLP), Certified Lender Program (CLP), Standard Eligible Lender (SEL)). The comment was assumed to mean a loan by loan basis, since these statuses will be awarded on a per lender basis, as proposed. The comment is not being adopted because lender status designation will be based on its overall experience, including servicing, and expertise in conducting business with the Agency. The lender is responsible for servicing the loan in accordance with its agreements with the Agency. If a lender chooses to ignore these requirements, that noncompliance will result in the reduction or denial of a loss claim, should one be submitted. The Agency cannot assume that lenders will purposely ignore Agency requirements. The guaranteed loan is the lender's loan; lenders have requested the additional responsibility placed upon them in this rule with the full understanding that the Agency will hold them accountable for carrying out servicing in accordance with regulations and loan agreements.

A comment requested that the Agency require an annual loan classification of the guaranteed loan in order to determine the risk of loss. Currently the Agency uses existing loss rates on guaranteed loans in determining the subsidy cost for this program. Guaranteed loan loss rates have remained fairly stable since the farm crisis of the mid 1980's and, as a result, the Agency's current method of projecting losses, which does take into effect noted weather or related economic setbacks, is adequate for risk determination. Therefore, the Agency is not adopting the comment at this time.

Another comment requested that the Agency not allow retroactive servicing authority. In order to maintain consistency and provide a more simplified approach for Agency personnel, the rule must be retroactive. For example, Agency internal review procedures provide that 20 percent of an SEL lender's loans and 40 percent of a CLP lender's loan files will be reviewed annually. If the lender is worthy of an enhanced status, it will likely service all loans equally well. Requiring FSA field office review of 40 percent of a lender's loans made before a certain date and 20 percent of the loans made after that date would be burdensome and confusing.

A comment was made requesting that the Agency clarify that a line of credit balance can go to zero. In the past the Agency has heard concern from lenders that if a line is paid to a zero balance, then it is paid in full. This is not an Agency requirement and our interpretation is that a line of credit must be paid as its security is sold. The fact that a multiple advance note may be paid to $0 does not terminate it. Thus, no change was made in the final rule. The rule does not prohibit or require an annual balance of zero.

Negligent Servicing

The Agency received multiple comments requesting clarification of the definition of negligent servicing and how it would affect the determination of a loss payment as stated in § 762.149(c)(6). Negligent servicing was defined in § 1980.102(b) of the proposed rule as follows:

> The failure to perform those services which would be considered normal industry standards of loan management or failure to comply with any servicing requirement of this subpart. The term includes the concept of a failure to act or failure to act timely consistent with actions of a reasonable lender in loan making, servicing and collection.

In addition, the Agency's guaranteed documents under the full faith and credit provisions describe negligent servicing as those actions which a reasonably prudent lender will take in the servicing of a loan if such loan were not guaranteed. Moreover, failure to service a loan in accordance with the corresponding lender's agreements and Agency regulations can lead to reduction or denial of a loss claim due to negligent servicing. The Agency believes that to protect the government's interest, the definition of negligent servicing must remain flexible, and no change is being made.

Borrower Analysis

One comment requested that the Agency remove the requirement that all lenders complete a borrower analysis for chattel secured loans. Along this same line, a few comments suggested that the Agency delete the requirement for SEL to provide an annual statement of financial condition. Since chattel loan security often depreciates quickly, and is likely to deteriorate very quickly if an operation is struggling financially, the first suggestion is not being adopted. Contrary to the comment, the Agency has found that some level of security monitoring and financial performance measurement is performed by most lenders on their chattel secured agricultural loans. This analysis quickly identifies potential problems and can be used to correct the problem, change the operation or avoid future problems. It is a valuable decision making tool for any chattel secured loan and is not overly burdensome to lenders. As far as an annual balance sheet or statement of financial condition is concerned, this comment appears to address real estate loans and the SEL reporting requirements. While the Agency has removed this requirement for CLP lenders, SEL may be more inexperienced and may require a closer level of monitoring by the Agency. The Agency will only review a sample of an SEL guaranteed loan files in a given year; therefore a balance sheet in the Agency loan file will assist monitoring of these loans.

A comment requested that the Agency clarify the rule to state that any decision not to perform an annual analysis will be made after consultation with the Agency. This comment deals with proposed § 1980.141(d)(1) that allowed CLP lenders to forgo a complete analysis if there is sufficient financial strength to support the decision. The comment is not being adopted. A large number of comments indicated their support for the analysis requirements as proposed. The Agency's internal handbook will provide examples of financial strength factors that may be acceptable as reasons to waive the analysis. If lenders do not perform an analysis, § 762.141(d)(1) requires that the reasons be documented in their file and in their narrative, which is submitted to the Agency. FSA will review the narrative and the case file can be audited during a routine lender monitoring visit.

Consolidation

Several comments were received discussing loan consolidation. The Agency is also making some clarifications and minor modifications. First, the Agency has removed consolidation from the distressed servicing section. As used by FSA, consolidation is simply a combination of two or more similar performing loans into one loan and, thus, is not a distressed servicing action and is not useful as a tool to correct default. Therefore, in the final rule, proposed § 1980.145(b) has been moved from the distressed servicing section to § 762.146(e), other servicing procedures.

A comment requested that loan consolidation authority be eliminated. Loan consolidation is included as an authorized loan restructuring action in the Consolidated Farm and Rural Development Act and must be maintained as an authorized action. Moreover, loan consolidation is a standard industry practice and, in the interest of allowing lenders to conduct business as usual on their guaranteed loans, the Agency wishes to allow the practice to continue.

A comment suggested that the prohibition against consolidating loans made prior to fiscal year (FY) 1992 with those made after FY 1992, proposed in § 1980.145(b)(3), be eliminated. The proposed rule provided that consolidation of an FY 1991 loan with a post FY 1991 loan that did not have interest assistance would eliminate the ability to provide interest assistance for servicing on the consolidated loan. This result ensues because, under Agency budgeting procedures, the consolidated loan becomes an FY 1992 loan. The Budget Reconciliation Act of 1991 eliminated budget authority for interest assistance on FO loans and greatly restricted the Agency's ability to provide interest assistance for servicing actions by, in effect, making the awarding of subsidy on these loans cost prohibitive. To implement this authority and adopt the comment would result in a dramatic increase in the assumed cost of the guaranteed OL program and a commensurate decrease in its loan funds. The result would be a drastic reduction in the number of loans the Agency could guarantee and the number of farmers it would be able to assist. Therefore, the comment was not adopted.

Comments were received requesting that consolidations be limited to only those loans with the same percent of guarantee. The comment was not adopted; however, the final rule provides that when a new guarantee will be provided for a consolidated loan, the percentage of guarantee will be the lesser of the loans being consolidated.

Interest Rates

Comments were received requesting that the Agency allow for refinancing of existing guaranteed loans when the interest rate can be fixed. The proposed rule at § 1980.146(d) and the final rule at § 762.146(d)(3) provide for a change in rates from variable to fixed even if the loan is not delinquent. Therefore refinancing for this purpose is not necessary.

Substitution of Lenders

One comment was received requesting the Agency to clarify substitution of lenders. When a borrower wishes to move a guaranteed loan from one lender to another, or a lender wishes to sell a guaranteed loan to another lender, with or without the borrower's consent, FSA must process a substitution of lender. When a substitution occurs, the existing guaranteed documents must be assigned to the new lender. The Agency agrees with the comment that the lender substitution provisions in § 1980.105(c) were inadequate. The Agency has revised § 762.105 to clarify that the original lender and the Agency must concur with the substitution. If the original lender does not agree to assign their promissory note, lien instruments, loan agreements, and other documents to the new lender, then the substitution cannot take place and the new lender could only refinance the original lender. Refinancing would require the use of new loan funds and a guarantee fee. The Agency believes that the new authorities provided to lenders in this rule, such as partial release, subordination and change in interest rates will provide lenders with additional tools to continue to service existing borrowers, so that a substitution request will be less likely.

Partial Releases

Almost every comment received was in support of the Agency proposal to add partial release authorities to its guaranteed lending regulations. Additionally, many comments suggested that we, ''clarify that partial release authority would be at the field office level,'' and ''clarify when appraisals will be required for partial releases.'' Agency approval authorities for partial releases is an administrative matter and will be delegated through internal FSA directives. It is not included as part of this rule. Authority is likely to be extended to local offices. However, the Agency agrees that the proposed rule contained excessive application requirements for some types of partial releases. Therefore, § 762.142 has been revised to clarify what items are needed to request a partial release by CLP lenders and SELs. Similarly, the proposed rule is revised from requiring Agency concurrence to not requiring Agency approval when the security is being sold for market value, and the proceeds will be applied in accordance with lien priorities, when the security will be used as a trade-in or as a source of down payment funds for a like item that will be taken as security, or when the security item has no present or prospective value. Agency concurrence is required only when the proceeds will be used to make improvements to real estate in an amount equal to the amount being released, as stated in the proposed rule, security is being released without consideration but the loan to value after the release will be .75 (loan balance to collateral value) or less. The handbook will provide guidance as far as how proceeds would be applied on the loan, and how input may be requested when there is a question of whether reasonable value is being obtained for the security.

As for appraisals, the proposed rule at § 1980.142(d)(2)(i) provided that, for CLP lenders and SEL, the Agency would determine the need for any chattel appraisals and that real estate appraisals will not be required of the lender unless the Agency specifically requests them. Section 762.142(b)(2)(vi) provides that appraisals will be required when security is released without consideration. A suggestion that the Agency never require an appraisal for restructuring a loan, or for a partial release, was not adopted. Appraisals are not required to reschedule a loan, but since partial releases involve releasing loan security, an appraisal was not viewed as overly burdensome.

Subordination

Several commenters suggested that the Agency delegate to local county offices concurrence with a lender's request to subordinate a guaranteed loan. This comment is being partially adopted. The Agency has revised § 762.142(c)(3) to allow for the subordination of normal income security for the guaranteed lender or another lender to make an operating expense loan without Agency concurrence. The Agency agrees that the subordination of normal income security for a lender to make an operating loan is consistent with the mission of the Agency, to help borrowers progress to the point of obtaining credit without Agency assistance.

Some comments were received requesting that the Agency expand its subordination authority to include real estate loans. This comment was not adopted because, in most cases, subordination of guaranteed loan security increases the risk of loss to the Government. The Agency will continue to discourage subordination of real estate security and not provide regulatory approval authority at levels lower than the Deputy Administrator for Farm Loan Programs. See § 762.142(c)(3). If a request is received that the State Executive Director feels is in the best interest of the Government and the borrower, it can be forwarded to National office for final consideration.

Other comments suggested that the Agency subordinate for tax exempt transactions. This comment is not being adopted. The Agency understands that tax exempt transactions often result in a lower interest rate for the borrower; however, has determined that a subordination of a Federal loan guarantee will not be provided in these types of transactions.

Emergency Advances

Overall comments were very favorable toward the proposal to add an emergency line of credit advance provision, although, several comments were received requesting that Agency approval be obtained on all emergency advances. The proposed rule did not specifically require Agency approval on emergency advances. The Agency recognizes that this may be confusing, so the suggestion to clarify approval is being adopted in § 762.146(a)(2), which will require CLP lenders and SEL to obtain prior FSA concurrence for emergency advances. PLP lenders will make these advances in accordance with the provisions of the PLP agreement. In all cases, the financial benefit to the lender and the Government must exceed the amount of the advance and the lender must document the financial justification for the advance.

Another comment requested that the Agency limit emergency advances to 10 percent of the line of credit ceiling or set a dollar limit. This comment is not being adopted. The Agency understands the comment's concern that there be a limit to the amount of the advances. However, if a specific percentage or dollar amount were established, it could have the opposite effect of what the comment intended. This policy would encourage lenders to assume 10 percent or a certain dollar limit is always acceptable. Therefore, FSA will not adopt this policy. The experiences supporting this proposal have shown that when this situation arises, the need is usually less than 10 percent of the line. However, in a few instances, a greater advance is required. In any case, the benefit to the lender and the Government must exceed the advance. For example, if a lender with a $400,000 line of credit advances $20,000 as an emergency advance for irrigation and saves a crop, the Government may pay $20,000 in losses on the loan. But had the crop not been watered, it may have been a total loss and the Agency loss may have been $400,000. In this example, the benefits derived obviously exceed the advance amount.

Several comments requested that the Agency clarify the emergency advance lien priority as it relates to the guaranteed loan and how it is paid, and a few comments indicated confusion regarding the difference among an emergency advance, protective advance, and an additional loan. These comments are addressed in § 762.146(a)(3)(iv) by requiring that the emergency advance must constitute an advance against the line of credit and be secured by the same lien instruments. Emergency advances are not a separate loan, but part of the guaranteed loan. To subordinate this advance in favor of the lender on a non guaranteed basis, as was suggested by some, would provide an effective 100 percent guarantee of repayment of the advance, because the emergency advance would be paid in full before application of payments to the line of credit. Because the emergency advance is necessary for the guaranteed loan, the lender should share the risk in proportion to the guarantee. Emergency advances are similar to protective advances in that they are made to protect security from being lost, constitute an obligation under the promissory note, and cannot be made in lieu of a new loan. They differ from protective advances in that emergency advances are made only in the case of a line of credit to protect, harvest or market only normal income security, when the borrower is not in liquidation. Protective advances are made to protect any type of security for a multitude of purposes, when a loan is in default and liquidation is likely.

The Agency received a comment requesting expansion of the lender's authority to make emergency advances in situations outside the limitations placed in the rule. This comment is not being adopted. The Agency does not agree that there are any circumstances justifying further exposure on the guarantee, other than when loss of crops or livestock is imminent, the advance is for authorized operating loan purposes, and the benefit derived will exceed the amount of the advance. These situations are covered by § 762.146(a)(3).

Restructuring

In the proposed rule, only SELs required Agency approval when restructuring a guaranteed loan. CLP and PLP lenders would not require Agency approval with restructuring actions, except for loan writedowns. While a majority of the comments were in favor of the rule, several commenters felt that Agency approval of all restructuring actions was necessary to assure that the restructuring is in accordance with regulations. This suggestion was not adopted. PLP and CLP lenders are more experienced lenders and they are more familiar with Agency requirements. Still, they must restructure loans in accordance with the minimum Agency requirements for restructuring for all lenders. Lenders who do not restructure in accordance with minimum regulatory requirements risk not being paid in the event of a loss. Furthermore, Agency approval of a lender's restructuring action does not endorse servicing that occurred prior to the restructuring, nor does a note's compliance with Agency regulations ensure that the restructuring was completed correctly. Agency officials often do not have the time to thoroughly analyze all facets of a lender's restructuring request, and lenders and their associations have suggested that Agency employees be less involved with approval of a lender's actions. Therefore, the Agency is placing this responsibility upon the more experienced lender.

A similar comment requested that the Agency require PLP lenders to submit a credit analysis prior to Agency approval of rescheduling. PLP lenders have significant agricultural lending experience in addition to their familiarity with Agency guaranteed loan programs. Having the Agency review the PLP lender analysis, in most instances serves no useful purpose. PLP lenders know how to analyze credit and make loan restructuring decisions based upon those analyses. In addition, they are required to have documentation of their analysis in the file. If a PLP lender does not take those actions required by the lender's agreement and Agency regulations prior to restructuring, in the event of a loss, the lender's loss claim under the guarantee may be reduced or denied.

One comment requested that the Agency make a decision on the PLP or CLP lender's servicing requests within 14 days, rather than state that the Agency will ''consider the request.'' Proposed § 1980.145(a)(1)(i)(C) states that only SELs are required to obtain Agency approval and the Agency must notify the SEL within 14 days of the request. The comment apparently mistook the Agency's discussion of proposed changes in the rule, which used the word ''consider'', for the regulatory requirement.

Another comment suggested that the Agency not be required to act in 14 days if the borrower has a direct loan that is being serviced under the provisions of 7 CFR part 1951, subpart S. This comment is also apparently a misunderstanding, because the rule stipulates certain items to be submitted to the Agency for approval before the 14 day period begins. If a guaranteed borrower is having direct loans rescheduled by the Agency, much of the required information, such as a feasible plan, cannot be provided by the lender until direct loan servicing is complete.

One comment requested that the Agency require the lender to account for security and provide a loan history as part of any loan restructuring action. The Agency believes that the adoption of this suggestion would not provide additional assurance that the loan was adequately serviced. The existing rule states that a final loss claim may be reduced, adjusted, or rejected as a result of negligent servicing after the concurrence with a restructuring action. The intent of this statement is to remind SELs that Agency concurrence with an action does not mean that all actions up to that point regarding servicing are satisfactory. The statement in the rule also applies to CLP and PLP lenders, who do not require Agency concurrence prior to restructuring.

Balloon Payments

Several comments were received requesting the Agency allow for the reamortization and restructuring of loans with a balloon payment in the repayment schedule. The Agency agreed to add a regulatory prohibition against rescheduling loans with balloon payments several years ago in response to a recommendation of the USDA Office of Inspector General (OIG). OIG determined that many Agency guaranteed loans were being restructured with no realistic planned repayment when the balloon payment came due. As a result, the borrower did not receive any real benefit and, in many cases, the balloon payment was used to simply put off the inevitable. This caused continuing difficulties for the borrower and, ultimately, a larger loss to the Agency. However, the Agency does recognize the need for the lender to have the flexibility of being able to restructure a loan with a payment schedule other than equal amortized payments. Thus, § 762.145(a)(3) allows a loan to be rescheduled with uneven payments provided the borrower projects a feasible plan for the upcoming year and can reasonably demonstrate that when the installments increase they will be repaid without further restructuring. The Agency intends that unequal installments will coincide with the need to re-establish an enterprise or an unusual cash flow cycle.

Prohibition of Advances on Rescheduled Lines of Credit

One comment requested that prohibiting advances on rescheduled lines of credit should not apply to those lines of credit already in effect. The comment suggested that FSA ‘‘grandfather in’’ all existing lines of credit to allow them to be rescheduled, and permit advances on the difference between the line maximum and the rescheduled balance. FSA's intent in § 762.145(b)(1)(ii) is that, on the effective date of this rule, the change will apply to all lines of credit except those that have been previously restructured. To adopt the comment's suggestion would require gradual implementation of the restriction for up to five years on existing lines of credit. This would create problems in administering the restriction. Therefore, the Agency will not adopt this suggestion for all lines of credit. While the final rule will allow rescheduled lines of credit with remaining balances to be re-advanced, on the effective date of this rule, the Agency will not allow advances on lines of credit where restructuring has not already occurred.

Debt Writedown

Several comments were received from Agency field offices concerning the Agency's debt writedown provisions proposed in § 1980.145(e). One comment was received suggesting that the Agency require an OL loan that is being written down to be amortized over a minimum of 10 years, as opposed to the 5 year minimum that was proposed in § 1980.145(e)(5). The Agency understands the commenter's concern that the amount written off and the resulting loss claim payment is higher when the loan has a shorter term. However, the Agency intends to be flexible in those situations where the life of the security is less than 10 years and it is the lender's policy to not restructure beyond the life of the security. This may provide an incentive for lenders to provide a writedown to a farmer that needs one to stay in business.

Another comment requested that the Agency require the lender to take a lien on all assets when writing down a guaranteed loan. The Agency considered this option; however, it was not adopted because it would create future credit problems for the operation. The Agency felt that this situation should be handled on a case-by-case basis, with guidance provided in the Agency handbook and in consideration of the lender's internal policies. Also, § 762.145(e)(9) does require a cross collateralization of security if the borrower has other guaranteed loans that are not secured with the same security as the loan being written down.

Several comments expressed concern over the 20 year minimum amortization for an FO loan that is being written down. For example, there is concern that if there are only 19 years left on a 40 year FO loan, in accordance with § 307(a)(1) of the CONACT, it cannot be reamortized to exceed 40 years from the original date of the loan. The Agency has written § 762.145(e)(5) to state that the loan will have a 20 year term minimum, unless the remaining term exceeds the statutory term. If the term cannot be extended to 20 years, it will be extended to the maximum term available under the CONACT.

Servicing Fees

One comment requested the Agency not pay the holder a servicing fee when repurchasing a guaranteed loan from the secondary market. The proposed rule at § 1980.144(b)(3) stated that the Agency will not reimburse the lender for any servicing fees which have been assessed to the holder. The comment is being adopted in § 762.144(b)(3) of the final rule by adding the words ‘‘after the Agency repurchase.’’

Bankruptcy Costs

The proposed rule at § 1980.148 contained several revisions to the Agency's loss claim procedures with regard to the costs incurred when a borrower files for protection under the provisions of the bankruptcy code. The most consequential of these changes is the reversal of current policy prohibiting the payment of legal fees and appraisal fees in a bankruptcy. A large number of comments were received on this proposal, with the majority in favor of the change. However, several comments were received requesting that these fees not be covered or that they be covered at a reduced percentage. The comments suggest that inclusion of these fees in the lender's guaranteed loss will reduce a lender's incentive to minimize these expenses and exacerbate the Government's losses on these loans. As stated in the discussion of this change in the proposed rule, the Agency believes that payment of the guaranteed percentage of legal fees in a bankruptcy is a legitimate and logical extension of current policies on the payment of a lender's losses. Also, this change will benefit more family farmers and ranchers by encouraging lenders who have not previously participated in the guaranteed loan program to now make loans. Many lenders have said that one of the reasons they do not participate, or participate at a minimum level in the Agency's guaranteed loan program, is because the Agency does not cover all fees with the guarantee. Maintaining the reasonableness of legal fees is an issue that will have to be dealt with through appropriate guaranteed loan portfolio management. The Agency will retain the option of scrutinizing a lender's claimed expenses and reducing a loss claim request when a lender has not monitored expenses and has allowed unfettered fees to accumulate.

Where appraisals are concerned, the court often requires the lender to have the collateral appraised, or at least share in the cost of an appraisal. The Agency allows appraisal costs in a liquidation loss claim, and this change will make bankruptcy procedures more consistent. More importantly, the coverage of the cost of an appraisal will assure that, in bankruptcy cases, accurate representations of security values will be obtained.

Several comments suggested modifications in the final rule, such as limiting coverage of lender legal fees to 50 percent, making sure that the fees are not excessive, clarifying what expenses are reasonable, requiring prior approval of estimated legal fees, and not guaranteeing legal fees at all. One comment suggested that covering legal fees is detrimental to the borrower. The Agency will only guarantee reasonable legal fees. We believe, and lenders have stated, that they are more likely to aggressively act in bankruptcy cases if they know that such costs are covered by the guarantee. While a lender's aggressive action in bankruptcy may be viewed as adverse to a borrower, the borrower's interest is protected by the court. The Agency's exposure on the guarantee is with the lender. The Agency believes it is unlikely that a borrower will lack due process as a result of covering legal fees under the guarantee. Since the Agency believes that the commenter's suggestion embellishes the likely effect of the rule, it will not adopt the comment. It is in the Government's interest to assure that the lender takes every action to protect its loan security and ensure that losses are minimized. The overriding consideration is that more lenders will participate in the guaranteed loan program, increasing credit availability and providing a benefit to family farmers and ranchers.

The suggestion that the Agency pre-approve estimates of fees was also not adopted. Agency approval of an estimated expense is time consuming and burdensome on both the Agency and the lender and serves no purpose other than to have an estimate which may be higher or lower than the actual amount.

