DEPARTMENT OF AGRICULTURE

Rural Utilities Service

7 CFR Part 1779

Rural Housing Service

7 CFR Part 3575

Rural Business-Cooperative Service

Rural Utilities Service

7 CFR Parts 4279 and 4280

Rural Business-Cooperative Service

Rural Housing Service

Rural Utilities Service

7 CFR Part 5001

RIN 0570–AA65

Rural Development Guaranteed Loans

AGENCIES: Rural Business-Cooperative Service, Rural Housing Service, Rural Utilities Service, USDA.

ACTION: Interim rule with request for comments.

SUMMARY: This interim rule establishes a unified guaranteed loan platform for the enhanced delivery of four existing Rural Development guaranteed loan programs—Community Facility; Water and Waste Disposal; Business and Industry; and Renewable Energy Systems and Energy Efficiency Improvement Projects. This interim rule eliminates the existing loan guarantee regulations for these four programs and consolidates them under a new, single part. In addition to consolidating these four programs, this interim rule incorporates provisions that will enable the Agency to better manage the risk associated with making and servicing guaranteed loans and that will reduce the cost of operating the guaranteed loan programs.

DATES: This interim rule is effective January 16, 2009. Comments must be received on or before February 17, 2009.

ADDRESSES: You may submit comments to this rule by any of the following methods:

• *Federal eRulemaking Portal: http://www.regulations.gov*. Follow the instructions for submitting comments.

• *Mail:* Submit written comments via the U.S. Postal Service to the Branch Chief, Regulations and Paperwork Management Branch, U.S. Department of Agriculture, STOP 0742, 1400 Independence Avenue, SW., Washington, DC 20250–0742.

• *Hand Delivery/Courier:* Submit written comments via Federal Express Mail or other courier service requiring a street address to the Branch Chief, Regulations and Paperwork Management Branch, U.S. Department of Agriculture, 300 7th Street, SW., 7th Floor, Washington, DC 20024.

All written comments will be available for public inspection during regular work hours at the 300 7th Street, SW., 7th Floor address listed above.

FOR FURTHER INFORMATION CONTACT: Mr. Michael Foore, Rural Development, Business and Cooperative Programs, U.S. Department of Agriculture, 1400 Independence Avenue, SW., Stop 3201, Washington, DC 20250–3201; e-mail: *Michael.Foore@wdc.usda.gov*; telephone (202) 690–4730.

SUPPLEMENTARY INFORMATION:

Executive Order 12866

This interim rule has been determined to be significant and was reviewed by the Office of Management and Budget in conformance with Executive Order 12866. The Agency conducted a qualitative benefit cost analysis to fulfill the requirements of Executive Order 12866. Based on the results of this qualitative analysis of the benefits and costs of the interim rule, the Agency has concluded that the net effect of the rule will be beneficial in part due to improved underwriting. Copies of the benefit cost analysis may be obtained from Cheryl Thompson, Regulations and Paperwork Management Branch, Support Services Division, U.S. Department of Agriculture, Rural Development, STOP 0742, 1400 Independence Ave., SW., Washington, DC 20250–0742 or by calling (202) 692–0043.

Unfunded Mandates Reform Act

Title II of the Unfunded Mandates Reform Act of 1995 (UMRA) of Public Law 104–4 establishes requirements for Federal agencies to assess the effects of their regulatory actions on State, local, and tribal governments and the private sector. Under section 202 of the UMRA, Rural Development generally must prepare a written statement, including a cost-benefit analysis, for proposed and final rules with ''Federal mandates'' that may result in expenditures to State, local, or tribal governments, in the aggregate, or to the private sector of $100 million or more in any one year. When such a statement is needed for a rule, section 205 of UMRA generally requires Rural Development to identify and consider a reasonable number of regulatory alternatives and adopt the least costly, more cost-effective, or least burdensome alternative that achieves the objectives of the rule. This interim rule contains no Federal mandates (under the regulatory provisions of 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 the UMRA.

Environmental Impact Statement

This document has been reviewed in accordance with 7 CFR part 1940, subpart G, ''Environmental Program.'' Rural Development has determined that this action does not constitute a major Federal action significantly affecting the quality of the human environment, and in accordance with the National Environmental Policy Act (NEPA) of 1969, 42 U.S.C. 4321 *et seq.*, an Environmental Impact Statement is not required. Loan applications will be reviewed individually to determine compliance with NEPA.

Executive Order 12988, Civil Justice Reform

This interim rule has been reviewed under Executive Order 12988, Civil Justice Reform. In accordance with this rule:

(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 this rule; and

(3) Administrative proceedings in accordance with the regulations of the Department of Agriculture National Appeals Division (7 CFR part 11) must be exhausted before bringing suit in court challenging action taken under this rule unless those regulations specifically allow bringing suit at an earlier time.

Executive Order 13132, Federalism

It has been determined, under Executive Order 13132, Federalism, that this interim rule does not have sufficient federalism implications to warrant the preparation of a Federal Assessment. The provisions contained in the interim rule will not have a substantial direct effect on States or their political subdivisions or on the distribution of power and responsibilities among the various government levels.

Regulatory Flexibility Act

This interim rule has been reviewed with regard to the requirements of the Regulatory Flexibility Act (5 U.S.C. 601–612). Rural Development has determined that this rule will not have a significant economic impact on a substantial number of small entities.

Rural Development made this determination based on the fact that this regulation only impacts those who choose to participate in the program. Small entity applicants will not be impacted to a greater extent than large entity applicants.

Executive Order 12372, Intergovernmental Review of Federal Programs

Rural Development Guaranteed Loans are subject to the Provisions of Executive Order 12372, which require intergovernmental consultation with State and local officials. Rural Development conducts intergovernmental consultation in the manner delineated in RD Instruction 1940–J, ''Intergovernmental Review of Rural Development Programs and Activities,'' available in any Rural Development office, on the Internet at *http://rurdev.usda.gov.regs*, and in 7 CFR part 3015, subpart V.

Executive Order 13175, Consultation and Coordination With Indian Tribal Governments

This executive order imposes requirements on Rural Development in the development of regulatory policies that have tribal implications or preempt tribal laws. Rural Development has determined that the interim rule does not have a substantial direct effect on one or more Indian tribe(s) or on either the relationship or the distribution of powers and responsibilities between the Federal Government and the Indian tribes. Thus, this interim rule is not subject to the requirements of Executive Order 13175.

Programs Affected

The Catalog of Federal Domestic Assistance Program numbers assigned to this program are: 10.760, Water and Waste Disposal Systems for Rural Communities; 10.766, Community Facilities Loans and Grants; 10.768, Business and Industry Loans; and 10.775, Renewable Energy Systems and Energy Efficiency Improvements Program.

Paperwork Reduction Act

Pursuant to the Paperwork Reduction Act of 1995 (44 U.S.C. Chap. 35; see 5 CFR part 1320), the information collection provisions associated with this interim rule have been submitted to the Office of Management and Budget (OMB) for approval as a new collection and assigned OMB number 0570–0054. In the publication of the proposed rule on September 14, 2007, the Agency solicited comments on the estimated burden. The Agency received one public comment letter in response to this solicitation. This information collection requirement will not become effective until approved by OMB. Upon approval of this information collection, the Agency will publish a notice in the **Federal Register**.

Title: Rural Development Guaranteed Loans.

OMB Number: 0570–0054 (assigned)

Type of Request: New collection.

Expiration Date: Three years from the date of approval.

Abstract: The majority of information being collected is associated with lender applications and its associated requirements for lender entities seeking to participate in the program and with loan guarantee applications. The types of information collected for lender applications include, but is not limited to, basic data about the lending entity and a summary of the lending entity's loan origination and servicing policies and procedures as well as, as applicable, its lending history and experience and its relationship with its regulator.

The type of information collected with the guarantee application depends on whether it is being submitted by an approved lender or a preferred lender. Approved lender guarantee applications require more information to be submitted than a guarantee application from a preferred lender. Guarantee applications from approved lenders must contain the lender's analysis and credit evaluation, environmental information, technical reports, energy audits or assessments, appraisals if available, business plan, feasibility study, credit reports, and financial statements. An Affirmative Fair Housing Marketing Plan is required where applicable.

Guarantee applications from preferred lenders must contain information sufficient for the Agency to confirm project and borrower eligibility, a copy of the lender's loan evaluation and analysis, internal loan approval documents, and environmental information.

Information is also collected when the loan is being approved (e.g., conditional commitment, lender's agreement). Once the loan is in place, information is collected during the servicing of the loan. For example, loan status reports, including information on loans that are in default, and borrower financial reports are provided to the Agency by the lender. Additional information is collected when changes occur during the life of the loan (e.g., mergers, subordinations, transfers and assumption).

The estimated information collection burden has increased by approximately $357,500, from $2,933,520 estimated for the proposed rule to $3,290,998 estimated for the interim rule. The majority of this increase is attributable to two changes. One change is the addition of the requirement for other lending entities (i.e., those that are not regulated or supervised) to undergo an examination acceptable to the Agency in order to participate in the program. This change, made in response to public comment, will help the Agency manage institutional risk. The second change is the removal of the low documentation application for guarantee. This was also eliminated in response to public comment and further helps the Agency manage institutional risk by requiring approved lenders to submit more information on each guaranteed loan requested. Together, these two changes account for approximately 90 percent of the increase in costs.

Other changes are accounted for by such changes as requiring additional notifications (e.g., loan classifications, changes in a lender's policies and procedures), additional guarantee application requirements (for Community Facility and Water and Waste Disposal guaranteed loans), and submittal of borrower financial reports. These changes further help the Agency mitigate the risk associated with the guaranteed loans it approves.

E-Government Act Compliance

Rural Development is committed to complying with the E-Government Act, to promote the use of the Internet and other information technologies to provide increased opportunities for citizen access to Government information and services, and for other purposes.

I. Overview

This interim rule implements a unified guaranteed loan platform for the delivery of four guaranteed loan programs. The guaranteed loan programs included in the interim rule are Community Facilities, Water and Waste Disposal Facilities, Business and Industry, and the Rural Energy for America Program (previously known as the Renewable Energy System and Energy Efficiency Improvements program). Provisions common to each of the four programs are found in subpart A of the rule. Provisions specific to an individual program are found in subpart B of the rule. The unified guaranteed loan platform will allow USDA Rural Development to simplify, improve, and enhance the delivery of these four guaranteed loan programs across their service areas.

II. Background

By statutory authority, USDA Rural Development is the leading Federal advocate for rural America, administering a multitude of programs, ranging from housing and community facilities to infrastructure and business development. Its mission is to increase economic opportunity and improve the quality of life in rural communities by providing the leadership, infrastructure, venture capital, and technical support that enables rural communities to prosper and adapt to new technologies, products, and markets.

To achieve its mission, USDA Rural Development provides financial support (including direct loans, grants, and loan guarantees) and technical assistance to help enhance the quality of life and provide the foundation for economic development in rural areas. USDA Rural Development has used the four guaranteed loan programs included in this interim rule, as well as other guaranteed loan programs, to achieve Rural Development's mission. The regulations that are being combined under the interim rule have developed over time and, in some aspects, independently of each other. Issues have developed when looking at all four program regulations as a whole as well as individually. This was stated in the proposed rule published on September 14, 2007, **Federal Register** (72 FR 52618). The four issue areas identified by Rural Development are:

Inefficiencies. Many of the same lenders and, in some cases, borrowers, seek loan guarantees under more than one of these four programs. Thus, the same entities are required to learn multiple programs. This is inefficient and costly to the lenders and makes the programs less attractive to lenders. Currently, when new programs are implemented, a whole new regulation is developed that, in many respects, addresses or adopts many of the same requirements. Time and effort are wasted in readdressing issues during the development of new program regulations leading to inefficient rulemaking and a delay in program implementation.

Inflexibility. Maintaining four separate sets of basic requirements creates certain inflexibilities. For example, with each program administered under separate regulations, any change to basic requirements calls for multiple concurrences. Similarly, adding a new program requires the addition of a new set of basic requirements, as these are not currently shared.

Use of Agency Resources. Agency personnel spend a large amount of time performing process-related tasks that are not necessarily productive in making loan guarantees available to more lenders and, in turn, to more borrowers. These tasks are often inefficient and could be better managed by the private sector at the lender level. Further, these tasks are applied equally regardless of the relative level of risk of the associated loans. In sum, the current delivery of these four programs is not making the best use of Agency resources.

Risk Management. In making and managing a portfolio of loan guarantees, consideration must be given to project risk, institutional risk, Agency loss exposure, and internal operational risk.

Project risk refers to the ability of a project to repay its debt. The current process relies on the lender's evaluation of the project and then the Agency's review of the lender's analysis. The types of information required to be assessed under each of the programs by the lender may vary. Currently, the Agency lacks definitive parameters to evaluate project risk and is inconsistent in its evaluation of risk across State Offices. The lack of definitive parameters might create more risk. It allows projects to be funded based on completed processes as opposed to set evaluation criteria. This can result in funding more risky projects that may come at the expense of less risky projects over time because of limited program funds.

Institutional risk refers to the quality of the lender seeking the loan guarantee. Some lenders simply do a better job at managing their portfolios and thereby have a lower rate of defaults. The current system does little to pre-qualify lenders; that is, the criteria for a lender to originate a loan with the Agency are insufficient.

Agency loss exposure refers to the Agency's risk for potential loss in any one project in terms of the percent of guarantee and the size of the loan. Currently, Agency loss exposure is managed by putting limits on the percent of guarantee relative to the size of the loan, by having collateral requirements, and, for some of the programs, by limiting the size of the loan. While these limits are the primary mechanism for managing Agency loss exposure, the current programs could do more to manage this risk.

Agency operational risk refers to internal weaknesses inherent in administering multiple programs using a variety of regulations that require unique sets of processes and procedures.

Rural Development is addressing the issues associated with these four guaranteed loan programs through this unified guaranteed loan platform. This platform addresses the inefficiencies in maintaining separate regulations, better manages the risks associated with their delivery, significantly reduces inconsistencies in the implementation of these four programs across State offices, improves underwriting for loan guarantees, and reduces operational risk. By implementing a defined set of criteria to assess lender performance, Rural Development improves its management of lenders participating in these programs.

III. Discussion of the Interim Rule

USDA Rural Development is issuing this regulation as an interim rule, with an effective date January 16, 2009. All provisions of this regulation are adopted on an interim final basis, are subject to a 60-day comment period, and will remain in effect until the Agency adopts a final rule.

IV. Changes to the Rule

This section presents changes to the proposed rule. Most of the changes were the result of the Agency's consideration of public comments to the proposed rule. Some changes, however, are being made in response to the provisions of the 2008 Farm Bill. The changes to the proposed rule are presented by section. Unless otherwise indicated, rule citations refer to those in the interim rule.

Highlighted Changes

There were several portions of the rule that drew numerous comments. The following list highlights some of the changes made to the rule. These changes are also presented in the section specific change portion that follows this list.

- Cash equity as a minimum financial criterion has been replaced with a debt-to-tangible net worth ratio criterion.
- Low application documentation provisions have been deleted.
- Preferred lender status now applies only to the Business and Industry program and the requirements for becoming a preferred lender have changed. The Agency may administratively allow other programs to have preferred lender status at some date in the future and, in this event, would publish a **Federal Register** Notice to this effect.
- The requirement that a lender comply with either its lending policies and procedures or those in the rule, whichever is more stringent, has been modified by the addition of the phrase

"unless otherwise approved by the Agency."

- Lenders are not required to submit copies of their policies and procedures, but are instead to submit a written summary of their policies and procedures when submitting an application.
- The proposed provision that "The guaranteed portion will be paid first and given preference and priority over the unguaranteed portion" has been replaced with "the unguaranteed portion of the loan will neither be paid first nor given any preference or priority over the guaranteed portion."

Section Specific Changes

Subpart A—General Provisions

Purpose and Scope (§ 5001.1)

This section has been revised in two ways.

First. Paragraph (a) of this section adds that the provisions of this part apply only to those guaranteed loan programs that are included in subpart B. This clarifies the scope of the part.

Second. The Agency added paragraph (b) to clarify the relationship between the provisions in subpart A and those in subpart B. By including this paragraph, the Agency was able to remove from the rest of the rule such clauses as "unless otherwise specified in subpart B."

Definitions (§ 5001.2)

The Agency made numerous changes to the definitions section of the rule, including redefining certain terms, adding new definitions, and deleting several definitions. The following identify each affected term.

Applicant. This definition was deleted.

Approved lender. This definition was added to clarify responsibilities.

Borrower. This definition was redefined, in two ways, in order to clarify who constitutes a borrower and to identify in the rule which requirements apply to the borrower or to the lender or to both.

First. The word "entity" was replaced with "person" and the phrase "or seeks to borrow" was added after "The person that borrows."

Second. The definition for "person" was added.

Business plan. This definition was clarified by replacing the word "applicant" with "borrower."

Conditional commitment. The Agency added "of commitment" after "The Agency-approved form" and replaced "it" with "the lender."

Conflicts of interest. This definition was removed. The Agency has made revisions elsewhere in the rule such that the Agency does not believe that this term needs to be defined in the rule. Instead, the Agency will provide guidance on this term in the handbook to the rule.

Cooperative organization. This definition was expanded to include "any entity that is legally chartered as a cooperative." This was done to correct an oversight in the proposed rule that would have excluded "true" cooperatives.

Day. This definition was added for clarity.

Debt coverage ratio. This definition was revised in response to comments to make the term more in keeping with normal banking practice.

Essential community facility. This definition was redefined in three ways:

First. At the beginning of the definition, the Agency added "(including machinery, and/or equipment)" after "The physical structure" and before "financed" to help illustrate what physical structure includes.

Second. The sentence "Not include a project that benefits a single individual or group of single individuals as opposed to a class within a community" was replaced with "Benefit the community at large." The Agency believes that this change better identifies the Agency's intent. (paragraph (3))

Third. The phrase "Be located in a rural area" was removed. The Agency moved this phrase to subpart B for the Community Facilities program, where the Agency believes it is more appropriate.

Existing businesses. The second sentence of this definition has been rewritten to further define certain types of changes that constitute existing businesses.

Feasibility study. This definition was revised to state that the analysis is "by a qualified consultant."

High impact business. Significant revisions to this definition clarify what businesses constitute a "high impact" business.

Immediate family. This definition adds reference to "or adoption," to individuals living within the same household, and to domestic partners. The definition now reads "Individuals who are closely related by blood, marriage, or adoption, or live within the same household, such as a spouse, domestic partner, parent, child, brother, sister, aunt, uncle, grandparent, grandchild, niece, or nephew."

Lender. This definition was redefined to clarify the relationship between an entity that is seeking to participate (lending entity) and one that has been approved (lender).

Lender's agreement. This definition was revised to refer to it as a form.

Lending entity. This definition was added to clarify the applicability of the rule's requirements.

Loan note guarantee. This definition was revised to refer to it as a form.

Material change. This definition replaces the definition for "substantive change" and is used to provide consistency with the rule.

Monetary default. This definition was added to clarify when certain requirements in the rule apply to "monetary defaults" or to defaults in general.

Negligent loan origination. This definition was revised by changing "at the time of the loan" to "at the time the loan is made." This clarifies how this aspect of negligent loan origination will be evaluated by the Agency. (paragraph (2))

Negligent loan servicing. The phrase "with its current servicing policies and procedures" was replaced with "with its servicing policies and procedures in use by the lender at the time the loan is made." This clarifies how this aspect of negligent loan servicing will be evaluated by the Agency. (paragraph (2))

Other lending entity. This definition was added to clarify the provisions of the rule.

Permanent working capital. This definition was deleted. Instead, as shown below, the Agency is defining "working capital." This change was made to clarify the Agency's intent and to make the Agency's intent clearer to the commercial lending community.

Person. This definition was revised to include public bodies, which will ensure such entities as Tribes are included.

Post-application. There were two changes to this definition.

First. The word "applicant" was replaced with "borrower" to clarify that it is the borrower's eligibility being determined and not the lender's eligibility.

Second. The phrase "to score the application" was removed because it is no longer needed under the rule.

Pre-application. This definition was added to clarify what constitutes a pre-application.

Preferred lender. This definition was added to clarify who is subject to the preferred lender provisions of the rule.

Preliminary architectural report. This definition was added as a conforming change to the rule.

Preliminary engineering report. Reference to the RUS bulletins was removed. These will be addressed in the handbook to the rule.

Promissory note. This definition was revised to remove the phrase ''or on demand'' from the end of the first sentence because guaranteeing a demand note can create a balloon payment.

Qualified consultant. This definition was added because the rule now has provisions that require the use of a ''qualified consultant.''

Regulated or supervised lender. This definition was revised by removing the word ''credit'' and by replacing the word ''and'' with ''or'' in two places to ensure that the sentence was not interpreted as requiring both conditions.

Renewable biomass. This definition was added because the revision to the definition of ''renewable energy'' uses the term. This definition is from the 2008 Farm Bill.

Renewable energy. This definition was revised based on the definition in the 2008 Farm Bill.

Rural or rural area. This definition was revised to clarify what constitutes rural or rural areas. In addition, a paragraph was added for determining which census blocks in an urbanized area are not in a rural area.

Startup business. This definition was completely revised in response to comments to clarify the types of business that would constitute startup businesses.

State. This definition was clarified to indicate that ''any of the 50 States'' referred to those ''of the United States.''

Substantive change. This definition was removed and replaced by the definition ''material change.''

Tangible net worth. This definition was added because it is now used in the financial metric criteria used to determine project eligibility.

Unincorporated area. This definition was deleted because it is no longer needed as the result of changes to the definition of ''rural or rural area.''

Working capital. This definition was added to the rule to replace ''permanent working capital.'' It is defined as ''Current assets available to support a business' operations and growth. Working capital is calculated as current assets less current liabilities.''

Finally, paragraph (b), ''abbreviations'' was removed because it is no longer needed for the rule.

Agency Authorities (§ 5001.3)

Exception authority (§ 5001.3(a)). The Agency revised paragraph (a)(1) in this section by replacing ''applicant'' with ''lender'' to clarify that it is both the lender's eligibility and the borrower's eligibility that cannot be excepted.

Review or appeal rights (§ 5001.3(b)). The words ''Review or'' were added to the heading. The definition was revised by removing reference to ''the appropriate Agency official that oversees the program in question'' so that a person seeking review would seek such review from the National Appeals Division in accordance with the Division's regulation.

Oversight and Monitoring (§ 5001.4)

Paragraph (a) was modified to clarify that the lender is required to cooperate fully with the Agency in the Agency's oversight and monitoring of lenders.

Paragraph (b)(1) was corrected by replacing the word ''lender'' with ''borrower'' so that it now reads ''any material change in the general financial condition of the borrower.''

Paragraph (b)(2) was revised to indicate that monthly default reports are required for loans that are in monetary default. At proposal, this provision referred to a loan that goes into default, without specifying what kind of default.

Paragraph (b)(3) was modified in two ways:

First. Notifications are required within 15 calendar days rather than 5 days as was proposed.

Second. Notifications are now being required for loans made under this part that receive any downgrade in their classification.

Paragraph (b)(4) was added to require, from a lender who receives a final loss payment, an annual report on the lender's collection activities for each unsatisfied account for 3 years following payment of the final loss claim. This requirement was added to help the Agency manage and mitigate risk inherent in delivering and administering this program.

Project Eligibility (§ 5001.6)

Numerous changes were made to this section.

First. The introductory text was modified to indicate that the requirements in this section apply to both borrower and project elements.

Second. A new paragraph (a) replaces paragraphs (a) and (b) in the proposed rule. Paragraph (a) references the reader to the project requirements specified in subpart B. Because the requirements in subpart B address the two requirements identified in proposed paragraphs (a) and (b), the Agency removed these two proposed paragraphs from this section.

Third. Paragraph (b), which corresponds to paragraph (c) in the proposed rule, addresses the financial metric criteria. Changes incorporated in this paragraph are:

- The rule clarifies that these financial metric criteria are based on the borrower and not on the individual project;
- The Agency has added that these financial metric criteria are to be calculated from ''the realistic information in the pro forma statements or borrower financial statements * * * of a typically operating year after the project is completed and stabilized;'' and
- The Agency has replaced the proposed cash equity criterion with a debt-to-tangible net worth ratio criterion.

Unauthorized Projects and Purposes (§ 5001.7)

Paragraph (b) has been revised to refer to only golf courses and similar recreational facilities. The references to racetracks, water parks, and ski slopes found in the proposed rule have been relocated to subpart B in the Community Facilities provisions. However, the Agency has added additional underwriting criteria that allows the Agency to require higher underwriting standards for projects that are deemed more risky, such as racetracks and water parks.

Paragraph (c), which addresses businesses deriving more than 10% of its annual gross revenue from gambling activity, has been modified by allowing State-authorized proceeds and, for public bodies and for not-for-profit approved projects only, any other funds derived from gambling proceeds, as approved by the Agency, to be excluded from this calculation.

Paragraph (e) was reorganized to make clear that ''made by other Federal agencies'' applies to loans and not to lines of credits or lease payment. The introductory text to paragraph (e) was revised to read ''Any guarantee of a:'' rather than ''Any:''.

Proposed paragraph (g), which addressed facilities used primarily for the purpose of housing Federal and State agencies, was removed from subpart A in the rule and is addressed, instead, in subpart B for Community Facilities.

Paragraph (h) addresses any business deriving income from illegal drugs, drug paraphernalia, and other illegal product or activity. At proposal, this paragraph used the phrase ''deriving income from the sale of illegal drugs.'' The Agency removed the phrase ''the sale of'' as it is unnecessary and potentially too restrictive.

Paragraph (i) was rephrased to clarify that payment to the borrower for the rental of equipment or machinery owned by the borrower is an unauthorized purpose.

Paragraph (j) was revised from ''The payment of a judgment'' to ''The payment of either a Federal judgment or a debt owed to the United States, excluding other Federal loans.''

Paragraph (k) was revised to read ''Any project that creates, directly or indirectly, a conflict of interest or an appearance of a conflict of interest.'' At proposal, this provision read ''Any project resulting in a conflict of interest.''

Borrower Eligibility (§ 5001.8)

Paragraph (a)(1)(i) was modified to make clear that citizens of the U.S. include citizens of the Republic of Palau, the Federated States of Micronesia, the Republic of the Marshall Islands, and American Samoa.

Paragraph (a)(1)(ii) was modified to address the clarification made in paragraph (a)(1)(i) of this section and to add ''or controlled'' after ''Entities other than individuals must be at least 51% owned.''

Paragraph (b) was revised to include the provision that a borrower would be ineligible if any owner with more than 20 percent ownership interest in the borrower was also found to be ineligible using the same criteria provided for the borrower itself.

Participation Eligibility Requirements (§ 5001.9)

The Agency has made numerous and significant changes to this section, which was titled Lender Eligibility and Designation in the proposed rule.

A new paragraph (a) was added that identifies three requirements applicable to all lending entities (at proposal, the term used was lenders) that wish to participate in this program. These three requirements are:

• Submittal of a written summary of their loan origination and servicing policies and procedures. Under the proposed rule, all lending entities would have been required to submit copies of these policies and procedures (see also § 5001.9(b)(1)(ii), (b)(2), and (c)(2)(i)).

• Maintenance of internal audit and management control systems to evaluate and monitor the overall quality of their loan origination and servicing activities. This was not part of the proposed rule.

• Not being otherwise debarred or suspended by the Federal government. This was part of the proposed rule.

Paragraph (b), which corresponds to paragraph (a) under this section in the proposed rule, includes revisions for regulated or supervised lending entities that do not have an outstanding Agency guaranteed loan with the Agency (referred to at proposal as not having an existing portfolio) and for regulated or supervised lending entities that have at least one outstanding Agency guaranteed loan. The interim rule makes clear that the determination of whether a lending entity has an outstanding Agency guaranteed loan is based on the date on which the interim rule is effective.

For regulated and supervised lending entities that do not have outstanding guaranteed loans, the interim rule makes clear as to whom the lending entity is to submit the lender application (§ 5001.9(b)(1)(i)). At proposal, the rule did not make clear to whom a federally chartered lending entity would submit the lender application.

The interim rule requires regulated and supervised lending entities that do not have outstanding guaranteed loans to submit information on their lending history and experience with their lender application (§ 5001.9(b)(1)(iii)). This was not part of the proposed rule. The Agency believes that this requirement will allow the Agency to further reduce institutional risk.

Lastly, for these lending entities, the interim rule identifies the process under which the Agency will determine whether or not to approve the lender application (§ 5001.9(b)(1)(iv)). At proposal, this process was not addressed other than to make reference to the requirement that the lending entity be in good standing with its regulator.

For regulated or supervised lending entities that have at least one outstanding Agency guaranteed loan, the interim rule makes clear the process under which the Agency will approve such lenders (§ 5001.9(b)(2)(i) and (ii)).

In paragraph (b)(4), the Agency has expanded the requirements for approved regulated or supervised lenders to maintain their approved status (proposed § 5001.9(a)(3)) to include the provision that if a lender fails to maintain its status as a lender or has no outstanding loans with the Agency for two consecutive years, it must reapply under this section for lender approval.

The Agency has also modified the requirements for other lending entities (referred to as ''other lenders'' in the proposed rule) to participate in this program. The Agency has added the requirement that other lending entities must have undergone an examination acceptable to the Agency in order to be eligible for submitting a lender application for approval (§ 5001.9(c)(1)(iv)). The Agency added this criterion in response to public comments and its assessment that such an examination will assist the Agency in mitigating institutional risk. The results of this examination are to be submitted with the lender application (§ 5001.9(c)(2)(viii)).

Paragraph 5001.9(c)(2) was modified to indicate that certificates of good standing must be obtained from the States in which the other lending entity is licensed and intends to conduct business; at proposal, this provision did not include the ''is licensed'' aspect of the provision.

Paragraph 5001.9(c)(3) makes clearer the process that the Agency will use in reviewing other lending entity applications for lender approval, which is very similar to what was proposed.

Paragraph 5001.9(c)(5), which addresses maintenance of approved status for approved other lenders, adds the requirement (as for regulated or supervised lenders) that if the lender fails to maintain its status as a lender or has no outstanding loans with the Agency for two consecutive years, it must reapply under this section for lender approval.

Lastly, the Agency has revised the requirements associated with preferred lenders. Under the interim rule, preferred lender status will apply only to lenders participating in the Business and Industry guaranteed loan program. The Agency may administratively allow other programs to have preferred lender status at some date in the future and, in this event, would publish a **Federal Register** Notice to this effect. Under the proposed rule, any approved lender could apply for preferred lender status. In making this change, the Agency has dropped in its entirety proposed § 5001.9(c), Lender designation.

Paragraph (d) of this section addresses all of the requirements associated with preferred lenders. The proposed rule (§ 5001.9(c)(1)(i) through (c)(1)(iii)) identified three criteria—current level of experience, number of losses (which varied depending on how long the lender was making commercial loans), and instances of Federal government negligent loan origination or servicing. The interim rule identifies seven criteria to be met to become a preferred lender:

• Lender loss rate not in excess of a maximum ''preferred lender'' loss rate;

• A minimum of 10 guaranteed Business and Industry loans, unless otherwise provided for in a notice in the **Federal Register**;

• Consistent practice of submitting guaranteed loan applications with accurate information supporting a sound loan proposal;

• No more than one instance of Federal government loan origination or servicing where a loss has been paid;

• Not be under any regulatory enforcement action;

• Demonstrated high standards of professional competence; and

• Adequate lender facilities to conduct its Agency business at a high level of performance.

The Agency will publish in the **Federal Register** notices that identify the maximum preferred lender loss rate and minimum number of guaranteed Business and Industry loans to qualify for preferred lender status when there are changes in these rates or numbers.

Paragraph (d)(2) requires the lender to identify the States in which the lender is seeking preferred status and to identify those branch offices for which it is seeking preferred lender status. Under the proposed rule, a lender approved as a preferred lender would have preferred lender status in each State.

Paragraph (d)(3) allows the lender to have preferred lender status for a period not to exceed 4 years and requires the lender to submit material to retain preferred status once the 4 years (or other applicable time period) has expired. At proposal, there was no timeframe associated with preferred lender status.

Paragraph (d)(4) identifies the situations under which a lender may lose its preferred status. The interim rule contains more specifics than found in the proposed rule and applies the criteria under which a lender can lose its preferred lender status regardless of how long the lender has been making commercial loans.

Guarantee Application Process (§ 5001.11)

The Agency has made two changes to this section.

First. The Agency has clarified § 5001.11(b)(2) by defining what is meant by ''those areas'' in the paragraph where it states, in part, ''the Agency may require the lender to obtain additional assistance in those areas where the lender does not have the requisite expertise to originate or service the loan.''

Second. The Agency has added a new paragraph (c) in which the Agency will approve (subject to the availability of funds) or reject complete applications from preferred lenders within 10 working days after their receipt. This processing timeframe will not begin until all information required to make an approval decision, including a completed environmental review, is received by the Agency.

Application for Loan Guarantee Content (§ 5001.12)

The Agency has made significant changes to this section in the interim rule.

First. The rule no longer differentiates between full documentation applications and low documentation applications. Instead, all approved lenders submit applications that contain information that is very similar to what would have been required under the proposed rule's ''full documentation'' applications. The interim rule does not contain a low documentation application provision and, as such, no longer requires a ''determination of documentation level'' provision as provided in the proposed rule (proposed § 5001.12(c)).

Second. The interim rule provides requirements for guarantee loan applications from preferred lenders. While guarantee loan applications from preferred lenders require less documentation than those from approved lenders, they are not referred to as ''low documentation'' applications in the interim rule, but as ''preferred lender'' loan guarantee applications.

The loan guarantee application requirements for approved lenders are the same as those found in the proposed rule for full documentation applications, with the following exceptions:

• A copy of Form 10–K is no longer required to be submitted for companies listed on major stock exchanges (proposed § 5001.12(a)(5)).

• The proposed loan agreement between the lender and the borrower is no longer required to be submitted (proposed § 5001.12(a)(6)).

• Appraisals acceptable to the Agency are to be submitted if available. If they are not available at the time the application is submitted, complete appraisals must be submitted to the Agency before loan closing. At proposal, this requirement stated ''Appraisals (as specified in § 5001.16(c))'' (proposed § 5001.12(a)(8)).

• In newly designated § 5001.12(a)(8), the ''for for-profit'' qualifier for nursing homes has been removed (proposed § 5001.12(a)(11)).

• In newly designated § 5001.12(a)(9), the word ''prospective'' was removed because it is no longer needed (proposed § 5001.12.(a)(13)).

• Proposed § 5001.12(a)(12) for preliminary engineering report was relocated to subpart B for the water and waste disposal facility program.

• Proposed § 5001.12(a)(14) requiring the most recent audited financial statements if the guaranteed loan is $1 million or more is significantly revised. In the interim rule, this paragraph (§ 5001.12(a)(10)) requires borrowers that have been in existence for one or more years seeking a guaranteed loan of $3 million or more to submit their most recent audited financial statements, unless alternative financial statements are authorized by the Agency. For borrowers that have been in existence for one or more years seeking a guaranteed loan of less than $3 million, the interim rule requires such borrowers to submit either the most recent audited or Agency-acceptable financial statements of the borrower. Lastly, for borrowers that have been in existence for less than one year, the interim rule requires the submittal of ''the most recent Agency-authorized financial statements of the borrower regardless of the amount of the guaranteed loan request.'' Paragraph 5001.12(a)(10)(iii) allows the Agency to request additional financial statements and related information depending on the complexity of the project.

• Finally, newly designated § 5001.12(a)(11) has been added to provide the Agency the flexibility to request any additional information determined by the Agency as necessary to evaluate the application.

The provisions for guaranteed loan applications for preferred lenders are found in § 5001.12(b), and are new to the rule. Preferred lenders are required to submit:

• A copy of Form RD 5001–3, ''Application for Loan Guarantee'';

• Information sufficient for the Agency to confirm project and borrower eligibility;

• A copy of lender's loan evaluation and analysis;

• An internal loan approval document showing approval by in-house appropriate office/committee; and

• Environmental information required by the Agency to conduct its environmental reviews (as specified in § 5001.16(h)).

Lender Responsibilities—General (§ 5001.15)

The interim rule contains three additional requirements applicable to all lenders participating in this program to help further mitigate institutional risk. These requirements are:

• Notifying the Agency of any changes to its loan origination and servicing policies and procedures provided under § 5001.9(a). For any changes to the lender's loan origination and servicing policies and procedures that are inconsistent with the requirements of this part, the lender must notify the Agency in writing and receive written Agency approval prior to applying the changes to loan guarantees under this part.

• Compiling and maintaining in its files a complete application for each guaranteed loan for at least one year after the final loss has been paid.

• Maintaining internal audit and management control systems to evaluate and monitor the overall quality of its loan origination and servicing activities.

Lender Responsibilities—Origination (§ 5001.16)

The Agency has made a number of changes to this section. One editorial change throughout the section was the replacement of the words ''prospective borrower'' with ''borrower'' (e.g., § 5001.16(b)(2)(i)).

General (§ 5001.16(a)). In the introductory text to § 5001.16(a), the Agency made two substantive changes.

First. The Agency revised the first sentence to read: ''The lender is responsible for originating all loans in accordance with its loan origination policies and procedures at the time the loan is made and with the requirements of this part.'' The text in the proposed rule did not include ''at the time the loan is made.'' The revised sentence also replaces the phrase ''current written policies and procedures'' with ''loan origination policies and procedures.''

Second. The Agency revised the second sentence to read: ''Where a lender's loan origination policies and procedures address a corresponding requirement in this part, the lender must comply with whichever is more stringent, unless otherwise approved by the Agency.'' The text in the proposed rule did not include the phrase ''unless otherwise approved by the Agency.'' This added phrase is cross-referenced as necessary in other places within the interim rule (e.g., § 5001.16(b)). The inclusion of this phrase allows the Agency and the lender to work together and to consider each loan application on a case-by-case basis.

The Agency has also added a requirement (§ 5001.16(a)(2)) for the lender to provide the Agency the lender's classification of the loan no later than 90 days after loan closing.

Appraisals (§ 5001.16(c)). The Agency made three changes to the introductory text to this paragraph and one change to § 5001.16(c)(2).

In the introductory text, the Agency included chattel collateral appraisals, which were not addressed in the proposed rule. In addition, the Agency dropped reference to specific sections within the Uniform Standards of Professional Appraisal Practices (USPAP) standards, as these were unnecessary to continue to include in the rule. Lastly, the Agency added the provision that complete appraisals must be submitted to the Agency before loan closing.

In § 5001.16(c)(2), the Agency added that the potential effect of environmental hazards on the market value of the collateral are to be ''determined in accordance with the appropriate ASTM Real Estate Assessment and Management environmental standards.''

Personal, partnership, and corporate guarantees (§ 5001.16(d)). The heading has been revised to include ''partnership.'' In addition, here and elsewhere in the rule, the Agency revised the phrase ''personal or corporate guarantees'' (and similar phrases) to ''personal, partnership, or corporate guarantees.''

The proposed rule was not clearly written as which personal, partnership, and corporate guarantees could be used to secure a loan. A new paragraph (d)(1) has been added to make clear that secured, unconditional personal, partnership, and corporate guarantees may be used to determine the security of the loan, but that unsecured, unconditional personal, partnership, and corporate guarantees will not be considered in determining whether a loan is adequately secured for loan making purposes.

Re-designated paragraph (d)(2) addresses Agency-approved, unsecured personal, partnership, and corporate guarantees and incorporates the provision found in the proposed rule under proposed § 5001.16(d)(1) and (d)(2). Concerning exceptions to the requirement for personal guarantees, the Agency replaced ''concurred by the Agency approval official'' with ''approved by the Agency.''

Lastly, a new paragraph (d)(3) was added to address the requirement for guarantors to execute an Agency-approved unconditional guarantee (which was required in the proposed rule). The interim rule adds three provisions to explain how amounts paid by the Agency will constitute a Federal debt and the handling of interest charges. These provisions are:

• Any amounts paid by the Agency on account of liabilities of an Agency guaranteed loan borrower will constitute a Federal debt owed to the Agency by the guaranteed loan borrower. In such case, the Agency may use all remedies available to it, including offset under the Debt Collection Improvement Act of 1996, to collect the debt from the borrower.

• Any amounts paid by the Agency pursuant to a claim by a guaranteed program lender will constitute a Federal debt owed to the Agency by a third-party guarantor of the loan, to the extent of the amount of the third-party guarantee. In such case, the Agency may use all remedies available to it, including offset under the Debt Collection Improvement Act of 1996, to collect the debt from the third-party guarantor.

• In all instances under the above paragraphs, interest charges will be assessed in accordance with 7 CFR 1951.133.

Design requirements (§ 5001.16(e)). The Agency made two substantive changes to this paragraph.

First. The phrase ''or other Agency-approved code'' was added to the end of the first sentence.

Second. In the second sentence the word ''original'' was replaced with the word ''approved.''

Compliance with other Federal Laws (§ 5001.16(g)). The Agency removed the last sentence in the proposed rule text, because it is not applicable to guaranteed loans.

Conflicts of interest (§ 5001.16(i)). The Agency added the phrase ''and appearances of conflicts of interest'' to the end of this paragraph, which should have been included in the proposed rule.

Surety (§ 5001.16(j)). The Agency added this paragraph to the rule. Under this paragraph, surety will be required in cases when the guarantee will be issued prior to completion of construction unless the contractor will receive a lump sum payment at the end of work. In addition, surety is to be made a part of the contract, if the applicant requests it or if the contractor requests partial payments for construction work. Finally a latent defects bond may be required to cover the work in instances where no surety is provided and the project involves pre-commercial technology, first of its type in the U.S., or new designs without sufficient operating hours to prove their merit.

Lender's Responsibilities—Servicing (§ 5001.17)

General (§ 5001.17(a)). Consistent with the revision made to § 5001.16(a), the Agency revised the second sentence to read ''Where a lender's loan servicing policies and procedures address a corresponding requirement in this part, the lender must comply with whichever is more stringent, unless otherwise approved by the Agency.'' The text in the proposed rule did not include the phrase ''unless otherwise approved by the Agency.'' This added phrase is cross-referenced as necessary in other places within the interim rule (e.g., § 5001.17(b)). The inclusion of this phrase allows the Agency and the lender to work together and to consider each loan application on a case-by-case basis.

The revised sentence also replaces ''current written policies and procedures'' with ''loan servicing policies and procedures.''

Certification (§ 5001.17(b)). The phrase ''current written'' was removed from this paragraph and a cross-reference to the exception to the ''whichever is more stringent'' requirement in paragraph (a) of this section was added.

Audits (§ 5001.17(c)). This is a new provision, which requires lenders, when applicable, to audit a borrower in accordance with Office of Management and Budget requirements.

Financial reports (§ 5001.17(d)). This is a new provision addressing when lenders are to submit financial reports of the borrower. The requirements differ depending on whether or not the lender is a regulated or supervised lender. Specifically, these requirements are:

- For regulated or supervised lenders, the information that would be contained in financial reports required by the appropriate regulatory institution. Unless otherwise provided in the Conditional Commitment, such information must be submitted at the same time it should be made available to the appropriate regulatory institution.
- For lenders who are not regulated or supervised, financial reports as required in the Conditional Commitment.

Collateral inspection and release (§ 5001.17(e)). As proposed (§ 5001.17(c)), the Agency would have been allowed to require the lender to obtain prior Agency approval of any release of collateral and to require an appraisal on the remaining collateral in cases in which the Agency determined that it may be adversely affected by the release. Because the proposed rule did not clearly indicate when such appraisals would be required, the Agency has revised this provision to state that:

- It will require prior approval of the release of collateral except in two instances—where the proceeds are used to pay down debt in order of lien priority, or to acquire replacement equipment, or where the release of collateral is made under the abundance of collateral provision of an applicable security agreement (*e.g.*, a blanket security agreement); and
- Appraisals on the collateral being released will be required on all transactions exceeding $250,000.

The Agency has also revised this paragraph by adding the phrase ''unless otherwise approved by the Agency in writing'' to the end of the last sentence and deleting ''In all cases'' from the beginning of the last sentence, which now reads in full ''The sale or release of collateral must be based on an arm's length transaction, unless otherwise approved by the Agency in writing.''

Processing transfers and assumptions (§ 5001.17(f)(2)). As proposed (§ 5001.17(d)(2)), this paragraph would have allowed the lender to release the transferor (including any guarantor) from liability without Agency approval. The Agency has revised this provision to now require such releases to be subject to Agency approval.

The Agency also added conditions under which the transferor (including any guarantor) may be released from liability (§ 5001.17(f)(2)(iii)).

Mergers (§ 5001.17(g)). As proposed (§ 5001.17(e)), the Agency would have been allowed to withdraw the guarantee when a borrower participates in a merger. This provision has been revised entirely. In the interim rule, all borrower mergers require prior approval by the Agency and the lender. Further, if a borrower merges without Agency approval, the lender must accelerate the loan unless subsequently agreed to in writing by the Agency.

Subordination of lien position (§ 5001.17(h)). The Agency has made several revisions to the Agency's concurrence as follows:

- The proposed rule required that the Agency's financial interest be enhanced. This has been changed to the subordination being in the Agency's best financial interest.
- The proposed rule required that the collateral will remain adequate to secure the loan. This has been removed from the interim rule.
- The proposed rule limited a subordination to a revolving line of credit to no more than one year. This has been changed to read ''the subordination of line of credit does not extend the term of the line of credit and in no event exceeds more than three years.''

Repurchases from holder(s) (§ 5001.17(i)). The Agency has made two changes to the introductory text to this paragraph.

First. The first sentence was revised to refer to ''monetary default'' rather than ''default'' so that the first sentence now reads, in part, ''the Agency to repurchase the unpaid guarantee portion of the loan in the case of borrower monetary default or failure of the lender to pay the holder its pro-rata share.''

Second. In the beginning of the second sentence the word ''or'' is replaced with ''and'' to read: ''When the lender and the Agency determine that repurchase is necessary to adequately service the loan, the holder must sell the guaranteed portion to the requesting entity.'' This edit was made in order to ensure that the Agency always participates in this decision.

The Agency added to this section a new paragraph (i)(2) addressing provisions regarding repurchase by lender for servicing.

Within the provisions for repurchases by the Agency (§ 5001.17(i)(3)), ''unless provided for in the Assignment Guarantee Agreement'' was deleted from the end of the sentence ''The lender may not charge the Agency any fees.'' In addition, language was added addressing the calculation of the amount of the repurchase and the length of accruing interest that will be covered (§ 5001.17(i)(3)(iii)).

Additional expenditures and loans (§ 5001.17(j)). The Agency made two edits to this provision. The words ''will not'' were replaced by the word ''may'' and the phrase ''unless the expenditure or loan will violate one or more of the loan covenants of the borrower's loan agreement'' was added at the end of the paragraph.

Lender failure (§ 5001.17(k)). The Agency added the phrase ''or ceases servicing the loan,'' in the first sentence to read: ''In the event a lending institution fails or ceases servicing the loan, the Agency will provide instruction to the successor entity on a case-by-case basis.''

Delinquent loans (§ 5001.17(l)). The phrase ''coordinate with the Agency and the borrower to'' was removed so that the second sentence reads: ''If a borrower is delinquent more than 30 days, the lender must implement appropriate curative actions to resolve the problem.''

Protective advances (§ 5001.17(m)). The Agency added four additional conditions associated with protective advances. These additional conditions are:

- Protective advances must constitute an indebtedness of the borrower to the lender and be secured by the security instruments. (§ 5001.17(m)(4))
- Upon Agency approval, protective advances can be used to pay Federal tax liens and other Federal debt. (§ 5001.17(m)(5))
- Protective advances and interest thereon at the note rate will be guaranteed at the same percentage of

loss as provided in the Loan Note Guarantee. (§ 5001.17(m)(6))

• The maximum loss to be paid by the Agency will be determined according to the procedures specified in § 5001.17(p)(1) regardless of any protective advances made. (§ 5001.17(m)(7))

Liquidation (§ 5001.17(n)). The Agency has made several modifications to this paragraph.

First. In the introductory text, the phrase ''and the Agency will then liquidate the loan'' was added to the end of the paragraph to read: ''The Agency reserves the right to unilaterally conclude that liquidation is necessary and require the lender to assign the security instruments to the Agency and the Agency will then liquidate the loan.''

Second. The Agency has added the provisions that it will approve or disapprove the plan within 30 days and that, upon approval of the liquidation plan by the Agency, the lender may implement the plan. (§ 5001.17(n)(1)(i)).

Third. A new paragraph (n)(1)(ii) has been added that addresses liquidation appraisals. This paragraph requires liquidation appraisals to be a part of the liquidation planning process. It further states that they are not required for liquidation plan approval, provided they are obtained prior to the completion of the liquidation. Lastly, this paragraph states that, if the outstanding principal loan balance including accrued interest is more than $200,000, the lender will obtain an independent appraisal report on all collateral securing the loan, which will reflect the current market value and potential liquidation value.

Fourth. A new paragraph (n)(1)(iii) has been added containing provisions for appraisal costs. Under this new paragraph, any independent appraiser's fee will be shared equally by the Agency and the lender. In addition, if an environmental site assessment in accordance with the appropriate ASTM Real Estate Assessment and Management environmental standards of the property is necessary in connection with liquidation, the cost will be shared equally between the Agency and the lender.

Fifth. A new paragraph (n)(1)(iv) has been added containing provisions for rent. Under this new paragraph, any net rental or other income that has been received by the lender from collateral will be applied on the guaranteed loan debt.

Loss calculations and payment (§ 5001.17(p)). The Agency has substantially rewritten the introductory paragraph to this section detailing how estimated losses and final losses are calculated. The Agency also made several other revisions to this paragraph.

First. A new paragraph (p)(1) has been added to address maximum loss. The proposed rule (§ 5001.17(n)) stated in the introductory text that ''The maximum loss allowed is the lower of the percent of loss guarantee times the foregoing or the sum of principal advances and accrued interest. The amount due the lender is adjusted to take into account protective advances and accrued interest. The amount due the lender is adjusted to take into account protective advances and interest.'' The interim rule has revised the calculation of maximum loss to be in-line with current Business and Industry provisions.

Second. The Agency added to this section a new paragraph (p)(2)(iv) stating that, upon payment of an estimated loss to the lender, interest accrual on the defaulted loan will be discontinued.

Third. In § 5001.17(p)(5)(i), the Agency has revised this paragraph to indicate that ''any loss will be based on the collateral value at the time the collateral is liquidated'' rather than, as proposed, ''at the time the lender obtains title.''

Fourth. In § 5001.17(p)(5)(ii), the Agency has revised this paragraph to include that the lender ''must submit an estimated loss claim when liquidation is expected to exceed 90 days.'' At proposal, this paragraph read ''it may request an estimated loss payment by submitting an estimate of loss that will occur in connection with liquidation of the loan.''

Fifth. In § 5001.17(p)(6), the Agency has replaced the proposed text (§ 5001.17(n)(4)) that stated ''The lender shall submit with each loss claim the current version of its written policies and procedures for origination and servicing'' with ''In response to a loss claim, the Agency may request and the lender must provide the Agency with a copy of the applicable loan origination and servicing policies and procedures in place for the loan.''

Sixth. A new paragraph (§ 5001.17(p)(7)) has been added addressing final loss. This new paragraph states: When the Agency finds the final report of loss to be proper in all respects, it will approve the final loss. If the loss is less than the estimated loss payment, the lender will reimburse the Agency for the overpayment plus interest at the note rate from the date of the estimated loss payment.

Basic Guarantee and Loan Provisions

General (§ 5001.30)

The Agency made three revisions to provisions within this section.

First. Paragraph (b)(1) was revised so that the last sentence reads: ''The unguaranteed portion of the loan will neither be paid first nor given any preference or priority over the guaranteed portion.'' This means, for example, that in the case of a 1 million dollar loan where the Agency's participation is $800,000 and the lender's share is $200,000, each will be repaid pari passu; that is for each dollar repaid, the Agency would receive 80 cents and the lender 20 cents. This change addresses one of the major concerns expressed by commenters. At proposal, this sentence read: ''The guaranteed portion will be paid first and given preference and priority over the unguaranteed portion.''

Second. Paragraph (c)(1) was revised so that the last sentence reads: ''Any claim against a Loan Note Guarantee or Assignment Guarantee Agreement that is attached to, or relating to, a note that provides for payment of interest on interest will be reduced to remove the interest on interest.'' At proposal, this provision read: ''any Loan Note Guarantee or Assignment Guarantee Agreement attached to, or relating to, a note which provides for payment of interest on interest is void.''

Third. Paragraph (c)(2) was revised so that the sentence that began ''Any losses occasioned will not be enforceable by the lender to the extent'' now states ''Any losses occasioned by the lender will not be enforceable to the extent''.

Guaranteed Loan Requirements (§ 5001.31)

The Agency has made changes to interest rates, renewal fees, and lender fees, as described below.

Interest rates (§ 5001.31(a)). In the introductory text, the last sentence of the paragraph was removed. This sentence had stated: ''When combined fixed and variable rates are used, the lender will provide the Agency with the overall effective interest rate for the entire loan.''

Negotiated rates (§ 5001.31(a)(1)). The Agency has added to the end of this paragraph ''and will be subject to Agency concurrence'' so that this paragraph now reads ''Interest rates, interest rate caps, and incremental adjustment limitations will be negotiated between the lender and the borrower and will be subject to concurrence by the Agency.''

Interest rate changes (§ 5001.31(b)(1)(i)). The Agency has qualified the need to approve any change in the interest by adding ''unless the only change is to the base rate of a variable interest rate.''

Increases (§ 5001.31(b)(3)). The Agency has revised this paragraph in identifying when increases in the interest rate are not permitted. At proposal, this paragraph read: ''Increases in interest rates are not permitted except when the increase results from normal fluctuations in approved variable interest rates, or the increase returns the rate to the rate prior to the temporary reduction.'' In the interim rule, this paragraph now reads: ''Increases in interest rates are not permitted beyond what is provided in the loan documents. Increases from a variable interest rate to a higher interest rate that is a fixed rate are allowed, subject to concurrence by the Agency.''

Guarantee fee (§ 5001.31(g)(1)). The payment of the guarantee fee was changed from ''at the time the Guarantee is issued'' to ''the time the lender requests the Loan Note Guarantee.''

Renewal fee (§ 5001.31(g)(2)). As proposed, the annual renewal fee would have been assessed annually based on a fixed fee rate established ''at the beginning of the loan.'' The Agency has revised this phrase to read: ''at the time the loan is obligated.''

Lender fees (§ 5001.31(h)). The Agency has added text to indicate that late payment fees can be part of the lender fees that lenders may levy. The revised text reads, in part, ''The lender may levy reasonable, routine, and customary charges and fees, including late payment fees, for the guaranteed loan.''

The Agency has also identified default charges and additional interest expenses as two additional expenses that will not be covered by the Loan Note Guarantee.

Conditional Commitment (§ 5001.32)

The Agency has identified two specific conditions to which the lender must certify in the Conditional Commitment (§ 5001.32(a)(1) and (2)). These two conditions are:

(1) The lender will monitor construction in accordance with approved plans and specifications, and

(2) Project funds will be used only for Agency-approved project costs.

Conditions Precedent to Issuance of Loan Note Guarantee (§ 5001.33)

The Agency has substantially revised this section. Except for certification for insurance obtained by the borrower, the entire section has been revamped and greatly expanded by including in the rule 17 specific conditions (§ 5001.33(a)) to which the lender must certify prior to the Agency's issuance of the Loan Note Guarantee under § 5001.34. Subject areas addressed by the 17 conditions in § 5001.33(a) are:

- Changes in the lender's loan conditions and requirement since issuance of the Conditional Commitment;
- Planned property acquisitions;
- Insurance;
- Truth-in-lending and equal credit opportunity requirements;
- Closing and security instruments;
- Title to the collateral;
- Disbursement of working capital;
- Personal, partnership, or corporate guarantees;
- Requirements of the Conditional Commitment;
- Lien priorities;
- Disbursement of loan proceeds;
- Material changes during period between Conditional Commitment and issuance of the Loan Note Guarantee;
- Financial interest in the borrower;
- Loan agreement content;
- Anti-Lobby Act (18 U.S.C. 1913);
- Title to rights-of-ways and easements and title opinion or insurance; and
- Maintaining the minimum financial criteria under which a loan application has been submitted, including those financial criteria contained in the Conditional Commitment, through the issuance of the Loan Note Guarantee. If these financial criteria are not maintained, the application will be ineligible.

In addition, a new paragraph (b) has been added, which requires the lender to provide an explanation satisfactory to the Agency if the lender is unable to provide any of these certifications.

Issuance of the Guarantee (§ 5001.34)

A new paragraph (a), Loan agreement, has been added, which requires the lender to provide a copy of the loan agreement between the lender and the borrower to the Agency prior to loan closing.

The Agency has moved the proposed requirement to provide the lender's certification and guarantee fee from proposed § 5001.34(a) into § 5001.34(b) and requires their provision at the time the lender requests the Loan Note Guarantee (rather than at loan closing as was proposed). Reference to the secondary market sale document has been dropped.

Paragraph (c) essentially is the same as proposed § 5001.34(b), with the reference to the issuance of the Assignment Guarantee Agreement dropped in the interim rule.

Reorganizations (§ 5001.36)

The Agency has made changes to paragraphs (a) and (b) of this section.

Change in borrower prior to closing (§ 5001.36(a)). As proposed, the last sentence in this paragraph read: ''Once the Conditional Commitment for Guarantee is issued, no substitution of borrower(s) or change in the form of legal entity will be approved, except that a change in the legal entity may be approved when the original borrower is replaced with substantially the same individuals or officers with the same interest as originally approved.'' The Agency has replaced the ''exception'' clause with ''unless Agency approval, in writing, is obtained'' so that this sentence now reads: ''Once the Conditional Commitment is issued, no substitution of borrower(s) or change in the form of legal entity will be approved, unless Agency approval, in writing, is obtained.''

Transfer of lender prior to issuance of the Loan Note Guarantee (§ 5001.36(b)). The Agency has reorganized this paragraph and has made a few edits to it. One change to note is the clarification that when the transfer is from a preferred lender to an approved lender, the approved lender submits an application that conforms to the requirements for an approved lender application for guarantee as found in § 5001.12(a).

Sale or Assignment of Guaranteed Loan (§ 5001.37)

General (§ 5001.37(a)). The Agency revised the requirement for lender retention. At proposal, the lender would have been required to maintain ''sufficient interest to perform its duties under this part.'' In the interim rule, this has been revised to read that the lender must ''retain a minimum of 5% of the total loan amount in its portfolio. The amount required to be retained must be of the unguaranteed portion of the loan and cannot be participated.''

The Agency also modified paragraph (a)(5) by:

(1) Removing ''at, or'', and

(2) Replacing ''market'' with ''sell'' and ''in default'' with ''in monetary default'' so that the paragraph now reads: ''If the lender desires to sell all or part of the guaranteed portion of the loan subsequent to loan closing, the loan must not be in monetary default.''

Lastly, the Agency removed proposed paragraph (a)(6), which addresses lender retention. This paragraph is no longer needed as a result of the other changes made in the interim rule.

Servicing fee (§ 5001.37(b)). The Agency revised this paragraph to read:

''The lender cannot charge the Agency a servicing fee and no such fees are covered under the guarantee.'' At proposal, the paragraph was titled ''Termination of lender servicing fee,'' and read: ''The lender's servicing fee will stop when the Agency purchases the guaranteed portion of the loan from the secondary market. No such servicing fee may be charged to the Agency and all loan payments and collateral proceeds received will be applied first to the guaranteed loan.'' Provisions in this paragraph were revised in § 5001.37(b) or carried over and revised in new paragraph, § 5001.37(c), as discussed below.

Distribution of proceeds (§ 5001.37(c)). The Agency added a separate paragraph to address the distribution of proceeds. As proposed, all loan payments and collateral proceeds received would have been applied first to the guaranteed loan. Instead, under the interim rule, all loan payments and collateral proceeds received will be applied to the guaranteed and unguaranteed portions of the loan on a pro rata basis.

Subpart B—Program Specific Provisions

Community Facilities Program (§ 5001.101)

Eligible projects (§ 5001.101(a)). The Agency has added ''except as provided in paragraph (a)(6) of this section'' to the end of the introductory text of paragraph (a). In addition, the Agency revised the requirements associated with refinancing (paragraph (a)(1)(vii) of this section) and added leasehold interest as a new eligible project (paragraph (a)(1)(viii) of this section).

As proposed, the eligible project was ''refinancing any loan,'' and provided that ''Except for the refinancing of Agency direct loans, refinancing of other loans will be limited to a minority portion of the guaranteed loan.'' In the interim rule, this eligible purpose is now titled ''refinancing debt (excluding working capital debt, operating or other debt whose repayment is scheduled to take place in one year or less)'' and includes three specific conditions to be met:

- The debts being refinanced are less than 50% of the total loan;
- The debts were incurred for the facility or service being financed or any part thereof (such as interim financing, construction expenses, etc.); and
- Arrangements cannot be made with the creditors to extend or modify the terms of the debts so that a sound basis will exist for making a loan.

The Agency, as noted above, has added ''leasehold interest'' as an eligible project and identifies several conditions, at a minimum, that must be met. These conditions are:

- The length of lease must be greater than or equal to loan term;
- There are no reverter clauses in the lease; and
- There are no restrictive clauses that would impair the use or value of the property as security for the loan.

The Agency has added a new paragraph (a)(5) to this section, which requires the project to primarily serve a rural area.

The Agency has revised the demonstration of community support (paragraph (a)(6)) to indicate that community support can be used in lieu of the debt-to-tangible net worth ratio and the loan-to-value ratio requirements for in subpart A. This is a conforming change.

Unauthorized projects and purposes (§ 5001.101(b)). Proposed paragraphs (b)(1) and (b)(6) were removed because they were duplicative of subpart A provisions.

