

Proposed Rules

Federal Register

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This section of the FEDERAL REGISTER contains notices to the public of the proposed issuance of rules and regulations. The purpose of these notices is to give interested persons an opportunity to participate in the rule making prior to the adoption of the final rules.

DEPARTMENT OF AGRICULTURE

Rural Housing Service

Rural Business-Cooperative Service

Rural Utilities Service

Farm Service Agency

7 CFR Part 1980

RIN 0575-AC17

Community Programs Guaranteed Loan Program

AGENCIES: Rural Housing Service and Rural Utilities Service, USDA.

ACTION: Proposed rule.

SUMMARY: The Agencies are proposing to issue a new Community Programs (CP) guaranteed loan regulation (part 1980, subpart I) to replace the current regulation for the program. This action is needed to streamline and update the program. The intended effect is to simplify and clarify the regulation; shift some responsibility for loan documentation and analysis from the Government to the lenders; make the program more responsive to the needs of lenders, local community public bodies, and nonprofit corporations; and provide for smoother processing of applications.

DATES: Written comments must be received on or before December 8, 1997. The comment period for information collections under the Paperwork Reduction Act of 1995 continues through December 8, 1997.

ADDRESSES: Submit written comments to the Chief, Regulations and Paperwork Management Branch, Support Services Division, Rural Development, U.S. Department of Agriculture, STOP 0743, 1400 Independence Ave. SW., Washington, D.C. 20250-0743. Also, comments may be submitted via the Internet by addressing them to "comments@rus.usda.gov" and must contain Community Programs Guaranteed Loans in the subject line. All written comments will be available for public inspection during regular work hours at the above address.

FOR FURTHER INFORMATION CONTACT: Mel Padgett, Community Programs Senior Loan Specialist, Rural Housing Service, U.S. Department of Agriculture, STOP 3222, 1400 Independence Ave. SW., Washington, D.C. 20250-3222, telephone: (202) 720-1495.

SUPPLEMENTARY INFORMATION:

Classification

This proposed rule has been determined to be not significant for the purposes of Executive Order 12866 and, therefore, has not been reviewed by OMB.

Programs Affected

The Catalog of Federal Domestic Assistance Programs impacted by this action are 10.766, Community Facilities loans, and 10.760, Water and Waste Disposal Systems for Rural Communities.

Intergovernmental Review

These loans are subject to the provisions of Executive Order 12372 which require intergovernmental consultation with State and local officials. RHS conducts intergovernmental consultations for each loan in the manner delineated in FmHA Instruction 1940-J.

Civil Justice Reform

The proposed rule has been reviewed under Executive Order 12778, 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 to this rule; and (3) administrative proceedings of the National Appeals Division (7 CFR part 11) must be exhausted before bringing suit in court challenging action taken under this rule.

Environmental Impact Statement

The action has been received in accordance with 7 CFR part 1940, subpart G, "Environmental Program." The Agencies have 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 of 1969, Pub. L. 91-190, an Environmental Impact Statement is not required.

Unfunded Mandates Reform Act

Title II of the Unfunded Mandates Reform Act of 1995 (UMRA), Pub. L. 104-4, established 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, the Agencies 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 1 year. When such a statement is needed for a rule, section 205 of the UMRA generally requires the Agencies to identify and consider a reasonable number of regulatory alternatives and adopt the least costly, most cost-effective, or least burdensome alternative that achieves the objectives of the rule.

This 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. Therefore, this rule is not subject to the requirements of sections 202 and 205 of the UMRA.

National Performance Review

This regulatory action is being taken as part of the National Performance Review program to eliminate unnecessary regulations and improve those that remain in force.

Regulatory Flexibility Act

This proposed rule has been reviewed with regard to the requirements of the Regulatory Flexibility Act (5 U.S.C. 601-612). The undersigned has determined and certified by signature of this document that this rule will not have a significant economic impact on a substantial number of small entities since this rulemaking action does not involve a new or expanded program.

Discussion of the Proposed Rule

This action replaces the CP guaranteed loan program administered under 7 CFR part 1980. Under the proposed rule, this guaranteed loan program will be more flexible and place more reliance on lenders. There are fewer specific requirements for lenders. The lender has added responsibility for analyzing credit quality; for making, securing, and servicing the loan; and for

monitoring construction. Application processing procedures will be more efficient; less burdensome for borrowers, lenders, and Rural Development staff; and will provide for more rapid decisions.

The CP loan program was authorized by the Rural Development Act of 1972. The Agencies were authorized to guarantee CP loans under Pub. L. 101-161 enacted November 21, 1989. The loans are made by private lenders to public bodies and nonprofit corporations for the purpose of improving rural living standards and for other purposes that create essential community facilities located in cities, towns, or unincorporated areas of up to 50,000 population required by the Federal Agriculture Improvement and Reform Act of 1996 (Pub. L. 104-127) and water and waste disposal facilities located in cities or towns of up to 10,000 population. The previous statutory population limit for loans for essential community facilities had been 20,000.

Since 1990, more than 240 community programs projects, totaling slightly more than \$210 million, have received loans which were guaranteed through the CP program.

These loans can be made for a variety of purposes including health care; public buildings and improvements; fire and rescue; easements; purchase of equipment, machinery, and supplies; repair and modernization; pollution control; transportation studies; and water and waste disposal facilities. The rate and terms of the loan are negotiated between the borrower and the lender.

The Agencies propose to replace the regulation for the CP guaranteed loan programs with a completely new regulation. This is a high-priority effort to streamline the administration and operation of the program, respond to the requests of users of the program, and assist the field staff administering the program. The revised regulation is shorter, simpler, clearer, and more logically organized. The volume of regulatory material which a lender must review to request, make, or service a CP guaranteed loan under the new regulation is significantly less than the current regulation. Clarifications of various items are also included, such as what is meant by the term "essential community facility."

Except for the increase in the population limit, the revisions are not required by statute. However, the President, as well as the Secretary of Agriculture, are committed to streamlining all Federal regulations. This CP regulation streamlines our application procedures, reduces loan

application processing time by placing greater emphasis on State resources, allows more management flexibility and decision-making capacity at the State Office level, and expands eligible loan purposes to include recreation.

Recognizing the need to streamline the regulation, the Agencies established two task forces. One was comprised of CP Program Chiefs, CP Loan Specialists, and other field office personnel. The second was comprised of lenders, secondary market representatives, and National Office management. They examined changes that needed to be made in the program to attract additional lenders and to make the program more user friendly and customer oriented. Task force recommendations have been incorporated into this regulation.

Based on the recommendations of the task forces, the Agencies have proposed these revisions to make the program more usable by lenders and borrowers. Also, the Agencies recognize that changes are necessary to make the program more effective in creating jobs and stimulating economic activity (particularly in chronically low-income rural areas). Under the proposed new CP regulation, the material that must be submitted to, and reviewed by, the Agencies before approval of the guarantee has been streamlined. Responsibilities for credit and analysis and application processing tasks will be shifted from the Agencies' National Offices to field offices and from the Agencies to the lender, where feasible. Following is a discussion of some of the most significant policy revisions included in the proposed new regulation.

To streamline the regulation, the Agencies have combined applicable portions of the Direct Community Loan Programs (7 CFR part 1942, subpart A), Fire and Rescue (7 CFR part 1942, subpart C), General Guaranteed Regulation (7 CFR part 1980, subpart A), previously drafted Guaranteed Community Programs Regulation, and parts of forms which were not in regulations into the Guaranteed Community Programs Regulation (7 CFR part 1980, subpart I). The Agencies also divided the regulation into general, processing, and servicing sections. These actions should significantly reduce the amount of regulatory material that a lender and a borrower must peruse to determine eligibility and complete the application. This will also simplify making and servicing a CP loan.

Additionally, the necessary information contained in the preapplication package can be

submitted simultaneously with the application. The threshold for requiring audited financial statements has been increased from \$100,000 to \$500,000 to reduce the reporting burden on small organizations. Also, we have included recreation as well as clarified telecommunications as eligible loan purposes.

Under the revised regulations, the lender is responsible for legal sufficiency. The lender will not only be able to negotiate interest rates but will also be able to negotiate interest rate incremental increases and caps for each loan. This will give the lender more flexibility to fit the CP guaranteed loan program to its lending policies and procedures. The lender does not have to be a local lender provided it can demonstrate the ability to adequately service the loan. This will permit an expansion of eligible lenders to include such organizations as State bond banks, the Rural Utilities Cooperative Finance Corporation, and Sallie Mae. All of these organizations have expressed an interest in the CP guaranteed lending program in the past.

Conclusion

The Agencies believe the streamlining of the regulation for this program will enhance the use of the program in improving the future prosperity of rural residents through targeted investments that enhance rural competitiveness, improve and diversify community services, and enable rural residents to have a better quality of life. The proposed revisions are consistent with Administration efforts to streamline Government functions, improve efficiency and the effectiveness of Government activities, and be more customer friendly. The changes proposed will enable the Agencies to deliver a larger program with fewer staff resources, simultaneously meet the objectives of the National Performance Review regarding customer service, reduce regulation, and streamline Agencies operations.

The proposed changes will provide more flexibility for both lenders and Agencies staff. Many errors will be reduced because the guidelines and requirements are much clearer and items are more easily found in a reduced and better-organized regulation. Lenders will be more interested in using the program because the procedures are simpler and more direct with significantly fewer cross references to other regulations. The ultimate benefits to be realized are increased lending activity resulting in a better-living standard for rural communities with the infrastructure to attract new businesses

and the creation of more jobs in rural areas, particularly in those areas that have experienced historical economic distress.

Paperwork Reduction Act

In accordance with the Paperwork Reduction Act of 1995, the Agencies will seek Office of Management and Budget (OMB) approval of the reporting and recordkeeping requirements contained in this regulation. These reporting and recordkeeping requirements have been previously approved under control numbers 0575-0024 and 0575-0137. We have made the appropriate adjustments based upon the programs' 6-year history.

The loans are made by private lenders to public bodies and nonprofit corporations for the purpose of improving rural living standards and for other purposes that create employment opportunities in rural areas. Eligibility for this program includes community facilities located in cities, towns, or unincorporated areas of up to 50,000 population and water and waste disposal facilities located in cities of up to 10,000 population.

The information collected is used by the Agencies to manage, plan, evaluate, and account for Government resources. The reports are required to ensure the proper and judicious use of public funds.

Estimate of Burden: Public reporting burden for this collection of information is estimated to average 13.97 hours per response.

Respondents: Nonprofit corporations and public bodies.

Estimated Number of Respondents: 125.

Estimated Number of Responses per Respondent: 10.12.