Also, in response to another comment, the Agency will guarantee attorney fees based upon the assumption that lenders will be using sound, licensed, professional legal counsel when involved in such an action. Losses incurred as a result of servicing deficiencies may not be paid under a loss claim. Such deficiencies may include the failure of a lender's legal counsel to represent its interest by not filing objections where appropriate or other actions.

On a related subject, a comment suggested that FSA guarantee legal fees incurred outside of bankruptcy, as well as fees incurred as a result of lender liability suits brought by the borrower. For the former, the rule provides that lenders subtract reasonable liquidation expenses from the proceeds received from a liquidation action. However, lender liability suits are actions specific to the relationship between the lender and the borrower. As such, they are recognized as a risk of business for which the Government is neither responsible, nor prepared to assume responsibility for under the guarantee.

This rule does not expound on what the Agency regards as reasonable or frivolous expenses as suggested by several comments. The Agency acknowledges the potential for inconsistency in how ''frivolous'' or ''unreasonable'' is determined. By ''frivolous'', the Agency is referring to those expenses which, in its opinion, the lender's attorney cannot legitimately claim, or the lender cannot legitimately request coverage of by FSA. The decision of what is ''reasonable'' is situational. The Agency believes that the terms ''frivolous'' and ''unreasonable'' are sufficiently precise to establish standards of ''reasonable'' expenses. The standards are based on each case considering the legal costs in the locality, the size of the debt, the type of security, and the amount of opposition encountered. The expenses will be adjusted based on a comparison of each of these items for similar cases in the area. Guidance on review and approval of bankruptcy loss claims will be included in the Agency field office handbooks. Current policy of not covering the lender's in house, or normal operating expenses, will continue. See § 762.148(b)(1)(i) of the final rule.

Default Meeting

One comment requested that the Agency require its personnel to be included in a meeting described in the proposed rule at § 1980.143(b)(3). The Agency does not feel that it is necessary to attend the meeting between the lender and the borrower to discuss the loan delinquency. Agency personnel have the option to attend the meeting, if requested by the lender, if they are unsure what actions may or may not jeopardize the guarantee. However, the lender often needs to act quickly and there may be scheduling conflicts. Placing Agency employees at the meeting can leave the impression with the borrower that Agency guidance regarding regulations means the FSA employee is making the decisions. The loan is the lender's and it is the lender's responsibility to service it.

Liquidation

Several comments were received regarding the time frames lenders are required to meet in a liquidation action. A similar comment suggested that the Agency not require the consideration of interest assistance prior to liquidation. Both comments suggest removal of proposed § 1980.143(b)(3)(v). The reasons for the suggestion are understandable, as nothing is accomplished by the required 60 day waiting period. Nonetheless, lenders who participate in the Agency guaranteed loan program are required by § 351(g) the CONACT to wait 60 days after considering interest assistance before initiating liquidation. However, if restructuring is not an option and liquidation should proceed, the lender can conduct preliminary activities to liquidation, to expedite recoveries after the 60 day period has passed. Also, if the borrower waives interest assistance, liquidation may begin immediately. This rule includes clarification of how interest assistance is considered in conjunction with a distressed servicing action and the FSA handbooks will include additional guidance on how this provision is to be dealt with. The Agency believes the other time frames for liquidations provided are reasonable considering the complexities involved in any liquidation action.

A similar comment asked the Agency to clarify how the borrower's eligibility for interest assistance is automatically determined upon receipt of the default status report. As stated above, interest assistance will not cure a default, except as part of a rescheduling proposal. In response to this comment, the Agency added language to § 762.143(b)(iii) to state that lender's consideration of a borrower for interest assistance will be included on a default status report. This amended procedure will advise the Agency that interest assistance has been considered, and to assure that the interest assistance has been considered in all cases.

Liquidation Plans

Several comments requested that the Agency not require PLP lenders to submit liquidation plans, while other comments requested that the Agency not require lenders prepare liquidation plans. The first suggestion is being adopted and § 762.149(b)(2) is revised so that PLP lenders are not required to submit liquidation plans unless the lender's agreement requires it. PLP lenders will be required to have a plan developed for liquidation, although each PLP liquidation plan may differ slightly, as spelled out in the PLP agreement. Agency monitoring of default status reports, which will contain previous actions and planned actions, will allow Agency officials to monitor PLP progress on liquidations. As far as non PLP lenders are concerned, the Agency feels that a liquidation plan is necessary to protect the Government's interest, and provide guidance on the status of defaulted guaranteed loans. Plans can be brief as long as they include the items required to be addressed by § 762.149(b). Agency personnel must be kept informed when a guaranteed loan moves to the liquidation stage. The liquidation plan's preparation assures the Agency that repurchase from a secondary market holder has been considered and advance preparation to minimize losses has begun. Also it serves to assure the lender that the Agency is in agreement with its actions, so misunderstandings may be avoided.

The Agency was requested not to specify how estimated loss payments will be applied. The comment stated that since interest accrual ceases upon payment of the estimated loss claim, it does not matter how the lender applies the loss claim payment. The application of the proceeds becomes insignificant because interest accrual on the defaulted loan ceases. The Agency is adopting this comment and has amended § 762.149(d)(2) accordingly.

The Agency was also requested to respond to lenders' liquidation plans sooner than 30 days. The Agency agrees that there is little justification for the 30 day period since the Agency reply requirement is based on a complete plan and the Agency must simply respond with an approval, request for clarification or additional information. As a result, § 762.149(c)(2) was revised to state that the Agency will respond within 20 calendar days; otherwise, the lender may assume the plan is approved and proceed with reasonable actions to protect its interest and liquidate the loan.

A commenter suggested that the Agency hold a lender harmless for liquidation actions taken prior to FSA concurrence as long as they are prudent and reasonable. The standard to which a lender will be held is ''reasonableness.'' The Agency will not penalize a lender in this situation for reasonable actions. This comment will be addressed further as an administrative matter in the Agency handbook, providing that loss claims will only be reduced as far as the lender's actions contributed to the loss.

Several comments requested that the Agency not require a liquidation value appraisal be provided with a liquidation plan and another suggested requiring a value in between the liquidation value and the market value to be bid at any forced security sale. The comment's suggestion that all estimated losses be based upon a market value appraisal, less estimated liquidation costs, is being adopted. The Agency agrees that the ''liquidation value'' term is confusing when used in context of liquidation plans and estimated loss claims. Section 762.149(b)(4) has been revised to require the lender to provide a net recovery value determination, defined in the final rule as the difference between market value and anticipated selling expenses. At a minimum the lender must bid the lesser of this value or the unpaid guaranteed loan balance at any forced sale. See § 762.149(h). This complies with standard industry practices and the Agency sees no benefit in bidding higher than net recovery value at a distress sale. Another comment on this section requested that the Agency be flexible on the requirement to obtain a balance sheet as part of the liquidation plan, as it may be difficult for a lender to obtain a current balance sheet from a distressed borrower. The comment is not being adopted; however, clarification of expectations when a borrower is uncooperative has been added to § 762.149(b)(1). The Agency would expect the lender to provide the most recent financial information available in these instances.

Protective Advances

Comments were received requesting the Agency raise the limits on protective advances proposed in § 1980.149(e)(1). The proposed rule required that protective advances in excess of $500 for SELs and $3,000 for CLP lenders must be approved in writing by the Agency. These limits have been in place for several years and the Agency agrees that costs have increased and these limits may be outdated. Therefore the rule has been revised to raise the limits for CLP lenders to $5,000 and SELs to $3,000. The Agency believes that these limits are sufficient for advances that a lender must make before receiving a written response from the Agency. PLP lenders will make protective advances in accordance with the PLP agreement. These limits do not apply to emergency advances described in § 762.146(a).

Net Recovery Value

The Agency received a comment suggesting that it amend the definition of net recovery value to reflect the difference between the market value and the lender's cost of liquidation, instead of the Government's cost. We have adopted this suggestion and made the change in § 762.102(b).

Another comment suggested the Agency define net recovery value. The proposed rule at § 1980.102(b) did define net recovery value; however, further clarification was needed regarding the term ''estimated future value'' which was used in the definition. Section 762.102(b) has been revised to replace that element of net recovery value with ''market value.'' This value, less the lender's estimated cost associated with the disposal of the property, is the net recovery value. Further guidance on net recovery value calculations and their use in loan servicing actions will be provided in FSA handbooks.

Interest Accrual

One comment requested that the Agency clarify interest accrual on loss claims. The suggestion is being adopted. While the rule clearly states that interest accrual will cease upon the payment of an estimated loss claim, the comment is concerned about a case where no loss is expected, but there is a loss after final disposition. Section 762.149(d)(2) requires the lender to provide the Agency a loss estimate of zero, whereupon interest accrual will cease on the defaulted loan. This will encourage the lender to liquidate the account expeditiously and provide the Agency with a record of a liquidating account. The lender may collect all manner of late charges, fees, costs, and interest on the loan up to the point it is paid in full, as long as security proceeds are sufficient to pay the entire debt. If a loss occurs upon submission of the final claim, the guaranteed percentage of the loss will be paid; however, interest that accrues after receipt of the no-loss estimate will not. This is consistent with the handling of those accounts that have an additional final loss, not including interest accrual which ceased upon the Agency's payment of an estimated loss claim.

Final Loss Payment

Several comments suggested clarification of the Agency's policies and procedures on payment of final loss settlements contained in proposed § 1980.149(i). One comment dealt with losses when a lender takes possession of real estate collateral. The comment requested that the Agency allow lenders to request a final loss payment upon the borrower's transfer of the security, provided the lender receives the full appraised value of the security. A related comment requested that all final losses be based upon the ultimate disposition of collateral. Agency experience and common sense, as discussed in the proposed rule, indicates that few lenders opt for final payment prior to ultimate disposition. In order to establish consistency in the final payment process and avoid the misunderstandings that have occurred, this seldom used option was eliminated.

One comment requested the Agency clarify proposed § 1980.149(i)(6) as to how the deduction for the value of security that has not been accounted for will be calculated. Failure to obtain a lien on, monitor, inspect, or properly apply proceeds from the sale of collateral in most cases will be used as a reason for a reduction or denial of a lender's claim under a guarantee due to negligent servicing. However, the fact that there is unaccounted for security will not necessarily cause a reduction because of negligent servicing. The decision will be based upon the lender's servicing and collection efforts. Also the Agency will not penalize a lender for servicing deficiencies that did not contribute materially to a loss. The Agency has clarified this provision in § 762.149(i)(6) as suggested.

Future Recovery

Another comment requested that the Agency include specific procedures and time frames for additional collection actions after a guaranteed loan loss claim has been paid. The proposed rule at §§ 1980.149(j) and 1980.141(f) outlined what the lender's responsibility is for future collections. The rule proposed submission of an annual report on all unsatisfied accounts for three years following payment of a claim. Sections 762.149(j) and 762.141(f) adopts these provisions unchanged. Further explanation of the administrative aspects of the rule will be provided in the Agency handbook.

Release of Liability

One commenter questioned why the Agency is giving the lender release of liability authority. The meaning of the comment is unclear since §§ 1980.146(b) and (c) of the proposed rule provided for Agency approval of release of liability in the case of SEL and CLP lenders. Also, as outlined in the proposed rule, releases of liability will only occur in cases of divorce, bankruptcy, withdrawal from the operation (without retention of any farm assets), and liquidation, and will be based on the strength of the remaining liable party. The Agency estimates that this new authority will not impact current loss levels.

Termination

One comment was received requesting that the termination of guaranteed loans be expanded to include the denial of loss claims upon written notification by the Agency. The comment is not being adopted, as such a provision is included in the guarantee document itself. Also, termination of the guarantee automatically occurs upon the denial of a loss claim after all appeal rights are concluded. Requiring Agency personnel to specifically state this in a letter is an administrative issue that will be covered in the Agency handbook. Similarly, it was suggested that the Agency require lenders to return guarantees marked paid in full on all paid guaranteed loans. The Agency has revised § 762.149(i)(11) to require this.

Interest Assistance

On February 28, 1991, Farmers Home Administration (FmHA) published an interim rule [56 Fed. Reg. 8258–8272] with a comment period ending April 29, 1991. The Omnibus Budget Reconciliation Act of 1990: (1) increased the potential level of government reimbursement for interest rate reductions made by lenders on guaranteed farm loans; (2) extended the potential term of interest rate reduction on guaranteed farm loans; and (3) extended authorization for the subsidy program through September 30, 1995. On February 10, 1996, it was extended until November 30, 2002. See Pub. L. 104–105 § 220. It was necessary to implement this rule upon publication to provide assistance to a large number of farmers who would otherwise be unable to obtain sufficient credit to operate in 1991. In response to the interim rule, 175 respondents from 24 States and the District of Columbia commented in writing. Many of the respondents' letters contained comments on a number of the sections of the interim rule. Comments were received from individuals, Agency employees, interest groups, lenders, bankers associations, Farmer Mac, Members of the Congress, and the Department of Treasury. Several comments complimented various segments of the program.

There were four comments on the consideration of significant non-essential assets. Of those, one comment recommended that significant non-essential assets be made available for security but that their sale not be forced or assumed in cash flow. A second comment suggested that all members of entities be required to pledge all non-essential assets. Two respondents requested that borrowers be required to liquidate significant non-essential assets before the interest assistance loan is closed or before the subsidy is continued. In the interim rule, cash flow is calculated based on the assumption that significant non-essential assets will be sold. There is no requirement to actually sell non-essential assets if the obligations can be met otherwise. The Agency has adopted the recommendation to continue with the policy of the interim rule, with a clarification in § 762.150(b)(3) to consider non-essential assets of entity members. FSA has a long-standing policy not to provide subsidized credit to enable applicants to retain assets which are not essential to the farming operation.

The interim rule provided for a floating maximum subsidy rate not to exceed 4 percent. Two respondents commented that it was clearly the intent of the legislation that the 4 percent subsidy be made available to all eligible borrowers based on need. One comment suggested that the maximum rate available be reduced in stages over the life of the agreement.

Under the interim rule, the level of interest assistance to be received is determined and set at .25 percent increments. One hundred fourteen comments objected to the use of the increments. The Agency agrees that projected farm budgets cannot be as precise as the .25 percent increment required and implied. Granting interest assistance at the 4 percent level in every case would give recipients subsidy for their need, and increase their probability of remaining a viable farming enterprise. On December 17, 1993, the Agency published a change at 58 FR 65871,65887 adopting the recommendation to determine and set interest assistance at 4 percent in all interest assistance situations which require any level of subsidy. This is adopted at § 762.150(d)(1)(i).

The Agency changed from incremental amounts of interest assistance to a straight subsidy amount of 4 percent on December 17, 1993. The Agency is considering whether alternative methods such as a return to the use of increments in determining subsidy levels would be appropriate. During the review of the regulations, questions were raised as to whether alternative subsidy calculation methods would produce a cost savings and increase the number of producers that could be helped. By using incremental subsidy, rather than a 4 percent subsidy, the Agency might be able to target the amount of interest assistance subsidy paid more closely to borrower need, reducing the assistance in some cases, so that more qualifying producers could be assisted with the available subsidy. To assist us in considering alternative proposals, we are specifically asking for comments regarding the use of incremental subsidies, at what increments should the subsidy be established, and any other alternative methods of establishing the subsidy rate.

The interim rule provides for interest assistance payments to be made to lenders on the basis of claims which can be submitted only once annually. All comments on this issue wanted to be able to submit claims more often than once annually. Various methods of payment were suggested by the comments. Based upon the comments received, the Agency believes that more frequent claims may be conducive to lenders sale of the guaranteed portion of loans with interest assistance into the secondary market and may allow the lender to offer a slightly lower interest rate to the borrower. However, the lender's increased earnings would be minimal and may or may not be passed on to the borrower in the form of lower rates. Because Agency resources are limited, processing frequent (i.e., monthly) claims would overload Agency offices. Therefore, the Agency has decided to continue to allow claims only at 12-month intervals.

All comments regarding the cap on variable interest rates were in opposition to it. The Agency has adopted the recommendation to remove the cap on variable interest rate increases to be consistent with other loan programs and the industry standard. See § 762.150(b)(7).

The interim rule required that the need for interest assistance be reviewed annually, and the level of assistance be adjusted if necessary. One hundred twenty-one separate comments requested various changes in this requirement. Most of the comments recommended the review period be increased to 2 or 3 years, several recommended a 5 year interval and others objected the review, but offered no alternative. The Agency acknowledges that periodic reviews place a burden on the lender. However, this requirement was established as a control to prevent borrowers whose financial position improves from receiving unneeded subsidy in later years of the loan. The Agency has considered the comments and believes that less frequent reviews will create a significant risk of payment of excess subsidy. Therefore, the Agency has decided to not change the review period.

Eight comments were received regarding the minimum loan terms for interest assistance. Minimum terms are specified as a safeguard to prevent use of a reduced payment term which would increase installments so that an applicant or borrower, who would otherwise not need interest assistance, might qualify. Two of these comments suggested that existing loans whose original terms met the requirements, even though they do not meet them now, should qualify for interest assistance. Other comments suggested permitting a balloon payment in 5 or 10 years. Balloon installments place additional risk on the long term viability of the operation and are not acceptable for borrowers in need of a subsidy. The Agency has changed § 762.150(b)(1)(iii) to consider the 20-year requirement on farm ownership and soil and water loans secured by real estate, to begin on the loan closing date (on loans with existing guarantees) instead of the effective date of the interest assistance agreement. This is consistent with the intent of the provision, and reduces the cost and paperwork for borrowers who had a loan with terms of 20 years or more, but have less than 20 years remaining.

The interim rule required that requests for interest assistance on annual operating loans and lines of credit be accompanied by a monthly cash-flow budget. The Agency received seven comments in opposition to the requirement. The purpose of this budget is to accurately estimate the maximum credit needs of the borrower and the average loan balance. This is a fundamental part of sound credit analysis. Therefore, the Agency is not adopting this suggestion, since it would reduce the quality of the analysis.

Three comments discussed the issue of the inadequacy of compensation for lenders for the extra work required by the subsidy program. Two of them suggested higher interest rates or assessing fees to the borrower as compensation. One comment suggested that the Agency pay a fee to the lender to cover additional costs. It is not reasonable to expect that borrowers whose financial position allows them to qualify for the subsidy program to afford the additional cost for payment of a fee. Section 351(c) of the CONACT prohibits the Agency from paying a fee in addition to 100% of the cost of interest reduction. Therefore, the Agency has not adopted these suggestions.

One comment requested clarification of the penalty for lenders who fail to complete annual analyses or submit claims within the 60-day timeframe. The Agency is concerned that the analysis needs to be tied to the claim to encourage timely analysis and planning. Section 762.150(d)(1)(ii) has been revised to encourage filing within 60 days and state that failure to submit a claim within 1 year will result in forfeiture of the payment.

Several comments requested that the Agency establish timeframes to process claims. The Agency agrees that claims should be processed in a timely manner. Suggested timeframes have been established in the agency handbook.

The interim rule limited the term of interest assistance to 10 years on each loan. Eighty-seven comments were received on this subject; one suggested that we should make the term of eligibility limitation per borrower rather than per loan, two suggested allowing interest assistance for the life of the loan, one was concerned that the period of assistance is too long, and 83 were pleased to see the increase from 3 to 10 years. The program is designed to provide temporary assistance to borrowers. It is most reasonable to tie the eligibility period to the borrower rather than any particular loan. Tying eligibility to any loan provides an almost unending subsidy as borrowers can receive additional loans and continue the subsidy almost indefinitely. The Agency adopted the recommendation to limit the term of interest assistance to 10 consecutive years per borrower.

The interim rule required a positive cash flow (with a 10-percent margin) to be eligible for interest assistance. This subject drew a variety of comments from 94 respondents. A few comments were in support of the interim rule while the vast majority were opposed to various aspects of the margin requirement. Recommendations ranged from deleting the requirement altogether to allowing a greater than 10-percent margin. Many respondents suggested allowing continuation of interest assistance or applying subsidy to existing guaranteed loans, with no margin requirement. The Agency continues to believe that as a cash flow lender, a margin of at least 10 percent of the term debt payments is essential for an applicant to have reasonable prospects for success. See the definition of positive cash flow contained in § 762.102, which is required in § 762.150(b)(4)(i) for interest assistance on new guaranteed loans. However, it also agrees that withdrawing or prohibiting subsidy in cases where the Agency already has exposure only increases that exposure and is not consistent with program objectives. The Agency partially adopted this recommendation by deleting the requirement for a margin on continuation requests or existing loans. See § 762.150(b)(5)(i).

The interim rule provides for the level of need for subsidy to be based upon a projected cash flow. One comment suggested that a second needs test should be calculated at the end of the claim period based on the borrower's actual performance, to determine the level of subsidy to be paid. In order for the borrower and lender to make sound business decisions, they must be able to project the effective interest rate for the next plan period. Since this recommendation would reduce the ability to plan, the Agency is not adopting it.

One respondent requested clarification on the method of performing the needs test on multiple loans. This clarification has been provided in the Agency handbook and lender manual.

One comment suggested that the definition of ''positive cash flow'' be added. An explanation of positive cash flow has been added in § 762.102.

Two respondents requested guidance on accounting for the subsidy portion of the interest payment. This is a management decision to be made by each individual lender and should not be dictated by the Agency. Therefore, no change is made.

One respondent requested clarification as to whether ''other debt'' is to be considered for restructuring before interest assistance is to be considered. This is not a requirement but an option under the interim rule. No change is being made.

Many of the respondents who sent similar letters, recommended that the Agency not cancel interest assistance due to a court ordered reduction in the interest rate. Such a policy could result in having to process two claims. For administrative simplicity, the Agency prefers that the lender request the interest reduction through the loss claim process rather than through an interest assistance claim. The interest assistance agreement is changed to clarify this point. The interest assistance agreement will also be revised for administrative simplicity, to say that interest assistance will be canceled when a debt write down is approved.

One comment requested clarification that lenders can reduce their interest rate voluntarily in conjunction with interest assistance. This has always been the policy and clarification is added to § 762.150(b)(7).

One comment feels that the proposed rule contains more stringent rules and will hinder the ability of Agency direct loan customers to graduate to guaranteed loans. The Agency feels that the new program is less stringent and should be more appealing as several of the changes being made with this final rule will be more beneficial to the loan applicant and lender. Examples of these changes include a simplified claim process, Agency timeframes to process claims, reduced margin requirements for servicing, and elimination of .25 percent increments.

One respondent commented that the Agency does not seem to trust the commercial lender in implementing the interest assistance program. The regulations of this program reflect a balance of internal controls to protect the Government's interest, with a workable program to benefit the borrower and to appeal to lenders. No change will be made.

One comment suggested that mid-year adjustments of the subsidy level should be available. Such an adjustment would not be significant to either the lender or the borrower, especially since elimination of the .25 percent increments, and would add to the administrative time required of all parties. No change is made.

Thirty-four comments recommended limiting a borrower's effective interest rate to a level no lower than the limited resource rate for the same loan type. The limited resource rate is the lowest rate charged for Agency direct loans. However, the standards for the guaranteed program do not correlate with the direct loans program. Such a limitation would be administratively burdensome to the lender and would complicate the program. Therefore, the Agency is not adopting this recommendation.