The Agency added a new paragraph (b)(5), which identifies racetracks, water parks, and ski slopes as unauthorized projects and purposes. At proposal, these projects were identified in subpart A as unauthorized projects and purposes.

Borrower eligibility (§ 5001.101(c)). The Agency added introductory text to this paragraph, added a new paragraph (c)(1) to clearly specify the eligible borrowers, and revised paragraph (c)(2) to identify the YMCA, YWCA, Girl Scouts, and Boy Scouts as eligible organizations. At proposal, this paragraph only made reference to the later organizations.

Additional application documentation provisions (§ 5001.101(d)). The Agency has added four additional documentation requirements—organizational documents of the borrower, a complete list of governing board members of the borrower, a copy of the management and other legal documents between the borrower and the proposed management company, and a preliminary architectural report.

Additional application processing requirements—appraisals (§ 5001.101(e)). This is a new paragraph to the rule. This paragraph states: ''When a loan's collateral appraises at a level less than 100% of the loan amount, the Agency will consider community support in evaluating the application for guarantee.''

Additional origination responsibilities—leasehold interest (§ 5001.101(f)). This is a new paragraph to the rule. This paragraph states: ''Subject to approval by the Agency, a leasehold interest may be used as collateral for loans under this section provided the leasehold interest meets each of the conditions specified in paragraphs (a)(1)(viii)(A) through (C) of this section.'' The cross-referenced paragraphs refer to the requirements for leasehold interest to be an eligible project.

Additional servicing responsibilities—financial reports (§ 5001.101(g)). This is a new paragraph, which states: ''Annual financial reports required shall conform to 7 CFR part 3052.''

Additional guarantee- and loan-related requirements (§ 5001.101(h)). With the elimination of the low documentation and the preferred lender provisions for this program, the maximum percent guarantee for all projects under this section is now 90%. At proposal, a lower maximum percent guarantee (80%) was identified for lenders without preferred lending status who submit low documentation applications.

Water and Waste Disposal Facilities Program (§ 5001.102)

Project eligibility (§ 5001.102(a)). The Agency has revised the introductory text of paragraph (a) inserting ''except as provided in paragraph (a)(4) of this section'' to the end of the introductory text.

Paragraph (a)(1)(i) was revised from ''a water or wastewater facility'' to now read ''a water, waste disposal, solid waste disposal, or storm water facility.''

As for the Community Facilities program, the Agency has added a new paragraph (a)(3) to this section, which requires the project to primarily serve a rural area.

Also, as for the Community Facilities program, the Agency has revised the demonstration of community support (paragraph (a)(4) of this section) to indicate that community support can be used in lieu of the debt-to-tangible net worth ratio and the loan-to-value ratio requirements for in subpart A. This is a conforming change.

Unauthorized projects and purposes (§ 5001.102(b)). Proposed paragraph (b)(2) was removed because it was duplicative of a subpart A provision.

The Agency clarified paragraphs (b)(5) and (b)(8) by replacing the word ''applicant'' with ''borrower.''

The Agency added a new unauthorized project/purpose in paragraph (b)(6), which states: ''Any project where an individual, or membership of another organization sponsors the creation of a nonprofit organization with the intent to control negotiations for employment or contracts that provide financial benefit to the sponsoring organization, affiliate organization, or a subsidiary organization of the sponsoring individuals or organization.''

The Agency also removed proposed paragraph (b)(8), which addressed the payment of a judgment which would disqualify a borrower for a loan under proposed § 5001.102(c)(2), because changes elsewhere in the interim rule made this paragraph duplicative and thus no longer necessary.

Additional lender approval requirements (§ 5001.102(d)). This paragraph was added and states: ''The examination required under § 5001.9(c)(1)(iv) may be conducted by the Agency or a qualified consultant.'' This allows for the Agency to conduct the examination, whereas the referenced paragraph requires the examination to be conducted by a qualified consultant.

Additional application documentation provisions (§ 5001.102(e)). In paragraph (e)(1), the Agency rephrased ''qualified independent consultant'' to ''qualified consultant,'' because the term defined is ''qualified consultant'' and, as defined, includes the concept of ''independent.''

As for the Community Facilities program, the Agency has added three additional documentation requirements—organizational documents of the borrower, a complete list of governing board members of the borrower, and a copy of the management and other legal documents between the borrower and the proposed management company.

The Agency removed proposed § 5001.102(d)(3), which addressed financial reports, because the requirement for financial reports is addressed in subpart A in the rule.

The Agency added a new paragraph, § 5001.(e)(6), requiring lenders to submit intergovernmental consultation comments in accordance with 7 CFR part 3015, subpart V, of this title.

Additional servicing responsibilities—financial reports (§ 5001.102(f)). As for the Community Facilities program, this is a new paragraph, which states: ''Annual financial reports required shall conform to 7 CFR part 3052.''

Additional guarantee- and loan-related requirements (§ 5001.102(g)). With the elimination of the low documentation and the preferred lender provisions for this program, the maximum percent guarantee for all projects under this section is now 90%. At proposal, a lower maximum percent guarantee (80%) was identified for lenders without preferred lending status who submit low documentation applications.

Business and Industry Loan Program (§ 5001.103)

Definitions (§ 5001.103(a)). The Agency added two new definitions specific to this program in response to the 2008 Farm Bill. These definitions are for locally or regionally produced agricultural food product and for underserved community.

Project eligibility (§ 5001.103(b)). The Agency made several changes in this paragraph.

First. The Agency added the requirement that a project be located in a rural area (§ 5001.103(b)(1)).

Second. The Agency removed the word ''permanent'' so that § 5001.103(b)(2)(iv) now refers to working capital rather than to permanent working capital.

Third. The Agency revised the conditions under which refinancing would be an acceptable use of Agency funds. At proposal (§ 5001.103(a)(1)(x)), the provision for refinancing any loan read: ''Except for the refinancing of Agency direct loans, refinancing of other loans will be limited to a minority portion of the guaranteed loan.'' In the interim rule, this provision (§ 5001.103(b)(2)(x)) reads: ''refinancing any loan when the Agency determines that the project is viable and equal or better rates or terms are offered. Same lender debt refinancing will be additionally required to be less than 50% of the new loan amount unless the amount of the loan to be refinanced is already Federally guaranteed. Subordinated owner debt is not eligible.''

Fourth. The Agency moved the word ''complete'' from in front of ''pre-application'' and placed it in front of ''application'' in § 5001.103(b)(2)(xi).

Fifth. The Agency clarified that, while Business and Industry guarantee loan funds can be used for ''professional services,'' they cannot be used for either packager fees or broker fees (see § 5001.103(b)(2)(xii)).

Sixth. The Agency modified the conditions associated with tourist and recreation facilities, including hotel, motels, and bed and breakfast establishments (§ 5001.103(b)(2)(xiii)) by adding ''when the owner's living quarters is not included in the guaranteed loan'' at the end of the paragraph. This change also makes this provision consistent with the change to § 5001.103(c)(1).

Seventh. The Agency modified § 5001.103(b)(2)(xv) by replacing ''with certain restrictions'' with ''with Agency-approved restrictions'' so that this paragraph reads: ''housing development sites with Agency-approved restrictions.''

Eighth. The Agency added five additional uses and purposes for which guaranteed loan funds could be used as follows:

- Mixed use commercial and residential buildings on a pro-rata basis (residential real estate use portion not eligible);
- Operating lines of credit that are part of an overall guaranteed loan financing package under this section and that are used for certain payments (see § 5001.103(b)(2)(xix));
- Leasehold improvements, provided the underlying lease meets the requirements specified in § 5001.101(a)(1)(viii);
- The purchase of preferred stock or similar equity issued by a cooperative organization or a fund that invests primarily in cooperative organizations, if the guarantee significantly benefits one or more entities eligible for assistance for the purposes described in paragraph (d) of this section; and
- Establish and facilitate enterprises that process, distribute, aggregate, store, and market locally or regionally produced agricultural food products to support community development and farm and ranch income.

The provision to allow lines of credit as an authorized use of loan funds, as noted above, is only available for the Business and Industry loan guarantee program at this time.

Ninth. Lastly, the Agency removed proposed § 5001.103(a)(1)(xviii), assisting cooperative organizations, because such organizations are eligible borrowers and thus this provision is not required in this part of the section.

Unauthorized projects and purposes (§ 5001.103(c)). The Agency made changes to several paragraphs.

First. The Agency clarified the end of § 5001.103(c)(1). At proposal, this provision read: ''Businesses housed in private homes, except when the pro-rata value of the owner's living quarters is deleted from the value of the project.'' The rule changes this to now read: ''Businesses housed in private homes, except when the pro-rata value of the owner's living quarters is not included in the guaranteed loan.''

Second. The Agency recast how § 5001.103(c)(2) reads, but did not change its effect. At proposal, this provision (§ 5001.103(b)(2)) read: ''Projects in excess of $1 million that would likely result in the transfer of jobs from one area to another and increase direct employment by more than 50 employees.'' In the rule, this now reads: ''Any project that does not meet the requirements of paragraphs (d)(2), (d)(3), and (d)(4) in 7 U.S.C.,

§ 1932.'' This same change was made later in this section to § 5001.103(g)(2).

Third. The Agency removed from the rule proposed § 5001.103(b)(3).

Fourth. The Agency revised § 5001.103(c)(4) to address distributions or payment to immediate family members and employee-owned cooperatives. At proposal, § 5001.103(b)(5) read: ''Distribution or payment to an individual owner, partner, stockholder, or beneficiary of the borrower or a close relative of such an individual when such individual will retain any portion of the ownership of the borrower.'' In the rule, this provision now reads: ''Distribution or payment to an individual owner, partner, stockholder, or beneficiary of the borrower or the immediate family of such an individual when such individual will retain any portion of the ownership of the borrower, unless the Agency has determined that the distribution or payment is a part of the transfer of ownership within: (i) The immediate family; or (ii) an Employee-owned Cooperative.

Fifth. The Agency added a new paragraph (c)(5), addressing loan guarantees to lending institutions, investment institutions, and insurance companies.

Sixth. The Agency removed proposed § 5001.103(b)(6), assistance to Government employees, because this is adequately covered by conflict of interest prohibitions.

Seventh. The Agency added a new paragraph (c)(9) addressing loan funds may not be used to support inherently religious activities.

Borrower eligibility (§ 5001.103(d)). The Agency added a new paragraph (d)(1)(v), which makes cooperative organizations housed in an urban area eligible provided certain rural benefits and requirements are met.

Additional borrower requirements (§ 5001.103(e)). This is a new paragraph added as a result of the 2008 Farm Bill. This provision adds a requirement for borrowers with projects that establish and facilitate enterprises that process, distribute, aggregate, store, and market locally or regionally produced agricultural food products to support community development and farm and ranch income.

Additional application process requirements (§ 5001.103(f)). Two changes were made under this paragraph.

First. Proposed § 5001.103(d) would have obligated funds using a priority scoring system if funds were insufficient to cover all applications pending approval. The Agency would also have established a scoring priority system each year for publication in the **Federal Register**. In the interim rule, the Agency has replaced this method for determining which applications pending approval would be funded (when there are insufficient funds to cover all applications pending approval) based on the date and time a complete application is received, with first priority going to those complete applications received first.

Second. In response to the 2008 Farm Bill, a new paragraph has been added (§ 5001.103(f)(2)) in which the Agency in making or guaranteeing a loan for projects that establish and facilitate enterprises that process, distribute, aggregate, store, and market locally or regionally produced agricultural food products to support community development and farm and ranch income will give priority to projects that have components benefiting underserved communities.

Additional application documentation provisions (§ 5001.103(g)). The Agency added two new provisions to this paragraph.

First. The Agency added a new paragraph (g)(1)(iii) addressing the requirement for intergovernmental consultation comments to be submitted in accordance with 7 CFR part 3015, subpart V, of this title.

Second. The Agency added a new paragraph (g)(2) addressing simplified applications. This paragraph allows lenders to submit applications in accordance with § 5001.12(b) for loan guarantees of $400,000 or less.

Additional origination responsibilities (§ 5001.103(h)). The Agency has added four paragraphs concerning additional origination responsibilities and removed one proposed paragraph as described below.

First. The Agency added paragraph (h)(1) on financial statements to this section. This paragraph requires consolidated financial statements for variable interest entities in accordance with the Financial Accounting Standards Board financial interpretation 46, Consolidation of Variable Interest Entities, and eliminating intercompany transactions.

Second. The Agency added paragraph (h)(2)(ii) on leasehold interest as collateral to this section. This paragraph allows the use of leasehold interest as collateral subject to approval by the Agency provided the leasehold interest meets the requirements specified in § 5001.101(a)(1)(viii).

Third. The Agency has added paragraph (h)(2)(iii) for the discounting of collateral to this section. This paragraph identifies requirements to be followed when discounting collateral for this program. These requirements are specified in paragraphs (h)(2)(iii)(A) through (E) of this section.

Fourth. The Agency added paragraph (h)(3) on payment and performance bonds to this section. This paragraph requires a payment and performance bond sufficient to mitigate Agency risk if the project is never completed.

Fifth. The Agency removed proposed § 5001.103(e)(1), which addressed audited financial statements, because the rule now contains the financial statements requirements in subpart A for all of the programs included in the rule. Thus, this proposed paragraph is not required in this section.

Additional servicing requirements (§ 5001.103(i)). The Agency added this paragraph, which addresses repurchases. This paragraph states: ''Repurchased loans may be sold without recourse to third-party private investors.''

Additional guarantee- and loan-related requirements (§ 5001.103(j)). The Agency added two new paragraphs and revised three proposed paragraphs as described below.

First. The Agency added paragraph (j)(1) addressing marginal or substandard loans to this section. This paragraph states: ''It is not intended that the guarantee authority will be used for marginal or substandard loans or for the relief of lenders having such loans.''

Second. The Agency added paragraph (j)(3) addressing five conditions for lines of credit, which are found in paragraphs (j)(3)(i) through (v) of this section.

Third. The Agency has added a condition under which it may issue the Loan Note Guarantee prior to all planned property acquisition having been completed and all development having been substantially completed in accordance with plans and specification. This provision is found in paragraph (j)(4) of this section.

Fourth. The Agency revised paragraph (j)(5) (paragraph (g)(3) at proposal) to specify that the funding limits are to be applied on a per borrower basis. At proposal, individual borrowers could have obtained guaranteed loans totaling more than $25 million (or $40 million, if a cooperative). In addition, the Agency removed reference to ''under this section'' in paragraphs (j)(3), (j)(3)(i), and (j)(3)(ii). Lastly, the Agency added a provision under which the maximum principal amount of $40 million may be made to cooperative organizations. As proposed, the $40 million limit would apply to rural projects processing value added commodities (proposed § 5001.103(g)(3)). In the interim rule, this maximum amount can now be applied to a project that ''significantly benefits one or more entities eligible for assistance for the purposes described in paragraph (d) of this section.'' This provision was added as required by the 2008 Farm Bill.

Fifth. Because low documentation applications were dropped from the rule, the Agency has simplified the maximum loan guarantee percentages, which now apply equally to both approved and preferred lenders. There have been no changes to the maximum percent guarantees and loan amounts.

Rural Energy for America Program (§ 5001.104)

Project eligibility (§ 5001.104(a)). The Agency has added the requirement that the project be located in a rural area in order to be eligible (§ 5001.104(a)(3)). The Agency also revised paragraph (a)(1) by removing the word ''project'' from the end of the paragraph, so that it now reads, in part, ''or to make energy efficiency improvements.'' The Agency has added a provision (§ 5001.104(a)(4)) that would enable a project to include the refinancing of any loan when the Agency determines that the project is viable and equal or better rates or terms are offered provided that the debt being refinanced will be less than 50% of the new loan amount.

Additional application process requirements—obligation of funds (§ 5001.104(c)). As for the Business and Industry program, proposed § 5001.104(c) would have obligated funds using a priority scoring system if funds were insufficient to cover all applications pending approval. The Agency would also have established a scoring priority system each year for publication in the **Federal Register**. In the interim rule, the Agency has replaced this method for determining which applications pending approval would be funded (when there are insufficient funds to cover all applications pending approval) based on the date and time a complete application is received, with first priority going to those complete applications received first.

Additional application documentation provisions (§ 5001.104(d)). The Agency made several modifications to this paragraph as described below.

First. The Agency made two changes to the technical report requirement (§ 5001.104(d)(2)):

- The $200,000 threshold in the interim rule is to be based on total eligible project costs, whereas at proposal this threshold was based on the size of the loan guarantee being sought.
- In the interim rule, the lender is to submit the technical report ''to the Department of Energy (DOE) for review unless otherwise stated in a **Federal Register** Notice.'' This replaces the proposal language that discussed, in part, approval by the DOE and the submittal of a DOE technical report.

Second. For energy assessments and audits (§ 5001.104(d)(3)), the interim rule makes clear that the lender is to submit energy assessments and audits to the Agency for review. This direction was not included in the proposed rule.

Third. The Agency has clarified that the feasibility study is required for renewable energy system projects, and not for all projects, as would have been the case under the proposed rule, seeking a loan guarantee greater than $200,000 (§ 5001.104(d)(4)).

Fourth. The Agency added a new paragraph (d)(5) addressing the requirement for intergovernmental consultation comments to be submitted in accordance with 7 CFR part 3015, subpart V, of this title.

Additional origination responsibilities (§ 5001.104(e)). The Agency has added this paragraph, which contains three requirements. These three requirements parallel those in the Business and Industry program.

First. The Agency added a paragraph on financial statements (paragraph (e)(1) of this section). This paragraph requires consolidated financial statements for variable interest entities in accordance with the Financial Accounting Standards Board financial interpretation 46, Consolidation of Variable Interest Entities, and eliminating intercompany transactions.

Second. The Agency added a paragraph on discounting collateral (paragraph (e)(2) of this section). This paragraph requires the discounting collateral for this program in accordance with the provision found in § 5001.103(h)(2)(iii).

Third. The Agency added a paragraph on payment and performance bonds (§ 5001.104(e)(3)). This paragraph requires a payment and performance bond sufficient to mitigate Agency risk if the project is never completed.

Additional guarantee- and loan-related requirements (§ 5001.104(g)). The Agency has made a number of revisions to this paragraph, several of which were made in response to requirements in the 2008 Farm Bill. These revisions are described below.

First. The Agency clarified in paragraph (g)(1) that the lender must certify to the conditions specified in the paragraph.

Second. In response to the 2008 Farm Bill, the Agency added to this section paragraph (g)(2)(i), which establishes the maximum loan amount under this program at $25,000,000 and applies this limit on a per borrower basis.

Third. In response to the 2008 Farm Bill, the Agency added to this section paragraph (g)(2)(ii), which lays out seven criteria that the Agency will take into account in determining the amount of a loan guarantee under this section (see paragraphs (g)(2)(ii)(A) through (G) of this section).

Fourth. In response to the 2008 Farm Bill, the limit on matching funds has been raised from 50% to 75% (see paragraph (g)(3) of this section).

Fifth. The Agency clarified that, while professional service fees are considered part of eligible project costs, packager fees and broker fees are not eligible project costs (see paragraph (g)(3)(v) of this section).

Sixth. The Agency replaced ''permanent working capital'' with ''working capital'' in the list of eligible project costs (see paragraph (g)(3)(x) of this section).

Discussion of Comments

The proposed rule was published in the **Federal Register** on September 14, 2007 (72 FR 52618), with a 60-day comment period that ended November, 13, 2008. Comments were received from 55 commenters, yielding over 800 individual comments on the proposed rule, which have been grouped into similar comments. Commenters included Rural Development personnel, attorneys, financial institutions, trade groups, lender associations, and individuals. Most of the comments that the Agency judged to have merit have resulted in changes in the rule. There are also responses to many of the comments where the Agency has indicated that it will provide additional guidance in the handbook to the rule. The Agency sincerely appreciates the time and effort of all commenters. Responses to the comments on the proposed rule are discussed below.

General

Comment: Nine commenters stated that they ''commend'' or ''support'' USDA in proposing a unified guaranteed loan platform for its existing guaranteed loan programs.

Response: The Agency appreciates the commenters' support of the proposed platform.

Comment: In expressing their general opposition to the proposed rule, nine commenters stated that, if adopted as proposed, the rule would be the final step in getting the Agency out of the guaranty loan business and its mandate to create and preserve American jobs, because the Agency will have no lenders left participating in its programs.

One commenter noted that the proposed rule is much more restrictive than the current regulations and that, if this rule is implemented, the Agency will lose the support of the lenders, particularly because of the requirement that lenders use the more restrictive of lender's loan policy or program regulations.

Response: The Agency has made revisions to the rule in response to specific comments that address the general concerns of these commenters. For example, the rule does not require lending entities that wish to participate in the guaranteed loan programs included in this rule to submit copies of their loan origination policies and procedures, but instead a summary of those policies and procedures. As another example, the Agency reinstituted the current policy that the unguaranteed portion of the loan will neither be paid first nor given any preference or priority over the guaranteed portion.

The Agency disagrees with the commenter that the requirement for a lender to comply with its own policies and procedures where those are more stringent than those in the rule will result in a lender being more or less inclined to participate in the loan guaranteed programs included in this rule. Where a rule provision is more stringent than a lender's particular corresponding loan origination or servicing policy or procedure, the Agency understands that such a lender may be more inclined not to participate. However, the Agency believes that in such instances it is necessary to require compliance with the rule's more stringent policy or procedure, unless otherwise approved by the Agency, in order to manage risk.

Comment: One commenter stated that, as proposed, the requirements are too burdensome and serve no practical utility in eliminating project risk, borrower risk, or loan guaranty risk. This commenter also stated that, as proposed, the rule serves no practical utility to the Agency in making rural development guaranteed loan decisions, and increases the Agency's administration of the program rather than concentrating on rural economic development.

Response: The Agency agrees with the commenter that the proposed rule had provisions that were unnecessarily burdensome and perhaps provided limited benefits. The Agency has revised the rule to incorporate many suggestions made by commenters. Under the interim rule, the Agency is requesting the minimum amount of information necessary to suitably evaluate risk. For example, rather than requesting copies of a lender's policies and procedures, the Agency is requesting that the lender provide a summary of its policies and procedures. In addition, the Agency is implementing a preferred lender program for Business and Industry guaranteed loans that further reduces lender burden and Agency staff time on such loan applications. Further, the preferred lender program in the rule has more tangible benefits to the lender. With these and other changes made throughout the rule, the Agency does not believe that the provisions of the rule will impose undue financial hardship or unattainable eligibility requirements for lending entities wishing to participate in the loan guaranteed programs included in this rule.

Lastly, the Agency's goal is to better manage and reduce the risks discussed in the rule, not eliminate them as suggested by the commenter, from current program practices. To this end, the Agency believes that the rule achieves this goal.

Comment: One commenter stated that the Agency's Rural Development loan programs included in the proposed rule have a mission to create jobs and stimulate rural economies. According to the commenter, most of the proposed rule would impose undue financial hardship or unattainable eligibility requirements, making them ineligible projects.

Response: The Agency does not believe that the provisions will impose undue financial hardship or unattainable eligibility requirements. In addition, in response to specific comments that suggest reduction of unnecessary financial hardships and eligibility requirements, the Agency has made appropriate adjustments to the rule. For example, the Agency has revised the definition of debt coverage ratio to reflect its calculation on the basis of a typical year for the project. This reduces the eligibility issue for startup businesses and those that might experience hardships during economic downturns. The Agency has also removed the proposed equity requirement and replaced it with debt-to-tangible net worth ratio, a more useful and practical eligibility requirement.

Comment: One commenter stated that he did not see an improvement with offering a unified guarantee loan platform, especially from the lenders' perspective. In the commenter's opinion, the complaint of inconsistency from the Agency is overblown by a very few lenders who cross state lines and program lines. According to the commenter, having the guaranteed loan program regulations located in one series (7 CFR part 5001) will be handy for Agency staff but doubts that the lending community will really care or appreciate the effort.

Response: The Agency believes that having these guaranteed loan programs under one series (i.e., 7 CFR part 5001) will be useful to both Agency staff and lenders. It is the Agency's experience that there are a number of lenders currently participating in these guaranteed loan programs that cross state lines. This rule would expand the number of programs that these lenders can offer. Thus, the Agency believes there are tangible benefits to this platform that lenders will appreciate.

Comment: One commenter stated that the proposed rule fails to address what the commenter characterized as a ''lender- and borrower-unfriendly atmosphere (us against them)''.

Another commenter stated that the Agency should look at financial institutions as partners in a worthwhile endeavor, and that the proposed changes will seriously diminish that partnership and will drive lenders away from the program.

Response: The goal of the rule is to strengthen the partnership between the Agency and its lenders and borrower partners by streamlining the regulatory requirements of the guaranteed loan programs included in the rule. In addition, in preparing the rule, the Agency has accepted numerous comments from program stakeholders to further strengthen this relationship.

Comment: One commenter stated that the Business and Industry program must leverage the skill and delivery systems that already exist within the commercial bank lending community of this country and that the key is to develop a sound and measurable approval process for lenders that includes (among other things) minimum capital, minimum reserves, qualified personnel, risk rate management, documentation and delinquency review, underwriting supervision, and historical review for continued authority.

Response: The Agency agrees with the commenter and has accepted many of the lender's comments to ensure that this rule is consistent with business practices of the commercial lending community for the Business and Industry program and all of the programs associated with this rule's guaranteed loan platform.

Comment: Five commenters stated that the Agency should address the current problems with the slow delivery system of the guaranty programs (minimum 1 month, but usually much longer). The commenters stated that these issues result in borrowers and/or lenders declining to be involved in the guaranty programs because the timeframes for turnaround and the variance in requirements are not realistic in today's world. Two of these commenters stated that they do not believe the rule, as proposed, does enough to address the slow delivery system. One commenter suggested that a better program for lenders, especially for Business and Industry lenders, would include streamlining the process to make sure the Agency can deliver the guarantees in a very timely basis.

One of the commenters suggested that the Agency mandate approval time for loan approval and servicing actions, as the Small Business Administration (SBA) did years ago.

Response: One of the goals of this regulatory process is to develop a better balance between the needs of the Agency to provide proper oversight over the loan guarantee programs versus the needs of our lender partners for rapid loan guarantee decisions. In response to this and other comments, the Agency has revised the rule to further reduce the burden on lenders and the Agency to address only those areas necessary to properly manage risk associated with the programs. For preferred lenders, the rule now commits the Agency to act on loan applications from preferred lenders within 10 working days of the receipt of a complete loan guarantee application. Lastly, the Agency notes that, through this new platform, the paperwork burden for this program has been reduced by approximately 25 percent.

Comment: One commenter stated that the proposal retains the current limited delegated lending authority. According to the commenter, there is no value to requiring lenders to submit origination and servicing policies, provide monthly reports on loans in default, and provide notification within 5 days of any loan agreement violation, because these further restrict a lender's ability to manage these loans. The commenter recommended using the SBA's Preferred Lender Program as a guideline to expand delegated lending authority.

Response: In response to this and other related comments, the Agency has revised the rule to provide more tangible benefits to the lender by:

(1) Requiring lending entities seeking to participate in the guaranteed loan programs included in this rule to submit summaries of their loan origination and servicing policies and procedures,

(2) Providing monthly reports on loans that are in monetary default (rather than any kind of default as was proposed), and

(3) Providing notification of loan agreement violations within 15 calendar days (rather than 5 days as was proposed).

Finally, the Agency reviewed several other loan guarantee programs, including those for the SBA and for the Farm Services Agency (FSA). The Agency determined that the FSA loan guarantee program had features more appropriate for this rule and has adopted a number of the FSA program features for this rule.

Comment: One commenter stated that the delivery system that is so unique to the Agency, that has been so successful in the past, and that is envied by so many within government is being substantially abolished. The commenter also stated that local outreach, information, and accountability would become practically nonexistent.

Response: The Agency agrees that its delivery system provides extraordinary service to our rural customers. The Agency believes that the adoption of this rule will better empower the Agency's delivery system team to provide even better service in the future by enabling Agency staff to engage in increased program outreach and community development, in large measure by eliminating regulatory redundancy and emphasizing lender expertise.

Comment: One commenter stated that there is no provision in the proposed rule for outreach to lenders, and two commenters recommended that the Agency participate in the National Association of Government Guaranteed Lenders (NAGGL) and the National Association of Development Companies (NADCO) to improve communication with its lenders. Another commenter suggested that making sure the USDA staff are well trained and experienced in the programs they are administering will do more for the program than a new platform, especially for the Business and Industry program.

A fourth commenter stated that local outreach, information, and accountability would become practically nonexistent under the proposed platform.

Response: Outreach, information, and accountability are delivered at the State and local level to ensure our relationship with lenders is maintained. At the national level, the Agency works with a variety of national organizations to promote the programs and to determine if program adjustments are necessary to better meet the needs of our rural customers.

Comment: Two commenters stated that the proposed rule should address the current problems with the lack of uniformity in administration, due largely to decentralization and lack of training both at USDA and with lenders. One of the commenters encouraged the Agency to address these issues and offer a more responsive, more uniformly delivered, and more efficiently administered guaranty program that is borrower and lender friendly, but still maintains program integrity. The other commenter recommended that the Agency needed to better manage staff.

Response: The Agency acknowledges the commenters' points and considers the new platform to be just the first step in achieving greater uniformity in its administration of the loan guarantee programs. In addition, after the adoption of this rule, the Agency will accelerate its numerous training activities to ensure uniform and consistent adoption of the requirements of the regulation nationwide.

Comment: Two commenters stated that the Agency should rely more on the input of local offices and staff. One of the commenters stated that the proposed rule practically ignores grassroots participation and is aimed at large lenders, stating that ''local involvement is too little, too late'' and that local knowledge and input should be obtained as soon as a request is received. This commenter recommended that the present structure and Divisions become an integral part of the rule.

The other commenter stated that local directors should be allowed to approve loans high enough to allow for reasonable loan volume. According to this commenter, micro-management by the Agency's central office makes no sense at all—let your offices perform the tasks at local levels—this is why you hired them.

Response: The Agency believes that its field delivery system is critical to the operations of its loan guarantee activities. The regulation does nothing to diminish the importance of the field office in developing and processing loan guarantee applications. In fact, by eliminating unnecessary differences among the loan guarantee programs, the field offices will be able to spend more time in processing and servicing loan guarantees in these programs.

Lastly, with regard to the comment concerning the level of loans that local directors can approve, certain Agency field offices currently have approval authority of up to $10 million. The

Agency believes that this level is sufficiently high and has not modified approval authority levels in this rule.

Comment: One commenter stated that the Agency has attempted to create a Loan Specialist Accreditation Plan to help, but there is no implementation plan for this program nor has it been determined who is responsible to schedule and pay for the proposed training to the field specialists, the State Director or the National Office. The commenter stated that the skill level of the field specialists needs to be at least on par with the bank's commercial loan officers, so the field specialists can understand what the lender is doing with their loan analysis and why. The commenter concluded that anything less will hurt the Business and Industry program in quantity and quality of the portfolio.

Response: The Loan Specialist Accreditation Plan is not part of this rule, but, at the discretion of Agency managers, may be used in support of Agency training associated with the implementation of this rule.

Comment: One commenter suggested making each regulation self-contained, even if it means repeating the same rules four times. The commenter also stated that there are simply too many differences between these four lending programs to make them fit into the same mold.

Response: The Agency appreciates the commenter's concern and will use guidance material to assemble program-specific requirements for each of the programs included in the rule. However, as far as the rule itself is concerned, the Agency is retaining the subpart A and subpart B structure. Agency experience shows that there are more common elements associated with the guaranteed loan programs included in this rule than there are differences. Provisions for these differences are provided for in subpart B. Having a common platform for each of the guaranteed loan programs included in this rule will reduce burden for Agency staff, lenders, and borrowers, easing program delivery and improving efficiency. Grouping common elements in subpart A will assist lenders in managing diverse program portfolios and meeting Federal requirements.

Comment: One commenter provided a suggested list of the elements that increase the probability of a loss, in approximate order of risk:

—Startup company,
—Management without a proven business track record,
—Company that is unprofitable or has inconsistent retained earnings or cash flow,
—Equity which just meets a 10% or 20% minimum threshold,
—Personal guarantees with little outside net worth,
—Collateral which is unique or remote from an urban center,
—Loan officer with no Business and Industry experience,
—Collateral coverage which is not discounted sufficiently, and
—Lending institution with no Business and Industry experience.

Response: The Agency thanks the commenter for the input on those elements that contribute to risk. The Agency has taken these elements into consideration during the development of both the proposed and interim rules. The challenge in administering a loan guarantee program is the need to balance the interest in minimizing losses versus the need to take reasonable risk to promote rural development. This rule attempts to better balance interests by focusing on the risk management approach described in the proposed rule.

Comment: One commenter recommended that the Agency centralize its loan process, as SBA did years ago, and, except for the differences in eligibility and guaranty amounts, copy SBA regulations and standard operating procedures (SOPs), including SBA's preferred lender program (it works, and most USDA lenders know it and are members). Two other commenters stated that USDA should "copy" the SBA program, which the commenters described as a successful program.

Response: The Agency believes that the strength of its programs and program delivery systems is found in the local relationship our field offices develop in rural communities that we serve. To the extent that centralization of certain processes will improve the efficiency of the programs without damaging the critical local relationship, the Agency will centralize such processes. The centralized servicing center for the single family housing programs is but one example.

In its consideration of all of the comments received on the proposed rule, the Agency notes that it looked at a number of other guaranteed loan programs, most notably SBA and FSA programs. The Agency has revised various portions of the rule based on the FSA program, which the Agency found to be more in line with the types and size of loans the Agency guarantees than in the SBA guaranteed loan program.

Comment: One commenter stated that the publication of the new 1970 Environmental Regulation is critical to the successful implementation of this Unified Guaranteed Loan regulation for three reasons:

First. Currently, two separate environmental regulations will be used by the lenders. This will be confusing.

Second. For large projects that may require an environmental impact statement (EIS), 7 CFR § 1940.336 imposes upon the Agency the responsibility to contract and pay for the EIS which could cost millions of dollars.

Third. The new 1970 environmental regulations include streamlining in many aspects that will make the National Environmental Policy Act (NEPA) process more practicable.

The commenter stated that the 1970 regulation has been cleared by all Rural Development program areas and has been awaiting OGC review since June 2007. The commenter also recommended that every effort be made to expedite that review.

Response: The environmental regulation is a critical regulation in the operation of USDA Rural Development programs, including the loan guarantee program. The Agency is currently reviewing the environmental regulation to determine whether it is appropriate to revise it. The consideration of amendments to the environmental regulation is outside the scope of the proposed rule. Therefore, these comments have not been considered in the context of the finalization of this rule.

Comment: One commenter noted that the proposed rule indicates Subpart B of Part 4280 is removed and reserved. The commenter also noted that Section A of 7 CFR part 4280, subpart B, addresses the grant portion of the Agency's Renewable Energy Systems and Energy Efficiency Improvements Program and that no new grant regulation has been proposed. The commenter recommended that only Section B of 7 CFR part 4280, subpart B, be removed and reserved, thus leaving the grant, direct loan, and combination financing sections in the regulation. The commenter also questioned whether, if this new regulation is adopted, subpart A of 7 CFR part 4279 and subpart B of 7 CFR part 4287 should also be removed and reserved?

Response: The Agency agrees with the commenter that only Section B of subpart B of 7 CFR part 4280 should have been reserved and removed, and has made this correction. The Agency notes that the combined funding provisions found in Section D of subpart B of 7 CFR part 4280 have been revised to make necessary conforming changes as the result of the removal of Section B.

Comment: Two commenters stated that in Exhibit II—Guarantee Fee and Loan Closing Procedure Procedures: Item (b) should include a statement that all conditions in the Conditional Commitment have been met by the lender before approving the lender's loan closing documents.

Response: The proposed rule does not include an Exhibit II and therefore the Agency has not considered the comment.

Subpart A—General Provisions

Purpose (§ 5001.1)

Comment: Two commenters pointed out that proposed § 5001.1 stated that this part regulates ''Rural Development guaranteed loans.'' The commenters stated that this is misleading because the proposed new part covers only four of the guaranteed loan types offered by Rural Development.

Response: Although it is the Agency's intention to add the other guaranteed loan programs to this platform as determined by the Agency on a program-by-program basis at a later date, the Agency has revised the purpose statement to clarify that this part applies to the guaranteed loan programs specified in subpart B of this part.

Definitions and Abbreviations (§ 5001.2)
Applicant

Comment: Two commenters stated that the definition of ''applicant'' does not indicate whether it means the business or the lender because both are seeking a guarantee. One of the commenters stated that it is the lender who is seeking the guarantee and, therefore, the applicant and the lender are the same and asked why define both.

A third commenter suggested revising the definition of applicant to include both persons and entities to be consistent with the Business and Industry and the Renewable Energy programs.

Response: The Agency reviewed the use of the term applicant throughout the proposed rule and agrees that in some places the specific entity being referred to is unclear. The Agency decided that the term is unnecessary and has deleted it from the rule. In its place, the rule now specifies directly whether a particular requirement applies to the lender, the borrower, or both.

In making this change, the Agency also revised the definition of ''borrower'' to include a person that seeks to borrow money, which was referred to as a ''prospective borrower'' in the proposed rule. By making this change, the rule is simplified by using the term ''borrower'' and letting the context of the rule make the differentiation between ''borrower'' and ''prospective borrower.''

Finally, because the definition of applicant has been deleted, it becomes unnecessary to revise the definition to include ''persons.''

Comment: One commenter recommended that the term ''prospective borrower'' be replaced throughout the rule with the term ''applicant'' when appropriate, to be consistent with the definition of applicant.

Response: After considering this comment, the Agency agrees that the terminology in the proposed rule was inconsistent. In the rule, the Agency has elected to delete the term ''applicant'' and use the term ''borrower.'' The Agency then redefined the term ''borrower'' to cover ''the person that borrows, or seeks to borrow, money from the lender.'' The context in which the term borrower is used in the rule determines whether the rule is referring to the person that borrows money, or is seeking to borrow money, from the lender.

Approved Lender and Preferred Lender

Comment: One commenter suggested that definitions be provided for the terms ''approved lender'' and ''preferred lender.''

Response: The Agency agrees with the commenter and has added definitions for both terms to § 5001.2 of the rule.

Business Plan

Comment: Two commenters stated that the definition of ''Business plan'' should include a statement that all projected financial statements are to be completed by an independent certified public accountant in accordance with Generally Accepted Accounting Principles (GAAP) for all for-profit businesses. The commenters also noted that nonprofit corporations and public bodies should be required to obtain this only if the loan request exceeds $1 million.

Response: The intent of the definition of business plan is to provide broad guidance as to the minimum requirements of a business plan. The Agency notes that not all borrowers will be able to provide financial statements that are prepared in accordance with GAAP, but that such financial statements can still be acceptable if they are prepared in accordance with Agency-approved guidelines. The Agency will identify additional guidance as to what a business plan should contain for each specific program in a handbook. The Agency notes that, in response to comments specific to financial statements, the requirements associated with financial statements have been modified in the rule to require, for borrowers that have been in existence one or more years, the most recent audited financial statements of the borrower, unless alternative financial statements have been authorized by the Agency, if the guaranteed loan is $3 million or more, or the most recent audited or Agency-acceptable financial statements of the borrower if the guaranteed loan is less than $3 million. If the borrower has been in existence for less than one year, the rule requires the most recent Agency-authorized financial statements of the borrower regardless of the amount of the guaranteed loan request. Therefore, the Agency has not revised the definition of business plan in response to this comment.

Comment: One commenter stated that the definition of ''Business plan'' is too specific. The commenter stated that, with loans ranging from several hundred thousand dollars to tens of millions of dollars the requirements for business plans, the definition should be reasonably general to allow the borrower and lender to achieve reasonableness depending on the project.

Response: The Agency does not agree with the commenter that the definition of business plan is too specific. The definition is intended to identify the requirements that constitute a minimal business plan that would be adequate for the smallest projects where one is required. For larger, more complex projects, the Agency and/or the lender may require a more detailed business plan. Therefore, the Agency has not revised the definition of business plan in response to this comment.

Comment: One commenter noted that the definition of ''Business plan'' calls for description of the ''applicant's'' ownership structure, etc., and commented that, by definition, this would be in reference to the lender (''The entity that is seeking a loan guarantee under this part.'') rather than the borrower. The commenter suggested that ''applicant'' be replaced by ''borrower.''

Response: The Agency agrees with the commenter that, as the proposed rule defined applicant, this would refer to the lender when in fact this requirement should apply to the ''potential borrower.'' The Agency has revised the definition to indicate that this requirement applies to the borrower and not the lender.

Cash Equity

Comment: Twelve commenters commented on the need for a definition of cash equity. Commenters stated that the proposed rule did not provide a definition of cash equity and that a definition needs to be fully and carefully defined.

One commenter expressed concern that without a clear definition, the public could not effectively comment on the rule and stated that the point in time of its measurement should also be established. Another commenter added that depending on how cash equity is defined and the timing in the year, this could be a challenge for even strong businesses to meet.

Three commenters wondered if by cash equity, the USDA meant cash contribution.

One commenter suggested the cash equity could be 10% down payment, or define equity as the owner's interest in a building based upon the appraised value.

Response: As noted elsewhere in response to comments on the financial criteria associated with project eligibility, the rule does not contain a ''cash equity'' criterion (cash equity has been replaced with debt-to-tangible net worth ratio). Therefore, it is unnecessary to define ''cash equity'' because that term is no longer used in the rule.

Conflicts of Interest

Comment: One commenter stated that the definition of ''Conflicts of interest'' needs to be revised because, as written, it makes inter-family transfers of ownership ineligible.

Response: In response to a similar comment made by this commenter on proposed § 5001.103(b)(5) concerning unauthorized projects and purposes, the Agency has revised the rule to allow for inter-family transfers of ownership (see § 5001.103(c)(4) in the rule). The Agency believes that this addresses the commenter's concern both on proposed § 5001.103(b)(5) and on the proposed definition of conflicts of interest, and the Agency does not believe it is necessary to modify the definition of conflicts of interest. However, the Agency has decided not to include a definition of conflicts of interest in the rule and will instead provide guidance in a handbook on what the Agency considers to be conflicts of interest or appearances of conflicts of interest.

Cooperative Organization

Comment: One commenter stated that, by not including true cooperatives as part of the definition of ''Cooperative organization'', true cooperatives are no longer eligible entities for the Business and Industry program.

Response: The Agency agrees with the commenter that the proposed rule would have excluded true cooperatives as eligible entities and this was not the Agency's intention. Therefore, the Agency has revised the definition of cooperative organization to include true cooperatives.

Debt Coverage Ratio

Comment: One commenter stated that debt coverage ratio needs to be defined. Another commenter stated that the proposed definition is vague and that, if USDA uses the ''net operating income'' criteria, the minimum coverage ratio of 1.0 is a very high requirement and may result in the exclusion of some very worthwhile projects.

Two other commenters stated that the proposed definition needs to be revised to conform to normal banking practice and that non-cash expenses (e.g., depreciation) and debt service expenses (e.g., interest) should be added back to net operating income. One of these commenters suggested that debt coverage ratio should be defined as ''the ratio obtained when dividing a business's realistically-projected Earnings Before Interest, Taxes, Depreciation (and depletion for natural resource companies), and Amortization (EBITDA) by its annual debt service (principal and interest) on all loans of the business.'' This commenter noted that EBITDA is a clearly, widely-used and well-understood term in the banking industry. The other commenter offered a similar definition of ''a comparison of the company's cash flow, measured as EBITDA to the required debt service (principal and interest payments).'' This commenter stated that they prefer this standard industry definition over the definition that compares net operating income to the principal and interest requirements.

Response: The Agency agrees that the definition of debt coverage ratio needs to be revised and agrees with the commenters who suggested that the definition more conform to normal banking practice. Therefore, the Agency has incorporated the concept of EBITDA into the definition of debt coverage ratio in the rule.

Environmental Review

Comment: One commenter suggested adding a definition for ''Environmental review'', as follows: ''An analysis, as required by The National Environmental Policy Act (NEPA), of potential environmental impacts likely to result from the implementation of a proposal. This is documented by the appropriate report in the form of a: Categorical Exclusion (CE), Environmental Assessment (EA), or Environmental Impact Statement (EIS)''.

Response: The rule contains sufficient guidance as to what is expected for an environmental review. Thus, the Agency does not believe it is necessary to create a definition for environmental review.

Essential Community Facility

Comment: One commenter questioned the meaning of the phrase ''Not include a project that benefits a group of single individuals as opposed to a class within a community'' in paragraph (iii) of the proposed definition of ''Essential community facility.'' The commenter stated that a list of some examples of projects that are being referred to should be included.

Response: The Agency agrees with the commenter that the meaning in paragraph (iii) of the proposed definition was not clear. In the rule, the Agency has revised this paragraph to read ''benefit the community at large.'' The intent is that the project not benefit a specific individual or a uniquely defined set of individuals within the community. The Agency will provide additional guidance, including a list of examples, in a handbook for the rule.

Comment: Two commenters suggested that paragraph (vi) of the proposed definition of ''Essential community facility'' be expanded to state: ''Be located in and provide service to a rural community''.

Response: The Agency disagrees that it is necessary to modify the referenced paragraph to include ''provide service to a rural community.'' The introductory paragraph to this definition already states that the resulting service is to be provided to ''primarily rural residents.'' The Agency notes that in the rule the subject paragraph has been removed from the definition and placed in subpart B as a specific project eligibility criterion, where the Agency believes it is more appropriately addressed.

High Impact Business

Comment: One commenter noted that the definition of ''high-impact business'' could reasonably be construed to include a day-spa, an art store, or some other small business creating few jobs. The commenter stated that the Agency has developed the Socio-Economic Benefit Assessment System measurement tool, which can estimate a project's impact in terms of job creation, tax base increases, and gross domestic product, and recommended that ''high-impact'' be redefined in these terms versus the vague generality currently adopted.

Response: The Agency agrees that the types of businesses described by the commenter should not be considered ''high impact businesses'' as intended under this rule. The Agency, therefore, has revised the definition of high impact business to include reference to jobs with an average wage exceeding 125% of the Federal minimum wage. The Agency does not believe it is necessary to incorporate the metrics proposed by the commenter (e.g., tax base increases) to appropriately define high impact businesses.

Lender's Agreement

Comment: One commenter stated that the lender's agreement should be referred to as a form and not as an agreement.

Response: The Agency agrees with the commenter and has made the suggested edit.

Loan Agreement

Comment: One commenter noted that the definition of ''loan agreement'' refers to an Agency approved agreement and asked what the process is to approve a loan agreement.

Response: The process used by the Agency to approve a loan agreement is internal to the Agency and it is inappropriate to include internal procedures in the rule. The Agency will make clear the process in a handbook to this rule or in other internal guidance material.

Loan Note Guarantee

Comment: One commenter stated that a Loan Note Guarantee should be referred to as a form, not an agreement.

Response: The Agency agrees with the commenter and has made the suggested edit.

Negligent Loan Origination

Several commenters expressed concerns with the second paragraph of the proposed definitions of negligent loan origination and negligent loan servicing, which states the failure of the lender to perform its origination or servicing responsibilities in accordance with the origination or servicing policies and procedures in use by the lender.

Comment: One commenter suggested revising the definition of ''negligent loan origination'' to rephrase the ambiguous phrase ''at the time of the loan'' with ''at the time the loan is made.''

Response: The Agency agrees with the commenter and has made the suggested edit.

Comment: One commenter stated the proposed rule creates unpublished program eligibility guidelines and standards for loan origination and servicing for lenders. The Agency proposed to use unpublished origination standards, credit policies, and procedures of each lender that are unavailable to other lenders as a new standard. According to this commenter, this requirement places a dual, unfair, and undue burden on the lender. The commenter stated that the Agency proposes double, unpublished standards and procedures that are burdensome to lenders, mandating that lenders use their own credit policies or procedures if more stringent than the Agency's.

Elsewhere, the commenter stated that the Agency is proposing to hold lenders to three standards—a reasonable prudent lender, the lender's own credit policies and procedures, and acts and omissions standards. The commenter concluded that, combined, they are confusing, overly burdensome, and difficult to administer.

Response: The Agency believes that the commenter misunderstands the intention of the Agency. Each lender will, as is currently their practice, be using its own policies and procedures in underwriting a loan for Agency guarantee and need not be concerned with those of another lender. Thus, lenders will have full knowledge of the requirements necessary under this rule for submitting an application for loan guarantee.

Further, the Agency would expect a lender's policies and procedures to be consistent with a ''reasonable prudent lender'' standard, which would include acts and omissions standards. Therefore, the Agency disagrees with the commenter's conclusion that this rule and the lender's own policies and procedures would be confusing, overly burdensome, or difficult to administer. If the lender has any questions on the implementation on this issue, then they can seek Agency guidance.

Comment: One commenter stated that, as proposed, the rule would create unpublished eligibility metrics by including lender credit policies and procedures if those procedures are more stringent than published procedures and that it is unreasonable to use those policies, if stricter than the Agency's published standards, as unpublished credit, project eligibility, loan terms, or servicing standards not otherwise made available to the public. According to the commenter, this is unfair to borrowers, such as small businesses, because a borrower will have no knowledge as to how to become eligible and a borrower working with a lender with a stricter credit policy than the Agency's standard will not know that their project could possibly qualify with another Agency approved lender. Further, this requirement creates an unfair standard for projects by discriminating against projects that would qualify under one prudent lender with less stringent credit policies and procedures.

Response: While the Agency does not disagree with the commenter's concern, the Agency points out that this rule is intended to define the relationship between the lender and the Agency in order for the Agency to guarantee the loan presented to it by the lender. It is not the intent of this rule to lay out one set of conditions that all loans would be approved under, which is no different from the current situation that a borrower faces. In other words, a borrower seeking a loan will not know the various conditions required by one lender or another. This rule does not change that situation. If a borrower works with a lender who cannot qualify the loan under that lender's policies and procedures, the borrower is always free to work with another lender.

Comment: One commenter stated that the proposed unpublished standards go beyond current USDA Rural Development regulations and are onerous and unreliable for all lenders to equally comply to and be held accountable for.

Response: The Agency has intentionally set out to develop a new regulatory platform for administering its loan guarantee programs. In developing this platform, the Agency has implemented provisions that are different from the current programs being included in this rule. Thus, to the extent that this rule results in different and new requirements than current program regulations, this is intentional.

With regard to the concept that the rule established ''unpublished'' standards, the Agency considers this a matter of perspective. The Agency has elected to lay out a framework for originating and servicing guaranteed loans that relies more on the lender's own policies and procedures than on the Agency setting, or trying to set, one comprehensive standard that would apply to each of the included programs. To the extent that lenders have different loan origination and servicing standards, then the Agency understands the perspective that those policies and procedures are ''unpublished''; at least in the sense that they are not spelled out in a **Federal Register** notice or in the Code of Federal Regulations.

However, the Agency does not believe this to be a critical issue in the successful implementation of its guaranteed loan programs. Each lender that is approved for participation in this program will know both its own policies and procedures and those that are spelled out in the rule. Thus, the Agency does not agree that this results in a rule that is either ''onerous'' or ''unreliable'' to each lender.

Comment: One commenter stated that the proposed rule contains no credit or loan servicing standards that are not already found in the current regulations.

Response: The Agency believes that the rule contains the necessary elements for guaranteeing loans. In the absence of specific suggestions or recommendations from the commenter associated with this topic, the Agency cannot be more specific in its response.

Comment: One commenter stated that the proposed rule does nothing to eliminate the inefficiencies and inconsistencies that the Agency currently acknowledges exist in the programs.

Response: The Agency disagrees with the commenter. The Agency believes that developing a single platform for the delivery of these guaranteed loan programs improves the efficiency with which the Agency can deliver the programs and allows the Agency to reduce any inconsistencies across Agency offices.

Comment: One commenter disagreed with the third paragraph of the proposed definitions for negligent loan origination and negligent loan servicing for dealing with the inclusion of acts and omissions to act. According to the commenter, the prudent lender standard in the first paragraph of the proposed definition should prevail as in the current regulation.

Response: The third paragraph is not intended to narrow the requirement of the first paragraph, but rather is intended to include the notion of failure to act in addition to actual acts performed. As such, the Agency does not accept this comment.

Participation

Comment: One commenter stated, with regard to defining participation, that no participations will occur under the program because the new rule would preclude selling participations under the regulations due to the fact that the Agency requires no pari passu.

Response: The Agency has reinstated the concept of pari passu in the rule.

Permanent Working Capital

Comment: One commenter stated that, in the definition of ''Permanent working capital,'' the word ''liquid'' should be replaced with ''current.''

Response: The Agency has removed the definition of ''permanent working capital'' from the rule because the term is no longer used. In its place, the Agency is using the term ''working capital.''

Preliminary Engineering Report

Comment: One commenter noting that the definition of ''Preliminary engineering report'' is pertinent to the Water and Waste Disposal guaranteed loan program, there should also be a definition of a ''Preliminary architectural report'' for the Community Facilities guaranteed loan program.

Response: The Agency agrees with the commenter and has provided a definition of ''preliminary architectural report.''

Promissory Note

Comment: One commenter recommended that the words ''or on demand'' be deleted from the definition of ''promissory note,'' because guaranteeing a demand note can create a balloon payment, which is not allowed under the Business and Industry program.

Response: The Agency agrees with the commenter and has made the suggested edit. The Agency notes that, because of potential considerations on this edit with regard to acceleration, the Agency will provide guidance on this definition and change relative to the acceleration of loans in the handbook to the rule.

Comment: One commenter noting that ''bonds'' are included within the definition of ''promissory note'' in the proposed rule and can be the guaranteed instrument, suggested clarifying that a ''lender'' is the entity providing the debt financing, regardless of whether they are making a traditional loan or providing investment (''bond'') financing.

Response: The Agency agrees with the commenter that further clarification that a lender is the entity providing the debt financing is needed. However, the clarification is more appropriately addressed outside of the rule and the Agency will address this issue in the handbook to the rule.

Rural or Rural Area

Comment: One commenter stated that the proposed definition of ''rural or rural area'' includes Census Designated Places (CDPs), which are not part of the Consolidated Farm and Rural Development Act definition contained in § 343(13)(A)(i) and (ii).

Response: While the Agency would be able to include CDPs in the definition of rural or rural area as it applies to the Business and Industry and the Rural Energy for America programs even though CPDs are not part of the Consolidated Farm and Rural Development Act, the Agency agrees that CDPs are not required to be part of the definition of rural or rural area for these two programs. Therefore, the Agency has removed reference to CDPs in the definition of rural or rural areas for these two programs. The Agency notes that for both Community Facilities and Water and Waste Disposal Facilities, reference to CDPs in the rural or rural area definition remains in the rule.

Small Business

Comment: One commenter noted that, under the current program regulations, there is no definition of ''small business'' or size standards. According to the commenter, the proposed rule excludes, by implication, those businesses that exceed SBA size limitations, such as publicly traded companies or other large private entities. The commenter recommended that the definition of small business should be excluded from the defined terms under the program because it implies limiting the size of business entities that may be eligible to participate in the program.

Response: The rule keeps the definition of small business because it is a statutory requirement for the Rural Energy for America Program guaranteed loan program (as that program applies to rural small businesses). The Agency notes that the term applies only to this program and not to the other programs and does not limit the size of businesses that participate in the other programs.

Startup Business

Comment: One commenter stated that the proposed definition of ''Startup business'' needs to be clarified because it could be interpreted that only newly formed entities that are constructing ground up facilities would be considered startups. According to this commenter, all newly formed entities should be considered startup businesses.

Another commenter stated that, for borrowers that have established track records/experience operating businesses, but for accountant or attorney, recommended formation of a new entity for each additional site, the proposed definition is prohibitive and should not require the same tangible net worth requirements as a truly new business by a borrower with no prior history or experience owning and operating the business.

Response: The Agency agrees that the definition of startup business needs to be revised and has done so in the rule.

With regard to the comment recommending that all newly formed entities be considered startup businesses, in the revised definition, a newly formed entity would be considered to be a startup business even if the owners of the startup business own affiliated businesses doing the same kind of business, unless it buys an existing business or facility and the business or facility being bought remains in operation and there is no significant change in operations. In such instances, the newly formed entity would be considered an existing business, not a startup business.

With regard to the second comment, the Agency agrees that an existing business should not be treated as a new entity solely on the basis of changes that merely restructure the business. The revised definition of ''Existing business'' addresses this issue.

However, the Agency disagrees that it is appropriate to use the experience of individuals in an associated business in determining whether the business will be treated as a startup business or an existing business. While the track record of such individuals is helpful in evaluating the strength of the applicant, it does not change the fact that the entity itself is a new business that lacks an existing track record. Therefore, the Agency believes such a business should be treated as a startup business. The Agency has revised the definition of startup business accordingly.

Unincorporated Area

Comment: One commenter stated that the proposed definition of ''Unincorporated rural area'' only includes census defined place. The commenter stated that any unincorporated places that are less than 20,000 and not currently included as a CDP are not eligible as the language is written. The commenter suggested adding language to the definition of unincorporated area to include open country and small unincorporated places that are not included as census defined places.

Another commenter questioned whether all unincorporated areas are a Census Designated Place. The commenter then stated that, if not, this should be changed.

Response: The Agency did not intend to exclude open space from being considered a rural area. The Agency has revised the definition of ''rural or rural area'' to address the commenter's concern. The statute uses the phrase ''unincorporated area'' in the definition of rural area for the Community Facilities and the Water and Waste Disposal facilities programs. The Agency has determined to use the concept of census designated places as defined by the Bureau of the Census to be the equivalent of the term unincorporated area in the statute.

Abbreviations

Comment: One commenter recommended that abbreviations in addition to RUS and SBA be included in the rule.

Response: The Agency has removed the abbreviations section from the rule because it is no longer needed.

Agency Authorities (§ 5001.3)

Comment: One commenter stated that the Office of Inspector General required Administrator exceptions for the Business and Industry program to be reviewed by the Office of the General Counsel and the Under Secretary and questioned why that requirement was removed.

Response: The requirement referred to by the commenter reflects procedures internal to the Agency. Even though previously included in Agency regulations, the Agency has determined that it is not necessary to keep this reference to internal procedures in the regulation and, therefore, removed them from the rule.

Comment: One commenter recommended that appeals should only be conducted if the lender requests the appeal. The commenter stated that a business should not be permitted to appeal a guaranteed loan decision without the participation of a lender. The commenter noted that this approach is already in practice for USDA's Single Family Housing guaranteed loan program (see RD Instruction 1980–D, § 1980.399) and FSA guaranteed loan programs.

Another commenter stated that, because lenders are the applicants in all guarantee programs, appeals should be allowed only when participated in by the lender involved in the project.

Response: Both appeal situations referred to by the commenters are controlled by the National Appeals Division (7 CFR part 11). Because these rules apply to this regulation, there is no need for this rule to specifically address these appeal situations.

Oversight and Monitoring (§ 5001.4)

Comment: One commenter noted that the proposed rule seems to be increasing the USDA's micromanagement of lenders, rather than following SBA's lead in being an administrator of a lender's program for thousands of lenders.

Response: The Agency disagrees with the commenter's remarks. The Agency has made substantial changes to the rule to address similar concerns, especially with regard to no longer requiring copies of the lender's policies and procedures.

General (§ 5001.4(a))

Comment: One commenter suggested revising § 5001.4(a) to read ''The lender will cooperate fully with Agency oversight and monitoring of lenders'' in order to move the focus to the lender.

Response: The Agency agrees with the commenter's suggestion and has revised the text in the rule accordingly.

Comment: One commenter asked what the Agency review requirements for other lenders was, noting approved and preferred lenders are reviewed every two years.

Response: Under the rule, all participating lenders are either ''approved lenders'' or ''preferred lenders.'' This includes regulated and supervised lenders as well as other lenders. Thus, another lender would be subject to review at least every two years, regardless of its being an approved or a preferred lender.

Comment: One commenter suggested adding language that permits the Agency to assess the costs of the reviews of certain lenders (*e.g.*, safety and soundness examinations) to the lenders being reviewed. According to the commenter, this would be consistent with the current practices of the Federal Deposit Insurance Corporation and Farm Credit Administration.

Response: In response to comments made concerning lender eligibility, the Agency has included in the rule a provision that other lenders undergo an examination acceptable to the Agency in order to be eligible for participation in the guaranteed loan programs included in the rule. Thus, it is unnecessary for the Agency to include a provision in the rule for assessing the costs of the reviews of these lenders.

Reports and Notifications (§ 5001.4(b))

Comment: One commenter stated that requiring lenders to submit origination and servicing policies, provide monthly reports on loans in default, and provide notification within 5 days of any loan agreement violation, restrict a lender's ability to manage these loans, and there is no value to this.

Another commenter stated that § 5001.4(b) needs to be totally reworked to better address risk, and suggested completely replacing this paragraph with the following:

(b) Reports and Agency notifications. Lenders will submit to the Agency reports and notifications to facilitate the Agency's oversight and monitoring.

These reports and notifications include, but are not necessarily limited to:

(1) For all loans in monetary default, the lender shall provide monthly default reports in a form approved by the Agency.

(2) Notification in writing within 5 days of:

(i) Downgrade in the loan classification of any loan. The lender will advise the Agency of classifications upgrades in a reasonable period of time.

(ii) Loan is 30 days past due or is otherwise in monetary default.

(3) Any material change in the general financial condition of the lender since the last periodic report to be submitted semiannually.

(4) Otherwise required for non-routine servicing actions and as specified in this section.

Response: In consideration of these and other related comments, the Agency has made changes to the rule that address most of these commenter's concerns. Specifically, the rule does not require that lenders submit copies of their origination and servicing policies and provides for 15 calendar days, instead of the proposed 5 days, for providing the Agency with information on loan violations. In addition, the Agency is requiring under the rule default reports only for monetary defaults rather than all types of defaults as that term is defined in the rule.