Estimated Total Annual Burden on Respondents: 17,677.

Copies of this information collection can be obtained from Barbara Williams, Information Collection Coordinator, Regulations and Paperwork Management Branch, Support Services Division, Rural Development, telephone (202) 720-9734.

Comments are invited on (a) whether the proposed collection of information is necessary for the proper performance of the functions of the Agencies, including whether the information will have practical utility; (b) the accuracy of the Agencies' estimate of the burden of the proposed collection of information, including the validity of the methodology and assumptions used; (c) ways to enhance the quality, utility, and clarity of the information to be collected; and (d) ways to minimize the burden of the collection of information

on those who are to respond, including through the use of appropriate automated, electronic, mechanical, or other technological collection techniques or other forms of information technology.

All responses to this notice will be summarized, included in the request for OMB approval, and will become a matter of public record. Comments should be submitted to the Desk Officer for Agriculture, Office of Information and Regulatory Affairs, Office of Management and Budget, Washington, D.C. 20503 and to Barbara Williams, Information Collection Coordinator, Regulations and Paperwork Management Branch, Support Services Division, Rural Housing Service, U.S. Department of Agriculture, STOP 0743, 1400 Independence Avenue SW., Washington, D.C. 20250-0743. A comment to OMB is best assured of having its full effect if OMB receives it within 30 days of publication of this rule.

List of Subjects in 7 CFR Part 180

Loan programs—Agriculture, Loan programs—Business and industry—Rural development assistance, Loan programs—Community facilities—Rural development assistance, Loan programs—Housing and community development.

Accordingly, part 180, chapter XVIII, title 7 of the Code of Federal Regulations, is proposed to be amended as follows:

PART 180—GENERAL

1. The authority citation for part 180 is revised to read as follows:

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

Subpart A—General

§ 180.47 [Amended]

2. Section 180.47(d) is removed.

§ 180.60 [Amended]

3. Section 180.60(a)(12) is amended by removing the words "or Form FmHA or its successor agency under Public Law 103-354 1980-10, 'Application for Loan and Guarantee' (Community Programs)," in the first sentence.

Subpart I—Community Programs Guaranteed Loans

4. Subpart I is revised to read as follows:

Sec.
180.801 General.
180.802 Definitions.
180.803 Full faith and credit.
180.804 Conditions of Guarantee.
180.805—180.807 [Reserved]

180.808 Access to lender's records.
180.809 Environmental requirements.
180.810—180.811 [Reserved]
180.812 Inspections.
180.813 Appeals.
180.814—180.816 [Reserved]
180.817 Exception authority.
180.818—180.819 [Reserved]
180.820 Eligibility.
180.821 Priorities.
180.822—180.823 [Reserved]
180.824 Eligible loan purposes.
180.825 Ineligible loan purposes.
180.826 [Reserved]
180.827 Eligible Lenders.
180.828 Transfer of lender or borrower prior to issuance of loan note guarantee.
180.829 Fees and charges by lender.
180.830 Loan guarantee limitations.
180.831—180.832 [Reserved]
180.833 Interest rates.
180.834 Terms of loan repayment.
180.835—180.836 [Reserved]
180.837 Insurance and fidelity bonds.
180.838—180.839 [Reserved]
180.840 Equal opportunity and Fair Housing Act requirements.
180.841 [Reserved]
180.842 Design and construction requirements.
180.843 Other Federal, State, and local requirements.
180.844—180.846 [Reserved]
180.847 Economic feasibility requirements.
180.848 Security.
180.849—180.851 [Reserved]
180.852 Processing.
180.853 Evaluation of application.
180.854—180.858 [Reserved]
180.859 Review of requirements.
180.860—180.862 [Reserved]
180.863 Conditions precedent to issuance of the Loan Note Guarantee.
180.864 Issuance of Lender's Agreement, Loan Note Guarantee, and Assignment Guarantee Agreement.
180.865 Lender's sale or assignment of the guaranteed portion of loan.
180.866—180.868 [Reserved]
180.869 Loan servicing.
180.870—180.872 [Reserved]
180.873 Replacement of loss, theft, destruction, mutilation, or defacement of Loan Note Guarantee or Assignment Guarantee Agreement.
180.874 [Reserved]
180.875 Defaults by borrower.
180.876—180.877 [Reserved]
180.878 Repurchase of loan.
180.879 Transfer of lender after issuance of Loan Note Guarantee.
180.880 Interest rate changes after loan closing.
180.881 Liquidation.
180.882 [Reserved]
180.883 Protective advances.
180.884 Additional loans or advances.
180.885 Bankruptcy.
180.886—180.887 [Reserved]
180.888 Transfers and assumptions.
180.889 Mergers.
180.890 Disposition of acquired property.
180.891—180.893 [Reserved]
180.894 Determination and payment of loss.

1980.895 Future recovery.
 1980.896 Termination of Loan Note
 Guarantee.
 1980.897—1980.900 [Reserved]

PART 1980—GENERAL

Subpart I—Community Programs Guaranteed Loans

§ 1980.801 General.

(a) This subpart contains the regulations for Community Programs loans guaranteed by the Agency and applies to lenders, holders, borrowers, and other parties involved in making, guaranteeing, holding, servicing, or liquidating such loans.

(b) The purpose of the Community Programs guaranteed loan program is to improve, develop, or finance essential community and water and waste disposal facilities in rural areas. This purpose is achieved through bolstering the existing private credit structure through the guarantee of quality loans which will provide lasting community benefits.

§ 1980.802 Definitions.

The following general definitions are applicable to the terms used in this subpart:

Agency. The Rural Housing Service and the Rural Utility Service which are within the Rural Development mission area of the United States Department of Agriculture (USDA) or their successor agencies with authority delegated by the Secretary of Agriculture to administer the Community Facilities and Water and Waste Disposal programs. This also includes the Rural Development mission area.

Application. An Agency prescribed form to request an Agency guarantee. (Available in any Agency office.)

Arm's length transaction. The sale, release, or disposition of assets in which the title to the property passes to a ready, willing, and able third party who is not affiliated with, or related to, and has no security, monetary, or stockholder interest in the borrower or transferor at the time of the transaction.

Assignment Guarantee Agreement. The signed agreement among the Agency, the lender, and the holder setting forth the terms and conditions of an assignment of the guaranteed portion of a loan or any part thereof. (This is an Agency prescribed form available in any Agency office.)

Borrower. The entity that borrows money from the lender.

Collateral. Property pledged to secure the guaranteed loan.

Community facility (essential). The term "facility" as used in this subpart refers to both the physical structure

financed and the resulting service provided to rural residents. An essential community facility must:

(1) Be 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) Not include private affairs or commercial or business undertakings (except for limited authority for industrial parks);

(4) Be the area of jurisdiction or operation for the public bodies eligible to receive assistance or a similar local rural service area of a not-for-profit corporation; and

(5) Be located in a rural area.

Conditional Commitment for Guarantee. The Agency's written statement to the lender that the material submitted is approved subject to the completion of all conditions and requirements set forth in the agreement. (This is an Agency prescribed form available in any Agency office.)

Guaranteed loan. A loan made and serviced by a lender for which the Agency and lender have entered into a Lender's Agreement and for which the Agency has issued a Loan Note Guarantee.

Holder. The person or entity (other than the lender) who holds all or a part of the guaranteed portion of the loan with no servicing responsibilities. When the lender assigns parts of the guaranteed portion of the loan to an assignee, the assignee becomes a holder when the Assignment Guarantee Agreement is signed by all parties.

Immediate Family. Individuals who are closely related by blood or by marriage, such as a spouse, significant other, parent, child, brother, sister, aunt, uncle, grandparent, grandchild, niece, nephew, or first cousin.

Insurance. Fire, windstorm, lightning, hail, explosion, riot, civil commotion, aircraft, vehicles, smoke, builder's risk, public liability, property damage, flood or mudslide, worker's compensation, fidelity bond, malpractice, or any similar insurance that is available and needed to protect the security, or that is required by law.

Joint financing. The situation occurring when two or more lenders (or any combination of lenders and other financial sources) make separate loans to supply the funds required by one borrower. For example, such joint financing may consist of the Agency's financial assistance with the Economic Development Administration, Department of Housing and Urban Development (HUD), or other Federal and State agencies, and private and quasi-public financial institutions.

Lender. The person or organization making and responsible for servicing the loan. The lender is also referred to in this subpart as the applicant who is requesting a guarantee during the preapplication and application stage of processing.

Lender's Agreement. The signed agreement between the Agency and the lender setting forth the lender's responsibilities when the Loan Note Guarantee is issued. (This is an Agency prescribed form available in any Agency office.)

Loan classification system. The process by which loans are examined and categorized by degree of potential for loss in the event of default.

Loan Note Guarantee. The signed commitment issued by the Agency setting forth the terms and conditions of the guarantee of an identified loan. (This is an Agency prescribed form available in any Agency office.)

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.

Note. An evidence of debt. In those instances where the Agency guarantees a bond issue, "note" shall also be construed to include a bond or other evidence of indebtedness, as appropriate.

Participation. Sale of an interest in a loan in which the lender retains the note, collateral securing the note, and all responsibility for loan servicing and liquidation.

Principals of borrowers. The owners, officers, directors, entities, and others directly involved in the operation and management of the borrower.

Problem loan. A loan which is not performing according to its terms and conditions.

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, special purpose district, an Indian Tribe on a Federal or State reservation, or another federally recognized Indian Tribe.

Report of loss. An Agency prescribed form used by lenders when reporting a loss under an Agency guarantee. (Available in any Agency office.)

Rural and rural area. Any area defined by the latest Decennial Census of the United States except:

(1) For water and waste disposal facilities—any city or town with a population in excess of 10,000 inhabitants.

(2) For essential community facilities—any city, town, or unincorporated area with a population in excess of 50,000 inhabitants, and any urbanized area immediately adjacent to a city, town, or unincorporated area that has a population of more than 50,000 inhabitants.

Service area. The area reasonably expected to be served by the facility being financed by the guaranteed loan.

State. Any of the 50 States, the Commonwealth of Puerto Rico, the Virgin Islands of the United States, Guam, American Samoa, Commonwealth of the Northern Mariana Islands, Republic of the Marshall Islands, Republic of Palau, and the Federated States of Micronesia.

State Director. The Rural Development State Director or the staff member who has been delegated authority to perform action on behalf of the State Director.

Substantive Change. Any change in the purpose of the loan or any change in the financial condition of the borrower or the collateral which would jeopardize the performance of the loan.

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 or waste disposal facility. A facility designed to provide, enlarge, extend, or otherwise improve water, wastewater or sanitary sewer, solid waste disposal, or storm wastewater services to rural residents.