Seventy-nine respondents, requested that the Agency adopt a policy that no guarantee fee will be charged for loans in which a majority of the funds are used to refinance Agency loans. This would encourage graduation of borrowers from the direct loan program to the guaranteed loan program. The Agency implemented this recommendation without publication in 1993 and in § 762.130(d)(4).

Eighty-three comments, stated the amount of paperwork and preparation time involved with the interest assistance application process will prove too difficult and costly for borrowers and banks and will decrease participation in the program. No specific changes were recommended. Every effort has been made to minimize paperwork, while protecting the interest of the Government and meeting statutory requirements. Many changes that are being made in this rule will reduce the paperwork associated with interest assistance loans. Examples include a much less complex claims process, simplified needs test, and elimination of an amortization schedule for loans with equal payments. The Agency will continue to accept comments on specific changes which will result in a burden reduction.

Twenty-two comments requested that consideration be given to an Agency developed software program that would complete forms associated with interest assistance. Development of software for public use is outside the scope of the Agency's current focus. Commitment of time necessary for development, service and maintenance of such software would reduce the effectiveness of the Agency's other loan programs and the software is available commercially. The Agency will not adopt this recommendation at this time.

One comment suggested that an amortization table beyond the initial 24 months is not useful in analyzing the request. For loans with unequal payments, this schedule is necessary to evaluate the long-term viability of the plan. Since it is not essential for loans with equally amortized installments, the Agency is changing the requirement to exclude loans with equal payments from the amortization table.

Four comments recommended allowing lenders to cancel interest rate buy down (IRBD) and have the interest rate revert back to the rate in effect before IRBD. This recommendation cannot be adopted because it would result in windfall gains to lenders while offering no benefit to the borrower or the Agency.

One comment recommended that a provision be made for the Agency to cancel interest assistance if borrowers do not adhere to their plan. While this would be prudent lending, it is nearly impossible to monitor and enforce such a requirement and would be primarily subjective. If borrowers do not adhere to the plan, the appropriate remedy is liquidation. The change will not be adopted.

Various comments concerning forms were received; as a result, the forms were redesigned for clarity.

Justification for Effective Date

Good cause is shown for an immediate effective date because of the need to accelerate the availability of assistance under this program. Numerous natural disasters throughout the country have reduced farm production and widespread reductions in commodity prices have lowered income which has resulted in deteriorating financial conditions for many producers. As a result of those deteriorating financial conditions, we anticipate an increased demand for guaranteed farm loans. These streamlining regulations will enable the Agency to serve the needs of the financially stressed farmers and lenders more quickly and efficiently; therefore an immediate implementation is justified.

List of Subjects

7 CFR Part 762

Agriculture, Loan programs—Agriculture.

7 CFR Part 1980

Agriculture, Loan programs—Agriculture.

The Farm Service Agency adopts the proposed rule published September 25, 1998, in the **Federal Register** [63 FR 51458–51488] and also adopts its interim rule published February 28, 1991, in the **Federal Register** [56 FR 8258–8272] with changes based upon comments received. Accordingly, 7 CFR chapters VII and XVIII are amended as follows:

7 CFR Chapter VII

1. Part 762 is added to read as follows:

PART 762—GUARANTEED FARM LOANS

Sec.

Authority: 5 U.S.C. 301; 7 U.S.C. 1989; 42 U.S.C. 1480.

PART 762—GUARANTEED FARM LOANS

§§ 762.1–762.100 [Reserved].

§ 762.101 Introduction.

(a) *Scope.* This subpart contains regulations governing Operating Loans and Farm Ownership loans guaranteed by the Farm Service Agency. This subpart applies to lenders, holders, borrowers, Agency personnel, and other parties involved in making, guaranteeing, holding, servicing, or liquidating such loans.

(b) *Policy.* The Agency issues guarantees on loans made to qualified loan applicants without regard to race, color, religion, sex, national origin, marital status, or age, provided the loan applicant can enter into a legal and binding contract, or whether all or part of the applicant's income derives from any public assistance program or whether the applicant, in good faith, exercises any rights under the Consumer Protection Act.

(c) *Lender list and classification.*

(1) The Agency maintains a current list of lenders who express a desire to participate in the guaranteed loan program. This list is made available to farmers upon request.

(2) Lenders who participate in the Agency guaranteed loan program will be classified into one of the following categories:

(i) Standard Eligible Lender under § 762.105,

(ii) Certified Lender, or

(iii) Preferred Lender under § 762.106.

(3) Lenders may continue to make loans under Approved Lender Program (ALP) agreements until they expire; however, these agreements will not be renewed when they expire. All ALP agreements with farm credit institutions will expire on February 12, 2001.

(d) *Type of guarantee.* Guarantees are available for both a loan note or a line of credit. A loan note is used for a loan of fixed amount and term. A line of credit has a fixed term, but no fixed amount. The principal amount outstanding at any time, however, may not exceed the line of credit ceiling contained in the contract. Both guarantees are evidenced by the same loan guarantee form.

(e) *Termination of loan guarantee.* The loan guarantee will automatically terminate as follows:

(1) Upon full payment of the guaranteed loan. A zero balance within the period authorized for advances on a line of credit will not terminate the guarantee;

(2) Upon payment of a final loss claim; or

(3) Upon written notice from the lender to the Agency that a guarantee is no longer desired provided the lender holds all of the guaranteed portion of the loan. The loan guarantee will be returned to the Agency office for cancellation within 30 days of the date of the notice by the lender.

§ 762.102 Abbreviations and definitions.

(a) *Abbreviations.*

ALP—Approved lender program
CLP—Certified lender program
CONACT—Consolidated Farm and Rural Development Act (7 U.S.C. 1921 et seq.)
EPA—Environmental Protection Agency
EIS—Environmental impact statement
EM—Emergency loans
FO—Farm ownership loans
FSA—Farm Service Agency
OL—Operating loans
PLP—Preferred lender program
SW—Soil and water
USDA—United States Department of Agriculture

(b) *Definitions.*

Additional security. Collateral in excess of that needed to fully secure the loan.

Agency. The Farm Service Agency, including its employees and state and area committee members, and any successor agency.

Allonge. An attachment or an addendum to a note.

Applicant. For guaranteed loans, the lender requesting a guarantee is the applicant. The party applying to the lender for a loan will be considered the loan applicant.

Aquaculture. The husbandry of aquatic organisms in a controlled or selected environment. An aquatic organism is any fish, amphibian, reptile, or aquatic plant. An aquaculture operation is considered to be a farm only if it is conducted on the grounds which the loan applicant owns, leases, or has an exclusive right to use. An exclusive right to use must be evidenced by a permit issued to the loan applicant and the permit must specifically identify the waters available to be used by the loan applicant only.

Assignment of guaranteed portion. A process by which the lender transfers the right to receive payments or income on the guaranteed loan to another party, usually in return for payment in the amount of the loan's guaranteed principal. The lender retains the unguaranteed portion in its portfolio and receives a fee from the purchaser or assignee to service the loan, and receive and remit payments according to a written assignment agreement. This assignment can be reassigned or sold multiple times.

Average farm customers. Those conventional farm borrowers who are required to pledge their crops, livestock, and other chattel and real estate security for the loan. This does not include those high-risk farmers with limited security and management ability who are generally charged a higher interest rate by conventional agricultural lenders. Also, this does not include those low-risk farm customers who obtain financing on a secured or unsecured basis, who have as collateral such items as savings accounts, time deposits, certificates of deposit, stocks and bonds, and life insurance, which they are able to pledge for the loan.

Basic Security. All farm machinery, equipment, vehicles, foundation and breeding livestock herds and flocks, including replacements, and real estate which serves as security for a loan guaranteed by the Agency.

Beginning farmer or rancher. A beginning farmer or rancher is an individual or entity who:

(1) Meets the loan eligibility requirements for OL or FO assistance, as applicable, in accordance with this subpart;

(2) Has not operated a farm or ranch, or who has operated a farm or ranch for not more than 10 years. This requirement applies to all members of an entity;

(3) Will materially and substantially participate in the operation of the farm or ranch:

(i) In the case of a loan made to an individual, individually or with the immediate family, material and substantial participation requires that the individual provide substantial day-to-day labor and management of the farm or ranch, consistent with the practices in the county or State where the farm is located.

(ii) In the case of a loan made to an entity, all members must materially and substantially participate in the operation of the farm or ranch. Material and substantial participation requires that the individual provide some amount of the management, or labor and management necessary for day-to-day activities, such that if the individual did not provide these inputs, operation of the farm or ranch would be seriously impaired;

(4) Agrees to participate in any loan assessment and financial management programs required by Agency regulations;

(5) Does not own real farm or ranch property or who, directly or through interests in family farm entities owns real farm or ranch property, the aggregate acreage of which does not exceed 25 percent of the average farm or ranch acreage of the farms or ranches in the county where the property is located. If the farm is located in more than one county, the average farm acreage of the county where the loan applicant's residence is located will be used in the calculation. If the applicant's residence is not located on the farm or if the loan applicant is an entity, the average farm acreage of the county where the major portion of the farm is located will be used. The average county farm or ranch acreage will be determined from the most recent Census of Agriculture developed by the U.S. Department of Commerce, Bureau of the Census or USDA;

(6) Demonstrates that the available resources of the loan applicant and spouse (if any) are not sufficient to enable the loan applicant to enter or continue farming or ranching on a viable scale; and

(7) In the case of an entity:

(i) All the members are related by blood or marriage; and

(ii) All the stockholders in a corporation are beginning farmers or ranchers.

Borrower. An individual or entity which has outstanding obligations to the lender under any Agency loan or loan guarantee program. A borrower includes all parties liable for Agency debt, including collection-only borrowers, except those whose total loan and accounts have been voluntarily or involuntarily foreclosed or liquidated, or who have been discharged of all Agency debt.

Capital leases. Agreements under which the lessee effectively acquires ownership of the asset being leased. A lease is a capital lease if it meets any one of the following criteria:

(1) The lease transfers ownership of the property to the lessee at the end of the lease term.

(2) The lessee has the right to purchase the property for significantly less than its market value at the end of the lease.

(3) The term of the lease is at least 75 percent of the estimated economic life of the leased property.

(4) The present value of the minimum lease payments equals or exceeds 90 percent of the fair market value of the leased property.

Cash flow budget. A projection listing all anticipated cash inflows (including all farm income, nonfarm income and all loan advances) and all cash outflows (including all farm and nonfarm debt service and other expenses) to be incurred by the borrower during the period of the budget. Cash flow budgets for loans under $50,000 do not require income and expenses itemized by categories. A cash flow budget may be completed either for a 12 month period, a typical production cycle or the life of the loan, as appropriate. It may also be prepared with a breakdown of cash inflows and outflows for each month of the review period and includes the expected outstanding operating credit balance for the end of each month. The latter type is referred to as a ''monthly cash flow budget''.

Collateral. Property pledged as security for a loan to ensure repayment of an obligation.

Conditional commitment. The Agency's commitment to the lender that the material it has submitted is approved subject to the completion of all conditions and requirements contained therein.

Consolidation. The combination of outstanding principal and interest balance of two or more OL loans.

Controlled. When a director or employee has more than a 50 percent ownership in the entity or, the director or employee, together with relatives of the director or employee, have more than a 50 percent ownership.

Cooperative. An entity which has farming as its purpose and whose members have agreed to share the profits of the farming enterprise. The entity must be recognized as a farm cooperative by the laws of the State in which the entity will operate a farm.

Cosigner. A party who joins in the execution of a promissory note to assure its repayment. The cosigner becomes jointly and severally liable to comply with the terms of the note. In the case of an entity applicant, the cosigner cannot be a member, partner, joint operator, or stockholder of the entity.

County average yield. The historical average yield for a commodity in a particular political subdivision, as determined or published by a government entity or other recognized source.

Debt writedown. To reduce the amount of the borrower's debt to that amount that is determined to be collectible based on an analysis of the security value and the borrower's ability to pay.

Deferral. A postponement of the payment of interest or principal or both. Principal may be deferred in whole or in part, interest may only be partially deferred.

Depreciation and amortization expenses. An annual allocation of the cost or other basic value of tangible capital assets, less salvage value, over the estimated life of the unit (which may be a group of assets), in a systematic and rational manner.

Direct loan. A loan serviced by the Agency as lender.

Entity. Cooperatives, corporations, partnerships, or joint operations.

Family farm. A farm which:

(1) Produces agricultural commodities for sale in sufficient quantities so that it is recognized in the community as a farm rather than a rural residence;

(2) Provides enough agricultural income by itself, including rented land, or together with any other dependable income to enable the borrower to:

(i) Pay necessary family living and operating expenses;

(ii) Maintain essential chattel and real property; and

(iii) Pay debts;

(3) Is managed by:

(i) The borrower when a loan is made to an individual; or,

(ii) The members, stockholders, partners, or joint operators responsible for operating the farm when a loan is made to an entity;

(4) Has a substantial amount of the labor requirement for the farm and nonfarm enterprise provided by:

(i) The borrower and the borrower's immediate family for a loan made to an individual; or

(ii) The members, stockholders, partners, or joint operators responsible for operating the farm, along with the families of these individuals, for a loan made to an entity; and

(5) May use a reasonable amount of full-time hired labor and seasonal labor during peak load periods.

Family living expenses. Any withdrawals from income to provide for needs of family members.

Family members. The immediate members of the family residing in the same household with the individual borrower, or, in the case of an entity, with the operator.

Farm. A tract or tracts of land, improvements, and other appurtenances which are used or will be used in the production of crops, livestock, or aquaculture products for sale in sufficient quantities so that the property is recognized as a farm rather than a rural residence. The term ''farm'' also includes any such land and improvements and facilities used in a nonfarm enterprise. It may also include the residence which, although physically separate from the farm acreage, is ordinarily treated as part of the farm in the local community.

Feasible plan. A plan for loan servicing purposes which shows the elements of ''positive cash flow'' except that the minimum acceptable ''Term Debt and Capital Lease Coverage Ratio'' is 1.0 rather than 1.1 required for ''positive cash flow.''

Financially viable operation. An operation which, with Agency assistance, is projected to improve its financial condition over a period of time to the point that the operator can obtain commercial credit without further Agency direct or guaranteed assistance. A borrower that will meet the Agency classification of ''commercial,'' as defined in Agency Instruction 2006–W, available in any Agency office, will be considered to be financially viable. Such an operation must generate sufficient income to:

(1) Meet annual operating expenses and debt payments as they become due;

(2) Meet basic family living expenses to the extent they are not met by dependable nonfarm income;

(3) Provide for replacement of capital items; and

(4) Provide for long-term financial growth.

Fish. Any aquatic, gilled animal commonly known as ''fish'' as well as mollusks, or crustaceans (or other invertebrates) produced under controlled conditions (that is, feeding, tending, harvesting, and such other activities as are necessary to properly raise and market the products) in ponds, lakes, streams, artificial enclosures, or similar holding areas.

Fixture. An item of personal property attached to real estate in such a way that it cannot be removed without defacing or dismantling the structure, or substantially damaging the structure itself.

Graduation. The Agency's determination that a borrower of a direct loan, is financially stable enough to refinance that loan with a commercial lender with or without a guarantee.

Guaranteed loan. A loan made and serviced by a lender for which the Agency has entered into a lenders agreement and for which the Agency has issued a loan note guarantee. This term also includes lines of credit except where otherwise indicated.

Hazard insurance. Includes fire, windstorm, lightning, hail, explosion, riot, civil commotion, aircraft, vehicles, smoke, builder's risk, public liability, property damage, flood or mudslide, workers compensation, or any similar insurance that is available and needed to protect the security, or that is required by law.

Holder. The person or organization other than the lender who holds all or a part of the guaranteed portion of an Agency guaranteed loan but who has no servicing responsibilities. When the lender assigns a part of the guaranteed loan to an assignee by way of execution of an assignment form, the assignee becomes a holder.

In-house expenses. Expenses associated with credit management and loan servicing by the lender and the lender's contractor. In-house expenses include, but are not limited to: employee salaries, staff lawyers, travel, supplies, and overhead.

Interest assistance agreement. The signed agreement between the Agency and the lender setting forth the terms and conditions of the interest assistance.

Interest assistance anniversary date. Date on which interest assistance reviews and claims will be effective. This date is established by the lender. Once established, it will not change unless the loan is restructured.

Interest assistance review. The yearly review process which includes an analysis of the borrower or applicant's farming operation and need for continued interest assistance, completion of the needs test and request for continuation of interest assistance.

Joint operation. Individuals that have agreed to operate a farm or farms together as a business unit. The real and personal property is owned separately or jointly by the individuals. Joint operations include limited liability companies having more than one member.

Land development. Items such as terracing, clearing, leveling, fencing, drainage and irrigation systems, ponds, forestation, permanent pastures, perennial hay crops, basic soil amendments, and other items of land improvements which conserve or permanently enhance productivity.

Lender. The organization making and servicing the loan or advancing and servicing the line of credit which is guaranteed under the provisions of

Agency regulations. The lender is also the party requesting a guarantee.

Lender's agreement. The appropriate Agency form executed by the Agency and the lender setting forth the loan responsibilities of the lender and agency when the loan guarantee is issued.

Lien. A legally enforceable hold or claim on the property of another obtained as security for the repayment of indebtedness or an encumbrance on property to enforce payment of an obligation.

Liquidation expenses. The cost of an appraisal, due diligence evaluation, environmental assessment, outside attorney fees and other costs incurred as a direct result of liquidating the security for the guaranteed loan. Liquidation fees do not include in-house expenses.

Loan or line of credit agreement. A document which contains certain lender and borrower agreements, conditions, limitations, and responsibilities for credit extension and acceptance in a loan format where loan principal balance may fluctuate throughout the term of the document.

Loan applicant. The party applying to a lender for a guaranteed loan or line of credit.

Loan transaction. Any loan approval or servicing action.

Loss claim. A request made to the Agency by a lender to receive a reimbursement based on a percentage of the lender's loss on a loan covered by an Agency guarantee.

Loss rate. The net amount of guaranteed OL, FO, and SW loss claims paid on loans made in the past 7 years divided by the total loan amount of OL, FO, and SW made in the past 7 years.

Major deficiency. A deficiency that directly affects the soundness of the loan.

Majority interest. Any individual or a combination of individuals owning more than a 50 percent interest in a cooperative, corporation, joint operation, or partnership.

Market value. The amount which an informed and willing buyer would pay an informed and willing, but not forced, seller in a completely voluntary sale.

Minor deficiency. A deficiency that violates Agency regulations, but does not affect the soundness of a loan.

Mortgage. A legal instrument giving the lender a security interest or lien on real or personal property of any kind.

Negligent servicing. The failure to perform those services which would be considered normal industry standards of loan management or failure to comply with any servicing requirement of this subpart or the lenders agreement or the guarantee. The term includes the concept of a failure to act or failure to act timely consistent with actions of a reasonable lender in loan making, servicing, and collection.

Net farm operating income. The gross income generated by a farming operation annually, minus all yearly operating expenses (including withdrawals from entities for living expenses), operating loan interest, interest on term debt and capital lease payments, and depreciation and amortization expenses. Net farm operating income does not include off-farm income and social security taxes, carryover debt and delinquent interest.

Net recovery value. The market value of the security property assuming that it will be acquired by the lender, and sold for its highest and best use, less the lender's costs of property acquisition, retention, maintenance, and liquidation.

Nonessential asset. Assets in which the borrower has an ownership interest that do not contribute an income to pay essential family living expenses or maintain a sound farming operation, and are not exempt from judgment creditors.

Normal income security. All security not considered basic security.

Participation. A loan arrangement where a primary or lead lender is typically the lender of record but the loan funds may be provided by one or more other lenders due to loan size or other factors. Typically, participating lenders share in the interest income or profit on the loan based on the relative amount of the loan funds provided after deducting the servicing fees of the primary or lead lender.

Partnership. Any entity consisting of two or more individuals who have agreed to operate a farm as one business unit. The entity must be recognized as a partnership by the laws of the State in which the entity will operate and must be authorized to own both real estate and personal property and to incur debts in its own name.

Positive cash flow. The ability of a borrower's operation to demonstrate: a term debt and capital lease coverage ratio of at least 1.1; and a capital replacement and term debt repayment margin equal to or greater than any planned capital asset purchases not financed. The term debt and capital lease coverage ratio and the capital replacement and term debt repayment margin are calculated as follows:

(1) Add projected net farm operating income, projected annual nonfarm income, projected capital depreciation and amortization expenses, scheduled annual interest on term debt, and scheduled annual interest on capital leases.

(2) Subtract from this sum projected annual income and social security tax payments, including any delinquent taxes, and family living expenses. The difference is the balance available for term debt repayment.

(3) Divide the balance available for term debt repayment by the sum of the annual scheduled principal and interest payments on term debt, plus the annual scheduled principal and interest payments on capital leases, excluding delinquent installments. The quotient is the term debt and capital lease coverage ratio.

(4) Add the balance available for term debt repayment to any cash carryover from the preceding year.

(5) Subtract from this sum the amount of the total annual scheduled term debt and capital lease payments, and any debt carried over from the previous year. The difference is the capital replacement and term debt repayment margin.

Potential liquidation value. The amount of the lender's protective bid at the foreclosure sale. Potential liquidation value is determined by an independent appraiser using comparables from other forced liquidation sales.

Present value. The present worth of a future stream of payments discounted to the current date.

Primary security. The minimum amount of collateral needed to fully secure a proposed loan.

Principals of borrowers. Includes owners, officers, directors, entities and others directly involved in the operation and management of a business.

Protective advances. Advances made by a lender to protect or preserve the collateral itself from loss or deterioration. Protective advances include but are not limited to:

(1) Payment of delinquent taxes,

(2) Annual assessments,

(3) Ground rents,

(4) Hazard or flood insurance premiums against or affecting the collateral,

(5) Harvesting costs,

(6) Other expenses needed for emergency measures to protect the collateral.

Recapture. The amount that a guaranteed lender is entitled to recover from a guaranteed loan borrower in consideration for the lender writing down a portion of their guaranteed loan debt when that loan was secured by real estate and that real estate increases in value. Also, the act of collecting shared appreciation.

Related by blood or marriage. Individuals who are connected to one another as husband, wife, parent, child, brother, or sister.

Relative. An individual or spouse and anyone having the following relationship to either: parent, son, daughter, sibling, stepparent, stepson, stepdaughter, stepbrother, stepsister, half brother, half sister, uncle, aunt, nephew, niece, grandparent, granddaughter, grandson, and the spouses of the foregoing.

Rescheduling. To rewrite the rates and terms of a single note or line of credit agreement.

Restructuring. Changing terms of a debt through either a rescheduling, deferral, or writedown or a combination thereof.

Sale of guaranteed portion. See assignment of guaranteed portion.

Security. Property of any kind subject to a real or personal property lien. Any reference to ''collateral'' or ''security property'' shall be considered a reference to the term ''security.''

Shared appreciation agreement. An agreement between a guaranteed lender and borrower that requires a borrower that has received a write down on a guaranteed loan secured by real estate to repay the lender some or all of the writedown received, based on a percentage of any increase in the value of that real estate at some future date, if certain conditions exist.

State. The major political subdivision of the United States and the organization of program delivery for the Agency.

Subordination. A document executed by a lender to relinquish their priority of lien in favor of another lender that provides the other lender with a priority right to collect a debt of a specific dollar amount from the sale of the same collateral.