The Agency agrees with the suggestion that any downgrades in a loan's classification be reported and has added this requirement to the list of items to be reported within 15 calendar days to the Agency. However, the Agency does not believe it is necessary to receive reports on upgrades in a loan's classification and has not added this to the rule.

With regard to the suggestion that the Agency be notified of only monetary defaults rather that all defaults, as that term is defined in the rule, the Agency is requiring that notifications on all defaults be submitted within 15 calendar days because it is the Agency's intent in managing risk that such problem loans are addressed in a timely fashion and provides the Agency with better and more up-to-date information in its monitoring of a lender's portfolio of Agency loans.

With regard to the suggestion on the material change in the financial condition of the borrower, the Agency intended this requirement to address the borrower rather than the lender, as was stated in the proposed rule. Thus, the Agency has retained this provision, but corrected it to apply to the borrower, as was suggested by the commenter.

Finally, one commenter suggested that reports and notifications include those ''otherwise required for non-routine servicing actions and as specified in this section.'' As the Agency understands this comment, we believe that text in § 5001.4(b) stating ''These reports and notifications include, but are not necessarily limited to:'' sufficiently covers the intent of the commenter's suggestion. Therefore, the Agency has not included the commenter's suggestion as a separate paragraph in the rule.

Periodic Reports (§ 5001.4(b)(1))

Comment: One commenter stated that the semiannual Guarantee Loan Status Report requirements of 7 CFR § 3575.69(d), which require the lender to report to the Agency the outstanding principal and interest balance on each guaranteed loan semiannually, should be stated and retained.

Response: The rule provides for the submittal of a periodic report on a semiannual basis under § 5001.4(b)(1). The periodic report to be used is Form RD 5001–8, Guaranteed Loan Borrower Status. The form provides for the reporting of outstanding principal and interest balance for the guaranteed loan.

Default Reports (§ 5001.4(b)(2))

Comment: One commenter noted that the proposed regulations do not define whether a default is based on the inability to make the payment from cash flows or if the facility is delinquent only if the payment is not made.

Response: The intent was to require monthly default reports for loans that are in monetary default, which occurs if payment is not made within 30 days after the payment due date. The Agency has revised the rule, including adding a definition for monetary default, to make its intention clear.

Comment: One commenter suggested that loan classification be adopted as the primary risk indicator used by Rural Development, because essentially all lenders use loan classification to monitor the risk in their portfolios. Requiring lenders to immediately notify the Agency of any change in loan classification is the most effective risk indicator to help the Agency focus its oversight activities on the highest risk borrowers and lenders and better understand its risk exposure in the portfolio.

Response: The Agency believes that there are a number of factors important to managing risk. The Agency agrees with the commenter that changes in a loan's classification is an important factor in managing risk and, therefore, has added a provision to the rule requiring lenders to notify the Agency when there has been an adverse change in a loan's classification. The Agency does not believe that it is necessary to require reporting when a loan's classification has improved.

Comment: Seven commenters stated that monthly reporting for loans in default is over-burdensome and recommended continuing to require every 60 days. Two other commenters suggested that a quarterly reporting frequency, rather than monthly, is sufficient.

Response: The Agency proposed a monthly reporting frequency for loans in default in order to better manage risk and potential Agency loss, and as noted in a response to a previous comment, the rule clarifies that monthly reporting is limited to loans that are in monetary default. The Agency further recognizes that monthly reporting, compared to quarterly or semiannual reporting, imposes increased burden on those lenders who have loans that are in monetary default. On balance, though, the Agency believes that the benefits of focusing on loans in monetary default on a monthly basis outweigh such increased costs and has retained the monthly reporting frequency for loans in monetary default.

Notifications (§ 5001.4(b)(3))

Comment: Several commenters stated that the 5-day period for providing notifications was too short.

One commenter stated that notification within 5 days is too short of a timeframe and not consistent with industry time standards and unreasonable for institutions. The commenter recommended that the Agency adopt 15-day notification period timeframes for paragraphs (b)(3)(i) and (b)(3)(ii) within this section.

Three other commenters stated that the five-day notification of a loan agreement violation is burdensome and unnecessary. One of these commenters suggested allowing the lender 30 days to report real problems to the Agency.

Two commenters recommended retaining the current regulation requiring notification within 10 days of any permanent or temporary reduction in interest rate.

Response: The Agency agrees that the proposed 5-day period for notifying the Agency is unnecessarily short and has changed this to a 15-calendar day period in the rule.

Comment: One commenter stated that it seemed unnecessary for the Agency to require immediate notification of an interest rate cut, because the Agency's exposure is reduced by this action and the interest rate changes will show up on the next quarterly or monthly status report.

Response: As noted in the previous response, the Agency has revised the rule to allow lenders up to 15 calendar days to provide notification of reductions in interest rate. However, the Agency is still requiring notification of all interest changes in order to ensure compliance with the underlying promissory note.

Comment: Five commenters provided comments on notification of a loan agreement violation.

One commenter recommended that, instead of a 5-day notice to the Agency if the lending agreement has been violated, notification to the Agency of borrower covenant default occur within 30 days of the lender's knowledge of the default. In support of this recommendation, the commenter stated that there are many items in a Lending Agreement, not all of which are readily discernable within 5 days of default. Other items may be readily discernable but create much overhead if tied to a 5-day notice. Such items include:

1. Reporting requirements: Notifying Rural Development within 5 days of covenant violation creates excessive reporting overhead and is burdensome to the lender. Thirty days is much more appropriate.
2. Insurance coverage: If the insurance company has failed to notify the lender of failure to pay insurance, the lender cannot notify USDA until it has knowledge of default.
3. Financial Covenants: Guaranteed Community Facilities may have annual, semiannual, quarterly or monthly reporting requirements. Breach of financial covenants cannot be known until reporting is received and the lender has had time to review the reports.
4. There are many other criteria including capital expenditures, negative pledges, no debt incursion, controls on the use of funds, etc., that may have drag time between the covenant breach, the lender's knowledge, the lender's response to the breach and lender's notification to USDA.

One commenter recommended that, for Community Facilities, notification of delinquencies be provided within 30 days of monetary default. The commenter pointed out that Community Facilities are non-profit organizations or public bodies. Debt Service Reserve requirements stipulate funding of the reserve overtime. The reserve fund may allow the payment to be made as agreed. The proposed regulations do not define whether the default is based on the inability to make the payment from cash flows or if the facility is delinquent only if the payment is not made. Thirty days is the normal collection period for regulated lenders. Reporting to its regulatory agency is based on 30, 60, 90 days past due and non-accrual.

One commenter added that placing more reporting requirements on lenders will only make it more difficult for lenders to participate in the Business and Industry program. This commenter pointed out that the Lender must certify in the Lender's Agreement at closing that the loan will be serviced in a prudent manner. This proposed oversight by the Agency is restrictive, and the Agency should trust that lenders will act in their best interest. Placing more reporting requirements on lenders will only make it more difficult for lenders to participate in the Business and Industry program.

Another commenter added that current reporting requirements are adequate for the Agency to mitigate its risk. Specifically, this commenter stated that requiring notification within 5 days of the violation of any term of the loan agreement is onerous and unnecessary, and does not allow for management of loss exposure other than by creating improbable standards so the Agency can claim improper servicing. For example, a borrower fails to submit financial statements by the specified date—the lender must notify the Agency within 5 days that the financial statements weren't received. To what effect? What will the Agency do with this information to mitigate its risk? Similarly, the loan agreement has financial covenants measured as of the end of the borrower's fiscal year but not due to the lender for several months. The lender wouldn't even know of the covenant violation until almost three months after it occurred.

This commenter also suggested that this type of requirement is more intuitively found in the Lender Servicing section than in Oversight and Monitoring and suggested moving it there.

Two commenters recommended that the current regulation be retained, stating that the current schedules are difficult enough for the lenders to meet, and to tighten them up would make them more difficult to accomplish and add no value to the servicing process.

Response: As noted in a previous response, the Agency has revised the 5-day reporting period to a 15-calendar day reporting period in the rule.

The Agency has not modified the language in the rule with regards to notifying the Agency based on when the lender became aware of the loan violation for two reasons. First, the lender is responsible for being ''on top'' of each loan it services. Second, writing into the rule a timeframe based on ''when the lender became aware of the loan violation'' would result in very practical issues of documenting when the lender did become aware of the loan violation. The Agency believes that it is more practical for the lender to properly service the loan and in the course of doing so will have knowledge of such issues. The Agency will provide guidance for failure to provide the Agency with information on loan agreement violations in a handbook for use by its field offices.

Comment: One commenter noted that there is an inconsistency in the language. Section 5001.4(b)(3) requires notifying the Agency within 5 days of default, but the Administrative section states that the Agency must be notified upon discovery.

Response: The Agency's intent is to require notifying the Agency as stated within the rule and not as stated in the preamble. As provided in the rule, notification is required within 15 calendar days.

Project Eligibility (§ 5001.6)

Comment: One commenter stated that the project eligibility section is redundant, because the existing and proposed rules provide Agency authorized and unauthorized projects, and thus should be eliminated. The commenter stated that the Agency has outlined eligible and ineligible projects in the proposed rule and no further eligibility criteria are needed unless the Agency has examples of projects that produced losses that should be included in the ineligible classification.

Response: The two areas of the rule being referred to by the commenter—(1) authorized and unauthorized projects, and (2) project eligibility criteria—have different purposes. The authorized and unauthorized project lists identify the types of projects that are, respectively, eligible or not eligible for loan guarantees. The project eligibility criteria then identify for those projects that are eligible for loan guarantees the minimum financial metrics required for the Agency to consider approving loan guarantees. The project eligibility criteria directly address potential project risks. Therefore, the Agency has retained both of these aspects in the rule.

Comment: One commenter suggested that the major eligibility requirements should be repeated and self-contained in the individual program portions so that the reader does not have to flip back and forth between sections.

Response: In developing the rule, the Agency considered what the commenter is suggesting. However, the Agency's fundamental rule of organization and structure provides for maintaining common provisions in subpart A and program specific provisions in subpart B. The Agency will use the handbook to address the commenter's suggestion.

Comment: One commenter suggested adding paragraph (e) to § 5001.6 stating that the project must comply with all environmental policies of the agency. The commenter states that non-compliance would then provide the Agency with a valid reason for rejection. The commenter recognizes that reference is made to environmental compliance in § 5001.7, and states that projects should also comply with the Consolidated Farm and Rural Development Act to protect wetlands and the National Historic Preservation Act (NHPA) to prohibit anticipatory demolition.

Response: The Agency currently relies on its existing environmental regulations and clearance process to ensure that projects comply with its environmental policies. This rule would continue this practice and a separate section as proposed by the commenter is not required to continue this practice. The Agency will provide its staff with additional guidance in a handbook on this rule to ensure projects comply with the Agency's environmental policies, as well as the provisions identified by the commenter contained in the Consolidated Farm and Rural Development Act and the National Historic Preservation Act.

Benefit a Rural Area (Proposed § 5001.6(a))

Comment: Two commenters suggested changing the wording under proposed § 5001.6(a) from requiring a project to benefit a rural area to: ''The project must be located in a rural area.'' According to the commenters, this would eliminate confusion and misdirection of assistance; otherwise, virtually any business transaction could claim to ''benefit'' some rural area.

Response: The Agency agrees with the commenters that the proposed requirement that all projects to be eligible must ''benefit a rural area'' needs to be revised. The Agency has revised the rule as follows: First, the Agency has moved the requirement concerning a project's relationship to a rural area from subpart A to subpart B so that each program can address it specifically. Second, except for the Water and Waste Disposal guaranteed loan program, the rule requires the project to be located in a rural area. Third, for the Community Facilities and the Water and Waste Disposal guaranteed loan programs, the rule requires that, for a project to be eligible, it must ''primarily serve a rural area.'' An example of primarily serving a rural area is where 51% or more of those being served must live in a rural area. The Agency will provide additional guidance on ''primarily serve a rural area'' in the handbook to the rule.

Comment: Two commenters requested that the concept of ''benefit'' be more fully defined. The commenters stated that the Agency needs to identify what constitutes a benefit to a rural area (e.g., jobs created, service provided, and whether the size of the benefit matters) because leaving this concept up to interpretation may lead to inconsistency, ambiguity, and Agency/lender conflict. One of the commenters added that the clarification should be opened for public comment.

Response: As noted in the response to the previous comment, the Agency has removed the provision that a project ''must benefit a rural area.'' Thus, there is no need to identify what constitutes a ''benefit.'' For the Community Facilities and the Water and Waste Disposal guaranteed loan programs, this requirement has been replaced with the requirement that the project ''primarily serve a rural area.''

Comment: Three commenters noted that existing regulations require the project to be in rural area, while the proposed rule states that the project must benefit a rural area. These commenters stated that ''benefit'' be the key element in determining eligibility, not ''location'' because many projects located outside of rural areas (such as food processing plants and ethanol plants) have major benefit to rural farmers and employees living in rural areas.

Response: As noted in the responses to the two previous comments, the Agency has replaced the requirement that a project must ''benefit a rural area'' with the requirement(s) that the project be located in a rural area and/or primarily serve a rural area. This change was made, in part, because the authorizing statutes for some programs require the project to be located in a rural area, which in itself provides benefit to the rural area. In addition, the requirement for some programs that the project ''primarily serve'' a rural area allows for the location of the project outside a rural area, provided a program's authorizing statute does not require the project to be located in a rural area.

Financial Criteria (§ 5001.6(b)) (Proposed § 5001.6(c))

Comment: Several commenters are against setting minimum financial criteria. One commenter said that current regulations are more than sufficient for policy. The second commenter expressed concern that some very viable projects may not be allowed if they are required to meet these financial criteria and that these financial criteria may limit the Agency's flexibility and flexibility is necessary to using the programs. The third commenter stated that credit decisions are subjective and rely on the analysis and decisions by credit personnel who are not constrained by specific requirements, but create unique loan proposals and terms based on each individual request. The third commenter also suggested allowing the Federal and State Program Directors to set the standards of measure through their underwriting processes rather than through regulations.

A fourth commenter stated that there is a possibility that a number of eligible applicants will be eliminated due to the loan-to-value requirement. Because of the inflexibilities or inconsistencies in project eligibility and loan-to-value ratio, this restriction of approval authority would not allow for the mitigation of situations that have merit, but that are not 100% consistent with these regulations.

The fifth commenter stated that project risk is not mitigated with the proposed metrics, but instead the metrics mitigate economic expansion in rural areas and that rural businesses that otherwise would qualify under the program would be ineligible under the proposed rules thereby discriminating against rural small businesses. This commenter stated that the Agency is making a mistake to mitigate project risk through eligibility metrics rather than through establishing credit evaluation and loan structuring standards. According to this commenter, the proposed project eligibility standard offers no utility to the Agency or program, creates an administrative burden on the Agency that it is not experienced to handle, is a disincentive for small businesses to participate in the Agency guaranty programs, and do little to create fair and published eligibility standards for projects, borrowers, and lenders to follow.

In contrast, a sixth commenter expressed support for having minimum financial criteria as a requirement for program eligibility. This commenter also stated that these criteria must be fully and clearly defined, as well as being somewhat consistent with GAAP and the realities of the business world.

Lastly, one commenter urged the Agency to distinguish borrower credit risk.

Response: The Agency first points out that it has modified the financial metric criteria to reflect that they are to be applied to the borrower's financial condition and not to the individual project.

The Agency proposed, and is maintaining in the rule, minimum financial criteria that borrowers must meet for their projects to be considered eligible for a loan guarantee under this rule. These minimum criteria have been established, primarily, as part of the Agency's overall effort under this rule to manage risk; in this case, project risk. These minimum criteria also provide program delivery consistency across the States and provide multi-State lenders the same level of expectation.

Any financial criteria established for the borrower will not be able to predict with 100% accuracy the success or failure of their projects. However, the Agency believes that the minimum financial criteria will reduce the number of unsuccessful projects.

Finally, it is important to note that these financial metric criteria neither replace the credit analysis that a lender undertakes in originating a loan nor guarantee that a borrower that meets the criteria will be issued a loan guarantee by the Agency. These financial metric criteria simply provide minimum financial thresholds for borrowers for their projects to be eligible under the program.

Comment: One commenter stated that the proposed metric criteria are credit evaluation standards that belong in the credit evaluation section of the regulations and should not be used as program eligibility standards.

Response: The financial metric criteria referred to by the commenter are not credit evaluation criteria, but set minimum financial thresholds for determining whether or not a loan guarantee application will be accepted by the Agency. Further, these minimum financial metric criteria do not replace the credit evaluation performed by the lender that is required when the application is submitted. Also, as noted elsewhere in this preamble, the purpose of these financial criteria is to address project risk, which is one of the three areas of risk the Agency is addressing under the new platform. For these reasons, the Agency is not moving these criteria to the credit evaluation section of the rule and is keeping them as minimum project eligibility requirements.

Comment: Two commenters expressed concern that a project would be ineligible if it fails to meet any one of the three financial metric criteria. One of the commenters noted that this is the biggest impact of the proposed rule and that these minimum eligibility requirements cannot be waived. The other commenter suggested that requiring a project to meet these criteria is going to make deals harder to get approved and make the program less feasible. This commenter also noted that, if a lender has stricter eligibility requirements, a project would be required to meet the lender's requirements. A third commenter stated that the metrics are too restrictive for rural businesses and will not create, retain or promote jobs or economic growth in rural communities.

Response: The Agency agrees that providing minimum financial metrics will eliminate some worthy projects from consideration for a loan guarantee. The Agency disagrees, however, that having the criteria will make it harder for a project to get approved because, even in the absence of the rule, the borrower would still need to meet the requirements of the lender. Finally, the Agency points out that the overall intent of this provision and others in the rule is to manage risk and these financial metrics are but one example of achieving the objective to mitigate project risk.

Comment: One commenter requested that the rules allow the project eligibility criteria to be met on a pro forma basis.

Response: As this comment applies to startup businesses, the Agency agrees that these eligibility criteria would be met on a pro forma basis and the rule allows this. However, for existing businesses, it is unnecessary and inappropriate to allow these criteria to be met on a pro forma basis. Existing businesses have a historical record and that record should be the basis for determining eligibility.

Comment: One commenter requested that the rule allow the financial criteria to be met at the time of issuance of the Loan Note Guarantee, not at time of application.

Similarly, another commenter stated that the Agency is proposing that rural businesses meet these metrics prior to evaluating the application and approving a loan guaranty rather than the current regulation which is prior to issuing the loan note guaranty. According to the commenter, this will result in fewer rural businesses, non-profits, and municipalities in participating in the Agency loan guaranty programs.

Response: As noted in responses to previous comments on this section of the rule, these financial metric represent minimum thresholds and do not determine whether or not the Agency will issue the loan guarantee. The Agency believes that borrowers meeting these minimum threshold criteria are more likely to succeed than those that do not. Thus, the Agency believes it needs to have this information at the time the application is received. Further, these minimum financial metric criteria, including any financial criteria identified in the Conditional Commitment, are to be maintained up to and through the point in time when the Agency issues the Loan Note Guarantee. Failure to maintain these minimum criteria will result in an ineligible application. Again, as stated in a previous response, just because a borrower meets the minimum financial metric criteria does not mean that the borrower will automatically receive the Loan Note Guarantee. The Agency will still review the lender's analysis and other information in making its determination on whether or not to issue the Loan Note Guarantee.

Comment: Two commenters stressed the difference in requirements for profit and nonprofit lending. One commenter stated that program underwriting should be different for profit and nonprofit lending and is against posting minimum standards through USDA regulations. It recommends the retention of the Guaranteed Facilities regulations on this subject as is. The other commenter pointed out that the accounting standards are different, the revenue streams are different, and the protection of stockholders in the event of a default is significantly different from the protection afforded taxpayers or rate payers in the event of a municipal default.

Two other commenters expressed similar concerns, stating that many of the requirements for lending to nonprofit corporations and public bodies do not work well with for-profit businesses. The commenters illustrated their concerns by referring to the proposed collateral requirement indicating a 1-to-1 debt-to-value ratio. According to the commenters this is common when lending to non-profit organizations and public bodies in the Water and Waste Disposal and Community Facility programs, but it is extremely uncommon and not recommended when loaning to for-profit businesses. A common maximum collateral ratio for for-profit businesses is a 1-to-1 debt to discounted value. Current regulations do permit lending over the maximum debt to discounted value only if the cash flow is unusually strong for the type of business and the ratio does not exceed 1-to-1 on the loan-to-value ratio.

Response: The Agency disagrees with the commenters that the financial metric criteria setting minimum thresholds need to be different solely on the basis of whether the borrower is a nonprofit or for-profit entity. Further, it is unnecessary at this stage of the process to require discounting when calculating the financial metric criteria, as suggested by the commenters referring to the loan-to-value criterion. Such discounting will occur, as directed by the Agency, when the lender conducts its analysis.

Debt Coverage Ratio

Numerous commenters expressed concern over using debt coverage ratio as a financial metric criterion, ranging from dropping this as a financial metric criterion to its appropriateness. These concerns are addressed below.

Comment: Three of the commenters stated that using this criterion would most likely eliminate most startups and expansions of businesses, which in general do not have a positive debt service coverage in the startup or expansion phases of operations. A fourth commenter stated that this specific metric would curtail the Agency's ability to support new businesses in rural areas that frequently have insufficient debt service coverage during ramp-up and, therefore, should be removed from the rule. Further, according to the commenter, it is common for solid businesses to expand into new projects which do not, initially, have debt service as individual projects, but have substantial long-term possibilities. Lastly, a fifth commenter stated that this criterion is particularly unfair to startup businesses who may not project this threshold for one or two years.

Response: The Agency agrees with the commenters that as proposed this financial metric could pose unnecessary difficulties for startup borrowers and expansions of such borrowers. Therefore, the Agency has revised the definition of debt coverage ratio to be based, in part, on the ''realistically projected earnings and cash injection.'' This change addresses the concerns of the commenters.

Comment: One commenter stated that defining a specific debt service coverage ratio could result in the exclusion of credit accommodations to otherwise qualified and desirable borrowers. According to this commenter, a mandatory coverage ratio would eliminate those companies who may have had a significant, but nonrecurring expense item in the most recent reporting period, applicants with growing and improving trends which permit a reliable projection of prospective repayment ability, and, by definition, startup applications. The commenter stated that a standard that sets forth a reasonable expectation of repayment ability is inherent in every reasonable loan request, but to attempt to quantify and codify a requirement that is often subjectively determined is inappropriate.

Response: The Agency believes that it is appropriate to include basic financial metric criteria as part of the Agency risk management strategy under this rule. However, we agree, as noted in the response to the previous comment, that revision to the definition of debt coverage ratio is needed to address startups and business expansions. This revision requires this ratio to be calculated based, in part, on the business' ''realistically projected earning and cash injection.'' This change provides flexibility to a business that has experienced, as the commenter states, a ''significant, but nonrecurring expense item in the most recent reporting period.'' Thus, the rule addresses this comment.

Comment: One commenter stated that it is not critical that a project has debt service as long as the borrower has debt service.

Response: The Agency agrees with the commenter. Because the rule allows the Agency to review borrower statements, the Agency does not believe it is necessary to make revisions to the rule in response to this comment.

Comment: One commenter stated that having a litmus test with no flexibility could be unfair to rural businesses with unusual circumstances, such as natural disasters or national economic downturns. Three other commenters also suggested that the rule should also provide for mitigating circumstances in case the ratio is not met.

Response: The intended benefits of improved risk management provisions included in the rule outweigh the potential loss of projects due to the occurrence of individual and unusual instances. Further, the rule has been modified to base the criteria on a typical operating year, which would accommodate businesses affected by unusual circumstances, such as those suggested by the commenter.

Comment: One commenter stated that a debt coverage ratio of 1.0:1 is a credit criterion and should not be used as a project eligibility standard. According to the commenter, it discriminates against borrowers and projects that may have high impact to rural communities that do not generate income for two or three years that the current regulations allow. The commenter recommended that the debt coverage ratio of 1.0:1 be incorporated in § 5001.16(b)(2)(ii), under Lender responsibilities—Origination, to provide parameters desired by the Agency without compromising project eligibility. By inserting credit evaluation standards in the proposed rules, the Agency can reserve the right not to approve a project either in the pre-application or application stage as opposed to never seeing a possible high impact project. In other words, project risk mitigation can be accomplished in credit evaluation and structuring the loan, not in creating an eligibility criterion.

Response: The rule allows the calculation of the debt-coverage ratio to be based on the ''realistically projected earnings and cash injection before interest, taxes, depreciation, and amortization by the annual debt service (principal and interest)'' rather than, as proposed, on ''the net operating income by a business's annual debt.'' This change in the calculation of the debt coverage ratio addresses the concern expressed by the commenter for borrowers and projects that may have high impact to rural communities, but that do not generate income for two or three years.

As noted in a response to an earlier related comment, the Agency continues to believe that providing minimum financial criteria for project eligibility is necessary to mitigate project risk and thus has not moved this or the other two financial criteria to the origination provisions of the rule as suggested by the commenter.

Debt Ratio Definition and Calculation

Several commenters commented on the definition of debt coverage ratio and how it is to be calculated. For example, one commenter stated that a minimum debt coverage of 1.0 is fine, but that the definition and calculation of this ratio is crucial. Specific comments suggesting changes are addressed below.

Comment: One commenter asked if the requirement is based on historical or projected financial statements or both. Another commenter expressed a similar question, noting that the proposed regulations do not state how long this coverage must be in effect, and then asked if this is historical debt service coverage or projected, a year or six months?

Response: The calculation of this financial metric would be based on either ''realistic information in the pro forma statements or borrower financial statements.'' The ratio is to be calculated based on ''a typical operating year after the project is completed and stabilized.''

Comment: One commenter suggested that there are many ways to look at debt coverage, and the less prescriptive, the better. A second commenter stated that instead of using debt coverage criterion, the Agency should use EBITDA (earnings before interest, taxes, depreciation, and amortization) coverage or allow USDA officers to ensure adequate demonstrated debt coverage. In addition, defining debt coverage based on net operating income is not appropriate for operating businesses, as this term is used with rental property and not with owner-user underwriting.

Response: The Agency agrees that there are many ways to assess and calculate debt coverage ratio. In consideration of this and other comments, the Agency has revised the definition of debt coverage ratio to take into account, in part, the concepts suggested by the one commenter on using EBITDA as a basis for determining the debt coverage ratio.

Comment: Three commenters stated that the proposed wording for Business and Industry guaranteed loans pertaining to debt service coverage ratio of 1.0 or higher is unclear and provided alternate wording to describe debt service coverage for Business and Industry guaranteed loans as ''loans for 100% refinancing should be able to demonstrate a historical debt service coverage ratio of 1.0 or higher for the refinanced loan and loans other than for 100% refinancing should be able to demonstrate a pro forma debt service coverage ratio of 1.0 or higher once fully operational'' for a project to be eligible. According to these commenters, the language in the proposed rule could suggest that historical cash flow must provide debt service coverage of 1.0 even though proceeds of the new Business and Industry guaranteed loan will be used to expand that business resulting in additional cash flow available for debt service, which is not logical.

Response: The Agency agrees the definition of debt coverage ratio as it pertains to the Business and Industry guaranteed loan program (as well as for the Rural Energy for America Program) needs to be further clarified. The Agency has revised the rule to incorporate part of the commenters' suggestion by requiring the financial metric criteria to be calculated from the ''realistic information in the pro forma statements or borrower financial statements of a typically operating year after the project is completed and stabilized.''

Comment: Two commenters stated that during the startup phase, the business's debt service coverage ratio may actually be less than 1.0 until later years when it is fully functional, and asked if this makes the projects ineligible.

Response: As noted in a response to a previous comment, startup businesses would be required to calculate this ratio based on a ''typical operating year'' once the project is completed and stabilized. If, based on that ''typical operating year,'' the ratio is less than 1.0, the project would not be eligible for a loan guarantee under this program.

Comment: Three commenters suggested that the debt coverage ratio of 1.0 is too low. Two of these commenters suggested that the debt coverage ratio should be increased to 1.20:1 or use the lender's normal established debt coverage ratio standard. The third commenter stated that the metric of 1.0 or higher may be acceptable for Community Facilities and Utilities, but is too low for Business and Industry, and that for-profit entities should have a ratio that is higher than 1.0.

A fourth commenter described its procedure for evaluating and monitoring the credit. The commenter compares the company's cash flow, measured as Earnings Before Interest, Taxes, Depreciation, and Amortization, to the required debt service (principal and interest payments). The commenter expects a sufficient coverage (1:1), but allows for periods of shortages when alternative sources of repayment or working capital are available. The long-term objective is for the customer to attain a coverage ratio that provides a 10 to 20% margin.

Two commenters expressed concern about the requirement of a debt service coverage (DSC) of 1.0 or higher to be eligible, because a DSC ratio of 1.0 is considered marginal or substandard when lending to a for-profit business and current Business and Industry regulations (7 CFR § 4279.101(b) last paragraph) prohibits issuing loan guarantees to marginal or substandard loans.

Response: As noted in previous responses, this financial metric criterion is intended to be a minimum threshold to be met in order for an application for loan guarantee to be submitted. It does not represent an assurance that any project that meets the minimum will be approved for the loan guarantee. The Agency may require, as reflected in the Conditional Commitment, a higher ratio be met in order to approve the loan guarantee.

In addition, in response to another comment, the rule in subpart B for business and industry specifically states under § 5001.103(j)(1): ''Marginal/substandard loans. It is not intended that the guarantee authority will be used for marginal or substandard loans or for the relief of lenders having such loans.'' In summary, the rule provides for the concerns expressed by these commenters.

Comment: One commenter stated that the proposed financial metric criteria are below industry standards for municipal finance. According to the commenter, a 1:1 debt service coverage is too low and is not acceptable in municipal financing and most USDA direct loans for utility financings require at least a 1.2:1 coverage ratio.

Response: The value selected for this criterion is the minimum acceptable value for a project to be considered for a loan guarantee; it is a minimum threshold value. As such, it is not intended to reflect industry standards or imply that all projects that meet this value will be issued a Loan Note Guarantee. The Agency will evaluate the lender's analysis on the project and determine if it will issue a Loan Note Guarantee on the basis of that evaluation and other material, not just the debt service coverage ratio. Therefore, the Agency has retained this value in the rule.

Cash Equity (Proposed § 5001.6(c)(2))

Numerous commenters were concerned over the proposed cash equity requirement for project eligibility. Many commenters stated that this proposed criterion was not well defined, was too stringent and inflexible, and needed to be dropped. For example, one commenter stated that a 10% cash equity requirement will eliminate most Business and Industry projects. Many commenters suggested alternatives to cash equity as potential financial metrics. The following summarizes the comments received on cash equity as a financial metric criterion.

Comment: One of the commenters asked, ''What is cash equity?'' and stated that the cash equity criterion would make it difficult for most loan proposals processed through Business and Industry to be eligible. One commenter suggested going with the GAAP definition of equity.

Another commenter stated that if the cash equity requirement is a cash match requirement, rather than a tangible book equity requirement as per the current Business and Industry Guarantee regulations, it will prohibit 100% loan financing of a new building even if the business or community facility currently has no long term debt, needs its cash for inventory or working capital, and has operated successfully for years. The commenter concluded that this requirement should be eliminated from the WEP, CF, and 9006 sections.

A third commenter stated that this metric should be dropped for several reasons:

(1) Requiring this metric to be met prior to an application being submitted rather than prior to loan note guaranty being issued is very restrictive to rural business, more so than the current Business and Industry Regulations, which will result in fewer eligible projects for consideration that offer job creation, growth or retention that would contribute to rural economic growth.

(2) Quality projects that otherwise would qualify under the existing regulations would not be eligible under the proposed rule.

(3) The Agency is proposing a confusing metric. This metric does not provide any indication of a company's capitalization, does not mitigate project risk, provides no assurance of cash flow, and adds no utility in determining a project's eligibility or mitigating a project's risk.

Two commenters stated that the proposed cash equity requirement would disqualify many of their existing USDA guaranteed customers. One of these two commenters added that these customers would not be disqualified because they were bad borrowers, but because they had invested all their available cash into growing their businesses, and this commitment by them should not be punished.

One commenter does not favor cash equity because business owners will have only enough cash on hand to operate their business, with the balance being reinvested or used to pay down their debt.

Response: While the Agency agrees that the proposed rule did not clearly identify what was meant by ''cash equity,'' the Agency has replaced cash equity as a financial metric criterion with debt-to-tangible net worth ratio, as discussed below in a response to comments suggesting alternatives to cash equity. For reasons stated previously in response to comments concerning the financial metric criteria in general, the Agency continues to believe that these financial metrics provide useful risk management aspects to the rule and has retained such criteria in the rule.

Comment: One commenter suggested eliminating the tangible equity requirement, because State loan committees provide additional objectivity in reviewing Business and Industry guarantees to mitigate perceived risk. According to the commenter, any remaining perceived risk could be mitigated by revising 7 CFR 4279.16(c) regarding State Loan Committees. These committees could be encouraged to supplement the credit quality standards found in 7 CFR § 4279.131 with loan-to-value maximums based on type of collateral, industry risk, regional lending practices, and other underwriting standards for credit quality.

Response: As noted in the previous response, the Agency is replacing cash equity with debt-to-tangible net worth ratio. Further, the Agency points out that §§ 4279.16 and 4279.131 are not relevant to the 7 CFR 5001 rulemaking process. Finally, the Agency notes that, in response to a comment from this same commenter on the use of State Loan Committees, the Agency will provide guidance in the handbook to the rule, which will note, in part, that each program will make a determination as to whether or not to have a loan committee. Therefore, the Agency has not revised the rule in response to this comment.

Comment: One commenter stated that GAAP does not define cash equity, financial statements are prepared in accordance with GAAP, GAAP does not calculate ratios, and that this is part of credit analysis.

Response: As noted in the previous responses, the Agency is replacing cash equity with debt-to-tangible net worth ratio, which is a GAAP defined measure. Thus, the concerns expressed by the commenter over the proposed cash equity criterion are no longer relevant.

Comment: Seventeen commenters suggested modifying the cash equity criterion as proposed or replacing it. Commenters frequently suggested using the current tangible balance sheet requirements, but others expressed concern with using them. The suggested alternatives and modifications were:

- Tangible net worth;
- Follow Title 12, Part 34, Subpart D, Appendix A, which gives detailed requirements for appraisals and loan-to-value ratios for construction loans;
- An overall balance sheet requirement is appropriate and has been a part of the Rural Development Administration's Business and Industry standards. Require GAAP balance sheet equity of 10% for existing business or 20% for new business. Most private sector lenders normally require balance sheet equity as defined by GAAP, not tangible balance sheet equity or cash balance sheet equity.
- GAAP equity with the addition of appraisal surplus at 10% and 20% for existing businesses and startup businesses, respectively. The 20% requirement for startup projects should allow equity contributions other than cash, such as land and buildings. Change the current tangible equity to 10% equity for existing businesses, figured according to GAAP, and allow subordinated debt to be considered equity.
- Replace ''cash equity'' with ''equity,'' including fair market value, with no reference specifically to ''cash.''
- Tangible sheet equity. For example, many businesses have substantial equity, but are short on cash.
- Tangible balance sheet equity for the Business and Industry section, as per the current regulations, and eliminate the cash equity requirement from the WEP, CF, and 9006 sections.
- Adjust tangible balance sheet equity requirement such that it is a balance sheet equity test (not tangible) for existing businesses, and stay at 20% tangible balance sheet for new businesses.
- Expand to an either/or whereby a borrower must have 10 or 20% tangible equity or inject 10 or 20% cash into the proposed project.

Some commenters stated that the inclusion of off balance sheet equity, such as the equity found in commonly owned real estate, should be allowed when calculating the leverage/equity requirement for program eligibility. One commenter stated that the balance sheet equity requirement should be eliminated completely, or at a minimum be modified to include the off balance sheet value of tangible assets and subordinated debt owed to the owner. The difference between the depreciated book value of real property assets and their current market value, as well as subordinated owner debt, should be considered if a balance sheet equity requirement is in place.

One commenter stated that the current requirements of tangible balance sheet equity of 10% for existing businesses and 20% for new businesses should remain the same for equity measurement; if cash is a concern, a liquidity measure should be imposed, such as 1:1 current ratio.

Two commenters suggested changing the requirement to tangible book equity for the Business and Industry section as per the current regulations. According to these commenters, the cash equity requirement appears to be a cash match requirement for the project and not a tangible book equity requirement as per the current Business and Industry Guaranteed regulations. If this is a cash match requirement, it will prohibit 100% loan financing of a new building even if the business (or community facility) currently has no long term debt, needs its cash for inventory and working capital for the expanded venture, and has operated successfully for years. The commenter stated that this is not good loan structuring. This commenter also stated that generally there has not been a tangible balance sheet equity (TBE) requirement for lending to nonprofit corporations or public bodies, but there have been very specific TBE requirements for lending to for-profit businesses. This commenter noted that this requirement was omitted from the proposed regulation and suggested that it be reinstated only for the Business and Industry portion of Subpart B of Part 5001.

Another commenter provided three reasons for using tangible balance sheet equity versus cash equity, and adds that cash equity should be removed from the Section 9006 Energy Program and be replaced with tangible balance sheet equity requirements that Business and Industry currently use for the same three reasons. This commenter's reasons, in brief, were:

(1) There is no difficulty in applying the tangible balance sheet equity criterion and GAAP provides clear guidance on tangible and intangible assets;

(2) The private sector is not moving away from the use of tangible sheet equity; and

(3) Requiring cash equity will result in significantly weaker guarantee applications and greater losses to the agency.

Another commenter believes that the minimum cash equity is generally not enough overall equity needed for a company; however, the balance of the cash equity and lender's expectation of the total equity or net worth allows for a balanced approach for USDA guaranteed loans. The commenter added that the contribution of specific operating assets, existing net worth, and subordinated debt positions often allow for a company to attain adequate equity for improved probabilities of a successful business.

Response: The Agency considered carefully all of the suggestions made by the commenters concerning cash equity as a criterion and the alternatives they presented. On balance, the Agency agrees with the commenters that cash equity may not be the most useful or practical metric to evaluate the project's equity, even if the Agency were to adopt some of the suggested revisions to cash equity offered by the commenters. Therefore, the Agency has decided to drop cash equity from the rule.

The Agency then examined the alternatives posed by the commenters, as discussed briefly below. In assessing a replacement criterion, the Agency agrees with the sentiment of many commenters that the metric needs to be commonly used and understood by lenders; for example, the metric is GAAP defined. Based on its assessment of the alternatives, the Agency determined that debt-to-tangible net worth ratio, a GAAP defined measure, is the most suitable replacement for cash equity.

One commenter suggested using Title 12, Part 34, Subpart D, Appendix A. Title 12 is a Comptroller of the Currency, Department of the Treasury regulation that describes real estate lending standards. As such, it is not suitable to be included as a metric for programs included in this rule because the purposes of these programs are much broader than real estate lending. However, the three financial metrics discussed in Title 12 are otherwise provided for in this rule. Further, in response to other commenters, the Agency modified the rule in subpart B for the Business and Industry and the Rural Energy for America programs to provide standards for discounting collateral. This modification addresses the commenter's concern.

Many commenters recommended using the current tangible balance sheet requirement, or some variation thereon, under the Business and Industry regulations. The Agency determined that tangible balance sheet equity is an Agency derived measure and is not either a GAAP measure or a measure used by the Risk Management Association. Further, even though this measure is familiar to Business and Industry lenders, the Agency has determined that other measures are more suitable and less complicated. Therefore, the Agency has decided not to adopt tangible balance sheet equity for any of the programs under this rule.

With respect to the suggestion that the Agency use GAAP equity with the addition of appraisal surplus at 10% and 20% for existing and startup businesses, respectively, the Agency points out that appraisals are used when making loans, but not for determining project eligibility. The Agency does not want to make lenders conduct appraisals with each application because this would be cost prohibitive. If appraisals are available at the time of application, they are to be submitted with the application. Otherwise, the lender must submit complete appraisals to the Agency before loan closing. Finally, this metric is used in the rule to establish a minimum threshold.

With respect to the suggestion that the Agency replace "cash equity" with "equity," including fair market value, with no reference specifically to "cash," the Agency points out that cash equity has been dropped from the rule and fair market value would be required when conducting appraisals and, as noted the above paragraph, appraisals are not required in determining any of the minimum financial metrics.

Some commenters suggested that the metric selected allow consideration of "off balance sheet equity." The Agency is concerned about allowing appraisal surplus in the calculation. If a lender wishes to use off balance sheet equity from another business, then that business can simply become a co-borrower. Thus, the Agency has not included "off balance sheet equity" in the rule.

Comment: Two commenters indicated that the cash equity requirement is too restrictive. One commenter stated that the result would be that many quality applications would become ineligible and that those that can come up with 20% cash equity most likely would not need a guaranteed loan. The other commenter stated that most businesses it works with struggle to meet the current requirement (10% tangible balance sheet equity for an existing business and 20% tangible balance sheet equity for a new business), and the proposed new rule would make most of its applicants not qualify for the program.

Response: As noted in responses to previous comments, the Agency has dropped cash equity as a financial metric criterion. In its place, the Agency is using debt-to-tangible net worth ratio. This financial metric differs from cash equity, in part, by not requiring the business to tie up assets in cash and provides more flexibility to businesses seeking a loan guarantee. Thus, the rule addresses these commenters' concerns.

Comment: One commenter stated that this metric may be acceptable for business and industry guaranteed loan, but is not acceptable for Community Facilities and Utilities. While the proposed regulations allow for community support to mitigate this measure, this will, according to the commenter, place Rural Development in the position of trying to quantify the value of community support versus cash equity.

Response: As noted in responses to previous comments, the rule does not include cash equity as a financial metric. Further, the Agency agrees with the commenter that certain financial metrics are not appropriate for all projects. Thus, the applicable financial metrics to be applied to Community Facilities and Water and Waste Disposal projects differ from those to be applied to business and industry projects. Specifically, Community Facilities and Water and Waste Disposal projects would be allowed to satisfy the debt coverage ratio and the debt-to-tangible net worth ratio criteria with community support. This approach is appropriate for these types of broad community supported projects and is also consistent with current program administration, with which the Agency has had good experience.

Loan-to-Value Ratio (§ 5001.6(b)(3)) (Proposed § 5001.6(c)(3))

Comment: One commenter stated that it would seem reasonable to require a certain loan-to-value, regardless of tangible net worth, because, given a fully depreciated building, the real net worth would be substantially higher than book value. According to the commenter, the real net worth is what would repay a loan if the collateral is liquidated.

Response: The Agency appreciates the commenter's support for a loan-to-value ratio, which the rule continues to provide for. Further, the Agency points out that it makes its decision on whether to issue a Loan Note Guarantee based on the value of the asset, in accordance with commercial lending standards and generally acceptable account principles, as the commenter suggests.

Comment: One commenter stated that the proposed rule is unclear in its application of loan-to-value and that adding this standard is not likely to improve credit quality, but will add confusion.

Response: The loan-to-value ratio will be applied in the rule as one of three metrics that must be met at the time an application is submitted for a loan guarantee under this program. Including loan-to-value ratio as a criterion is consistent with OMB Circular A–129, which provides guidance on the management of Federal credit programs and specifically refers to loan-to-value ratio as a criterion for managing programmatic risk. Thus, the Agency has retained this criterion in the rule.

Comment: Seven commenters suggested that the loan-to-value ratio be modified to take into account discounted values, as is the practice under the current Business and Industry regulations, and that the value of 1.0 is too lenient. Commenters also suggested either specific discounting values for certain types of collateral or letting lenders use their own policies for setting discounted values. Specific comments are presented below.

Two commenters suggested using current loan-to-value criteria for for-profit businesses as explained in RD AN 4279 (4279–B).

Three commenters agree that a loan-to-value of 1.0 would be okay if it is loan-to-discounted-value. Two of the commenters added that this means that you would use the market appraised value discounted as in the old regulation, and that this ratio should also be used. Another commenter recommended changing this proposed criterion to a discounted loan-to-value of 1.0 to 1.0 for Business and Industry projects.

One commenter suggested that a 1.0 loan-to-value ratio is extremely lenient and that it would be more prudent to insist on a loan-to-discounted value of no more than 1.0, specifying that collateral discounts are to be set by lender policy but never higher than 80% for fixed assets (real property and equipment) and 60% for current assets (accounts receivable and inventory).

Another commenter suggested that the Agency use the lender's commercial loan loan-to-value ratios established for commercial real estate/fixed assets, equipment, inventory, and accounts receivable and project specific.

Another commenter states that higher loan-to-value ratios would seem appropriate, as banks will normally go up to 85% on accounts receivable, 65% on land with entitlements/utilities, 50% on raw, and 100% on new equipment.

One commenter states that it generally wants a ratio of less than 1.0:1 for the loan-to-value, where value is defined as market value of the on-going operation.

One commenter stated that the proposed loan-to-value is too lenient. Federal regulations require lenders to establish discounted values for their credit policy. For real estate and equipment, normal advance rates would be 80% of fair market value or less.

One commenter suggests that this metric is too low for some programs.

One commenter stated that a loan-to-value ratio of no more than 1.0:1 is too risky and does not meet the Agency's goal of reducing risk. This measurement, as defined, means the loan will equal 100% of the value of the collateral. According to the commenter, a more appropriate loan-to-value ratio is a discounted-loan-to-value no greater than 1.0:1 and the commenter recommended that the Agency adopt an additional requirement that states that no loan should be greater than the discounted-loan-to-value ratio. According to the commenter, loan-to-value, as a measurement of risk, is a poor guideline in that a 1.0:1 loan-to-value means the loan equals 100% of the value of the collateral; or, in other words, there is no equity cushion. The commenter then stated that a discounted-loan-to-value is a better measurement of collateral coverage in that a discount is applied to the type of collateral pledged for the loan. The commenter noted that it is prudent to have equity in collateral.

Response: The Agency agrees that it is appropriate in evaluating a loan to determine the loan-to-discounted value ratio. The Agency further agrees that, for most loans, a loan-to-value of 1.0 is too lenient. However, the rule proposed a loan-to-value ratio of 1.0 as one of three minimum threshold levels that must be met in order for an application for loan guarantee to be submitted, not as a criterion for determining whether the Agency would issue a Loan Note Guarantee. As a threshold criterion, the Agency continues to believe it is appropriate to keep this ratio as ''loan-to-value'' and at a 1.0 level. Each individual program will evaluate loan applications and loan-to-discounted value ratios appropriate for the program. This will be done when the Agency considers whether to issue the Loan Note Guarantee and not at the application stage.

With regard to the suggested specific discounted values, the rule contains discounted values for the Business and Industry program and the Rural Energy for America program. For other types of collateral in these two programs and for the other programs, the Agency will identify appropriate discounted values in the Conditional Commitment. The lender is required to use either the discounted values in the rule or in its own policies and procedures, whichever is more stringent, unless otherwise approved by the Agency.

Comment: One commenter expressed concern over how ''value'' will be determined, and used examples of rural water pipelines and special purpose community facility buildings to show where the value is not equal to their cost. Similarly, another commenter suggested that this metric is not applicable at all for other programs, citing as examples that valuation of community facilities or utilities is very difficult and while they are invaluable to the community, they are valueless if not in operation or not operated to the expected level of efficiency.

A third commenter stated that no collateral value should be given on other assets, such as intangibles, unless the lender is a preferred lender, and then, it should be limited to a 25% discounted value.

Response: The Agency agrees with the concern expressed by the one commenter as to how value will be determined for those situations cited by the commenter.

With regard to the second commenter's concern not providing collateral value to other assets, such as intangibles, unless the lender is a preferred lender and then limiting it to 25% discounted value, the Agency agrees with basic tenet of comment with respect to intangibles and with discounting collateral as it applies to the Business and Industry and the Rural Energy for America programs. The Agency, as noted in a previous response, has addressed these concerns in the rule in subpart B for these two programs. However, for the Community Facilities and the Water and Waste Disposal programs, in consideration of the limited market for these facilities, the Agency will consider community support in lieu of the evaluation of equity. Finally, the Agency reiterates that at this stage of the process the loan-to-value ratio is a screening metric and does not need to address these concerns, which will be addressed when the Agency reviews the lender's analysis in determining whether or not to issue the Loan Note Guarantee.

Comment: One commenter recommended that the Agency specify that it may alter the discounted values in the rule from time to time as underwriting conditions change through the publication of a **Federal Register** notice.

Response: The Agency agrees with the commenter that the **Federal Register** provides a mechanism for modifying discounting metrics found in the rule. If the Agency elects to use this mechanism, it would do so through a proposed rule published in the **Federal Register** allowing for public comment.

Comment: Two commenters stated that there appears to be confusion in setting an equity ratio for applicants pointing out that project equity and tangible book equity do not mean the same thing. Project equity means the applicant has to provide matching dollars to the total project cost and is unusual when lending to for-profit businesses. This equity is determined more by discounting the value of the collateral than actually setting the project equity, and if a business has sufficient collateral even after discounting, USDA could approve a loan for 100% of the project so long as the business has sufficient tangible balance sheet equity.

Response: The Agency has revised the rule to state that the financial metric criteria are to be determined based on the borrower's position and the loan being sought. In addition, the proposed cash equity criterion has been replaced with a debt-to-tangible net worth ratio.

Unauthorized Projects and Purposes (§ 5001.7)

Comment: One commenter noted that under this section, it is proposed that certain projects not be considered as eligible type projects. The commenter expressed concern that certain projects, while financially risky, can still make good projects for the agency to be involved with, if additional financial and/or environmental assurances are in place to mitigate the risk. The commenter would prefer that new regulations require additional financial and/or environmental assurance in order to be guaranteed.

Response: There are several reasons as to why projects are identified as being ineligible. For example, some projects are ineligible because of the program's authorizing statute. Some projects are included as ineligible because they are not of the type that would be consistent with the types of projects authorized by a program's statute. This is especially true for racetracks and the authorizing statute for Community Facilities program. In other instances, the Agency has experienced losses to the extent that the Agency has determined that such projects are not acceptable. The Agency believes that the environmental and additional financial requirements in this regulation, and elsewhere, are sufficient to address project risk and does not believe it is in the best interest of the rule to include additional criteria in order to allow specific projects that fall within the list of ineligible projects.

Comment: One commenter stated that, although illegal in most States, cock-fighting (and possibly other businesses) is legal in Puerto Rico and possibly other areas of the country or U.S. territories, but probably not an appropriate business for a Federal loan guarantee. The commenter suggested considering language to address this issue.

Response: While lengthy and specific, the list of ineligible projects is not intended to be ''all inclusive.'' The Agency can use the annual NOFA process to identify additional other inappropriate projects, as specified in § 5001.7(o), as warranted. The Agency does not believe that it is necessary to include cockfighting in the list of ineligible projects.

Comment: One commenter recommended deleting proposed § 5001.7(a), investment or arbitrage, or speculative real estate investment, as an unauthorized project or purpose. The commenter explained that this is necessary for many rural development projects. The commenter also questioned what would constitute investment vs. non-investment properties. The commenter stated that both proposed § 5001.7(a) and (m), commercial rental, still meet USDA's mission to create jobs in rural areas and that to no longer allow this type of development is contradictory.

Response: The Agency does not disagree that certain projects included in the list of ineligible projects would provide jobs in rural areas. However, it is the Agency's experience that investment and arbitrage (which are currently prohibited in the current rules) and speculative real estate (where someone builds a property with the intent to sell when completed) do not create a lasting community benefit. With regard to proposed § 5001.7(m), properties to be used for commercial rental, not all such projects are ineligible. If the borrower has the authority to determine the tenants, then such a project would be eligible. The Agency will provide additional guidance in the handbook to the rule to further explain what is and what is not allowed under § 5001.7(l).

Comment: One commenter asked why water parks are no longer eligible projects under the Business and Industry program. Another commenter stated that golf courses have been great for community development in small communities, and that they would like to keep golf courses and other ''certain recreational facilities'' as eligible guaranteed purposes. The commenter added that these recreational facilities add to the quality of life for many rural citizens.

Response: After considering these comments, the Agency believes that the restrictions proposed by this paragraph are too broad across all of the programs. The Agency has revised this paragraph in subpart A to address golf courses and other similar recreational activities. All of the other projects identified in the proposed paragraph (racetracks, water parks, ski slopes) have been moved in the rule to subpart B for the Community Facilities program. This revision addresses the one commenter's question concerning water parks, which would be eligible under the Business and Industry program in the rule. Golf courses, however, remain as an ineligible purpose for all programs because the Agency has determined that, based on past experience, these projects represent unacceptable risk in comparison to the impact on the quality life for such rural community.

Comment: One commenter noted that proposed § 5001.7(c) would continue to disallow Business and Industry financing for businesses which receive 10% or more of their annual gross revenue from gambling activity. The commenter stated that State lottery programs are now widespread and are an accepted State Government revenue vehicle. The commenter also stated that many restaurants and recreational businesses receive significant lottery revenue, and it is a rare business that can afford to shun this State-authorized revenue source. The commenter recommended that ''Gambling'' should be defined to exclude State lottery programs, so that these otherwise-eligible businesses are not disqualified. Two other commenters also agreed that if a State allows and promotes a lottery, this should be allowed under Federal Business and Industry lending programs and the 10% requirement should be abolished.

Response: The Agency agrees with the commenter that this paragraph needs to be revised to recognize that State-authorized lottery proceeds are an important source of income for otherwise eligible businesses. Because such proceeds are State-authorized, the Agency believes it is appropriate to modify this paragraph to accommodate State-authorized lottery proceeds and has provided an exclusion for such proceeds from the calculation of the ''10 percent from gambling proceeds.'' In addition, the Agency has incorporated an exemption for public bodies and for not-for-profit approved projects only, such that any other funds derived from gambling activity, as approved by the Agency, conducted for the purpose of raising funds for the approved project would also be excluded from the same calculation.

Comment: Three commenters objected to § 5001.7(e) prohibiting the guaranteeing of lines of credit. One commenter stated that making lines of credit eligible would likely significantly increase program usage, as there is a need for working capital. The commenter pointed out that it is not an automation issue, since FSA Farm Programs regulations permit guaranteeing lines of credit. The commenter also noted that those FSA loans generally perform well, but that additional regulatory and administrative guidance would be needed to implement. One commenter stated that cooperative lenders commonly provide their financing to coops as lines of credit rather than promissory notes and that USDA should, at the very least, try out this authority on a demonstration basis, limiting it to loans to cooperatives only at first. Another commenter stated that today a seven year term loan is used to support a guarantee of the operating needs of a company but that this structure is often not the most effective method; especially, when you have borrowers with large seasonal needs for operational credit. This commenter suggested that guarantees for lines of credit be approved for a specific time period, possibly three to five years, provided the line of credit renewal is within the previously approved guarantee conditions.

Response: The Agency agrees with the commenters to the extent that lines of credit should be an eligible purpose under the Business and Industry loan guarantee program only. The Agency also believes that it is necessary to establish certain limitations on lines of credit. The rule, thus, has been modified to allow lines of credits as an eligible purpose under subpart B for the Business and Industry program.

Comment: Three commenters expressed opposition to the elimination of finders', packagers', or brokers' fees from the eligible list of costs. These commenters stated that the Business and Industry program and many lenders work closely with these entities to match clients with appropriate capital sources.

One of the commenters explained that intermediaries who understand and promote the guaranteed loan programs provided by Rural Development, are a valuable resource that should be utilized to continue promoting the programs as well as providing feedback to Rural Development. The commenter further stated that it is appropriate for Rural Development to pass on the ''reasonableness'' of those fees for each transaction and that the elimination of the fees would curtail the use of the programs in many parts of the country.

A fourth commenter stated that broker fees should not be allowed in loan proceeds unless the broker agrees to sign a compensation agreement form (and signed under penalty of perjury), disclosing all fees received—before and after closing, from all parties relating to loan, including secondary market purchasers of guaranteed loans, and lenders. The commenter also explained that many brokers are making large fees while providing very little benefit.

Finally, a fifth commenter recommended deleting finder's and packager's fees from the unauthorized projects and purposes list, as this is a way to refer quality projects to the program.

Response: Currently, the Community Facility program does not allow these types of fees as part of the guarantee. The Agency believes this is a reasonable position for all guaranteed loan programs because the Agency believes that the interests of the programs are best served by guaranteeing the project and not those entities who ''bring us'' the project. The Agency notes that the rule does not prohibit these fees from being charged; they just cannot be part of the guaranteed loan.

Comment: One commenter suggested expanding the language in proposed § 5001.7(i) to specifically prohibit the financing of any illegal activity, and proposed the following language: ''Any business deriving income from illegal drugs, drug paraphernalia, or any other illegal product or activity.''

Response: The Agency agrees with the commenters suggested language and has incorporated it into the rule.

Comment: Six commenters stated their opposition to disallowing the use of loan proceeds to pay a judgment. One commenter explained that in rural areas of America they sometimes encounter a business that has had a credit problem, but it is a problem that is a one time occurrence and that they need the flexibility to be able to pay off judgments to help put deals together. Another commenter also mentioned that the payoff of tax liens should be permitted if it is a reasonable situation. One of the commenters stated that eliminating the payment of any judgment seems to be going too far and that this should be underwriting criteria, not eligibility criteria. The commenter also stated that if the judgment can be refinanced as part of a debt restructure, then it should be okay. One commenter stated that clearing a judgment as a part of a larger project can be of significant benefit to a rural business and help to continue or restore its economic contribution to its community.

Response: As proposed, this paragraph would have prohibited the ''payment of a judgment.'' In reviewing the proposed language and considering the commenters' concerns, the Agency believes that the proposed paragraph was too broad, prohibiting certain actions that could benefit both the borrower and the Agency. In the interim rule, this has been changed to ''The payment of either a Federal judgment or a debt owed to the United States, excluding other Federal loans.''

Comment: Two commenters stated that they assumed that proposed § 5001.70(j) means that guaranteed loan funds cannot be used to pay the applicant for rental of machinery and equipment owned by the applicant, but that the language in the paragraph needs to be clarified.

Response: The Agency has rewritten this paragraph (§ 5001.7(i) in the rule) to better express its intent, which is, as the commenters pointed out, that loan funds cannot be used to pay the borrower for rental of machinery and equipment owned by the borrower.

Comment: Ten commenters were opposed to the disqualification of ''properties to be used for commercial rental when the borrower has no control over tenants and services offered.'' These commenters provided numerous reasons why this provision should be removed, including:

—The Business and Industry program is the only guaranteed loan program that can be used for non-owner occupied purposes;
—Financing for retail centers and office buildings has been a very good market for rural lenders;
—It helps establish shopping centers, office condos, and other multi-tenant properties in rural areas;
—Retail opportunities are born from such investments by developers;
—Such loans don't significantly add risk to the Agency;
—They support economic expansion and job creation in rural communities;
—Not all businesses can afford to build and renting is a good option to create vitality;
—There is a huge need for this type of commercial property in the rural areas;
—This provision will restrict the growth of infrastructure to be used in private enterprise in Rural America;
—It will take opportunities away from community banks, and put those in the hands of larger regional and national banks;
—Many rural areas lack suitable/modern commercial office space and the program helps to meet an important rural need; and
—The SBA cannot do these types of projects and therefore the use of funds is a good marketing tool for the Agency.

Response: As noted in a previous response, the Agency has not revised this provision. The Agency believes that it is important that only those commercial properties over which the borrower has control of the tenants will be eligible for a loan guarantee. For example, if a borrower builds a property with the intent to sell (e.g., speculative real estate), this may be inconsistent with the purpose of the program. Further, where an owner does not have control over the tenants, this may result in tenants using the property for unauthorized purposes. The Agency will provide additional guidance on this provision in the handbook to the rule.

Comment: One commenter recommended that § 5001.7(o) include restrictions in accordance with the Consolidated Farm and Rural Development Act (the prohibition against disturbing wetlands) and the National Historic Preservation Act (the prohibition against ''anticipatory demolition'').

Response: The Agency does not believe that it is necessary to revise proposed § 5001.7(o) (§ 5001.7(n) in the rule) to include restrictions associated with disturbing wetlands or anticipatory demolition because the rule already requires compliance with applicable Federal laws. Thus, the Agency does not believe it is necessary to include the suggestion here.

Borrower's Eligibility (§ 5001.8)

Comment: One commenter urged the Agency to include a credit standard of eligibility in addition to the eligibility requirements in this section.

Response: While the Agency agrees with the basic concern of the commenter, the provisions of § 5001.8 are intended to be the most fundamental eligibility criteria applicable across all programs. The rule provides for assessing the credit worthiness of the borrower through the project eligibility criteria and through the lender's credit evaluation (§ 5001.16(b)), in which the lender applies credit standards and analysis to the borrower. Further, through the Agency's process for approving lenders for participation in this program, the reasonableness of the lender's credit analysis procedures is reviewed.

Comment: One commenter stated that the mission of USDA programs is to assist rural communities and that the citizenship of owners should be irrelevant when the financing is for a fixed asset located in a rural area of the U.S. that will result in U.S. jobs created and retained in a rural area. The commenter recommended that a good solution is to add the provision, ''If the applicant does not fit this criteria, the guaranteed financing purposes must be limited to real estate improvements only.''

Response: The Agency has decided to not change the citizenship requirement as suggested by the commenter, but to leave it as was proposed. The Agency believes that the language, as proposed, will ensure the returns realized on the investments in rural America stay within the U.S. The Agency points out that foreign entities can still participate in these guaranteed loan programs if they partner with domestic companies.

Comment: One commenter recommended that § 5001.8(b) be revised to include language requiring any owner with 20% or more ownership interest in the borrower to also comply. This would be consistent with agency implementation of the Debt Collection Act of 1996 (DCIA).