§ 1980.803 Full faith and credit.

The Loan Note Guarantee constitutes an obligation supported by the full faith and credit of the United States and is not contestable except for fraud or misrepresentation (including negligent misrepresentation) of which the lender or holder has actual knowledge, participates in, or condones. A note which provides for the payment of interest on interest shall not be guaranteed and 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. The guarantee and right to require purchase will be directly enforceable by the holder notwithstanding any fraud, misrepresentation, or any unenforceability of the Loan Note Guarantee. The Loan Note Guarantee will not be enforceable by the lender to the extent any loss is occasioned by violation of usury laws, negligent servicing, or failure to obtain the required security regardless of the time

at which the Agency acquires knowledge of the foregoing. Any losses occasioned will not be enforceable by the lender to the extent that loan funds are used for purposes other than those specifically approved by the Agency in its Conditional Commitment for Guarantee. Negligent servicing is defined as the failure to perform those services which a reasonably prudent lender would perform in servicing its own portfolio of loans that are not guaranteed. The term includes not only the concept of a failure to act but also not acting in a timely manner, acting in a manner contrary to the manner in which a reasonably prudent lender would act up to the time of loan maturity, or until a final loss is paid. The Loan Note Guarantee or Assignment Guarantee Agreement in the hands of a holder shall not cover interest accruing 90 days after the holder has demanded repurchase by the lender, nor shall the Loan Note Guarantee or Assignment Guarantee Agreement in the hands of a holder cover interest accruing 90 days after the lender or Agency has requested the holder to surrender the evidence of debt for repurchase.

§ 1980.804 Conditions of Guarantee.

A loan guarantee under this part will be evidenced by a Loan Note Guarantee issued by the Agency. Each lender will also execute a Lender's Agreement. The provisions of this subpart in effect at the issuance of the Loan Note Guarantee and execution of the Lender's Agreement will control the Loan Note Guarantee or Lender's Agreement.

(a) The entire loan will be secured by the same security with equal lien priority for the guaranteed and non-guaranteed portions of the loan. The non-guaranteed portion of the loan will not be paid first nor given any preference or priority over the guaranteed portion.

(b) The lender will be responsible for servicing the entire loan and will remain mortgagee or secured party of record notwithstanding the fact that another party may hold a portion of the loan.

(c) When a guaranteed portion of a loan is sold to a holder, the holder shall have all rights of the lender under the Loan Note Guarantee to the extent of the portion purchased. The lender will remain bound by all the obligations under the Loan Note Guarantee, Lender's Agreement, and Agency program regulations. 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. If the Agency makes a payment to a holder, then the lender must reimburse the Agency.

(d) A lender will receive all payments of principal and interest on the account of the entire loan and will promptly remit to each holder a pro rata share, less any lender servicing fee.

(e) The lender may retain all of the unguaranteed portion of the loan or may sell part of the unguaranteed portion of the loan through participation. However, the lender is required to retain 5 percent of the loan amount from the unguaranteed portion in their portfolio.

§§ 1980.805—1980.807 [Reserved]

§ 1980.808 Access to lender's records.

Upon request by the Agency, the lender will permit representatives of the Agency (or other agencies of the U.S. Department of Agriculture authorized by that Department) to inspect and make copies of any of the records of the lender pertaining to the guaranteed loans. Such inspection and copying may be made during regular office hours of the lender or at any other time the lender and the Agency agree upon.

§ 1980.809 Environmental requirements.

Requirements for an environmental review or mitigation actions are contained in part 1940, subpart G, of this chapter. The lender must assist the Agency to ensure that the borrower complies with any mitigation measures required by the Agency's environmental review for the purpose of avoiding or reducing the adverse environmental impact of construction or operations of the facility financed with the guaranteed loan.

§§ 1980.810—1980.811 [Reserved]

§ 1980.812 Inspections.

The lender will notify the Agency of any scheduled field inspections during construction and after issuance of the Loan Note Guarantee. The Agency may attend such field inspections. Any inspections or review conducted by the Agency, including those with the lender, are for the benefit of the Agency only and not for other parties of interest. Agency inspections do not relieve any parties of interest of their responsibilities to conduct necessary inspections.

§ 1980.813 Appeals.

Only the borrower, lender, or holder can appeal an Agency decision. In cases where the Agency has denied or reduced the amount of final loss payment to the lender, the adverse

decision may be appealed only by the lender. A decision by a lender adverse to the interest of the borrower is not a decision by the Agency, whether or not concurred in by the Agency. Appeals will be handled in accordance with the regulations of the National Appeals Division, U.S. Department of Agriculture, published at 7 CFR part 11.

§§ 1980.814—1980.816 [Reserved]

§ 1980.817 Exception authority.

The appropriate Agency Administrator may, in individual cases, make an exception to any requirement or provision of this subpart or address any omission of this subpart provided the Administrator determines that application of the requirement, or provision, or failure to take action in the case of an omission would adversely affect the Government's financial interest. Requests for exceptions must be in writing by the State Director.

§§ 1980.818—1980.819 [Reserved]

§ 1980.820 Eligibility.

(a) 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 period of time. This determination shall become a part of the Agency casefile. The Agency should also determine if an outstanding judgment obtained by the United States in a Federal Court (other than the U.S. Tax Court) has been entered against the borrower or if the borrower has an outstanding debt with any Federal agency that is in a delinquent status. Such judgment or delinquency shall cause the potential borrower to be ineligible to receive a loan guarantee until the judgment is paid in full or otherwise satisfied or the delinquency is cured.

(b) Legal authority and responsibility.

(1) Each borrower must have, or will obtain, the legal authority necessary to construct, operate, and maintain the proposed facility and services. They must also have legal authority for obtaining security and repaying the proposed loan.

(2) The borrower shall be responsible for operating, maintaining, managing the facility and services, and providing for the continued availability and use of the facility and services at reasonable rates and terms.

(i) These responsibilities must be exercised by the borrower even though the facility may be operated, maintained, or managed by a third party

under contract, management agreement, or written lease.

(ii) Leases may only be used when this is the only feasible way to provide the service, is the customary practice to provide such service in the State, and must provide for the borrower's management control of the facility.

(iii) Contracts, management agreements, or leases must not contain options or other provisions for transfer of ownership.

(3) The lender is responsible for reviewing any contracts, management agreements, or leases to determine that they will not adversely impact the borrower's repayment ability or the security value of the guaranteed loan.

(c) Borrower. (1) A public body such as a municipality, county, district, authority, or other political subdivision of a State located in a rural area.

(2) An organization operated on a not-for-profit basis such as an association, cooperative, or private corporation. Borrowers organized under the general profit corporation laws may be eligible if they actually will be operated on a not-for-profit basis under their charter. Single member corporations or corporations owned or substantially controlled by other corporations or associations are not eligible organizations. Before a loan is made to a borrower other than a public body, the articles of incorporation or the loan agreement will include a condition similar to the following:

If the corporation dissolves or ceases to perform the community facility objectives and functions, the board of directors shall distribute all business property and assets to one or more nonprofit corporations or public bodies. This distribution must be approved by 75 percent of the users or members and must serve the public welfare of the community. The assets may not be distributed to any members, directors, stockholders, or others having financial or managerial interest in the corporation. Nothing herein shall prohibit the corporation from paying its debts.

(3) A non-public body essential community facility borrower (other than utility-type) 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) Indian tribes on Federal and State reservations and other federally recognized Indian tribes.

(d) Facilities must be located in rural areas, except:

(1) For utility-type services such as water, sewer, natural gas, or hydroelectric serving both rural and non-rural areas. In such cases, Agency funds may be used to finance only that portion serving rural areas, regardless of facility location.

(2) Telecommunication projects. The part of the facility located in a non-rural area must be necessary to provide the essential services to rural areas.

(e) All facilities financed under the provisions of this subpart shall be for public use.

(1) Facilities will be installed to serve any user within the service area who desires service and can be feasibly and legally served.

(2) In no case will boundaries for the proposed service area be chosen in such a way that any user or area will be excluded because of race, color, religion, sex, marital status, age, handicap, or national origin. This does not preclude:

(i) Financing or constructing projects in phases when it is not practical to finance or construct the entire project at one time, and

(ii) 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 facilities 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.

(3) The lender will determine that, when feasible and legally possible, inequities within the proposed project's service area for the same type service proposed (*i.e.*, water or waste disposal) 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.

§ 1980.821 Priorities.

The Agency will publish a project selection guide for administrative use. This guide will include items and conditions which must be considered in selecting preapplications for further development. Copies of this project selection guide will be available in any Agency office. When ranking eligible preapplications for consideration for limited funds, Agency officials must consider the priority items met by each preapplication and the degree to which those priorities are met. The project selection guide may change from time to time but preapplication and application will be evaluated in accordance with the project selection guide in existence at the time the preapplication is submitted.

(a) The preapplication (and supporting information submitted with it) will be used to determine the proposed project's priority for available funds.

(b) Those lenders with eligible lower-scoring preapplications which cannot be funded within the foreseeable future should be notified that funds are not available and asked if they wish to have their preapplication maintained in an active file for future consideration. Lenders whose preapplications are found to be ineligible will be advised.

(c) After completing the review, the Agency will normally select the preapplications with the highest scores for further processing. The Agency may select a lower-scoring preapplication for processing when an eligible, high-scoring preapplication:

(1) Requires more than 25 percent of the State allocation, or

(2) Exceeds the remaining State allocation for the fiscal year, or

(3) Is incomplete in that the lender has not met the administrative requirements to develop the loan. However the higher-scoring preapplication must be notified and given an opportunity to revise and resubmit their proposal. A written justification must be prepared and placed in the project file when an eligible higher-rating preapplication is not selected for further processing.

(d) The Agency will notify the lender if an application should be developed. Applications should be developed expeditiously following good management practices. Applications that are not developed in a reasonable period of time may be removed from the State's active file. Lenders will be advised when such action is taken.

(e) A cost overrun will receive consideration for funding before others.

§§ 980.822—1980.823 [Reserved]**§ 1980.824 Eligible loan purposes.**

(a) Funds may be used to construct, enlarge, extend, or otherwise improve water or waste disposal and other essential community facilities providing essential service primarily to rural residents and rural businesses.

(1) Water or waste disposal facilities include water, sanitary sewerage, solid waste disposal, and storm wastewater facilities.