Subsequent loans. Any loans processed by the Agency after an initial loan has been made to the same borrower.

Transfer and assumption. The conveyance by a debtor to an assuming party of the assets, collateral, and liabilities of the loan in return for the assuming party's binding promise to pay the debt outstanding.

Typical plan. A projected income and expense statement listing all anticipated cash flows for a typical 12-month production cycle; including all farm and nonfarm income and all expenses (including debt service) to be incurred by the borrower during such period.

Unaccounted for security. Items, as indicated on the lender's loan application, request for guarantee, or any interim agreements provided to the Agency, that are security for the guaranteed loan that were misplaced, stolen, sold, or otherwise missing, where replacement security was not obtained or the proceeds from their sale have not been applied to the loan.

United States. The United States itself, each of the several States, the Commonwealth of Puerto Rico, the Virgin Islands of the United States, Guam, American Samoa, and the Commonwealth of the Northern Mariana Islands.

Veteran. Any person who served in the military, naval, or air service during any war as defined in section 101(12) of title 38, United States Code.

§ 762.103 Full faith and credit.

(a) *Fraud and misrepresentation.* The loan guarantee constitutes an obligation supported by the full faith and credit of the United States. The Agency may contest the guarantee only in cases of fraud or misrepresentation by a lender or holder, in which:

(1) The lender or holder had actual knowledge of the fraud or misrepresentation at the time it became the lender or holder, or

(2) The lender or holder participated in or condoned the fraud or misrepresentation.

(b) *Lender violations.* The loan guarantee cannot be enforced by the lender, regardless of when the Agency discovers the violation, to the extent that the loss is a result of:

(1) Violation of usury laws;

(2) Negligent servicing;

(3) Failure to obtain the required security; or,

(4) Failure to use loan funds for purposes specifically approved by the Agency.

(c) *Enforcement by holder.* The guarantee and right to require purchase will be directly enforceable by the holder even if:

(1) The loan guarantee is contestable based on the lender's fraud or misrepresentation; or

(2) The loan note guarantee is unenforceable by the lender based on a lender violation.

§ 762.104 Appeals.

(a) The loan applicant or borrower and lender must jointly execute the written request for review of an alleged adverse decision made by the Agency. However, in cases where the Agency has denied or reduced the amount of the final loss payment, the decision may be appealed by the lender only.

(b) A decision made by the lender adverse to the borrower is not a decision by the Agency, whether or not concurred in by the Agency, and may not be appealed.

(c) The lender or Agency may request updated information from the borrower to implement an appeal decision.

(d) Appeals will be handled in accordance with parts 11 and 780 of this title.

§ 762.105 Eligibility and substitution of lenders.

(a) *General.* To participate in FSA guaranteed farm loan programs, a lender must meet the eligibility criteria in this part. The standard eligible lender must demonstrate eligibility and provide such evidence as the Agency may request.

(b) *Standard eligible lender eligibility criteria.*

(1) A lender must have experience in making and servicing agricultural loans and have the capability to make and service the loan for which a guarantee is requested;

(2) The lenders must not have losses or deficiencies in processing and servicing guaranteed loans above a level which would indicate an inability to properly process and service a guaranteed agricultural loan.

(3) A lender must be subject to credit examination and supervision by an acceptable State or Federal regulatory agency;

(4) The lender must maintain an office near enough to the collateral's location so it can properly and efficiently discharge its loan making and loan servicing responsibilities or use Agency approved agents, correspondents, branches, or other institutions or persons to provide expertise to assist in carrying out its responsibilities. The lender must be a local lender unless it:

(i) normally makes loans in the region or geographic location in which the loan applicant's operation being financed is located, or

(ii) demonstrates specific expertise in making and servicing loans for the proposed operation.

(5) The lender, its officers, or agents must not be debarred or suspended from participation in Government contracts or programs or be delinquent on a Government debt.

(c) *Substitution of lenders.* A new eligible lender may be substituted for the original lender, upon the original lender's concurrence, under the following conditions:

(1) The Agency approves of the substitution in writing;

(2) The new lender agrees in writing to:

(i) Assume all servicing and other responsibilities of the original lender and to acquire the unguaranteed portion of the loan;

(ii) Execute a lender's agreement if one is not in effect;

(iii) Execute a modification of the guarantee provided by the Agency to identify the new lender, and contain the amount of debt at the time of the substitution and the new loan terms if applicable; and,

(iv) Give any holder written notice of the substitution. If the rate and terms are changed, written concurrence from the holder is required.

(3) The original lender will:

(i) Assign their promissory note, lien instruments, loan agreements, and other documents to the new lender.

(ii) If the loan is subject to an existing interest assistance agreement, submit a request for subsidy for the partial year that it has owned the loan.

(d) *Lender name or ownership changes.*

(1) When a lender begins doing business under a new name or undergoes an ownership change the lender will notify the Agency.

(2) The lender's CLP or PLP status is subject to reconsideration when ownership changes.

(3) The lender will execute a new lender's agreement when ownership changes.

§ 762.106 Preferred and certified lender programs.

(a) *General.*

(1) Lenders who desire PLP or CLP status must prepare a written request addressing:

(i) The States in which they desire to receive PLP or CLP status and their branch offices which they desire to be considered by the Agency for approval; and

(ii) Each item of the eligibility criteria for PLP or CLP approval in this section, as appropriate.

(2) The lender may include any additional supporting evidence or other information the lender believes would be helpful to the Agency in making its determination.

(3) The lender must send its request to the Agency State office for the State in which the lender's headquarters is located.

(4) The lender must provide any additional information requested by the Agency to process a PLP or CLP request if the lender continues with the approval process.

(b) *CLP criteria.* The lender must meet the following requirements to obtain CLP status:

(1) Qualify as a standard eligible lender under § 762.105;

(2) Have a lender loss rate not in excess of the maximum CLP loss rate established by the Agency and published periodically in a **Federal Register** Notice. The Agency may waive the loss rate criteria for those lenders whose loss rate was substantially affected by a disaster as defined in part 1945, subpart A, of this title.

(3) Have proven an ability to process and service Agency guaranteed loans by showing that the lender:

(i) Submitted substantially complete and correct guaranteed loan applications; and

(ii) Serviced all guaranteed loans according to Agency regulations;

(4) Have made the minimum number of guaranteed OL, FO, or Soil and Water (SW) loans established by the Agency and published periodically in a **Federal Register** Notice.

(5) Not be under any regulatory enforcement action such as a cease and desist order, written agreement, or an appointment of conservator or receiver, based upon financial condition;

(6) Designate a qualified person or persons to process and service Agency guaranteed loans for each of the lender offices which will process CLP loans. To be qualified, the person must meet the following conditions:

(i) Have attended Agency sponsored training in the past 12 months or will attend training in the next 12 months; and

(ii) Agree to attend Agency sponsored training each year;

(7) Use forms acceptable to the Agency for processing, analyzing, securing, and servicing Agency guaranteed loans and lines of credit;

(8) Submit to the Agency copies of financial statements, cash flow plans, budgets, promissory notes, analysis sheets, collateral control sheets, security agreements and other forms to be used for farm loan processing and servicing;

(c) *PLP criteria.* The lender must meet the following requirements to obtain PLP status:

(1) Meet the CLP eligibility criteria under this section.

(2) Have a credit management system, satisfactory to the Agency, based on the following:

(i) The lender's written credit policies and underwriting standards;

(ii) Loan documentation requirements;

(iii) Exceptions to policies;

(iv) Analysis of new loan requests;

(v) Credit file management;

(vi) Loan funds and collateral management system;

(vii) Portfolio management;

(viii) Loan reviews;

(ix) Internal credit review process;

(x) Loan monitoring system; and

(xi) The board of director's responsibilities.

(3) Have made the minimum number of guaranteed OL, FO, or SW loans established by the Agency and published periodically in a **Federal Register** Notice.

(4) Have a lender loss rate not in excess of the rate of the maximum PLP loss rate established by the Agency and published periodically in a **Federal Register** Notice. The Agency may waive the loss rate criteria for those lenders whose loss rate was substantially affected by a disaster as defined in part 1945, subpart A, of this title.

(5) Show a consistent practice of submitting applications for guaranteed loans containing accurate information supporting a sound loan proposal.

(6) Show a consistent practice of processing Agency guaranteed loans without recurring major or minor deficiencies.

(7) Demonstrate a consistent, above average ability to service guaranteed loans based on the following:

(i) Borrower supervision and assistance;

(ii) Timely and effective servicing; and

(iii) Communication with the Agency.

(8) Designate a person or persons, approved by the Agency, to process and service PLP loans for the Agency.

(d) *CLP and PLP approval.*

(1) If a lender applying for CLP or PLP status is or has recently been involved in a merger or acquisition, all loans and losses attributed to both lenders will be considered in the eligibility calculations.

(2) The Agency will determine which branches of the lender have the necessary experience and ability to participate in the CLP or PLP program based on the information submitted in the lender application and on Agency experience.

(3) Lenders who meet the criteria will be granted CLP or PLP status for a period not to exceed 5 years.

(4) PLP status will be conditioned on the lender carrying out its credit management system as proposed in its request for PLP status and any additional loan making or servicing requirements agreed to and documented the PLP lender's agreement. If the PLP lender's agreement does not specify any agreed upon process for a particular action, the PLP lender will act according to regulations governing CLP lenders.

(e) *Monitoring CLP and PLP lenders.* CLP and PLP lenders will provide information and access to records upon Agency request to permit the Agency to audit the lender for compliance with these regulations.

(f) *Renewal of CLP or PLP status.*

(1) PLP or CLP status will expire within a period not to exceed 5 years from the date the lender's agreement is executed, unless a new lender's Agreement is executed.

(2) Renewal of PLP or CLP status is not automatic. A lender must submit a written request for renewal of a lender's

agreement with PLP or CLP status which includes information:

(i) Updating the material submitted in the initial application; and,

(ii) Addressing any new criteria established by the Agency since the initial application.

(3) PLP or CLP status will be renewed if the applicable eligibility criteria under this section are met, and no cause exists for denying renewal under paragraph (g) of this section.

(g) *Revocation of PLP or CLP status.*

(1) The Agency may revoke the lender's PLP or CLP status at any time during the 5 year term for cause.

(2) Any of the following instances constitute cause for revoking or not renewing PLP or CLP status:

(i) Violation of the terms of the lender's agreement;

(ii) Failure to maintain PLP or CLP eligibility criteria;

(iii) Knowingly submitting false or misleading information to the Agency;

(iv) Basing a request on information known to be false;

(v) Deficiencies that indicate an inability to process or service Agency guaranteed farm loan programs loans in accordance with this subpart;

(vi) Failure to correct cited deficiencies in loan documents upon notification by the Agency;

(vii) Failure to submit status reports in a timely manner;

(viii) Failure to use forms, or follow credit management systems (for PLP lenders) accepted by the Agency; or

(ix) Failure to comply with the reimbursement requirements of § 762.146(c)(7).

(3) A lender which has lost PLP or CLP status must be reconsidered for eligibility to continue as a Standard Eligible Lender (for former PLP and CLP lenders), or as a CLP lender (for former PLP lenders) in submitting loan guarantee requests. They may reapply for CLP or PLP status when the problem causing them to lose their status has been resolved.

§§ 762.107–762.109 [Reserved]

§ 762.110 Loan Application.

(a) *Loans for $50,000 or less.* All lenders except PLP lenders will submit the following items:

(1) A complete application for loans of $50,000 or less must, at least, consist of:

(i) The application form;

(ii) Loan narrative;

(iii) Balance sheet;

(iv) Cash flow budget;

(v) Credit report;

(vi) A plan for servicing the loan.

(2) In addition to the minimum requirements, the lender will perform at least the same level of evaluation and documentation for a guaranteed loan that the lender typically performs for non-guaranteed loans of a similar type and amount.

(3) The $50,000 threshold includes any single loan, or package of loans submitted for consideration at any one time. A lender must not split a loan into two or more parts to meet the threshold thereby avoiding additional documentation.

(4) The Agency may require lenders with a lender loss rate in excess of the rate for CLP lenders to assemble additional documentation from paragraph (b) of this section.

(b) *Loans over $50,000.* A complete application for loans over $50,000 will consist of the items required in paragraph (a) of this section plus the following:

(1) Verification of income;

(2) Verification of debts over $1,000;

(3) Three years financial history;

(4) Three years of production history (for standard eligible lenders only);

(5) Proposed loan agreements; and,

(6) If construction or development is planned, a copy of the plans, specifications, and development schedule.

(c) *Applications from PLP lenders.* Notwithstanding paragraphs (a) and (b) of this section, a complete application for PLP lenders will consist of at least:

(1) An application form;

(2) A loan narrative; and

(3) Any other items agreed to during the approval of the PLP lender's status and contained in the PLP lender agreement.

(d) *Submitting applications.*

(1) All lenders must compile and maintain in their files a complete application for each guaranteed loan. See paragraphs (a), (b), and (c) of this section.

(2) The Agency will notify CLP lenders which items to submit to the Agency.

(3) PLP lenders will submit applications in accordance with their agreement with the Agency for PLP status.

(4) CLP and PLP lenders must certify that the required items, not submitted, are in their files.

(5) The Agency may request additional information from any lender or review the lender's loan file as needed to make eligibility and approval decisions.

(e) *Incomplete applications.* If the lender does not provide the information needed to complete its application by the deadline established in an Agency request for the information, the application will be considered withdrawn by the lender.

(f) *Conflict of interest.*

(1) When a lender submits the application for a guaranteed loan, the lender will inform the Agency in writing of any relationship which may cause an actual or potential conflict of interest.

(2) Relationships include:

(i) The lender or its officers, directors, principal stockholders (except stockholders in a Farm Credit System institution that have stock requirements to obtain a loan), or other principal owners having a financial interest (other than lending relationships in the normal course of business) in the loan applicant or borrower.

(ii) The loan applicant or borrower, a relative of the loan applicant or borrower, anyone residing in the household of the loan applicant or borrower, any officer, director, stockholder or other owner of the loan applicant or borrower holds any stock or other evidence of ownership in the lender.

(iii) The loan applicant or borrower, a relative of the loan applicant or borrower, or anyone residing in the household of the loan applicant or borrower is an Agency employee.

(iv) The officers, directors, principal stockholders (except stockholders in a Farm Credit System institution that have stock requirements to obtain a loan), or other principal owners of the lender have substantial business dealings (other than in the normal course of business) with the loan applicant or borrower.

(v) The lender or its officers, directors, principal stockholders, or other principal owners have substantial business dealings with an Agency employee.

(3) The lender must furnish additional information to the Agency upon request.

(4) The Agency will not approve the application until the lender develops acceptable safeguards to control any actual or potential conflicts of interest.

§§ 762.111–762.119 [Reserved]

§ 762.120 Loan applicant eligibility.

Loan applicants must meet all of the following requirements to be eligible for a guaranteed OL or a guaranteed FO:

(a) *Agency loss.* The loan applicant, and anyone who will execute the promissory note, have not caused the Agency a loss by receiving debt forgiveness on more than three occasions on or prior to April 4, 1996, or on any occasion after April 4, 1996, on all or a portion of any direct or guaranteed loan made under the authority of the CONACT by debt write-down, write-off, compromise under the provisions of section 331 of the CONACT, adjustment, reduction, charge-off, or discharge in bankruptcy or through any payment of a guaranteed loss claim under the same circumstances. Notwithstanding the preceding sentence, applicants who receive a write-down under section 353 of the CONACT, or are current on payments under a confirmed bankruptcy reorganization plan, may receive direct and guaranteed OL loans to pay annual farm and ranch operating expenses, which include family subsistence, if the applicant meets all other requirements for the loan.

(b) *Delinquent Federal debt.* The loan applicant, and anyone who will execute the promissory note, is not delinquent on any Federal debt, other than a debt under the Internal Revenue Code of 1986. (Any debt under the Internal Revenue Code of 1986 may be considered by the lender in determining cash flow and creditworthiness.)

(c) *Outstanding judgments.* The loan applicant, and anyone who will execute the promissory note, have no outstanding unpaid judgment obtained by the United States in any court. Such judgments do not include those filed as a result of action in the United States Tax Courts.

(d) *Citizenship.*

(1) The loan applicant is a citizen of the United States or an alien lawfully admitted to the United States for permanent residence under the Immigration and Nationalization Act. Indefinite parolees are not eligible. For an entity applicant, all members of an entity must meet this citizenship test.

(2) Aliens must provide the appropriate Immigration and Naturalization Service forms to document their permanent residency.

(e) *Legal capacity.* The loan applicant and all borrowers on the loan must possess the legal capacity to incur the obligations of the loan.

(f) *False or misleading information.* The loan applicant, in past dealings with the Agency, must not have provided the Agency with false or misleading documents or statements.

(g) *Credit history.*

(1) The individual or entity loan applicant and all entity members must have acceptable credit history demonstrated by debt repayment.

(2) A history of failures to repay past debts as they came due when the ability to repay was within their control will demonstrate unacceptable credit history.

(3) Unacceptable credit history will not include:

(i) Isolated instances of late payments which do not represent a pattern and were clearly beyond their control; or,

(ii) Lack of credit history.

(h) *Test for credit.*

(1) The loan applicant is unable to obtain sufficient credit elsewhere without a guarantee to finance actual needs at reasonable rates and terms.

(2) The potential for sale of any significant nonessential assets will be considered when evaluating the availability of other credit.

(3) Ownership interests in property and income received by an individual or entity loan applicant, and any entity members as individuals will be considered when evaluating the availability of other credit to the loan applicant.

(i) *For OLs:*

(1) The individual or entity loan applicant must be an operator of not larger than a family farm after the loan is closed.

(2) In the case of an entity borrower:

(i) The entity must be authorized to operate, and own if the entity is also an owner, a farm in the State or States in which the farm is located; and

(ii) If the entity members holding a majority interest are related by marriage or blood, at least one member of the entity must operate the family farm; or,

(iii) If the entity members holding a majority interest are not related by marriage or blood, the entity members holding a majority interest must also operate the family farm.

(j) *For FOs:*

(1) The individual must be the operator and owner of not larger than a family farm after the loan is closed.

(2) In the case of an entity borrower:

(i) The entity must be authorized to own and operate a farm in the state or states in which the farm is located; and

(ii) If the entity members holding a majority interest are related by marriage or blood, at least one member of the entity also must operate the family farm and at least one member of the entity or the entity must own the family farm; or,

(iii) If the entity members holding a majority interest are not related by marriage or blood, the entity members holding a majority interest must operate the family farm and the entity members holding a majority interest or the entity must own the family farm.

(k) *For entity loan applicants.* Entity loan applicants must meet the following additional eligibility criteria:

(1) Each entity member's ownership interest may not exceed the family farm definition limits;

(2) The collective ownership interest of all entity members may exceed the family farm definition limits only if the following conditions are met:

(i) All of the entity members are related by blood or marriage;

(ii) All of the members are or will be operators of the entity; and,

(iii) The majority interest holders of the entity must meet the requirements of paragraphs (d), (f), (g), and (i) through (j) of this section;

(3) The entity must be controlled by farmers or ranchers engaged primarily and directly in farming or ranching in the United States after the loan is made; and

(4) The entity members are not themselves entities.

(l) Neither the applicant nor any entity member has been convicted of planting, cultivating, growing, producing, harvesting, or storing a controlled substance under Federal or state law within the last five crop years. ''Controlled substance'' is defined at 21 CFR 1308. Applicants must certify on the application that it and its members, if an entity, have not been convicted of such a crime within the relevant period. If the lender uses the lender's Agency approved forms, the certification may be an attachment to the form.

§ 762.121 Loan purposes.

(a) *Operating Loan purposes.*

(1) Loan funds disbursed under an OL guarantee may only be used for the following purposes:

(i) Payment of costs associated with reorganizing a farm or ranch to improve its profitability;

(ii) Purchase of livestock, including poultry, and farm or ranch equipment or fixtures, quotas and bases, and cooperative stock for credit, production, processing or marketing purposes;

(iii) Payment of annual farm or ranch operating expenses, examples of which include feed, seed, fertilizer, pesticides, farm or ranch supplies, repairs and improvements which are to be expensed, cash rent and family subsistence;

(iv) Payment of scheduled principal and interest payments on term debt provided the debt is for authorized FO or OL purposes;

(v) Other farm and ranch needs;

(vi) Payment of costs associated with land and water development for conservation or use purposes;

(vii) Refinancing indebtedness incurred for any authorized OL purpose, when the lender and loan applicant can demonstrate the need to refinance;

(viii) Payment of loan closing costs;

(ix) Payment of costs associated with complying with Federal or State-approved standards under the Occupational Safety and Health Act of 1970 (29 U.S.C. 655, 667). This purpose is limited to applicants who demonstrate that compliance with the standards will cause them substantial economic injury; and

(x) Payment of training costs required or recommended by the Agency.

(2) Loan funds under a line of credit may be advanced only for the following purposes:

(i) Payment of annual operating expenses, family subsistence, and purchase of feeder animals;

(ii) Payment of current annual operating debts advanced for the current operating cycle; (Under no circumstances can carry-over operating debts from a previous operating cycle be refinanced);

(iii) Purchase of routine capital assets, such as replacement of livestock, that will be repaid within the operating cycle;

(iv) Payment of scheduled, non-delinquent, term debt payments provided the debt is for authorized FO or OL purposes.

(v) Purchase of cooperative stock for credit, production, processing or marketing purposes; and

(vi) Payment of loan closing costs.

(b) *Farm ownership loan purposes.* Guaranteed FO are authorized only to:

(1) Acquire or enlarge a farm or ranch; examples include, but are not limited to, providing down payments, purchasing easements for the loan applicant's portion of land being subdivided, and participating in the beginning farmer downpayment FO program under part 1943, subpart A, of this title;

(2) Make capital improvements; examples include, but are not limited to, the construction, purchase, and improvement of a farm dwelling, service buildings and facilities that can be made fixtures to the real estate, (Capital improvements to leased land may be financed subject to the limitations in § 762.122);

(3) Promote soil and water conservation and protection; examples include the correction of hazardous environmental conditions, and the construction or installation of tiles, terraces and waterways;

(4) Pay closing costs, including but not limited to, purchasing stock in a cooperative and appraisal and survey fees; and

(5) Refinancing indebtedness incurred for authorized FO and OL purposes, provided the lender and loan applicant demonstrate the need to refinance the debt.

(c) *Highly erodible land or wetlands conservation.* Loans may not be made for any purpose which contributes to excessive erosion of highly erodible land or to the conversion of wetlands to produce an agricultural commodity. A decision by the Agency to reject an application for this reason may be appealable. An appeal questioning whether the presence of a wetland, converted wetland, or highly erodible land on a particular property must be filed directly with the USDA agency making the determination in accordance with the agency's appeal procedures.

(d) *Judgment debts.* Loans may not be used to satisfy judgments obtained in the United States District courts. However, Internal Revenue Service judgment liens may be paid with loan funds.

§ 762.122 Loan limitations.

(a) *Dollar limits.* Guaranteed loans are limited to the following:

(1) The total outstanding combined Direct and Guaranteed FO and OL principal balance cannot exceed $700,000 and,

(2) The total outstanding direct and guaranteed FO principal balance cannot exceed $700,000 and,

(3) The total outstanding direct and guaranteed OL principal balance cannot exceed $700,000 and,

(4) The total combined outstanding direct and guaranteed FO and OL balance cannot exceed $900,000.