Response: The Agency agrees with the commenter—that in order to be eligible not only must the borrower not be ineligible under the provisions of § 5001.8(b), but that each of the borrower's owners with 20% or more ownership interest in the borrower must also not be found to be ineligible under the provisions of § 5001.8(b). Such a provision is consistent with the DCIA. Thus, the Agency has revised this paragraph in the rule to reflect the commenter's recommendation.

Participation Eligibility Requirements (§ 5001.9) (Proposed Lender Eligibility Requirements)

Comment: One commenter stated that the proposed standards have no relationship to Agency guaranteed loan making and servicing or to current published regulations and provide no basis for assurance of lender Agency guaranty loan making competence, regulatory compliance, or reduction of lender risk.

Response: The Agency has made changes to the proposed rule in response to comprehensive public comments received that the Agency anticipates will improve the delivery of its guaranteed loan programs. These changes are most noticeable in the revised requirements for both approved lenders and preferred lenders, including, but not limited to, requirements associated with lender experience in similar loan guarantee programs. Thus, the Agency disagrees with the comment.

Comment: One commenter recommended deleting the two categories of lenders to be created, because there is no real advantage to either the lenders or the borrowers. According to the commenter, the two application requirements only serve to confuse the lenders, borrower, and Agency staff.

Response: As noted earlier in this preamble (see Changes to the Proposed Rule), the Agency has revamped the lender eligibility requirements such that there is only one type of lender (approved lender) for all programs except for the Business and Industry guaranteed loan program, and that approved lenders must submit ''full documentation'' applications. The

Agency is implementing a preferred lender program for the Business and Industry guaranteed loan program that provides distinct advantages. Thus, the Agency has made modifications to the proposed rule that address the commenter's concerns.

Comment: Two commenters submitted comments on institution eligibility. One commenter recommended the inclusion of language requiring that a federally chartered entity submit applications and other required documentation to the state office in the state where it maintains its principal place of business. The other commenter suggested clarifying that all Farm Credit System institutions with direct lending and investing authority are eligible lenders for all four existing Rural Development guaranteed loan programs.

Response: The Agency agrees with the two commenters that the rule needs to cover federally chartered entities. Therefore, the rule has been modified to state that state chartered entities are to submit applications and other required documentation to the State in which it is chartered. If the lending entity is federally chartered, then it is to submit the application to the State in which the entity's headquarters is located.

The Agency disagrees with the comment that the rule needs to clarify that all Farm Credit institutions with direct lending and investing authority are eligible lenders. The rule language stating ''Any regulated or supervised lender'' is sufficiently clear to provide that Farm Credit System institutions are covered by the provisions regarding eligible ''regulated or supervised lenders.''

Comment: One commenter stated that the entire section needs to be rewritten. According to the commenter, USDA Rural Development should not become a bureaucratic reviewer of lenders' worthiness to make a guaranteed loan. The commenter stated that this would slow the Agency's response on every bank's first time use of the program and send the opposite message that should be sent. The commenter stated that USDA should be doing everything possible to simplify the process and speed up the process. The commenter also noted that requiring approval of every new lender will make the process appear to be bureaucratic and will definitely slow the process, discouraging use of the Business and Industry program by every regulated lender.

Response: The Agency recognizes that requiring lender approval for participation in the guaranteed loan programs included in the rule adds a step to the process. However, the Agency believes that it is an appropriate step from the perspective of mitigating lender/institutional risk. Therefore, the Agency rejects this comment.

Comment: Two commenters addressed appeals. One commenter expressed opposition to a National Appeals Division and recommended that the final authority for guaranteed lending decisions rest with the Program Director. The ability to appeal should be restricted to the highest level of professional position rather than to a committee, which may be politically influenced. The other commenter stated that preferred lender eligibility should be a privilege rather than an absolute right, and that USDA should retain the non-appealable authority to determine that the conference of preferred lender status on any given lender is not in the Government's best interest.

Response: The Agency has not revised provisions associated with appeals because the appeals process is statutorily-driven and the Agency cannot change it within the context of this rule. Similarly, the Agency cannot make the decision to deny a lender preferred status and determine that decision to be non-appealable within the context of this rule. Therefore, no changes have been made to the rule with regard to appeals.

Comment: Two commenters suggested additional lender eligibility criteria. One commenter recommended that one criteria for both regulated and other lenders should be added—evidence of good standing with SBA and/or FSA's guaranteed loan programs if the lender has used either of their programs in the past two years.

The other commenter requested that any approved traditional or nontraditional lender be required to meet the following requirements:

(1) If not a credit regulated institution, the institution should be required to submit to Federal/State credit examination; and

(2) The lender must show its ability to perform as a Lender of Record and to service, through the Loan Agreement (loans) or Trust Indenture (bonds) and through the history of the organization's past performance.

Response: The Agency believes that the commenters' suggestions for evaluating lender eligibility are valid. In the application for lender approval, the Agency is asking for other guaranteed loan experience, which would identify any SBA and FSA guaranteed loan program experience that the lender may have. However, to ensure such information is provided, the Agency has revised the rule to require regulated and supervised lending entities with no outstanding Agency guaranteed loans and other lending entities provide other guaranteed loan experience, which would include any SBA and FSA experience. The Agency will also provide guidance in the handbook to the rule to assist program staff in evaluating such experience when reviewing lender approval applications.

The Agency has also revised the rule to require that other lenders obtain an examination acceptable to the Agency. The Agency believes that such an examination will further mitigate the institutional risks associated with the program. The Agency will provide guidance in the handbook to the rule as to what examinations will be acceptable to it.

Finally, the Agency believes that the requirement in the rule to provide the Agency information on the lender's credit management system and the information required in the lender's application (Form RD 5001–1) are already sufficient for the Agency to assess a lender's ability to perform and to adequately originate and service guaranteed loans. Therefore, the Agency has not added any additional provision specific to this comment.

Loan Origination and Servicing Policies and Procedures

Comment: Eight commenters provided comments on the submittal of lender policies and procedures. Two commenters suggested that not all lenders will be willing to submit a copy of their written policies and procedures for loan origination and servicing. One commenter also pointed out that some lenders may submit binders full of policy or provide reference to their websites, and that this requirement may not provide the expedited application review the Agency wants.

Three commenters stated that adopting it would further deter new lenders from using the program. One commenter stated that this requirement would be very burdensome to the Agency and the lender. This commenter also suggested that it would create a number of separate eligibility criteria and exceed the Agency's expertise and stated mission.

Another commenter stated that lender's credit and evaluation policy and procedures must be provided to the Agency. Banks credit policies are changed regularly and keeping up with changes would be impossible for the Agency.

One commenter stated that there is no value to requiring lender's to submit origination and servicing policy; it just serves to further restrict a lender's ability to manage these loans.

Two commenters pointed out that current Business and Industry regulations do not include the requirement that if the lender's credit policies and procedures are more restrictive than Agency regulations, the more restrictive lender's policy shall be followed.

Three commenters suggested that the requirements of the agencies that regulate lenders should be sufficient.

One commenter stated that requiring a lender to supply its written policies and procedures to become an Agency approved lender is too burdensome on the lender and the Agency and serves no practical utility or purpose in guaranteed loan making. Instead, the commenter suggested that it serves the Agency more utility and efficiency that the lender adopts the Agency's regulations to the lender's existing credit policies and procedures and executes the Lender Agreement with the Agency that states so. According to the commenter, the Agency is not equipped to evaluate lender credit policies and procedures for commercial loans that do not relate to loan guarantees issued by the Agency.

Response: The Agency has revised the rule to not require lenders to submit copies of their policies and procedures at the time of lender application. Instead, the rule requires lenders to submit a written summary of their loan origination and servicing policies and procedures. Such information is still important to the Agency in its evaluation of lenders for approval for participation in the program. Further, the Agency revised the rule (see § 5001.15(d)) to require the lender to notify the Agency of any changes to its loan origination and servicing policies and procedures provided under § 5001.9(a). In addition, if a lender makes any changes to its loan origination and servicing policies and procedures that are inconsistent with the requirements of this part, the lender is required to notify the Agency in writing and the lender must receive written Agency approval prior to applying the changes to loan guarantees under this part.

Comment: One commenter stated that it is not unreasonable to request copies of lender credit policies and procedures. The commenter noted that there are over 1,400 lenders now participating in Rural Development guarantee loan programs who would be required, under the proposed rule, to present their credit policies and procedures to become a Rural Development approved lender and when a loan loss report is submitted. This requirement is burdensome to the lender and the Agency and adds no value to granting loans with guarantees, or mitigating what the Agency has referred to as ''institutional risk.''

The commenter further stated that the Agency proposes to monitor over 1,400 credit policies and procedures, which serves no utility in loan servicing or guaranteed loan making. According to the commenter, the Agency is not qualified or experienced enough to monitor this requirement and that it will be virtually impossible for the Agency to monitor over 1,400 lender credit policies and procedures and compare them to the proposed rule for compliance.

Response: In response to this and other related comments, the Agency has revised the rule to require lending entities seeking to participate in this program to submit a summary of their loan origination and servicing policies and procedures rather than copies. This will reduce the burden on the lenders and reduce the amount of material to be reviewed by the Agency. The Agency continues to believe that such information is important in considering lenders for approval, especially those who do not have guaranteed loan portfolios with the Agency, as one of many provisions for managing institutional risk.

The Agency disagrees with the commenter's characterization that the Agency does not possess the necessary qualifications to assess a lender's policies and procedures for originating and servicing loans under this program.

Comment: One commenter suggested changing the word ''participate'' to ''originate'' in the introductory language to § 5001.9, which states that only lenders approved by the agency can participate in the program.

Response: The Agency has not changed ''participate'' to ''originate'' as suggested by the commenter because the word ''participate'' covers both originate and service, which is what the Agency intends.

Regulated or Supervised Lenders

Comment: Several commenters stated that regulated and supervised lenders should not have to submit an application for lender approval, while non-regulated lenders should receive scrutiny.

One commenter stated that all federally regulated financial institutions should be approved by default. The commenter also stated that non-regulated lenders should receive heavy scrutiny.

Another commenter stated that they believe that the non-traditional and non-regulated lenders are the only ones that should face an approval process from USDA. The commenter further stated that the automatic approval of all state and federally regulated commercial lenders should remain the way it is, but that it would be acceptable to require the extra approval process for the preferred lenders.

Two commenters stated that regulated and supervised lenders should not need to submit an application to the USDA. One commenter pointed out that existing federal regulations cover such lenders already, and the other commenter stated that because the standards for approved lender status appear to be very simple, any regulated lender should qualify. The other commenter suggested that, in lieu of application, USDA should only ask for the written policies (and certificate of good standing) with the first application.

One commenter stated that the current practice in the Business and Industry program requiring only non-traditional lenders to apply is sufficient; the requirement for regulated lenders to apply for participation is unnecessary and does not significantly reduce Agency risk. The commenter pointed out that the issue is suspending poor performing lenders rather than creating burdens for those not yet involved. The commenter also offered an alternative for reducing risk: Any lender with greater than 15% guaranteed loan portfolio delinquency (measured on September 30 each year) be suspended from new loan generation for 12 months. Standards for first-year or first-three-year delinquency and/or portfolio losses could also be promulgated.

Response: The Agency disagrees that federally regulated financial institutions should be approved by default. As noted in a previous response, the Agency recognizes that lender approval adds a step to the process, but believes it is appropriate and prudent from a risk management perspective. In addition, the Agency has revised the rule to require other lenders to have undergone an examination acceptable to the Agency. The Agency believes that the rule provides sufficient and necessary requirements both for regulated and supervised lenders and for other lenders. Additional steps to become a preferred lender are included in the rule.

With regard to the suggestion that the Agency rely on the evaluation of lender performance once a year and suspend those that fail to meet an acceptable level of performance in lieu of an initial approval step, the Agency believes that removing the approval step places too much of the risk management after the fact. The rule incorporates provisions for maintaining approved and preferred lender status and these provisions address lender performance. By requiring an approval process up front, the Agency intends to reduce the number of lenders failing to meet acceptable performance later on. Thus, the Agency is retaining the lender approval process.

Finally, one commenter suggested that, in lieu of a regulated or supervised lending entity submitting a lender approval application, the Agency should only ask for the written policies and certificate of good standing with the first application. The Agency agrees with the commenter for those regulated or supervised lending entities that have at least one outstanding Agency guaranteed loan. However, for the reasons stated above, the Agency continues to believe that regulated or supervised lending entities that do not have any outstanding Agency guaranteed loans need to go through an approval process, which the Agency views as an effective tool for managing risk. Therefore, the Agency has not accepted this specific suggestion with regard to regulated or supervised lending entities that do not have any outstanding Agency guaranteed loans.

Comment: One commenter stated that § 5001.9(a)(1) is redundant and can be removed, as it is restated in § 5001.9(a)(1)(i) and (ii).

Response: The Agency agrees that the text provided in this paragraph is redundant, but it is included in accordance with administrative policy. Therefore, the Agency has not modified this paragraph in response to this comment.

Application Content

Comment: One commenter noted the requirement that a lender without an existing portfolio with Rural Development must submit an application for lender approval to the Rural Development State Office and asked what the application would consist of.

Response: Lenders with no outstanding guaranteed loans would submit a lender's application to be approved for participation for the guaranteed loan programs included in this rule. This application requires the lender to provide:

(1) General information on the lender such as name, tax identification number, and contact information;

(2) A written summary of the lender's loan origination and servicing policies and procedures;

(3) Evidence of good standing with its regulator; and

(4) A description of its lending history and experience.

Comment: One commenter questioned how the Agency will know if a lender is in good standing with its regulator.

Response: The Agency will address the procedures it will use to determine if a lender is in good standing in the handbook to the rule.

Comment: One commenter noted a typo in proposed § 5001.9(a)(1)(ii)—the word ''proved'' should be ''approved.''

Response: The Agency has revised this proposed paragraph and making the correction is no longer needed.

Other Lenders

Comment: Two commenters questioned the requirement the other lenders have an ''Agency approved line of credit that totals $5 million or more.'' One commenter stated that the language is not clear, as the Agency does not provide lines of credit to lenders. The other commenter recommended eliminating the requirement, as the requirement seems both vague and unnecessary.

Response: The Agency agrees that it does not provide lines of credit to lenders and that the language in the proposed rule is unclear. The Agency does intend that lines of credit be suitable and necessary in order to demonstrate adequate sources of funds for funding and closing loans and they provide evidence that the lender has the necessary capital, resources, and funding capacity to successfully meet its responsibilities. In order to make this assessment, the Agency needs to review and consider the line(s) of credit available to the lender. For these reasons, the Agency is retaining the requirement for lines of credit, but has revised the language to make clear that the Agency is not providing lines of credit.

Comment: One commenter noted the requirement that other lenders have liquid assets of at least $500,000 and requested that USDA provide a definition of ''liquid assets.''

Response: The term ''liquid assets'' refers to cash and cash equivalents. The Agency will identify in the handbook to the rule what qualifies as liquid assets.

Comment: One commenter stated that it is unfair to require other lenders with an existing USDA guaranteed loan portfolio to reapply for eligible status, and suggested that a simple approach paralleling § 5001.9(a)(1)(i) should be instituted instead.

Response: The Agency believes that the risk management approach being implemented under the new rule is best served by requiring all non-regulated/non-supervised lenders to undergo the same approval requirements regardless of whether or not they have existing Agency guaranteed loan experience. Therefore, the Agency has not adopted the suggestion made by the commenter.

Guarantee Application Process (§ 5001.11)

Comment: Five commenters provided comments on the pre-application. Three commenters noted that there is no definition of pre-application, and two commenters suggested that the pre-application be defined simply as a draft version of the lender's analysis and credit evaluation (i.e., a draft credit memo from the lender). Two commenters noted that there is no description of what material will constitute a pre-application, and recommended using the pre-application material now required by the 7 CFR part 4279, subpart B.

Response: The Agency agrees that a definition of ''pre-application'' is needed and has defined a pre-application as ''Information submitted to the Agency for which the applicant requests the Agency to make an informal assessment prior to submitting a full application. The information must be sufficient for the Agency to make a determination that the borrower and project are eligible.'' The Agency has intentionally not included the specific contents of a pre-application because they may vary between programs and because the Agency prefers to work with the applicant on the basis of what they submit. Further, an applicant may seek an informal assessment for only a part of the project and to provide a prescriptive list of items that must be in a pre-application could discourage this. The Agency will provide guidance in the handbook to the rule to assist applicants as to what items should be included in a pre-application for each program.

Comment: One commenter questioned the utility of submitting a pre-application if the Agency is not going to render a favorable or adverse decision, noting that the purpose of the pre-application is to determine if the Agency will look favorably or unfavorably on a potential loan with a USDA guarantee. The commenter, therefore, recommended that this section be amended to include favorable or adverse decisions.

Response: The pre-application is an optional tool available to the applicant to help provide feedback before spending resources to submit a full application. If an applicant wants a formal determination, the applicant can still submit a full application without having submitted a pre-application. Therefore, the Agency has retained this provision.

Comment: Three commenters expressed concern over the proposed § 5001.11(b)(2) that would allow the Agency to require a lender to obtain additional assistance in those areas where the lender does not have the requisite expertise to originate or service the loan. One of the commenters stated that, if the lender does not have the requisite expertise to originate or service the loan, they should not be an approved lender. The other two commenters stated that the regulator's chartering and monitoring process requires that lenders have origination and servicing experience, and that the Agency is overstepping its expertise and authority with this proposed regulation, thus further reducing the number of lenders waiting to participate. These two commenters also noted that current Business and Industry regulations do not address this issue.

Response: It was not the intent of the phrase ''those areas'' to point to loan origination or servicing, as interpreted by the one commenter. The Agency agrees with this commenter that a lender's expertise in origination or servicing would be evaluated when the lender submits its lender's application (Form RD 5001–1) and if the Agency determined that the lender did not have sufficient expertise, the lender would not be approved.

The intent of this provision was to take into account that some otherwise qualified lenders may seek to originate and service a loan in an area outside of their expertise and, in such instances, the Agency could require the lender to obtain additional assistance. What the Agency had in mind was that an approved lender may seek to originate and service a loan (1) the type and complexity of which (e.g., asset-based financing) or (2) in an industry (e.g., renewable energy) in which the lender did not have experience or very little experience. Because of the lack of specificity of the proposed rule, the Agency has revised the rule to define ''those areas'' in which the Agency may require a lender to seek additional assistance.

The Agency believes that the ability to require such additional assistance in these instances is consistent with the risk management approach of this rule. Therefore, the Agency has retained this provision in the rule.

Comment: One commenter suggested editing § 5001.11(b)(2) to add the following language to the end of the sentence: ''(e.g., environmental compliance).''

Response: As noted in the response to the previous comment, the phrase ''those areas where the lender does not have requisite expertise'' is referring to the type and complexity of the financing and the industries with which the lender has little or no origination and/or servicing experience. There are other provisions in the rule that address the obligation of lenders with regard to environmental compliance. Furthermore, there are other obligations in addition to environmental compliance for which the lender is responsible. The Agency finds it neither necessary nor appropriate to refer to environmental compliance within this paragraph. Therefore, the Agency rejects this comment.

Comment: One commenter suggested that proposed § 5001.11(b)(2), which allows the Agency to require a lender to obtain additional experience, be deleted. The commenter pointed out that the Agency in the proposed rule has provided provisions for lender approval for an Agency Approved Lender and Preferred Lender designation and thus this paragraph has no utility and is burdensome to the lender. To the extent that the Agency has another level of concern not already addressed, the commenter suggested that the Agency should clearly state the concern and address it in the lender approval process.

Response: The Agency cannot anticipate the level of expertise that a lender has for specific projects until the Agency reviews the actual application, and the determination of the lender's level of expertise for specific projects cannot be covered in the lender approval process. As part of its risk management approach, the Agency needs to have the ability to require the lender to obtain additional assistance in those areas where the Agency determines that the lender lacks the requisite expertise. For these reasons, the Agency rejects this comment.

Comment: Four commenters expressed concern over the length of time that the application process takes. One of the commenters, noting that lenders get frustrated with how long it takes to get a Business and Industry application approved, suggested that the Agency include a paragraph that discusses the maximum length of time the application process will take. This commenter also suggested that a preferred lender should be guaranteed a short (3 to 5 days) turnaround time on any application they submit, and that this could be an incentive for lenders to become preferred lenders.

One commenter stated that the proposed regulations do not address the USDA's long turnaround time (minimum of one month, but usually three to six months) and unfriendly lender atmosphere. Another commenter suggested that a decision on the loan application should be made by the Agency within 30 days. Another commenter said that 60 days for processing applications is too long and suggested that it should be reduced to two weeks at the State level and two weeks in Washington.

Response: As noted in a response to a previous comment, the Agency has revised the proposed rule to incorporate a turnaround time for applications from preferred lenders (which under the rule only applies to the Business and Industry program). In the rule, the Agency will approve or disapprove complete applications from preferred lenders within 10 business days from the receipt of complete applications. The Agency believes that 3 to 5 days is too short to commit to even for preferred lender applications because of uncertainty associated with the availability and allocation of Agency resources.

For applications from approved lenders that do not have preferred status, the Agency cannot incorporate a specific turnaround time because such applications will be more complicated (than from preferred lenders) and the amount of time to review such applications is dependent on the availability and allocation of Agency resources. Incorporating a specific timeline for such applications, even if it is as long as 30 days as suggested by one of the commenters, could encourage the Agency to deny applications before the deadline is reached, which could lead to the Agency not approving applications in the areas where they are most needed. For these reasons, the Agency has not incorporated a turnaround time for applications from approved lenders who do not have preferred status.

Comment: One commenter addressed the issue of State Loan Committees and suggested revising the regulation to include the following language: ''Applications processed under this paragraph are exempt from any mandatory State Loan Committee review so long as the State Director has a written policy in place that incorporates a discretionary Committee certification for applications of $600,000 or less.''

Response: The Agency agrees with the comment, but disagrees that it needs to be addressed in the rule. Instead, the Agency will provide guidance in the handbook to the rule, which will note, in part, each program will make a determination as to whether or not have a loan committee. Therefore, the Agency has not revised the rule in response to this comment.

Comment: One commenter stated that it believes there are significant benefits to be realized to both lender and the Agency by review and approval of the loan application prior to the issuance of the Conditional Commitment and, therefore, encouraged the Agency to study this issue further.

Response: The Agency considered this issue and, as provided in the rule, loan applications submitted by approved lenders without preferred lender status will be reviewed by the Agency prior to issuance of the Loan Note Guarantee. For preferred lenders, while the Agency will not re-underwrite the lender's credit evaluation and determination, the Agency will review the loan applications for borrower and project eligibility prior to issuance of the Loan Note Guarantee.

Application for Loan Guarantee Content (§ 5001.12)

Comment: One commenter noted that the process appears very cumbersome and without advantage to anyone other than the USDA. Another commenter said that the proposed preferred lender and approved lender with low documentation and full documentation makes the process more confusing. This commenter suggested that, if a lender wants to participate, it should be approved by the Agency and submit a full set of documentation for each loan requested.

Response: In response to this and other comments, the Agency has revised the guarantee application requirements so that all approved lenders without preferred lender status submit ''full documentation'' guarantee applications. If a lender has preferred lender status, which in the rule is currently available only under the Business and Industry loan guarantee program, the rule requires a different content for the guarantee application. These changes simplify the rule and are consistent with rule provisions for managing risk.

Comment: One commenter recommended that forms common to all four programs should be listed here, and program specific forms should be listed in their particular sections in subpart B.

Response: The Agency recognizes the value of identifying the forms relevant to each of the four guaranteed loan programs, but it is not necessary to do so. Identifying the forms in the rule may require revising the regulation if any of the forms substantially change. Instead, it is the Agency's intent to identify the forms in the handbook to the rule rather than in the regulation. Therefore, the Agency has not incorporated the commenter's suggestion in the rule.

Comment: One commenter suggested that after ''Environmental Information'' in § 5001.12(a)(3) the following words be added: ''as required by 7 CFR part 1940, subpart G or 7 CFR part 1794, as applicable, and any future and succeeding Agency environmental regulation.'' The commenter made this suggestion for both the full documentation and low documentation guarantee loan applications. The commenter also suggested that this paragraph should be relocated to § 5001.11(a) and the information be submitted with the pre-application. The commenter noted that the environmental review needs to happen at the earliest time possible in the application process to avoid difficulties in loan processing.

Response: The rule text referred to by the commenter states ''Environmental information required by the Agency to conduct its environmental reviews (as required in § 5001.16(h)).'' The cross-referenced paragraph states, in § 5001.16(h)(1): ''Provided the necessary environmental information to enable the Agency to undertake its environmental review process in accordance with subpart G of either 7 CFR part 1940 or 7 CFR part 1794, or successor regulations, including the provision of all required Federal, State, and local permits.'' The rule, therefore, already addresses the commenter's suggestion and the Agency has not revised the ''environmental information'' paragraph for the loan guarantee application.

With regard to the commenter's second suggestion concerning the placement of the environmental information in § 5001.11(a) and its submittal with the pre-application, the Agency has not incorporated either suggestion. Under this rule, a pre-application provides the opportunity for a potential applicant to obtain an informal assessment from the Agency on the applicant's and project's eligibility and to comment on the pre-applications strengths and weaknesses. It is in the best interest of both the applicant and the Agency that environmental considerations be considered at the earliest point in the process at which such information becomes available. However, the Agency does not believe that such information should be a prerequisite to the applicant's submitting a pre-application. Therefore, the Agency has not incorporated this suggestion in the rule.

Comment: One commenter suggested consolidating proposed § 5001.12(a)(4) and (7) into one item, and recommended that they be moved to § 5001.104 because they only relate to the section 9006 program.

Response: The paragraphs referred to by the commenter addressed technical reports and energy audits (§ 5001.12(a)(4)) and energy assessments (§ 5001.12(a)(7)). These requirements are not limited to the Rural Energy for America Program guaranteed loan programs. For example, similar types of projects could be funded under the Community Facilities guaranteed loan program. However, the Agency agrees that these three items can be combined into a single item and has done so in the rule.

Comment: One commenter noted that the Form 10–K is now available to the general public online and that there is no need to require it from the lender or business as part of a complete application.

Response: The Agency agrees with the commenter that it is not necessary to require submittal of a company's Form 10–K with the guaranteed loan application and has removed this requirement from the rule.

Comment: Nine commenters commented on the proposed requirement to submit a copy of the loan agreement with the guaranteed loan application. One commenter stated that the draft loan agreement is redundant and unnecessary. This commenter added that most lenders use a standardized system for generating their primary documents, and if the USDA requires more than that, it can be placed in the document as an additional item in the standard Commercial Security Agreement.

One commenter stated that USDA absolutely needs to get out of the practice of micromanaging the lender's loan agreement with its borrower. This commenter stated that if there are specific conditions that the Agency needs met, these should be spelled out in the global Lender's Agreement between the lender and USDA so that the lender knows what USDA's baseline requirements are whenever using USDA guaranteed programs. Beyond this, USDA as a guarantor should rely on its ''approved'' and ''preferred'' lender partners to be able to craft a prudent, comprehensive loan agreement with the borrower.

Three commenters stated that the draft loan agreement should be eliminated. One of these commenters stated that USDA should rely on its lender partners to craft a prudent, comprehensive loan agreement with the borrower. The other commenter recommended that the financial covenants in the final loan agreement should be very limited, allowing more flexibility depending on the individual proposal. This commenter also noted that if the USDA continues to require specific covenants, the USDA agent should have the authority to decide when, which ones, and at what level.

One commenter stated that the draft agreement seems like overkill, since 95% is boilerplate information. The commenter stated that USDA should ask for the other 5%, which basically means loan covenants.

Two commenters said that this section should identify the minimum acceptable conditions for a loan agreement rather than waiting until the Conditional Commitment is issued.

One commenter said that there should be no USDA loan agreement review. Instead, USDA should lay out specific conditions, covenants, or requirements to be included in the loan agreement. Another commenter stated that the loan agreement requirement should be carefully reviewed and should not include absolute requirements that are not always applicable. Another commenter suggested that it would be beneficial for the review and approval of the loan documentation following USDA approval to allow the inclusion of any USDA requirements.

Response: Overall, the Agency agrees with the commenters that it is not necessary to require a copy of the loan agreement between the borrower and the lender when the guarantee loan agreement is submitted. The Agency further agrees that lenders approved to participate in the guaranteed loan programs under this part have the experience and expertise to produce loan agreements to acceptable industry standards and, therefore, the Agency does not believe it is necessary to provide within the rule an itemization of the minimum requirements of a loan agreement acceptable to the Agency. (The Agency may elect to provide such information in the handbook to the rule.) Instead, the Agency agrees that the proper time to review the loan agreement is prior to loan closing.

Comment: Three commenters addressed appraisals. Two commenters suggested that allowance should be provided for USDA approvals to be issued subject to an acceptable appraisal being obtained and reviewed before issuance of the USDA guarantee. Another commenter suggested that appraisals should be a contingency of a Conditional Commitment rather that being required to be submitted with the application.

Response: The Agency continues to believe that appraisals acceptable to the Agency should be submitted with the guaranteed loan application, but recognizes that the guaranteed loan application process can move forward in their absence. Therefore, the Agency has kept this requirement, but conditioned it based on the appraisal being available. If the appraisal is not available at the time the guaranteed loan application is submitted, the lender must submit the complete appraisal to the Agency before loan closing.

Comment: Nine commenters provided comments on the business plan requirement in proposed § 5001.12(a)(9). Six commenters did not recommend requiring a business plan (especially for existing businesses), and four commenters suggested that the lenders should decide if they need to see a business plan for their credit evaluation. One of these commenters also stated that for startups, the business plan and feasibility study should be combined. One commenter said that this requirement will only serve as a deterrent to the loan program.

Two commenters said that for existing businesses, a business history, budget, and projections should be enough.

Two commenters stated that the Agency should say what it expects to be in a business plan, and suggested adding a reference to the definition section for business plan so that the financial statements described in the definition are included.

Response: The Agency has left intact the requirement that a business plan be included with the guaranteed loan application, although a separate business plan does not need to be submitted if the information required in the business plan is included in the feasibility study (as was proposed) or in the lender's analysis (as added in the rule). The Agency continues this provision for existing businesses because existing businesses may be expanding into new areas and/or markets, in which case the business' history, budget, and projection may not be sufficient to evaluate the borrower.

As noted above, the rule does not require a separate business plan if the information is contained in the lender's analysis. This addresses commenters' suggestion that the lender be responsible for deciding if a business plan is needed.

Finally, there is no need to add a cross-reference back to the definition of ''business plan.'' When a term is used in the rule and that term is defined in the definitions section of the rule, then that term has that meaning regardless of whether or not there is a cross-reference back to the definitions section. The Agency does not intend to insert such cross-references for the defined terms in this rule.

Comment: One commenter stated that a feasibility study should not be a standard requirement, but should be required only on an as-needed basis, to be determined by the lender based on the nature of the project. This commenter also noted that feasibility studies are not typical in the small business lending industry underwriting process.

Another commenter stated that the requirement for a feasibility study or analysis should remain a requirement. The specific type, scope of work, and preparer should remain the lender's responsibility to propose and obtain with Agency concurrence.

Response: The Agency has elected to retain in subpart A the identification of a feasibility study as part of the guarantee loan application and use subpart B to identify whether a specific program requires it (as under § 5001.104) or may require it (as under §§ 5001.101, 5001.102, and 5001.103). Thus, the rule does not make it a ''standard'' requirement and it will be required only to the extent identified in subpart B for a specific program.

Comment: Five commenters provided comments on the Affirmative Fair Housing Marketing (AFHM) plan in proposed § 5001.12(a)(11). One commenter noted that this requirement is currently used by the U.S. Department of Housing and Urban Development and that it is a timely/difficult report.

One commenter noted that the proposed rule requires the AFHM plan for for-profit nursing homes or assisted living center, and questioned whether it is required for non-profit facilities of this type. The commenter also noted that presently the AFHM plan is required for these type of facilities regardless of the profit type. Another commenter recommends deleting the requirement for for-profit facilities.

One commenter stated that this requirement is duplicative and unnecessary, and noted that because in all Business and Industry loans and in the Conditional Commitment, the borrower must certify compliance with Equal Employment Opportunity and Civil Rights law, the requirement is already in place. Another commenter also stated that because this requirement is already handled through compliance with Civil Rights laws, etc., the proposed requirement should not be part of the guaranteed loan program, and that it would be an extra burden on the lenders and duplicate what they already have to do as lenders.

A sixth commenter suggested that the Agency insert the phrase ''to the extent that state or Federal statute requires this certification''.

Response: This rule implements requirements already established by Rural Development under 7 CFR § 1901.203(c)(2)(i), which applies to all Rural Development programs involving housing, which includes both profit and not-for-profit housing. If the requirements associated with 7 CFR part 1901, subpart E are to be changed, it would occur under another rulemaking, not this one. Therefore, the Agency has retained the requirement for the AFHM plan in the rule.

The Agency, however, has revised proposed § 5001.12(a)(8) because, as noted in the above paragraph, the requirement for the AFHM plan applies to both profit and not-for-profit housing. The revision deletes the reference to ''for profit'', and makes reference to nursing homes and assisted-living centers as being included under residential units (''residential units, including nursing homes and assisted-living centers'').

The Agency notes that the requirement for preparing the AFHM plan is borne by the borrower and not the lender. Thus, it is not a burden on the lender. In addition, the AFHM plan is a marketing tool whose purpose is to promote the project in order to have people move into the housing and makes underserved and minority populations aware of the project. The AFHM plan is required by legislation separate from applicable Equal Employment Opportunity and Civil Rights regulations.

Finally, because the requirement for the AFHM plan is based on 7 CFR part 1901, subpart E, the Agency rejects the suggestion to add the phrase ''to the extent that state or Federal statute requires this certification.''

Comment: Three commenters commented on the proposed requirement to submit a preliminary engineering report with the guaranteed loan application. One commenter stated that this requirement should be moved to § 5001.101 because it is only related to the water and waste disposal guaranteed program. Another commenter recommended deleting the requirement for a preliminary engineering report for all new construction. The third commenter stated that the engineering report should only be required for projects where the technology and engineering is not an industry standard or has sufficient historical applications.

Response: In consideration of these comments, the Agency has elected to delete reference to preliminary engineering report (PER) from subpart A and the rule only references it in subpart B with respect to the water and waste disposal guaranteed program. As additional guaranteed loan programs are added to this part, the Agency will place any PER requirement in subpart B as appropriate.

With regard to the suggestion that this requirement be deleted for all new construction, the Agency first notes that the rule is consistent with the current implementation of the water and waste disposal guaranteed loan program. It is not the Agency's intent to deviate from the current implementation of the program because, as a matter of Agency policy and experience, the PER is invaluable in ensuring that the engineering principles are sound and that viable alternatives have been considered.

Finally, with regard to the suggestion that the PER only be required for projects where the technology and engineering is not an industry standard or has sufficient historical applications, the Agency disagrees that the PER should not still be prepared and submitted. Even in these situations, the PER allows the Agency to evaluate possible alternatives and helps determine eligible project costs. The complexity of the PER depends on the complexity of the project. Thus, those projects that meet industry standards or have historical applications could be less complex and require less time to prepare. But in all instances, the PER still provides value to the Agency in evaluating the guaranteed loan application.

Comment: One commenter suggested adding the following language to proposed § 5001.12(a)(13): ''Current credit reports or equivalent on the applicant and any parent, affiliate, and subsidiary firms, and other persons or entities liable for the debt, except for public bodies; and.''

Response: The proposed rule stated, in part, that current credit reports or equivalent would be submitted for ''any other person liable for the debt.'' The phrase ''any other person'' includes, but is not limited, to those entities identified by the commenter (i.e., parent, affiliate, and subsidiary firms). Therefore, it is unnecessary to revise the provision as suggested by the commenter. To the extent that the Agency determines it useful, the Agency will clarify ''any other person'' in the handbook to the rule.

Comment: Eleven commenters recommended deleting proposed § 5001.12(a)(14), Audited financial statements. One commenter noted that requiring an audit for more than $1 million would be punitive. Five commenters noted that audited financials are expensive. One commenter said that it was not necessary and was a bad idea, and another commenter said it was inappropriate. Two commenters said that $1 million is a ''ridiculously low level'' at which to require audited statements. Six commenters stated that it should be up to the lender. One commenter stated that the change from an independent accountant prepared statement to an audited financial statement would severely limit the number of companies who would be eligible for the program, and two commenters said that the proposed requirement would be detrimental to the program. One commenter said inclusion of this requirement would be a significant hindrance to the Agency's ability to support many of its current borrowers.

Response: The Agency has considered these comments and has made revisions to this requirement to differentiate between startup businesses and existing businesses. For borrowers that have been in existence less than one year, the Agency revised this requirement by eliminating the threshold and requiring the submittal of the most recent ''Agency-authorized financial statements'' of the borrower regardless of the amount of the guaranteed loan request. For borrowers that have been in existence for one or more years, the Agency raised the threshold from $1 million to $3 million at which audited financial statements would be required and has added a provision that would allow the submittal of alternative financial statements provided such statements have been authorized by the Agency. For borrowers that have been in existence for one or more years that request guaranteed loans of less than $3 million, the most recent audited or Agency-acceptable financial statements of the borrower would be submitted. The Agency believes that these revisions address most of the concerns expressed by the commenters while maintaining the Agency's intent in this rule to manage risk.

Comment: Nine commenters suggested different threshold levels for when audited financial statements would be required. One commenter suggested that the minimum should apply to loans over $3.0 million. Five commenters suggested audited statements for loans over $5 million.

Two commenters suggested audited statements for loans over $10 million.

One commenter stated that audited statements make sense only for loans of over $5 million because reviewed statements are good for $3,000,000 to $4,999,999, and statements prepared by certified public accountants are good for $1.00 to $2,999,999. Another commenter suggested review statements for loans under $5 million.

One commenter stated that current regulations have a floor of $3 million for certified financial statements which has been cost prohibitive for small business owners. The commenter expressed concern that lowering the floor, as in the proposed rule, will make this very problematic and should be eliminated. The commenter recommended that the Agency consider CPA reviewed financial statements for all loans under $5 million and that all financial statements must be prepared in accordance with GAAP.

Response: The Agency considered the suggestions made by the commenters as to an alternative, higher threshold at which audited financial statements would be required. Among other changes concerning the submittal of financial statements, the Agency has raised the threshold from $1 million to $3 million. The Agency is concerned that raising this threshold to a higher limit ($5 million or $10 million) may unnecessarily result in increased risk.

Comment: Eleven commenters suggested alternatives to requiring audited financial statements. Two commenters recommended retaining the current regulation whereby the USDA may require annual audited financial statements after the Business and Industry guaranteed loan closes. These commenters also stated that the intention of the proposed regulation is unclear, and that if the intention is to require applicants for loans over $1 million to have audited financial statement for prior years, this will severely impact many otherwise good credit worthy potential rural businesses that need Business and Industry guaranteed loans.

One commenter recommended returning to the requirements in the old 7 CFR part 4279, subpart B regulation which called for a current balance sheet; and projected balance sheets, income and expense statements, and cash flow statements for the next two years. Existing businesses must also submit balance sheets and income statements for the three previous years. This commenter also noted that the lender's policies may require the applicant to provide more, but suggested that the Agency not impose additional requirements, including GAAP prepared financials.

Four commenters suggested requiring tax returns. These commenters stated that they are now the most widely used financial tool in business banking and that they are the only financial statement that is uniformly and consistently available from all businesses. One of the commenters added that they are the common statement used in underwriting owner-occupied real estate loans.

Two commenters pointed out that 99 percent of for-profit businesses that will apply do not have audited financial statements, and will not go through the expense of an audit to apply for a Business and Industry guarantee. These commenters suggested that the requirement for for-profit businesses should be for ''accountant prepared financial statements'' and added that the statements should be ''completed in accordance with Generally Accepted Accounting Principles.'' Another commenter also supported requiring accountant prepared financial statements for for-profit businesses.

Response: As noted in previous responses to comments on financial statements, the Agency has revised this provision to allow for the submittal of Agency-authorized financial statements for all businesses that have been in existence for less than one year regardless of the amount of the guaranteed loan request. For businesses that have been in existence for one or more years seeking a guaranteed loan size that is less than $3 million, the Agency revised the rule to allow such borrowers to submit either the most recent audited or Agency-acceptable financial statements of the borrower. In such situations, the types of financial statements identified by the commenters may be acceptable to the Agency, which will work with the lenders on a case-by-case basis. However, for guaranteed loans of $3 million or more from businesses that have been in existence for one or more years, the Agency believes that requiring audited financial statements (unless alternative financial statements are authorized by the Agency) is reasonable relative to the potential risk associated with such guaranteed loans.

Comment: One commenter stated that the Agency's annual audits requirements were inconsistent and atypical of lender's requirements. The commenter questioned why, if only annual audits are needed for risk projects over $3 million, up front audits are needed for a sound borrower and a $1 million project.

Response: The Agency has revised, among other changes, the level at which audited financial statements are required to be submitted with the guaranteed loan application to $3 million. As noted in responses to other related comments, the Agency has removed the requirement for annual audited statements for projects over $3 million and has replaced it with a requirement for the submittal of financial reports, either as required by the lender's regulatory authority if the lender is regulated or supervised or as contained in the Conditional Commitment if the lender is an other lender (*see* § 5001.17(d), Financial reports).

Comment: One commenter noted that no allowance is made for startup businesses where there would be no audit available.

Response: The Agency agrees with the commenter and has revised the rule to allow borrowers in existence less than one year, which includes startup businesses, to submit ''Agency-authorized'' financial statements.

Comment: One commenter suggested that the full documentation guarantee application should also include the following items: Complete organizational documents of the borrower, list of governing board members of the borrower, community support documentation, historical financial statements of the borrower, State Clearinghouse/Intergovernmental Review comment letter, copies of any existing or proposed lease, management agreement, or other applicable legal documents involving the borrower and the proposed facility, and the lender's letter on the need for the guarantee.

Response: The Agency has considered each suggested item for inclusion in a full documentation application, which corresponds to an approved lender application in the rule (see § 5001.12(a)), and has made the following determinations.

With regard to the submittal of complete organizational documents of the borrower, the Agency as a matter of policy has determined that these documents are needed in verifying if a borrower is a non-profit and has the authority to engage in obtaining the loan. Of the four programs included in the rule, such documents are relevant to the Community Facility and Water and Waste Disposal programs, but not to the other two programs. While Form RD 5001–3 requires lender certification to the borrower's authority to obtain a loan, the Agency has determined that it is necessary to ensure these organizational documents are obtained for the Community Facilities and the

Water and Waste Disposal programs. Therefore, the Agency has added this as a requirement in subpart B for both programs.

With regard to the list of governing board members of the borrower, such information is needed to determine whether a facility is locally controlled. This is important to the Community Facility and the Water and Waste Disposal programs, but not to the other two programs under the rule. Therefore, the Agency has added this as a requirement in subpart B for both programs.

With regard to community support documentation, Form RD 5001–3 requires the lender to certify that the borrower has obtained a certificate of support. Lender certification is sufficient to meet the needs of the Community Facilities and Water and Waste Disposal programs and, thus, there is no need to require submittal of such documentation with the loan guarantee application.

With regard to historical financial statements of the borrower, if the Agency determines that the financial statements in § 5001.12(a)(10) are insufficient to properly assess the viability of an individual project, the Agency may at its discretion request additional financial information (see § 5001.12(a)(10)(iii)).

With regard to State Clearinghouse/Intergovernmental Review comment letter, the requirement to submit such a letter is covered under USDA's Office of the Chief Financial Officer regulations in 7 CFR part 3015, subpart V. This requirement is applicable to this rule under § 5001.16(g), which requires compliance with ''applicable Federal laws.'' Therefore, the Agency has not included this item as a separate line item for applications. However, the Agency recognizes that this letter is not very well known and will address this issue in the handbook to the rule.

With regard to copies of any existing or proposed leases, the rule allows the Agency to request any additional information it determines is necessary to evaluate the application (§ 5001.12(a)(11)). Thus, while Form RD 5001–3 contains a provision to address the relationship between the length of the loan and the length of the lease (e.g., to ensure that the lease is longer than the loan term), if the Agency determines that additional information is needed to properly assess the lease, the Agency may request that the lender provide a copy of the lease under this provision of the rule. The Agency will provide guidance in the handbook to the rule as to the circumstances under which it might request a copy of the lease.

With regard to a management agreement and other applicable legal documents involving the borrower and the proposed facility, the Agency agrees that submittal of such agreements, where applicable, is useful to ensure that a for-profit company does not receive the benefit of Federal government subsidized funds. This suggestion is applicable to the Community Facilities and the Water and Waste Disposal programs and has been provided for in subpart B for both programs.

Finally, with regard to the lender's letter on the need for the guarantee, Form RD 5001–3 addresses through the lender's certification the need for the guarantee. Therefore, there is no need to add this as a separate item to the application.

Comment: One commenter recommended that non-preferred lenders submit a complete application package for all loans and a full loan package should be required for all loans above $5 million.

Response: The Agency has revised the rule, as discussed in responses to other related comments, such that all non-preferred lenders must submit full documentation applications regardless of the size of the loan. For preferred lenders, which would only be allowed under the rule for the Business and Industry guaranteed loan program, the Agency is requiring a different set of application requirements to be submitted regardless of loan size.

Comment: One commenter noted that many of the application requirements refer the reader to subpart B. This commenter suggested that each section in subpart B should have its own application section so that they can be program specific without having the reader flipping around the regulation.

Response: The Agency intentionally developed the new platform to improve the administrative efficiency of adding new programs to the rule, recognizing that this format would require readers to consider requirements for a single program in both subpart A and subpart B of the rule. The Agency will provide implementation materials and application guides in which the requirements of the rule will be presented in a manner as suggested by the commenter.

Low Doc Applications (Proposed § 5001.12(b))

Comment: The Agency received a number of comments pertaining to low documentation applications, including the lack of significant differences and relief between low documentation and full documentation applications, the potential for abuse, and the importance of full and careful review of all applications.

Response: The Agency has removed low documentation applications from the rule. The requirements contained in the rule are those necessary to ensure applications are adequately evaluated and these comments are no longer relevant.

Determination of Documentation Level (Proposed § 5001.12(c))

Comment: The Agency received a number of comments on the determination of documentation level for existing businesses in the context of low documentation applications, including loan amount threshold, credit criteria for preferred and non-preferred lenders, debt coverage ratios, equity requirements, and loan to value ratio.

Response: As noted above, the Agency has removed low documentation applications from the rule. The requirements contained in the rule are those necessary to ensure applications are adequately evaluated and these comments are no longer relevant.

Lender Responsibilities—General (§ 5001.15)

Comment: After noting the manner in which the proposed rule attempts to manage risk to the Agency, one commenter suggested placing the burden of risk management on those with the expertise to do so (i.e., on the lenders) because, while financial and other criteria as part of project eligibility will assist in identifying risk, experienced lenders have a good understanding on how to mitigate an identified risk.

Response: As discussed in the preamble to the proposed rule, the new platform for guaranteed loans addresses four types of risk—loss exposure, project risk, institutional risk, and operational risk. One of the key components in managing risk is to ensure that applications for projects that will repay their loans are submitted by the lender. While the Agency ultimately approves or disapproves the guarantee, the rule relies on the lender's experience and expertise to originate such loans. Further, under the rule, preferred lenders are afforded more responsibility in loan origination as Agency review of loans from preferred lenders is limited. The rule also relies heavily on the lender's servicing policies and procedures for monitoring loans and for taking corrective actions when necessary for loans that start experiencing problems. In sum, the rule employs provisions that manage risk using both Agency and lender expertise and experience. The Agency believes it has struck an appropriate balance between responsibilities to ensure minimizing losses in the Agency's guaranteed loan portfolio.

Comment: One commenter stated that, to the extent that the Agency's action or inaction created a loss, the lender should be compensated accordingly to the extent that the lender continued its responsibilities to originate and service the loan.

Response: The Agency understands the commenter's concern that there are actions or inactions that the Agency may take that could result in a loss to the lender. For example, collateral value could degrade while the Agency is making a determination. However, there are statutory constraints, as contained under the Consolidated Farm and Rural Development Act, that prohibit the Agency from implementing a provision as suggested by the commenter. While the lender has the right to pursue an appeal of a loss claim if it disagrees with the loss claim payment, the Agency cannot establish a separate category of loss claims associated solely with alleged agency action or inaction. Therefore, the Agency has not revised the rule as suggested by the commenter.

Comment: One commenter recommended adding the following language: ''Guaranteed loans must be properly classified. Within 90 days after the Agency issues the Loan Note Guarantee, the Lender must notify the Agency of the loan's classification or rating under its regulatory standards. The Lender must also notify the Agency when there is a change in the original loan classification.'' The commenter then asked ''If this is not published, how will the lender be required to notify the Agency of the loan classifications?''

Response: In response to this and other related comments, the Agency has revised the rule to require the lender to notify the Agency of a loan's classification no later than 90 days after loan closing (see § 5001.16(a)(2)), and to notify the Agency within 15 calendar days of when a loan's classification has been downgraded (see § 5001.4(b)(3)(iii)). As noted in a response to another comment, the Agency does not believe that it is necessary to report all changes in a loan's classification, just those that result in a downgrade. Finally, the loan classifications that would be used to classify guaranteed loans will be identified in the handbook to the rule. The Agency does not believe there is any utility in incorporating those classifications in the rule.

Lender Responsibilities—Origination (§ 5001.16)

Comment: One commenter stated that it is better for the Agency to have its own underwriting standard and administer that exclusively.

A second commenter also suggested that the Agency set its own reasonable standards and accept projects that meet the Agency's standards even though it might be outside the lender's normal credit criteria. This is a valid reason for a lender to seek a government guarantee.

A third commenter stated that the Agency is establishing more stringent eligibility requirements under the program that are unfair and will not achieve the Agency's desired goal. According to this commenter, the proposed rule will not reduce the Agency's so called ''institutional risk,'' but will instead create unpublished standards of metrics for Agency program eligibility, credit evaluation, servicing, and liquidation that discriminates against those lenders with tighter credit standards. Therefore, this commenter recommended that the Agency:

(1) Establish clear credit evaluation and loan servicing standards that it expects from lenders,

(2) Hold the lenders accountable to those standards as a reasonable and prudent lender, and

(3) Mandate that all lenders adopt the Agency's regulations as part of their written policies and procedures after the proposed rule and credit evaluation standards are established in order to ensure compliance.

A fourth commenter stated that the Agency should have its own credit policies that it follows regardless of the lender's credit policies. The commenter pointed out that typically a guarantee is needed because there are exceptions to the lender's credit policy and a guarantee mitigates the risk allowing for the credit to be approved and then stated that if the Agency reverted to the lender's credit policy, it would not be able to approve the guarantee because there would be exceptions to the credit policy.

Response: The Agency has intentionally not tried to create a comprehensive set of requirements to cover all aspects of loan origination and servicing under this program, because, in part, the Agency does not believe that a comprehensive set of standards can be established to fit all guaranteed loans (one size does not fit all). Instead, the Agency is setting specific minimum standards in certain areas it has determined important to managing risk for the loans it will guarantee under this program. Further, for the reasons stated in the preamble to the proposed rule, the Agency intends to leverage lender experience in originating and servicing loans and to do so using those policies and procedures with which they are most familiar (i.e., their own) and that are satisfactory to their regulators. This provides a flexibility for the individual loan programs as well as for the lenders seeking to participate in the program and allows the lender to develop case-by-case analyses for individual projects.

Comment: One commenter suggested that, as an alternative, the Agency should mandate that all Rural Development approved lenders, preferred lenders, and approved non-regulated or supervised lenders include Agency loan origination, servicing, and liquidation servicing regulations into their origination policies and procedures in use by the lender to level the playing field. This should be included in the Lender Agreement, Conditional Commitment, and Lender Certification given at loan closing. According to the commenter, this will eliminate the burden of monitoring lender credit policies and procedures, and create more time for Agency personnel to devote to approving more loan guarantees.

Response: First, the Agency believes that setting the standards it has in this rule sufficiently levels the playing field to help ensure that risk is being mitigated across all loans that are originated and serviced under this program. The Agency does not believe that it is necessary that each loan and its accompanying documents require the same exact set of conditions, policies, and procedures in order to ensure its likelihood of repayment.

Second, the Agency expects lenders to monitor all loans guaranteed under this program in accordance with their policies and procedures as they would any other loan they make. The lender is required to notify the Agency of changes in a loan's status (any downgrades). Further, the rule requires lenders to notify the Agency of any changes to those policies and procedures and, where the change is inconsistent with the requirements of this rule, the lender must notify the Agency in writing and receive written Agency approval prior to applying the changes to loan guarantees under this part. This places the primary responsibility on the lender and allows the Agency to more efficiently allocate its resources.

Comment: One commenter noted that the SBA currently requires in the bank note that it would not do the deal without the government enhancement. The commenter recommended that the

USDA program should match this SBA requirement.

Response: The Agency agrees that the issue raised by the commenter needs to be addressed in this program. In Form RD 5001–3, item 2 under the Community Facility sheet and item 2 under the Water and Waste Disposal sheet require the lender to indicate whether or not the lender is willing to provide financing for the project at reasonable rates and terms without the reduced risk derived from the USDA loan guarantee. The Agency believes this sufficiently addresses the commenter's suggestion.

Comment: One commenter made two suggestions of language that should be added:

—''The lender is primarily responsible for determining credit quality. Lenders are responsible for developing and maintaining adequately documented loan files, recommending only loan proposals that are eligible and financially feasible, following Agency regulations, and performing a thorough credit evaluation addressing all credit factors. The lender is required to have an adequate underwriting process to ensure that loans are reviewed by a qualified loan officer other than the originating officer. The Agency relies upon the lender to perform these and other credit evaluation responsibilities outlined in the regulations.''

—''Lenders are responsible for obtaining valid evidence of debt and collateral in accordance with sound lending practices.''

Response: The Agency has considered the commenter's suggestions and the rule addresses each substantive suggestion. As part of the lender approval process, the rule requires all lenders to maintain internal audit and management control systems to evaluate and monitor the overall quality of its loan origination and servicing activities (§ 5001.9(a)(2)). This is also required in § 5001.15(f). Lenders are also required to compile and maintain in their files a complete application for each guaranteed loan (§ 5001.15(e)). In addition, the rule requires each lender to originate loans in accordance with its loan origination policies and procedures, to follow the requirements of this part with regard to origination and servicing, and to service loans in accordance with its servicing policies and procedures. Further, the rule clearly states, in § 5001.16(b), that lenders are required to conduct credit evaluations for all applications for guarantee. Lastly, the rule requires lenders to provide real property and chattel collateral appraisals conducted by an independent qualified appraiser. To the extent that additional guidance on these requirements is required, the Agency will provide such guidance in the handbook to the rule.

Comment: One commenter suggested adding a new paragraph (j) on surety bonds, as follows: ''(j) Surety bonds. The lender must ensure that surety bonds will be provided by construction contractors if Agency grant funds are provided to the borrower prior to completion of construction.''

Response: The Agency agrees with the commenter that the rule needs to address surety bonds. The Agency has revised the rule in two ways. First, in subpart A, the Agency has added a provision for surety bonds. Second, the Agency has added in subpart B a requirement for payment and performance bonds sufficient to mitigate Agency risk if the project is never completed for both the Business and Industry guaranteed loan program and the Rural Energy for America Program guaranteed loan program.

General (§ 5001.16(a))

Numerous commenters (as detailed below) expressed varying degrees of concern over the proposed requirement that the lender meet the more stringent requirements of either its policies and procedures or those of the Agency. Many commenters stated that this requirement should be removed from the rule, with some commenters stating that the Agency needs to set its own reasonable standards. Because their concerns were addressed at both loan origination and loan servicing, all of these comments are addressed in this section. Though similar, comments are addressed by individual commenter.

Comment: One commenter stated that the Agency's requirement to apply the lender's more restrictive portion of its credit policy and procedures to either credit evaluation or servicing rather than conform to the Agency's regulation is too restrictive and penalizes those lenders with more restrictive credit policies. The commenter further characterized this requirement as onerous and unjust, placing higher standards on some lenders and less on others, and punitive to lenders with more stringent credit guidelines, who would be held to higher standards than those of the Agency, while other lenders with prudent credit policies and procedures have lesser standards to meet.

Two other commenters stated that, for both origination and servicing, they disagree with the ''whichever is more stringent'' requirement, in part, because it would have the lenders operating at different levels.

Response: First, as noted in responses to other related comments, the Agency has revised the rule to allow exceptions to the ''whichever is more stringent'' requirement by adding the phrase ''unless otherwise approved by the Agency.'' This reduces the ''restrictiveness'' of this requirement as objected to by the commenter.

Second, the Agency disagrees that lenders with more stringent standards are being placed in a ''punitive'' position compared to those lenders with less stringent standards. The rule does not change how lenders currently apply their criteria to projects and borrowers under their lending practices. What the rule is doing is allowing lenders to apply their own policies and procedures, the ones with which they are familiar, to loans being guaranteed under this program. For any lender, where the rule has a policy or procedure that is more stringent than a lender's corresponding policy or procedure, the lender must comply with the more stringent policy or procedure in the rule.

Comment: One commenter stated that requiring lenders with stricter term limits and larger collateral discount requirements to use those criteria rather than the standard Agency criteria will lead to such lenders offering shorter loan terms, which will create the concept of balloon, puts, and calls currently not allowed under the current regulations. According to the commenter, this will lead to shorter loan terms with balloons, resulting in fewer project and small business qualification and participation under the Agency program, because lenders will be required to use shorter terms with balloons if their policies and procedures are stricter than the Agency's terms limits. The commenter then stated that this result is inconsistent with the intent of the current and proposed rules.

Response: The Agency disagrees with the commenter because the rule requires loans subject to Agency guarantee to be fully amortized.

Comment: One commenter noted that the ''whichever is more stringent'' requirement removes one of the incentives for using the program, as many lenders use the Business and Industry program as a credit enhancer. The commenter illustrated this by stating that lenders' internal policies may limit the term of the loan to less than is allowed by Business and Industry program regulations. According to the commenter, this does not mean that the loans are more risky, but it allows payments to be spread out over a longer period providing the borrower with a smaller debt service requirement and a better opportunity for success.

A second commenter similarly noted that making the bank's more restrictive credit policy take precedence over the Agency's defeats the purpose of the Business and Industry Guarantee Program in that the Business and Industry program should make credit available when a lender would not ordinarily make the loan.

Response: The Agency agrees with the commenter that the situation posed would need to be considered. In response to this and other related comments, the Agency revised the rule to require that the lender comply with its own policies and procedures or those in the rule, whichever is more stringent, unless otherwise approved by the Agency. The addition of this ''unless otherwise approved by the Agency'' allows the Agency and the lender to work together to address such situations as posed by this commenter and to consider each loan application on a case-by-case basis. Any agreement reached between the Agency and the lender must be reflected in the Conditional Commitment.

Comment: One commenter stated that the ''whichever is more stringent'' requirement is inappropriate and unwieldy. This commenter recommended that the Agency establish its standards and lenders should be able to present any project that meets the Agency's standards even though it may be outside the lender's normal credit criteria. The commenter stated that this is a valid reason for a lender to seek a government guarantee. To illustrate its concern, the commenter gave the following example: If a lender's standard criteria for a loan to a non-profit group is 30% cash equity but they have a long-standing customer with significant assets, good debt service coverage, but only 23% cash equity, the lender may use a guarantee to mitigate the exception. The project still meets Agency standards, but could not be done as the language is currently written.

The commenter also stated that this requirement should be eliminated because, in part, it eliminates the opportunity for lenders to use a guarantee to mitigate a policy exception.

Response: The Agency agrees with the commenter that the proposed rule could have prohibited the lender from submitting an application for a loan guarantee and that this would not necessarily have been desirable. As noted in the response to the previous comment, the Agency has revised the rule to provide for ''unless otherwise approved by the Agency.'' The addition of this conditional phrase allows the Agency and lender to address such situations as posed by the commenter.

Comment: One commenter stated that the ''whichever is more stringent'' requirement is redundant because where the lender has more stringent policies than the Agency's, the lender will have to follow those to get the loans through its own credit administration policies.

Response: While this requirement might be considered redundant for those lenders that have policies and procedures more stringent than those contained in the rule, it is not redundant for those lenders that have policies and procedures less stringent than those contained in the rule.

Comment: One commenter stated that if the Agency's rules are more stringent, it is up to the Agency personnel to ensure that the lender follows Agency rule. The commenter stated that they believe this does not have to be a written rule, it is obvious. Another commenter stated that this requirement should be eliminated because, in part, it unrealistically expects Agency staff to be able to verify that a project/borrower met all of the lender's criteria.

Response: The Agency disagrees with the commenter's assertion that it is up to Agency personnel to ensure that a lender follows Agency rules. It is the lender's responsibility to know and follow the requirements in the rule. While the Agency may not have sufficient information to determine the lender's standards on a case-by-case basis, the Agency can still verify that the requirements are being met through other rule provisions for routine servicing and lender oversight.

Comment: One commenter asked what would happen if the more stringent Agency's policies resulted in a default, and suggested that this requirement increases the potential for the Agency to micromanage the loan itself.

Response: The Agency's standards establish minimum criteria for loans that the Agency is willing to guarantee. If the lender's standards are less stringent than these, then the Agency would not guarantee that loan. The Agency's standards do not cause the borrower to go into default.

The Agency disagrees with the commenter's characterization that the rule increases the potential for the Agency to micromanage the loan itself. The entire rule is built around providing lenders with more independence in originating and servicing loans than under the current regulations for the programs included in this rule. In addition, the lender knows beforehand what policies and procedures will be required when the lender agrees to participate in this program.