(2) Essential community facilities include but are not limited to:

(i) Fire, rescue, and public safety,

(ii) Health services,

(iii) Community, social, or cultural services,

(iv) Transportation facilities such as streets, roads, and bridges,

(v) Telecommunication equipment,

(vi) Hydroelectric generating facilities and related connecting systems and appurtenances only when not eligible for financing under the authorities of the Rural Utilities Service. Funds may not be used to finance other types of electrical generating or transmitting facilities,

(vii) Supplemental and supporting structures for other rural electrification or telephone systems (including facilities such as headquarters and office buildings, storage facilities, and maintenance shops) only when not eligible for financing under the authorities of the Rural Utilities Service,

(viii) Natural gas distribution systems,

(ix) Industrial park sites (but only to the extent of land acquisition and necessary site preparation) including access ways and utility extensions to and throughout the site. Funds may not be used in connection with industrial parks to finance on-site utility systems or business and industrial buildings, and

(x) Recreational facilities.

(3) Otherwise improve includes, but is not limited to, the following:

(i) The purchase of major equipment (such as solid waste collection trucks, telecommunication equipment, and X-ray machines) which will in themselves provide an essential service to rural residents;

(ii) The purchase of existing facilities, when necessary, either to improve or to prevent a loss of service; and

(iii) Payment of tap fees and other utility connection charges as provided in utility purchase contracts.

(b) Funds also may be used:

(1) To construct or relocate public buildings, roads, bridges, fences, or utilities and to make other public improvements necessary to the successful operation or protection of

facilities authorized in paragraphs (a)(1) and (a)(2) of this section.

(2) To relocate private buildings, roads, bridges, fences, or utilities, and other private improvements necessary to the successful operation or protection of facilities authorized in paragraph (a) of this section.

(3) To pay the following expenses (but only when such expenses are a necessary part of a loan to finance facilities authorized in paragraphs (a), (b)(1), and (b)(2) of this section):

(i) Reasonable fees and costs such as origination fee, loan guarantee fee, legal, engineering, architectural, fiscal advisory, recording, environmental impact analyses, archaeological surveys, possible salvage or other mitigation measures, planning and establishing or acquiring rights.

(ii) Interest on loans until the facility is self-supporting, but not for more than 2 years unless a longer period is approved by the Agency; interest on loans secured by general obligation bonds until tax revenues are available for payment, but not for more than 2 years unless a longer period is approved by the National Office; and interest on interim financing.

(iii) Costs of acquiring interest in land; rights such as water rights, leases, permits, rights-of-way; and other evidence of land or water control necessary for development of the facility.

(iv) Purchasing or renting equipment necessary to install, maintain, extend, protect, operate, or utilize facilities.

(v) Initial operating expenses for a period ordinarily not exceeding 1 year when the borrower is unable to pay such expenses.

(vi) Refinancing debts incurred by, or on behalf of, a community when all of the following conditions exist:

(A) The debts being refinanced are less than 50 percent 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.

(4) To pay obligations for construction incurred prior to filing a preapplication and application with the Agency. Construction work should not be started (and obligations for such work or materials should not be incurred) before the Conditional Commitment for Guarantee is issued. However, if there are compelling reasons for proceeding with construction before the Conditional Commitment for Guarantee is issued, lenders may request Agency

approval to pay such obligations. Such request must comply with the following:

(i) Provide conclusive evidence that the contract was entered into without intent to circumvent the requirements of Agency regulations.

(ii) Modify the outstanding contract to conform with the provisions of this subpart. Where this is not possible, modifications will be made to the extent practicable and, as a minimum, the contract must comply with all State and local laws and regulations as well as statutory requirements and executive orders related to the Agency financing. When construction is complete and it is impracticable to modify the contracts, the borrower and lender must provide the certification required by paragraph (b)(5)(iii) of this section.

(iii) Provide a certification by an engineer or architect that any construction performed complies fully with the plans and specifications.

(iv) The borrower and the contractor must have complied with all statutory and executive order requirements related to Agency financing for construction already performed even though the requirements may not have been included in the contract documents.

§ 1980.825 Ineligible loan purposes.

Loan funds may not be used to finance:

(a) Properties to be used for commercial rental when the borrower has no control over tenants and services offered except for industrial-site development,

(b) Facilities primarily for the purpose of housing Federal or State agencies,

(c) Community antenna television services or facilities,

(d) Telephone systems,

(e) Facilities which are not modest in size, design, and cost,

(f) Finder's and packager's fees,

(g) Projects located within the Coastal Barriers Resource System that do not qualify for an exception as defined in section 6 of the Coastal Barriers Resource Act, Pub. L. 97-348 (available in any Agency office),

(h) New combined sanitary and storm water sewer facilities,

(i) Projects located in a special flood or mudslide hazard area (as designated by the Federal Insurance Administration (FIA) of the Department of Housing and Urban Development) when it is not part of an approved floodplain area management plan or flood insurance is not available.

§ 1980.826 [Reserved]

§ 1980.827 Eligible lenders.

(a) Eligible lenders (as defined in this section) may participate in the loan guarantee program. These lenders must be subject to credit examination and supervision by either an agency of the United States or a State. A lender must have the capability to adequately service loans for which a guarantee is requested. Eligible lenders are:

(1) Any Federal or State chartered:

(i) Bank, or

(ii) Savings and loan association.

(2) Any mortgage company that is a part of a bank holding company,

(3) Bank for Cooperatives, National Rural Utilities Cooperative Finance Corporation, Farm Credit Bank of the Federal Land Bank, or other Farm Credit System institution with direct lending authority authorized to make loans of the type guaranteed by this subpart,

(4) An insurance company regulated by a State or National insurance regulatory agency,

(5) State Bond Banks and State Bond Pools, and

(6) Other lenders that possess the legal powers necessary and incidental to making and servicing guaranteed loans involving community development-type projects. These lenders must also be subject to credit examination and supervision by either an agency of the United States or a State and provide documentation acceptable to the Agency that they have the ability to service the loan. Lenders under this category must be approved by the National Office prior to the issuance of the loan guarantee.

(b) When the lender's officers, stockholders, directors, or partners (including their immediate families) or the borrower, its officers, stockholders, directors, or partners (including their immediate families) own, or have management responsibilities in each other, the lender must disclose such business or ownership relationships. The Agency shall determine if such relationships are likely to result in a conflict of interest. This does not preclude lender officials from being on the borrower's board of directors.

§ 1980.828 Transfer of lenders or borrowers (prior to issuance of Loan Note Guarantee)

(a) Prior to issuance of the loan guarantee, the Agency may approve the transfer of an outstanding Conditional Commitment for Guarantee from the present lender to a new eligible lender, provided there are:

(1) A letter from the former lender stating why they do not wish to continue to be the lender for this project,

(2) No substantive changes in ownership or control of the borrower,

(3) No substantive changes in the borrower's written plan, scope of work, or changes in the purpose or intent of the project,

(4) No substantive changes in the loan agreement or Conditional Commitment for Guarantee,

(b) The substitute lender must execute a new application for loan and guarantee (available in any Agency office).

(c) If approved, the Agency will issue a letter of amendment to the original Conditional Commitment for Guarantee reflecting the new lender who will acknowledge acceptance of the offer in writing.

(d) Once the Conditional Commitment for Guarantee is issued, the Agency will not approve any substitution of borrowers including changes in the form of the legal entity. Exceptions to a change in the legal entity may be requested by Agency staff from the Agency's National Office when the original borrower is replaced with substantially the same individuals or officers with the same interest as originally approved.

§ 1980.829 Fees and charges by lender.

(a) The lender may establish the charges and fees for the loan, provided they do not exceed those charged other borrowers for similar types of transactions. "Similar types of transactions" mean those transactions involving the same type of loan which a non-guaranteed loan borrower would be assessed charges and fees.

(b) Late payment charges 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. Late payment charges may be made only if:

(1) They are routinely made by the lender in all types of loan transactions.

(2) Payment has not been received within the customary timeframe allowed by the lender.

(3) The lender agrees with the borrower, in writing, that the rate or method of calculating the late payment charges will not be changed to increase charges while the Loan Note Guarantee is in effect.

(c) The guaranteed loan fee will be the applicable guarantee fee rate multiplied by the principal loan amount multiplied by the percent of guarantee. The one-time guarantee fee is paid when the Loan Note Guarantee is issued.

(1) The fee will be paid to the Agency by the lender and is nonreturnable. The lender may pass the fee to the borrower.

(2) The guarantee fee rates are available in any Agency office.

§ 1980.830 Loan guarantee limitations.

The percentage of guarantee, up to the maximum allowed by this section, is a matter for negotiation between the lender and the Agency.

(a) The maximum allowable guarantee will be 90 percent.

(b) The lender will retain a minimum of 5 percent of the total guaranteed loan amount. The retained amount must be from the unguaranteed portion of the loan and cannot be participated to another lender.

§§ 1980.831–1980.832 [Reserved]**§ 1980.833 Interest rates.**

(a) Rates will be negotiated between the lender and the borrower. They may be either fixed or variable rates. Interest rates will be those rates customarily charged borrowers in similar circumstances in the ordinary course of business and are subject to Agency review and approval.

(b) A variable interest rate must be tied to a base rate published periodically in a recognized national or regional financial publication specifically agreed to by the lender and borrower. Such an agreement must be documented in the borrower or lender loan agreement.

(1) Interest rate caps and incremental adjustment limitations will also be negotiated between the lender and the borrower. Notice of any interest rate change proposed by the lender should allow a sufficient time period for the borrower to obtain any required State or other regulatory approval and to implement any user rate adjustments necessary as a result of the interest rate change. The intervals between interest rate adjustments will be specified in the loan agreement (but not more often than quarterly).

(2) The lender must incorporate within the variable rate note, the provision for adjustment of payments coincident with an interest rate adjustment. This will ensure the outstanding principal balance is properly amortized within the prescribed loan maturity and eliminate the possibility of a balloon payment at the end of the loan.

(c) Any change in the interest rate between the date of issuance of the Conditional Commitment for Guarantee and before the issuance of the Loan Note Guarantee must be approved by the Agency. Approval of such change will be shown on an amendment to the Conditional Commitment for Guarantee.

(d) It is permissible to have one interest rate on the guaranteed portion of the loan and another interest rate on the unguaranteed portion of the loan,

provided the lender and borrower agree, and:

(1) The rate on the unguaranteed portion does not exceed that currently being charged on loans for similar purposes to borrowers under similar circumstances; and,

(2) The rate on the guaranteed portion of the loan will not exceed the rate on the unguaranteed portion.

(e) When multi-rates are used, the lender will provide the Agency with the overall effective interest rate for the entire loan. Multi-rate loans may be either fixed, variable, or a combination of fixed and variable. When a combination of fixed and variable interest rates are used, the interest rate for the unguaranteed portion will not be lower than the guaranteed portion of the loan.