(b) *Line of credit advances.* The total dollar amount of line of credit advances and income releases cannot exceed the total estimated expenses, less interest expense, as indicated on the borrower's cash flow budget, unless the cash flow budget is revised and continues to reflect a feasible plan.

(c) *OL term limitations.*

(1) No guaranteed OL shall be made to any loan applicant after the 15th year that a loan applicant, or any individual signing the promissory note, first received direct or guaranteed OL.

(2) Notwithstanding paragraph (c)(1) of this section, if a borrower had any combination of direct or guaranteed OL closed in 10 or more prior calendar years prior to October 28, 1992, eligibility to receive new guaranteed OL is extended for 5 additional years from October 28, 1992, and the years need not run consecutively. However, in the case of a line of credit, each year in which an advance is made after October 28, 1992, counts toward the 5 additional years. Once determined eligible, a loan or line of credit may be approved for any authorized term.

(d) *Leased land.* When FO funds are used for improvements to leased land the terms of the lease must provide reasonable assurance that the loan applicant will have use of the improvement over its useful life, or provide compensation for any unexhausted value of the improvement if the lease is terminated.

(e) *Tax-exempt transactions.* The Agency will not guarantee any loan made with the proceeds of any obligation the interest on which is excluded from income under section 103 of the Internal Revenue Code of 1986. Funds generated through the issuance of tax-exempt obligations may not be used to purchase the guaranteed portion of any Agency guaranteed loan. An Agency guaranteed loan may not serve as collateral for a tax-exempt bond issue.

(f) *Floodplain restrictions.* The Agency will not guarantee any loan to purchase, build, or expand buildings located in a special 100 year floodplain as defined by FEMA flood hazard area maps unless flood insurance is available and purchased.

§ 762.123 Insurance and farm inspection requirements.

(a) *Insurance.*

(1) Lenders must require borrowers to maintain adequate property, public liability, and crop insurance to protect the lender and Government's interests.

(2) By loan closing, loan applicants must either:

(i) Obtain at least the catastrophic risk protection (CAT) level of crop insurance coverage, if available, for each crop of economic significance, as defined by part 402 of this title, or

(ii) Waive eligibility for emergency crop loss assistance in connection with the uninsured crop. EM loan assistance under part 1945, subpart D, of this title is not considered emergency crop loss assistance for purposes of this waiver and execution of the waiver does not render the borrower ineligible for EM loans.

(3) Loan applicants must purchase flood insurance if buildings are or will be located in a special flood hazard area as defined by FEMA flood hazard area maps and if flood insurance is available.

(4) Insurance, including crop insurance, must be obtained as required by the lender or the Agency based on the strengths and weaknesses of the loan.

(b) *Farm inspections.* Before submitting an application the lender must make an inspection of the farm to assess the suitability of the farm and to determine any development that is needed to make it a suitable farm.

§ 762.124 Interest rates, terms, charges, and fees.

(a) *Interest rates.*

(1) The interest rate on a guaranteed loan or line of credit may be fixed or variable as agreed upon between the

borrower and the lender. The lender may charge different rates on the guaranteed and the non-guaranteed portions of the note. The guaranteed portion may be fixed while the unguaranteed portion may be variable, or vice versa. If both portions are variable, different bases may be used.

(2) If a variable rate is used, it must be tied to a rate specifically agreed to between the lender and borrower in the loan instruments. Variable rates may change according to the normal practices of the lender for its average farm customers, but the frequency of change must be specified in the loan or line of credit instrument.

(3) Neither the interest rate on the guaranteed portion nor the unguaranteed portion may exceed the rate the lender charges its average agricultural loan customer. At the request of the Agency, the lender must provide evidence of the rate charged the average agricultural loan customer. This evidence may consist of average yield data, or documented administrative differential rate schedule formulas used by the lender.

(4) Interest must be charged only on the actual amount of funds advanced and for the actual time the funds are outstanding. Interest on protective advances made by the lender to protect the security will be charged at the note rate but limited to paragraph (a)(3) of this section.

(5) The lender and borrower may collectively obtain a temporary reduction in the interest rate through the interest assistance program in accordance with § 762.150.

(b) *OL terms.*

(1) Loan funds or advances on a line of credit used to pay annual operating expenses will be repaid when the income from the year's operation is received, except when the borrower is establishing a new enterprise, developing a farm, purchasing feed while feed crops are being established, or recovering from disaster or economic reverses.

(2) The final maturity date for each loan cannot exceed 7 years from the date of the promissory note or line of credit agreement. Advances for purposes other than for annual operating expenses will be scheduled for repayment over the minimum period necessary considering the loan applicant's ability to repay and the useful life of the security, but not in excess of 7 years.

(3) All advances on a line of credit must be made within 5 years from the date of the Loan Guarantee.

(c) *FO terms.* Each loan must be scheduled for repayment over a period not to exceed 40 years from the date of the note or such shorter period as may be necessary to assure that the loan will be adequately secured, taking into account the probable depreciation of the security.

(d) *Balloon installments under loan note guarantee.* Balloon payment terms are permitted on FO or OL subject to the following:

(1) Extended repayment schedules may include equal, unequal, or balloon installments if needed on any guaranteed loan to establish a new enterprise, develop a farm, or recover from a disaster or an economical reversal.

(2) Loans with balloon installments must have adequate collateral at the time the balloon installment comes due. Crops, livestock other than breeding livestock, or livestock products produced are not sufficient collateral for securing such a loan.

(3) The borrower must be projected to be able to refinance the remaining debt at the time the balloon payment comes due based on the expected financial condition of the operation, the depreciated value of the collateral, and the principal balance on the loan.

(e) *Charges and Fees.*

(1) The lender may charge the loan applicant and borrower fees for the loan provided they are no greater than those charged to unguaranteed customers for similar transactions. Similar transactions are those involving the same type of loan requested (for example, operating loans or farm real estate loans).

(2) Late payment charges (including default interest charges) are not covered by the guarantee. These charges may not be added to the principal and interest due under any guaranteed note or line of credit. However, late payment charges may be made outside of the guarantee if they are routinely made by the lender in similar types of loan transactions.

(3) Lenders may not charge a loan origination and servicing fee greater than 1 percent of the loan amount for the life of the loan when a guaranteed loan is made in conjunction with a down payment FO for beginning farmers under part 1943, subpart A, of this title.

§ 762.125 Financial feasibility.

(a) *General.*

(1) Notwithstanding any other provision of this section, PLP lenders will follow their internal procedures on financial feasibility as agreed to by the Agency during PLP certification.

(2) The loan applicant's proposed operation must project a positive cash flow.

(3) For standard eligible lenders, the projected income and expenses of the borrower and operation used to determine positive cash flow must be based on the loan applicant's proven record of production and financial management.

(4) For CLP lenders, the projected income and expenses of the borrower and the operation must be based on the loan applicant's financial history and proven record of financial management.

(5) For those farmers without a proven history, a combination of any actual history and any other reliable source of information that are agreeable with the lender, the loan applicant, and the Agency will be used.

(6) The cash flow budget analyzed to determine positive cash flow must represent the predicted cash flow of the operating cycle.

(7) Lenders must use price forecasts that are reasonable and defensible. Sources must be documented by the lender and acceptable to the Agency.

(8) When positive cash flow depends on income from other sources in addition to income from owned land, the income must be dependable and likely to continue.

(9) The lender will analyze business ventures other than the farm operation to determine their soundness and contribution to the operation. Guaranteed loan funds will not be used to finance a nonfarm enterprise. Nonfarm enterprises include, but are not limited to: raising earthworms, exotic birds, tropical fish, dogs, or horses for nonfarm purposes; welding shops; boarding horses; and riding stables.

(10) When the loan applicant has or will have a cash flow budget developed in conjunction with a proposed or existing Agency direct loan, the two cash flow budgets must be consistent.

(b) *Estimating production.*

(1) Standard eligible lenders must use the best sources of information available for estimating production in accordance with this subsection when developing cash flow budgets.

(2) Deviations from historical performance may be acceptable, if specific to changes in operation and adequately justified and acceptable to the Agency.

(3) For existing farmers, actual production for the past 3 years will be utilized.

(4) For those farmers without a proven history, a combination of any actual history and any other reliable source of information that are agreeable with the lender, the loan applicant, and the Agency will be used.

(5) When the production of a growing commodity can be estimated, it must be considered when projecting yields.

(6) When the loan applicant's production history has been so severely affected by a declared disaster that an accurate projection cannot be made, the following applies:

(i) County average yields are used for the disaster year if the loan applicant's disaster year yields are less than the county average yields. If county average yields are not available, State average yields are used. Adjustments can be made, provided there is factual evidence to demonstrate that the yield used in the farm plan is the most probable to be realized.

(ii) To calculate a historical yield, the crop year with the lowest actual or county average yield may be excluded, provided the loan applicant's yields were affected by disasters at least 2 of the previous 5 consecutive years.

(c) *Refinancing.* Loan guarantee requests for refinancing must ensure that a reasonable chance for success still exists. The lender must demonstrate that problems with the loan applicant's operation that have been identified, can be corrected, and the operation returned to a sound financial basis.

§ 762.126 Security requirements.

(a) *General.*

(1) The lender is responsible for ensuring that proper and adequate security is obtained and maintained to fully secure the loan, protect the interest of the lender and the Agency, and assure repayment of the loan or line of credit.

(2) The lender will obtain a lien on additional security when necessary to protect the Agency's interest.

(b) *Guaranteed and unguaranteed portions.*

(1) All security must secure the entire loan or line of credit. The lender may not take separate security to secure only that portion of the loan or line of credit not covered by the guarantee.

(2) The lender may not require compensating balances or certificates of deposit as means of eliminating the lender's exposure on the unguaranteed portion of the loan or line of credit. However, compensating balances or certificates of deposit as otherwise used in the ordinary course of business are allowed for both the guaranteed and unguaranteed portions.

(c) *Identifiable security.* The guaranteed loan must be secured by identifiable collateral. To be identifiable, the lender must be able to distinguish the collateral item and adequately describe it in the security instrument.

(d) *Type of security.*

(1) Guaranteed loans may be secured by any property if the term of the loan and expected life of the property will not cause the loan to be undersecured.

(2) For loans with terms greater than 7 years, a lien must be taken on real estate.

(3) Loans can be secured by a mortgage on leasehold properties if the lease has a negotiable value and is subject to being mortgaged.

(4) The lender or Agency may require additional personal and corporate guarantees to adequately secure the loan. These guarantees are separate from, and in addition to, the personal obligations arising from members of an entity signing the note as individuals.

(e) *Lien position.* All guaranteed loans will be secured by the best lien obtainable. Provided that:

(1) When the loan is made for refinancing purposes, the guaranteed loan must hold a security position no lower than on the refinanced loan.

(2) Any chattel-secured guaranteed loan must have a higher lien priority (including purchase money interest) than an unguaranteed loan secured by the same chattels and held by the same lender.

(3) Junior lien positions are acceptable only if the equity position is strong. Junior liens on crops, or livestock products will not be relied upon for security unless the lender is involved in multiple guaranteed loans to the same borrower and also has the first lien on the collateral.

(4) When taking a junior lien, prior lien instruments will not contain future advance clauses (except for taxes, insurance, or other reasonable costs to protect security), or cancellation, summary forfeiture, or other clauses that jeopardize the Government's or the lender's interest or the borrower's ability to pay the guaranteed loan, unless any such undesirable provisions are limited, modified, waived or subordinated by the lienholder for the benefit of the Agency and the lender.

(f) Additional security, or any loan of $10,000 or less may be secured by the best lien obtainable on real estate without title clearance or legal services normally required, provided the lender believes from a search of the county records that the loan applicant can give a mortgage on the farm and provided that the lender would, in the normal course of business, waive the title search. This exception to title clearance will not apply when land is to be purchased.

(g) *Multiple owners.* If security has multiple owners, all owners must execute the security documents for the loan.

(h) *Exceptions.* The Deputy Administrator for Farm Loan Programs has the authority to grant an exception to any of the requirements involving security, if the proposed change is in the best interest of the Government and the collection of the loan will not be impaired.

§ 762.127 Appraisal requirements.

(a) *General.* The Agency may require a lender to obtain an appraisal based on the type of security, loan size, and whether it is primary or additional security. Except for authorized liquidation expenses, the lender is responsible for all appraisal costs, which may be passed on to the borrower, or a transferee in the case of a transfer and assumption.

(b) *Exception.* Notwithstanding other provisions of this section, an appraisal is not required for any additional security, or for loans of $50,000 or less if a strong equity position exists.

(c) *Chattel appraisals.* A current appraisal (not more than 12 months old) of primary chattel security is generally required on all loans. An appraisal for loans or lines of credit for annual production purposes that are secured by crops is only required when a guarantee is requested late in the current production year and actual yields can be reasonably estimated. The appraised value of chattel property will be based on public sales of the same, or similar, property in the market area. In the absence of such public sales, reputable publications reflecting market values may be used. Appraisal reports may be on the Agency's appraisal of chattel property form or on any other appraisal form containing at least the same information. Chattel appraisals will be performed by appraisers who possess sufficient experience or training to establish market (not retail) values as determined by the Agency.

(d) *Real estate appraisals.* A current real estate appraisal is required when real estate will be primary security. Agency officials may accept an appraisal that is not current if there have been no significant changes in the market or on the subject real estate and the appraisal was either completed within the past 12 months or updated by a qualified appraiser if not completed within the past 12 months.

(1) Appraiser qualifications. On loan transactions of $250,000 or less, the lender must demonstrate to the Agency's satisfaction that the appraiser possesses sufficient experience or training to estimate the market value of agricultural property. On loan

transactions greater than $250,000, which includes principal plus accrued interest through the closing date, the appraisal must be completed by a State certified general appraiser.

(2) Appraisals. Real estate appraisals must be completed in accordance with the Uniform Standards of Professional Appraisal Practice. Appraisals may be either a complete or limited appraisal provided in a self-contained or summary format. Restricted reports, as defined in the Uniform Standards of Professional Appraisal Practice, are not acceptable.

§ 762.128 Environmental and special laws.

(a) *Environmental requirements.* The requirements found in part 1940, subpart G, of this title must be met for guaranteed OL and FO. CLP and PLP lenders may certify that they have documentation in their file to demonstrate compliance with paragraph (c) of this section. Standard eligible lenders must submit evidence supporting compliance with this section.

(b) *Determination.* The Agency determination of whether an environmental problem exists will be based on:

(1) The information supplied with the application;

(2) The Agency Official's personal knowledge of the operation;

(3) Environmental resources available to the Agency including, but not limited to, documents, third parties, and governmental agencies;

(4) A visit to the farm operation when the available information is insufficient to make a determination;

(5) Other information supplied by the lender or loan applicant upon Agency request. If necessary, information not supplied with the application will be requested by the Agency.

(c) *Special requirements.* Lenders will assist in the environmental review process by providing environmental information. In all cases, the lender must retain documentation of their investigation in the loan applicant's case file.

(1) A determination must be made as to whether there are any potential impacts to a 100 year floodplain as defined by Federal Emergency Management Agency floodplain maps, Natural Resources Conservation Service data, or other appropriate documentation.

(2) The lender will assist the borrower in securing any applicable permits or waste management plans. The lender may consult with the Agency for guidance on activities which require consultation with State regulatory agencies, special permitting or waste management plans.

(3) The lender will examine the security property to determine if there are any structures or archeological sites which are listed or may be eligible for listing in the National Register of Historic Places. The lender may consult with the Agency for guidance on which situations will need further review in accordance with the National Historical Preservation Act and part 1940, subpart G, and part 1901, subpart F, of this title.

(4) The loan applicant must certify they will not violate the provisions of § 363 of the CONACT, the Food Security Act of 1985, and Executive Order 11990 relating to Highly Erodible Land and Wetlands.

(5) All lenders are required to ensure that due diligence is performed in conjunction with a request for guarantee of a loan involving real estate. Due diligence is the process of evaluating real estate in the context of a real estate transaction to determine the presence of contamination from release of hazardous substances, petroleum products, or other environmental hazards and determining what effect, if any, the contamination has on the security value of the property. The Agency will accept as evidence of due diligence the most current version of the American Society of Testing Materials (ASTM) transaction screen questionnaire available from 100 Barr Harbor Drive, West Conshohocken, Pennsylvania 19428–2959, or similar documentation, approved for use by the Agency, supplemented as necessary by the ASTM phase I environmental site assessments form.

(d) *Equal opportunity and nondiscrimination.*

(1) With respect to any aspect of a credit transaction, the lender will not discriminate against any applicant on the basis of race, color, religion, national origin, sex, marital status, or age, provided the applicant can execute a legal contract. Nor will the lender discriminate on the basis of whether all or a part of the applicant's income derives from any public assistance program, or whether the applicant in good faith, exercises any rights under the Consumer Protection Act.

(2) Where the guaranteed loan involves construction, the contractor or subcontractor must file all compliance reports, equal opportunity and nondiscrimination forms, and otherwise comply with all regulations prescribed by the Secretary of Labor pursuant to Executive Orders 11246 and 11375.

(e) *Other Federal, State and local requirements.* Lenders are required to coordinate with all appropriate Federal, State, and local agencies and comply with special laws and regulations applicable to the loan proposal.

§ 762.129 Percent of guarantee and maximum loss.

(a) *General.* The percent of guarantee will not exceed 90 percent based on the credit risk to the lender and the Agency both before and after the transaction. The Agency will determine the percentage of guarantee.

(b) *Exceptions.* The guarantee will be issued at 95 percent in any of the following circumstances:

(1) The sole purpose of a guaranteed FO or OL is to refinance an Agency direct farm loan. When only a portion of the loan is used to refinance a direct Agency farm credit program loan, a weighted percentage of a guarantee will be provided;

(2) When the purpose of an FO guarantee is to participate in the down payment loan program; or

(3) When a guaranteed OL is made to a farmer or rancher who is participating in the Agency's down payment loan program. The guaranteed OL must be made during the period that a borrower has the down payment loan outstanding.

(c) *CLP and PLP guarantees.* All guarantees issued to CLP or PLP lenders will not be less than 80 percent.

(d) *Maximum loss.* The maximum amount the Agency will pay the lender under the loan guarantee will be any loss sustained by such lender on the guaranteed portion including:

(1) The pro rata share of principal and interest indebtedness as evidenced by the note or by assumption agreement;

(2) Any loan subsidy due and owing;

(3) The pro rata share of principal and interest indebtedness on secured protective and emergency advances made in accordance with this subpart; and

(4) Principal and interest indebtedness on recapture debt pursuant to a shared appreciation agreement. Provided that the lender has paid the Agency its pro rata share of the recapture amount due.

§ 762.130 Loan approval and issuing the guarantee.

(a) *Processing timeframes.*

(1) Standard Eligible Lenders. Complete applications from Standard Eligible Lenders will be approved or rejected, and the lender notified in writing, no later than 30 calendar days after receipt.

(2) CLP and PLP lenders.

(i) Complete applications from CLP or PLP lenders will be approved or rejected not later than 14 calendar days after receipt.

(ii) For PLP lenders, if this time frame is not met, the proposed guaranteed loan will automatically be approved, subject to funding, and receive an 80 or 95 percent guarantee, as appropriate.

(3) Complete applications. For purposes of determining the application processing timeframes, an application will be not be considered complete until all information required to make an approval decision, including the information for an environmental review, is received by the Agency.

(4) The Agency will confirm the date an application is received with a written notification to the lender.

(b) *Funding preference.* Loans are approved subject to the availability of funding. When it appears that there are not adequate funds to meet the needs of all approved loan applicants, applications that have been approved will be placed on a preference list according to the date of receipt of a complete application. If approved applications have been received on the same day, the following will be given priority:

(1) An application from a veteran

(2) An application from an Agency direct loan borrower

(3) An application from a loan applicant who:

(i) Has a dependent family,

(ii) Is an owner of livestock and farm implements necessary to successfully carry out farming operations, or

(iii) Is able to make down payments.

(4) Any other approved application.

(c) *Conditional commitment.*

(1) The lender must meet all of the conditions specified in the conditional commitment to secure final Agency approval of the guarantee.

(2) The lender, after reviewing the conditions listed on the conditional commitment, will complete, execute, and return the form to the Agency. If the conditions are not acceptable to the lender, the Agency may agree to alternatives or inform the lender and the loan applicant of their appeal rights.

(d) *Lender requirements prior to issuing the guarantee.*

(1) Lender certification. The lender will certify as to the following on the appropriate Agency form:

(i) No major changes have been made in the lender's loan or line of credit conditions and requirements since submission of the application (except those approved in the interim by the Agency in writing);

(ii) Required hazard, flood, crop, worker's compensation, and personal life insurance (when required) are in effect;

(iii) Truth in lending requirements have been met;

(iv) All equal employment and equal credit opportunity and nondiscrimination requirements have been or will be met at the appropriate time;

(v) The loan or line of credit has been properly closed, and the required security instruments have been obtained, or will be obtained, on any acquired property that cannot be covered initially under State law;

(vi) The borrower has marketable title to the collateral owned by the borrower, subject to the instrument securing the loan or line of credit to be guaranteed and subject to any other exceptions approved in writing by the Agency. When required, an assignment on all USDA crop and livestock program payments has been obtained;

(vii) When required, personal, joint operation, partnership, or corporate guarantees have been obtained;

(viii) Liens have been perfected and priorities are consistent with requirements of the conditional commitment;

(ix) Loan proceeds have been, or will be disbursed for purposes and in amounts consistent with the conditional commitment and as specified on the loan application. In line of credit cases, if any advances have occurred, advances have been disbursed for purposes and in amounts consistent with the conditional commitment and line of credit agreements;

(x) There has been no material adverse change in the borrower's condition, financial or otherwise, since submission of the application; and

(xi) All other requirements specified in the conditional commitment have been met.

(2) Inspections. The lender must notify the Agency of any scheduled inspections during construction and after the guarantee has been issued. The Agency may attend these field inspections. Any inspections or review performed by the Agency, including those with the lender, are solely for the benefit of the Agency. Agency inspections do not relieve any other parties of their inspection responsibilities, nor can these parties rely on Agency inspections for any purpose.

(3) Execution of lender's agreement. The lender must execute the Agency's lender's agreement and deliver it to the Agency.

(4) Closing report and guarantee fees.

(i) The lender must complete an Agency closing report form and return it to the Agency along with any guarantee fees.

(ii) Guarantee fees are 1 percent and are calculated as follows: Fee = Loan Amount x % Guaranteed x .01. The nonrefundable fee is paid to the Agency by the lender. The fee may be passed on to the borrower and included in loan funds.

(iii) The following guaranteed loan transactions are not charged a fee:

(A) Loans involving interest assistance;

(B) Loans where a majority of the funds are used to refinance an Agency direct loan; and

(C) Loans to beginning farmers or ranchers involved in the direct beginning farmer downpayment program.