Comment: One commenter asserted that the proposed ''whichever is more stringent'' requirement could lead to a scenario where an Agency reviewer starts second-guessing lenders on what their in-house underwriting standards say.

Response: The Agency disagrees with the commenter's assertion. While the Agency may not have sufficient information to determine the lender's standards on a case-by-case basis, the Agency can still verify that the requirements are being met through other rule provisions for routine servicing and lender oversight.

Comment: One commenter stated that the ''whichever is more stringent'' requirement should be eliminated because, in part, by using this policy, the Agency is inviting more participation from lenders with the lowest credit standards as they will be able to find more rural businesses that meet their credit standards.

Response: The fact that a lender has less stringent policies and procedures than another lender is, by itself, an insufficient reason not to allow the former to participate in this program. If the former lender's policies and procedures are determined by the Agency to be sufficient for participation, then the Agency believes such lenders should be allowed to participate. Therefore, the Agency has not eliminated this requirement as requested by the commenter.

Comment: Two commenters stated that, for both origination and servicing, they disagree with the ''whichever is more stringent'' requirement, in part, because it would interfere with the authority of the lender's regulators. These commenters recommended keeping the current regulation.

Response: The rule sets up a relationship between the lender and the Agency in guaranteeing loans for programs included in this rule. The relationship between the lender and its regulator is outside the purview of this rule.

Comment: Two commenters stated that, with regard to servicing, if the ''whichever is more stringent'' requirement is adopted, it would cause confusion and generate many legal suits and would not be acceptable to lenders. These commenters recommended keeping the current regulation.

Response: The Agency does not believe that this requirement would create the ''confusion'' claimed by the commenter. Each lender would be responsible for complying with its own policies and procedures or those in the rule, and would not be responsible for or concerned with the policies and procedures of other lenders. Thus, the Agency does not agree that there would be confusion for what an individual lender is required to do to comply with this rule.

In addition, the rule allows the Agency and the lender to reach agreement under the ''unless otherwise approved by the Agency'' provision, which the Agency believes resolves most, if not all, of a lender's concern with this requirement.

Comment: One commenter stated that, in reading the requirement that the lender must comply with whichever is more stringent, they interpreted the requirement to say that, if the lender would not approve a deal at 80% loan-to-value conventionally, then it could not use the USDA program to add value to the property and relax its credit policy.

Response: The Agency has revised the rule to require the lender to comply with whichever is more stringent, unless otherwise approved by the Agency. The proposed rule did not contain the ''unless otherwise approved by the Agency'' clause. Thus, the rule would allow the Agency and the lender to reach agreement on how to handle the situation posed by the commenter and such agreements would be reflected in the Conditional Commitment.

Comment: One commenter had questions regarding § 5001.16(a)(1) in which the Agency may require an independent credit risk analysis on the loan. The commenter questioned what this analysis is, who would do it, who would pay for it, and what it is for.

Response: On a case-by-case basis, the Agency may require the lender to provide a rating or opinion of the underlying credit by an independent credit rating organization at other than Agency expense.

Credit Evaluation (§ 5001.16(b))

Comment: One commenter stated that the lender should be required to compare the financial projections to the industry averages for reasonableness.

Response: The Agency agrees that this can be a reasonable comparison as part of credit evaluation. Such a comparison, though, would be applicable to Business and Industry and the Rural Energy for America programs and would not be applicable to the Community Facilities and Water and Waste Disposal programs. The rule (§ 5001.16(b)(2)(v)), Conditions) provides the Agency with the ability to require this when it is appropriate or is needed to address reasonableness. Therefore, the Agency has not revised the rule in response to this comment.

Comment: Two commenters noted that although the proposed rule requires the lender to prepare a credit evaluation that is consistent with Agency standards ''found in this part,'' there are no standards found in this part, only a general description of the 5 C's of credit. They also noted that the proper standards to use are detailed in RD AN No. 4308 (4279–B, 4280–B, and 4287–B), and suggested using the Administrative Notice's definition in the **Federal Register** (rather than in the Administrative Notice).

A third commenter noted that the Agency has issued a variety of Administrative Notices and Unnumbered Letters relating to, but not limited to: credit due diligence, lender credit due diligence, project risk, and collateral evaluation and appraisal requirements, as guidelines for State Offices. We find that those standards are missing from the proposed rule. The commenter encouraged the Agency to incorporate its administrative notices, including but not limited to, RD AN No. 4280 and RD AN No. 4308, in this section in order to establish published regulations for credit evaluations.

Response: The standards being referred to by the commenters are the ''5 C's of credit'' (§ 5001.16(b)(2)(i) through (v)) as well as the eligibility standards set forth in § 5001.6(b). With regard to the Administrative Notices referred to by the commenters, the Agency will incorporate the appropriate notices in the handbook for the rule.

Comment: One commenter stated that the correct 5 Cs of credit are character, capacity, capital, collateral, and conditions, not credit worthiness, cash flow, capital, collateral, and conditions.

Response: For the purposes of this rule, the Agency is characterizing the 5 C's of credit as proposed and has not modified the rule as suggested by the commenter.

Comment: One commenter suggested that the following be incorporated in § 5001.16(b)(2)(i): ''Credit history should indicate no derogatory past or present credit or payment performance, no bankruptcy, foreclosures, judgments, collections, no Federal, State, Municipal, County unpaid tax liens, no fraud or felonies individually, corporately or of any related concerns, affiliates, subsidiaries.'' If so, explain.

Response: ''Credit history'' is a well understood industry term that contains the elements identified by the commenter. Therefore, the Agency does not believe it necessary to spell out to this level of detail in the regulation and no changes to the rule have been made in response to this comment.

Comment: One commenter suggested the following for § 5001.16(b)(2)(ii): Including, but not limited to, cash flow available to service the proposed and historical debt with a service requirement of 1.0 to 1 as defined in the proposed regulation.

Response: ''Cash flow'' is a well understood industry term that contains the elements identified by the commenter. Therefore, the Agency does not believe it necessary to spell out to this level of detail in the regulation and no changes to the rule have been made in response to this comment.

Comment: One commenter suggested the following for § 5001.16(b)(2)(iii): Capital, including, but not limited to, for existing businesses, 10% tangible balance sheet equity, new company 20% tangible balance sheet equity.

Response: The Agency does not intend this part of the rule to spell out specific metrics that each project must meet when a lender conducts its credit evaluation (other than as specified in § 5001.6(b) as minimum threshold levels). Rather, the Agency is relying on the lender to perform its credit evaluation in accordance with its policies and procedures and the Agency will review such evaluations when determining whether or not to issue the Loan Note Guarantee.

Comment: Two commenters stated that there is no discussion on the proper discounting of collateral for Business and Industry guarantees. The commenters added that § 5001.16(b)(2)(iv) is adequate for lending to nonprofit entities and public bodies, but is inadequate for lending to for-profit businesses. The commenters recommended using the language found in RD AN No. 4279 (4279–B).

A third commenter offered suggested discount loan to value ratios as follows:

Land: 40% (low), 80% (high)

Improved Commercial Property: 50% (low), 85% (high)

Chattels: 50% (low), 65% (high)

Inventory: 25% (low), 60% (high)

Accounts Receivable (Less than 90 days): 50% (low), 85% (high)

Response: As noted in responses to previous comments, the Agency has revised the rule for the Business and Industry and the Rural Energy for America programs by adding specific discounted values in subpart B for the two programs. For other types of collateral in these two programs and for the other programs, the Agency will identify appropriate discounted values in the Conditional Commitment. The lender is required to use either the discounted values in the rule or in its own policies and procedures, whichever is more stringent, unless otherwise approved by the Agency.

Appraisals (§ 5001.16(c))

Comment: One commenter recommended that appraisal requirements should follow 7 CFR part 3575, subpart A in that appraisals may be required by the lender or the Agency. According to the commenter, community facility projects are typically specialized facilities and may very well not appraise for the cost to actually construct them. The security package generally relies on revenues and community support of the facility to pay the debt. This is the primary reason a lender will need the guarantee, because there is not enough hard security to secure the loan without the guarantee.

Another commenter requested the removal of the appraisal requirement and fair market evaluation for real estate collateral taken as security for Community Facilities. The commenter noted that currently more than 50% of Guaranteed Community Facilities are made for benefit of healthcare. The commenter stated that the focus for the next several years will be on Critical Access Hospitals, which are aged and in critically in need of replacement and that for healthcare facilities a fair market valuation is difficult to obtain and comparables within proximity are likely impossible.

Response: As noted in a response to a previous comment on appraisals under § 5001.12, Applications, the Agency is requiring that appraisals acceptable to the Agency be submitted with the application, if they are available. If they are not available at the time the application is submitted, complete appraisals must be submitted to the Agency before loan closing.

With regard to appraisals and community facilities, the Agency agrees with the commenter that issues may arise when obtaining appraisals for community facility projects because such projects may not appraise for the full value of the guarantee. However, the Agency believes that, in those instances where this may occur, the project can still be considered for a loan guarantee without compromising risk mitigation if there is sufficient demonstration of community support. Therefore, the Agency has added a provision to subpart B for community facilities (see § 5001.101(e)) that specifically allows the Agency to consider community support in evaluating the application for guarantee when a loan's collateral appraises at a level less than 100% of the loan amount.

Comment: One commenter recommended adding the following language: ''Chattel property will be evaluated in accordance with normal banking practices and generally accepted methods of determining value.''

Response: The Agency agrees that the rule needs to address chattel property as suggested by the commenter. The Uniform Standards of Professional Appraisal Practices (USPAP) contains standards that cover chattel property. The rule requires that such appraisals be completed in accordance with USPAP standards.

Comment: Two commenters commented on who would conduct the appraisals. One commenter noted that Certified General Appraisals perform appraisals, not lenders. This comment recommended that the requirement should read that the lenders will obtain a real property appraisal in accordance with USPAP Standards 1 and 2. The other commenter noted that collateral will be appraised by the lender in accordance with the appropriate guidelines contained in the current USPAP Standards 1 and 2 or successor standards. This commenter stated that it is generally not appropriate for the lender to conduct real estate appraisals, and wondered if the Financial Institutions Reform, Recovery and Enforcement Act standards were intentionally left out and suggested adding the following language, so as to put the responsibility on the lender: ''Lenders will be responsible for ensuring that appraisal values adequately reflect the actual value of the collateral.''

Response: The Agency agrees with the commenters that appraisals should be conducted by an independent qualified appraiser, not by a lender. Therefore, the Agency has modified the rule text to state, in part, that ''lenders are required to provide real property and chattel collateral appraisals conducted by an independent qualified appraiser.''

Comment: One commenter stated that appraisals should not be required prior to approval, because borrowers would have to pay cash for the appraisal with no assurance that financing would follow. The commenter recommended requiring the appraisal after the guarantee is approved, but before its issuance.

Response: The Agency understands the concern expressed by the commenter. In the rule, appraisals acceptable to the Agency are to be submitted with the application if they are available. If they are not available at the time the application is submitted, complete appraisals must be submitted to the Agency before loan closing.

Comment: Several commenters raised concerns over environmental hazards and appraisals.

One commenter requested that the requirement that appraisals include consideration of the potential effects from a release of hazardous substances or petroleum products or other environmental hazards on the market value of the property be removed. The commenter noted that an environmental assessment is already performed by USDA on the property and that for certain types of facilities local, state, and federal regulations provide for certain criteria in the handling of hazardous substances and the facilities must be built to those specifications. Another commenter stated that, because environmental assessment reports are already required, the process of identifying possible contaminants is already being performed and any potential threat would already be identified.

One commenter recommended that because appraisers are not usually experts on the scientific aspects of contamination, experts from other fields, such as appropriate regulatory authorities, be consulted to confirm the presence or absence of any contamination or potential release. Another commenter stated that this requirement is not going to be effective because appraisers are not qualified to test for or detect environmental hazards and the appraised value is based on the assumption that no environmental contaminants exist on the subject property. This commenter also noted that unless there is a quantifiable clean up cost, the appraiser cannot be expected to forecast that effect on the future market value.

One commenter stated, in general, that the present process of the lender obtaining an environmental assessment report for the proposed site and including a review of adjacent properties coupled by the NEPA review by USDA personnel would seem to be extraordinary processing. For new construction, the borrower must obtain permits from local authorities that would already include this type of review process.

Response: The first commenter is assuming that, under NEPA, the Agency will always conduct an environmental assessment. However, in accordance with the applicable regulation, environmental assessments are not always required especially if a project qualifies for a categorical exception. In addition, NEPA is a Federal requirement that the Agency cannot waive. For these reasons, the Agency believes it would be inappropriate to remove this requirement from the regulation and rejects this request.

With regard to the concern expressed about the qualifications of the appraiser with regard to environmental hazards, the Agency agrees with the commenters that appraisers may lack the requisite expertise to assess environmental hazards adequately. In such instances, the Agency would expect an appraiser to seek qualified assistance or to note in the report his/her opinion on environmental hazards. However, the Agency does not believe it is necessary to address this concern in the rule.

Personal, Partnership, and Corporate Guarantees (§ 5001.16(d))

The Agency notes that provisions in the rule now include reference to partnership guarantees, although this term is not used in the following comments and responses to those comments.

Comment: One commenter suggested adding the following language to the end of the paragraph as follows: ''Personal and corporate guarantees. Unconditional personal and corporate guarantees are part of the collateral for the loan, but should not be considered when calculating the loan-to-value ratio.''

Response: The Agency agrees, in part, with the commenter's suggestion in that unconditional personal and corporate guarantees should not be considered when calculating the loan-to-value ratio if these unconditional guarantees are unsecured. The Agency believes that unconditional personal and corporate guarantees that are secured can be used to determine security of the loan. Secured, unconditional guarantees can be used in calculating the loan-to-value ratio because they are part of the security. Because unsecured, unconditional guarantees are not part of the security of the loan, they, by definition, cannot be used in calculating the loan-to-value ratio.

Comment: One commenter suggested that the unconditional guarantee form for personal guarantees be modified to allow for some negotiation, for example, pro-rata guarantees based on one's percentage of ownership.

Response: The Agency agrees with the commenter that the proposed rule was unclear on whether the unconditional guarantee is secured or not. The commenter appears to believe that such guarantees must be secured and, therefore, should be adjusted on a pro-rata basis. In the rule, the Agency has clarified the difference between secured and unsecured guarantees and believes that this clarification addresses the commenter's concern.

Design Requirements (§ 5001.16(e))

Comment: One commenter recommended deleting the entire design requirement because lenders do not have the expertise to certify that design requirements meet accepted practices or that the design and construction of the project conform to applicable federal, state, and local codes and requirements. The commenter also stated that by virtue of the borrower obtaining a building permit, a qualified person and/or agency has already made those determinations of qualifications.

This commenter also expressed concern with the requirement for the lender to ensure that the project is constructed within the original budget. According to the commenter, there are many times when a contractor ''comes across'' an unknown (e.g., abandoned leach line not previously identified, a finding of Native American artifacts on the site, etc.) that would necessitate a change in the overall construction budget that was beyond the control of the borrower, contractor, or the lender. All of these are examples that would necessitate a change in the overall construction budget that were beyond the control of the borrower, the contractor of the lender.

Response: The Agency disagrees with the recommendation to delete this requirement. Building permits may not reflect all Federal requirements (e.g., Americans with Disabilities Act). In addition, the Agency believes that lenders either have or can procure the appropriate expertise to address these requirements. Therefore, the Agency has not revised this requirement in response to this comment.

With regard to the comment concerning ensuring that the project is constructed within the original budget, the Agency agrees with the concerns expressed by the commenter. The Agency has revised the rule to state that the project will be fully constructed with the ''approved'' budget, rather than the ''original'' budget as was proposed.

Comment: One commenter suggested that a section should be added to require that the design consultant or an independent qualified inspector certify that the project was built in accordance with the plans and specifications as well as all applicable building codes.

This commenter suggested adding the following sentence: ''Lenders must also ensure that all projects are designed using Agency recommended environmental mitigation measures.''

Response: The certification that the project was built in accordance with the plans and specifications and all applicable building codes will be provided in the loan documentation. The Agency does not believe it is necessary to state such in the rule.

With regard to the suggestion to add language ensuring that all projects are designed using Agency recommended environmental mitigation measures, this is provided for in § 5001.16(h)(2) and the Agency does not believe any changes are required in this regard.

Comment: One commenter noted that in some rural areas, no commercial building code has been adopted by the state or local jurisdiction. The commenter stated that in the Agency's direct programs, the Agency adopts a minimum model building code standard for those areas to meet, and questioned how this issue will be addressed under a guaranteed program with lender involvement. The commenter suggested that it might be simplest to have the lender/borrower/project architect use the commercial building code adopted by the Agency rather than pick another model building code. The commenter noted that in jurisdictions where there is no officially adopted commercial building code, there would be considerable risk involved in development unless some generally recognized commercial building code is followed.

Response: The Agency agrees that the situation identified by the commenter needs to be addressed. The Agency has modified the rule to ''or other Agency-approved code.'' This will allow the Agency to address specific situations on a program-by-program basis. In addition, the Agency will provide additional guidance in the handbook to the rule.

Monitoring Requirements (§ 5001.16(f))

Comment: One commenter questioned how the Agency will monitor that the lender actually monitored construction and processed funds, ensuring that the funds are used only for eligible project costs. The commenter suggested that attendance at a final inspection could provide verification that work was adequately performed and that there is a product for the funds expended.

Response: The rule requires the lender to commit to monitoring construction in accordance with approved plans and specifications and to ensure that project funds are used only for Agency-approved project costs by certifying to such in the Conditional Commitment. While the Agency's general policy is not to monitor construction, either during or at a final inspection, the Agency reserves the right to take any monitoring action for its own purposes.

Compliance With Other Federal Laws (§ 5001.16(g))

Comment: One commenter suggested providing a more comprehensive list that would include all the Federal laws that would apply for a loan guarantee, and suggested that the Office of General Counsel should be consulted. The commenter provided several additional laws that would also apply:

—Copeland Anti-Kickback Act (18 U.S.C. 874)
—Restrictions on Lobbying (Pub. L. 101–121, section 319)
—Suspension/Debarment requirements (7 CFR part 3017)
—Residential Lead-Based Paint Hazard Reduction Act of 1992 (24 CFR part 35)

Response: The Agency disagrees with the commenter that additional laws should be added to this list provided in this paragraph. An accounting of all applicable Federal laws is better addressed outside of the regulation. The Agency will consider identifying additional applicable Federal regulations in the handbook to the rule. The Agency has not revised this paragraph in response to this comment.

Comment: One commenter recommended verifying with the Civil Rights Staff the language about compliance reviews as being required every three years and that they end three years after the date of loan closing is correct. The commenter suggests that the correct language is more likely three years after loan payoff, because loan closing typically occurs at the end of construction and compliance reviews would end with the first review after completion of building construction.

Response: The Agency consulted with their Civil Rights staff in considering this comment. The last sentence of the proposed paragraph, which is what is being commented on, applies to grants and direct loans and not to guaranteed loans. However, if a guaranteed loan is combined with a direct loan or a grant, then this provision needs to be taken into account. Such situations will be identified in the handbook to the rule. Because it is not needed, the Agency has removed this sentence from the rule and further response to this comment is unnecessary.

Environmental Responsibilities (§ 5001.16(h))

Comment: One commenter questioned how the Agency will take responsibility for ensuring that the lender has made certain that the borrower has provided the necessary environmental information (e.g., permits), has adopted and implemented required mitigation measures, and is not taking any actions that may limit the range of alternatives (e.g., anticipatory demolition).

This commenter also suggested that the Agency take responsibility for ensuring the lender has made certain that the borrower has complied and then asked: ''How will the Agency monitor such assurances?''

Response: The information provided by the lender in § 5001.16(h)(1) provides the Agency with the information necessary to evaluate compliance with the requirements specified in § 5001.16(h)(2) and (h)(3). Furthermore, as proposed, the rule reflects the current practices and operation employed by the Agency and has proven adequate to protect the interests of the government.

With regard to the comment concerning the monitoring of lender's assurances that the borrower has complied, if the Agency discovers that the lender's certifications are false, the Agency may pursue debarment.

Conflicts of Interest (§ 5001.16(i))

Comment: One commenter questioned how a lender would identify a conflict of interest and how the Agency would monitor this lender activity.

Response: Lenders would identify what the Agency considers to be conflicts of interest or appearance of conflicts of interest through guidance in a handbook to the rule. With regard to monitoring the lender's identification of conflicts of interest, the lender is required to submit a written summary of its origination policies and procedures, which would describe the process to be used to identify such conflicts. The Agency would then depend on the lender to notify the Agency of conflicts. Finally, through its monitoring of the lender, including during lender visits, the Agency may discover conflicts.

Lender Responsibilities—Servicing (§ 5001.17)

Comment: One commenter recommended that the Agency incorporate into the rule the requirement that a lender obtain financial statements from the borrower and submit them to the Agency within 120 days (or preferable 150 days) with their written analysis and comments, as found in the existing 7 CFR 3575.69(b).

Two commenters noted that there appears to be no requirements for the borrower to provide annual financial statements to the lender. One of these commenters suggested developing a section that requires annual financial statements from the borrower prepared by a certified public accountant in accordance with GAAP.

The other commenter suggested adding the following paragraph: ''(c) Borrower financial statements. The lender must obtain and forward to the Agency the financial statements required by the Conditional Commitment and Loan Agreement. The lender must submit annual financial statements to the Agency within 120 days of the end of the borrower's fiscal year. The lender must analyze the financial statements and provide the Agency with a written summary of the lender's analysis and conclusions, including trends, strengths, weaknesses, extraordinary transactions, other indications of the financial condition of the borrower, and the borrower's current loan classification.''

Response: The Agency agrees with the commenters that the proposed rule did not adequately address requirements for financial statements once the guaranteed loan is in place and that such a requirement needs to be provided for in the servicing section of the rule. The Agency has determined that the requirement for financial information on borrowers can be handled in a similar fashion for all of the programs included in this final rule. Specifically, the rule contains a provision for the submittal of financial reports once the loan is in place (see § 5001.17(d), Financial reports). This provision requires regulated or supervised lenders to submit the information that would be contained in financial reports required by the lender's appropriate regulatory institution. This information would be submitted to the Agency at the same time it should be made available to the appropriate regulatory institution, unless otherwise provided in the Conditional Commitment. For other lenders, the rule requires financial reports as specified in the Conditional Commitment.

Collateral (§ 5001.17(e) (Proposed § 5001.17(c))

Comment: Five commenters provided comments on the requirement to obtain prior approval from the Agency. Two of the commenters stated that the requirement is ''pretty loose'' because the Agency is guaranteeing the lender against loss on 60 to 90% of the loan, and recommended that prior Agency approval be required on all releases of collateral.

Another commenter stated that this requirement is ''overreaching'' Agency needs and should be further defined and limited. According to the commenter, lenders and borrowers need to have clear understanding of their rights and responsibilities and must be free to run their business, service their loans, and conduct normal business transactions without Agency review. Above a point certain, defined early in the processing, sure, the lender should approach the Agency. But this section needs to identify what that demarcation line is, not leave it completely open-ended and unilateral.

One commenter stated that it is not clear how the lender is to know when prior Agency approval is required. Another commenter recommended a dollar threshold of $20,000 for when the Agency may require Agency approval prior to releasing collateral, and that any release for more that that would require prior Agency approval.

Response: In considering these comments, the Agency has rewritten parts of this paragraph to clearly identify those situations in which the Agency will not require prior approval. Those instances are where the proceeds are used to pay down debt in order of lien priority, or to acquire replacement equipment, or where the release of collateral is made under the abundance of collateral provision of the security agreement. In all other instances, the Agency will require written approval.

Comment: Two commenters stated that there are instances where a lender will take a lien on collateral as ''additional security'' to be released later without monetary consideration under certain specified conditions. Therefore, the commenters recommended that the rule allow a lender such flexibility subject to USDA's prior written concurrence. A third commenter stated that the proposed regulation on the release of collateral is too restrictive on the lender. This commenter suggested that maximum flexibility should be allowed for application of sale proceeds, as long as the lender and USDA can agree.

Response: In order to manage the risk inherent in the Agency's portfolio of guaranteed loans, the Agency has provided significant flexibility in certain instances as identified in the rule (§ 5001.17(e)) and will consider all other releases on a case-by-case basis and provide written approval as appropriate.

Transfers and Assumptions (§ 5001.17(f)) (Proposed § 5001.17(d))

Comment: One commenter recommended adding the following language to proposed § 5001.17(d)(2)(i): ''While a transfer and assumption is a loan servicing action, it is subject to an Agency review of its credit quality, and must be in compliance with published eligibility requirements set forth in this subpart. This would normally require submitting a new application; business plans with pro forma balance sheets, 2 years projected balance sheets and income statement, in addition to the lender's financial analysis of the new business and current guarantor financial statements.'' The commenter noted that, if this is not published, how will lenders know to submit this information when processing a transfer and assumption.

Response: As proposed and as retained in the rule, any time a third-party assumes a loan guarantee under this part, the loan guarantee will be processed and approved by the Agency as if it were a new loan guarantee application. This means that the assumption will be subject to a review of the credit quality and compliance with the eligibility requirements of the rule, just as would a new loan guarantee application. Therefore, there is no need to revise the rule as suggested by the commenter. The Agency will provide additional guidance on this point in the handbook to the rule.

Comment: One commenter recommended deleting the transfer and assumption fees because the loan guarantee program already obtains an annual renewal fee from each lender and an additional fee would be an undue burden on the lender.

Response: The Agency has not adopted the suggestion made by the commenter to delete the provision for transfer and assumption fees. The Agency notes that the rule does not require the Agency to charge such fees, but that they are optional. If, in the future, the Agency determines that such fees adversely affect the programs, the Agency will either stop charging such fees or make an adjustment to them.

Mergers (§ 5001.17(g)) (Proposed § 5001.17(e))

Comment: Ten commenters requested that the Agency not be allowed to withdraw the guarantee when a borrower participates in a merger.

Several commenters pointed out that current Business and Industry regulations establish that a borrower cannot participate in a merger without prior approval of the lender and USDA. One commenter stated that, under the existing regulation, lender documents contain language that the borrower cannot participate in a merger without prior approval by the Bank and USDA.

One commenter noted that it is possible for borrowers to participate in mergers without lender knowledge and suggested that a more reasonable and equitable solution would be to require prior Agency approval for mergers or the Agency would have a case for negligent servicing. The commenter also wondered why this action is being singled out.

One commenter stated that the merger of a company should not be grounds for the guarantee being withdrawn, and recommended that the current regulations requiring the lender to obtain approval from the Agency for a merger remain.

One commenter stated that if the Agency can withdraw the guarantee for something as simple as a borrower merger, the lender will fear the Agency can withdraw the guarantee at every chance it gets. The commenter pointed out that a borrower merger is out of the control of the lender and the lender cannot and should not be penalized if the borrower decides to merge with another company and not seek permission from the lender and USDA prior to the merger. According to the commenter, one withdrawal would ruin the reputation of the program and then asked ''What would become of the innocent holders in this scenario?''

Three commenters stated that this will be detrimental to the borrower, the lender, and the secondary market, is not borrower, lender, or secondary market friendly, and would reduce the number of borrowers, lenders, and investors interested in the programs.

Another commenter said that this is unduly harsh. According to the commenter, a borrower could merge without the permission or knowledge of the lender, notwithstanding contract requirements prohibiting such an act. The commenter stated that the risk that such an event could occur is one which is shared by both the lender and the guaranteeing agency and that the partnership between our bank and various agencies offering federal guarantees has always been one of partnership, with each of us assuming our share of the risks associated with lending. This provision represents a significant preference in favor of the guaranteeing agency, a circumstance which is a major departure from our historical sharing of risks and responsibilities.

One commenter stated that this provision would cause major problems with the lending and secondary market. The commenter noted that the guarantee is supposed to be a full faith in credit guarantee from the Agency to the secondary market note holder. According to the commenter, this proposed paragraph should be eliminated because no mergers can occur without the prior written consent of the Agency or Lender and it places a great burden on lenders and secondary note holders.

Response: In considering the comments submitted, the Agency has revised the provision that would have allowed the Agency to withdraw a guarantee in situations where a borrower participates in a merger. This provision was intended to help ensure that the merger did not result in a less desirable borrower (i.e., one who might not be able to repay the loan). The Agency agrees that withdrawal of the guarantee is not the best way to help avoid this outcome. Instead, the Agency is requiring that both Agency and lender approval is required prior to a borrower participating in a merger. In this fashion, both the Agency and the lender will discuss the proposed merger and evaluate the quality of the new borrower.

In addition, the Agency recognizes that a borrower may participate in a merger without notifying its lender or the Agency. To help address this situation, the Agency has added a provision to the rule that requires the lender to accelerate the loan if a borrower merges without prior Agency approval, unless subsequently agreed to by the Agency in writing.

Subordination (§ 5001.17(h)) (Proposed § 5001.17(f))

Comment: Seven commenters expressed concern over the one-year time frame.

One commenter noted that most banks are now trying to set up operating lines of credit for two to three years, and to have to go back to the USDA every year would be counterproductive and inefficient. Another commenter stated that to have to approve subordinations every year for lines of credit is burdensome and that consideration should be given to extending this for a longer period.

One commenter pointed out that lines of credit are often extended for periods of three to five years and suggested that the rule allow for subordination on working assets (A/R and inventory) for more than up to at least three years. Another commenter recommended that the rule allow subordination on working assets for more than one year, noting that flexibility to approve multi-year subordinations is appropriate and beneficial to the borrower. Two commenters suggested that this provision should allow three to five years, with one commenter stating that the one-year limit may not allow the company to operate past the one-year time frame.

One commenter stated that limiting subordination of term debt to one year for a revolving line of credit has never been a good or workable policy. This commenter questioned if the lender can trust USDA to be reasonable with this, and if the subordination is not continued, what happens to the line of credit's lien position and what does this do to the borrower's ability to operate the business. The commenter stated that the subordination should be automatic if the line is renewed at the same level from year to year.

Response: After considering the reasons cited by the commenters, the Agency agrees that one year is too short a time frame. The Agency has replaced the one-year time frame in the rule such that the subordination of line of credit cannot extend the term of the line of credit and cannot be more than three years under any circumstances.

Comment: One commenter stated that it is reasonable for the Agency's financial interests to be maintained, but that it is not reasonable to require the Agency's financial interests to be enhanced by subordination. The commenter also stated that it is not reasonable to require the loan to remain adequately secured if it was not adequately secured before the subordination. According to this commenter, the Agency should not be in a worse position as a result of subordination.

A second commenter urged the Agency to incorporate the current regulation, which states that the subordination must enhance the borrower's business and the Agency, into the proposed rule.

Response: The Agency considered the two commenter's comments on the relationship of the subordination to the Agency's interest, including the provisions in the current regulation. The Agency agrees that the proposed provision that the Agency's financial interest be enhanced was not reasonable, but that the Agency should not be in a worse position as a result of subordination. The Agency has revised the rule to require that the subordination ''be in the best financial interest of the Agency.''

With regard to the comment concerning the proposed requirement that the loan ''remains adequately secured,'' the Agency has determined that this requirement does not need to be spelled out in the rule, because the relationship of collateral to the loan is inherent in the requirement that the subordination be in the best financial interest of the Agency. Thus, the Agency has removed this provision from the rule.

Repurchases From Holders (§ 5001.17(i)) (Proposed § 5001.17(g))

Comment: One commenter suggested adding language requiring Agency concurrence when a holder objects to selling its interest in a loan to the lender. The commenter noted that, in some cases, the holder is not asked if they would concur in the servicing action and that they have handled calls from holders that object to selling their interest so the lender can complete simple servicing actions that the holder would not oppose. The commenter stated that this becomes increasingly objectionable when the notes are repeatedly sold by the lender at a premium and repurchased at par.

Response: The Agency agrees with the concern expressed by the commenter about a holder who objects to selling its interest in a loan to the lender. The Agency has revised this provision to require that both the lender and the Agency (rather than either the lender or the Agency as was proposed) must determine that the repurchase is necessary to protect the loan. This change prevents a lender from making the sole determination of when to effect a repurchase and should adequately address the commenter's concern.

Comment: One commenter stated that provisions should be expressly added to the requirements for repurchases from holders that when a borrower cures the default and the loan returns to performing status, the Agency is allowed to resell the guaranteed portion back to the lender at par value, whereupon the guaranteed portion could be further sold by the lender back into the secondary market. The commenter believed that this would result in considerable administrative savings to the Agency.

Response: In considering this comment, the Agency discussed with the Treasury Department what, if any, constraints there are associated with the Agency reselling a repurchased loan. Based on this discussion, the Agency has found that it is prohibited from reselling any repurchased loan except under the Business and Industry guaranteed loan program. Therefore, the Agency has accepted the comment as it applies to the Business and Industry program, but cannot accept it for the other programs. The Agency has added a provision to subpart B of the rule (§ 5001.103(i)) to provide for the reselling of repurchased Business and Industry guaranteed loans, without recourse to third-party private investors. In making this provision, the Agency notes that its exposure is not increased because the Agency will pay to the lender under the guarantee no more than the guaranteed principal and the guaranteed interest regardless of any advances made.

Additional Expenditures and Loans (§ 5001.17(j)) (Proposed § 5001.17(h))

Comment: Five commenters suggested dropping the requirement for Agency concurrence. Two of the commenters stated that the requirement for Agency approval on all additional expenditures is not needed unless the expenditure or loan will violate one or more of the loan covenants of the borrower's loan agreement.

Two other commenters stated that lenders should be allowed to extend unguaranteed loans without USDA concurrence, provided any USDA guarantee loan's collateral position is not altered and the borrower is current and performing as agreed. One of these two commenters added that the proposed requirement may limit the future growth and needs of the borrower, and the other commenter added that the requirement is cumbersome and intrusive.

Finally, the fifth commenter suggested that the Agency not be involved in a lender's decision to make additional loans to the borrower outside the guarantee by revising the rule by being silent on this issue. According to the commenter, a lender follows its own internal guidelines and prudent lending practices, and if the lender violates its own policies and procedures, the Agency would have a case of negligent servicing. In addition, the commenter believed that it would be difficult to support a decision to prohibit a lender from extending additional credit.

Response: The Agency agrees that Agency approval for all additional expenditures and loans is not required, but need only be required when such expenditures or loans would violate the borrower's loan agreement. Therefore, the Agency has revised the provisions to indicate that the lender may make additional expenditures without Agency approval unless the expenditure or loan will violate one or more of the loan covenants of the borrower's loan agreement. While the Agency agrees that making additional loans to the borrower outside the guarantee could serve as a basis for negligent servicing, the Agency disagrees that it is appropriate to be ''silent on this issue.'' By making the change to the rule as indicated, the Agency has narrowed the situations in which approval is required.

Comment: One commenter recommended revising this paragraph to require Agency approval only on loans involving large-scale expenditures or loans. According to the commenter, requiring Agency pre-approval on every single loan or increase on line of credit is an undue burden on the lender, the Agency staff, and the borrower.

Response: As noted in the response to the previous comment, the Agency has modified the provisions of this paragraph to require Agency approval only when the additional expenditure or loan would violate one or more of the loan covenants of the borrower's loan agreement and not for all additional expenditures and loans, as was proposed. As rewritten, the Agency believes its approval is necessary whenever a violation of the borrower's loan agreement would occur, regardless of the size of the additional expenditure or loan.

Lender Failure (§ 5001.17(k)) (Proposed § 5001.17(i))

Comment: One commenter asked if no successor entity can be determined in the event of a lender failure, does the Agency have the right or legal authority to enforce the provisions of the loan documents on the lender's behalf.

Response: The Agency agrees that the situation identified by the commenter was not adequately addressed in the proposed rule and should have been. Therefore, the Agency has revised the rule to address situations where the lender ceases servicing the loan.

Delinquent Loans (§ 5001.17(l)) (Proposed § 5001.17(j))

Comment: One commenter asked why the lender has to coordinate this with the Agency at this time and suggested that the lender should be allowed to service the loan and advise the Agency as to what is being done.

Response: The Agency agrees with the commenter that allowing the lender to implement appropriate curative actions for loans that are delinquent more than 30 days in accordance with its policies and procedures is sufficient and does not require coordination with the Agency and has removed this requirement from the rule. The Agency also revised the text to remove reference to coordination with the borrower because the text is unnecessary. The rule requires the lender to notify the Agency when a loan's classification has been downgraded (§ 5001.4(b)(3)(iii)) and the Agency believes that this is sufficient notice in adverse situations.

Protective Advances (§ 5001.17(m)) (Proposed § 5001.17(k))

Comment: Four commenters provided comments on the level at which Agency approval of protective advances would be required.

One commenter stated that, because protective advances are covered by the guarantee, this is a significant increase in risk to the government, and expressed concern that the subsidy calculations did not consider this additional exposure.

Another commenter also expressed concern about the increase in risk to the government, stating that allowing a lender to advance $200,000 of protective advances without concurrence from USDA is too large a sum, exposing the Government to significant additional losses. This commenter suggested that a more reasonable standard would be to require prior concurrence from USDA whenever cumulative advances exceed $25,000, and added that certain protective advances should be exempted from this cumulative total and should be authorized without USDA concurrence because they are clearly essential in preserving collateral (e.g., the payment of delinquent property taxes).

On the other hand, another commenter stated that increasing protective advance expenditures to $200,000 without pre-approval is a good change and should remain.

Response: In consideration of these comments, the Agency has not changed the level associated with protective advances for which Agency approval is required. Being a higher level than suggested by the commenter, there is no need to identify exceptions, such as the payment of delinquent property taxes. The Agency does not believe that the proposed levels increase Agency exposure because the Agency will pay to the lender under the guarantee no more that the guaranteed principal advanced to or assumed by the borrower and any interest due.

Comment: One commenter recommended that the following language should be added:

''(a) The maximum loss to be paid by the Agency will never exceed the original principal plus accrued interest regardless of any protective advances made.

(b) Protective advances and interest thereon at the note rate will be guaranteed at the same percentage of loss as provided in the Loan Note Guarantee.

(c) Protective advances must constitute an indebtedness of the borrower to the lender and be secured by the security instruments.''

Response: The Agency agrees with the commenter that these provisions are useful in ensuring protective advances are considered appropriately under this rule and has added these provisions to the rule. Specifically, the rule includes the second and third suggestions in § 5001.17(m)(4) and (6). The Agency has incorporated the commenter's first suggestion in § 5001.17(m)(7), although this maximum loss provision is slightly different than as suggested.

Liquidation (§ 5001.17(n)) (Proposed § 5001.17(l))

Comment: One commenter stated that a much more detailed section on liquidation is needed, as the guidance provided is scattered and incomplete. The commenter recommended adopting the rules used by the USDA FSA's guaranteed loan program (see 2–FLP paragraph 14; 7 CFR 76.149), because, according to the commenter, FSA has had more experience with liquidations and loss claims and its regulations are more developed and thorough, as a result. The commenter then pointed out that FSA's rules are well-accepted by the agricultural lending community, which constitutes a significant share of Rural Development guaranteed lenders as well.

Response: As described earlier in this preamble, the Agency has added some additional requirements to this part of the interim rule. The Agency believes these additions, in conjunction with the Agency's intent to use the handbook to provide additional guidance on liquidation, are sufficient to meet the commenter's concerns.

Comment: Two commenters provided comments related to the last sentence in the introductory text to proposed § 5001.17(l). The commenters questioned that, if the Agency concludes that liquidation is necessary, why would the security instruments be assigned to the Agency, especially because the lender is required to liquidate the collateral. The commenters suggested that this section be rewritten.

Response: The proposed rule should have stated that, once the lender has assigned the security instruments to the Agency, the Agency, not the lender, will liquidate the loan. The Agency has modified proposed § 5001.17(l) accordingly (*see* § 5001.17(n)).

Comment: One commenter disagreed with the 30-day suspension period in proposed § 5001.17(l)(1), stating that rapid action is critical in liquidations. The commenter suggested that:

(1) Liquidation should be allowed upon approval of the liquidation plan by the Agency;

(2) The Agency should be required to approve or disapprove the lender's liquidation plan within five working days (not 30);

(3) Although liquidation appraisals should be required as part of the liquidation planning process, they should not be absolutely required for liquidation plan approval, provided they are obtained prior to the completion of the liquidation; and

(4) The Agency should continue the process of splitting the cost of liquidation appraisals and the authority for doing this should be spelled out here.

Response: The Agency considered each of the commenter's suggestions for revising the proposed requirements for the liquidation plan. The Agency agrees with each of the commenter's suggestions, except for the suggestion that approval or disapproval be provided with five working days, rather than 30 working days. The 30-day period proposed was not and is not intended to be a suspension period, but was proposed to allow the Agency sufficient time to review the final liquidation plan and to either approve or disapprove it. The Agency anticipates that its decision on liquidation plans could take less time and, when possible, will do so.

With regard to the commenter's other three suggestions, the Agency agrees and has modified the rule text to incorporate each suggestion. Specifically, if the outstanding principal loan balance including accrued interest is more than $200,000, the lender is required to obtain an independent appraisal report on all collateral securing the loan, which will reflect the current market value and potential liquidation value. All appraisals must meet the requirements set forth in the USPAP. If an environmental assessment of the property is necessary in connection with liquidation, the cost will be shared equally between the Agency and the lender.

Loss Calculations and Payment (§ 5001.17(p)) (Proposed 5001.17(n))

Comment: One commenter stated that the paragraph discussing loss calculations and payment needs expansion to enable the lender to liquidate the collateral to establish the final loss. The commenter pointed out that lenders take title to collateral through, but not limited to, foreclosure process, deed in lieu of foreclosure, and bankruptcy process. The lender then liquidates the collateral and prepares final loss settlement as per proposed § 5001.17(n)(3).

Response: The Agency disagrees with the commenter that § 5001.17(p) (in the rule), Loss calculations and payment, needs to be expanded as suggested. The text in § 5001.17(p) does not prohibit the lender from liquidating collateral (liquidation is covered in § 5001.17(n)). In addition, the methods identified by the commenter on how lenders may acquire title to collateral does not need to be addressed in the rule, but can be, as the Agency intends to do, covered in the handbook to the rule. Therefore, no changes have been made to the rule text in response to this comment.

Comment: Three commenters requested the Agency reconsider proposed § 5001.17(n)(3)(i) with regard to how the value of collateral obtained would be determined when calculating loss. Two of the commenters noted that the proposed rule states that the loss will be calculated based on the value of the collateral at the time the lender obtains title, but does not provide guidance on how the value of the collateral is to be determined. These commenters then asked: If an appraisal is obtained, would the Agency use the market value or liquidation value?

The third commenter stated that the statement that loss should be based on collateral value is too vague, and suggested that the loss should be expressly based on the appraised liquidation value.

Response: After considering these comments, the Agency has revised § 5001.17(p)(5)(i) to reflect that the collateral's value for purposes of determining loss claim will be based on the liquidation value of the collateral.

Comment: One commenter suggested that proposed § 5001.17(n)(3)(iii) state that the lender will request an estimated loss payment when liquidation is expected to exceed 90 days when a loss is anticipated. According to the commenter, such a provision would stop the interest accrual covered by the guarantee.

The other commenter stated that, except in the case of bankruptcy-related losses, estimated loss claims should be required on all liquidations that will take more than 90 days to complete.

Response: The Agency agrees with the suggestion that, when a loss is anticipated, the lender must submit an estimated loss claim to the Agency when liquidation is expected to exceed 90 days. In addition, the Agency has revised the rule to make clear that, once the liquidation plan has been approved by the Agency, no more than an additional 90 days of accrued interest will be payable.

Borrower Responsibilities (§ 5001.25)

Comment: One commenter suggested that § 5001.25(a)(3) be divided into two separate items. The commenter pointed out that consumer affairs is not related to protection of the environment, and, if anything, protection of the environment should be coupled with land use and zoning. The commenter stated that the borrower should be prepared to supply both the lender and the Agency with a copy of all environmental permits and/or status of securing such permits as early in the planning process as possible.

Response: The Agency has not divided § 5001.25(a)(3) into two separate paragraphs as there is no substantive benefit obtained in doing so.

With regard to the comment concerning environment permits and the status of securing such permits, the rule requires borrowers to obtain all permits, which would include all applicable environmental permits, under § 5001.25(b). As the Agency has the right to request the permits at any time for any project if permits may be a concern, the Agency agrees that such permits should be obtained as early as possible, but that it is not necessary to include such language in the rule.

Comment: One commenter noted that, regarding § 5001.25(d), the Agency's contract is with the lender, not the borrower. The commenter questioned what gives the Agency the right to access the borrower's records, and also asked if the borrower shouldn't have to sign something acknowledging this?

Response: Because borrowers are, at a minimum, third-party beneficiaries, the Agency has the right to access the borrower's records. While it is normal Agency practice for the Agency to work through lenders, the Agency may find it necessary to go to the borrower's records, especially in the case of a NAD appeal brought by the borrower. Finally, Form RD 5001–3 contains borrower certifications, which include acknowledgement of records access.

Basic Guarantee and Loan Provisions

General (§ 5001.30)

Conditions of Guarantee (§ 5001.30(b))

Comment: One commenter noted they recognize that the proposed regulation has retained the requirement found in the existing programs that the guarantees issued will be ''guarantees of loss'' rather than ''guarantees of payment''. We observe that most commercial guarantees today guarantee payment, rather than performance, to attract lenders when guarantees are needed. While a guarantee of payment may not be generally suitable for the Agency's loan programs, the selective use of a guarantee of payment by the Agency should be considered.

Response: The Agency has not changed the rule as requested by the commenter. The rule implements current practice, which is the Agency's intent, and to modify it as suggested by the commenter would increase the cost to the program. Therefore, the Agency has not accepted the commenter's suggestion.

Comment: Twenty six commenters provided comments in opposition of the proposal that ''the guaranteed portion would be paid first and be given preference and priority over the unguaranteed portion'' of loans. These commenters stated that the Agency should continue its current regulation that establishes ''the unguaranteed portion of the loan will neither be paid first nor given any preference or priority over the guaranteed portion''. The commenters also expressed their belief that the ''first loss'' proposed change would likely effectively kill the Business and Industry and CF guaranteed loan programs. Two commenters stated that this ''pari passu'' issue negates any material value of the guaranty by putting the lender more at risk than the agency and that it would also cloud any decisions in the liquidation process in favor of the agency.

Response: The Agency agrees with commenters and revised the rule to adopt the prior methodology, which provides that the unguaranteed portion of the loan will neither be paid first nor given any preference or priority over the guaranteed portion.

Full Faith and Credit (§ 5001.30(c))

Comment: One commenter noted that § 5001.30(c)(1) states that any Loan Note Guarantee or Assignment Guarantee Agreement relating to a note which provides for payment of interest on interest is void. The commenter stated that this appears inconsistent with full faith and credit provisions.

Another commenter stated that USDA should better define the prohibition against payment of interest on interest to include elevated default interest charges that apply to the entire loan. The commenter stated that USDA should not include language that voids a guarantee on a note that contains such prohibited interest on interest charges. The commenter further stated that USDA should never threaten to void a guarantee for anything short of fraud and misrepresentation and that if prohibited interest on interest is found after the fact, the loss occasioned by the prohibited charges should be negotiated downward, but no one should have the right to void the guarantee for what could be an oversight of the lenders standard note language.

Response: In response to the comment that § 5001.30(c)(1) appears to be inconsistent with full faith and credit provisions, the Agency points out that full faith and credit only applies on terms that the Agency has agreed to guarantee and that the Agency has not agreed to insure interest-on-interest. Therefore, there is no inconsistency.

With regard to the comment concerning elevated default interest changes, the Agency does not consider elevated default interest charges to be interest-on-interest and, therefore, would not void the guarantee. As otherwise provided in the rule, the Agency requires all rates to be reasonable (reasonable rates and terms apply). The Agency does agree that the rule needs to be revised with regard to the voiding of the guarantee attached to or relating to a note that provides for payment of interest-on-interest. The Agency has revised the rule (see § 5001.30(c)(1)) to state that ''any claim against a Loan Note Guarantee or Assignment Guarantee Agreement attached to, or relating to, a note that provides for payment of interest on interest will be reduced to remove interest on interest.''

Soundness of Guarantee (§ 5001.30(d))

Comment: One commenter noted that § 5001.30(d) requires all loans to be financially sound and feasible, with reasonable assurance of repayment, and suggested adding a less subjective requirement by also requiring all loans to meet or exceed the characteristics of a loan classified Special Mention by the Uniform Classification System as defined by the Agency, with no consideration being given to the guarantee.

Response: The Agency does not accept the suggestion to replace the current language with a requirement that loans meet or exceed the characteristics of a loan classified as Special Mention. The Agency's intent is to provide general requirements in subpart A that will be common to all programs included in the rule as well as to programs that may be added in the future. In addition, the Agency believes that the commenter's suggestion is effectively provided for by revising subpart B for the Business and Industry guaranteed loan program in accordance with the following comment.

Comment: Two commenters stated that the last sentence of 7 CFR § 4279.101(b) should be added to § 5001.30(d) for Business and Industry loans. The sentence reads: '' It is not intended that the guarantee authority will be used for marginal or substandard loans or for the relief of lenders having such loans.''

Response: The Agency agrees with the commenters that this provision in the current Business and Industry guaranteed loan regulations should have been included in this rule. Therefore, the Agency has modified subpart B for the Business and Industry program to include the suggested text (see § 5001.103(j)(1)).

Reduction of Loss Claims Payable (§ 5001.30(f))

Comment: One commenter stated that § 5001.30(f) appears to give USDA much more opportunity to reduce the guaranty once a loan is in liquidation; therefore, pushing more of the risk back to the lender. The commenter recommended the rule regarding reduction of loss claims not be changed and that the current rule of bad faith or gross negligence be retained.

Another commenter recommended deleting the negligent loan origination criteria and providing a clearer definition for loan origination. The commenter stated that the burden of possibly repaying the Agency for loss claims paid under the guarantee is of utmost concern for continuation by lenders in the program. The commenter further stated that a repayment to the Agency should be limited only to those instances where a lender commits fraud.

Response: With regard to the comment concerning the current rule of bad faith or negligence be retained, the Agency notes that there is no standard currently for bad faith or negligence.

With regard to the concerns expressed concerning negligent loan origination, as proposed, the only change that this paragraph made to existing rule text was to clarify that negligent loan origination can be a cause for reducing the guarantee. The proposed rule implements current practice and, thus, the Agency disagrees that this paragraph results in putting more risk back on the lender. To delete negligent loan origination from the rule would eliminate lender negligence as a cause for reducing the guarantee and the Agency disagrees with this result. Therefore, the Agency has retained this paragraph as proposed.

Guaranteed Loan Requirements (§ 5001.31)

Interest Rates (§ 5001.31(a))

Comment: One commenter suggested that USDA clarify that interest rates, interest rate caps, and incremental adjustment limitations will be negotiated between the lender and the borrower and will be subject to Agency concurrence. The commenter also suggested that the rule should state that interest rate caps (annual and lifetime) and incremental adjustment limitations are required by the Agency in order for the lender to offer some long term stability to the borrower and the proposed facility. The commenter stated that because the revenues of facilities operated by non-profit organizations and public bodies are quite often largely dependent on State and Federal payments and user fees that cannot be readily increased on short notice, it is vital to the success of these types of community projects that they have some built in parameters to prevent sudden or substantial long term interest rate increases.

Another commenter stated that prepayment penalties are a common practice in Business and Industry loans and suggested adding language stating that they are also a matter of negotiation between the lender and applicant.

Response: The Agency agrees with the commenter's suggestion that the interest rates, interest rate caps, and incremental adjustment limitations negotiated between the lender and the borrower be subject to Agency concurrence and has modified this paragraph in the rule accordingly. The Agency will also provide additional guidance in the negotiated rate section of the handbook for this rule.

With regard to the commenter's suggestion that the rule state that interest rate caps (annual and lifetime) and incremental adjustment limitations are required by the Agency in order for the lender to offer some long term stability to the borrower and the proposed facility, the Agency plans on addressing this in the handbook for the rule. Thus, no changes were made to the rule in response to this suggestion.

Lastly, with regard to the suggestion to add language stating that prepayment penalties are also a matter of negotiation between the lender and applicant, the Agency does not believe it is necessary to address this specific matter in the rule. The rule does not preclude the lender and the borrower from negotiating and adopting prepayment penalties and the Agency does not believe it is necessary to interject itself in such matters. Therefore, the Agency has not revised the rule in response to this suggestion.

Comment: One commenter noted that, currently, USDA guaranteed loans with a variable rate cannot vary more often than quarterly and that the proposed rule seemingly would allow daily variable rates. Another commenter stated that the Agency should allow for interest rate adjustments as often as the lenders desire; which is typically whenever the Prime rate changes (or other index used). Another commenter stated that variable interest rate adjustments due to changes in the base rate should not be allowed to occur more frequently than quarterly, while another commenter recommended that changes not be allowed more often than monthly.

Response: As proposed, the rule allowed the lender and borrower to negotiate interest rate adjustments as often as desired. The Agency has the opportunity to consider the rates, terms, frequency of adjustment, etc., when the Agency issues the Loan Note Guarantee. Thus, there is no need to provide a specific rate of adjustment in the rule and the Agency has not modified the rule to specify a specific rate of adjustment.

Comment: One commenter noted that § 5001.31 requires the lender to provide the Agency with the overall effective interest rate for the entire loan for variable rate loans and questioned why the Agency cares about the effective interest rate, and what would be done with the information.

Response: The Agency agrees that providing the overall effective interest rate does not need to be included in the rule and has removed this requirement from the rule.

Interest Rate Changes (§ 5001.31(b))

Comment: One commenter noted that proposed § 5001.31(b)(2) prohibits increases in interest rates except for normal fluctuations in variable rate notes. The commenter stated that the intent of this prohibition is not clear and questioned whether it is attempting to protect the borrower from lender actions. The commenter suggested not limiting or prohibiting customary lender practices, including increases in interest rates that are clearly disclosed in the loan documents and the lender underwriting and servicing policies and procedures.

Response: The Agency agrees that the proposed rule text was too limiting. The Agency has revised the rule to allow increases in interest rates that are permitted in the loan documents (see § 5001.31(b)(3)).

Comment: One commenter recommended amending the prohibition on the increase in interest rates. The commenter noted that there are times when a borrower continues to negotiate with the lender and a variable rate is changed to a fixed rate. A fixed rate option is generally at a higher initial rate; however, the borrower sometimes feels more comfortable for long-range planning with the fixed rate. This rule would prohibit what could be a borrower's request.

Response: The Agency agrees with the commenter and has revised the rule to allow the situation described by the commenter (§ 5001.31(b)(3)).

Comment: One commenter stated that interest rate sensitivity should have been considered in the project's evaluation by the Agency and, thus, there should be no requirement to get a written concurrence to adjust the rate when it was proposed and approved as variable. The commenter stated that this requirement is excessive, onerous, and unnecessary and that it subjects the Conditional Commitment to uncertainty as a rate change may not be approved by the Agency.

Two commenters stated that proposed § 5001.31(b) should state that normal variable rate fluctuations do not need to be approved by the Agency.

Response: The situations described by the commenters concern changes to variable interest rates. Variable interest rates are required in the rule to be tied to an index. When there is a change in the base rate of that index, the Agency agrees with the commenters that Agency concurrence is not needed—this is a normal fluctuation in the variable rate. Thus, the Agency has revised the rule to provide this exception to the requirement for Agency concurrence (§ 5001.31(b)(3)). The Agency still believes that it is necessary for it to provide concurrence if the change to the variable interest rate is, for example, from ''prime plus one'' to ''prime plus three.'' This type of change in the spread of the variable interest rate would still require Agency concurrence in the rule. In addition, changes in fixed interest rate loans would also still require Agency concurrence.

Term Length (§ 5001.31(c))

Comment: Three commenters stated that the term length provision is too flexible in allowing the lender to set the maximum term, ultimately only insisting that the term not exceed 40 years and that loan purposes should have stated maximum term limits, as they currently do in the Business and Industry program. Two commenters recommended: 30 years for real estate, 15 for machinery and equipment, and 7 for working capital. One commenter stated that loan terms for Business and Industry loans, except for those to municipalities, should be limited to 30 years. Another commenter recommended 7 years for working capital, 20 years for the useful life for equipment, and 40 years for real estate projects. This last commenter also stated that debt refinancing should be tied to the type of collateral used for the loan.

Response: The Agency has determined not to provide more specific term limits in the rule, as requested by the commenters, in order to provide flexibility. With regard to tying debt refinancing to the type of collateral used for the loan, the Agency believes that the rule is sufficient to allow the Agency to provide specifics in the handbook to the rule. Therefore, the Agency has not modified the rule in response to these comments.

Loan Schedule and Repayment (§ 5001.31(d))

Comment: One commenter noted that § 5001.31 requires the lender to incorporate the provision for adjustment of payment installments into the Note when variable rate notes are used. The commenter stated that this is, presumably, to eliminate the possibility of a balloon payment and the possibility that the Agency would have to pay a loss. The commenter suggested that balloon payments be permitted. The commenter also stated that if a lender is not satisfied with a borrower's performance at the end of the term, and wishes to call the note and possibly liquidate the collateral, it is not clear why the Agency should interfere. The commenter stated that this would likely expedite the acceleration and liquidation process, and possibly reduce loss exposure. The commenter also pointed out that FSA permits balloons, and has good experience with it.

Response: The agency remains concerned with allowing balloons under its guaranteed loan programs because balloons can cause hardship on the borrower/business and create agency risk and exposure. Therefore, the agency has not modified the rule as suggested by the commenter.

Maximum Loan Amounts (§ 5001.31(e))

Comment: Two commenters noted that § 5001.31(e) states the maximum amount that may be guaranteed will be determined on a program-by-program basis and will be published each year in the **Federal Register**. The commenters questioned the need to publish this information when the maximum loan amount is contained in proposed § 5001.101(e)(1) for Community Facilities and proposed § 5001.103(g)(3) for Business and Industry. A third comment similarly asked why publish in accordance with § 5001.31(e) when the limit is found in proposed § 5001.101(e)(1).

Response: The provisions in subpart B provide the ''default'' maximum loan amounts for these two programs. The program offices for these two programs may determine that they wish to impose a lower maximum loan amount in a given year. The provision for the annual **Federal Register** notice allows these two programs to reduce their maximum funding limits in any fiscal year. Therefore, the rule retains the paragraph questioned by the commenters.

Maximum Percent of Guarantee (§ 5001.31(f))

Comment: One commenter stated that, as proposed, if the low documentation application is from a lender who does not have preferred status, the maximum percent guarantee that the Agency will consider for that loan is 10 percentage points lower than for a full documentation application. The commenter stated that this change may have a negative effect in encouraging new lenders to participate in the program. According to the commenter, new lenders usually find the numerous requirements of the guarantee program to be intimidating and, with a reduction in guarantee, may consider the program too burdensome for participation. The commenter stated that the guarantee is attractive to lenders who may not be able to participate in certain projects, for a variety of reasons, even though they would be sound loans, and concluded that the reduction in guarantee will act as a deterrent in this situation.

Response: As noted in this preamble, the Agency has revised the rule to require all approved lenders to submit ''full documentation'' applications and, in addition, the Agency is removing the proposed rule provisions for ''low documentation'' applications. As a result, there is no longer a need for the accompanying 10% reduction in guarantee provision. The rule has been changed to reflect this.

Comment: One commenter stated that the guarantee percentages should be different when comparing the four programs because of the significance of infrastructure versus development; non-profit/municipality vs. for-profit. Another commenter recommended standardizing the guaranty percentages and suggested a consistent 80% regardless of loan size.

Response: With regard to the comment that the guarantee percentages should be different when comparing the four programs because of the significance of infrastructure versus development; non-profit/municipality versus for-profit, the Agency notes that the proposed rule did this and has been retained in the rule.

With regard to the comment recommending standardizing the guaranty percentages and suggesting a consistent 80% regardless of loan size, the Agency disagrees with the recommendation and suggestion. Because different projects have different risks, the Agency uses adjustments in guarantee percentage as a mechanism to address project risk. In the context of managing risk inherent in individual loan programs, including changes to a program subsidy scoring, the Agency, therefore, rejects the comment and the suggestion.

Fees (§ 5001.31(g))

Comment: One commenter expressed concern that the renewal fee can be changed annually, with no parameters to limit the fees or the fee changes. The commenter stated that lenders will see renewal fees or, at the very least, renewal fees with no parameters as an unmanageable risk, thus limiting their interest in program participation. The commenter also stated that the use of a renewal fee will eliminate participation by a number of lenders.

Response: The Agency has revised the rule to clarify that any renewal fee applied by a program will be that fee rate established at the time the loan is obligated and, thus, will not change over time (*see* § 5001.31(g)(2)). The Agency understands that imposition of a renewal fee can create a disincentive to participate. However, the rule states that the provision for a renewal fee is ''as applicable,'' meaning that it will be applied on a program-by-program basis. It does not mean that each program will necessarily charge a renewal fee.

Comment: One commenter stated that § 5001.31(g)(2) indicates the fee rate is established ''at the beginning of the loan''. The commenter stated that this is ambiguous because the rate is tied to the fiscal year of the obligation. The commenter suggested the use of the following language: ''Renewal fee. As applicable, the renewal fee is assessed annually, is based on a fixed fee rate established at the time the loan is obligated, and will be calculated on the unpaid guaranteed principal balance as of close of business on December 31 of each year. The fee will be billed to the lender and may be passed on to the borrower.''

Response: The Agency agrees with the commenter's suggested language, which replaces ''at the beginning of the loan'' with ''at the time the loan is obligated,'' and has made this revision to the rule.