§ 1980.834 Terms of loan repayment.

(a) Principal and interest on the loan will be due and payable as provided in the note except, any interest accrued as the result of the borrower's default on the guaranteed loan over and above that which would have accrued at the note rate on the guaranteed loan will not be guaranteed by the Agency. The lender will structure repayments as established in the loan agreement between the lender and borrower. Ordinarily, such installments will be scheduled for payment as agreed upon by the lender and borrower on terms that reasonably ensure repayment of the loan. However, the first installment to include a repayment of principal may be scheduled for payment after the project is operable and has begun to generate income. Such installment must be due and payable within 3 years from the date of the note and at least annually thereafter. Interest will be due at least annually from the date of the note. Monthly payments will be required except for borrowers with income limited to less frequent intervals.

(b) The maximum time allowable for final maturity for a guaranteed CP loan will be limited to the useful life of the facility, not to exceed 40 years.

(c) The principal balance should be properly amortized within the prescribed loan maturity. Balloon payments at the end of the loan are prohibited.

§§ 1980.835–1980.836 [Reserved]**§ 1980.837 Insurance and fidelity bonds.**

The lender must provide evidence that the borrower has adequate insurance and fidelity bond coverage by loan closing or start of construction, whichever occurs first. Adequate coverage must be maintained for the life

of the loan and is subject to Agency review and approval.

§§ 1980.838–1980.839 [Reserved]**§ 1980.840 Equal opportunity and Fair Housing Act requirements.**

(a) The lender will comply with the requirements of title V of the Equal Credit Opportunity Act (Pub. L. 93–495). See the Federal Reserve Board Regulation, 12 CFR part 202.

(b) Certain housing-related projects such as nursing homes, group homes, or assisted-living facilities must comply with the requirements of the Fair Housing Amendment Act of 1988 (Pub. L. 100–430). This includes completion of an Affirmative Fair Housing Marketing Plan and compliance with the Housing and Urban Development accessibility guidelines except for areas open to the public which are covered by the Americans with Disabilities Act (Pub. L. 101–336). The lender will determine that the borrower has a valid plan in effect at all times.

§ 1980.841 [Reserved]**§ 1980.842 Design and construction requirements.**

The lender will provide the Agency with a written certification at the end of construction that all funds were utilized for authorized purposes. The borrower and the lender will authorize designs and plans based upon the preliminary architectural and engineering reports approved by the lender and concurred in by the Agency. The borrower will take into consideration any lender or Agency comments when the facility is being designed.

(a) All project facilities must be designed utilizing accepted architectural and engineering practices and must conform to applicable Federal, State, and local codes and requirements. The lender must ensure that the planned project will be completed within the available funds and, once completed, will be suitable for the borrower's needs.

(b) The lender will monitor the progress of construction and undertake the reviews and inspections necessary to ensure that construction proceeds in accordance with the approved plans, specifications, and contract documents and that funds are used for eligible project costs. The lender must expeditiously report any problems in project development to the Agency.

(c) For all construction contracts in excess of \$10,000, the contractor must comply with Executive Order 11246 entitled "Equal Employment Opportunity" as amended by Executive Order 11375, and as supplemented by

applicable Department of Labor regulations (41 CFR part 60). The borrower and lender are responsible for ensuring that the contractor complies with these requirements.

(d) Community Facilities loans which involve the construction of, or addition to, facilities that accommodate the public and commercial facilities as defined by the Americans with Disabilities Act (Pub. L. 101-336) must comply with this Act. The lender and borrower are responsible for compliance.

§ 1980.843 Other Federal, State, and local requirements.

In addition to the specific requirements of this subpart and beginning on the date of issuance of the Loan Note Guarantee, proposals for facilities financed in whole or in part with a loan guaranteed by the Agency will be coordinated with all appropriate Federal, State, and local agencies. Borrowers and lenders will be required to comply with any Federal, State, or local laws or regulatory commission rules which are in existence and which affect the project including, but not limited to:

- (a) Organization and authority to design, construct, develop, operate, and maintain the proposed facilities;
- (b) Borrowing money, giving security, and raising revenues for repayment;
- (c) Land use zoning;
- (d) Health, safety, and sanitation standards; and
- (e) Protection of the environment and consumer affairs.

§§ 1980.844–1980.846 [Reserved]

§ 1980.847 Economic feasibility requirements.

All projects financed under the provisions of this section must be based on taxes, assessments, revenues, fees, or other sources of revenues in an amount sufficient to provide for facility operation and maintenance, a reasonable reserve, and debt payment. Other sources of revenue or guarantors are particularly important in considering the feasibility of recreation-type loans. The lender is responsible for determining the credit quality and economic feasibility of the proposed loan and must address all elements of the credit quality in a written financial feasibility analysis which includes adequacy of equity, cash flow, security, history, and management capabilities. Financial feasibility reports must take into consideration any interest rate adjustment which may be instituted under the terms of the note.

(a) The borrower may prepare the financial feasibility analysis (suggested

financial feasibility guidelines are available in any Agency office) in the following instances:

- (1) Facilities primarily used for fire and rescue services;
- (2) Facilities that are not dependent on facility revenues for debt payment;
- (3) Loans of less than \$500,000; or
- (4) Projects in which the borrower has operated similar facilities on a financially successful basis.

(b) The borrower's consulting engineer may complete the financial feasibility analysis for utility systems.

(c) Financial feasibility reports for all other facilities must be prepared by a qualified entity not having a direct interest in the management of the facility. The lender may prepare the feasibility study if qualified staff is available.

(d) The Agency loan approval official may exempt the lender from the requirement for an independent financial feasibility report (when requested by the borrower and the lender) provided the approval official determines that the financial feasibility analysis prepared by the borrower fairly represents the financial feasibility of the facility and the financial feasibility analysis contains an accurate projection of the usage, revenues, and expenses of the facility.

(e) When the lender or Agency has insufficient information to determine the borrower's repayment ability, an independent feasibility analysis will be required.

§ 1980.848 Security.

(a) The lender is responsible for obtaining and maintaining proper and adequate security to protect the interest of the lender, the holder, and the Government.

(b) Security must be of such a nature that repayment of the loan is reasonably ensured when considered with the integrity and ability of project management, soundness of the project, and the borrower's prospective earnings. The security may include, but is not limited to, the following: General obligation bonds, revenue bonds, pledge of taxes or assessments, assignment of facility revenue, land, easements, rights-of-way, water rights, buildings, machinery, equipment, accounts receivable, contracts, cash, or other accounts or assignments of leases or leasehold interest.

(c) All security must secure the entire loan. The lender will not take separate security to secure only the unguaranteed portion of the loan. The lender will not require compensating balances or certificates of deposit as a means of

eliminating the lender's exposure on the unguaranteed portion of the loan.

(d) For projects utilizing joint financing with the same security to be shared, the Agency guaranteed loan will be secured by at least a parity (equal) lien position.

§§ 1980.849–1980.851 [Reserved]

§ 1980.852 Processing.

(a) *Preapplications.* (1) The preapplication package may be submitted alone or simultaneously with the application. The preapplication package will contain:

(i) An application for Federal assistance (available in any Agency office).

(ii) State intergovernmental or other type review comments and recommendations for the borrower's project (clearinghouse comments, if applicable).

(iii) Supporting documentation necessary to make an eligibility determination such as financial statements, audits, copies of organizational documents, existing debt instruments, etc. The Agency will advise lenders and borrowers on what documents are necessary. Borrowers should not expend significant amounts of money or time developing supporting documentation at the preapplication stage.

(iv) Documentation of lender eligibility in accordance with § 1980.828.

(2) The Agency will review each application for Federal assistance along with other information that is deemed necessary to determine eligibility and whether financing from commercial sources at reasonable rates and terms is available without a guarantee.

(3) If the project appears to be eligible, has sufficient priority, is economically feasible, and loan guarantee authority is expected to be available, the Agency will inform the lender and borrower, in writing, and request a complete application. An environmental review will be necessary, and no major commitment should be made by the lender or borrower that could affect the consideration of alternatives.

(b) *Applications.* Contents of application package.

(1) Application for loan and guarantee (available in any Agency office),

(2) Proposed loan agreement,

(3) Request for environmental information (available in any Agency office),

(4) Preliminary architectural or engineering report,

(5) Cost estimates,

(6) Appraisal reports (as appropriate),

- (7) Credit reports,
- (8) Financial feasibility analysis and report, and
- (9) Any additional information required.

§ 1980.853 Evaluation of application.

The Agency will evaluate the application and determine whether the borrower is eligible, the proposed loan is for an eligible purpose, there is reasonable assurance of repayment ability, sufficient collateral and equity exists, the proposed loan complies with all applicable statutes and regulations, and adequate funds are available. If approved, the Agency will provide the lender and the borrower with the Conditional Commitment for Guarantee, listing all conditions for the guarantee. Applicable requirements will include the following:

- (a) Approved use of guaranteed loan funds (source and use of funds),
- (b) Rates and terms of the loan,
- (c) Scheduling of payments,
- (d) Number of customers,
- (e) Security and lien priority requirements,
- (f) Appraisal requirements,
- (g) Insurance and bonding requirements,
- (h) Financial reporting requirements,
- (i) Equal opportunity and nondiscrimination requirements,
- (j) Environment or mitigation requirements,
- (k) Americans with Disabilities Act requirements,
- (l) By-laws and articles of incorporation change requirements, and
- (m) Other requirements necessary to protect the Government.

§§1980.854—1980.858 [Reserved]

§1980.859 Review of requirements.

(a) Immediately after reviewing the Agency's conditions and requirements in the Conditional Commitment for Guarantee, the lender and borrower must complete and sign the Acceptance of Conditions and return a copy to the Agency. Notwithstanding the preceding sentence, if certain conditions cannot be met, the lender and borrower may propose alternate conditions for Agency consideration.

(b) If the lender indicates in the Acceptance of Conditions that it desires to obtain a Loan Note Guarantee and subsequently decides at any time after receiving a Conditional Commitment for Guarantee that it no longer wants a guarantee, the lender must immediately advise the Agency.

§§ 1980.860—1980.862 [Reserved]

§ 1980.863 Conditions precedent to issuance of the Loan Note Guarantee.