(e) *Promissory notes, line of credit agreements, mortgages, and security agreements.* The lender will use its own promissory notes, line of credit agreements, real estate mortgages (including deeds of trust and similar instruments), and security agreements (including chattel mortgages in Louisiana and Puerto Rico), provided:

(1) The forms meet Agency requirements;

(2) Documents comply with State law and regulation;

(3) The principal and interest repayment schedules are stated clearly in the notes and are consistent with the conditional commitment;

(4) The note is executed by the individual liable for the loan. For entities, the note is executed by the member who is authorized to sign for the entity, and by all members of the entity as individuals. Individual liability can be waived by the Agency for members holding less than 10 percent ownership in the entity if the collectability of the loan will not be impaired; and

(5) When the loan purpose is to refinance or restructure the lender's own debt, the lender may continue to use the existing debt instrument and attach an allonge that modifies the terms of the original note.

(f) *Replacement of loan guarantee, or assignment guarantee agreement.* If the guarantee or assignment guarantee agreements are lost, stolen, destroyed, mutilated, or defaced, except where the evidence of debt was or is a bearer instrument, the Agency will issue a replacement to the lender or holder upon receipt of acceptable documentation including a certificate of loss and an indemnity bond.

§§ 762.131–762.139 [Reserved]

§ 762.140 General servicing responsibilities.

(a) General.

(1) Lenders are responsible for servicing the entire loan in a reasonable

and prudent manner, protecting and accounting for the collateral, and remaining the mortgagee or secured party of record.

(2) The lender cannot enforce the guarantee to the extent that a loss results from a violation of usury laws or negligent servicing.

(b) *Borrower supervision.* The lender's responsibilities regarding borrower supervision include, but are not limited to the following:

(1) Ensuring loan funds are not used for unauthorized purposes.

(2) Ensuring borrower compliance with the covenants and provisions contained in the promissory note, loan agreement, mortgage, security instruments, any other agreements, and this part. Any violations which indicate non-compliance on the part of the borrower must be reported, in writing, to both the Agency and the borrower.

(3) Ensuring the borrower is in compliance with all laws and regulations applicable to the loan, the collateral, and the operations of the farm.

(4) Receiving all payments of principal and interest on the loan as they fall due and promptly disbursing to any holder its pro-rata share according to the amount of interest the holder has in the loan, less only the lender's servicing fee.

(5) Performing an annual analysis of the borrower's financial condition to determine the borrower's progress. The annual analysis will include:

(i) For loans secured by real estate only, the analysis for standard eligible lenders must include an analysis of the borrower's balance sheet. CLP lenders will determine the need for the annual analysis based on the financial strength of the borrower and document the file accordingly. PLP lenders will perform an annual analysis in accordance with the requirements established in the lender's agreement.

(ii) For loans secured by chattels, all lenders will review the borrower's progress regarding business goals, trends and changes in financial performance, and compare actual to planned income and expenses for the past year.

(iii) An account of the whereabouts or disposition of all collateral.

(iv) A discussion of any observations about the farm business with the borrower.

(c) *Monitoring of development.* The lender's responsibilities regarding the construction, repairs, or other development include, but are not limited to:

(1) Determining that all construction is completed as proposed in the loan application;

(2) Making periodic inspections during construction to ensure that any development is properly completed within a reasonable period of time; and

(3) Verification that the security is free of any mechanic's, materialmen's, or other liens which would affect the lender's lien or result in a different lien priority from that proposed in the request for guarantee.

(d) The guaranteed loan installments will be paid before unguaranteed loans held by the same lender.

§ 762.141 Reporting requirements.

Lenders are responsible for providing the local Agency credit officer with all of the following information on the loan and the borrower:

(a) When the guaranteed loan becomes 30 days past due, and following the lender's meeting or attempts to meet with the borrower, all lenders will submit the appropriate Agency form showing guaranteed loan borrower default status. The form will be resubmitted every 60 days until the default is cured either through restructuring or liquidation.

(b) All lenders will submit the appropriate guaranteed loan status reports as of March 31 and September 30 of each year;

(c) CLP lenders also must provide the following:

(1) A written summary of the lender's annual analysis of the borrower's operation. This summary should describe the borrower's progress and prospects for the upcoming operating cycle. This annual analysis may be waived or postponed if the borrower is financially strong. The summary will include a description of the reasons an analysis was not necessary.

(2) For lines of credit, an annual certification stating that a cash flow projecting at least a feasible plan has been developed, that the borrower is in compliance with the provisions of the line of credit agreement, and that the previous year income and loan funds and security proceeds have been accounted for.

(d) In addition to the requirements of paragraphs (a), (b), and (c) of this section, the standard eligible lender also will provide:

(1) Borrower's balance sheet, and income and expense statement for the previous year.

(2) For lines of credit, the cash flow for the borrower's operation that projects a feasible plan or better for the upcoming operating cycle. The standard eligible lender must receive approval from the Agency before advancing future years' funds.

(3) An annual farm visit report or collateral inspection.

(e) PLP lenders will submit additional reports as required in their lender's agreement.

(f) A lender receiving a final loss payment must complete and return an annual report on its collection activities for each unsatisfied account for 3 years following payment of the final loss claim.

§ 762.142 Servicing related to collateral.

(a) *General.* The lender's responsibilities regarding servicing collateral include, but are not limited to, the following:

(1) Obtain income and insurance assignments when required.

(2) Ensure the borrower has or obtains marketable title to the collateral.

(3) Inspect the collateral as often as deemed necessary to properly service the loan.

(4) Ensure the borrower does not convert loan security.

(5) Ensure the proceeds from the sale or other disposition of collateral are accounted for and applied in accordance with the lien priorities on which the guarantee is based or used for the purchase of replacement collateral.

(6) Ensure the loan and the collateral are protected in the event of foreclosure, bankruptcy, receivership, insolvency, condemnation, or other litigation.

(7) Ensure taxes, assessments, or ground rents against or affecting the collateral are paid.

(8) Ensure adequate insurance is maintained.

(9) Ensure that insurance loss payments, condemnation awards, or similar proceeds are applied on debts in accordance with lien priorities on which the guarantee was based, or used to rebuild or acquire needed replacement collateral.

(b) *Partial releases.*

(1) A lender may release guaranteed loan security without FSA concurrence as follows:

(i) When the security item is being sold for market value and the proceeds will be applied to the loan in accordance with lien priorities. In the case of term loans, proceeds will be applied as extra payments and not as a regular installment on the loan.

(ii) The security item will be used as a trade-in or source of down payment funds for a like item that will be taken as security.

(iii) The security item has no present or prospective value.

(2) A partial release of security may be approved in writing by the Agency upon the lender's request when:

(i) Proceeds will be used to make improvements to real estate that increase the value of the security by an amount equal to or greater than the value of the security being released.

(ii) Security will be released outright with no consideration, but the total unpaid balance of the guaranteed loan is less than or equal to 75 percent of the value of the security for the loan after the release, excluding the value of growing crops or planned production, based on a current appraisal of the security.

(iii) Significant income generating property will not be released unless it is being replaced and business assets will not be released for use as a gift or any similar purpose.

(iv) Agency concurrence is provided in writing to the lender's written request. Standard eligible lenders and CLP lenders will submit the following to the Agency:

(A) A current balance sheet on the borrower; and

(B) A current appraisal of the security. Based on the level of risk and estimated equity involved, the Agency will determine what security needs to be appraised. Any required security appraisals must meet the requirements of § 762.127; and

(C) A description of the purpose of the release; and

(D) Any other information requested by the Agency to evaluate the proposed servicing action.

(3) The lender will provide the Agency copies of any agreements executed to carry out the servicing action.

(4) PLP lenders will request servicing approval in accordance with their agreement with the Agency at the time of PLP status certification.

(c) *Subordinations.*

(1) The Agency may subordinate its security interest on a direct loan when a guaranteed loan is being made if the requirements of the regulations governing Agency direct loan subordinations are met and only in the following circumstances:

(i) To permit a guaranteed lender to advance funds and perfect a security interest in crops, feeder livestock, livestock offspring, or livestock products;

(ii) When the lender requesting the guarantee needs the subordination of the Agency's lien position to maintain its lien position when servicing or restructuring;

(iii) When the lender requesting the guarantee is refinancing the debt of another lender and the Agency's position on real estate security will not be adversely affected; or

(iv) To permit a line of credit to be advanced for annual operating expenses.

(2) The Agency may subordinate its basic security in a direct loan to permit guaranteed line of credit only when both of the following additional conditions are met:

(i) The total unpaid balance of the direct loans is less than or equal to 75 percent of the value of all of the security for the direct loans, excluding the value of growing crops or planned production, at the time of the subordination. The direct loan security value will be determined by an appraisal. The lender requesting the subordination and guarantee is responsible for providing the appraisal and may charge the applicant a reasonable appraisal fee.

(ii) The applicant cannot obtain sufficient credit through a conventional guaranteed loan without a subordination.

(3) The lender may not subordinate its interest in property which secures a guaranteed loan except as follows:

(i) The lender may subordinate its security interest in crops, feeder livestock, livestock offspring, or livestock products when no funds have been advanced from the guaranteed loan for their production, so a lender can make a loan for annual production expenses; or

(ii) The Agency's national office may provide an exception to the subordination prohibition if such action is in the Agency's best interest. However, in no case can the loan made under the subordination include tax exempt financing.

(d) *Transfer and assumption.* Transfers and assumptions are subject to the following conditions:

(1) For standard eligible and CLP lenders, the servicing action must be approved by the Agency in writing.

(2) For standard eligible and CLP lenders, the transferee must apply for a loan in accordance with § 762.110, including a current appraisal, unless the lien position of the guaranteed loan will not change, and any other information requested by the Agency to evaluate the transfer and assumption.

(3) PLP lenders may process transfers and assumptions in accordance with their agreement with the Agency.

(4) Any required security appraisals must meet the requirements of § 762.127.

(5) The Agency will review, approve or reject the request in accordance with the time frames in § 762.130.

(6) The transferee must meet the eligibility requirements and loan limitations for the loan being transferred, all requirements relating to loan rates and terms, loan security, feasibility, and environmental and other laws applicable to a loan applicant under this part.

(7) The lender will use its own assumption agreements or conveyance instruments, providing they are legally sufficient to obligate the transferee for the total outstanding debt. The lender will provide the Agency copies of any agreements executed to carry out the servicing action.

(8) The lender must execute a modification of the guarantee provided by the Agency to designate the party that assumed the guaranteed debt, the amount of debt at the time of the assumption (including interest that being capitalized), and the new loan terms, if applicable.

(9) The lender must give any holder notice of the transfer. If the rate and terms are changed, written concurrence from the holder is required.

(10) The Agency will agree to releasing the transferor or any guarantor from liability only if the requirements of § 762.146(c) are met.

§ 762.143 Servicing distressed accounts.

(a) A borrower is in default when 30 days past due on a payment or in violation of provisions of the loan documents.

(b) In the event of a borrower default, SEL and CLP lenders will:

(1) Report to the Agency in accordance with § 762.141.

(2) Determine whether it will repurchase the guaranteed portion from the holder in accordance with § 762.144, if the guaranteed portion of the loan was sold on the secondary market.

(3) Arrange a meeting with the borrower within 15 days of default (45 days after payment due date for monetary defaults) to identify the nature of the delinquency and develop a course of action that will eliminate the delinquency and correct the underlying problems. Non-monetary defaults will be handled in accordance with the lender's note, loan agreements and any other applicable loan documents.

(i) The lender and borrower will prepare a current balance sheet and cash flow projection in preparation for the meeting. If the borrower refuses to cooperate, the lender will compile the best financial information available.

(ii) The lender or the borrower may request the attendance of an Agency credit officer. If requested, the Agency credit officer will assist in developing solutions to the borrower's financial problems.

(iii) The lender will summarize the meeting and proposed solutions on the Agency form for guaranteed loan borrower default status completed after the meeting. The lender will indicate the results on this form for the lender's consideration of the borrower for interest assistance in conjunction with rescheduling under § 762.145(b).

(iv) The lender must decide whether to restructure or liquidate the account within 90 days of default, unless the lender can document circumstances that justify an extension by the Agency.

(v) The lender may not initiate foreclosure action on the loan until 60 days after eligibility of the borrower to participate in the interest assistance programs has been determined by the Agency. If the lender or the borrower does not wish to consider servicing options under this section, this should be documented, and liquidation under § 762.149 should begin.

(vi) If a borrower is current on a loan, but will be unable to make a payment, a restructuring proposal may be submitted in accordance with § 762.145 prior to the payment coming due.

(c) PLP lenders will service defaulted loans according to their lender's agreement.

§ 762.144 Repurchase of guaranteed portion from a secondary market holder.

(a) *Request for repurchase.* The holder may request the lender to repurchase the unpaid guaranteed portion of the loan when:

(1) The borrower has not made a payment of principal and interest due on the loan for at least 60 days; or

(2) The lender has failed to remit to the holder its pro-rata share of any payment made by the borrower within 30 days of receipt of a payment.

(b) *Repurchase by the lender.*

(1) When a lender is requested to repurchase a loan from the holder, the lender must consider the request according to the servicing actions that are necessary on the loan. In order to facilitate servicing and simplified accounting of loan transactions, lenders are encouraged to repurchase the loan upon the holder's request.

(2) The repurchase by the lender will be for an amount equal to the portion of the loan held by the holder plus accrued interest.

(3) The guarantee will not cover separate servicing fees that the lender accrues after the repurchase.

(c) *Repurchase by the Agency.*

(1) If the lender does not repurchase the loan, the holder must inform the Agency in writing that demand was made on the lender and the lender refused. Following the lender's refusal, the holder may continue as holder of the guaranteed portion of the loan or request that the Agency purchase the guaranteed portion. Within 30 days after written demand to the Agency from the holder with required attachments, the Agency will forward to the holder payment of the unpaid principal balance, with accrued interest to the date of repurchase. If the holder does not desire repurchase or purchase of a defaulted loan, the lender must forward the holder its pro-rata share of payments, liquidation proceeds and Agency loss payments.

(2) With its demand on the Agency, the holder must include:

(i) A copy of the written demand made upon the lender.

(ii) Originals of the guarantee and note properly endorsed to the Agency, or the original of the assignment of guarantee.

(iii) A copy of any written response to the demand of the holder by the lender.

(iv) An account to which the Agency can forward the purchase amount via electronic funds transfer.

(3) The amount due the holder from the Agency includes unpaid principal, unpaid interest to the date of demand, and interest which has accrued from the date of demand to the proposed payment date.

(i) Upon request by the Agency, the lender must furnish upon Agency request a current statement, certified by a bank officer, of the unpaid principal and interest owed by the borrower and the amount due the holder.

(ii) Any discrepancy between the amount claimed by the holder and the information submitted by the lender must be resolved by the lender and the holder before payment will be approved by the Agency. The Agency will not participate in resolution of any such discrepancy. When there is a discrepancy, the 30 day Agency payment requirement to the holder will be suspended until the discrepancy is resolved.

(iii) In the case of a request for Agency purchase, the government will only pay interest that accrues for up to 90 days from the date of the demand letter to the lender requesting the repurchase. However, if the lender requested repurchase from the Agency within 60 days of the request to the holder and for any reason not attributable to the holder and the lender, the Agency cannot make payment within 30 days of the holder's demand to the Agency, the holder will be entitled to interest to the date of the payment.

(4) At the time of purchase by the Agency, the original assignment of guarantee will be assigned by the holder to the Agency without recourse, including all rights, title, and interest in the loan.

(5) Purchase by the Agency does not change, alter, or modify any of the lender's obligations to the Agency specified in the lender's agreement or guarantee; nor does the purchase waive any of the Agency's rights against the lender.

(6) The Agency succeeds to all rights of the holder under the Guarantee including the right of set-off against the lender.

(7) Within 180 days of the Agency's purchase, the lender will reimburse the Agency the amount of repurchase, with accrued interest, through one of the following ways:

(i) By liquidating the loan security and paying the Agency its pro-rata share of liquidation proceeds; or

(ii) Paying the Agency the full amount the Agency paid to the holder plus any accrued interest.

(8) The lender will be liable for the purchase amount and any expenses incurred by the Agency to maintain the loan in its portfolio or liquidate the security. While the Agency holds the guaranteed portion of the loan, the lender will transmit to the Agency any payment received from the borrower, including the pro-rata share of liquidation or other proceeds.

(9) If the borrower files for reorganization under the provisions of the bankruptcy code or pays the account current while the purchase by the Government is being processed, the Agency may hold the loan as long it determines this action to be in the Agency's interest. If the lender is not proceeding expeditiously to collect the loan or reimbursement is not waived under this paragraph, the Agency will demand payment by the lender and collect the purchase amount through administrative offset of any claims due the lender.

(10) The Agency may sell a purchased guaranteed loan on a non-recourse basis if it determines that selling the portion of the loan that it holds is in the Government's best interest. A non-recourse purchase from the Agency requires a written request to the Agency from the party that wishes to purchase it, and written concurrence from the lender;

(d) *Repurchase for servicing.*

(1) If, due to loan default or imminent loan restructuring, the lender determines that repurchase is necessary to adequately service the loan, the lender may repurchase the guaranteed portion of the loan from the holder, with the written approval of the Agency.

(2) The lender will not repurchase from the holder for arbitrage purposes. With its request for Agency concurrence, the lender will notify the

Agency of its plans to resell the guaranteed portion following servicing.

(3) The holder will sell the guaranteed portion of the loan to the lender for an amount agreed to between the lender and holder.

§ 762.145 Restructuring guaranteed loans.

(a) *General.*

(1) To restructure guaranteed loans standard eligible lenders must:

(i) Obtain prior written approval of the Agency for all restructuring actions; and,

(ii) Provide the items in paragraph (b) and (e) of this section to the Agency for approval.

(2) If the standard eligible lender's proposal for servicing is not agreed to by the Agency, the Agency approval official will notify the lender in writing within 14 days of the lender's request.

(3) To restructure guaranteed loans CLP lenders must:

(i) Obtain prior written approval of the Agency only for debt write down under this section.

(ii) Submit all calculations required in paragraph (e) of this section for debt writedown.

(iii) For restructuring other than write down, provide FSA with a certification that each requirement of this section has been met, a narrative outlining the circumstances surrounding the need for restructuring, and copies of any applicable calculations.

(4) PLP lenders will restructure loans in accordance with their lender's agreement.

(5) All lenders will submit copies of any restructured notes or lines of credit to the Agency.

(b) *Requirements.* For any restructuring action, the following conditions apply:

(1) The borrower meets the eligibility criteria of § 762.120, except the provisions regarding prior debt forgiveness and delinquency on a federal debt do not apply.

(2) The borrower's ability to make the amended payment is documented by the following:

(i) A feasible plan (see § 762.102(b)). If interest assistance is required to achieve a feasible plan, the items required by § 762.150(d) must be submitted with a restructuring request. Feasible plan is defined in § 762.102(b).

(ii) Current financial statements from all liable parties.

(iii) Verification of nonfarm income.

(iv) Verification of all debts of $1,000 or more.

(v) Applicable credit reports.

(vi) Financial history (and production history for standard eligible lenders) for the past 3 years to support the cash flow projections.

(3) A final loss claim may be reduced, adjusted, or rejected as a result of negligent servicing after the concurrence with a restructuring action under this section.

(4) Balloon payments are prohibited; however, the loan can be restructured with unequal installments, provided that, in addition to a feasible plan for the upcoming operating cycle, a feasible plan can be reasonably projected after the installments increase. Feasible plan is defined in § 762.102(b).

(5) If a borrower is current on a loan, but will be unable to make a payment, a restructuring proposal may be submitted prior to the payment coming due.

(6) The lender may capitalize the outstanding interest when restructuring the loan as follows:

(i) As a result of the capitalization of interest, a rescheduled promissory note may increase the amount of principal which the borrower is required to pay. However, in no case will such principal amount exceed the statutory loan limits contained in § 762.122.

(ii) When accrued interest causes the loan amount to exceed the statutory loan limits, rescheduling may be approved without capitalization of the amount that exceeds the limit. Noncapitalized interest may be scheduled for repayment over the term of the rescheduled note.

(iii) Only interest that has accrued at the rate indicated on the borrower's original promissory notes may be capitalized. Late payment fees or default interest penalties that have accrued due to the borrower's failure to make payments as agreed are not covered under the guarantee and may not be capitalized.

(iv) The Agency will provide the lender with a modification of guarantee form to identify the new loan principal and the guaranteed portion if greater than the original loan amounts, and to waive the restriction on capitalization of interest, if applicable, to the existing guarantee documents. The modification form will be attached to the original guarantee as an addendum.

(v) Approved capitalized interest will be treated as part of the principal and interest that accrues thereon, in the event that a loss should occur.

(7) The lender's security position will not be adversely affected because of the restructuring. New security instruments may be taken if needed, but a loan does not have to be fully secured in order to be restructured.

(8) Any holder agrees in writing to any changes in the original loan terms, including the approval of interest assistance. If the holder does not agree, the lender must repurchase the loan from the holder for any loan restructuring to occur.

(9) After a guaranteed loan is restructured, the lender must provide the Agency with a copy of the restructured promissory note.

(c) *Rescheduling.* The following conditions apply when a guaranteed loan is rescheduled or reamortized:

(1) Payments will be rescheduled within the following terms:

(i) FO and existing SW may be amortized over the remaining term of the note or rescheduled with an uneven payment schedule. The maturity date cannot exceed 40 years from the date of the original note.

(ii) OL notes must be rescheduled over a period not to exceed 15 years from the date of the rescheduling. An OL line of credit may be rescheduled over a period not to exceed 7 years from the date of the rescheduling or 10 years from the date of the original note, whichever is less. Advances cannot be made against a line of credit loan that has had any portion of the loan rescheduled.

(2) The interest rate for a rescheduled loan is the negotiated rate agreed upon by the lender and the borrower at the time of the action, subject to the loan limitations for each type of loan.

(3) A new note is not necessary when rescheduling occurs. However, if a new note is not taken, the existing note or line of credit agreement must be modified by attaching an allonge or other legally effective amendment, evidencing the revised repayment schedule and any interest rate change. If a new note is taken, the new note must reference the old note and state that the indebtedness evidenced by the old note or line of credit agreement is not satisfied. The original note or line of credit agreement must be retained.

(d) *Deferrals.* The following conditions apply to deferrals:

(1) Payments may be deferred up to 5 years, but the loan may not be extended beyond the final due date of the note.

(2) The principal portion of the payment may be deferred either in whole or in part.

(3) Interest may be deferred only in part. Payment of a reasonable portion of accruing interest as indicated by the borrower's cash flow projections is required for multi-year deferrals.

(4) There must be a reasonable prospect that the borrower will be able to resume full payments at the end of the deferral period.

(e) *Debt writedown.* The following conditions apply to debt writedown:

(1) A lender may only write down a delinquent guaranteed loan or line of

credit in an amount sufficient to permit the borrower to develop a feasible plan as defined in § 762.102(b).

(2) The lender will request other creditors to negotiate their debts before a writedown is considered.

(3) The borrower cannot develop a feasible plan after consideration is given to rescheduling and deferral under this section.

(4) The present value of the loan to be written down, based on the interest rate of the rescheduled loan, will be equal to or exceed the net recovery value of the loan collateral.

(5) The loan will be restructured with regular payments at terms no shorter than 5 years for a line of credit and OL note and no shorter than 20 years for FO, unless required to be shorter by § 762.145(c)(1)(i) and (ii).

(6) No further advances may be made on a line of credit that is written down.

(7) Loans may not be written down with interest assistance. If a borrower's loan presently on interest assistance requires a writedown, the writedown will be considered without interest assistance. If approved, the existing interest assistance agreement will be canceled.