Comment: One commenter requested that Guaranteed Community Facilities be codified within the regulations at 1% of the guaranteed portion of the facility and also that the regulations reflect and codify no annual service fee for Guaranteed Community Facilities. The commenter explained that Community Facilities by definition are non-profits and public bodies. The commenter also stated that increasing fees, particularly in an environment by which the Combined Program Platform may not delineate between the successes and challenges of the individual programs, may inhibit the long-term success of Guaranteed Community Facilities. The commenter added that by placing the determinant of fees within the **Federal Register**, particularly the success of the four programs is based on the blended default rate of for-profit and non-profit borrowers, the fees may become cost prohibitive to Community Facilities and to Waste and Waste Disposal Facilities.

Response: The Agency reserves the right to modify the fees assessed for any guaranteed loan program, including the Community Facility program, based on a variety of factors, including Agency loss experience and the effect of such losses on a program's subsidy rate. Therefore, the Agency rejects the commenter's request to codify the guarantee fee at 1% for the Community Facility guaranteed loan program. In addition, as noted in a previous response, the Agency may determine it is desirable to implement a renewal fee for the Community Facility guaranteed loan program (or any other program) and reserves the right to do so. Therefore, the Agency similarly rejects the commenter's suggestion to codify no annual service fee for Community Facilities.

Comment: One commenter stated that fees should be different when comparing these programs because of the significance of infrastructure vs. development; non-profit/municipality versus for-profit.

Response: When implementing these programs under the rule, the Agency will consider fees on a program-by-program basis. This includes determining what guarantee fee levels to use for each program and whether to require a renewal fee and, if so, what level. Because the Agency will make these determinations on a program-by-program basis, it will take into account the differences noted by the commenter.

Lender Fees (§ 5001.31(h))

Comment: One commenter stated that the proposed rule prohibits late payment charges from being covered by the Loan Note Guarantee and that the lender would be prohibited from adding such charges to the principal and interested due under any guaranteed note. The commenter expressed concern that a borrower would read this and think that they are not required to pay any late fees. The commenter explained that this is public information and, if read literally, could be construed to say that USDA loans cannot have that fee. The commenter suggested that this should be reworded and revised.

Response: The Agency agrees with that commenter that this paragraph needs to make clear that lenders can have late payment charges, but that the Agency still wants to prohibit late payment charges from being covered by the Loan Note Guarantee. Thus, the Agency has modified this paragraph to explicitly state that lenders may ''levy reasonable, routine, and customary charges and fees, including late payment fees.'' In addition, the Agency has added language to this paragraph to specifically state, in part, that late payment charges are not covered by the Loan Note Guarantee.

Comment: One commenter stated that § 5001.31(h) needs to include ''make whole'' calculations for fixed rate funding. The commenter stated that when the lender provides a fixed rate to the borrower, which helps to mitigate the borrower's interest rate risk, the lender becomes exposed to potential funding losses if the loan does not go full term of the period of the fixed interest rate. The commenter suggested that this cost should be included as a collectable fee or cost in the case of default.

Response: The Agency disagrees with the commenter and has not revised the rule as suggested. The situation being described by the commenter is a normal part of their business practice that the lender can account for in their terms and conditions with the borrower when arranging the loan. The Agency will guarantee loans with or without a prepayment clause. If an approved loan contains a prepayment clause, the prepayment fees are not covered by the Loan Note Guarantee.

Comment: One commenter stated that it is common practice for lenders to increase the interest rate on loans in default and suggested that the language in this section be expanded to state that late payment charges and additional interest expense associated with default interest rates will not be covered by the Loan Note Guarantee. Another commenter also suggested that this paragraph be expanded to mention default penalty interest charges as well as not being covered by the guarantee.

The first commenter also suggested removing the language prohibiting these charges from being added to the principal and interest due under any guaranteed note, and that the lender be required to thoroughly disclose charges and fees in appropriate loan documents. The commenter explained that these charges are common practice, and the agency should not prohibit the practice when the agency risk is mitigated by not covering them under the guarantee.

The commenter suggested the following language for the section: ''(h) Lender fees. The lender may levy reasonable, routine, and customary charges and fees for the guaranteed loan provided they are similar to those charged other applicants for the same type of loan for which a non-guaranteed borrower would be assessed. Late payment charges and additional interest expense associated with default interest rates will not be covered by the Loan Note Guarantee. The lender will thoroughly disclose charges and fees in appropriate loan documents.''

Response: The Agency agrees with the commenters that both default charges and additional interest expenses should not be covered by the Loan Note Guarantee and has modified this paragraph to reflect this. With regard to the suggestion that this paragraph also state that the ''lender will thoroughly disclose charges and fees in appropriate loan documents,'' the Agency does not believe this is necessary because such disclosures are required by current disclosure regulations and do not need to be restated in this rule.

Conditional Commitment (§ 5001.32)

Comment: Four commenters expressed varying levels of concern with the value of the Conditional Commitment and its relationship to the issuance of the Loan Note Guarantee and the closing and funding of the loan.

One commenter stated that commercial lending is a just-in-time business and the current six-working-day reservation of funds period is completely incompatible for this reality. This commenter recommended that Conditional Commitments be issued on a same-day-as-approved basis until funding is exhausted. The commenter then stated that the reservation of funds process should absolutely be eliminated, at the very least for Business and Industry guaranteed loans, and ideally for all other USDA guaranteed loans as well.

Two commenters expressed concern over the value of the Conditional Commitment and because of negative experiences over the last 12 months involving nearly $14 million over three loans (as detailed below) have implemented procedures whereby they will limit any future USDA loans to those where the Loan Note Guarantee is issued simultaneously with the closing and funding of the loan. The commenters point out that this will result in a dramatic decrease in the number of USDA loans that they will do in the future. One of the commenters stated that they would like to see the guarantee process handled the same way the SBA does to avoid these occurrences (see following paragraph) in the future.

One commenter provided detailed experience on three loans to support their comments as follows:

Over the past 12 months the Agency has denied issuing the Loan Note Guarantee on three loans totaling $13,700,000, which has been a serious matter for our company. In two of the loans, we relied on the Conditional Commitment issued by the Agency and disbursed loan proceeds in accordance with the Conditional Commitment. The disbursement period in each case was over several months. When the loans were fully disbursed, we requested the Loan Note Guarantee, but were denied because of an adverse change in the borrower. Although we, as the lender, did nothing wrong, the borrower's circumstances changed and we were denied the guarantee. In the third instance, we received a Conditional Commitment for a tug boat and two barges that were to be constructed in Oregon and Louisiana, respectively. We arranged for a local bank to provide the construction financing due to the long construction period and relied on the Conditional Commitment for the long term take out. Due to hurricane Katrina, the shipyards in Louisiana fell behind on their production and the delivery of the barges were delayed which caused the customer not meeting its projections for 2007, thus the Loan Note Guarantee was denied. This brought the credibility of Alaska Growth Capital into question with our local bank.

A fifth commenter suggested that Lenders should continue to be required to submit certifications listed in the current 7 CFR 3575.63(a)(1) through (14).

Response: With regard to the comment that commercial lending is a just-in-time business and the current six-working-day reservation of funds period is completely incompatible for this reality, the Agency points out that the Agency's reservation of funds is an internal fund administration policy that is not governed by the proposed rule. Thus, the Agency has not made any changes to the rule in response to this comment.

While the Agency understands the commenters concerns and frustrations with their recent experience, the Agency needs the ability to not issue the Loan Note Guarantee when there has been an adverse change. As stated in the Conditional Commitment: ''A Loan Note Guarantee will not be issued until the Lender certifies that there has been no adverse change in the Borrower's financial condition, nor any other adverse change in the Borrower's condition, for any reason, during the period of time from USDA's issuance of this Conditional Commitment to issuance of the Loan Note Guarantee regardless of the cause or causes of the change and whether the cause or causes of the change were within the Lender's or Borrower's control. The Lender's certification must address all adverse changes and be supported by financial statements of the borrower and its guarantors executed not more than 60 days before the time of certification. As used in this paragraph, the term ''Borrower'' includes any parent, affiliate, or subsidiary of the Borrower.''

Finally, with regard to the comment concerning the certifications found in 7 CFR 3575.63(a)(1) through (14), the Agency will identify required certifications in the handbook to this rule.

Conditions Precedent to Issuing Loan Note Guarantee (§ 5001.33)

Comment: One commenter stated that proposed § 5001.33(a) appropriately requires the lender to pay the guarantee fee.

Response: The Agency acknowledges the comment. This provision is now found in § 5001.34(b).

Comment: In reference to the requirement in proposed § 5001.33(b) that requires the lender to advise the Agency of plans to sell or assign any part of the loan, one commenter stated that it was unaware of any compelling reason to require this information in advance. The commenter stated that, if and when the Agency receives a lender's request to execute an Assignment Guarantee Agreement, the Agency acts on it.

Response: The Agency agrees with the commenter and this provision has been removed from the rule.

Comment: In reference to the requirement under proposed § 5001.33(c) to require the lender to certify that the prospective borrower or applicant has obtained all appropriate insurance, the commenter stated that, while this requirement is appropriate, it is not clear why this requirement was singled out.

Response: The Agency agrees with the commenter that it is unnecessary to single out this certification requirement. Instead, the handbook to this rule and the Conditional Commitment form will include the various lender certification requirements. Thus, this provision has been removed from the rule.

Comment: One commenter suggested a complete rewrite of proposed § 5001.33, including the lender certification, as follows:

''§ 5001.33 Conditions Precedent to Issuance of Loan Note Guarantee. The Loan Note Guarantee will not be issued

until the lender, including a preferred lender, has paid the guarantee fee, and certifies to the following.

''(a) All conditions of the Conditional Commitment have been met.

''(b) The lender's current classification of the loan is Special Mention or better under the Uniform Classification System as defined by Rural Development, with no consideration being given to the guarantee. The loan is classified __________.

''(c) The lender possesses and has analyzed the information specified in § 5001.12 and has identified in its credit evaluation all significant risks that could potentially jeopardize the timely repayment of the loan in full.

''(d) No major changes have been made in the lender's loan conditions and requirements since the issuance of the Conditional Commitment, unless such changes have been approved by the Agency in writing.

''(e) All truth-in-lending and equal credit opportunity requirements have been met.

''(f) The loan has been properly closed. The borrower has marketable title to all the collateral. The liens on the collateral have been perfected with the priority consistent with the requirements of the Conditional Commitment. No claims or liens of laborers, subcontractors, suppliers of machinery and equipment, or other parties have been or will be filed against the collateral and no suits are pending or threatened that would adversely affect the collateral when the security instruments are filed. Any exceptions must be thoroughly disclosed in the certification.

''(g) All loan proceeds have been disbursed for purposes and in amounts consistent with the Conditional Commitment and the application. A copy of the detailed loan settlement statement of the lender must be attached to support this certification. Appropriate lender controls were utilized to assure that all funds were properly disbursed, including funds for working capital.

''(h) All required personal, partnership, and corporate guarantees have been obtained.

''(i) All planned property acquisition has been completed. All development has been substantially completed in accordance with plans and specifications, and in conformance with applicable Federal, state, and local codes. The lender is to disclose any costs that exceeded the project costs identified in the Conditional Commitment and the application.

''(j) There has been neither any material adverse change in the borrower's financial condition nor any other material adverse change in the borrower, for any reason, during the period of time from the Agency's issuance of the Conditional Commitment to issuance of the Loan Note Guarantee regardless of the cause or causes of the change and whether or not the change or causes of the change were within the lender's or borrower's control. The lender must disclose any assumptions or reservations in the requirement and must disclose all adverse changes of the borrower, any parent, affiliate, or subsidiary of the borrower, and guarantors.

''(k) None of the lender's officers, directors, stockholders, or other owners (except stockholders in an institution that has normal stock share requirements for participation) has a substantial financial interest in the borrower and neither the borrower nor its officers, directors, stockholders, nor other owners has a substantial financial interest in the lender. If the borrower is a member of the board of directors or an officer of a Farm Credit System (FCS) institution that is the lender, the lender will certify that an FCS institution on the next highest level will independently process the loan request and act as the lender's agent in servicing the account.

''(l) Required hazard, flood, liability, worker compensation, and personal life insurance, when required, are in effect.

''(m) The Loan Agreement includes all measures identified in the Agency's environmental impact analysis for this proposal (measures with which the borrower must comply) for the purpose of avoiding or reducing adverse environmental impacts of the proposal's construction or operation.

''(n) If the lender is unable to provide any of this certification, provide a full explanation as a part of its certification.''

Response: The Agency appreciates the commenter's extensive suggestions on this section. In light of the commenter's suggestions and a reconsideration of the current programs' requirements, the Agency has decided to enumerate in the rule specific conditions to be met prior to the issuance of the Loan Note Guarantee. Many of these conditions are as suggested by the commenter. The disposition of each of the commenter's suggestions is discussed below.

Concerning the commenter's proposed § 5001.33(a), the Agency agrees with the concept, which was contained in proposed § 5001.33. In the rule, we have incorporated this in § 5001.33(a)(9). In addition, the Agency will provide further instruction in the handbook for the rule.

Concerning the commenter's proposed § 5001.33(b), the Agency, as noted in a response to an earlier comment, does not plan to incorporate in the rule the current classification of the loan as Special Mention or better. Therefore, the Agency is not incorporating this suggestion in the rule.

Concerning the commenter's proposed § 5001.33(c), the lender will have conducted their lender's analysis, which is required under § 5001.12, and will have submitted it to the Agency. The lender will, thus, already have in their possession this analysis. Therefore, the Agency does not believe it is necessary to include this suggestion as a requirement for the issuance of the Loan Note Guarantee.

Concerning the commenter's proposed § 5001.33(d) that no major changes have been made in the lender's loan conditions and requirements since the issuance of the Conditional Commitment, unless such changes have been approved by the Agency, the Agency agrees that this needs to be addressed and has included it in the rule (§ 5001.33(a)(1)).

Concerning the commenter's proposed § 5001.33(e) that all truth-in-lending and equal credit opportunity requirements have been met, even though the rule requires that lenders comply with all Federal law, which applies to both truth-in-lending and to equal credit opportunity, the Agency believes that stating this as part of the requirements for the issuance of the Loan Note Guarantee is useful (§ 5001.33(a)(4)).

Concerning the commenter's proposed § 5001.33(f), the Agency has included the provisions currently found in the Business and Industry guaranteed loan program, which are very similar to what the commenter recommended. The Agency did not accept the commenter's suggestion that the ''borrower has marketable title to all the collateral,'' because that language is not as effective in protecting the security as the current Business and Industry language. The Agency also did not accept the commenter's suggested language ''Any exceptions must be thoroughly disclosed in the certification'' because the Agency will not allow for any exceptions.

Concerning the commenter's proposed paragraphs (g) and (j) through (m), the Agency notes that these are the same as currently found in the Business and Industry guaranteed loan rule and the Agency has included these in the rule.

Concerning the commenter's proposed § 5001.33(h), the Agency has incorporated the corresponding provision found in the current Business and Industry guaranteed loan regulation, which is essentially the same as suggested by the commenter.

Concerning the commenter's proposed § 5001.33(i), the Agency has incorporated the corresponding provision found in the current Business and Industry guaranteed loan regulation, which is similar to what the commenter suggested except for the treatment of costs. The commenter suggested that the lender be required to disclose ''any costs that exceeded the project costs identified in the Conditional Commitment and the application,'' which is different from the current Business and Industry guaranteed loan rule which states ''costs have not exceeded the amount approved by the lender and the Agency.'' The Agency rejected the commenter's suggested alternative treatment of costs because this would notify the Agency after such costs were incurred and the Agency wants to know conditions before such excess costs are incurred.

Concerning the commenter's proposed § 5001.33(n), the Agency has incorporated the intent of the lender's suggested language in § 5001.33(b).

Comment: One commenter stated that the proposed rule is nearly silent on whether or not USDA will guarantee loans prior to the completion of construction—aside from prohibiting it for Section 9006 guarantees at § 5001.104(f)(1). The commenters stated that construction-related risks represent a major exposure to any guaranteed loan program, and currently the acceptance of such risks under the guarantee is discouraged. For example, 7 CFR § 4279.156(b) sets forth a set of practices expected to offset this risk. The commenter recommended that, at the very least, these should be incorporated into the new regulation.

The commenter also recommended that this should be accompanied by a policy of dropping the guaranteed loan percentage by 10 points if the guarantee will be issued prior to the completion of development work and a provision could then be included to increase the percent of guarantee by 10 points after the construction is successfully completed and the construction risk is over.

Response: The Agency has considered this issue with regard to each of the guaranteed loan programs included in the rule. The Agency has determined that it will guarantee loans prior to construction being completed only for the Business and Industry guaranteed loan program. The Agency will not guarantee loans prior to construction being complete for Community Facilities, Water and Waste Disposal Facilities, and Rural Energy for America programs. The Agency will also consider reducing the loan guarantee by 10 percentage points for Business and Industry loans, as discussed in the following paragraph.

For projects other than turnkey operations where the Loan Note Guarantee will be issued at the time of loan closing, there are added risks to the Agency. In considering the conditions under which the Agency will guarantee Business and Industry loans prior to construction being completed, the Agency will consider, during the review process, the added risk associated with issuing the Loan Note Guarantee prior to the substantial completion of the project. When negotiating the percent of guarantee with the lender, these risks will be considered in conjunction with the credit risks and the lender's experience in financing the type of project. The percent of guarantee will be reduced by a minimum of 10% where the Agency determines that this is warranted.

Comment: One commenter suggested adding a new paragraph to this section as follows: ''The lender has certified that the borrower has secured any and all necessary environmental permits and all Agency recommended mitigation measures have been adopted and implemented appropriate to the proposal.''

Response: The rule covers environmental requirements elsewhere in the regulation and the Agency does not see the need to repeat, or to move, them here. Therefore, the Agency has not implemented the commenter's suggestion.

Issuance of the Guarantee (§ 5001.34)

Comment: In reference to the proposed § 5001.34(a) requiring the lender's certification be provided at loan closing, one commenter stated that the lender should not be asked to provide its certification until it is requesting the guarantee because the borrower or lender may still be working out some agency imposed conditions, and that is okay.

Response: The Agency agrees with the commenter's suggestion that the lender's certification be submitted at the time the lender requests the guarantee. The Agency has incorporated this suggestion in the rule (see § 5001.34(b)).

Comment: In reference to the proposed requirement that the guarantee fee be paid at loan closing in proposed § 5001.34(a), one commenter stated the guarantee fee should be paid when the Loan Note Guarantee is being issued, not at loan closing. According to the commenter, if the fee is paid early, and then the borrower/lender cannot meet all conditions to issue the guarantee, the fee would/may have to be refunded, and § 5001.31(g) says the fees are not refundable.

Response: The Agency agrees with the commenter's suggestion that the guarantee fee not be paid at loan closing. The rule requires the guarantee fee to be paid when the lender requests the Loan Note Guarantee (see § 5001.34(b)).

Comment: One commenter referred to the portion of the last sentence in proposed § 5001.36(a) that reads ''except that a change in the legal entity may be approved when the borrower is replaced with substantially the same individuals or officers with the same interest as originally approved'' and asked if this is referring to ownership interest and if it is, then revise the language to say so.

Another commenter recommended deleting ''with the same interest'' in this same portion of the last sentence. According to the commenter, keeping ''with the same interest'' could require undue hardship on Agency personnel to process cancellations and reapplications, while not including it should still result in satisfactory protection of the interest of the Agency.

Response: With regard to the commenter's request for clarification on the ''exception'' language, the Agency agrees that as proposed this language was unclear as to its meaning. In the rule, the Agency has deleted this ''exception'' language and Agency approval is required for a substitution of borrower(s) or change in the form of legal entity. Note that the deletion of the ''exception'' clause removes the ''with the same interest'' phrase on which the second commenter expressed concern. The Agency will provide guidance in a handbook to address such issues as raised by both commenters.

Sale or Assignment of Guaranteed Loan (§ 5001.37)

Comment: Two commenters suggested that the Agency add a new section to incorporate RD AN 4240 to generate an agency form and certificate for lenders selling their excess servicing fee to a third party. The commenters suggested patterning this form after SBA's Confirmation of Originators Fee, but that USDA's form should be between the selling lender and the purchasing third party because the Agency has no centralized servicing agent like SBA. According to the commenters, a standardized form should make secondary market sales of servicing fees uniform, encouraging more investors thereby generating lower rates for borrowers.

Response: Form RD 5001–6, Agency Assignment Guarantee Agreement, has a provision for servicing fees. Therefore, the rule does not need to have a section added as suggested by the commenters.

Comment: One commenter noted that proposed § 5001.37(a)(2) requires the lender to retain sufficient interest to perform its duties under this part and asked ''How much interest is sufficient?'' and ''How will this be enforced?''

Response: In response to this and comments made on proposed § 5001.37(a)(6), the Agency has rewritten § 5001.37(a)(2) to require that all lenders maintain a minimum 5% exposure to all loans. The revised paragraph no longer refers to ''retain sufficient interest.''

Comment: Nine commenters stated that all lenders should be required to have a minimum of 5% exposure on any guaranteed loan and recommended removal of the provision allowing preferred lenders not to have any exposure on a loan found in proposed § 5001.37(a)(6). The commenters gave several reasons for this recommendation.

Two commenters stated that allowing any lender to not have any exposure to the loan they are servicing will complicate servicing on a defaulted loan. According to the commenter, based on the commenter's experience, a lender will not want to spend the money to liquidate a loan in which they have no financial interest. The commenter also stated that there is no advantage to the business in allowing the lender to participate out the unguaranteed portion since there is no participant that will provide the types of rates and terms the secondary market makes available for the guaranteed portion.

One commenter stated that if preferred lenders are not required to retain any portion of the loan, there is little incentive for them to service the loan properly.

One commenter stated that the provision to sell 100% of the loan appears to ''cater to the nontraditional lender who is who is undercapitalized and probably not the best partner to have with a guaranteed loan portfolio, because most banks retain the entire unguaranteed portion of the loan anyway. The commenter suggested that this change should not be allowed to occur, but if it does go forward, the commenter suggested clarification concerning who can sell 100% of the loan.

Two commenters stated that all lenders should be required to retain 5% of the entire loan, which must be an unguaranteed portion because this keeps the lenders at risk. However, lenders in good standing should be able to securitize 95% of their loans.

One commenter stated that the provision to allow selling of 100% of the loan is not a prudent provision because it contravenes the fundamental guaranteed principle of share risk. Similarly, another commenter stated that this effectively eliminates any exposure on the part of the preferred lender and all lenders should be required to retain a minimum of 5% of the loan from the unguaranteed portion so the originating lender will share in the loan's risk.

Finally, one commenter was concerned that this provision, in conjunction with the low documentation application process, could lead to poor lending practices because the preferred lender would not have to risk its own capital on the project. According to the commenter, this could in turn lead to an increase in defaulted projects. The commenter further stated that such ''no risk'' lenders would have no incentive to monitor or service loans, a function that is vital to the success of the four guaranteed loan programs. The commenter expressed specific concern about the potential effect on a default on a project by a municipality, stating that the municipal finance industry is ultra conservative and a default by a municipality on a project has not only a detrimental effect on that entity but can cause a ripple effect throughout a state or region, resulting in higher borrowing costs for public entities.

Response: The Agency agrees with the commenters that all lenders should be required to maintain a minimum 5% exposure and that the proposed provision to allow preferred lenders to have no exposure on a loan is unnecessary and could lead to increased risk. Therefore, the rule requires all lenders to maintain at least a 5% interest in all loans.

Comment: One commenter requested that the last sentence of proposed § 5001.37(a)(6), which reads ''Lenders may sell the remaining amount of the un-retained amount of the loan [un-guaranteed portion], only through participation'' be changed. According to the commenter, this language is acceptable for loans but incorrect for bonds. Bonds would typically be sold, whether guaranteed or un-guaranteed portions. The un-guaranteed portions would be clearly defined as not being guaranteed.

Response: While the Agency agrees with the commenter that the phrase ''only through participation'' is appropriate for loans and not for bonds, making this and other changes to the rule, this paragraph is no longer required. Thus, the Agency has removed this paragraph from the rule.

Comment: Two commenters stated that the first sentence in proposed § 5001.37(b), which reads ''The lender's servicing fee will stop when the Agency purchases the guaranteed loan portion of the loan from the secondary market,'' is misleading because the lender's servicing fee actually stops at the time of the last principal payment by the borrower. This is true because, according to the Lender's Agreement, the lender cannot charge the Agency a servicing fee, and when the Agency purchases the guaranteed portion from the holder it assumes the principal and accrued interest which cannot be charged a servicing fee. For instance, if the last principal payment by the borrower was July 1st and the Agency repurchased the guaranteed portion from the holder on October 1st, there is 3 months interest included that the lender cannot charge a servicing fee on because the Agency is the holder. So the servicing fee actually was stopped on July 1st not October 1st.

Response: The commenters are correct in pointing out that the first sentence is misleading for the reasons cited by the commenters. Therefore, the Agency has removed this sentence from the rule. The commenters are also correct in pointing out that the lender cannot charge the Agency for servicing fees. The Agency has revised and renamed this paragraph to address provisions associated with servicing fees, which includes, in part, this prohibition on charging servicing fees to the Agency. In addition, the revised paragraph states that such fees are not covered under the guarantee.

Comment: Three commenters were concerned about the second part of the sentence in proposed § 5001.37(b), which reads ''all loan payments and collateral proceeds received will be applied first to the guaranteed loan.''

One commenter stated that this language is not clear and asked what happens when the guaranteed loan is in a junior position.

One commenter stated that it is the word ''first'' that is confusing, asking ''Aren't all loan payments and collateral proceeds (net of liquidation costs) supposed to be applied against the guaranteed loan until it is paid in full?'' This commenter then referred to comments submitted on § 5001.30(b)(1) concerning the payment of the guaranteed portion of the loan being paid first and given preference and priority over the unguaranteed portion.

One commenter recommended that this language be deleted because it will prevent most lenders and buyers of loans from participating in the guaranteed loan program. The commenter recommended instead the following language, which has been used in the past: Will be applied first to the guaranteed loan and, when applied to the guaranteed loan, will be applied on a pro rata basis.

Response: The Agency agrees with the commenters that the proposed language was not clear with regard to guaranteed loans in a junior position and the concern over the payment of loans. Therefore, the Agency has modified this provision (see § 5001.37(c)(3)) to state that all loan payments and collateral proceeds received will be applied to the guaranteed and unguaranteed portions of the loan on a pro rata basis.

Community Facilities Program (§ 5001.101)

Comment: One commenter requested that Community Facilities be removed from the combined platform. This commenter stated that underwriting and other aspects of lending to for-profit vs. non-profit organizations is very different, and merging the programs invites confusion in interpretation and in application of the programs.

Response: The Agency has intentionally developed a unified platform for the implementation of these guaranteed loan programs and for the incorporation of new authorized guaranteed loan programs in the future. The Agency understands that this results in the inclusion of guaranteed loan programs that have different characteristics, as indicated by the commenter. By using subpart A to identify common provisions and subpart B for program-specific provisions, the rule obtains, in part, an efficiency in the implementation of all guaranteed loan programs and minimizes the potential for confusion. Therefore, the Agency has retained the Community Facilities guaranteed loan program in the proposed rule.

Project Eligibility (§ 5001.101(a))

Comment: One commenter noted that wherever possible, the Agency should allow for refinancing of the current debt structure, up to 100% of the funds represented by the current request, and requested that the 50% limitation for refinance of existing indebtedness be restated as follows:

''(vi) Refinancing debts incurred by, or on behalf of, a community when all of the following conditions exist:

(A) The total debt service payments after refinance are less than the current total service payments without an extension of the maturity date,

(B) The debts were originally incurred for the facility or service being financed or any part thereof (such as interim financing, construction expenses, etc.), and

(C) The proposed refinance represents a legitimate transaction. Care must be taken to ensure the refinance is not coupled with a conversion from for-profit to non-profit with a management contract provided by the previous For-Profit owners or companies/subsidiary under control of the previous for-profit owners.''

Response: The Agency's experience with making guaranteed loans for community facilities is that there needs to be a balance between providing loan guarantees to new rural services and refinancing existing loans. The Agency does not believe that allowing 100% refinancing is consistent with the goal of providing new rural services. Limiting refinancing to 50% represents, based on Agency experience, the appropriate balance. Therefore, the Agency has not modified the provisions concerning the refinancing of the minority portion of the debt. The Agency notes that it has revised the refinancing requirements to include the commenter's second suggestion (i.e., debts incurred for the facility or service being financed or any part thereof (such as interim financing, construction expenses, etc.)).

Comment: One commenter stated that if hydroelectric generating facilities and natural gas facilities are eligible, then other power generating facilities should be included, especially if it is an alternative and/or clean/energy/green energy project.

Response: Other power generating facilities are eligible for a Community Facilities guaranteed loan if they are part of an improvement to an already eligible community facility. In such instances, the Agency plans to continue to fund alternative energy projects. The rule does not need to be revised in order for the Agency to continue to fund such projects. Therefore, no changes have been made to the rule in response to this comment.

Comment: One commenter requested that the criteria for leased space (proposed § 5001.101(a)(3)) be expanded to represent 75% utilization of the facility for benefit of community services based on shared/common space measured as a percentage of total square feet floor space, and shared/common time usage of the space measured as a percentage of annual usage.

Response: The suggestion by the commenter is essentially the same as what the rule requires, but would add to it the calculation of the ''shared/common time usage of space measured as a percentage of annual usage.'' To implement the commenter's suggestion would require the keeping of records of how often each space is used. The Agency does not have the administrative resources necessary to verify and monitor time usage. Therefore, the Agency does not believe that this suggestion is practical or necessary and has retained the provision in the rule as proposed.

Comment: Two commenters addressed the issue of demonstration of community support (proposed § 5001.101(a)(5)). Both commenters noted that the rule gives the option to either satisfy the cash equity requirement or demonstrate community support. One commenter believed that a community facility project should always demonstrate significant community support. Another commenter recommended revising the section as follows: ''Section 5001.101 (a)(5)(i)—Evidence of tangible community support such as community fund raising, assignments of tax revenues, or grants from other organizations and when required by § 5001.101 (a)(5)(ii) a certificate of support.''

Response: With regard to the comment that community facility projects should always demonstrate significant community support, the Agency believes that there is no increase in risk if a community facility project could demonstrate the equivalent financial metric (at proposal, this was cash equity; in the rule, it is debt-to-tangible net worth ratio). Therefore, the Agency believes that it is still reasonable to allow the option to demonstrate either.

With regard to the comment suggesting to revise § 5001.101(a)(6)(i), which reads ''Evidence of community support in the form of a certification of support for each project or facility from any affected local government body is required,'' the Agency believes that requiring evidence of ''tangible'' community support would eliminate too many viable and worthwhile projects. Therefore, the Agency has not accepted the commenter's suggested revision and has retained this paragraph as proposed in the rule.

Unauthorized Projects and Purposes (§ 5001.101(b))

Comment: One commenter stated that the proposed definition of conflict of interest limits the award of a contract to another party only when they will retain an interest in the borrower; the language would not include a member of the board of directors awarding a contract during the origination phase and then withdrawing from the board of directors. According to the commenter that, while the definition actually indicates that it includes but is not limited to, it may also provide a supportable defense when the person clearly intends to withdraw prior to contract ratification. Therefore, the commenter proposed amending the proposed regulation as follows: ''§ 5001.101(b)(7) Any project where an individual, or membership of another organization sponsors the creation of a nonprofit organization with the intent to control negotiations for employment or contracts that provide financial benefit to the sponsoring organization, affiliate organization, or a subsidiary organization of the sponsoring individuals or organization.''

Response: The Agency agrees with the concern raised by the commenter and the rule addresses the commenter's concern. Rather than creating a new paragraph as suggested by the commenter, the rule relies simply on the concept that any project that creates a conflict of interest or an appearance of a conflict of interest is prohibited. The rule no longer defines ''conflicts of interest.'' Instead, the Agency will rely on guidance in the handbook to the rule to address conflicts of interest, including the situation posed by the commenter.

Borrower Eligibility (§ 5001.101(c))

Comment: One commenter stated that the proposed rule would allow lenders to make loans to for-profit borrowers without restrictions to distribution of profit. The commenter made three recommendations to remedy this:

(1) Require in the definition of an essential community facility that all community facilities be operated on a nonprofit basis;

(2) Require that eligible borrowers for an essential community facility be a public body or nonprofit corporation; and

(3) Require that all essential community facilities operate as though they were nonprofit entities.

Response: The Agency has revised the borrower eligibility requirements to focus on those borrowers that are the intended clients for the Community Facilities guaranteed loan program—public bodies, not-for-profit entities, and Indian tribes. This revision accommodates the commenter's second suggestion and main concern. The Agency does not believe it is necessary to implement the other two suggestions in order to target the Community Facilities program to its intended clients.

Comment: Two commenters recommended deleting the ''credit not available elsewhere'' requirement (proposed § 5001.101(c)(3)). One commenter stated that this is the one area that should follow the current Agency Guarantee Business and Industry procedure and not require this documentation from the lender or Agency determination. The other commenter requested that the requirement for Community Facilities to show proof of inability to obtain credit at reasonable pricing, terms, and conditions be deleted. According to this commenter, the requirement may be appropriate for Business and Industry (for-profit ventures), but is not relevant to non-profit and public organizations serviced through Community Facilities.

Response: The Agency cannot remove this provision from the Community facility program because it is a requirement under the program's authorizing statute.

Comment: One commenter stated that the credit not available elsewhere requirement conflicts with § 5001.16.

Response: The Agency disagrees with the commenter that there is a conflict between these two provisions. A borrower may be credit worthy as required under § 5001.16, but this does not mean that the borrower is able to receive a loan at reasonable rates and terms, which is the relevant test for ''credit not available elsewhere.''

Comment: One commenter requested more written examples of eligible community facilities, including rural health clinics, first responders, immediate care centers, assisted living facilities, nursing homes, roads, toll roads, bridges, ports, airports, charter schools, day care, YMCA, YWCA, Girl Scouts, Boy Scouts, university/college/technical schools for education/multipurpose, and community student housing.

Response: The list provided in the proposed rule was not intended to be an exhaustive list; other examples will be provided in the handbook to the rule. The organizations listed in the referenced paragraph do not meet the normal requirements of an eligible borrower. Therefore, the Agency has listed these four organizations separately to ensure that they continue to be eligible for Community Facilities guaranteed loans.

Additional Application Documentation Provisions (§ 5001.101(d))

Comment: One commenter stated that guidance should be provided that explains when a Feasibility Study is necessary (e.g., in a Staff instruction or Handbook).

Response: The Agency agrees with the commenter and will provide additional guidance and instruction on when a feasibility study is necessary within the handbook to the rule.

Additional Guarantee- and Loan-Related Requirements (§ 5001.101(h)) (Proposed § 5001.101(e))

Comment: One commenter requested that no limit be placed on Guaranteed Community Facilities, and that the State and Program Directors be allowed to administer funding for the greatest benefit rather than imposing a regulatory limit. According to the commenter, while the premise for the limit is credible, under the current economic environment Rural Development encourages joint efforts by rural communities to consolidate services, when reasonable and when services will not be compromised. In addition, county-wide or joint community projects may well exceed $50 million and may be fully justified.

Response: The Agency has not revised the rule as requested by this commenter. The funding limit allows the Agency to better diversify its portfolio, improve risk management, and provide for a greater geographic distribution of funds.

Comment: Two commenters expressed concern over the proposed parity lien requirements. One commenter recommended deleting the parity lien requirements, because this is an undue requirement for lenders since they will be harder to obtain approval from lender boards, especially considering non-profit status in addition to the other high risk factors. The other commenter stated that this requirement has hurt the promotion of the guaranteed CF loan program, and recommended that the loan approval officer be given the option to approve a Guaranteed CF in first lien position.

Response: The Agency disagrees with the recommendation to delete or modify this requirement, which implements current Agency policy, because to do so would reduce lender risk, which defeats the concept of shared risk, one of the goals of the new platform. In addition, such changes would have a negative effect on program costs and reduce the number of viable projects that the Agency can finance.

Water and Waste Disposal Facilities (§ 5001.102) Borrower Eligibility (§ 5001.102(c))

Comment: One commenter stated that the credit not available elsewhere requirement conflicts with § 5001.16.

Response: As noted in a previous response, the Agency disagrees with the commenter that there is a conflict between these two provisions. A borrower may be credit worthy as required under § 5001.16, but this does not mean that the borrower is able to receive a loan with reasonable rates and terms, which is the relevant test for ''credit not available elsewhere.''

Business and Industry (§ 5001.103)

Comment: One commenter suggested combining the cooperative stock requirements into one section, rather than mixing them in with general requirements in several sections.

Response: The Agency appreciates the commenter's suggestion, but has not revised the rule as suggested. Instead, the Agency will provide a section specific to requirements for cooperative stocks in the handbook for the rule.

Project Eligibility (§ 5001.103(b)) (Proposed § 5001.103(a))

Comment: Two commenters noted that the proposed rule does not address the eligibility of mixed use commercial buildings projects, which consist of a combination of commercial and residential use. One of the commenters stated that such projects should be expressly authorized given their importance in rural development.

Response: The Agency currently provides guaranteed loans under the Business and Industry program to such mixed-use projects and agrees that such projects should be eligible. Therefore, the Agency has specifically included in the rule a provision identifying such projects as being eligible, provided the residential real estate portion is not included in the loan (see § 5001.103(b)(xviii)).

Comment: Two commenters noted that currently Business and Industry assistance cannot be used to guarantee letters of credit and suggested that a Business and Industry guarantee for Industrial Development Bonds could be a useful tool and should be expressly permitted.

Response: Under the proposed rule, Industrial Development (ID) Bonds were not precluded, either by statute or by the rule, from the Agency guaranteeing such bonds. However, there may be tax implications affecting the tax free status of an ID bond when it is part of a loan guaranteed by the Agency. Regardless, the Agency does not believe it is necessary to add a specific provision to the rule addressing ID bonds.

Comment: Two commenters noted that the proposed rule no longer states that agricultural production guaranteed loans will be limited to the lesser of $1 million or 50% of the guaranteed loan when a value-added enterprise is associated with it. One commenter stated that many would argue that there is a need for guarantees on larger agricultural enterprises. The other commenter asked why this is being expanded.

Another commenter said that the proposed rule sets up a confusing new standard for agricultural operations, where the proposed rule would vaguely allow loans for ''agricultural production, with advance written approval from the Agency.'' This commenter asked what the criteria would be for the Agency to provide such advance written approval, and recommended retaining the current workable Business and Industry rules (§ 4279.113(h)).

Response: The Agency agrees with the commenters' observation that the rule would no longer impose a limit on guaranteed loans for agricultural production, thereby expanding the number of agricultural operations for which loans could be guaranteed. Instead of imposing the current regulations' monetary requirements for determining whether an agricultural project would be eligible, the Agency elected a more flexible approach of requiring prior written approval from the Agency. The criteria that the Agency will use in determining whether to issue that approval or not will be provided in the handbook to the rule.

Comment: Two commenters recommended eliminating refinancing as an eligible purpose. One commenter offered examples of the types of obligations that are often refinanced under the current regulations and stated that the proposed regulation would eliminate a substantial portion of the transactions currently undertaken in the Business and Industry program. It would shift the program to focus more on startup companies which would create direct competition with the SBA. In addition, the proposed regulations would have a discouraging effect on lenders, further reducing the number who are willing to deal with many of the issues that currently exist in the program(s). Examples included: Leases or other debt instruments that are often very expensive and onerous, Bank loans that are often ''over collateralized'' or improperly collateralized and have tied the borrowers' hands for expansion or recapitalization, Bank loans that are ''maxed out'' due to lending limitations of the local lender(s) which are preventing the borrower from growing, banking relationships which have become restrictive to the borrower and are preventing the company from growing due to an ''honest'' disagreement over risk, and planning for the sale of the business through an orderly transition of the business and assumption of the debt over a scheduled period of time.

One commenter noted that providing the lender with a guarantee on other existing lender debt has been a highly desired loan purpose under the program. It is a good marketing tool for the program and has been the primary loan purpose for the commenter's involvement with existing businesses.

One commenter also stated that a definition of ''refinance'' would be helpful in responding to this proposed regulation.

Response: The Agency has revised this provision to more closely follow the provision in the existing regulations and has restricted the proposed minority portion requirement to same lender debt refinancing (see response to the following comment).

Comment: Nine commenters expressed concern regarding the requirement limiting refinancing to 50% or less of the loan funds. One commenter noted that refinancing is a large part of the program, and as long as the refinancing helps the cash flow of the company and keeps the company profitable, it should be eligible.

One commenter stated that, if this requirement stands, it would eliminate this lender's ability to offer a valuable service that the lender has found to be a successful use of this program. This commenter requested that some qualifying language be added to allow loans such as monies for remodeling and refurbishment and for removal of looming balloon payments, to continue to be possible. Two commenters said that limiting refinancing of any debt to a minority portion of the loan will adversely affect many businesses attempting to restructure debt that was inappropriate to begin with. These commenters added that the commercial loan aspect of the Business and Industry Guarantee should not put unnecessary restrictions that can be better served with proper credit underwriting by the Agency.

One commenter stated that if refinancing of other loans would be limited to a minority portion of the guaranteed loan, debt refinancing that provides an improvement in cash flow or that allows a lender to obtain a needed lien position when financing a new project would disrupt the business/banking relationship of the borrower and lender. One commenter said that limiting refinancing to less than 50% of the total project could disqualify some important transactions and that refinancing is frequently an integral part of a company's overall financial planning. Imposing this rule would remove a great deal of flexibility from the program, thereby diminishing its desirability for lenders and borrowers alike.

One commenter recommended continuing with the existing program and not limiting refinancing to 50% of loan funds, as this new arbitrary limit does not fit the real world of business and finance. The existing program is beneficial to businesses looking to expand and gives the lenders the ability to properly structure and secure debt for companies. Another commenter noted that current regulations allow the Agency to support projects to improve the cash flow and viability of some borrowers, enabling them to grow and provide benefit to their communities. Limiting this opportunity does not reduce Agency risk, but does reduce the program's potential effectiveness. One commenter stated that this proposed regulation limiting the refinancing should not even exist, as it limits a company's ability to refinance existing debts over better terms.

Response: The Agency agrees with the commenters that the 50% limit would unnecessarily limit refinancing as an eligible purpose. Therefore, the Agency has eliminated this provision with the exception for same lender debt refinancing. In the rule, same lender debt refinancing must be less than 50% of the new loan amount unless the amount of loan to be refinanced is already Federally guaranteed. If the amount of the loan to be refinanced is Federally guaranteed, then the 50% requirement does not apply.

Comment: Fourteen commenters recommended continuing with the current policy for refinancing.

One commenter noted the change from the old regulations and simply recommended using the policy in the old regulation. Three commenters said that USDA should continue with its current policy and delete the proposed change. According to these commenters, the proposed change will adversely impact many other good credit worthy rural businesses that need to refinance existing loans to improve cash flow to make their rural business more viable or that need to refinance loans that are ballooning with a loan that makes their rural business more viable.

Another commenter stated that current policy should be continued and that refinancing debt obtained during business startup is less risky and is often necessary to improve cash flow and allow a lender to obtain a senior lien position.

One commenter requested that the existing rule be retained and stated that rural America does not need to have more restrictions placed on it for financing. One commenter stated that this is the single-most detrimental provision to the Business and Industry program in the proposed rule. This commenter recommended continuing with the current Business and Industry regulations, and said that the proposed change is arbitrary and unhelpful.

One commenter stated the this change would severely impact the volume of loans that would be guaranteed by the Business and Industry program and said that current Business and Industry regulations permitting debt refinancing should be continued. According to this commenter, the ability to refinance debt is crucial when providing financial assistance to business, and this is one of the selling points of the Business and Industry programs. The commenter also noted that refinancing usually always strengthens a credit.

One commenter recommended retaining the current language and noted that limiting refinancing will eliminate a major draw for the Business and Industry program. To take this away, according to the commenter, will greatly reduce the demand for the Business and Industry guarantee program and remove a great tool from the lenders involved with the program. Two commenters recommended keeping the existing rules for refinancing in place or lose lenders.

One commenter stated that this section is confusing with regard to financing debt. The commenter pointed out that the proposed rule states that refinancing is an eligible use, but then specifies that any refinancing, except for Agency Direct loans, must be a minority portion of the loan. According to the commenter, this change would be detrimental to the Business and Industry program, as many loans are for refinancing. This commenter sees no reason to change the program from its current intent.

One commenter recommended making no changes to the old rule for refinancing. The commenter noted that by refinancing to a fixed rate product, borrowers are better served and provide a more sustained outlook for job retention and possibly job creation. Therefore, according to the commenter, a refinance into a fixed interest rate is a method for business owners to predict their expenses and make sound decisions for growth.

After referring to what the current program allows, one commenter suggested that the Agency expand this section to allow refinancing of existing Agency debt; excluding Agency direct loans, as long as the loan has been current for 12 months with no extensions, loan rewrites or debt forgiveness by the lender and the Agency. The commenter stated that lender debt should be allowed to be refinanced so long as the lender debt is less than 50% of Agency debt, excluding the unguaranteed portion of the guaranteed loan.

Response: As noted in the previous response, the Agency has revised the provision for refinancing in the rule. The rule incorporates essentially the same provisions found in the current regulations.

Comment: Two commenters addressed the issue of flexibility and refinancing. One commenter stated that the restriction should be relaxed since it prevents lenders who have not previously used the Business and Industry program from offering the benefits of the Business and Industry guarantee to its current portfolio of business borrowers. This commenter recommended allowing any and all Business and Industry guaranteed debt refinancing of loans already in a lender's portfolio, as long as they meet the following four criteria:

(a) There will be at least a 20% reduction in debt service cost on the debt after the refinance,

(b) The portfolio debt being refinanced has been in the lender's portfolio for at least 12 months,

(c) The portfolio debt being refinanced has been current (not due to deferral or other restructuring) for at least the past 12 months, and

(d) The portfolio debt being refinanced is classified at a level better than ''Doubtful''.

The other commenter stated that the proposed rule would severely limit Business and Industry debt refinancing, and said that more flexibility regarding debt refinancing would be beneficial to the borrower and is important to ensure the effectiveness of this program.

Response: As noted in previous responses, the Agency has revised this provision in the rule. In the rule, refinancing is allowed when the Agency determines that ''the project is viable and equal or better rates or terms are offered.'' The Agency believes that the revised provision allows the Agency flexibility in assessing each individual refinancing and to consider the risk for each proposed refinancing and that it is unnecessary to incorporate the prescriptive conditions suggested by the commenter.

Comment: One commenter recommended allowing refinancing of the entire debt with another lender to be an eligible purpose and stated that this paragraph may not allow this. The commenter then requested clarification.

Response: The revised provision on refinancing in the rule allows the refinancing of any loan under certain conditions, except that same lender debt refinancing is limited to 50% unless the amount of the loan to be refinanced is already Federally guaranteed. The rule allows the refinancing of the entire debt with another lender provided the project is viable and equal or better terms are offered. The Agency does not believe it is necessary or appropriate to include this specific type of refinancing in the rule.

Comment: One commenter noted that the proposed provision for fees and packagers as an eligible purpose seems to contradict § 5001.7(h) and suggested that packager or broker fees may be considered ''professional services.''

Response: The Agency understands why the commenter thinks that allowing professional service fees appears to contradict the general prohibition in subpart A for packager and broker fees. Subpart A identifies packager fees and broker fees as ineligible, while subpart B further provides for what is eligible; in this case, professional service fees are eligible. Thus, the proper reading of the rule is that professional service fees are eligible, except for packager and broker fees. The Agency has revised subpart B to indicate clearly that where professional service fees are eligible costs, they do not include packager or broker fees.

Comment: One commenter identified a contradiction between proposed § 5001.103(a)(1)(xiii), which allows loans to tourist and recreational businesses, and § 5001.7 which prohibits loans to golf courses, racetracks, water parks, ski slopes, and similar recreational facilities, and recommended that this contradiction should be clarified.

Response: In response to another comment, the Agency has limited the specific paragraph reference in § 5001.7 to racetracks and other similar recreational facilities. Nevertheless, as noted in the previous response, subpart B lists those projects that are eligible for a Business and Industry guaranteed loan, while the recreational projects listed in subpart A will never be eligible for a Business and Industry guaranteed loan. If a recreational project is not listed in subpart A, then it would be eligible under subpart B for a Business and Industry guaranteed loan.

Comment: Two commenters asked for clarification as to what the ''certain restrictions'' are for housing development sites.

Response: The Agency will provide guidance on the restrictions in the handbook for the rule. In the rule, the Agency has rephrased this to read ''with Agency-approved restrictions.''

Comment: One commenter asked why the provisions in the 2002 Farm Bill for loan guarantees to cooperative organizations that were headquartered in an urban area as long as certain rural benefits/requirements were met, were omitted from the proposed rule.

Another commenter asked what ''assisting cooperative organizations'' means.

This commenter also asked whether housing cooperatives would be eligible and suggested that because cooperatives are already listed as an eligible entity for Business and Industry loans, this item could be eliminated here as redundant.

Response: The Agency agrees that loan guarantees to cooperative organizations that were headquartered in an urban area are eligible as long as certain rural benefits/requirements were met need to be part of the rule, and has added this provision to § 5001.103(d)(1)(v) concerning borrower eligibility. The Agency also agrees that the word ''assisting'' in proposed paragraph (d)(1)(xviii), as well as in paragraph (xvii), made those two paragraphs unclear in their meaning. The Agency also determined that it is not needed in either paragraph and thus has removed it from these two paragraphs in the rule. Finally, the Agency deleted proposed § 5001.103(xviii) in its entirety because cooperative organizations are eligible entities and it was redundant to identify cooperative organizations as an eligible purpose.

Unauthorized Projects and Purpose (§ 5001.103(c)) (Proposed § 5001.103(b))

Comment: One commenter stated that the proposed rule does not say anything about the eligibility of projects that 7 CFR part 4279, subpart B currently prohibits (charities, churches, fraternal organizations per 7 CFR § 4279.114(d) and lending, investment, and insurance companies per 7 CFR 4279.114(e). This commenter recommended that it would be best to continue with established Business and Industry practices in the new rule.

Another commenter stated that currently the Business and Industry program prohibits loan guarantees to insurance companies, lending institutions, charitable institutions, and businesses owned by Government employees, but that under the proposal these are no longer listed as ineligible. The commenter questioned why this was changed and stated that guaranteeing loans to insurance companies to pay claims or to lending institutions to make loans is extremely risky. The commenter further explained that if these type businesses cannot generate sufficient cash flow and have to resort to borrowing, it is an indication of an unsuccessful business.

Response: The Agency agrees with the commenters that the rule should have incorporated the current Business and Industry regulations pertaining to the ineligibility of lender, investment, and insurance companies. The rule includes these as ineligible purposes. However, it is not the intent of the Agency, as a policy matter, to preclude the eligibility of certain projects associated with charities, churches, and fraternal organizations. The Agency will provide guidance in the handbook for the rule concerning such projects.

Comment: One commenter did not believe that the intent of this rule was to prohibit financing of small businesses doing business from the owner's home, and suggested returning to the language in the old Business and Industry regulations. The commenter suggested using the following: ''Owner-occupied housing. Bed and breakfasts, storage facilities, et al., are eligible when the pro-rata value of the owner's living quarters is deleted from the value of the project.'' Another commenter stated that the proposed rule does not say anything about the eligibility of projects that RD Instruction 4279–B currently prohibits, including owner-occupied housing per § 4279.114(n)). This commenter recommended that it would be best to continue with established Business and Industry practices in the new rule.

Response: The Agency believes the provisions in both § 5001.103(b)(2)(xiii) and in § 5001.103(c)(1) adequately address owner-occupied housing, including bed and breakfast establishments, sufficiently to determine whether owner-occupied housing is eligible or not. The provision in § 5001.103(c)(1) is sufficiently broad to cover owner-occupied housing. The Agency will provide additional guidance in the handbook for the rule concerning businesses housed in private homes.

Comment: One commenter noted that the need to have the Department of Labor give its approval for any project that will be creating more than 50 jobs should be changed, because adding another layer of approval does not make any sense and takes too much time. The commenter stated that this requirement needs to be changed and has no value to the whole system.

Response: The requirement referred to by the commenter is a statutory requirement and as such the Agency cannot change it within this rulemaking. However, the Agency has recast this provision to reference the statutory provisions as follows: Any project that does not meet the requirements of paragraphs (d)(2), (d)(3), and (d)(4) in 7 CFR part 1932.

Comment: One commenter suggested that with regard to interim financing the rule should be amended to allow for partial pre-applications or simple notifications of intent to use the program in cases where the borrower is unable to provide all of the information necessary to complete a pre-application.

Response: The Agency has not implemented the commenter's suggestions because interim financing is not an eligible purpose and, thus, there are no applicable pre-application or notification requirements.

Comment: One commenter stated that this provision as written would prohibit inter-family transfers of business ownership and needs to be fixed. A second commenter recommended replacing the term ''immediate family'' with ''close relative'' to use (and be consistent with) a definition established in § 5001.2. This commenter also noted that the term ''close relative'' is not defined.

Response: The Agency agrees with both suggestions. This provision in the rule now uses the term ''immediate family'' and specifically provides an exemption that allows for the inter-family transfer of business ownership.

Comment: One commenter noted that this rule does not define what ''Government Employees'' consist of in relationship to assistance to government employees. The commenter recommended that ''Government Employees'' should be qualified to mean any federal employee of the United States Federal Government. If the proposed regulation is not clarified, it would be unfair as some U.S. government employees would be eligible for guaranteed funding while others would not.

Response: Subpart A prohibits projects and purposes where there are conflicts of interest or appearances of conflicts of interest. The Agency believes that this subpart A provision is sufficient such that proposed § 5001.103(b)(6) is not required and this paragraph has been removed from the rule. With its removal, there is no need to define, within the rule, ''government employee.''

Borrower Eligibility (§ 5001.103(d)) (Proposed § 5001.103(c))

Comment: One commenter noted that eligible borrowers for Business and Industry loans will now include virtually any legally-organized entity, including purely charitable, fraternal and religious organizations, which is a difference from the existing regulations.

Response: The Agency agrees with the commenter's observation.

Comment: One commenter noted that true cooperatives are omitted as eligible borrowers.

Response: The Agency agrees that the proposed rule did not include true cooperatives as eligible borrowers. This was an oversight and the rule now includes true cooperatives as eligible borrowers. To effect this change, the Agency redefined cooperative organization.

Additional Application Process Requirements (§ 5001.103(f)) (Proposed § 5001.103(d))

Comment: Three commenters commented on the proposed priority scoring of Business and Industry applications. Two of the commenters stated that it makes no sense to require the Agency to publish its priority scoring process every year in the **Federal Register**. These commenters suggested reprinting the current scoring criteria from the 7 CFR part 4279, subpart B regulation.

The third commenter said that priority scoring should be eliminated, noting that commercial lending is a just-in-time business and the use of a priority scoring system ever in the delivery of loan guarantees is anathema. According to this commenter, the guarantees must be available on a first-come-first-served basis until funding is exhausted.

Response: In considering these comments, the Agency believes that the suggestion to eliminate priority scoring for guaranteed loan programs is appropriate in order to deliver the programs in line with commercial lending practices. Therefore, the Agency has revised the rule to eliminate references to scoring and has replaced scoring with a ''first in, first out'' basis; that is, the Agency will approve loan applications based on the date and time complete applications are received by the Agency. In determining the date and time for receipt of complete applications, the Agency will convert the date and time to Eastern time.

Additional Application Documentation Provisions (§ 5001.103(g)) (Proposed § 5001.103(e))

Comment: Six commenters expressed a variety of concerns on the proposed requirement for audited financial statements.

One commenter recommended that USDA continue its current Business and Industry guaranteed loan regulation regarding audited financial statements. The proposed regulation is unclear; however, if the intention is to require applicants for loans over $1 million to have audited financial statements for prior years, it will adversely impact many otherwise good, credit worthy potential rural businesses that need Business and Industry guaranteed loans.

Two commenters suggested deleting this requirement altogether. One commenter stated that this requirement is inappropriate for Business and Industry and should be eliminated. The commenter stated that:

(1) no allowance is made for startup businesses where there would be no audit available;

(2) if only annual audits are needed for risky projects over $3 million, so why are audits needed up front for a sound borrower and a $1 million project; and

(3) audits are expensive and burdensome and would be a significant hindrance to the Agency's ability to support many of its current borrowers. The other commenter questioned at whose discretion the audit would be required, the Agency or the loan officer. This commenter added that audited statements are a true financial hardship for the majority of borrowers and should be eliminated completely from the proposal requirements. This commenter also noted that the requirement for audited financial statements is not an industry norm.

Two commenters suggested using tax returns instead of audited financial statements. One commenter noted that the USDA needs to use the opportunity of this proposed rule to jettison its focus on GAAP financial statements in favor of tax returns, the financial tool now most widely used in business banking and the only financial statement that is uniformly and consistently available from all businesses. The other commenter stated that audited statements are expensive and not practical for many rural businesses, and suggested using tax returns, as it is more common and effective.

Another commenter noted that this seems to conflict with § 5001.12, and asked if they don't need an audit after they receive the loan, why require it before they even apply. This commenter believed that the paragraph in this section is correct, and stated that an audit requirement should be up to the lender first and USDA should have the option to require one on the larger loans about $3 million.

Response: As noted in responses to other related comments, the Agency has removed the requirement for annual audited statements for projects over $3 million and has replaced it with a requirement for the submittal of financial reports, either as required by the lender's regulatory authority if the lender is regulated or supervised or as contained in the Conditional Commitment if the lender is an other lender (*see* § 5001.17(d), Financial reports).

In addition, provisions in the rule address the commenter's concern for startup businesses by allowing borrowers that have been in existence for less than one year to submit an Agency-authorized financial statement, which may be an unaudited statement, with the application.

Comment: Three commenters stated that the requirement for annual audited financial statements is a loan servicing requirement, not an application requirement, and suggested that it be part of either the Loan Agreement requirements or Conditional Commitment section.

Response: The Agency agrees with the commenters that the requirement for annual financial statements is not an application requirement. In the rule, the Agency is requiring the submittal of financial reports as part of lender servicing requirements under subpart A (see § 5001.17(d)).

Additional Guarantee- and Loan-Related Requirements (§ 5001.103(j)) (Proposed § 5001.103(g))

Comment: One commenter recommended that the current practice in 7 CFR 4279.181, of having the lender provide a certification that all of the requisite conditions are met prior to issuance of the guarantee should be incorporated here.

Response: The rule provides in § 5001.34(c) that the Agency will not issue the Loan Note Guarantee until all of the conditions specified in the Conditional Commitment have been met. This provision applies to all of the guaranteed loan programs covered by this rule. Thus, there is no need to repeat this requirement in subpart B for the Business and Industry program.

Comment: Four commenters provided comments on funding limits. Two commenters noted that the proposed rule has no change in the Business and Industry maximum funding limit and recommended increasing the maximum loan limit for Business and Industry loans to $40 million due to the capital needed in all types of businesses, not just cooperatives.

One commenter recommended that limits be established for the total borrower indebtedness and for total indebtedness of the owners, guarantors, related businesses, or parties. This commenter suggested the following language: ''Funding limits. The total amount of Business and Industry (Business and Industry) loans to any one borrower, including:

(1) the guaranteed and unguaranteed portions,

(2) the outstanding principle and interest balance on any existing Business and Industry loans, and

(3) new Business and Industry loan requests, must not exceed $25 million except that the total Business and Industry amount to a cooperative organization may not exceed $40,000,000 for rural projects processing value added commodities.''

Response: It is the Agency's intent to continue the current Business and Industry program's funding limitations and the Agency has not revised the maximum loan limit in the rule. If the Agency determines at a future date that such an increase is warranted, the Agency would consider revising the rule at such time.

With regard to the suggestion that the Agency limit the amount of Business and Industry guaranteed loans to one borrower, the Agency has incorporated a provision that would limit the amount a borrower could receive. Specifically, as stated in 5001.103(j)(5), ''the full amount of outstanding principal and interest balance associated with Business and Industry loans, including the amount of the loan being approved, cannot exceed $25,000,000 for any one borrower.'' For a cooperative organization, this limit is $40,000,000.

Lastly, the commenter also suggested that an upper limit be based on the amount of indebtedness that a borrower has to the Agency (''The total amount of Business and Industry (Business and Industry) loans to any one borrower''). The Agency disagrees that, if an upper limit were to be adopted, such an upper limit would be based only on the borrower's indebtedness to the Agency. There is no rational basis to differentiate between a borrower's indebtedness to the Agency and the borrower's total indebtedness.

Comment: One commenter stated that the 1% guarantee fee is available if the borrower is a high impact business, which is currently determined by using the Priority Scoresheet that the State Office prepares for each loan. The commenter then asked how this will be determined because the proposed rule eliminated the Priority Scoresheet.

One commenter recommended that the 2% fee needs to be reduced to 1% and the annual servicing fee needs to be reduced to 0.125%.

Response: The Agency will determine if a business is a ''high impact'' business on the basis of whether it meets the definition of ''high impact business,'' which has been rewritten to make it clearer when a business is a high impact business. The Agency will provide additional guidance in the handbook for the rule to assist in making such determinations. The Agency does not see any need to reduce the guarantee fee further than provided for in the rule for high impact businesses. The rule does not specify a maximum annual servicing fee and the Agency will publish the applicable rate when such a fee will be assessed in a fiscal year.

Comment: Two commenters stated that the percentage of guarantee should be a constant at 80% on Business and Industry loans, and not decreased as the loan size increases. The commenters added that this would make the Business and Industry program more attractive to lenders and better enable the small and medium banks to handle and serve their customers.

A third commenter stated that the 60% guarantee amount and $25,000,000 loan amount limit the usefulness of the guarantee on larger projects. This low of a guarantee is very difficult to sell in the marketplace.

Response: The Agency has not revised the rule as requested by the commenters. The provisions on the level of the guarantee are based on the Agency's strategy for managing risk and the Agency believes that the percentage of guarantees as proposed are reasonable.