The Loan Note Guarantee will not be issued until:

- (a) The lender certifies that:
 - (1) No major changes have been made in the lender's loan conditions and requirements since the issuance of the Conditional Commitment for Guarantee except those approved in the interim by the Agency in writing.
 - (2) All planned property acquisition has been completed and all development has been substantially completed in accordance with plans and specifications. All costs have not exceeded the amounts approved by the lender and the Agency.
 - (3) Required insurance is in effect.
 - (4) Truth in lending requirements have been met.
 - (5) All equal employment opportunity and Fair Housing Plan requirements have been met.
 - (6) The loan has been properly closed and the required security instruments have been obtained on any after-acquired property that cannot be covered initially under State statutory provisions.
 - (7) The borrower has marketable title to the collateral then owned by the borrower, subject to the instrument securing the loan to be guaranteed and subject to any other exceptions approved, in writing, by the Agency.
 - (8) 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 time.
 - (9) All other requirements of the Conditional Commitment for Guarantee have been met.

(10) Lien priorities are consistent with requirements of the Conditional Commitment for Guarantee.

(11) The loan proceeds have been disbursed for purposes and in amounts consistent with the Conditional Commitment for Guarantee and as specified on the application for the guaranteed loan. A copy of a detailed statement by the lender detailing the use of loan funds will be attached to support this certification.

(12) There has been no substantive adverse change in the borrower's financial condition nor any other adverse change in the borrower during the period of time from the Agency's issuance of the Conditional Commitment for Guarantee to issuance of the Loan Note Guarantee. The lender's certification must address all adverse changes of the borrower and the guarantors. For purposes of this

paragraph, the term borrower includes any parent, affiliate, or subsidiary of the borrower.

(13) All Federal, State, and local design and construction requirements have been met.

(14) The lender understands and will meet the requirements of chapter 37 of title 31 of the United States Code.

(15) The lender would not make the loan without an Agency guarantee.

(b) The lender has executed and delivered the Lender's Agreement and closing report for the guaranteed loan along with the appropriate guarantee fee.

(c) The lender has advised the Agency of plans to sell or assign any part of the loan as provided in the Lender's Agreement.

(d) The lender agrees that once the Conditional Commitment for Guarantee is issued and accepted by the lender and borrower, it shall not be modified as to the scope of the project, overall facility concept, project purpose, use of proceeds, or terms and conditions. Only minor changes will be considered unless otherwise provided for in this subpart.

(e) Where applicable, the lender must certify that the borrower has obtained:

(1) 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.

(2) A title report showing ownership of the land and all mortgages or other lien defects, restrictions, 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 reservoir or pumping station) and the lender and borrower are able to obtain only a right-of-way or easement on such a site rather than a fee simple title, such a title report should be requested.

(f) For loans exceeding \$150,000, the lender has certified its compliance with Public Law 101-121 (Anti-lobbying Act). 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.

(g) If the Loan Note Guarantee cannot be issued before the Conditional Commitment expires, the lender must submit a written request for an extension of the expiration date. The lender must document and certify to paragraph (a)(1), (a)(12), and (e) of this section specifically identifying any modifications.

(h) Coincident with, or immediately after, loan closing, the lender will contact the Agency and provide those documents and certifications required in this section. For loans to public bodies, lenders may require an opinion from recognized bond counsel regarding the adequacy of the preparation and issuance of the debt instruments. Only when the Agency is satisfied that all conditions for the guarantee have been met will the Loan Note Guarantee be executed.

§ 1980.864 Issuance of Lender's Agreement, Loan Note Guarantee, and Assignment Guarantee Agreement.

(a) If the Agency finds that all requirements have been met, the lender and the Agency will execute the Lender's Agreement. The original will be retained by the Agency and a signed duplicate original will be retained by the lender. A Lender's Agreement must be executed for all loans to be guaranteed by the Agency.

(b) *Loan Note Guarantee.* (1) Upon receipt of the executed Lender's Agreement and after all requirements have been met, the Agency will execute the Loan Note Guarantee. All originals of the Loan Note Guarantee will be provided to the lender and attached to the note.

(2) If the lender has selected the multi-note system, a Loan Note Guarantee will be prepared and attached to each note the borrower issues. All the notes will be listed on the Loan Note Guarantee. Not more than ten notes will be issued for the guaranteed portion (unless the Agency and borrower agree otherwise) and one note issued for the unguaranteed portion.

(c) In the event the lender assigns the guaranteed portion of the loan to a holder, the lender, holder, and Agency will execute an Agency prescribed Assignment Guarantee Agreement. The original of the agreement will be provided to the holder with conformed copies to the lender and the Agency. If the lender desires to assign a part of the

guaranteed loan to a holder, an Agency prescribed Assignment Guarantee Agreement will be executed for each assigned portion.

(d) If requested by the lender, the Agency will provide a Certificate of Incumbency and signature and title of the Agency official who executes the Agency prescribed Loan Note Guarantee, Lender's Agreement, and Assignment Guarantee Agreement.

(e) If the Agency determines that it cannot execute the Loan Note Guarantee because all requirements have not been met, the lender will have a reasonable period within which to satisfy the objections. If the lender satisfies the objections within the time allowed, the guarantee will be issued.

(f) The lender will prepare and deliver a guaranteed loan closing report for each loan to be guaranteed and guarantee fee to the Agency which concurrently will deliver the Loan Note Guarantee.

§ 1980.865 Lender's sale or assignment of guaranteed portion of loan.

The lender may retain all of the guaranteed loan. The lender must not sell or participate any amount of the guaranteed or non-guaranteed portion of the loan to the borrower or to members of the borrower's immediate families, the borrower's officers, directors, stockholders, other owners, or a subsidiary or affiliate. Disposition of the guaranteed portion of a loan may not be made prior to full disbursement, completion of construction, and acquisition without the prior written approval of the Agency. If the lender desires to market all or part of the guaranteed portion of the loan at, or subsequent to, loan closing, such loan must not be in default.

(a) *Assignment.* 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. Should the lender know at the time the loan application is prepared that it plans to sell or assign any part of the guaranteed portion, the lender will provide this information with the application.

(b) *Participation.* The lender may obtain participation in the loan under its normal operating procedures.

(c) *Minimum retention.* The lender is required to hold in its own portfolio or retain a minimum of 5 percent of the total guaranteed loan amount. This amount must be of the non-guaranteed portion of the loan and cannot be participated to another. The lender may sell the remaining amount of the non-guaranteed portion of the loan only through participation.

§§ 1980.866—1980.868 [Reserved]

§ 1980.869 Loan servicing.

(a) The lender is responsible for servicing the entire loan in accordance with the lender's loan agreement. The unguaranteed portion of the loan will not be paid first nor given any preference or priority over the guaranteed portion of the loan. The lender is responsible for taking all servicing actions that a prudent lender would perform in servicing their portfolio of loans that are not guaranteed. This responsibility includes, but is not limited to, the collection of payments; obtaining compliance with the covenants and provisions in the note, loan agreement, security instrument, or any supplemental agreements; obtaining and analyzing financial statements; verifying the payment of taxes and insurance premiums; and maintaining liens on collateral. The lender will notify the Agency of any violations of the loan agreement with the borrower.

(b) The lender will require, at a minimum, annual audited financial statements which will be reviewed by the lender and a copy forwarded to the Agency with a summary evaluation by the lender. The lender will service delinquent loans in accordance with the lender's agreement. The Agency may waive the audit requirement for financial statements for borrowers with gross annual income of less than \$500,000.

(c) The lender must report the outstanding principal and interest balance on each guaranteed loan semi-annually.

(d) The lender will inspect the collateral as often as necessary to properly service the loan.

§§ 1980.870—1980.872 [Reserved]

§ 1980.873 Replacement of loss, theft, destruction, mutilation, or defacement of Loan Note Guarantee or Assignment Guarantee Agreement.

(a) The Agency may issue a replacement Loan Note Guarantee or Assignment Guarantee Agreement which may have been lost, stolen, destroyed, mutilated, or defaced to the lender or holder upon receipt of an acceptable certificate of loss and an indemnity bond.

(b) When a Loan Note Guarantee or Assignment Guarantee Agreement is lost, stolen, destroyed, mutilated, or defaced while in the custody of the lender or holder, the lender will coordinate the activities of the party who seeks the replacement documents and will submit the required documents to the Agency for processing. The

requirements for replacement are as follows:

(1) A certificate of loss properly notarized which includes:

(i) Legal name and present address of either the lender or the holder who is requesting the replacement forms,

(ii) Legal name and address of the lender of record,

(iii) Capacity of person certifying,

(iv) Full identification of the Loan Note Guarantee or Assignment Guarantee agreement including the name of the borrower, Agency case number, date of the Loan Note Guarantee, Assignment Guarantee Agreement, face amount of the evidence of debt purchased, date of evidence of debt, present balance of the loan, percentages of guarantee and, if Assignment Guarantee Agreement, the original named holder and the percentage of the guaranteed portion of the loan assigned to that holder. Any existing parts of the document to be replaced must be attached to the certificate,

(v) A full statement of circumstances of the loss, theft, or destruction of the Loan Note Guarantee or Assignment Guarantee Agreement, and

(vi) The holder shall present evidence demonstrating current ownership of the Loan Note Guarantee and Note or Assignment Guarantee Agreement. If the present holder is not the same as the original holder, a copy of the endorsement of each successive holder in the chain of transfer from the initial holder to present holder must be included. If copies of the endorsement cannot be obtained, best available records of transfer must be presented to the Agency (e.g., order confirmation, canceled checks, etc.).

(2) An indemnity bond acceptable to the Agency shall accompany the request for replacement except when the holder is the United States, a Federal Reserve Bank, a Federal Government corporation, a State or Territory, or the District of Columbia.

(3) All indemnity bonds must be issued and payable to the United States of America. The bond shall be in an amount not less than the unpaid principal and interest. The bond shall hold the Government harmless against any claim or demand which might arise or against any damage, loss, costs, or expenses which might be sustained or incurred by reasons of the loss or replacement of the instruments.

§ 1980.874 [Reserved]

§ 1980.875 Defaults by borrower.

(a) The lender must notify the Agency when a borrower is 30 days past due on

a payment, has not met its responsibilities of providing the required financial statements, or is otherwise in default. The lender will continue to keep the Agency informed on a bimonthly basis until such time as the loan is no longer in default. If a monetary default exceeds 60 days, the lender will arrange a meeting with the borrower to resolve the default. The lender must advise the Agency of the meeting in the event an Agency representative wishes to attend. The lender will provide a summary of the meeting and any decisions or actions agreed upon.

(b) In considering servicing options, the prospects for providing a permanent cure without adversely affecting the risks to the Agency and the lender must be the paramount objective. Temporary curative actions (such as payment deferrals or collateral subordination) must strengthen the loan and be in the best financial interest of the lender and the Agency. Some of these actions may require concurrence of the holder.