(8) The writedown is based on writing down the shorter-term loans first.

(9) When a lender requests approval of a writedown for a borrower with multiple loans, the security for all of the loans will be cross-collateralized and continue to serve as security for the loan that is written down. If a borrower has multiple loans and one loan is written off entirely through debt writedown, the security for that loan will not be released and will remain as security for the other written down debt. Additional security instruments will be taken if required to cross-collateralize security and maintain lien priority.

(10) The writedown will be evidenced by an allonge or amendment to the existing note or line of credit reflecting the writedown.

(11) The borrower executes an Agency shared appreciation agreement for loans which are written down and secured by real estate.

(i) The lender will attach the original agreement to the restructured loan document.

(ii) The lender will provide the Agency a copy of the executed agreement, and

(iii) Security instruments must ensure future collection of any appreciation under the agreement.

(12) The lender will prepare and submit the following to the Agency:

(i) A current appraisal of all security in accordance with § 762.127.

(ii) A completed report of loss on the appropriate Agency form for the proposed writedown loss claim.

(iii) Detailed writedown calculations as follows:

(A) Calculate the present value.

(B) Determine the net recovery value.

(C) If the net recovery value exceeds the present value, writedown is unavailable; liquidation becomes the next servicing consideration. If the present value equals or exceeds the net recovery value, the debt may be written down to the present value.

(iv) The lender will make any adjustment in the calculations as requested by the Agency.

§ 762.146 Other servicing procedures.

(a) *Additional loans and advances.*

(1) Notwithstanding any provision of this section, the PLP lender may make additional loans or advances in accordance with the lender's agreement with the Agency.

(2) SEL and CLP lenders must not make additional loans or advances without prior written approval of the Agency, except as provided in the borrower's loan or line of credit agreement.

(3) In cases of a guaranteed line of credit, lenders may make an emergency advance when a line of credit has reached its ceiling. The emergency advance will be made as an advance under the line and not as a separate note. The lender's loan documents must contain sufficient language to provide that any emergency advance will constitute a debt of the borrower to the lender and be secured by the security instrument. The following conditions apply:

(i) The loan funds to be advanced are for authorized operating loan purposes;

(ii) The financial benefit to the lender and the Government from the advance will exceed the amount of the advance; and

(iii) The loss of crops or livestock is imminent unless the advance is made.

(4) Protective advance requirements are found in § 762.149.

(b) *Release of liability upon withdrawal.* An individual who is obligated on a guaranteed loan may be released from liability by a lender, with the written consent of the Agency, provided the following conditions have been met:

(1) The individual to be released has withdrawn from the farming or ranching operation;

(2) A divorce decree or final property settlement does not hold the withdrawing party responsible for the loan payments;

(3) The withdrawing party's interest in the security is conveyed to the individual or entity with whom the loan will be continued;

(4) The ratio of the amount of debt to the value of the remaining security is less than or equal to .75, or the withdrawing party has no income or assets from which collection can be made; and

(5) Withdrawal of the individual does not result in legal dissolution of the entity to which the loans are made. Individually liable members of a general or limited partnership may not be released from liability.

(6) The remaining liable party projects a feasible plan (see § 762.102(b)).

(c) *Release of liability after liquidation.* After a final loss claim has been paid on the borrower's account, the lender may release the borrower or guarantor from liability if;

(1) The Agency agrees to the release in writing;

(2) The lender documents its consideration of the following factors concerning the borrower or guarantors:

(i) The likelihood that the borrower or guarantor will have a sufficient level of income in the reasonably near future to contribute to a meaningful reduction of the debt;

(ii) The prospect that the borrower or guarantor will inherit assets in the near term that may be attached by the Agency for payment of a significant portion of the debt;

(iii) Whether collateral has been properly accounted for, and whether liability should be retained in order to take action against the borrower or a third party for conversion of security;

(iv) The availability of other income or assets which are not security;

(v) The possibility that assets have been concealed or improperly transferred;

(vi) The effect of other guarantors on the loan; and

(vii) Cash consideration or other collateral in exchange for the release of liability.

(3) The lender will use its own release of liability documents.

(d) *Interest rate changes.*

(1) The lender may change the interest rate on a performing (nondelinquent) loan only with the borrower's consent.

(2) If the loan has been sold on the secondary market, the lender must repurchase the loan or obtain the holder's written consent.

(3) To change a fixed rate of interest to a variable rate of interest or vice versa, the lender and the borrower must execute a legally effective allonge or amendment to the existing note.

(4) If a new note is taken, it will be attached to and refer to the original note.

(5) The lender will inform the Agency of the rate change.

(e) *Consolidation.* Two or more Agency guaranteed loans may be consolidated, subject to the following conditions:

(1) The borrower must project a feasible plan after the consolidation. See § 762.102(b) for definition of feasible plan.

(2) Only OL may be consolidated.

(3) Existing lines of credit may only be consolidated with a new line of credit if the final maturity date and conditions for advances of the new line of credit are made the same as the existing line of credit.

(4) Guaranteed OL may not be consolidated with a line of credit, even if the line of credit has been rescheduled.

(5) Guaranteed loans made prior to October 1, 1991, cannot be consolidated with those loans made on or after October 1, 1991.

(6) OL secured by real estate or with an outstanding interest assistance agreement or shared appreciation agreement cannot be consolidated.

(7) A new note or line of credit agreement will be taken. The new note or line of credit agreement must describe the note or line of credit agreement being consolidated and must state that the indebtedness evidenced by the note or line of credit agreement is not satisfied. The original note or line of credit agreement must be retained.

(8) The interest rate for a consolidated OL loan is the negotiated rate agreed upon by the lender and the borrower at the time of the action, subject to the loan limitations for each type of loan.

(9) A modification of guarantee will be executed. The modification will indicate the consolidated loan amount, new terms, and percentage of guarantee, and will be attached to the originals of the guarantees being consolidated. If loans with a different guarantee percentage are consolidated, the new guarantee will be at the lowest percentage of guarantee being consolidated.

(10) Any holders must consent to the consolidation, or the guaranteed portion must be repurchased by the lender.

§ 762.147 Servicing shared appreciation agreements.

(a) *Lender responsibilities.* The lender is responsible for:

(1) Monitoring the borrower's compliance with the shared appreciation agreement;

(2) Notifying the borrower of the amount of recapture due; and,

(3) Beginning October 1, 1999, a notice of the agreement's provisions not later than 12 months before the end of the agreement; and

(4) Reimbursing the Agency for its pro-rata share of recapture due.

(b) *Recapture.*

(1) Recapture of any appreciation of real estate security will take place at the end of the term of the agreement, or sooner if the following occurs:

(i) On the conveyance of the real estate security (or a portion thereof) by the borrower.

(A) If only a portion of the real estate is conveyed, recapture will only be triggered against the portion conveyed. Partial releases will be handled in accordance with § 762.141(b).

(B) Transfer of title to the spouse of the borrower on the death of such borrower will not be treated as a conveyance under the agreement.

(ii) On repayment of the loan; or

(iii) If the borrower ceases farming.

(2) Calculating recapture.

(i) The amount of recapture will be based on the difference between the value of the security at the time recapture is triggered and the value of the security at the time of writedown, as shown on the shared appreciation agreement.

(ii) Security values will be determined through appraisals obtained by the lender and meeting the requirements of § 762.127.

(iii) All appraisal fees will be paid by the lender.

(iv) The amount of recapture will not exceed the amount of writedown shown on the shared appreciation agreement.

(v) If recapture is triggered within 4 years of the date of the shared appreciation agreement, the lender shall recapture 75 percent of any positive appreciation in the market value of the property securing the loan or line of credit agreement.

(vi) If recapture is triggered after 4 years from the date of the shared appreciation agreement, the lender shall recapture 50 percent of any positive appreciation in the market value of the property securing the loan or line of credit agreement.

(3) Servicing recapture debt.

(i) If recapture is triggered under the shared appreciation agreement and the borrower is unable to pay the recapture in a lump sum, the lender may:

(A) Reschedule the recapture debt with the consent of the Agency, provided the lender can document the borrower's ability to make amortized payments on the recapture debt, plus pay all other obligations. In such case, the recapture debt will not be covered by the guarantee;

(B) Pay the Agency its pro rata share of the recapture due. In such case, the recapture debt of the borrower will be covered by the guarantee; or

(C) Service the account in accordance with § 762.149.

(ii) If recapture is triggered, and the borrower is able but unwilling to pay the recapture in a lump sum, the lender will service the account in accordance with § 762.149.

(4) Paying the Agency. Any shared appreciation recaptured by the lender will be shared on a pro-rata basis between the lender and the Agency.

§ 762.148 Bankruptcy.

(a) *Lender responsibilities.* The lender must protect the guaranteed loan debt and all collateral securing the loan in bankruptcy proceedings. The lender's responsibilities include, but are not limited to:

(1) Filing a proof of claim where required and all the necessary papers and pleadings;

(2) Attending, and where necessary, participating in meetings of the creditors and court proceedings;

(3) Protecting the collateral securing the guaranteed loan and resisting any adverse changes that may be made to the collateral;

(4) Seeking a dismissal of the bankruptcy proceeding when the operation as proposed by the borrower to the bankruptcy court is not feasible;

(5) When permitted by the bankruptcy code, requesting a modification of any plan of reorganization if it appears additional recoveries are likely.

(6) Monitor confirmed plans under chapters 11, 12 and 13 of the bankruptcy code to determine borrower compliance. If the borrower fails to comply, the lender will seek a dismissal of the reorganization plan; and

(7) Keeping the Agency regularly informed in writing on all aspects of the proceedings.

(i) The lender will submit a default status report when the borrower defaults and every 60 days until the default is resolved or a final loss claim is paid.

(ii) The default status report will be used to inform the Agency of the bankruptcy filing, the reorganization plan confirmation date and effective date, when the reorganization plan is complete, and when the borrower is not in compliance with the reorganization plan.

(b) *Bankruptcy expenses.*

(1) Reorganization.

(i) Expenses, such as legal fees and the cost of appraisals incurred by the lender as a direct result of the borrower's chapter 11, 12, or 13 reorganization, are covered under the guarantee, provided they are reasonable, customary, and provide a demonstrated economic benefit to the lender and the Agency.

(ii) Lender's in-house expenses, which are those expenses which would normally be incurred for administration of the loan, including in-house lawyers, are not covered by the guarantee.

(2) Liquidation expenses in bankruptcy.

(i) Reasonable and customary liquidation expenses may be deducted from the proceeds of the collateral in liquidation bankruptcy cases.

(ii) In-house expenses are not considered customary liquidation expenses, may not be deducted from collateral proceeds, and are not covered by the guarantee.

(c) *Estimated loss claims in reorganization*.

(1) At confirmation. The lender may submit an estimated loss claim upon confirmation of the reorganization plan in accordance with the following:

(i) The estimated loss payment will cover the guaranteed percentage of the principal and accrued interest written off, plus any allowable costs incurred as of the effective date of the plan.

(ii) The lender will submit supporting documentation for the loss claim, and any additional information requested by the Agency, including justification for the legal fees included on the claim.

(iii) The estimated loss payment may be revised as consistent with a court-approved reorganization plan.

(iv) Protective advances made and approved in accordance with § 762.149 may be included in an estimated loss claim associated with a reorganization, if:

(A) They were incurred in connection with the initiation of liquidation action prior to bankruptcy filing; or

(B) The advance is required to provide repairs, insurance, etc. to protect the collateral as a result of delays in the case, or failure of the borrower to maintain the security.

(2) Interest only losses. The lender may submit an estimated loss claim for interest only after confirmation of the reorganization plan in accordance with the following:

(i) The loss claims may cover interest losses sustained as a result of a court-ordered, permanent interest rate reduction.

(ii) The loss claims will be processed annually on the anniversary date of the effective date of the reorganization plan.

(iii) If the borrower performs under the terms of the reorganization plan, annual interest reduction loss claims will be submitted on or near the same date, beyond the period of the reorganization plan.

(3) Actual loss.

(i) Once the reorganization plan is complete, the lender will provide the Agency with documentation of the actual loss sustained.

(ii) If the actual loss sustained is greater than the prior estimated loss payment, the lender may submit a revised estimated loss claim to obtain payment of the additional amount owed by the Agency under the guarantee.

(iii) If the actual loss is less than the prior estimated loss, the lender will reimburse the Agency for the overpayment plus interest at the note rate from the date of the payment of the estimated loss.

(4) Payment to holder. In reorganization bankruptcy, if a holder makes demand upon the Agency, the Agency will pay the holder interest to the plan's effective date. Accruing interest thereafter will be based upon the provisions of the reorganization plan.

(d) *Liquidation under the bankruptcy code.*

(1) Upon receipt of notification that a borrower has filed for protection under Chapter 7 of the bankruptcy code, or a liquidation plan under chapter 11, the lender must proceed according to the liquidation procedures of this part.

(2) If the property is abandoned by the trustee, the lender will conduct the liquidation according to § 762.149.

(3) Proceeds received from partial sale of collateral during bankruptcy may be used by the lender to pay reasonable costs, such as freight, labor and sales commissions, associated with the partial sale. Reasonable use of proceeds for this purpose must be documented with the final loss claim in accordance with § 762.149(a)(vi).

§ 762.149 Liquidation.

(a) *Mediation.* When it has been determined that default cannot be cured through any of the servicing options available, or if the lender does not wish to utilize any of the authorities provided in this part, the lender must:

(1) Participate in mediation according to the rules and regulations of any State which has a mandatory farmer-creditor mediation program;

(2) Consider private mediation services in those States which do not have a mandatory farmer-creditor mediation program; and

(3) Not agree to any proposals to rewrite the terms of a guaranteed loan which do not comply with this part. Any agreements reached as a result of mediation involving defaults and or loan restructuring must have written concurrence from the Agency before they are implemented.

(b) *Liquidation plan.* If a default cannot be cured after considering servicing options and mediation, the lender will proceed with liquidation of the collateral in accordance with the following:

(1) Within 30 days of the decision to liquidate, standard eligible and CLP lenders will submit a written liquidation plan to the Agency which includes:

(i) Current balance sheets from all liable parties or, if the parties are not cooperative, the best information available, or in liquidation bankruptcies, a copy of the bankruptcy schedules or discharge notice;

(ii) A proposed method of maximizing the collection of debt which includes specific plans to collect any remaining loan balances on the guaranteed loan after loan collateral has been liquidated, including possibilities for judgment;

(A) If the borrower has converted loan security, the lender will determine whether litigation is cost effective. The lender must address, in the liquidation plan, whether civil or criminal action will be pursued. If the lender does not pursue the recovery, the reason must be documented when an estimated loss claim is submitted.

(B) Any proposal to release the borrower from liability will be addressed in the liquidation plan in accordance with § 762.146(c)(2);

(iii) An independent appraisal report on all collateral securing the loan that meets the requirements of § 762.127 and a calculation of the net recovery value of the security as defined in § 762.102. The appraisal requirement may be waived by the Agency in the following cases:

(A) The bankruptcy trustee is handling the liquidation and the lender has submitted the trustee's determination of value;

(B) The lender's proposed method of liquidation rarely results in receipt of less than market value for livestock and used equipment; or

(C) A purchase offer has already been received for more than the debt;

(iv) An estimate of time necessary to complete the liquidation;

(v) An estimated loss claim if the liquidation period is expected to exceed 90 days.

(vi) An estimate of reasonable liquidation expenses; and

(vii) An estimate of any protective advances.

(2) PLP lenders will submit a liquidation plan as required by their lender's agreement.

(c) *Agency approval of the liquidation plan.*

(1) CLP lender's or standard eligible lender's liquidation plan, and any

revisions of the plan, must be approved by the Agency.

(2) If, within 20 calendar days of the Agency's receipt of the liquidation plan, the Agency fails to approve it or fails to request that the lender make revisions, the lender may assume the plan is approved. The lender may then proceed to begin liquidation actions at its discretion as long as it has been at least 60 days since the borrower's eligibility for interest assistance was considered.

(3) At its option, the Agency may liquidate the guaranteed loan as follows:

(i) Upon Agency request, the lender will transfer to the Agency all rights and interests necessary to allow the Agency to liquidate the loan. The Agency will not pay the lender for any loss until after the collateral is liquidated and the final loss is determined; and

(ii) If the Agency conducts the liquidation, interest accrual will cease on the date the Agency notifies the lender in writing that it assumes responsibility for the liquidation.

(d) *Estimated loss claims.* An estimated loss claim will be submitted by the lender with the liquidation plan if the liquidation is expected to exceed 90 days. The estimated loss will be based on the following:

(1) The Agency will pay the lender the guaranteed percentage of the total outstanding debt, less the net recovery value of the remaining security, less any unaccounted for security; and

(2) The lender will discontinue interest accrual on the defaulted loan at the time the estimated loss claim is paid by the Agency. If the lender estimates that there will be no loss after considering the costs of liquidation, interest accrual will cease 90 days after the decision to liquidate or an estimated loss of zero will be submitted.

(e) *Protective advances.*

(1) Prior written authorization from the Agency is required for all protective advances in excess of $5,000 for CLP lenders and $3,000 for standard eligible lenders. The dollar amount of protective advances allowed for PLP lenders will be specified when PLP status is awarded by the Agency or as contained in the lender's agreement.

(2) The lender may claim recovery for the guaranteed portion of any loss of monies advanced as protective advances as allowed in this part, plus interest that accrues on the protective advances.

(3) Payment for protective advances is made by the Agency when the final loss claim is approved, except in bankruptcy actions.

(4) Protective advances are used only when the borrower is in liquidation, liquidation is imminent, or when the lender has taken title to real property in a liquidation action.

(5) Legal fees are not a protective advance.

(6) Protective advances may only be made when the lender can demonstrate the advance is in the best interest of the lender and the Agency.

(7) Protective advances must constitute a debt of the borrower to the lender and be secured by the security instrument.

(8) Protective advances must not be made in lieu of additional loans.

(f) *Unapproved loans or advances.* The amount of any payments made by the borrower on unapproved loans or advances outside of the guarantee will be deducted from any loss claim submitted by the lender on the guaranteed loan, if that loan or advance was paid prior to, and to the detriment of, the guaranteed loan.

(g) *Acceleration.*

(1) If the borrower is not in bankruptcy, the lender shall send the borrower notice that the loan is in default and the entire debt has been determined due and payable immediately after other servicing options have been exhausted.

(2) The loan cannot be accelerated until after the borrower has been considered for interest assistance and the conclusion of mandatory mediation in accordance with § 762.149.

(3) The lender will submit a copy of the acceleration notice or other document to the Agency.

(h) *Foreclosure.*

(1) The lender is responsible for determining the necessary parties to any foreclosure action, or who should be named on a deed of conveyance taken in lieu of foreclosure.

(2) When the property is liquidated, the lender will apply the net proceeds to the guaranteed loan debt.

(3) When it is necessary to enter a bid at a foreclosure sale, the lender may bid the amount that it determines is reasonable to protect its and the Agency's interest. At a minimum, the lender will bid the lesser of the net recovery value or the unpaid guaranteed loan balance.

(i) *Final loss claims.*

(1) Lenders may submit a final loss claim when the security has been liquidated and all proceeds have been received and applied to the account.

(2) If a lender acquires title to property either through voluntary conveyance or foreclosure proceeding, the lender will submit a final loss claim after disposing of the property. The lender may pay reasonable maintenance expenses to protect the value of the property while it is owned by the lender. These may be paid as protective advances or deducted as liquidation expenses from the sales proceeds when the lender disposes of the property. The lender must obtain Agency written concurrence before incurring maintenance expenses which exceed the amounts allowed in § 762.149(e)(1).

(3) The lender will make its records available to the Agency for the Agency's audit of the propriety of any loss payment.

(4) All lenders will submit the following documents with a final loss claim:

(i) An accounting of the use of loan funds;

(ii) An accounting of the disposition of loan security and its proceeds;

(iii) A copy of the loan ledger indicating loan advances, interest rate changes, protective advances, and application of payments, rental proceeds, and security proceeds, including a running outstanding balance total; and

(iv) Documentation, as requested by the Agency, concerning the lender's compliance with the requirements of this part.

(5) The Agency will notify the lender of any discrepancies in the final loss claim or, approve or reject the claim within 40 days.

(6) The Agency will reduce a final loss claim based on its calculation of the dollar amount of loss caused by the lender's negligent servicing of the account. Loss claims may be reduced or rejected as a result of the following:

(i) A loss claim may be reduced by the amount caused by the lender's failure to secure property after a default, and will be reduced by the amount of interest that accrues when the lender fails to contact the borrower or takes no action to cure the default, once it occurs. Losses incurred as a result of interest accrual during excessive delays in collection, as determined by the Agency, will not be paid.

(ii) Unauthorized release of security proceeds, failure to verify ownership or possession of security to be purchased, or failure to inspect collateral as often required so as to ensure its maintenance.

(7) Losses will not be reduced for the following:

(i) Servicing deficiencies that did not contribute materially to the dollar amount of the loss.

(ii) Unaccounted security, as long as the lender's efforts to locate and recover the missing collateral was equal to that which would have been expended in the case of an unguaranteed loan in the lender's portfolio.

(8) Default interest, late charges, and loan servicing fees are not payable under the loss claim.

(9) The final loss will be the remaining outstanding balance after application of the estimated loss payment and the application of proceeds from the liquidation of the security.

(10) If the final loss is less than the estimated loss, the lender will reimburse the Agency for the overpayment, plus interest at the note rate from the date of the estimated loss payment.

(11) The lender will return the original guarantee marked paid after receipt of a final loss claim.

(j) *Future Recovery.* The lender will remit any recoveries made on the account after the Agency's payment of a final loss claim to the Agency in proportion to the percentage of guarantee, in accordance with the lender's agreement, until the account is paid in full or otherwise satisfied.

(k) *Overpayments.* The lender will repay any final loss overpayment determined by the Agency upon request.

(l) *Electronic funds transfer.* The lender will designate one or more financial institutions to which any Agency payments will be made via electronic funds transfer.

§ 762.150 Interest assistance program.

(a) *Requests for interest assistance.*

(1) To apply for interest assistance in conjunction with a new request for guarantee, the lender will submit the following:

(i) A completed cash flow projection and interest assistance needs analysis portion of the application form. Interest assistance can be applied to each loan, only to one loan or any distribution the lender selects; however, interest assistance is only available on as many loans as necessary to achieve a positive cash flow.

(ii) For loans with unequal payments, a proposed debt repayment schedule which shows principal and interest payments for the subject loan, in each year of the loan.

(2) To request interest assistance on an existing guaranteed loan, the lender must submit to the Agency the following:

(i) A completed cash flow projection and interest assistance needs analysis portion of the application form. Interest assistance can be applied to each loan, only to one loan or any distribution the lender selects as required to achieve a feasible plan.

(ii) For loans with unequal payments, a proposed debt repayment schedule which shows scheduled payments for the subject loan in each of the remaining years of the loan.

(iii) Cash flow budgets and supporting justification to document that the request meets the requirements outlined in paragraph (b) of this section. This will include a typical cash flow if the projected cash flow budget is atypical.

(3) Requests for interest assistance on lines of credit or loans made for annual operating purposes must be accompanied by a projected monthly cash flow budget.