Comment: One commenter stated that the asterisk to the chart should read ''Per § 5001.103(g)(3), the maximum * * * is $25 million except for a rural cooperative organization producing a value added commodity for which the maximum is $40 million.'' See 2002 Farm Bill.

Response: While the commenter is correct, the Agency has removed the table from the rule and thus there is no correction to make.

Rural Energy for America Program (§ 5001.104)

Application Documentation (§ 5001.104(d))

Comment: Two commenters stated that the certification should be corrected to specify that the prospective borrower is an agricultural producer (not a ''small'' agricultural producer) or rural small business. The commenters pointed out that there is no limitation in the 9006 program to assisting only ''small agricultural producers'', and this should not be imposed now. According to the commenters, to limit the 9006 guaranteed loans to producers grossing $600,000 or less would restrict the program only to the smallest of farmers.

Response: The Agency did not intend to change this certification from what the current program requires and thus agrees with the commenters. Therefore, the Agency has revised the rule to drop ''small'' in reference to agricultural producer. A conforming change was also made to the definitions section by dropping the term ''small agricultural producer'' as that term no longer appears in the rule.

Comment: Three commenters expressed concern as to who would review technical reports for renewable energy projects. One commenter suggested requiring the technical report to flow through USDA for submission to DOE. Another commenter also preferred to be able to coordinate this activity through the USDA as part of the USDA program. One commenter asked if the proposed process is actually possible and if the National Renewable Energy Laboratory (NREL) is agreeable. This commenter suggested requiring a technical report as part of any application for any loan over a certain size, and leave it up to USDA to arrange for the technical review.

Response: The Agency agrees that it should be responsible for ensuring that these technical reports are reviewed by the appropriate entity and has modified the rule to indicate that these reports are to be submitted to the DOE for review unless otherwise stated in a **Federal Register** notice. Beyond that, the Agency will provide guidance in the handbook to the rule to ensure the proper entities are engaged in reviewing the technical report.

Comment: One commenter suggested that the technical report threshold of a ''loan guarantee of more than $200,000'' should be changed from ''loan guarantee'' to either eligible project costs or the total loan amount, regardless of the percent of guarantee. According to the commenter, tying the $200,000 to the amount of the loan guarantee is confusing and is not a measure commonly used by USDA anywhere else and would surely cause problems.

Another commenter also suggested that this requirement be tied to total project cost rather than the size of the guaranteed loan. This commenter further suggested that the threshold be lowered to $50,000 because renewable energy projects are complex, even when they are small, since they rely on such factors as interconnection, resource availability, technology, etc.

Response: The Agency agrees with the two commenters that the criterion to determine when the technical report is required should be based on total eligible project costs and not on the loan guarantee amount. The Agency has made this change in the rule. However, the Agency disagrees that the threshold needs to be reduced and has retained the threshold at $200,000.

Comment: One commenter recommends that energy assessments/audits should only be required on energy efficiency projects costing in excess of $100,000.

Response: The Agency disagrees that the threshold for requiring an energy assessment or audit needs to be changed from the current level of $50,000, and has retained this threshold in the rule to ensure that loans of more than $50,000 are having an impact on energy savings.

Comment: One commenter noted that, unlike with renewable energy projects discussed in § 5001.104(d)(2), there is no mention of any NREL or other technical review for energy assessment and audits in § 5001.104(d)(3). The commenter asked what is intended, and said that this should be spelled out.

Response: As noted in the response to a similar comment on the technical reports required under this program, the Agency will ensure that the proper review of energy assessment and energy audits performed will take place, but that it is not necessary to identify in the rule who will perform such reviews.

Comment: One commenter noted that the limit for energy assessment/audit refers to eligible project costs greater than $50,000, compared to seeking a loan guarantee of $200,000 for the renewable energy technical report or the feasibility study required under § 5001.104(d)(4). The commenter recommended consistency, stating that the different amounts are confusing, and using different measures will be problematic.

Response: The Agency agrees, in part, with the commenter that the same measure for determining when an energy assessment or audit is required should be used for when a technical report is required. Thus, the Agency has modified the rule such that in both instances total eligible project costs is the measure. However, for determining when a feasibility study is required, the Agency is maintaining the proposed measure of the size of the loan guarantee because it is a better measure of risk than total eligible project costs and the Agency has direct control over the loan guarantee amount and not the project cost. The Agency believes that these requirements are clear enough that confusion will not be an issue.

Comment: One commenter suggested that the regulation simply require a feasibility study and that it may be appropriate for the applicant to obtain the study. The commenter noted that this would be more consistent with the language used for the Business and Industry program. The commenter suggested the following language be used: ''Feasibility study. A feasibility study by a qualified independent consultant is required for each project seeking a loan guarantee greater than $200,000.''

Response: The Agency agrees with the commenter that the text of this paragraph should simply state that a feasibility study is required and not to refer to the lender obtaining the study. The rule reflects the language suggested by the commenter. The Agency has not included in the rule who is responsible for obtaining the feasibility study as this is unnecessary.

Comment: One commenter noted that the requirement for a feasibility study does not currently apply to energy efficiency projects under section 9006 guarantees, and recommended that this exception should not be revoked as is proposed here.

Response: The Agency agrees with the commenter. It was not the intent in the proposed rule to require feasibility studies for energy efficiency projects and the rule has been modified to require feasibility studies only for renewable energy systems, as is found in the current regulations for this program.

Comment: One commenter questioned whether it is necessary to have a feasibility study on proven, ''cookie-cutter'' projects such as large wind, even if they cost more than $200,000.

Response: The Agency disagrees with the commenter's suggestion. The Agency believes that all renewable energy projects with guaranteed loan amounts of greater than $200,000 require a feasibility study because even ''cookie-cutter'' projects can have project- and site-specific issues.

Comment: Regarding the language that says that the Agency ''may'' require a feasibility study, one commenter suggested that guidance should be provided that explains when a feasibility study is necessary (e.g., in a staff instruction or handbook).

Response: The Agency reviewed the proposed rule and, as proposed, feasibility studies for projects under this program would be required; the proposed rule did not say that the Agency ''may require'' a feasibility study. Thus, no change is required to the rule in response to this comment. The Agency notes that the Agency ''may require'' feasibility studies for other programs and has addressed this same comment elsewhere.

Comment: One commenter noted that the proposed rule is silent on the annual financial statements requirement for Section 9006 borrowers, but then there is a reference to audited financial statements on loans over $3 million. The commenter stated that USDA needs to use the opportunity of this proposed rule to jettison any focus on GAAP financial statements in favor of tax returns, the financial tool now most widely used in business banking and the only financial statement that is uniformly and consistently available from all agricultural producers and small businesses.

Response: The financial statement requirements applicable to all programs under this part, including the Rural Energy for America Program, are found in subpart A in § 5001.12(a)(10). Under the rule, Agency-authorized financial statements may be used for businesses that have been in existence for less than one year regardless of the amount of the guaranteed loan request. If the guaranteed loan is for less than $3 million, borrowers that have been in existence for one or more years may submit either the most recent audited or Agency-acceptable financial statements of the borrower. Thus, for these set of borrowers, the rule allows for flexibility in the type of statement submitted. However, the Agency continues to believe that requiring audited financial statements is the best method for addressing risk for borrowers that have been in existence for one or more years that are seeking guaranteed loans of $3 million or more, unless alternative financial statements are authorized by the Agency.

Additional Guarantee- and Loan-Related Requirements (§ 5001.104(g)) (Proposed § 5001.104(f))

Comment: Two commenters noted that the proposed rule disallows issuance of the guarantee until after the Section 9006 project is complete and operating up to specifications. The commenters pointed out that the current regulations are vague as to what constitutes an operating cycle, and this requirement is too conservative to promote the Section 9006 program's goal of encouraging new projects. The commenters suggested allowing the issuance of the guarantee prior to development for all energy-efficiency projects and for renewable energy projects using commercially available, as opposed to pre-commercial technology. The commenters added that this will allow additional project opportunities as the construction phase is typically the highest risk period to the lender and the guarantee will help mitigate this risk and promote quality projects.

Response: The Agency disagrees with the commenters' suggestion to allow the issuance of the guarantee for projects under this program prior to completion because of the risk associated with the technologies associated with renewable energy projects. The rule continues current Agency policy with regards to projects under this program. With regard to current regulations being vague as to what constitutes an operating cycle, the Agency will provide guidance in the handbook to the rule.

Comment: One commenter said that, to be a serious contender in the energy-financing field, the program must let lenders loan more than 50% of eligible project costs. The commenter recommended raising the limit to 75% combined total between energy grants and guaranteed loans to allow for a larger percentage loan if no grant is involved in the project.

Response: The 2008 Farm Bill has raised this limit to 75%. Therefore, the Agency has revised the interim rule accordingly, raising the limit from 50% to 75%.

Comment: One commenter noted that the proposed rule does not limit the size of individual energy loans or the total indebtedness of the borrower, owners, or related entities, and suggested that established limits be considered. Another commenter asked if there is a maximum loan size specified in this regulation.

Response: The commenter is correct in that unlike the current regulation, which limits the amount of a loan to any one borrower to $10 million, the proposed rule did not include this limit. However, the 2008 Farm Bill has a provision that limits the maximum loan guarantee under this program to $25 million. Therefore, the Agency has added this limit to the rule. In addition, the interim rule applies this limit on a per borrower basis, stating that ''at the time of loan approval, the full amount of outstanding principal and interest balance associated with Rural Energy for America Program loans, including the amount of the loan being approved, cannot exceed $25 million for any one borrower.''

Comment: One commenter requested that the proposed rule clarify that customary lender fees associated with the loan and the section 9006 guaranteed loan fee are eligible purposes.

Response: It is the Agency's policy that each loan guarantee be attributed to hard project costs and not fees. Thus, no change was made to the rule in response to this comment.

List of Subjects

7 CFR Part 1779

Guaranteed loans, Loan programs, Waste treatment and disposal, Water supply.

7 CFR Part 3575

Community facilities, Guaranteed loans, Loan programs.

7 CFR Parts 4279 and 4280

Loan programs—Business and industry—Rural development assistance, Economic development, Energy, Direct loan programs, Grant programs, Guaranteed loan programs, Renewable energy systems, Energy efficiency improvements, Rural areas.

7 CFR Part 5001

Business and industry, Community facility, Energy efficiency improvement, Loan programs, Renewable energy, Rural development, Rural areas, Water and waste disposal.

■ For the reasons set forth in the preamble, under the authority at 5 U.S.C. 301 and 7 U.S.C. 1989, Chapters XVII, XXXV, and XLII of title 7 of the Code of Federal Regulations are amended and Chapter L is established as follows:

CHAPTER XVII—RURAL UTILITIES SERVICE, DEPARTMENT OF AGRICULTURE

PART 1779—[REMOVED]

■ 1. Part 1779 is removed and reserved.

CHAPTER XXXV—RURAL HOUSING SERVICE, DEPARTMENT OF AGRICULTURE

PART 3575—[REMOVED]

■ 2. Part 3575 is removed and reserved.

CHAPTER XLII—RURAL BUSINESS—COOPERATIVE SERVICE AND RURAL UTILITIES SERVICE, DEPARTMENT OF AGRICULTURE

PART 4279—GUARANTEED LOANMAKING

■ 3. The authority citation for part 4279 is revised to read as follows:

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

Subpart B—Business and Industry Loans

■ 4. Subpart B of part 4279 is removed and reserved.

PART 4280—LOANS AND GRANTS

■ 5. The authority citation for part 4280 continues to read as follows:

Authority: 7 U.S.C. 8106.

Subpart B—Renewable Energy Systems and Energy Efficiency Improvements Program [Amended]

§§ 4280.121–4280.160 [Removed and Reserved]

■ 6. Section B of Subpart B of part 4280, consisting of §§ 4280.121 through 4280.160, is removed and reserved.

■ 7. Section 4280.193 of subpart B of part 4280 is amended by revising the introductory text and paragraphs (a), (b)(1), (c) through (e), and (f)(2) to read as follows:

§ 4280.193 Combined funding.

The requirements for a project for which an applicant is seeking a combined grant and guaranteed loan are defined as follows:

(a) *Eligibility.* Applicants must meet the applicant eligibility requirements specified in § 4280.107. Projects must meet the project eligibility requirements specified in §§ 4280.108. Applicants may submit simplified applications if the project meets the requirements specified in § 4280.109.

(b) * * *

(1) The amount of any combined grant and guaranteed loan must not exceed 75% of total eligible project costs. For purposes of combined funding requests, total eligible project costs are based on the total costs associated with those items specified in §§ 4280.110(c) and 5001.104(g)(3) of this chapter. The applicant must provide the remaining total funds needed to complete the project.

* * * * *

(c) *Application and documentation.* When applying for combined funding, the applicant must submit separate applications for both types of assistance (grant and guaranteed loan). Each application must meet the requirements, including the requisite forms and certifications, specified in §§ 4280.111, 5001.12, and 5001.104(d) of this chapter. The separate applications must be submitted simultaneously. The applicant must submit at least one set of documentation, but does not need to submit duplicate forms or certifications.

(d) *Evaluation.* The Agency will evaluate each application according to applicable procedures specified in §§ 4280.112, 5001.11, and 5001.104(c) of this chapter.

(e) *Interest rate and terms of loan.* The interest rate and terms of the loan for the loan portion of the combined funding request will be determined based on the procedures specified in § 5001.31 of this chapter for guaranteed loans.

(f) * * *

(2) All other provisions of 7 CFR part 5001 shall apply to the guaranteed loan portion of the combined funding request.

■ 8. Chapter L consisting of parts 5000 through 5099 is established and a new part 5001 is added to read as follows:

CHAPTER L—RURAL BUSINESS—COOPERATIVE SERVICE, RURAL HOUSING SERVICE, AND RURAL UTILITIES SERVICE, DEPARTMENT OF AGRICULTURE

PART 5001—GUARANTEED LOANS

Subpart A—General Provisions

Authority: 5 U.S.C. 301; 7 U.S.C. 1926(a); 7 U.S.C. 1932(a); and 7 U.S.C. 8106.

§ 5001.1 Purpose and scope.

(a) *General.* The purpose and scope of this part is to simplify, standardize, and improve the making, guaranteeing, holding, servicing, and liquidating of Rural Development guaranteed loans. This part applies to those guaranteed loan programs specified in subpart B of this part.

(b) *Relationship between subpart A and subpart B requirements.* All guaranteed loan programs subject to this part are subject to the requirements specified in subpart A, unless there is a program specific provision in subpart B that overrides the corresponding subpart A provision. Such as subpart B provision may modify the scope of or replace entirely the corresponding subpart A provision.

§ 5001.2 Definitions.

The following definitions are applicable to the terms used in this part.

Agency. The Rural Housing Service; the Rural Utilities Service; and the Rural Business-Cooperative Service or the successors for the programs it administers.

Agricultural producer. An individual or entity directly engaged in the production of agricultural products, including crops (including farming); livestock (including ranching); forestry products; hydroponics; nursery stock; or aquaculture, whereby 50% or greater of their gross income is derived from the operations.

Approved lender. A lender that the Agency has determined meets the criteria specified in § 5001.9(a) through (c), as applicable, of this part.

Arm's length transaction. A transaction between ready, willing, and able disinterested parties who are not affiliated with or related to each other and have no security, monetary, or stockholder interest in each other.

Assignment guarantee agreement. A signed, Agency-approved agreement between the Agency, the lender, and the holder setting forth the terms and conditions of an assignment of a guaranteed portion of a loan or any part thereof.

Assurance agreement. A signed, Agency-approved agreement between the Agency and the lender that assures the Agency that the lender is in compliance with and will continue to be in compliance with Title VI of the Civil Rights Act of 1964, 7 CFR part 15, and Agency regulations promulgated there under.

Biomass. Any organic material, excluding paper that is commonly recycled and unsegregated solid waste, that is available on a renewable or recurring basis, including agricultural crops; trees grown for energy production; wood waste; wood residues; plants, aquatic plants and grasses; natural fibers; animal waste and other waste materials; and fats, oils, and greases, including recycled fats, oils, and greases.

Borrower. The person that borrows, or seeks to borrow, money from the lender, including any party or parties liable for the guaranteed loan except guarantors.

Business plan. A comprehensive document that clearly describes the borrower's ownership structure and management experience including, if applicable, discussion of a parent, affiliates, and subsidiaries; a discussion of how the borrower will operate the proposed project, including, at a minimum, a description of the business and project, the products and services to be provided, pro forma financial statements for a period of 2 years, including balance sheet, income and expense, and cash flows, and the availability of the resources necessary to provide those products and services.

Collateral. The asset(s) pledged by the borrower in support of the loan.

Commercially available. A system that has a proven operating history of viability of at least one year, specific to the proposed application. Such a system is based on established design, and installation procedures and practices. Professional service providers, trades, large construction equipment providers, and labor are familiar with installation procedures and practices. Proprietary and balance of system equipment and spare parts are readily available. Service is readily available to properly maintain and operate the system. An established warranty exists for parts, labor, and performance.

Community support. Sufficient evidence of the area to be served that there is enough demand and support for the service or facility to make the project economically viable.

Conditional commitment. An Agency-approved form of commitment to the lender that the loan guarantee the lender has requested is approved subject to the completion of all conditions and requirements contained in the commitment as set forth by the Agency.

Cooperative organization.

(1) Any entity that is legally chartered as a cooperative.

(2) Any entity that is not legally chartered as a cooperative, but is owned and operated for the benefit of its members, including the manner in which it distributes its dividends and assets, provided those members are not employees of the organization.

Day. Calendar day, unless otherwise stated.

Debt coverage ratio. The ratio obtained when dividing the realistically projected earnings and cash injection before interest, taxes, depreciation, and amortization by the annual debt service (principal and interest).

Default. The condition that exists when a borrower is not in compliance with the promissory note, the loan agreement, or other related documents evidencing the loan.

Delinquent loan. A loan for which a scheduled loan payment has not been received by the due date or within any grace period as stipulated in the promissory note and loan agreement.

Eligible project costs. Those expenses approved by the Agency for the project.

Energy assessment. A report conducted by an experienced energy assessor, certified energy manager or professional engineer assessing energy cost and efficiency. The report identifies and provides a savings and cost analysis of low-cost/no-cost measures, estimates overall costs and expected energy savings from the funded improvements, and dollars saved per year and provides an estimate of the anticipated weighted average payback period in years.

Energy audit. A report conducted by a Certified Energy Manager or Professional Engineer that focuses on potential capital-intensive projects and involves detailed gathering of field data and engineering analysis. The report will provide detailed project costs and savings information with a high level of confidence sufficient for major capital investment decisions similar to but in more detail than an energy assessment.

Energy efficiency improvement. A product or process installed in a facility, or building, that reduces energy consumption.

Essential community facility. The physical structure (including machinery and/or equipment) financed or the resulting service provided to primarily rural residents that combined or severally must:

(1) Perform or fulfill a function customarily provided by a local unit of government;

(2) Be a public improvement needed for the orderly development of a rural community;

(3) Benefit the community at large;

(4) Not include commercial or business undertakings (except for limited authority for industrial parks); and

(5) Be within the area of jurisdiction or operation for eligible public bodies or a similar local rural service area of a not-for-profit corporation.

Existing business. A business that has been in operation for at least one full year. Mergers, changes in the business name, or legal type of entity of a currently operating business, or expansions of product lines are considered to be existing businesses as long as there is not a significant change in operations.

Feasibility study. An analysis by a qualified consultant of the economic, market, technical, financial, and management capabilities of a proposed project or business in terms of its expectation for success.

Future recovery. Funds collected by lender after final loss claim.

Guaranteed loan. A loan made and serviced by a lender for which the Agency has issued a Loan Note Guarantee.

High Impact Business. A business that is part of an industry that has 20% or more of its sales in international markets; offers high value, specialized products and services that command high prices; and creates jobs with an average wage exceeding 125% of the Federal minimum wage.

Holder. The person or entity, other than the lender, who owns all or part of the guaranteed portion of the loan with no servicing responsibilities.

Immediate family. Individuals who are closely related by blood, marriage, or adoption, or live within the same household, such as a spouse, domestic partner, parent, child, brother, sister, aunt, uncle, grandparent, grandchild, niece, or nephew.

Interim financing. A temporary or short-term loan made with the clear intent that it will be repaid through another loan, cash, or other financing mechanism.

Lender. An entity that has been approved by the Agency to originate and service loans guaranteed under this part.

Lender's agreement. The Agency-approved signed form between the Agency and the lender setting forth the lender's loan responsibilities under an issued Loan Note Guarantee.

Lender's analysis. The analysis and evaluation of the credit factors associated with each guarantee application to ensure loan repayment through the use of credit document procedures and an underwriting process that is consistent with industry standards and the lender's written policy and procedures.

Lending entity. An entity that originates and services a loan that has not been approved to originate loans under this part.

Loan agreement. The Agency-approved agreement between the borrower and lender containing the terms and conditions of the loan and the responsibilities of the borrower and lender.

Loan classification. The process by which loans are examined and categorized by degree of potential loss in the event of default.

Loan note guarantee. The Agency-approved form containing the terms and conditions of the guarantee of an identified loan.

Loan-to-value ratio. The ratio of the dollar amount of a loan to the dollar value of the collateral pledged as security for the loan.

Local government. A county, municipality, town, township, village, or other unit of general government below the State level. The term also includes tribal governments when tribal lands are within the service area.

Market value. The amount for which property would sell for its highest and best use at a voluntary sale in an arm's length transaction.

Material change. Any change in the purpose of the loan, the financial condition of the borrower, or the collateral, that might jeopardize loan performance.

Monetary default. A loan is in monetary default if payment is not made within 30 days after the payment due date.

Negligent loan origination.

(1) The failure of a lender to perform those services that a reasonably prudent lender would perform in originating its own portfolio of unguaranteed loans; or

(2) The failure of the lender to perform its origination responsibilities in accordance with its origination policies and procedures in use by the lender at the time the loan is made.

(3) The term includes the concepts of failure to act, not acting in a timely manner, or acting in a manner contrary to the manner in which a reasonably prudent lender would act.

Negligent loan servicing.

(1) The failure of a lender to perform those services that a reasonably prudent lender would perform in servicing and liquidating its own portfolio of unguaranteed loans; or

(2) The failure of the lender to perform its servicing responsibilities in accordance with its servicing policies and procedures in use by the lender at the time the loan is made.

(3) The term includes the concepts of failure to act, not acting in a timely manner, or acting in a manner contrary to the manner in which a reasonably prudent lender would act.

Other lending entity. A lending entity who does not meet the definition of regulated or supervised lending entity.

Participation. Sale of an interest in a loan by the lender wherein the lender retains the note, collateral securing the note, and all responsibility for loan servicing and liquidation.

Person. Any individual, corporation, company, foundation, association, labor organization, firm, partnership, society, joint stock company, group of organizations, public body, or State or local government.

Post-application. The date that the Agency receives an essentially completed application. An ''essentially completed'' application is an application that contains all parts necessary for the Agency to determine borrower and project eligibility and to conduct the technical evaluation.

Pre-application. Information submitted to the Agency for which the applicant requests the Agency to make an informal eligibility assessment prior to submitting a full application. The information must be sufficient for the Agency to make a determination that the borrower and project are eligible.

Pre-commercial technology. Technology that has emerged through the research and development process and has technical and economic potential for commercial application, but is not yet commercially available.

Preferred lender. An approved lender that, as determined by the Agency, also meets the criteria specified in § 5001.9(d) of this part.

Preliminary architectural report. A document normally prepared by a professional, licensed architect that describes the existing situation and problem, analyzes alternatives, and proposes a specific course of action from an architectural and environmental perspective. Sufficient information must be provided to adequately assess the need for, the feasibility of, and the cost of the project.

Preliminary engineering report. A document normally prepared by the owner's consulting engineer that describes the owner's present situation, analyzes alternatives, and proposes a specific course of action from an engineering and environmental perspective.

Promissory Note. A legal instrument that a borrower signs promising to pay a specific amount of money at a stated time. ''Note'' or ''Promissory Note'' shall also be construed to include ''Bond'' or other evidence of debt where appropriate.

Protective advances. Advances made by the lender for the purpose of preserving and protecting the collateral where the debtor has failed to, and will not or cannot, meet obligations to protect or preserve collateral.

Public body. A municipality, county, or other political subdivision of a State; a special purpose district; or an Indian tribe on a Federal or State reservation or other Federally recognized Indian tribe or an organization controlled by any of the above.

Qualified consultant. An independent, third-party possessing the knowledge, expertise, and experience to perform in an efficient, effective, and authoritative manner the specific task required.

Regulated or supervised lender. A lender that is subject to examination or supervision by an appropriate agency of the United States or a State that supervises or regulates credit institutions.

Renewable biomass.

(1) Materials, pre-commercial thinnings, or invasive species from National Forest System land and public lands (as defined in section 103 of the Federal Land Policy and Management Act of 1976 (43 U.S.C. 1702)) that:

(i) Are byproducts of preventive treatments that are removed to reduce hazardous fuels; to reduce or contain disease or insect infestation; or to restore ecosystem health;

(ii) Would not otherwise be used for higher-value products; and

(iii) Are harvested in accordance with applicable law and land management plans and the requirements for old-growth maintenance, restoration, and management direction of paragraphs (2), (3), and (4) of subsection (e) of section 102 of the Healthy Forests Restoration Act of 2003 (16 U.S.C. 6512) and large-tree retention of subsection (f) of that section; or

(2) Any organic matter that is available on a renewable or recurring basis from non-Federal land or land belonging to an Indian or Indian tribe that is held in trust by the United States or subject to a restriction against alienation imposed by the United States, including:

(i) Renewable plant material, including feed grains; other agricultural commodities; other plants and trees; and algae; and

(ii) Waste material, including crop residue; other vegetative waste material (including wood waste and wood residues); animal waste and byproducts (including fats, oils, greases, and manure); and food waste and yard waste.

Renewable energy.

(1) Energy derived from a wind, solar, renewable biomass, ocean (including tidal, wave, current, and thermal), geothermal, or hydroelectric source;

(2) Hydrogen derived from renewable biomass or water using an energy source described in paragraph (1) of this definition.

Renewable energy system. A system that produces or produces and delivers usable energy from a renewable energy source.

Report of loss. An Agency-approved form used by lenders when reporting a loss under an Agency guarantee.

Rural or rural area.

(1) For the purpose of providing Community Facilities loan guarantees, rural and rural area are defined as any area not in a city, town, or Census Designated Place with a population of more than 20,000 inhabitants according to the latest decennial census of the United States.

(2) For the purpose of providing Water and Waste Disposal loan guarantees, rural and rural area are defined as any area not in a city, town, or Census Designated Place with a population in excess of 10,000 inhabitants, according to the latest decennial census of the United States.

(3) For purposes of providing Business and Industry and Renewable Energy/Energy Efficiency loan guarantees, rural and rural area are defined as any area of a State not in a city or town that has a population of more than 50,000 inhabitants, according to the latest decennial census of the United States, and the contiguous and adjacent urbanized area.

(4) Notwithstanding any other provision of this definition, in determining which census blocks in an urbanized area are not in a rural area, the Agency shall exclude any cluster of census blocks that would otherwise be considered not in a rural area only because the cluster is adjacent to not more than 2 census blocks that are otherwise considered not in a rural area under this definition.

(5) For the purposes of this definition, cities and towns are incorporated population centers with definite boundaries, local self government, and legal powers set forth in a charter granted by the State. For Puerto Rico, Census Designated Place, as defined by the U.S. Census Bureau, will be used as the equivalent to city or town. For the purpose of defining a rural area in the Republic of Palau, the Federated States of Micronesia, and the Republic of the Marshall Islands, the Agency shall determine what constitutes rural and rural area based on available population data.

Small business. An entity is considered a small business in accordance with the Small Business Administration's small business size standards by the North American Industry Classification System found in Title 13 CFR part 121. A private entity, including a sole proprietorship, partnership, corporation, cooperative (including a cooperative qualified under section 501(c)(12) of the Internal Revenue Code), and an electric utility, including a Tribal or governmental electric utility, that provides service to rural consumers on a cost-of-service basis without support from public funds or subsidy from the Government authority establishing the district, provided such utilities meet Small Business Administration's definition of small business. These entities must operate independent of direct Government control. With the exception of the entities described above, all other not-for-profit entities are excluded.

Startup business. A business that has been in operation for less than one full year. Startup businesses include newly formed entities leasing space or building ground up facilities in a new market area, even if the owners of the startup business own affiliated businesses doing the same kind of business. Newly formed entities that are buying existing businesses or facilities will be considered an existing business as long as the business or facility being bought remains in operation and there is no significant change in operations.

State. Any of the 50 States of the United States, the Commonwealth of Puerto Rico, the District of Columbia, the U.S. Virgin Islands, Guam, American Samoa, the Commonwealth of the Northern Mariana Islands, the Republic of Palau, the Federated States of Micronesia, and the Republic of the Marshall Islands.

State Bond Banks and State Bond Pools. An entity authorized by the State to issue State debt instruments and utilize the funds received to finance projects that qualify for a guaranteed loan under this part.

Tangible net worth. Tangible assets minus liabilities.

Total project cost. The sum of all costs associated with a completed project.

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 outstanding debt.

Water and waste disposal facility. A physical structure or series of structures used to provide water and waste disposal services. Such structures include, but are not necessarily limited to, those for rural drinking water, sanitary sewage, solid waste disposal, and storm wastewater disposal.

Working capital. Current assets available to support a business' operations and growth. Working capital is calculated as current assets less current liabilities.

§ 5001.3 Agency authorities.

(a) *Exception authority.* Except as specified in paragraphs (a)(1) through (4) of this section, the applicable Administrator may, on a case-by-case basis, make exceptions to any requirement or provision of this part, if such exception is necessary to implement the intent of the authorizing statute in a time of national emergency or in accordance with a Presidentially-declared disaster, or when such an exception is in the best financial interests of the Federal Government and is otherwise not in conflict with applicable law.

(1) *Lender and borrower eligibility.* No exception to lender or borrower eligibility can be made.

(2) *Project eligibility.* No exception to project eligibility can be made.

(3) *Rural area definition.* No exception to the definition of rural area, as defined in § 5001.2, can be made.

(4) *Term length.* No exception to the maximum length of the loan term, as specified in § 5001.31(c), can be made.

(b) *Review or appeal rights.* A person has review or appeal rights in accordance with 7 CFR part 11.

§ 5001.4 Oversight and monitoring.

(a) *General.* The lender will cooperate fully with Agency oversight and monitoring of all lenders involved in any manner with any guarantee under this program to ensure compliance with this part, including ensuring lenders continue to meet the criteria for being an approved lender or a preferred lender. Such oversight and monitoring will include, but is not limited to, reviewing lender records and meeting with lenders. In addition, the Agency will review all approved and preferred lenders for eligibility at least every two years.

(b) *Reports and notifications.* The Agency will require lenders to submit to the Agency reports and notifications to facilitate the Agency's oversight and monitoring. These reports and notifications include, but are not necessarily limited to:

(1) Periodic reports, to be submitted semiannually, regarding the condition of its Agency guaranteed loan portfolio (including borrower status and loan classification) and any material change in the general financial condition of the

borrower since the last periodic report was submitted.

(2) Monthly default reports for each loan in monetary default using a form approved by the Agency.

(3) Notification within 15 calendar days of:

(i) Any loan agreement violation by any borrower, including when a borrower is 30 days past due or is otherwise in default;

(ii) Any permanent or temporary reduction in interest rate; and

(iii) Any downgrade in the loan classification of any loan made under this part.

(4) If a lender receives a final loss payment, an annual report on its collection activities for each unsatisfied account for 3 years following payment of the final loss claim.

§ 5001.5 Forms, regulations, and instructions.

Copies of all forms, regulations, and instructions referenced in this part may be obtained through the Agency.

Basic Eligibility Provisions

§ 5001.6 Project eligibility.

To be eligible for a guaranteed loan under this part, at a minimum, a borrower and project, as applicable, must meet each of the requirements specified in paragraphs (a) through (c) of this section.

(a) The project must meet the requirements specified in subpart B of this part.

(b) The borrower must meet the financial metric criteria specified in paragraphs (b)(1) through (b)(3) of this section. These financial metric criteria shall be calculated from the realistic information in the pro forma statements or borrower financial statements, submitted in accordance with § 5001.12(a)(10), of a typical operating year after the project is completed and stabilized. For projects that the Agency deems to be more risky, such as racetracks and water parks, the Agency will require higher underwriting standards for such projects.

(1) A debt coverage ratio of 1.0 or higher;

(2) A debt-to-tangible net worth ratio of 4:1 or lower for startup businesses and of 9:1 or lower for existing businesses.

(3) A loan-to-value ratio of no more than 1.0.

(c) For projects that are determined by a service area, boundaries for the proposed service area must be chosen in such a way that no user or area will be excluded because of race, color, religion, sex, marital status, age, disability, or national origin. This does not preclude:

(1) Financing or constructing projects in phases when it is not practical to finance or construct the entire project at one time, and

(2) Financing or constructing facilities where it is not economically feasible to serve the entire area, provided economic feasibility is determined on the basis of the entire system or facility and not by considering the cost of separate extensions to, or parts thereof. Additionally, the borrower must publicly announce a plan for extending service to areas not initially receiving service. Also, the borrower must provide written notice to potential users located in the areas not to be initially served.

§ 5001.7 Unauthorized projects and purposes.

Loans guaranteed under this part must not be used for any projects other than those authorized in subpart B of this part. In addition, loan funds may not be used to finance:

(a) Investment or arbitrage, or speculative real estate investment.

(b) Golf courses or similar recreational facilities listed in the annual Notice of Funds Availability.

(c) Any business deriving more than 10% of its annual gross revenue from gambling activity, excluding State-authorized lottery proceeds and, for public bodies and for not-for-profit approved projects only, any other funds derived from gambling activity, as approved by the Agency, conducted for the purpose of raising funds for the approved project.

(d) Prostitution or businesses deriving income from activities of a prurient sexual nature.

(e) Any guarantee of a:

(1) Line of credit;

(2) Lease payment; or

(3) Loan made by other Federal agencies.

(f) Any project eligible for Rural Rental Housing and Rural Cooperative Housing loans under sections 515, 521, and 538 of the Housing Act of 1949, as amended.

(g) Finders', packagers', or loan brokers' fees.

(h) Any business deriving income from illegal drugs, drug paraphernalia, or any other illegal product or activity.

(i) To pay the borrower for the rental of equipment or machinery owned by the borrower.

(j) The payment of either a Federal judgment or a debt owed to the United States, excluding other Federal loans.

(k) Any project that creates, directly or indirectly, a conflict of interest or an appearance of a conflict of interest.

(l) Properties to be used for commercial rental when the borrower has no control over tenants and services offered except for industrial-site infrastructure development and limited sections of essential community facilities when the activity in the leased space is related to and enhances the primary purpose for which the facility is being established by the borrower.

(m) Any project located within the Coastal Barriers Resource System that does not qualify for an exception as defined in section 6 of the Coastal Barriers Resource Act, 16 U.S.C. 3501 *et seq.*

(n) Any project located in a special flood or mudslide hazard area as designated by the Federal Emergency Management Agency in a community that is not participating in the National Flood Insurance Program unless the project is an integral part of a community's flood control plan.

(o) Any other similar project or purpose that the Agency determines is ineligible for funding under this part and publishes in a **Federal Register** notice.

§ 5001.8 Borrower eligibility.

(a) *Eligible entities.* To be eligible, a borrower must meet the requirements specified in paragraphs (a)(1) and (2) of this section and in subpart B to this part, as applicable.

(1) *Citizenship.* Citizenship requirements are as follows:

(i) Individual borrowers must be citizens of the United States (U.S.), the Republic of Palau, the Federated States of Micronesia, the Republic of the Marshall Islands, or American Samoa, or reside in the U.S. after legal admittance for permanent residence.

(ii) Entities other than individuals must be at least 51% owned or controlled by persons who are either citizens as identified under paragraph (a)(1)(i) of this section or are legally admitted permanent residents residing in the U.S.

(2) *Legal authority and responsibility.* Each borrower must have, or obtain, the legal authority necessary to construct, operate, and maintain the proposed facility and services and to obtain, give security for, and repay the proposed loan.

(b) *Ineligible entities.* A borrower will be considered ineligible for a guarantee if either the borrower or any owner with more than 20% ownership interest in the borrower:

(1) Has an outstanding judgment obtained by the U.S. in a Federal Court (other than U.S. Tax Court),

(2) Is delinquent on the payment of Federal income taxes,

(3) Is delinquent on a Federal debt, or

(4) Is debarred or suspended from receiving Federal assistance.

§ 5001.9 Participation eligibility requirements.

Only lenders are eligible to participate in the guaranteed loan programs described in this part.

(a) *General requirements.* The requirements in this paragraph apply to all lending entities who wish to participate in the guaranteed loan programs described in this part.

(1) *Loan origination and servicing policies and procedures.* The lending entity must submit a written summary of its loan origination and servicing policies and procedures, addressing, at a minimum, the areas specified in paragraphs (a)(1)(i) through (ix) of this section. At the Agency's request, the lending entity must make available any or all of its loan origination and servicing policies and procedures.

(i) Internal credit review process.

(ii) Underwriting process.

(iii) Portfolio management.

(iv) Delinquent loan handling.

(v) Liquidation process.

(vi) Releases.

(vii) Termination.

(viii) Final loss claims.

(ix) Exceptions to loan policies and procedures and other information relevant to Agency guaranteed loans.

(2) *Audit and management control system.* The lending entity must maintain internal audit and management control systems to evaluate and monitor the overall quality of its loan origination and servicing activities.

(3) *Debarment and suspension.* The lending entity must not be otherwise debarred or suspended by the Federal government.

(b) *Regulated or supervised lending entities.* The requirements for a regulated or supervised lending entity that has no outstanding guaranteed loans with the Agency to be eligible to participate are identified in paragraph (b)(1) of this section. The requirements for a regulated or supervised lending entity that has at least one outstanding guaranteed loan with the Agency to be eligible to participate are identified in paragraph (b)(2) of this section.

(1) *No outstanding Agency guaranteed loans.* A regulated or supervised lending entity that does not have any outstanding guaranteed loans as of January 16, 2009 with the Agency must apply for lender approval.

(i) *Lender application.* If the lending entity is a state chartered entity, the lending entity must submit the application, and other required documentation, to the State in which it is chartered. If the lending entity is a federally chartered entity, the lending entity must submit the application, and other required documentation, to the State in which the entity's headquarters is located.

(ii) *Policies and procedures.* The lending entity must submit with the lender application a written summary of its loan origination and servicing policies and procedures, as specified in paragraph (a)(1) of this section.

(iii) *Lending history and experience.* The lending entity must submit with the lender application a description of its lending history and experience, including:

(A) Evidence of demonstrated expertise in loan origination, making, securing, servicing, and collecting loans;

(B) Length of time in the commercial lending business;

(C) Its experience with government guaranteed lending, particularly within any of the subject programs;

(D) The range and volume of its lending and servicing activity;

(E) The current status of its loan portfolio;

(F) Its commercial loan fee structure;

(G) The level of experience of its management, lending, and servicing staff; and

(H) Audited financial statements not more than 1 year old.

(iv) *Approval process.* The Agency will review the application, including the summary of the lending entity's loan origination and servicing policies and procedures, submitted under paragraph (b)(1) of this section, to determine whether the lending entity is approved for participation under this part. The Agency may request additional clarification or information as necessary in its determination of lender approval.

(A) The Agency will approve or disapprove the lending entity on the basis of the information in the application, including the information describing the lending entity's loan origination and servicing policies and procedures.

(B) The lending entity must be in good standing with its regulator to be approved for participation.

(2) *With outstanding Agency guaranteed loans.* A regulated or supervised lending entity that has at least one outstanding guaranteed loan with the Agency as of January 16, 2009 is required to certify to the Agency that the lending entity is in good standing with its regulator and to submit a written summary of its loan origination and servicing policies and procedures, as specified in paragraph (a)(1) of this section.

(i) The lending entity must submit this certification and description either with, or prior to, its first application for loan guarantee under this part.

(ii) Such lending entity is approved for participation under this part when the Agency receives the lending entity's certification that the lending entity is in good standing with its regulator and the written summary of the lending entity's loan origination and servicing policies and procedures, as specified in paragraph (a)(1) of this section.

(3) *Lender's agreement.* If approved, the lender may sign a Lender's Agreement with the Agency. If the Lender's Agreement is executed by the lender and the Agency, the lender may submit an application for guarantee in any State in which it is authorized to do business. Approval for participation constitutes approval to participate in all guaranteed loan programs described in this part.

(4) *Maintenance of approved status.* Approved status is maintained as long as the lender remains in good standing with its regulator, in conformance with this part, or until otherwise notified by the Agency. If a lender fails to maintain its status as a Lender or has no outstanding loans with the Agency for two consecutive years, it must reapply under this section for lender approval.

(c) *Other lending entities.* Any lending entity not eligible in paragraph (b) of this section that wishes to originate a new loan under this part may apply for approved status, as specified in paragraph (c)(2) of this section, provided it meets the criteria specified in paragraph (c)(1) of this section.

(1) *Criteria for submitting an application for lender approval.* An other lending entity may submit an application for lender approval provided the lending entity has:

(i) A minimum net worth of $2.5 million;

(ii) Liquid assets of at least $500,000;

(iii) Acceptable line(s) of credit that totals $5 million or more; and

(iv) Undergone an examination acceptable to the Agency.

(2) *Application for lender approval.* The lending entity must submit an application to the Rural Development State Office in the State in which the entity is chartered providing the information specified in paragraphs (c)(2)(i) through (viii) of this section.

(i) A written summary of its loan origination and servicing policies and procedures, as specified in paragraph (a)(1) of this section.

(ii) Evidence showing that it has the necessary capital, resources, and funding capacity to successfully meet its responsibilities.

(iii) Copies of any license, charter, or other evidence of its legal authority to engage in the proposed loan making and servicing activities.

(iv) Certificate(s) of good standing from the States in which the lender is licensed and intends to conduct business.

(v) A description of its lending history and experience, including:

(A) Evidence of demonstrated expertise in loan origination, making, securing, servicing, and collecting loans;

(B) Length of time in the commercial lending business;

(C) Its experience with government guaranteed lending, particularly within any of the subject programs;

(D) The range and volume of its lending and servicing activity;

(E) The current status of its loan portfolio;

(F) Its commercial loan fee structure;

(G) The level of experience of its management, lending, and servicing staff; and

(H) Its audited financial statements not more than 1 year old.

(vi) Documented sources of its funds for funding and closing loans.

(vii) Office location(s) and its proposed geographic lending area(s).

(viii) Results of the examination required under paragraph (c)(1) of this section.

(3) *Agency review.* The Agency will review the application, including the lending entity's loan origination and servicing policies and procedures, submitted under paragraph (b)(1) of this section to determine whether the lending entity is approved for participation under this part. The Agency may request additional clarification or information as necessary in its determination of lender approval. The Agency will approve or disapprove the lending entity on the basis of the information in the application, including the information describing the entity's loan origination and servicing policies and procedures.

(4) *Lender's agreement.* If approved, the lender may sign a Lender's Agreement with the Agency. If the Lender's Agreement is executed by the lender and the Agency, the lender may submit an application for guarantee in any State in which it is authorized to do business.

(5) *Maintenance of approved status.* Approved status is maintained as long as the lender meets or exceeds minimum Agency requirements. If the Lender fails to maintain its status as a lender or has no outstanding loans with the Agency for two consecutive years, it becomes a lending entity and must reapply under this section for lender approval.

(d) *Preferred lenders.* Approved lenders may apply to the Agency for preferred lender status for the Business and Industry (B&I) guaranteed loan program in subpart B of this part. In addition, this preferred lender status may be expanded to include other programs contained in this part pursuant to notice published in the **Federal Register**.

(1) *Criteria for receiving preferred lender status.* The lender must meet each of the requirements specified in paragraphs (d)(1)(i) through (vii) of this section to obtain preferred lender status.

(i) Have a lender loss rate not in excess of the maximum ''preferred lender'' loss rate established by the Agency and published in a **Federal Register** Notice.

(ii) Have made a minimum of 10 guaranteed Business and Industry loans, unless another minimum number is specified in a notice in the **Federal Register**.

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

(iv) Have no more than one instance of Federal government negligent loan origination or servicing where a loss has been paid.

(v) Not be under any regulatory enforcement action, such as a cease and desist order, written agreement, or an appointment of conservator or receiver.

(vi) Demonstrated high standards of professional competence for the lender's staff, particularly key underwriting and servicing staff.

(vii) Adequate lender facilities to conduct its Agency business at a high level of performance.

(2) *Locations.* The lender must identify in its application for preferred lender status the States in which the lender desires to receive preferred lender status and its branch offices which the lender desires to be considered by the Agency for approval. The Agency will determine which branches of the lender have the necessary experience and ability to participate in the preferred lender program based on the information submitted in the lender application and on Agency experience.

(3) *Timeframe and renewal.* A lender who is determined to be eligible for preferred lender status will be granted such status for a period not to exceed four years from the date the Lender's Agreement is executed. A lender must submit a written request for renewal of a Lender's Agreement with preferred lender 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.

(4) *Revocation of preferred lender status.* The Agency may revoke a lender's preferred lender status at any time during the four-year term for cause. Any of the following instances constitute cause for revoking or not renewing preferred lender status:

(i) Violation of a term of the Lender's Agreement;

(ii) Failure to maintain preferred lender 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 loan programs loans in accordance with this part;

(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 its loan origination and servicing policies and procedures accepted by the Agency; or

(ix) Failure to reimburse the holder the amount of repurchase, with accrued interest, in accordance with § 5001.17(i)(1).

§ 5001.10 [Reserved]

Basic Guarantee Application Provisions

§ 5001.11 Guarantee application process.

(a) *Beginning the process.* Any lender may submit a pre-application or a full application to begin an application for guarantee.

(1) *Pre-application.* Based on the information in the pre-application, the Agency will make an informal assessment of the eligibility of the borrower and project. The Agency will provide written informal comments regarding the pre-application's strengths and weaknesses. The Agency's assessment may change based on subsequently submitted information, is solely advisory in nature, does not obligate the Agency to approve a guarantee request, and is not considered a favorable or adverse decision by the Agency.

(2) *Guarantee application.* For each guarantee request, the lender must submit to the Agency an application that is in conformance with § 5001.12.

(b) *Guarantee application evaluation.* All loan guarantee applications will be evaluated according to this part.

(1) The Agency will notify the lender in writing of its decision.

(2) In the evaluation of the application, the Agency may require the lender to obtain additional assistance in those areas where the lender does not have the requisite expertise to originate or service the loan. For the purposes of this paragraph ''those areas'' mean:

(i) The type and complexity of the financing (e.g., asset based financing, cash flow financing, bond financing), and

(ii) The industries with which the lender has little or no origination and/or servicing experience.

(c) *Loan approval and issuing the guarantee.* Complete applications from preferred lenders will be approved, subject to the availability of funds, or rejected not later than 10 business days after receipt. For the purpose of determining the application processing timeframes, an application will not be considered complete until all information required to make an approval decision, including a completed environmental review, is received by the Agency.

§ 5001.12 Application for Loan Guarantee Content.

All loan guarantee applications must contain the information specified in paragraph (a) of this section for approved lenders and in paragraph (b) of this section for preferred lenders.

(a) *Approved lender loan guarantee applications.* Loan guarantee applications from approved lenders must contain the following:

(1) Agency-approved application forms;

(2) Lender's analysis and credit evaluation (conforming to § 5001.16(b));

(3) Environmental information required by the Agency to conduct its environmental reviews (as specified in § 5001.16(h));

(4) Technical reports, energy audits, and energy assessments (as specified in subpart B of this part);

(5) Appraisals acceptable to the Agency, if available;

(6) Business plan, unless the information is contained in the feasibility study or in the lender's analysis;

(7) Feasibility study (as specified in subpart B);

(8) If the application is for 5 or more residential units, including nursing homes and assisted-living centers, an Affirmative Fair Housing Marketing Plan that is in conformance with 7 CFR 1901.203(c)(3);

(9) Current credit reports or equivalent on the borrower and any other person liable for the debt, except for public bodies;

(10) Financial statements as follows:

(i) For borrowers that have been in existence for one or more years,

(A) The most recent audited financial statements of the borrower if the guaranteed loan is $3 million or more, unless alternative financial statements are authorized by the Agency; or

(B) The most recent audited or Agency-acceptable financial statements of the borrower if the guaranteed loan is less than $3 million.

(ii) For borrowers that have been in existence for less than one year, the most recent Agency-authorized financial statements of the borrower regardless of the amount of the guaranteed loan request.

(iii) Depending on the complexity of the project and the financial condition of the borrower, the Agency may request additional financial statements and additional related information; and

(11) Any other information as determined by the Agency is necessary to evaluate the application.

(12) If the lending entity is not yet an approved lender, the application for lender approval specified in § 5001.9(b) or (c), as applicable.

(b) *Preferred lender loan guarantee applications.* Loan guarantee applications from preferred lenders must contain the following:

(1) A copy of the Application for Loan Guarantee;

(2) Information sufficient for the Agency to confirm project and borrower eligibility;

(3) A copy of lender's loan evaluation and analysis;

(4) An internal loan approval document showing approval by in-house appropriate office/committee; and

(5) Environmental information required by the Agency to conduct its environmental reviews (as specified in § 5001.16(h)).

§§ 5001.13–5001.14 [Reserved]

Basic Lender Provisions

§ 5001.15 Lender responsibilities—General.

(a) Lenders must ensure that proposals for facilities seeking a guarantee under this part comply with all Federal, State, and local laws and regulatory rules that are in existence and that affect the project, the borrower, or lender activities.

(b) Any lender involved in any manner with any guarantee under this part must cooperate fully with all oversight and monitoring efforts of the Agency or its representatives as specified in § 5001.4.

(c) Any action or inaction on the part of the Agency does not relieve the lender of its responsibilities to originate and service the loan guaranteed under this part.

(d) The lender must notify the Agency of any changes to its loan origination and servicing policies and procedures provided under § 5001.9(a). For any changes to the lender's loan origination and servicing policies and procedures that are inconsistent with the requirements of this part, the lender must notify the Agency in writing and receive written Agency approval prior to applying the changes to loan guarantees under this part.

(e) The lender must compile and maintain in its files a complete application for each guaranteed loan for at least one year after the final loss has been paid.

(f) The lender must maintain internal audit and management control systems to evaluate and monitor the overall quality of its loan origination and servicing activities.

§ 5001.16 Lender responsibilities—Origination.

(a) *General.* The lender is responsible for originating all loans in accordance with its loan origination policies and procedures at the time the loan is made and with the requirements of this part. Where a lender's loan origination policies and procedures address a corresponding requirement in this part, the lender must comply with whichever is more stringent, unless otherwise approved by the Agency.

(1) The Agency may require, at its discretion, an independent credit risk analysis (e.g., a credit rating or assessment).

(2) The lender must provide the Agency the lender's classification of the loan no later than 90 days after loan closing.

(b) *Credit evaluation.* For all applications for guarantee, the lender must prepare a credit evaluation that is consistent with Agency standards found in this part and with the policies and procedures of the lender submitting the application. Where a lender's policies and procedures address a corresponding requirement in this part, the lender must comply with whichever is more stringent, unless otherwise provided in paragraph (a) of this section. An acceptable credit evaluation must:

(1) Use credit documentation procedures and an underwriting process that are consistent with generally accepted commercial lending practices, and the lender's own policies, procedures, and lending practices, and

(2) Include an analysis of the credit factors associated with each guarantee application to ensure loan repayment,

including consideration of each of the following five elements.

(i) *Credit worthiness*. Those financial qualities that generally impel the borrower to meet its obligations as demonstrated by its credit history.

(ii) *Cash flow*. A borrower's ability to produce sufficient cash to repay the loan as agreed.

(iii) *Capital*. The financial resources that the borrower currently has and those it is likely to have when payments are due. The borrower must be adequately capitalized.

(iv) *Collateral*. The assets pledged by the borrower in support of the loan. Adequacy will be based on market value. For the purchase of cooperative stock, the lender must at least secure the loan with a lien on the stock acquired with loan funds, an assignment of any patronage refund, and the full and unconditional personal, partnership, or corporate guarantee of the borrower.

(v) *Conditions*. The general business environment and status of the borrower's industry.

(c) *Appraisals*. Lenders are required to provide real property and chattel collateral appraisals conducted by an independent qualified appraiser in accordance with the Uniform Standards of Professional Appraisal Practices or successor standards. Complete appraisals must be submitted to the Agency before loan closing.

(1) All appraisals used to establish the fair market value of the real property must not be more than 1 year old.

(2) All appraisals will include consideration of the potential effects from a release of hazardous substances or petroleum products or other environmental hazards on the market value of the collateral as determined in accordance with the appropriate ASTM Real Estate Assessment and Management environmental standards.

(d) *Personal, partnership, and corporate guarantees*.

(1) Secured, unconditional personal, partnership, and corporate guarantees may be used to determine the security of the loan. Unsecured, unconditional personal, partnership, and corporate guarantees will not be considered in determining whether a loan is adequately secured for loan making purposes.

(2) Agency-approved, unsecured personal, partnership, and corporate guarantees for the full term of the loan and at least equal to the guarantor's percent interest in the borrower, times the loan amount are required from those owning greater than a 20% interest in the borrower, unless the lender documents to the Agency's satisfaction that collateral, equity, cash flow, and profitability indicate an above-average ability to repay the loan. When warranted by an Agency assessment of potential financial risk, Agency-approved guarantees may also be required of parent, subsidiaries, or affiliated companies (owning less than a 20% interest in the borrower) and require security for any guarantee provided under this section. Exceptions to the requirement for personal guarantees must be requested by the lender and approved by the Agency on a case-by-case basis. The lender must document that collateral, equity, cash flow, and profitability indicate an above-average ability to repay the loan.

(3) The guarantors will execute an Agency-approved unconditional guarantee form.

(i) Any amounts paid by the Agency on account of liabilities of an Agency guaranteed loan borrower will constitute a Federal debt owed to the Agency by the guaranteed loan borrower. In such case, the Agency may use all remedies available to it, including offset under the Debt Collection Improvement Act of 1996, to collect the debt from the borrower.

(ii) Any amounts paid by the Agency pursuant to a claim by a guaranteed program lender will constitute a Federal debt owed to the Agency by a third-party guarantor of the loan, to the extent of the amount of the third-party guarantee. In such case, the Agency may use all remedies available to it, including offset under the Debt Collection Improvement Act of 1996, to collect the debt from the third-party guarantor.

(iii) In all instances under paragraphs (d)(3)(i) and (ii) of this section, interest charges will be assessed in accordance with 7 CFR 1951.133.

(e) *Design requirements*. The lender must ensure that all projects are designed utilizing accepted architectural and engineering practices, taking into consideration any Agency comments when the facility is being designed, and conform to applicable Federal, State, and local codes and requirements or other Agency-approved code. The lender must also ensure that the planned project will be fully constructed, within the approved budget, to facilitate completion of the loan purpose and will be suitable, once completed, for the borrower's needs in accordance with the borrower's loan application.

(f) *Monitoring requirements*. The lender must monitor the progress of construction and ensure that construction conforms to applicable Federal, State, and local code requirements and proceeds in accordance with the approved plans, specifications, and contract documents. The lender must also ensure that funds are used for eligible project costs. The lender must expeditiously report any problems in project development to the Agency.

(g) *Compliance with other Federal laws*. Lenders must comply with other applicable Federal laws including Equal Employment Opportunities, Americans with Disabilities Act, Equal Credit Opportunity Act, Fair Housing Act, and the Civil Rights Act of 1964.

(h) *Environmental responsibilities*. The lender must ensure that the borrower has:

(1) Provided the necessary environmental information to enable the Agency to undertake its environmental review process in accordance with subpart G of either 7 CFR part 1940 or 7 CFR part 1794 or successor regulations, including the provision of all required Federal, State, and local permits;

(2) Complied with any mitigation measures required by the Agency; and

(3) Not taken any actions or incurred any obligations with respect to the proposed project that would either limit the range of alternatives to be considered during the Agency's environmental review process or which would have an adverse effect on the environment.

(i) *Conflicts of interest*. The lender must report to the Agency all conflicts of interest and appearances of conflicts of interest.

(j) *Surety*. Surety will be required in cases when the guarantee will be issued prior to completion of construction unless the contractor will receive a lump sum payment at the end of work. Surety will be made a part of the contract, if the applicant requests it or if the contractor requests partial payments for construction work. In such cases where no surety is provided and the project involves pre-commercial technology, first of its type in the U.S., or new designs without sufficient operating hours to prove their merit, a latent defects bond may be required to cover the work.

§ 5001.17 Lender's responsibilities—Servicing.

(a) *General*. The lender is responsible for servicing the loan in accordance with the Lender's Agreement, this part, and its loan servicing policies and procedures. Where a lender's loan servicing policies and procedures address a corresponding requirement in this part or in the Lender's Agreement, the lender must comply with whichever is more stringent, unless otherwise approved by the Agency.

(1) The lender must ensure that the borrower has obtained, and will maintain for the life of the loan, all necessary insurance coverage appropriate to the proposed project.

(2) If the Agency determines that the lender is not in compliance with its servicing responsibilities, the Agency reserves the right to take any action the Agency determines necessary to protect the Agency's interests with respect to the loan. If the Agency exercises this right, the lender must cooperate with the Agency. Any cost to the Agency associated with such action will be assessed against the lender.

(b) *Certification.* The lender will certify in the Lender's Agreement that it will service the guaranteed loan according to Agency requirements and the lender's servicing policies and procedures and that, where the lender's policies and procedures address corresponding requirements of this part, it will comply with whichever is more stringent, unless otherwise provided in paragraph (a) of this section.

(c) *Audits.* When applicable, the lender will require an audit of the borrower in accordance with Office of Management and Budget requirements.

(d) *Financial reports.* Lenders are required to submit financial reports of the borrower as specified in paragraphs (d)(1) and (d)(2) of this section.

(1) For regulated or supervised lenders, the information that would be contained in financial reports required by the appropriate regulatory institution. Unless otherwise provided in the Conditional Commitment, such information must be submitted at the same time it should be made available to the appropriate regulatory institution.

(2) For other lenders, financial reports as required in the Conditional Commitment.

(e) *Collateral inspection and release.* The lender must inspect the collateral as often as necessary to properly service the loan. The Agency will require prior approval of the release of collateral, except in those instances where the proceeds are used to pay down debt in order of lien priority, or to acquire replacement equipment, or where the release of collateral is made under the abundance of collateral provision of the applicable security agreement. Appraisals on the collateral being released will be required on all transactions exceeding $250,000 and will be at the expense of the borrower. The appraisal must meet the requirements of § 5001.16(c). The sale or release of collateral must be based on an arm's length transaction, unless otherwise approved by the Agency in writing.

(f) *Transfers and assumptions.*

(1) *General.* Any time that a third party assumes a loan guaranteed under this part, it shall be processed and approved by the Agency as if it were a new loan guarantee.

(2) *Processing transfers and assumptions.* Subject to Agency approval, the lender may release the transferor (including any guarantor) from liability, regardless of the amount of the loan being transferred or assumed.

(i) Loan terms cannot be changed unless previously approved in writing by the Agency with the concurrence of the holder and transferor (including guarantor if it has not been released from personal liability). Any new loan term cannot exceed those authorized in this part as measured from the date the loan was initially guaranteed.

(ii) In the case of a transfer and assumption of less than the outstanding balance, the lender (if holding the guaranteed portion) may file an estimated Report of Loss with respect to the difference.

(iii) The transferor, including any guarantor, may be released from liability only with prior Agency written concurrence and only when the value of the collateral being transferred is at least equal to the amount of the loan being assumed and is supported by a current appraisal and a current financial statement. The Agency will not pay for the appraisal. If the transfer is for less than the debt, the lender must demonstrate to the Agency that the transferor and guarantors have no reasonable debt-paying ability considering their assets and income in the foreseeable future.

(3) *Transfer fees.* The Agency may charge the lender a nonrefundable transfer fee at the time of a transfer application. The Agency will set the amount of the transfer fee in an annual notice of funds availability.

(g) *Mergers.* All borrower mergers require prior approval by the Agency and the lender. If a borrower merges without Agency approval, the lender must accelerate the loan unless subsequently agreed to in writing by the Agency.

(h) *Subordination of lien position.* A subordination of the lender's lien position must be requested in writing by the lender and concurred with in writing by the Agency in advance of the subordination. Agency concurrence requires that:

(1) The subordination be in the best financial interest of the Agency;

(2) The lien to which the guaranteed loan is subordinated is for a fixed dollar limit;

(3) Lien priorities remain for the portion of the loan that was not subordinated; and

(4) The subordination of line of credit does not extend the term of the line of credit and in no event exceeds more than 3 years.

(i) *Repurchases from holder(s).* The holder may make written demand on the lender or the Agency to repurchase the unpaid guaranteed portion of the loan in the case of borrower monetary default or failure of the lender to pay the holder its pro-rata share. When the lender and the Agency determine that repurchase is necessary to adequately service the loan, the holder must sell the guaranteed portion to the requesting entity.

(1) *Repurchases by lender.* The lender must respond to the holder's demand within 30 days and will notify the Agency in writing of its decision, including notifying the Agency in writing of all repurchases it makes. When repurchased, the lender will accept an assignment without recourse from the holder upon repurchase. All repurchases must be for an amount equal to the holder's interest in the unpaid principal balance of the guaranteed portion and accrued interest less the lender's servicing fee and cover the principal and interest on the guaranteed loan accruing only up to 90 days after the date of the demand by the holder.