(c) If the loan was closed with the multi-note option, the lender may need to possess all notes to take some servicing actions. In those situations when the Agency is holder of some of the notes, the Agency may endorse the notes back to the lender, provided a proper receipt is received from the lender which defines the reason for the transfer. Under no circumstances will the Agency endorse the original Loan Note Guarantee to the lender.

§§ 1980.876–1980.877 [Reserved]

§ 1980.878 Repurchase of loan.

(a) The lender has the option to repurchase the loan from a holder within 30 days of written demand from the holder when the borrower is in default not less than 60 days on principal or interest. The repurchase will be for an amount equal to the unpaid guaranteed portion of principal and accrued interest less the lender's servicing fee. The guarantee does not cover the note interest to the holder on the guaranteed loan accruing after 90 days from the date of the demand letter to the lender. The holder will concurrently send a copy of the demand to the Agency. The lender will accept an assignment without recourse from the holder upon repurchase. The lender is encouraged to repurchase the loan to facilitate the accounting of funds, resolve the problem, and permit the borrower to cure the default, where reasonable. The lender will notify the holder and the Agency of their decision within 30 days of receipt of demand from the holder.

(b) *Agency repurchase.* (1) If the lender does not repurchase as provided in paragraph (a) of this section, the Agency will purchase from the holder the unpaid principal balance of the guaranteed portion together with accrued interest to date of repurchase (less the lender's servicing fee) within 30 days after written demand to the Agency. The guarantee will not cover the note interest to the holder on the guaranteed loan accruing after 90 days from the date of the original demand letter. The lender shall not charge the Agency any servicing fees nor are any such fees collectible from the Agency.

(2) The holder's demand to the Agency must include a copy of the written demand made upon the lender. The holder or duly authorized agent must also include evidence of the right to require payment from the Agency. Such evidence will consist of either the original of the Loan Note Guarantee properly endorsed to the Agency or the original of the Assignment Guarantee Agreement properly assigned to the Agency without recourse including all rights, title, and interest in the loan. The Agency will be subrogated to all rights of the holder. The holder must include in the demand the amount due including unpaid principal, unpaid interest to date of demand, and interest subsequently accruing from the date of demand to the proposed payment date. Unless otherwise agreed to by the Agency, such proposed payment will not be later than 30 days from the date of demand.

(3) The lender must promptly provide the Agency with the information necessary for the Agency's determination of the appropriate amount due the holder upon the Agency's notification to the lender of the holder's demand for payment. This information must be certified by an authorized officer of the lender. Any discrepancy between the amount claimed by the holder and the information submitted by the lender must be resolved before payment will be approved. The Agency will notify both parties and such conflict will suspend the running of the 30-day payment requirement.

(4) 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 nor does it waive any of the Agency's rights against the lender. The Agency may set off against the lender all rights inuring to the Agency as the holder of the instrument against the Agency's obligation to the lender under the Loan Note Guarantee.

(c) When the lender determines that repurchase of the guaranteed portion of the loan is necessary to service the loan, the holder must sell the guaranteed portion to the lender for the unpaid principal and interest balance (less the lender's servicing fee). The guarantee does not cover interest accruing after 90 days from the date the lender's or Agency's letter requesting the holder to tender its guaranteed portion. The lender must not repurchase from the holder for arbitrage purposes to further its own financial gain. Any repurchase must be made only after the lender obtains the Agency written approval. If the lender does not repurchase the portion from the holder, the Agency may, at its option, purchase such guaranteed portion for servicing purposes.

§ 1980.879 Transfer of lender after issuance of Loan Note Guarantee.

Subsequent to issuance of the Loan Note Guarantee, the Agency may, under extraordinary circumstances, approve the transfer of an outstanding Loan Note Guarantee from the present lender to another eligible lender, provided the new lender agrees to assume all original loan requirements including liabilities, servicing responsibilities, and acquiring legal title to the unguaranteed portion of the loan.

§ 1980.880 Interest rate changes after loan closing.

(a) The borrower, lender, and holder (if any) may collectively effect a permanent reduction in the interest rate on the guaranteed loan at any time during the life of the loan on written agreement by these parties. After such a permanent reduction, the Loan Note Guarantee will only cover losses in interest at the reduced interest rate. The Agency must be notified by the lender, in writing, within 10 calendar days of the change. When the Agency is a holder, it will concur only when it is demonstrated that the change is more viable than liquidation and that the Government's financial interests are not adversely affected. Factors which will be considered in making such determination are the Government's cost of borrowing money and the project's enhancement of rural development. The monetary recovery must be greater than the liquidation recovery, and a financial feasibility analysis must show the project's continued viability.

(1) Fixed rates cannot be changed to variable rates to reduce the interest rate to the borrower unless the variable rate has a ceiling which is less than the original fixed rate.

(2) Variable rates can be changed to a lower fixed rate. 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 which adequately document the accrued interest claimed.

(3) The lender is responsible for the legal documentation of interest rate changes. However, the lender may not issue a new note.

(b) No increases in interest rates will be permitted under the loan guarantee except the normal fluctuations in approved variable interest rate loans.

§ 1980.881 Liquidation.

Liquidation will occur when the lender concludes that liquidation of the guaranteed loan is necessary because of one or more defaults or third party actions that the borrower cannot, or will not, cure or eliminate within a reasonable period of time and the Agency concurs with the lender; or the Agency, at any time, independently concludes that liquidation is necessary. The lender, or the Agency (if it liquidates) will proceed as expeditiously as possible, including giving any notices or taking any legal actions required by the security instruments.

(a) If a lender has made a loan guaranteed by the Agency under regulations in this subpart in effect prior to [the effective date of the final rule]¹, the lender has the option to liquidate the loan under the provisions of this subpart in effect on [the effective date of the final rule] or under the provisions in effect previous to that date. The lender will notify the Agency in writing within 10 days after its decision to liquidate, which regulatory provisions they choose to use. The lender may not choose some provisions in effect on one date and other provisions in effect on another date.

(b) If a lender acquires title to property, the Agency may elect to permit the lender the option of calculating the final loss settlement using the net proceeds received at the time of the ultimate disposition of such property. The lender must submit a written request within 15 days of acquiring title for this option to the Agency, and the Agency must agree, in writing, prior to the lender submitting any request for estimated loss payment.

¹ See 7 CFR part 180, subpart I, contained in the 7 CFR, parts 1950 to 1999, edition revised as of January 1, 1997 and amended at [Federal Register cites and dates to be inserted in final rule].

(c) The lender will (within 30 days after a decision to liquidate) submit to the Agency, in writing, a proposed, detailed liquidation plan. Upon approval by the Agency of the liquidation plan, the lender will commence liquidation. When the Agency liquidates, reasonable liquidation expenses will be assessed against the proceeds derived from the sale of the collateral. The lender's liquidation plan must include, but is not limited to, the following:

(1) Such proof as the Agency requires to establish the lender's ownership of the guaranteed loan notes and related security instruments, a copy of the payment ledger or other documentation which reflects the outstanding loan balance and accrued interest to date, and the method of computing the interest;

(2) A complete list of all collateral;

(3) The recommended liquidation methods for making the maximum collection possible on the indebtedness and the justification for such methods, including the recommended action for acquiring and disposing of all collateral;

(4) Necessary steps for preservation of the collateral;

(5) Copies of the borrower's latest available financial statements;

(6) An itemized list of estimated liquidation expenses expected to be incurred and justification for each expense;

(7) A schedule to periodically report to the Agency on the progress of the liquidation;

(8) Estimated protective advance amounts with justification;

(9) Proposed protective bid amounts on collateral to be sold at auction and a breakdown on how the amounts were determined;

(10) If a voluntary conveyance is considered, the proposed amount to be credited to the guaranteed debt;

(11) Legal opinions, as needed; and

(12) If the outstanding balance of principal and interest is less than \$200,000, the lender will obtain an estimate of fair market and potential liquidation value of the collateral. If the outstanding balance of principal and interest is \$200,000 or more, the lender will obtain an independent appraisal report on all collateral securing the loan which will reflect the fair market value and potential liquidation value. The independent appraiser's fee will be shared equally by the Agency and the lender.

(d) If actions are necessary to immediately preserve and protect the collateral, a partial liquidation plan may be submitted and when approved, must

be followed by a complete liquidation plan prepared by the lender.

(e) Disposition of collateral acquired by the lender must be approved by the Agency.

(1) There may be instances when the lender acquires the collateral of a borrower where the cost of liquidation exceeds the potential recovery value of the security. Whenever this occurs, the lender, with the concurrence of the National Office, may abandon the collateral in lieu of liquidation.

(2) Sale of acquired collateral to the borrower, borrower's stockholders or officers, or the lender or lender's stockholders or officers requires the written concurrence of the Agency.

(f) The Agency will exercise the option to liquidate only when there is reason to believe the lender is not likely to initiate liquidation efforts that will result in maximum recovery. When the Agency liquidates, reasonable liquidation expenses will be assessed against the proceeds derived from the sale of the collateral.

(g) Final loss payments will be made within the 60 days required but only after all collateral has been properly accounted for and liquidation expenses are determined to be reasonable and within approved limits. Any estimated loss payments made to the lender will be credited against the final loss on the guaranteed loan. The amount of an estimated loss payment must be credited as a deduction from the principal balance of the loan.

§1980.882 [Reserved]

§1980.883 Protective advances.

Protective advances constitute an indebtedness of the borrower to the lender and must be secured by collateral to the same extent as principal and interest. Protective advances include, but are not limited to, advances made for taxes, annual assessments, ground rent hazard, or flood insurance premiums affecting the collateral (including any other expenses necessary to protect the collateral). Attorney fees are not a protective advance.

(a) The Agency must approve, in writing, all protective advances on loans within their loan approval authority which exceed a total cumulative advance amount of \$500 to the same borrower. Protective advances must be reasonable when associated with the value of the collateral being preserved.

(b) When considering protective advances, sound judgment must be exercised in determining that the additional funds advanced will actually preserve collateral interests and recovery is actually enhanced by making the advance.

§1980.884 Additional loans or advances.

The lender will not make additional expenditures or new loans to the borrower without first obtaining the written approval of the Agency even though such expenditures or loans will not be guaranteed.

§1980.885 Bankruptcy.

(a) An Agency Report of Loss form will be used for calculating estimated and final loss determinations.

(b) Lender's are responsible to protect the guaranteed loan debt and all the collateral securing it in bankruptcy proceedings. These responsibilities include, but are not limited to, the following:

(1) Filing a proof of claim, where necessary, and all necessary papers and pleadings,

(2) Attending and, where necessary, participating in meetings of the creditors and all court proceedings,

(3) Immediately seeking adequate protection of the collateral if its collateral is subject to being used by the trustee in bankruptcy or the debtor in possession.