(b) *Requirements.*

(1) The typical term of scheduled loan repayment will not be reduced solely for the purpose of maximizing eligibility for interest assistance. To be eligible for interest assistance, a loan must be scheduled over the maximum terms typically used by lenders for similar type loans within the limits set by § 762.124 of this part. At a minimum, loans will be scheduled for repayment over the terms listed below, but for OL not to exceed the life of the security:

(i) An OL for the purpose of providing annual operating and living expenses will be scheduled for repayment when the income is scheduled to be received from the sale of the crops, livestock, and livestock products which will serve as security for the loan.

(ii) OL for purposes other than annual operating and living expenses (i.e. equipment, livestock, refinancing of existing debt) will be scheduled over 7 years from the effective date of the proposed interest assistance agreement.

(iii) FO and SW secured by real estate will be scheduled for 20 years from the closing date of the original note covered by the guarantee.

(2) The lender must document that positive cash flow, as defined in § 762.102(b), is not possible without reducing the interest rate on the borrower's loan and with the debt restructured over the term of repayment cited above.

(3) The lender must determine whether the borrower, including members of an entity, owns any significant assets which do not contribute directly to essential family living or farm operations. The lender must determine the market value of these assets and prepare a cash flow budget based on the assumption that the value of these assets will be used for debt reduction. If a positive cash flow can then be achieved, the borrower is not eligible for interest assistance. All interest assistance calculations will be based on the cash-flow budget which assumes that the assets will be sold.

(4) A borrower's new guaranteed loan is eligible for interest assistance if all the following conditions are met:

(i) The applicant needs interest assistance in order to achieve a positive cash flow as defined in § 762.102(b).

(ii) If significant changes in the borrower's cash flow budget are anticipated after the initial 12 months, then the typical cash flow budget must demonstrate that the borrower will still have a feasible plan, as defined in § 762.102(b), following the anticipated changes, with or without interest assistance.

(iii) If a positive cash flow cannot be achieved, even with other creditors voluntarily adjusting their debts and with the interest assistance, the interest assistance request will not be approved.

(5) An existing guaranteed loan is eligible for interest assistance if the borrower needs interest assistance to achieve a feasible plan as defined in § 762.102(b), and the borrower meets the eligibility criteria of § 762.120, except the provision regarding prior debt forgiveness. If a feasible plan cannot be achieved, even with other creditors voluntarily adjusting their debts and with the interest assistance, the interest assistance request will not be approved. If a borrower has multiple loans, interest assistance may be provided on one or each loan, as available, to the extent necessary to achieve a feasible plan.

(6) The term of the interest assistance agreement under this section shall not exceed 10 years from the date of the first interest assistance agreement signed by the loan applicant, including entity members, or the outstanding term of the loan, as limited by this section, whichever is less.

(7) The lender may charge a fixed or variable interest rate. The type of rate must be the same as the type of rate in the underlying note or line of credit agreement. The lender will reduce the interest rate charged the borrower's account by at least the amount of interest assistance.

(8) The borrower must be an operator of not larger than a family size farm.

(c) *Interest assistance closing.*

(1) Initial guaranteed loans will be closed in accordance with § 762.130.

(2) The lender will then prepare and deliver to the Agency a closing report for each initial and existing guaranteed loan which has been granted interest assistance.

(3) When all requirements have been met, the lender and the Agency will execute an interest assistance agreement.

(d) *Interest assistance claims and payments.*

(1) The interest assistance claim will be prepared by the lender. The following conditions apply to the claims process:

(i) No claim period can exceed 12 months. The initial and final claim periods may be less than 12 months. In such claims, the 4 percent payment will be prorated over the number of months in the claim period. The period for all other claims must be 12 months.

(ii) To permit the borrower to prepare for the upcoming year, a claim should be filed within 60 days of each anniversary date. Claims not filed within 1 year of the anniversary date will not be paid and the amount due the lender is permanently forfeited.

(iii) If a claim is submitted without an interest assistance review in accordance with § 762.102, when it is required, the claim will not be processed until the review is submitted by the lender.

(iv) Upon full payment of the note or line of credit, the lender will immediately prepare the request for interest assistance payment and submit it to the Agency.

(v) Interest assistance payments shall cease upon the assumption and transfer of the loan if the transferee was not liable for the debt on the effective date of the interest assistance agreement. The lender shall request payment through the date of the transfer or assumption. The claim must be submitted within 1 year or it will be denied and the payment permanently forfeited.

(vi) All claims will be supported by detailed calculations of average daily principal balances during the claim period.

(vii) The Agency will review the claim and the supporting documentation. If the information and the supporting documentation is not complete and correct, the reviewing official will notify the lender in writing, of the actions needed to correct the request.

(viii) If there is a substitution of lender, a claim for the first lender's interest assistance, through the effective date of the substitution, will be submitted by the first lender and processed at the time of the substitution.

(ix) Interest assistance claims shall be submitted concurrently with the submission of estimated loss claims where interest accrual ceases, or final loss claims that are not preceded by an estimated loss claim.

(2) [Reserved]

(e) *Request for continuation of interest assistance.*

(1) For all interest assistance agreements exceeding 12 months, the lender will perform an analysis of the applicant's farming operation and need for continued interest assistance. The following information will be submitted to the Agency:

(i) A summary of the operation's actual financial performance in the previous year, including a detailed income and expense statement.

(ii) A narrative description of the causes of any major differences between the previous year's projections and actual performance.

(iii) A current balance sheet.

(iv) A cash flow budget for the period being planned. A monthly cash flow budget is required for all lines of credit and operating loans made for annual operating purposes. All other loans may include either an annual or monthly cash flow budget.

(v) A copy of the interest assistance needs analysis portion of the application form which has been completed based on the planned period's cash flow budget.

(2) The loan will be eligible for continuation of interest assistance if a feasible plan, including interest assistance, can be projected for the plan period. If the evaluation indicates that the borrower needs a level of interest assistance greater than 4 percent to project a feasible plan, then the Agency will deny the continuation of interest assistance. interest assistance will be reduced to zero during that review period. See § 762.102(b) for the definition of feasible plan.

(3) The documentation listed above will be provided to the Agency concurrently with the lender's submission of its request for interest assistance payment. This information will be provided to the Agency within 60 days after the review date specified on the interest assistance agreement.

(4) A request for continuation of interest assistance will be completed for 12 month periods, effective on the anniversary date.

(5) The initial review may be submitted in conjunction with any claim within the initial 12 month period. The anniversary date and length of the review period will be stated on the interest assistance agreement. Any request for interest assistance adjustment submitted effective any time other than the review date will be denied, except for those cases where it is necessary to service the loan with rescheduling, reamortization, deferral or writedown.

(6) If the review is not completed and submitted to the Agency within 1 year of the review date, no claim will be paid for that period.

(f) *Notification of Adverse Action.* The lender will be notified in writing of all Agency decisions in which a request for interest assistance, a request for continuation of interest assistance or lender's claim for interest assistance are denied. The notification letter will provide specific reasons for the decision and appeals will be handled in accordance with parts 11 and 780 of this title.

(g) *Servicing of loans covered by an interest assistance agreement.*

(1) Loans covered by interest assistance agreements cannot be consolidated.

(2) The loan will be transferred with the interest assistance agreement only in cases where the transferee was liable for the debt at the time interest assistance was granted. Under no other circumstances will the interest assistance be transferred. If interest assistance is necessary for the transferee to achieve a positive cash flow, the lender may request such assistance, which may be approved if interest assistance funds are available and the applicant is eligible. The maximum length of the agreement will be 10 years from the date of the first agreement covering a loan for which the transferee was liable. If interest assistance is necessary for a positive cash flow and funds are not available, the request for assumption of the Agency guaranteed debt will be denied.

(3) When consideration is given to using a debt writedown to service a delinquent account, the subsidy level will be recalculated prior to any writedown. If a feasible plan can be obtained using interest assistance and funds are available, then the interest assistance will be authorized and no writedown will be approved. If a feasible plan cannot be achieved using 4 percent interest assistance, all further calculations for determining debt writedown eligibility and amounts to be written down will be based on the borrower receiving no interest assistance. If debt writedown is approved, the interest assistance claim for the previous review period will be processed in conjunction with the writedown loss claim. The interest assistance agreement will not be canceled and the anniversary date can remain the same or be re-established under the same guidelines that it was originally established. If the lender determines through its annual analysis that interest assistance is necessary for a feasible plan, a request to reinstate the subsidy in a subsequent review period may be submitted in accordance with paragraph (e) of this section.

(4) In the event of rescheduling or deferral of loans with interest assistance, interest assistance will remain available for that loan under the terms of the existing interest assistance agreement. Additional years of interest assistance and/or increases in the

restructured loan amount will require additional funding. If the additional interest assistance is needed in order to produce a feasible plan throughout the life of the rescheduled loan and funds are not available for the additional interest assistance, then the rescheduling will not be approved by the Agency. In no case will the subsidy be extended more than 10 years from the effective date of the first interest assistance agreement signed by the loan applicant or by anyone who signed the note or line of credit agreement. Rescheduling or deferral will only be processed in conjunction with a claim, effective on the claim date or anniversary date. A review will be completed, in accordance with paragraph (e)(1) of this section. The anniversary date can remain the same or be re-established under the same guidelines that it was originally established.

(5) In cases where the interest on a loan covered by an interest assistance agreement is reduced by court order in a reorganization plan under the bankruptcy code, interest assistance agreement will be terminated effective on the date of the court ordered interest reduction. The lender will file a claim due through the effective date of the court ordered interest reduction. Guaranteed loans which have had their interest reduced by bankruptcy court order are not eligible to receive interest assistance.

(6) For Loan Guarantees held by holders, Agency purchase of the guaranteed portion of a loan will stop interest assistance payments on that portion. Interest assistance payments will cease upon termination of the Loan Guarantee, upon reaching the expiration date contained in the agreement or upon cancellation by the Agency.

(7) When a borrower defaults on a loan, interest assistance may be considered in conjunction with a rescheduling action in accordance with § 762.145(b). After the meeting required by § 762.143(b)(3) and consideration of actions to correct the delinquency, the lender will notify the Agency of the results of the meeting. If the restructuring proposal includes interest assistance, the lender will provide the items required by paragraph (d) of this section in addition to those items required by § 762.145. Liquidation must not be initiated, except in accordance with § 762.145(b)(3)(v).

(h) *Cancellation of interest assistance agreement.* The interest assistance agreement is incontestable except for fraud or misrepresentation, of which the lender and borrower have actual knowledge at the time that the interest assistance agreement is executed, or which the lender or borrower participates in or condones.

(i) *Adjustment of assistance level between review dates.* After the initial or renewal request for interest assistance is processed, no adjustments can be made until the next review or adjustment date except when necessary to service the loan with a rescheduling or deferral.

(j) *Excessive interest assistance.* Upon written notice to the lender, borrower and any holder, the Agency may amend or cancel the interest assistance agreement and collect from the lender any amount of interest Assistance granted which resulted from incomplete or inaccurate information, an error in computation, or any other reason which resulted in payment that the lender was not entitled to receive.

(k) The Deputy Administrator for Farm Loan Programs has the authority to grant an exception to any requirement involving interest Assistance if it is in the best interest of the Government.

§§ 762.151–762.159 [Reserved].

§ 762.160 Sale, assignment and participation.

(a) The following general requirements apply to selling, assigning or participating guaranteed loans.

(1) Subject to Agency concurrence, the lender may sell, assign or participate all or part of the guaranteed portion of the loan to one or more holders at or after loan closing, only if the loan is not in default. However, a line of credit can be participated, but not sold or assigned.

(2) The Agency may refuse to execute the Assignment of Guarantee and prohibit the sale in case of the following:

(i) The Agency purchased and is holder of a loan that was sold by the lender that is requesting the assignment.

(ii) The lender has not complied with the reimbursement requirements of § 762.146(c)(7), except when the 180 day reimbursement or liquidation requirement has been waived by the Agency.

(3) The lender will provide the Agency with copies of all appropriate forms used in the sale or assignment.

(4) The guaranteed portion of the loan may not be sold or assigned by the lender until the loan has been fully disbursed to the borrower, except a line of credit may be participated prior to being fully advanced.

(5) The lender is not permitted to sell, assign or participate any amount of the guaranteed or unguaranteed portion of loan to the loan applicant or borrower, or members of their immediate families, their officers, directors, stockholders, other owners, or any parent, subsidiary, or affiliate.

(6) Upon the lender's sale or assignment of the guaranteed portion of the loan, or participation of the line of credit, the lender will remain bound to all obligations indicated in the Guarantee, lender's agreement, the Agency program regulations, and to future program regulations not inconsistent with the provisions of the Lenders agreement. The lender retains all rights under the security instruments for the protection of the lender and the United States.

(b) The following will occur upon the lender's sale or assignment of the guaranteed portion of the loan:

(1) The holder will succeed to all rights of the Guarantee pertaining to the portion of the loan purchased.

(2) The lender will send the holder the borrower's executed note attached to the Guarantee.

(3) The holder, upon written notice to the lender and the Agency, may assign the unpaid guaranteed portion of the loan. The holder must sell the guaranteed portion back to the original lender if requested for servicing or liquidation of the account.

(4) The guarantee or assignment of guarantee in the holder's possession does not cover:

(i) Interest accruing 90 days after the holder has demanded repurchase by the lender, except as provided in the assignment of guarantee and § 762.144(c)(3)(iii).

(ii) Interest accruing 90 days after the lender or the Agency has requested the holder to surrender evidence of debt repurchase, if the holder has not previously demanded repurchase.

(c) In a participation, the lender sells an interest in a loan but retains the note, the collateral securing the note, and all responsibility for loan servicing and liquidation. The guarantee does not encompass the participant.

(1) The lender must retain at least 10 percent of the total guaranteed loan amount from the unguaranteed portion of the loan in its portfolio, except when the loan guarantee exceeds 90 percent, the lender must retain the total unguaranteed portion.

(2) Participation with a lender by any entity does not make that entity a holder or a lender as defined in this part.

(d) Negotiations concerning premiums, fees, and additional payments for loans are to take place between the holder and the lender. The Agency will participate in such negotiations only as a provider of information.

7 CFR Chapter XVIII

PART 1980—GENERAL

2. The authority citation for part 1980 continues to read as follows:

Authority: 5 U.S.C. 301; 7 U.S.C. 1989; 42 U.S.C. 1480.

Subpart A—General

3. Revise § 1980.1 to read as follows:

§ 1980.1 Purpose.

This subpart contains the general regulations and prescribed forms which are applicable to Community Programs Guaranteed Loans under subpart I of this part.

4. Amend § 1980.6 as follows:

a. Remove in paragraph (a) the definitions of ''Conditional Commitment (Farmer Programs) (Form FmHA or its successor agency under Pub.L.103–354 1980–15),'' ''Contract of Guarantee (Line of Credit)(Form FmHA or its successor agency under Pub.L. 103–354 1980–27),'' ''Guaranteed line of credit,'' and ''Line of credit agreement'';

b. Remove in paragraph (a), in the definition of ''Guaranteed loan,'' the phrase ''or Form FmHA 1980–38,'';

c. Remove in paragraph (b), the abbreviations ''ASCS,'' ''CLP,'' ''EM,'' ''FO,'' ''OL,'' ''OL–Y,'' ''RL,'' and ''SW''; and

d. In paragraph (a), remove the definition of ''Lender's Agreement (Forms FmHA or its successor agency under Pub.L. 103–354 449–35 or 1980–38)'' and add a new definition to read as follows:

§ 1980.6 Definitions and abbreviations.

(a) * * *

Lender's Agreement (Form RD 449–35). The signed agreement between Rural Development and the lender setting forth the lender's loan responsibilities when the Loan Note Guarantee is issued.

* * * * *

§ 1980.11 [Amended]

5. Amend § 1980.11 as follows:

a. In the first sentence, remove the phrase ''and Contract of Guarantee'' and revise the word ''constitute'' to read ''constitutes'';

b. In the second sentence, remove the phrase '', Contract of Guarantee'';

c. In the fifth sentence, remove the phrase ''or Contract of Guarantee''; and

d. Remove the third and sixth sentences.

6. Amend § 1980.13 as follows:

a. In the introductory text to paragraph (b), remove the fourth sentence; and

b. Revise the introductory text of paragraph (b)(4) to read as follows:

§ 1980.13 Eligible lenders.

* * * * *

(b) * * *

(4) *Conflict of interest.* The Agency shall determine whether such ownership or business dealings are sufficient to result in a conflict of interest or an apparent conflict of interest. All lenders will, for each proposed loan, inform the Agency in writing and furnish such additional evidence as the Agency requests as to whether and the extent for those loans covered by Form RD 449–35, the lender or its principals or officers (including immediate family) or the borrower or its principals or officers (including immediate family) hold any stock or other evidence of ownership in the other.

* * * * *

7. Revise the last sentence of the introductory text of § 1980.20(a) to read as follows:

§ 1980.20 Loan guarantee limits.

(a) * * * Also, the maximum loss covered by Form RD 449–34 (available in any Agency office) can never exceed the lesser of:

* * * * *

8. Revise § 1980.21 to read as follows:

§ 1980.21 Guarantee fee.

The fee will be the applicable rate multiplied by the principal loan amount multiplied by the percent of guarantee, paid one time only at the time the Loan Note Guarantee is issued.

(a) The fee will be paid to the Agency by the lender and is nonreturnable. The lender may pass on the fee to the borrower.

(b) Guarantee fee rates are specified in exhibit K of RD Instruction 440.1 (available in any Rural Development Office).

9. Amend § 1980.22 as follows:

a. In the introductory text of paragraph (b) and in paragraph (b)(3), remove the phrase ''or Contract of Guarantee''; and

b. Revise paragraph (a) to read as follows:

§ 1980.22 Charges and fees by lender.

(a) *Routine charges and fees.* The lender may establish the charges and fees for the loan, provided they are the same as those charged other applicants for similar types of transactions. ''Similar types of transactions'' means those transactions involving the same type of loan requested for which a non-guaranteed loan applicant would be assessed charges and fees.

* * * * *

§ 1980.46 [Removed and reserved]

10. § 1980.46 is removed and reserved.

§ 1980.60 [Amended]

11. Amend § 1980.60 as follows:

a. In the heading, remove the phrase ''or Contract of Guarantee'';

b. In the introductory text of paragraph (a), in the second sentence, remove the phrase ''For all other loans, Form FmHA or its successor agency under Public Law 103–354'' to read and in its place add ''Form'',

c. In paragraph (a)(1), remove the phrases ''or line of credit'' and ''or Conditional Commitment for Contract of Guarantee'' and revise the phrase ''FmHA or its successor agency under Public Law 103–354'' to read ''the Agency'';

d. In paragraphs (a)(6) and (a)(7), remove the phrases ''or line of credit'';

e. In paragraph (a)(9), remove the phrase ''joint operation, (for Farmer Program loans only),'';

f. In paragraphs (a)(10) and (a)(11), remove the phrases ''or Conditional Commitment for Contract of Guarantee'';

g. In paragraph (a)(12), remove the second sentence;

h. In paragraph (b), remove the phrase ''or Contract of Guarantee''; and

i. In paragraph (c), remove the phrase ''or Form FmHA or its successor agency under Public Law 103–354 1980–38'' at the end.

§ 1980.61 [Amended]

12. Amend § 1980.61 as follows:

a. In the heading, remove the phrase ''Contract of Guarantee'';

b. In the first sentence of paragraph (a)(1), remove the phrase ''Except for Farmer Programs loans, the'' and add in its place ''The'';

c. Remove paragraph (a)(2) and redesignate paragraph (a)(3) as paragraph (a)(2);

d. In newly redesignated paragraph (a)(2), remove the phrase ''or Contract of Guarantee;''

e. In paragraph (b)(1) remove the phrase ''or Form FmHA or its successor agency under Public Law 103–354 1980–38'';

f. In paragraphs (b)(3) and (4), remove the phrases ''or § 1980.119 of subpart B of this part,'';

g. Remove paragraph (c) and redesignate paragraphs (d) through (h) as paragraphs (c) through (g), respectively;

h. In newly redesignated paragraph (c), remove the last sentence;

i. In newly redesignated paragraph (d), remove the phrase ''or Contract of Guarantee'' from the first sentence;

j. In newly redesignated paragraph (f), remove the phrase ''or Contract of Guarantee''

k. In newly redesignated paragraph (g), remove the phrases ''or Form FmHA or its successor agency under Public Law 103–354 1980–38'' and ''the Contract of Guarantee,'' from the last sentence.

§ 1980.62 [Amended]

13. Amend § 1980.62 as follows:

a. In the first and third sentences, remove the phrase ''or § 1980.119 of subpart B of this part''; and

b. Remove the last sentence.

§ 1980.63 [Amended]

14. Amend § 1980.63(a) to remove the phrase ''or I.D.6. of Form FmHA or its successor agency under Public Law 103–354 1980–38''.

§ 1980.64 [Amended]

15. Amend § 1980.64 as follows:

a. In paragraph (a), remove the phrase ''or paragraph I.D.6. of Form FmHA or its successor agency under Public Law 103–354 1980–38''; and

b. In paragraph (b), remove the phrase ''or line of credit'' wherever it occurs in the first sentence.

§ 1980.65 [Amended]

16. Amend § 1980.65 to remove the phrase '', or for Farmer Programs Loans, § 1980.136 of subpart B of this part''.

§ 1980.66 [Amended]

17. Amend § 1980.66 to remove the phrase '', or paragraph I.D.6.(b) of Form FmHA or its successor agency under Public Law 103–354 1980–38''.

§ 1980.67 [Amended]

18. Amend § 1980.67 as follows:

a. In paragraph (a), remove the first sentence; and

b. In paragraph (b), remove the phrase ''or line of credit''.

§ 1980.68 [Amended]

19. Amend § 1980.68 as follows:

a. In the heading, remove the phrase ''or Contract of Guarantee'';

b. In the first sentence, remove the phrase ''or Contract(s) of Guarantee'';

c. In the second sentence in the parentheticals, remove the phrase '', or paragraph 6 of Form FmHA or its successor agency under Public Law 103–354 1980–27'';

d. In the third sentence, remove the phrases ''or line(s) of credit,'' ''or Contract(s) of Guarantee,'' and ''or Form FmHA or its successor agency under Public Law 103–354 1980–27''; and

e. Remove the last two sentences.

§ 1980.83 [Amended]

20. Amend § 1980.83 (a) to remove the second sentence.

§ 1980.84 [Amended]

21. Amend § 1980.84 as follows:

a. In the heading, remove the phrase ''or line of credit'';

b. Remove the phrases ''Contract of Guarantee'' and ''or Contract of Guarantee'' from the first sentence of paragraph (b)(1)(iv);

b. Remove the phrase ''Contract of Guarantee'' from paragraph (b)(1)(v); and

c. Remove the phrase ''or § 1980.119 of subpart B of this part'' from the first and fourth sentences in paragraph (b)(4).

Appendices D–L to Subpart A [Removed]

22. Amend part 1980, subpart A by removing Appendices D through L.

Subpart B [Removed and reserved]

23. Subpart B (§§ 1980.101–1980.200 and Exhibits A through G) is removed and reserved.

Signed in Washington, D.C., on January 19, 1999.

James W. Schroeder,

Acting Under Secretary for Farm and Foreign Agricultural Services.

Jill Long-Thompson,

Under Secretary for Rural Development.

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