(2) *Repurchase by Lender for Servicing.* If, in the opinion of the lender, repurchase of the guaranteed portion of the loan is necessary to adequately service the loan, the holder will sell the portion of the loan to the lender for an amount equal to the unpaid principal and interest on such portion less lender's servicing fee. The Loan Note Guarantee will not cover the note interest to the holder on the guaranteed loan accruing after 90 days from the date of the demand letter of the lender or the Agency to the holder requesting the holder to tender its guaranteed portion.

(i) The lender will not repurchase from the holder for arbitrage purposes or other purposes to further its own financial gain.

(ii) Any repurchase will only be made after the lender obtains Agency written approval.

(iii) If the lender does not repurchase the portion from the holder, the Agency at its option may purchase such guaranteed portions for servicing purposes.

(3) *Repurchases by Agency.* When the Agency repurchases the loan, the holder must submit a specific written demand to the Agency, along with appropriate documentation. The Agency will be subrogated to all rights of the holder and, subject to satisfactory documentation, will purchase the unpaid principal and interest of the guaranteed portion to date of repurchase less the lender's servicing fee within 30 days after receipt of the demand. The lender may not charge the Agency any fees.

(i) The lender shall use a form approved by the Agency to send the guaranteed loan payments to the Agency on all loans repurchased by the Agency from holders.

(ii) Any purchase by the Agency does not change, alter, or modify any of the lender's obligations to the Agency arising from the loan or guarantee and does not waive any of the Agency's rights against the lender, borrower, or guarantor.

(iii) All repurchases must be for an amount equal to the holder's interest in the unpaid principal balance of the guaranteed portion and accrued interest less the lender's servicing fee and cover the principal and interest on the guaranteed loan accruing only up to 90 days after the date of the demand by the holder.

(j) *Additional expenditures and loans.* The lender may make additional expenditures or new loans to a borrower with an outstanding loan guaranteed under this part without obtaining prior written Agency approval unless the expenditure or loan will violate one or more of the loan covenants of the borrower's loan agreement.

(k) *Lender failure.* In the event a lending institution fails or ceases servicing the loan, the Agency will provide instruction to the successor entity on a case-by-case basis. Such instructions may include that the Agency may determine to service the entire loan or the guaranteed portion of the loan. In the event no successor entity can be determined, the Agency reserves the right to enforce the provisions of the loan documents on behalf of the lender or to purchase the lender's interest in the loan.

(l) *Delinquent loans.* The lender must service delinquent loans in accordance with the Lender's Agreement, its current servicing standards, and reasonable and prudent lending standards. If a borrower is delinquent more than 30 days, the lender must implement appropriate curative actions to resolve the problem. Any curative action that affects the return to the holder must receive the holder's concurrence. Any change in the repayment schedule must be limited to the remaining life of the collateral. Any loan performing in accordance with a curative action will no longer be delinquent.

(m) *Protective advances.* The following conditions apply to protective advances associated with guaranteed loans under this part.

(1) Protective advances are allowed only when they are necessary to preserve the value of the collateral and must be reasonable with respect to the outstanding loan amount and the value of the collateral being preserved.

(2) Protective advances will not include attorneys' fees or advances in lieu of additional loans.

(3) The lender must obtain written Agency approval for any protective advance that will singularly or cumulatively amount to more than $200,000 or 10% of the guaranteed loan, whichever is less.

(4) Protective advances must constitute an indebtedness of the borrower to the lender and be secured by the security instruments.

(5) Notwithstanding § 5001.7(j), upon Agency approval, protective advances can be used to pay Federal tax liens and other Federal debt.

(6) Protective advances and interest thereon at the note rate will be guaranteed at the same percentage of loss as provided in the Loan Note Guarantee.

(7) The maximum loss to be paid by the Agency will be determined according to the procedures specified in § 5001.17(p)(1) regardless of any protective advances made.

(n) *Liquidation.* The lender may liquidate a loan when one or more incidents of default or third party actions occur that the borrower cannot or will not cure or eliminate within a reasonable period of time. The Agency reserves the right to unilaterally conclude that liquidation is necessary and require the lender to assign the security instruments to the Agency and the Agency will then liquidate the loan.

(1) *Liquidation by the lender.* The lender must develop, in consultation with the Agency, a liquidation plan to determine the best course of action. The plan must include all aspects of liquidation, including, but not limited to reports to, the Agency, protection of collateral, loss payment, transmission of proceeds to the Agency, and future recovery.

(i) *Liquidation plan.* The lender must submit its liquidation plan to the Agency for approval at least 30 days before implementing the plan. The Agency will approve or disapprove the plan within 30 days. Upon approval of the liquidation plan by the Agency, the lender may implement the plan. The Agency must be notified of any changes to or deviations from the plan.

(ii) *Appraisals.* Liquidation appraisals must be a part of the liquidation planning process. They are not required for liquidation plan approval, provided they are obtained prior to the completion of the liquidation. If the outstanding principal loan balance including accrued interest is more than $200,000, the lender will obtain an independent appraisal report on all collateral securing the loan, which will reflect the current market value and potential liquidation value.

(iii) *Appraisal costs.* Any independent appraiser's fee will be shared equally by the Agency and the lender. If an environmental site assessment in accordance with the appropriate ASTM Real Estate Assessment and Management environmental standards of the property is necessary in connection with liquidation, the cost will be shared equally between the Agency and the lender.

(iv) *Rent.* Any net rental or other income that has been received by the lender from the collateral will be applied on the guaranteed loan debt.

(2) *Compromise settlement and release of personal guarantors.* A compromise settlement may be considered at any time. Before a guarantor is released from liability, the Agency must concur with the lender. Upon agreement, the lender may proceed to effect a compromise settlement.

(o) *Litigation.* In all litigation proceedings involving the borrower, the lender is responsible for protecting the rights of the lender or the Agency with respect to the loan, and keeping the Agency adequately and regularly informed, in writing, of all aspects of the proceedings. If the Agency determines that the lender is not adequately protecting the rights of the lender or the Agency with respect to the loan, the Agency reserves the right to take any legal action the Agency determines necessary to protect the rights of the lender, on behalf of the lender, or the Agency with respect to the loan. If the Agency exercises this right, the lender must cooperate with the Agency. Any cost to the Agency associated with such action will be assessed against the lender.

(p) *Loss calculations and payment.* Estimated losses are calculated from principal and accrued interest. From this amount deduct prior liens, net value of collateral, and other funds. Final losses include principal, protective advances, and accrued interest minus any estimated loss paid.

(1) The maximum loss allowed is the lower of:

(i) Any loss sustained by the lender on the guaranteed portion including:

(A) Principal and interest indebtedness as evidenced by said notes or by assumption agreements, and

(B) Principal and interest indebtedness on secured protective advances for protection and preservation of collateral made with the Agency's authorization, including but not limited to, advances for taxes, annual assessments, any ground rents, and hazard or flood insurance premiums affecting the collateral, or

(ii) The guaranteed principal advanced to or assumed by the borrower under said notes or assumption agreements and any interest due thereon.

(2) Accrued interest will be handled as specified in paragraphs (p)(2)(i) through (iv) of this section.

(i) If the Agency conducts the liquidation of the loan, loss occasioned to the lender by accruing interest after the date the Agency accepts responsibility for liquidation will not be covered by the Loan Note Guarantee.

(ii) If the lender conducts the liquidation of the loan, accruing interest shall be covered by the Loan Note Guarantee to 30 days after liquidation of collateral when the lender conducts the liquidation expeditiously in accordance with the liquidation plan approved by the Agency.

(iii) Under no circumstances will the Agency pay more than 90 days of additional accrued interest once the liquidation plan is approved.

(iv) Upon payment of an estimated loss to the lender, interest accrual on the defaulted loan will be discontinued.

(3) During the course of any reorganization plan, the lender will request and revise estimated loss payments using Agency-approved forms. The estimated loss claim, as well as any revisions to this claim, will be accompanied by documentation to support the claim.

(4) In a chapter 9 or chapter 11 reorganization, the lender must obtain an independent appraisal of the collateral if so directed by the Agency. The Agency and the lender will share the appraisal fee equally.

(5) Final settlement of liquidation will be made with the lender after the collateral is liquidated (unless otherwise designated as a future recovery) or after settlement and compromise of all parties has been completed. The Agency retains the right to recover losses paid under the guarantee from any liable party.

(i) If the lender takes title to collateral, any loss will be based on the collateral value at the time the collateral is liquidated.

(ii) When the lender is conducting the liquidation and owns any of the guaranteed portion of the loan, the lender must submit an estimated loss claim when liquidation is expected to exceed 90 days.

(iii) Within 30 days after liquidation of all collateral, except for certain unsecured personal, partnership, or corporate guarantees as provided for in this section, the lender must prepare a final report of loss and submit it to the Agency. The Agency will not guarantee interest beyond this 30-day period other than for the period of time it takes the Agency to process the loss claim. Before Agency approval of any final loss report, the lender must account for all funds, disposition of the collateral, and costs incurred, and must provide any other information necessary for successful completion of the liquidation.

(iv) After a final loss has been paid by the Agency, any future funds recovered by the lender will be pro-rated between the Agency and the lender based on the original percentage of guarantee even if the Loan Note Guarantee has been terminated.

(v) In a bankruptcy, the lender will submit an estimated loss claim based on the final orders of the bankruptcy court's direction. The Agency will pay the lender the estimated final loss based on these directions.

(6) In response to a loss claim, the Agency may request and the lender must provide the Agency with a copy of the applicable loan origination and servicing policies and procedures in place for the loan.

(7) When the Agency finds the final report of loss to be proper in all respects, it will approve the final loss. If the loss is less than the estimated loss payment, the lender will reimburse the Agency for the overpayment plus interest at the note rate from the date of the estimated loss payment.

§§ 5001.18–5001.24 [Reserved]

Basic Borrower Provisions

§ 5001.25 Borrower responsibilities.

(a) *Federal, State, and local regulations.* Borrowers must comply with all Federal, State, and local laws and rules that are in existence and that affect the project including, but not limited to:

(1) Land use zoning;

(2) Health, safety, and sanitation standards as well as design and installation standards; and

(3) Protection of the environment and consumer affairs.

(b) *Permits, agreements, and licenses.* Borrowers must obtain all permits, agreements, and licenses that are applicable to the project.

(c) *Insurance.* The borrower is responsible for maintaining all hazard, flood, liability, worker compensation, and personal life insurance, when required, on the project.

(d) *Access to borrower's records.* Upon request by the Agency, the borrower will permit representatives of the Agency (or other agencies of the U.S. Department of Agriculture authorized by that Department or the U.S. Government) to inspect and make copies of any of the records of the borrower pertaining to any Agency guaranteed loan. Such inspection and copying may be made during regular office hours of the borrower or at any other time agreed upon between the borrower and the Agency.

§§ 5001.26–5001.29 [Reserved]

Basic Guarantee and Loan Provisions

§ 5001.30 General.

(a) *Underwriting.* All loans guaranteed by the Agency must be underwritten in accordance with the credit evaluation requirements specified in § 5001.16(b).

(b) *Conditions of guarantee.* A loan guarantee under this part will be evidenced by a Loan Note Guarantee issued by the Agency. Each lender will execute a Lender's Agreement.

(1) The entire loan will be secured by the same security with equal lien priority for the guaranteed and unguaranteed portions of the loan. The unguaranteed portion of the loan will neither be paid first nor given any preference or priority over the guaranteed portion.

(2) The lender will remain mortgagee or secured party of record notwithstanding the fact that another party may hold a portion of the loan.

(3) The holder of a guaranteed portion shall have all rights of payment, as defined in the Loan Note Guarantee to the extent of the portion purchased. The lender will remain bound by all obligations under the Loan Note Guarantee, Lender's Agreement, and Agency program regulations.

(4) The lender will receive all payments of principal and interest on the entire loan and will promptly remit to each holder a pro-rata share, less any lender servicing fee.

(5) No loan guaranteed by the Agency under this part will be conditioned on

any requirement that the borrower accept or receive electric service from any particular utility, supplier, or cooperative.

(c) *Full faith and credit.* A guarantee under this part constitutes an obligation supported by the full faith and credit of the United States and is not contestable except for fraud or misrepresentation by the lender or holder, as appropriate, when the lender or holder has actual knowledge, participates in, or condones such fraud or misrepresentation.

(1) A note that provides for the payment of interest on interest will not be guaranteed. Any claim against a Loan Note Guarantee or Assignment Guarantee Agreement that is attached to, or relating to, a note that provides for payment of interest on interest will be reduced to remove the interest on interest.

(2) The guarantee will not be enforceable by the lender to the extent any loss is occasioned by the violation of usury laws, negligent loan origination or servicing, or failure to obtain the required security regardless of the time at which the Agency acquires knowledge of the foregoing. Any losses occasioned by the lender will not be enforceable to the extent that loan funds are used for purposes other than those specifically approved by the Agency in its Conditional Commitment.

(3) When in the hands of a holder, the Loan Note Guarantee or Assignment Guarantee Agreement shall not cover interest accruing 90 days after the holder has demanded repurchase by the lender. When in the hands of a holder, the Loan Note Guarantee or Assignment Guarantee Agreement shall not cover interest accruing 90 days after the lender or Agency has requested the holder to surrender the evidence of debt for repurchase.

(4) The Agency will guarantee payment as follows:

(i) To any holder, 100% of any loss sustained by the holder on the guaranteed portion of the loan and on interest due on such portion.

(ii) To the lender, the lesser of:

(A) Any loss sustained by the lender on the guaranteed portion, including principal and interest evidenced by the notes or assumption agreements and secured advances for protection and preservation of collateral made with the Agency's authorization; or

(B) The guaranteed principal advanced to or assumed by the borrower and any interest due thereon.

(d) *Soundness of guarantee.* All loans guaranteed under this part must be financially sound and feasible, with reasonable assurance of repayment.

(e) *Rights and liabilities.* When a guaranteed portion of a loan is sold to a holder, the holder shall succeed to all payments of the lender under the Loan Note Guarantee to the extent of the portion purchased. A guarantee and right to require purchase will be directly enforceable by a holder notwithstanding any fraud or misrepresentation by the lender or any unenforceability of the guarantee by the lender, except for fraud or misrepresentation of which the holder had actual knowledge at the time it became the holder or in which the holder participates or condones. The lender shall not represent a Conditional Commitment as a guarantee. The Agency reserves the right to collect from the lender any payments made to the holder that would not have been payable to the lender had they been the holder.

(f) *Reduction of loss claims payable.* Negligent loan origination or servicing will result in reduction of loss claims payable under the guarantee to the lender if any losses have occurred as the result of such negligence. The extent of the reduction, which could be a total reduction, of the loss claims payable, will depend on the extent of the losses occasioned as the result of the negligent loan origination and servicing.

(g) *Write-downs.* Debt write-downs for an existing borrower where the same principals retain control of and decision-making authority for the business are prohibited.

§ 5001.31 Guaranteed loan requirements.

(a) *Interest rates.* Interest rates may be fixed or variable or a combination of both, as long as they are legal. Variable interest rates must be tied to an acceptable published index and the lender must incorporate the provision for adjustment of payment installments into the Note.

(1) *Negotiated rates.* Interest rates, interest rate caps, and incremental adjustment limitations will be negotiated between the lender and the borrower and will be subject to concurrence by the Agency.

(2) *Different rates on guaranteed and unguaranteed portion of the loan.* If the lender and borrower agree, the interest rate on the guaranteed portion of a loan may differ from the rate on the unguaranteed portion provided:

(i) The rate on the unguaranteed portion is equal to or below the market rate and does not exceed that currently being charged on loans for similar purposes to borrowers under similar circumstances; and

(ii) The rate on the guaranteed portion does not exceed the rate on the unguaranteed portion unless the rate on the guaranteed portion is fixed and the unguaranteed portion is variable.

(b) *Interest rate changes.*

(1) *General.* Any change in the interest rate between issuance of the Conditional Commitment and issuance of the Loan Note Guarantee:

(i) Must be approved in writing by the Agency, unless the only change is to the base rate of a variable interest rate;

(ii) Must be shown as an amendment to the Conditional Commitment; and

(iii) Are subject to the restrictions specified in paragraphs (b)(2) and (b)(3) of this section.

(2) *Reductions.* The borrower, lender, and holder (if any) may collectively effect a permanent or temporary reduction in the interest rate on the guaranteed loan at any time during the life of the loan by their written agreement, subject to the conditions specified in paragraphs (b)(1)(i) through (iii) of this section. The lender must keep sufficient records to allow the Agency to calculate any loss at the reduced interest rate. The lender must notify the Agency of all permanent interest rate reductions, as specified in § 5001.4(b)(3)(ii).

(i) After a permanent reduction, the Loan Note Guarantee will only cover losses of interest at the reduced interest rate.

(ii) In a final loss settlement when qualifying rate changes are made with the required written agreements and notification, the interest will be calculated for the periods the given rates were in effect. The lender must maintain records that adequately document the accrued interest claimed.

(iii) The lender is responsible for the legal documentation of interest-rate changes by an endorsement or any other legally effective amendment to the promissory note; however, no new notes may be issued. Copies of all legal documents must be provided to the Agency.

(3) *Increases.* Increases in interest rates are not permitted beyond what is provided in the loan documents. Increases from a variable interest rate to a higher interest rate that is a fixed rate are allowed, subject to concurrence by the Agency.

(c) *Term length.* The loan term will be based on the use of proceeds, the useful economic life of the assets being financed, and the borrower's repayment ability. In no event may the term exceed 40 years.

(d) *Loan schedule and repayment.* Repayment will be structured in accordance with this section and the Loan Agreement, and will be due and payable in accordance with the Note. Only loans that require a periodic payment schedule that will retire the debt over the term of the loan without a balloon payment will be guaranteed. Lenders must ensure that the principal balance of a guaranteed loan is properly amortized within the prescribed loan maturity.

(e) *Maximum loan amounts*. The maximum amount that may be guaranteed will be determined on a program-by-program basis and will be published each year in the **Federal Register**.

(f) *Maximum percent of guarantee*. The maximum guarantee is specified in subpart B of this part for each guaranteed loan program covered by this part.

(g) *Fees*. Each year, the Agency will establish, and publish in a **Federal Register** notice, the guarantee fee and renewal fee for each guaranteed loan program. A guarantee fee and a renewal fee will be assessed on each loan, as specified in the **Federal Register** notice. Both the guarantee fee and the renewal fee are nonrefundable.

(1) *Guarantee fee*. The guarantee fee will be paid to the Agency by the lender at the time the lender requests the Loan Note Guarantee. The fee may be passed on to the borrower.

(2) *Renewal fee*. As applicable, the renewal fee is assessed annually, is based on a fixed fee rate established at the time the loan is obligated, and will be calculated on the unpaid guaranteed principal balance as of close of business on December 31 of each year. The fee will be billed to the lender and may be passed on to the borrower.

(h) *Lender fees*. The lender may levy reasonable, routine, and customary charges and fees, including late payment fees, for the guaranteed loan provided they are similar to those charged other borrowers for the same type of loan for which a non-guaranteed borrower would be assessed. Default charges, late payment charges, and additional interest expenses will not be covered by the Loan Note Guarantee. Such charges may not be added to the principal and interest due under any guaranteed note.

§ 5001.32 Conditional commitment.

Upon approval of a loan guarantee application, the Agency will issue a Conditional Commitment to the lender containing conditions under which the Loan Note Guarantee will be issued.

(a) The lender shall certify in the Conditional Commitment that:

(1) The lender will monitor construction in accordance with approved plans and specifications, and

(2) Project funds will be used only for Agency-approved project costs.

(b) The lender may propose alternate conditions for Agency consideration.

(c) The lender must complete and sign the Acceptance of Conditions and return a copy to the Agency.

§ 5001.33 Conditions precedent to issuance of loan note guarantee.

Each of the conditions specified in paragraphs (a)(1) through (17) of this section must be met prior to the Agency's issuance of a Loan Note Guarantee under § 5001.34.

(a) The lender must certify in writing to each of the following conditions.

(1) No major changes have been made in the lender's loan conditions and requirements since the issuance of the Conditional Commitment, unless such changes have been approved by the Agency in writing.

(2) All planned property acquisition has been or will be completed, all development has been or will be substantially completed in accordance with plans and specifications, conforms with applicable Federal, state, and local codes, and costs have not exceeded the amount approved by the lender and the Agency.

(3) Required hazard, flood, liability, worker compensation, and personal life insurance, when required, are in effect.

(4) All truth-in-lending and equal credit opportunity requirements have been met.

(5) The loan 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.

(6) The borrower has marketable title to the collateral then owned by the borrower, subject to the instrument securing the loan to be guaranteed and to any other exceptions approved in writing by the Agency.

(7) When required, the entire amount of the loan for working capital has been disbursed except in cases where the Agency has approved disbursement over an extended period of time. 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.

(8) When required, personal, partnership, or corporate guarantees have been obtained.

(9) All requirements of the Conditional Commitment have been met.

(10) Lien priorities are consistent with the requirements of the Conditional Commitment. No claims or liens of laborers, subcontractors, suppliers of machinery and equipment, or other parties have been or will be filed against the collateral and no suits are pending or threatened that would adversely affect the collateral when the security instruments are filed.

(11) The loan proceeds have been or will be disbursed for purposes and in amounts consistent with the Conditional Commitment and the Application for Loan Guarantee. A copy of the detailed loan settlement of the lender must be attached to support this certification. Appropriate lender controls were utilized to ensure that all funds were properly disbursed, including funds for working capital.

(12) There has been no material change in the borrower's financial condition and no other adverse material change in the borrower during the period of time from the Agency's issuance of the Conditional Commitment to issuance of the Loan Note Guarantee regardless of the cause or causes of the change and whether or not the change or causes of the change were within the lender's or borrower's control. The lender must address any assumptions or reservations in the requirement and must address all material changes of the borrower, any parent, affiliate, or subsidiary of the borrower, and guarantors.

(13) None of the lender's officers, directors, stockholders, or other owners (except stockholders in an institution that has normal stock share requirements for participation) has a substantial financial interest in the borrower and neither the borrower nor its officers, directors, stockholders, or other owners has a substantial financial interest in the lender. If the borrower is a member of the board of directors or an officer of a Farm Credit System institution that is the lender, the lender will certify that a Farm Credit System institution on the next highest level will independently process the loan request and act as the lender's agent in servicing the account.

(14) The Loan Agreement includes all measures identified in the Agency's environmental impact analysis for this proposal (measures with which the borrower must comply) for the purpose of avoiding or reducing adverse environmental impacts of the proposal's construction or operation.

(15) For loans exceeding $150,000, the lender has certified its compliance with the Anti-Lobby Act (18 U.S.C. 1913). Also, if any funds have been, or will be, paid to any person for influencing or attempting to influence an officer or employee of any agency, a Member of Congress, an officer or employee of Congress, or an employee of a Member of Congress in connection with this commitment providing for the United

States to guarantee a loan, the lender shall completely disclose such lobbying activities in accordance with 31 U.S.C. 1352.

(16) Where applicable, the lender must certify that the borrower has obtained:

(i) A legal opinion relative to the title to rights-of-way and easements. Lenders are responsible for ensuring that borrowers have obtained valid, continuous, and adequate rights-of-way and easements needed for the construction, operation and maintenance of a facility.

(ii) A title opinion or title insurance showing ownership of the land and all mortgages or other lien defects, restriction or encumbrances, if any. It is the responsibility of the lender to ensure that the borrower has obtained and recorded such releases, consents, or subordinations to such property rights from holders of outstanding liens or other instruments as may be necessary for the construction, operation and maintenance of the facility and to provide the required security. For example, when a site is for major structures for utility-type facilities (such as a gas distribution system) and the lender and borrower are able to obtain only a right-of-way or easement on such site rather than a fee simple title, such a title opinion must be requested.

(17) The minimum financial criteria for a program for which a loan application has been submitted, including those financial criteria contained in the Conditional Commitment, have been maintained through the issuance of the Loan Note Guarantee. Failure to maintain these financial criteria shall result in an ineligible application.

(b) If the lender is unable to provide any of the certifications in paragraphs (a)(1) through (17) of this section, the lender must provide an explanation satisfactory to the Agency as to why the lender is unable to provide the certification.

§ 5001.34 Issuance of the guarantee.

The Agency, at its sole discretion, will determine if the conditions within the Conditional Commitment have been met. The Agency, at its sole discretion, will determine whether or not to issue the guarantee.

(a) *Loan agreement.* The lender must submit to the Agency a copy of the loan agreement between the lender and the borrower prior to loan closing.

(b) *Requesting guarantee.* The lender must provide the lender's certification and the guarantee fee at the time it requests the Loan Note Guarantee.

(c) *Issuance.* Upon the lender's compliance with requirements of the Conditional Commitment and certification in accordance with § 5001.33(a), the Agency will issue the Loan Note Guarantee.

(d) *Refusal to execute Loan Note Guarantee.* If the Agency determines that it cannot execute the Loan Note Guarantee, the Agency will promptly inform the lender of the reasons and give the lender a reasonable period within which to satisfy the objections. If the lender satisfies the objections within the time allowed, the guarantee will be issued.

(e) *Replacement of Loan Note Guarantee or Assignment Guarantee Agreement.* If the Loan Note Guarantee or Assignment Guarantee Agreement has been lost, stolen, destroyed, mutilated, or defaced, the Agency may issue a replacement to the lender or holder upon receipt from the lender of a notarized certificate of loss and an indemnity bond acceptable to the Agency. If the holder is the United States, a Federal Reserve Bank, a Federal Government corporation, a State or Territory, or the District of Columbia, an indemnity bond is not required.

§ 5001.35 Alterations of loan instruments.

Under no circumstances shall the lender alter or approve any alterations of the Loan Note Guarantee or any other loan instrument without the prior written approval of the Agency.

§ 5001.36 Reorganizations.

(a) *Change in borrower prior to closing.* Any change in borrower ownership or organization prior to the issuance of the Loan Note Guarantee must meet program eligibility requirements and be approved by the Agency prior to the issuance of the Conditional Commitment. Once the Conditional Commitment is issued, no substitution of borrower(s) or change in the form of legal entity will be approved, unless Agency approval, in writing, is obtained.

(b) *Transfer of lender prior to issuance of the Loan Note Guarantee.* Prior to issuance of a Loan Note Guarantee, the Agency may approve the transfer of an outstanding Conditional Commitment to another lender, provided no material changes have occurred in the borrower, project, or loan agreement.

(1) The present lender must submit the requested transfer in writing to the Agency and the Agency must approve the transfer.

(2) The other lender must be approved under this part.

(3) The other lender must execute a new application for guarantee in conformance with this part. If the transfer is from a preferred lender to an approved lender, the approved lender must submit an application in accordance with the requirements specified in § 5001.12(a).

(c) *Substitution of lender after issuance of the Loan Note Guarantee.* After the issuance of a Loan Note Guarantee, the lender shall not be substituted without the prior written approval of the Agency. A substitution of the lender must be requested in writing by the borrower, the proposed substitute lender, and the original lender if still in existence. The Agency may approve the substitution of a lender if the new lender is Rural Development approved; agrees in writing to acquire title to any unguaranteed portion of the loan held by the original lender; and assumes all original loan requirements and lender responsibilities. The Agency will not pay any loss or share in any costs with a lender who is not in compliance with this section.

§ 5001.37 Sale or assignment of guaranteed loan.

(a) *General.* The lender may sell part of the guaranteed portion of the loan, subject to the conditions specified in paragraphs (a)(1) through (5) of this section.

(1) Any sale or assignment by the lender of the guaranteed portion of the loan must be accomplished in accordance with the conditions in the Lender's Agreement.

(2) The lender may obtain participation in the loan under its normal operating procedures; however, the lender must retain a minimum of 5% of the total loan amount in its portfolio. The amount required to be retained must be of the unguaranteed portion of the loan and cannot be participated.

(3) The lender must not sell or participate any amount of the guaranteed, or non-guaranteed, portion of the loan to the borrower or members of the borrower's immediate family, the borrower's officers, directors, stockholders, other owners, or a parent, subsidiary, or affiliate.

(4) Disposition of the guaranteed portion of a loan may not be made prior to full disbursement, completion of construction, and acquisition of real estate and equipment without the prior written approval of the Agency.

(5) If the lender desires to sell all or part of the guaranteed portion of the loan subsequent to loan closing, the loan must not be in monetary default.

(b) *Servicing fee.* The lender cannot charge the Agency a servicing fee and no such fees are covered under the guarantee.

(c) *Distribution of proceeds.* All loan payments and collateral proceeds received will be applied to the guaranteed and unguaranteed portions of the loan on a pro rata basis.

§ 5001.38 Termination of loan note guarantee.

Each Loan Note Guarantee issued under this part will terminate automatically upon:

(a) Full payment of the guaranteed loan; or

(b) Full payment of any loss obligation or negotiated loss settlement except for future recovery provisions and payments made as a result of the Debt Collection Improvement Act of 1996. After final payment of claims to lenders and/or holders, the Agency will retain all funds received as the result of the Debt Collection Improvement Act of 1996; or

(c) Written request from the lender to the Agency that the guarantee will terminate 30 days after the date of the request, provided that the lender holds all of the guaranteed portion, and the original Loan Note Guarantee is returned to the Agency to be canceled.

§§ 5001.39–5001.100 [Reserved]

Subpart B—Program-Specific Provisions

§ 5001.101 Community Facilities Program.

(a) *Project eligibility.* To be eligible for a Community Facility guaranteed loan, the project must meet the criteria specified in paragraphs (a)(1) through (5) of this section and in § 5001.6, except as provided in paragraph (a)(6) of this section.

(1) *Eligible projects.* All loans guaranteed with community facility funding shall be for:

(i) Essential community facilities;

(ii) Community services or community-based social, recreational or cultural services;

(iii) Transportation infrastructure and support;

(iv) Hydroelectric generating facilities or supplemental and supporting structures for rural electrification only with advance written approval from the Agency;

(v) Natural gas distribution systems;

(vi) Acquisition of land and site preparation for industrial parks;

(vii) Refinancing debts (excluding working capital debt, operating or other debt whose repayment is scheduled to take place in one year or less). Refinancing debts incurred by, or on behalf of, an eligible borrower is allowed when all of the following conditions exist:

(A) The debts being refinanced are less than 50% of the total loan;

(B) The debts were incurred for the facility or service being financed or any part thereof (such as interim financing, construction expenses, etc.); and

(C) Arrangements cannot be made with the creditors to extend or modify the terms of the debts so that a sound basis will exist for making a loan; or

(viii) Notwithstanding § 5001.7(e), a leasehold interest is eligible for funding as determined by the Agency. At a minimum,

(A) The length of lease must be greater than or equal to loan term;

(B) There are no reverter clauses in the lease; and

(C) There are no restrictive clauses that would impair the use or value of the property as security for the loan.

(2) *Facilities for public use.* All facilities financed under the provisions of this section shall be for public purposes.

(i) Facilities will be installed to serve any user within the service area who desires service and can be feasibly and legally served.

(ii) The lender will determine that, when feasibly and legally possible, inequities within the proposed project's service area for the same type service proposed (e.g., gas distribution systems) will be remedied by the owner on, or before, completion of the project. Inequities are defined as unjustified variations in availability, adequacy, or quality of service. User rate schedules for portions of existing systems or facilities that were developed under different financing, rates, terms, or conditions do not necessarily constitute inequities.

(3) *Leased space.* A facility will remain eligible for Community Facility funding provided:

(i) The facility has less than 25% of its floor space occupied by ineligible organizations or activities; and

(ii) The ineligible organization and the ineligible commercial activity are related to and enhance the primary purpose for which the facility is being established by the borrower.

(4) *Facility location.* Facilities must be located in rural areas, except as follows:

(i) For utility services, such as natural gas or hydroelectric, serving both rural and non-rural areas, Agency funds may be used to finance only that portion serving rural areas, regardless of facility location.

(ii) For telecommunication projects, the part of the facility located in a non-rural area must be necessary to provide the essential services to rural areas.

(5) *Serve rural area.* The project must primarily serve a rural area.

(6) *Demonstration of community support.* A project may demonstrate community support in lieu of the debt-to-tangible net worth ratio required under § 5001.6(b)(2) and in lieu of the loan-to-value ratio required under § 5001.6(b)(3).

(i) Evidence of community support in the form of a certification of support for each project or facility from any affected local government body is required.

(ii) With the exceptions of essential community facilities owned by a local public body or a Federally-recognized Indian tribe serving local residents or tribal members, a certificate of support must be obtained from each affected local government within the service area of the facility. The certificate of support must be signed by an authorized official of the local government.

(iii) The certificate of support should include sufficient information to determine that a community facility will provide needed services to the community and will have no adverse impact on other community facilities providing similar services. The organization is required to provide sufficient information to affected local governments as may be needed to obtain the certificate of support.

(b) *Unauthorized projects and purposes.* Loan funds may not be used to finance:

(1) Facilities that are 25% or more for the purpose of housing Federal or State agencies;

(2) Community antenna television services or facilities;

(3) Telephone systems;

(4) Facilities that are not modest in size, design, and cost;

(5) Racetracks, water parks, and ski slopes.

(c) *Borrower eligibility.* In addition to the requirements specified in subpart A of this part, an eligible borrower must also meet the following requirements where applicable:

(1) *Borrowers.* An eligible borrower must be:

(i) A public body such as a municipality, county, district, authority, or other political subdivision of a State located in a rural area;

(ii) A not-for-profit entity such as an association, cooperative, or private corporation; or

(iii) An Indian tribe on Federal and State reservations and other federally recognized Indian tribes.

(2) *Other eligible borrowers.* The following organizations are also eligible borrowers under this subpart: The YMCA, YWCA, Girl Scouts, and Boy Scouts.

(3) *Community ties.* A private not-for-profit essential community facility (other than utilities) must have significant ties with the local rural community. Such ties are necessary to ensure to the greatest extent possible that a facility under private control will carry out a public purpose and continue to primarily serve rural areas. Ties may be evidenced by items such as:

(i) Association with, or controlled by, a local public body or bodies or broadly based ownership and controlled by members of the community.

(ii) Substantial public funding through taxes, revenue bonds, or other local government sources, or substantial voluntary community funding such as would be obtained through a community-wide funding campaign.

(4) *Credit not available elsewhere.* The Agency must determine that the borrower is unable to obtain the required credit without the loan guarantee from private, commercial, or cooperative sources at reasonable rates and terms for loans for similar purposes and periods of time.

(d) *Additional application documentation provisions.* In addition to the application requirements specified in § 5001.12, lenders shall submit the following as applicable:

(1) *Feasibility study.* A feasibility study by a qualified consultant may be required by the Agency.

(2) *Organizational documents.* A copy of the complete organizational documents of the borrower.

(3) *Board Members.* A complete list of governing board members of the borrower.

(4) *Management agreement and other legal documents.* A copy of the management agreement and other legal documents between the borrower and the proposed management company.

(5) *Preliminary architectural report.* A preliminary architectural report conforming to customary professional standards. This report may be submitted to the Agency prior to the balance of the application material if a preliminary review by the Agency is desired.

(e) *Additional application processing requirements—appraisals.* When a loan's collateral appraises at a level less than 100% of the loan amount, the Agency will consider community support in evaluating the application for guarantee.

(f) *Additional origination responsibilities—leasehold interest.* Subject to approval by the Agency, a leasehold interest may be used as collateral for loans under this section provided the leasehold interest meets each of the conditions specified in paragraphs (a)(1)(viii)(A) through (C) of this section.

(g) *Additional servicing responsibilities—financial reports.* Annual financial reports required shall conform to 7 CFR part 3052.

(h) *Additional guarantee- and loan-related requirements.*

(1) *Funding limit.* The principal amount of a Community Facility loan guaranteed under this section may not exceed $50 million.

(2) *Maximum percent of guarantee.* The maximum loan guarantee issued to a Rural Development approved lender with Community Facilities funding is 90%.

(3) *Parity lien requirements.* Whenever both a Community Facilities guaranteed loan and a Community Facilities direct loan are utilized to finance a single project, the Agency will require a parity lien, unless the lender cannot meet its regulatory requirements.

§ 5001.102 Water and Waste Disposal Facilities Program.

(a) *Project eligibility.* To be eligible for a Water and Waste Disposal Facilities guaranteed loan, the project must meet the criteria specified in paragraphs (a)(1) through (3) of this section and in § 5001.6, except as provided in paragraph (a)(4) of this section.

(1) *Eligible projects and costs.* All loans guaranteed with Water and Waste Disposal funding shall be for:

(i) A water, waste disposal, solid waste disposal or storm water facility;

(ii) Payment of other utility connection charges as provided in service contracts between utility systems; or

(iii) Refinancing any loan. Except for the refinancing of Agency direct loans, refinancing of other loans will be limited to a minority portion of the guaranteed loan.

(2) *Facilities for public use.* All facilities financed under the provisions of this section shall be for public purposes.

(i) Facilities will be installed to serve any user within the service area who desires service and can be feasibly and legally served.

(ii) The lender will determine that, when feasible and legally possible, inequities within the proposed project's service area for the same type service proposed will be remedied by the owner on, or before, completion of the project. Inequities are defined as unjustified variations in availability, adequacy, or quality of service. User rate schedules for portions of existing systems or facilities that were developed under different financing, rates, terms, or conditions do not necessarily constitute inequities.

(3) *Serve rural area.* The project must primarily serve a rural area.

(4) *Demonstration of community support.* A project may demonstrate community support in lieu of the debt-to-tangible net worth ratio required under § 5001.6(b)(2) and in lieu of the loan-to-value ratio required under § 5001.6(b)(3). Demonstration of community support shall be made as specified in § 5001.101(a)(6)(i) through (iii).

(b) *Unauthorized projects and purposes.* Loan funds may not be used to finance:

(1) Facilities that are not modest in size, design, and cost;

(2) The construction of any new combined storm and sanitary sewer facilities;

(3) Any portion of the cost of a facility that does not serve a rural area;

(4) That portion of project costs normally provided by a business or industrial user, such as wastewater pretreatment;

(5) Rental for the use of equipment or machinery owned by the borrower;

(6) Any project where an individual, or membership of another organization sponsors the creation of a nonprofit organization with the intent to control negotiations for employment or contracts that provide financial benefit to the sponsoring organization, affiliate organization, or a subsidiary organization of the sponsoring individuals or organization; or

(7) For other purposes not directly related to operating and maintenance of the facility being installed or improved.

(c) *Borrower eligibility.* To be eligible for a Water and Waste Disposal Facilities guaranteed loan, a borrower must meet the criteria specified in paragraphs (c)(1) and (2) of this section and in § 5001.8(a)(1) and (2).

(1) *Eligible entity.* The borrower must be one of the following types of entities:

(i) A public body such as a municipality, county, district, authority, or other political subdivision of a State located in a rural area;

(ii) An organization operated on a not-for-profit basis, such as an association, cooperative, or private corporation. The organization must be an association controlled by a local public body or bodies, or have a broadly based ownership by or membership of people of the local community; or

(iii) An Indian tribe on a Federal or State reservation or any other Federally-recognized Indian tribe.

(2) *Credit not available elsewhere.* The Agency must determine that the borrower is unable to obtain the required credit without the loan guarantee from private, commercial, or

cooperative sources at reasonable rates and terms for loans for similar purposes and periods of time.

(d) *Additional lender approval requirements.* The examination required under § 5001.9(c)(1)(iv) may be conducted by the Agency or a qualified consultant.

(e) *Additional application documentation provisions.* In addition to the application requirements specified in § 5001.12, lenders shall submit the following as applicable:

(1) *Feasibility study.* A feasibility study by a qualified consultant may be required by the Agency.

(2) *Preliminary engineering report.* Two copies of the preliminary engineering report are to be submitted. Preliminary engineering reports must conform to customary professional standards. Preliminary engineering report guidelines for water, sanitary sewer, solid waste, and storm sewer are available from the Agency. The preliminary engineering report may be submitted to the Agency prior to the rest of the application material if a preliminary review by the Agency is desired.

(3) *Organizational documents.* A copy of the complete organizational documents of the borrower.

(4) *Board Members.* A complete list of governing board members of the borrower.

(5) *Management agreement and other legal documents.* A copy of the management agreement and other legal documents between the borrower and the proposed management company.

(6) *Intergovernmental consultation.* Intergovernmental consultation comments in accordance with 7 CFR part 3015, subpart V, of this title.

(f) *Additional lender servicing responsibilities—financial reports.* Annual financial reports required shall conform to 7 CFR part 3052.

(g) *Additional guarantee- and loan-related requirements—maximum percent of guarantee.* The maximum loan guarantee issued to a Rural Development approved lender with Water and Waste Disposal Facility funding is 90%.

§ 5001.103 Business and Industry Program.

(a) *Definitions.*

Locally or regionally produced agricultural food product. Any agricultural food product that is raised, produced, and distributed in:

(i) The locality or region in which the final product is marketed, so that the total distance that the product is transported is less than 400 miles from the origin of the product; or

(ii) The State in which the product is produced.

Underserved community. A community (including an urban or rural community and an Indian tribal community) that has, as determined by the Secretary:

(i) Limited access to affordable, healthy foods, including fresh fruits and vegetables, in grocery retail stores or farmer-to-consumer direct markets; and

(ii) A high rate of hunger or food insecurity or a high poverty rate.

(b) *Project eligibility.* To be eligible for a Business and Industry guaranteed loan, the project must meet the criteria specified in paragraphs (b)(1) through (b)(3) of this section, as applicable, and in § 5001.6.

(1) The project must be located in a rural area.

(2) All loans guaranteed with Business and Industry funding shall be for:

(i) Business and industrial acquisitions when the loan will keep the business from closing, prevent the loss of employment opportunities, or provide expanded job opportunities;

(ii) Business conversion, enlargement, repair, modernization, or development;

(iii) The purchase and development of land, easements, rights-of-way, buildings, or facilities;

(iv) The purchase of equipment, leasehold improvements, machinery, supplies, inventory, start up costs, working capital, pollution control and abatement, or feasibility studies;

(v) Transportation services incidental to industrial development;

(vi) Agricultural production, with advance written approval from the Agency, when it is not eligible for Farm Service Agency farmer program assistance and when it is part of an integrated business also involved in the processing of agricultural products;

(vii) The purchase of membership, stocks, bonds, or debentures or, as allowed under paragraph (a)(3) of this section, cooperative stock;

(viii) Commercial fishing, aquaculture, commercial nurseries, forestry, hydroponics, or the growing of mushrooms;

(ix) Interest during the period before the first principal payment becomes due or when the facility becomes income producing, whichever is earlier;

(x) Refinancing any loan when the Agency determines that the project is viable and equal or better rates or terms are offered. Same lender debt refinancing will be additionally required to be less than 50% of the new loan amount unless the amount of the loan to be refinanced is already Federally guaranteed. Subordinated owner debt is not eligible;

(xi) Providing takeout of interim financing when the lender submits a pre-application or a complete application in which the interim financing is proposed, prior to extending any portion of the interim loan;

(xii) Fees and charges for professional services (except for packager and broker fees) and routine lender fees and the Agency guarantee fee;

(xiii) Tourist and recreation facilities, including hotels, motels, and bed and breakfast establishments when the owner's living quarters is not included in the guaranteed loan;

(xiv) Educational, training, or community facilities;

(xv) Housing development sites with Agency-approved restrictions;

(xvi) Community antenna television services or facilities;

(xvii) Industries adjusting to terminated Federal agricultural programs or increased foreign competition;

(xviii) Mixed use commercial and residential buildings on a pro-rata basis (residential real estate use portion not eligible);

(xix) Notwithstanding § 5001.7(e), operating lines of credit that are part of an overall guaranteed loan financing package under this section and that are used for the payment of one or more of the following:

(A) Annual operating/business expenses;

(B) Debts advanced for the current operating cycle, excluding carry-over debt from previous operating cycles;

(C) Scheduled, non-delinquent term borrower debt; or

(D) Closing costs; or

(xx) Leasehold improvements, provided the underlying lease meets the requirements specified in § 5001.101(a)(1)(viii);

(xxi) The purchase of preferred stock or similar equity issued by a cooperative organization or a fund that invests primarily in cooperative organizations, if the guarantee significantly benefits one or more entities eligible for assistance for the purposes described in paragraph (d) of this section; or

(xxii) Establish and facilitate enterprises that process, distribute, aggregate, store, and market locally or regionally produced agricultural food products to support community development and farm and ranch income.

(3) *Purchase of cooperative stock.* Loans may be made to individual farmers or ranchers for the purchase of cooperative stock. The entity to receive the proceeds from the stock sale must be a farmer or rancher cooperative

established for the purpose of processing agricultural commodities. Proceeds from the stock sale may be used to recapitalize an existing cooperative, to develop a new processing facility or product line, or to expand an existing production facility. The cooperative may contract for services to process agricultural commodities or otherwise process value-added agricultural products during the 5-year period beginning on the operation startup date of the cooperative in order to provide adequate time for the planning and construction of the processing facility of the cooperative.

(c) *Unauthorized projects and purposes.*

(1) Businesses housed in private homes, except when the pro-rata value of the owner's living quarters is not included in the guaranteed loan.

(2) Any project that does not meet the requirements of paragraphs (d)(2), (d)(3), and (d)(4) in 7 U.S.C. 1932.

(3) Interim financing.

(4) Distribution or payment to an individual owner, partner, stockholder, or beneficiary of the borrower or the immediate family of such an individual when such individual will retain any portion of the ownership of the borrower, unless the Agency has determined that the distribution or payment is a part of the transfer of ownership within:

(i) The immediate family; or

(ii) An Employee owned Cooperative.

(5) Loan guarantees to lending institutions, investment institutions, or insurance companies.

(6) The guarantee of lease payments.

(7) The guarantee of loans made by other Federal agencies.

(8) Loans made with the proceeds of any obligation the interest on which is excludable from income under 26 U.S.C. 103 or a successor statute. Funds generated through the issuance of tax-exempt obligations may neither be used to purchase the guaranteed portion of any Agency guaranteed loan nor may an Agency guaranteed loan serve as collateral for a tax-exempt issue. The Agency may guarantee a loan for a project that involves tax-exempt financing only when the guaranteed loan funds are used to finance a part of the project that is separate and distinct from the part which is financed by the tax-exempt obligation, and the guaranteed loan has at least a parity security position with the tax-exempt obligation.

(9) Loan funds may not be used to support inherently religious activities.

(d) *Borrower eligibility.* In addition to the criteria specified in § 5001.8(a)(1) and (2), a borrower must meet both of the criteria specified in paragraphs (d)(1) and (2) of this section to be eligible for a Business and Industry guaranteed loan.

(1) A borrower must be:

(i) A cooperative organization, corporation, partnership, or other legal entity organized and operated on a profit or not-for-profit basis;

(ii) An Indian tribe on a Federal or State reservation or other Federally recognized tribal group;

(iii) A public body; or

(iv) An individual.

(v) A cooperative organization housed in an urban area is eligible provided certain rural benefits and requirements are met.

(2) A borrower must be engaged in or proposing to engage in a business. Business may include manufacturing, wholesaling, retailing, providing services, or other activities that will:

(i) Provide employment;

(ii) Improve the economic or environmental climate;

(iii) Promote the conservation, development, and use of water for aquaculture; or

(iv) Reduce reliance on nonrenewable energy resources by encouraging the development and construction of solar energy systems and other renewable energy systems (including wind energy systems, geothermal energy systems, and anaerobic digesters for the purpose of energy generation).

(e) *Additional borrower requirements.* The recipient of a loan guarantee under paragraph (a)(2)(xxii) of this section shall include in an appropriate agreement with retail and institutional facilities to which the recipient sells locally or regionally produced agricultural food products a requirement to inform consumers of the retail or institutional facilities that the consumers are purchasing or consuming locally or regionally produced agricultural food products.

(f) *Additional application process requirements.*

(1) *Obligation of funds.* If funds are insufficient to cover all applications pending approval, the Agency will allocate funds based on the date and time, based on Eastern time, a complete application is received, with those received first being funded first.

(2) *Priority.* In making or guaranteeing a loan under paragraph (a)(2)(xxii) of this section, the Secretary shall give priority to projects that have components benefiting underserved communities.

(g) *Additional application documentation provisions.*

(1) *Applications.* In addition to the application requirements specified in § 5001.12, lenders shall submit the following as applicable:

(i) *Feasibility study.* A feasibility study by a qualified consultant may be required by the Agency for startup businesses or existing businesses when the project will significantly affect the borrower's operations. If a feasibility study of a cooperative is required, the feasibility study will determine the viability of the business and not the individual farm operators.

(ii) *Certification of Non-Relocation and Market Capacity.* If the loan does not meet the requirements of paragraphs (d)(2), (d)(3), and (d)(4) in 7 U.S.C. 1932, a form approved by the Agency concerning non-relocation and market capacity.

(iii) Intergovernmental consultation comments in accordance with 7 CFR part 3015, subpart V, of this title.

(2) *Simplified applications.* For applications for loan guarantees of $400,000 or less, the lender may submit an application in conformance with § 5001.12(b).

(h) *Additional Origination Responsibilities.*

(1) *Financial statements.* Consolidated financial statements shall be required for variable interest entities in accordance with the Financial Accounting Standards Board financial interpretation 46, Consolidation of Variable Interest Entities, and eliminating intercompany transactions.

(2) *Collateral.*

(i) *Cooperative stock.* At a minimum, for the purchase of cooperative stock, the lender must secure the loan with a lien on the stock acquired with loan funds, an assignment of any patronage refund, and the full and unconditional personal, partnership, or corporate guarantee of the borrower.

(ii) *Leasehold interest.* Subject to approval by the Agency, a leasehold interest may be used as collateral for loans under this section provided the underlying lease meets the requirements specified in § 5001.101(a)(1)(viii).

(iii) *Discounting collateral.* When evaluating collateral for loans under this section, the lender shall comply with the requirements specified in paragraphs (h)(2)(iii)(A) through (E) of this section.

(A) No value will be assigned to unsecured personal, partnership, or corporate guarantees.

(B) A maximum of 80% of current market value will be given to real estate. Special purpose real estate should be assigned less value.

(C) A maximum of 60% of book value to be assigned to acceptable accounts receivable; however, all accounts over 90 days past due, contra accounts, affiliated accounts and other accounts deemed not to be collateral will be omitted. Calculations to determine the percentage to be applied in the analysis are to be based on the realizable value of the accounts receivable taken from a current aging of accounts receivable from the borrower's most recent financial statement.

(D) A maximum of 60% of book value will be assigned to inventory.

(E) Collateral value assigned to machinery and equipment, furniture and fixtures will be based on its marketability, mobility, useful life, and alternative uses, if any. Collateral value assigned to these types of security will not exceed 70%.

(3) *Payment and performance bond.* A payment and performance bond sufficient to mitigate Agency risk if the project is never completed must be provided.

(i) *Additional servicing requirements—repurchase.* Repurchased loans may be sold without recourse to third-party private investors.

(j) *Additional guarantee- and loan-related requirements.*

(1) *Marginal/substandard loans.* It is not intended that the guarantee authority will be used for marginal or substandard loans or for the relief of lenders having such loans.

(2) *Conditional Commitment.* For the purchase of cooperative stock, the Conditional Commitment shall require the cooperative to provide the lender with all required Federal, State, and local permits and other clearances involving the environmental aspects for review and approval.

(3) *Lines of credit.* Lines of credit are subject to the conditions identified in paragraphs (j)(3)(i) through (v) of this section.

(i) The maximum term of a line of credit is 7 years, or limited to the term of the other guaranteed loans approved under this subpart, whichever is less.

(ii) The total principal balance owed at any one time on line of credit advances may not exceed the line of credit ceiling. If a lender exceeds the credit ceiling, any loss payment will be reduced by the amount the credit ceiling was exceeded.

(iii) As part of the lender's annual review of the borrower's operation, and before funds are re-advanced, the lender will verify to the satisfaction of the Agency that the borrower is in compliance with the provisions of the lender's line of credit agreement and term loan agreement, income and loan proceeds for the previous operating cycle have been properly accounted for, and the borrower's projected cash flow for the borrower's upcoming operating cycle, using reasonable assumptions, indicates a reasonable chance of repayment. The total amount advanced will not exceed the projected credit needs for that operating cycle as indicated in the borrower's projections, unless the projections are revised and continue to reflect feasibility.

(iv) The lender must ensure that lines of credit remain adequately secured with any suitable collateral. At no time will advances be made when the outstanding principal balance exceeds the discounted value of the collateral securing the line of credit.

(v) Lines of credit must be retained by the lender; they cannot be assigned or sold on the secondary market.

(4) *Issuance of Loan Note Guarantee.*

(i) Paragraph § 5001.33(a)(2) notwithstanding, the Agency may, at its sole discretion, issue a Loan Note Guarantee prior to all planned property acquisitions having been completed and all development having been substantially completed in accordance with plans and specifications. In considering whether to issue a Loan Note Guarantee prior to construction being completed, the Agency will consider the added risk associated with issuing a Loan Note Guarantee under such conditions. When negotiating the percent of guarantee with the lender, the Agency will consider these added risks and the credit risks and the lender's experience in financing the type of project. Where the Agency determines it is warranted, the percent of guarantee will be reduced by a minimum of 10%.

(ii) If, for the purchase of cooperative stock, the lender requests the issuance of the Loan Note Guarantee before the cooperative becomes operational, the lender must certify to the Agency that the cooperative has all of the required Federal, State, and local permits and other clearances involving the environmental aspects for review and approval.

(5) *Funding limits.* At the time of loan approval, the full amount of outstanding principal and interest balance associated with Business and Industry loans, including the amount of the loan being approved, cannot exceed $25,000,000 for any one borrower, except that for a cooperative organization this limit shall be $40,000,000 for rural projects processing value added commodities or significantly benefits one or more entities eligible for assistance for the purposes described in paragraph (b) of this section.

(i) The total amount of Business and Industry loans made to cooperative organizations and guaranteed for a fiscal year with principal amounts that are in excess of $25,000,000 may not exceed 10% of the Business and Industry loans guaranteed for the fiscal year.

(ii) The principal amount of a Business and Industry loan made for the purchase of cooperative stock may not exceed $600,000.

(6) *Guarantee fee.* The maximum guarantee fee that may be charged is 2%. The guarantee fee may be reduced to 1% if the borrower is a high impact business and is located in an area of long term population decline and job deterioration as a result of persistent economic hardship, significant economic loss from a Presidentially-declared disaster, or a fundamental structural economic change. Each fiscal year, the Agency will establish a limit on the maximum portion of guarantee authority available for that fiscal year that may be used to guarantee loans with a guarantee fee of 1%. The limit will be announced by publishing a notice in the **Federal Register**. Once the limit has been reached, the guarantee fee for all additional loans obligated during the remainder of that fiscal year will be 2%.

(7) *Maximum percent of guarantee.* The maximum loan guarantees issued to a Rural Development approved lender with Business and Industry funding is:

(i) 80% if the guaranteed loan amount is $5 million or less;

(ii) 70% if the guaranteed loan amount $10 million or less, but greater than $5 million; or

(iii) 60% if the guaranteed loan amount is greater than $10 million.

§ 5001.104 Rural Energy for America Program.

(a) *Project eligibility.* To be eligible for a Rural Energy for America Program guaranteed loan, the project must meet the criteria specified in paragraphs (a)(1) through (a)(3) of this section and in § 5001.6.

(1) The project shall be for the purchase, installation, expansion and/or other energy-related improvement of a renewable energy system or to make energy efficiency improvements; and

(2) The project shall be for technology that is—

(i) Pre-commercial or commercially available, and

(ii) Replicable.

(3) The project must be located in a rural area.

(4) The project may include the refinancing of any loan when the Agency determines that the project is viable and equal or better rates or terms are offered provided that the debt being refinanced will be less than 50% of the new loan amount.

(b) *Borrower eligibility.* To be eligible for a Rural Energy for America Program guaranteed loan, a borrower must be an agricultural producer or rural small business and must meet the criteria specified in § 5001.8(a)(1) and (2).

(c) *Additional application process requirements—obligation of funds*. If funds are insufficient to cover all applications pending approval, the Agency will allocate funds based on the date and time, based on Eastern time, a complete application is received, with those received first being funded first.

(d) *Additional application documentation provisions*. In addition to the application requirements specified in § 5001.12, lenders shall submit the following as applicable:

(1) *Certifications*. The lender must certify in the application that the project is able to demonstrate technical merit and that the borrower is an agricultural producer or rural small business.

(2) *Technical report*. For renewable energy system projects with total eligible project costs of more than $200,000, a satisfactory technical report that demonstrates that the project is commercially viable and can be installed and perform as intended in a reliable, safe, cost-effective, and legally compliant manner must be provided to the Department of Energy (DOE) for review, unless otherwise stated in a **Federal Register** Notice To determine the overall technical merit of the renewable energy system, the lender must submit its proposal to the Agency for review.

(3) *Energy assessment/audit*. For energy efficiency improvement projects, an energy assessment, with adequate and appropriate evidence of energy savings expected when the system is operated as designed, must be provided. For energy efficiency improvement projects with total eligible project costs greater than $50,000, an energy audit is required. The lender must submit energy assessments and energy audits to the Agency for review.

(4) *Feasibility study*. A feasibility study by a qualified consultant is required for each renewable energy system project seeking a loan guarantee of greater than $200,000.

(5) Intergovernmental consultation comments in accordance with 7 CFR part 3015, subpart V, of this title.

(e) *Additional Origination Responsibilities*.

(1) *Financial statements*. Consolidated financial statements shall be required for variable interest entities in accordance with the Financial Accounting Standards Board financial interpretation 46, Consolidation of Variable Interest Entities, and eliminating intercompany transactions.

(2) *Discounting collateral*. When evaluating collateral for loans under this section, the lender shall comply with the requirements specified in § 5001.103(h)(2)(iii).

(3) *Payment and performance bond*. A payment and performance bond sufficient to mitigate Agency risk if the project is never completed must be provided.

(f) *Additional servicing responsibilities—post-construction reporting requirements*. Once the project has been constructed, the lender must provide to the Agency annual reports from the borrower on the performance characteristics and results of the projects.

(1) *Schedule*. For renewable energy system projects, these reports are to be provided commencing in the first full calendar year after construction is completed and continuing for 3 full years. For energy efficiency improvement projects, these reports are to be provided commencing the first full calendar year following the year in which project construction was completed and continuing for 2 full years.

(2) *Contents*. Reports for renewable energy system projects must contain, at a minimum, information on output and sales and/or energy savings. Reports for energy efficiency improvement projects must contain, at a minimum, information on energy savings. Additional information to be included in these reports will be negotiated between the Agency and the lender/borrower prior to the execution of the Loan Note Guarantee.

(g) *Additional guarantee- and loan-related requirements*.

(1) *Issuance of Loan Note Guarantee*. In addition to the requirements specified in § 5001.34, for Rural Energy for America Program loans, the lender must certify that all planned property acquisitions and development have been performing at a steady state operating level in accordance with the technical requirements, plans, and specifications; the project conforms with applicable Federal, State, and local codes; and costs have not exceeded the amount approved by the lender and the Agency.

(2) *Funding considerations*.

(i) *Maximum loan guarantee*. At the time of loan approval, the full amount of outstanding principal and interest balance associated with Rural Energy for America Program loans, including the amount of the loan being approved, cannot exceed $25,000,000 for any one borrower.

(ii) *Loan guarantee amount*. In determining the amount of a loan guarantee, the Agency will take into consideration the following seven criteria:

(A) The type of renewable energy system to be purchased;

(B) The estimated quantity of energy to be generated by the renewable energy system;

(C) The expected environmental benefits of the renewable energy system;

(D) The extent to which the renewable energy system will be replicable;

(E) The amount of energy savings expected to be derived from the activity, as demonstrated by an Agency-approved energy audit;

(F) the expected energy efficiency of the renewable energy system; and

(G) The estimated length of time it would take for the energy savings generated by the activity to equal the cost of the activity.

(3) *Matching funds*. The amount of a Rural Energy for America loan guarantee, including any grants and direct loans made under this program, that will be made available to an eligible project will not exceed 75% of total eligible project costs. Eligible project costs are only those costs associated with the items identified in paragraphs (g)(3)(i) through (xi) of this section, as long as the items are an integral and necessary part of the renewable energy system or energy efficiency improvement.

(i) Post-application purchase and installation of equipment (new, refurbished, or remanufactured), except agricultural tillage equipment, used equipment, and vehicles.

(ii) Post-application construction or improvements, except residential.

(iii) Energy audits or assessments.

(iv) Permit and license fees.

(v) Professional service fees, except for application preparation, packager fees, and broker fees.

(vi) Feasibility studies and technical reports.

(vii) Business plans.

(viii) Retrofitting.

(ix) Construction of a new energy efficient facility only when the facility is used for the same purpose, is approximately the same size, and based on the energy audit will provide more energy savings than improving an existing facility. Only costs identified in the energy audit for energy efficiency improvements are allowed.

(x) Working capital.

(xi) Land acquisition.

(4) *Maximum percent of guarantee*. The maximum loan guarantees issued to a Rural Development approved lender with Rural Energy for America Program funding is:

(i) 85% if the guaranteed loan amount is $600,000 or less;

(ii) 80% if the guaranteed loan amount $5 million or less, but greater than $600,000;

(iii) 70% if the guaranteed loan amount is greater than $5 million but less than or equal to $10 million; or

(iv) 60% if the guaranteed loan amount is greater than $10 million.

§§ 5001.105–5001.199 [Reserved]

§ 5001.200 OMB control number.

Pursuant to the Paperwork Reduction Act of 1995 (44 U.S.C. Chap. 35; *see* 5 CFR part 1320), the information collection provisions have been submitted to the Office of Management and Budget (OMB) for approval as a new collection and assigned OMB number 0570–0054.

Dated: December 1, 2008.

Thomas C. Dorr,

Under Secretary for Rural Development.

[FR Doc. E8–29151 Filed 12–16–08; 8:45 am]

BILLING CODE 3410–15–P