(4) Where appropriate, seeking involuntary conversion of a pending Chapter 11 case to a liquidation proceeding or seeking dismissal of the proceedings, and

(5) Keeping the Agency adequately and regularly informed, in writing, of all aspects of the proceedings.

(c) In a Chapter 9 or Chapter 11 reorganization, obtaining an independent appraisal of the collateral if the Agency believes an independent appraisal is necessary, the Agency and the lender will share the appraisal fee equally.

(d) Only expenses of Chapter 11 reorganizations, or Chapter 11 or Chapter 7 liquidations (unless the liquidation is by the lender) authorized by the court may be deducted from the collateral proceeds.

(e) The Agency or the lender, with the approval of the Agency, may initiate the repurchase of the unpaid guaranteed portion of the loan from the holder. If the lender is the holder, an estimated loss payment may be filed at the initiation of a Chapter 7 proceeding or after a Chapter 11 proceeding becomes a liquidation proceeding. On loans in bankruptcy, any loss payment must be approved by the Agency.

(f) The Agency must approve, in advance and in writing, the lender's estimated liquidation expenses of collateral in liquidation bankruptcy. These expenses must be reasonable and customary and not include in-house expenses of the lender.

§§ 1980.886–1980.887 [Reserved]

§ 1980.888 Transfers and assumptions.

(a) The Agency will approve in writing transfers and assumptions of loans to transferees who will continue the original purpose of the guaranteed loan.

(1) When the transaction is to a member of the borrower's organization, it will be at a price which will not result in a loss to the lender.

(2) Transfers to eligible borrowers will receive preference over transfers to ineligible borrowers if recovery to the lender from the sale price is not less than it would be if the transfer was to an ineligible borrower.

(3) The present borrower is unable or unwilling to accomplish the objectives of the guaranteed loan, and the transfer will be to the lender's and Agency's advantage.

(4) The transferee will assume an amount at least equal to either the present market value or the debt, whichever is less. The percentage of the Agency's guarantee will be based on the amount assumed.

(5) The lender concurs in the plans for disposition of funds in the transferor's debt service, reserve, and operation and maintenance account.

(b) Transfers to eligible borrower.

(1) The total indebtedness may be transferred to an eligible borrower on the same terms.

(2) The total indebtedness may be transferred to another eligible borrower on different terms not to exceed those terms for which an initial guaranteed loan can be made.

(3) Less than the total indebtedness may be transferred to another eligible borrower on the same or different terms.

(4) A guaranteed loan for which the transferee is eligible may be made in connection with a transfer subject to the policies and procedures governing the kind of loan being made.

(5) If the transferor is to receive a payment for the equity, the total debt must be assumed.

(c) Transfers to ineligible borrowers are considered only when needed as a method for servicing problem cases when an eligible transferee is not available. Transfers should not be considered as a means by which members can obtain equity or as a method of providing a source of easy credit for purchasers. Transfers are as follows:

(1) All transfers to ineligible borrowers will include a one-time nonrefundable transfer fee. Transfer fees will be collected, and payments applied, in accordance with paragraph (d) of this section.

(2) For all loans covered by this subpart, the Agency may approve a transfer of indebtedness to, and assumption of, a loan by a transferee who does not meet the eligibility requirements for the kind of loan being assumed when the ineligible borrower will:

(i) Make a significant downpayment, and

(ii) Agree to pay the remaining balance within not more than 15 years. Installments will be at least equal to the amount amortized over a period not greater than the remaining life of the debt being transferred, and the balance will be due the fifteenth year.

(3) Interest rates to ineligible transferees will be the rate specified in the note of the transferor or the rates customarily charged borrowers in similar circumstances in the ordinary course of business and are subject to Agency review and approval. The rates may be either fixed or variable.

(i) Transferees must have the ability to repay the debt according to the Assumption Agreement and must have the legal authority to enter into the contract. The transferee will submit a current balance sheet. The lender will obtain and analyze the credit history of the transferee. In all transfers, consideration will be given to obtaining individual liability agreements from members of the transferee organization.

(ii) The transferor may receive equity payments when the full amount of the debt is assumed. However, equity payments will not be made on more favorable terms than those on which the balance of the debt will be paid.

(d) Transfer fees are a one-time nonrefundable cost to be collected by the lender at the time of application or proposal.

(1) The transfer fees will be a standard fee plus the cost of the appraisal.

(2) The lender will collect and submit the fee to the Agency.

(3) The Agency's National Office may waive the transfer fee if it determines that such waiver is in the best interest of the Agency.

(e) *Processing transfers and assumptions.* (1) In any transfer and assumption case, the transferor (including any guarantors) may be released from liability by the lender 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, or part of the loan, being assumed. If the transfer is for less than the entire debt:

(i) The Agency must determine that the transferor and any guarantors have no reasonable debt-paying ability

considering their assets and income at the time of transfer, and

(ii) The lender must certify that the transferor has cooperated in good faith, used due diligence to maintain the collateral against loss, and has otherwise fulfilled all of the regulations of this subpart to the best of the borrower's ability.

(2) The lender will make, in all cases, a complete credit analysis to determine viability of the project (subject to the Agency review and approval) including any requirement for deposits in an escrow account as security to meet the determined equity requirements for the project.

(3) The lender will issue a statement that the transaction can be properly transferred and the conveyance instruments will be filed, registered, or recorded as appropriate and legally permissible.

(4) The assumption will be made on the lender's form of Assumption Agreement and will contain the Agency case number of the transferor and transferee.

(5) Loan terms cannot be changed by the Assumption Agreement unless previously approved in writing by the Agency with the concurrence of any holder and the transferor (including guarantors) if they have not been released from personal liability. Any new loan terms cannot exceed those authorized in this subpart. The lender's request will be supported by:

(i) An explanation of the reasons for the proposed change in the loan terms.

(ii) Certification that the lien position securing the guaranteed loan will be maintained or improved, proper hazard insurance will be continued in effect, and all applicable Truth in Lending requirements will be met.

(6) In the case of a transfer and assumption, it is the lender's responsibility to see that all such transfers and assumptions will be noted on all originals of the Loan Note Guarantee. The lender will provide the Agency a copy of the Transfer and Assumption Agreement.

(7) If a loss should occur upon a complete transfer of assets and assumption for less than the full amount of the debt and the transferor-debtor (including personal guarantor) is released from personal liability (as provided in paragraph (e) of this section), the lender (if holding the guaranteed portion) may file an estimated Report of Loss to recover their pro rata share of the actual loss at that time. Approved protective advances and accrued interest made during the arrangement of a transfer and assumption, if not assumed by the

transferee, will be entered on the estimated Report of Loss.

§ 1980.889 Mergers.

(a) The Agency may approve mergers or consolidations (referred to in this section as "mergers") when the resulting organization will be eligible for an Agency guaranteed loan and assumes all the liabilities and acquires all the assets of the merged borrower. Mergers may be approved when:

(1) The merger is in the best interest of the Government and the merging borrower.

(2) The resulting borrower can meet all required conditions as set forth in specific loan note agreements.

(3) All property can be legally transferred to the resulting borrower.

(b) Distinguishing mergers from transfers and assumptions. Mergers occur when one corporation combines with another corporation in such a way that the first corporation ceases to exist as a separate entity while the other continues. In a consolidation, two or more corporations combine to form a new, consolidated corporation with the original corporations ceasing to exist. Such transactions must be distinguished from transfers and assumptions in which a transferor will not necessarily go out of existence, and the transferee will not always take all the transferor's assets, nor assume all the transferor's liabilities.

§ 1980.890 Disposition of acquired property.

(a) When the lender acquires title to the collateral and the final loss claim is not paid until final disposition, the lender must proceed as quickly as possible to develop a plan to fully protect the collateral and the lender must dispose of the collateral without delay.

(b) Any collateral accepted by the lender must not be titled in the Agency's name in whole or in part. The Agency's position is that of a guarantor, relating to losses.

(c) After acquiring the collateral the lender must protect the collateral from deterioration (weather, vandalism, etc.). Hazard insurance in an amount necessary to cover the fair market value of the collateral must be maintained.

(d) The lender will prepare and submit to the Agency a plan on the best method of sale, keeping in mind any prospective purchasers. Concurrence or non-concurrence of the plan will be made in writing to the lender. If an existing liquidation plan addressed the disposition of acquired property, no further review is required unless modification of the plan is needed.

(e) Methods of liquidation.

- (1) Direct sale by lender.
- (2) Use of commercial broker.
- (3) Public auction.

(f) *Abandonment of the collateral.* (1)

The primary purpose of collateral is to afford a net return on the loan balance. However, there will be times when converting the collateral to cash would result in a loss.

(2) Anytime there is a case when the conversion of collateral to cash can reasonably be expected to result in a negative net recovery amount, abandonment of the collateral should be considered.

§§ 1980.891–1980.893 [Reserved]

§ 1980.894 Determination and payment of loss.

In all liquidation cases, final settlement will be made with the lender after the collateral is liquidated. The Agency will have the right to recover losses paid under the guarantee from any party liable.

(a) If the lender takes title to collateral any loss will be based on the collateral value at the time the lender obtains title.

(b) The Report of Loss form will be used for calculations of all estimated and final loss determinations. Estimated loss payments may only be approved after the lender has submitted a liquidation plan approved by the Agency.

(c) When the lender is conducting the liquidation and owns any of the guaranteed portion of the loan, it may request an estimated loss payment by submitting an estimate of loss that will occur in connection with liquidation of the loan. An estimated loss payment may be approved after the Agency has approved the liquidation plan.

(1) The estimate will be prepared and submitted by the lender on the Report of Loss form using the basic formula as provided on the report except that appraisal value will be used in lieu of amount received from sale of collateral.

(2) The estimated loss payment shall be applied as of the date of such payment. The total amount of the loss payment remitted by the Agency will be applied by the lender on the guaranteed portion of the loan debt. Such application does not release the borrower from liability. At the time of final loss settlement, the lender may notify the borrower that the loss payment has been so applied.

(3) After liquidation has been completed, a final Report of Loss will be submitted by the lender to the Agency.

(d) In all cases, a final Report of Loss must be submitted to the Agency. Before Agency approval of any final loss report,

the lender must account for all funds obtained, disposition of the collateral, all costs incurred, and any other information necessary for the successful completion of liquidation. Upon receipt of the final accounting and Report of Loss, the Agency may audit, and will determine the final loss. The lender will make its records available to, and otherwise assist, the Agency in making any audit it requires of the Report of Loss. The documentation accompanying the Report of Loss must support the loss claimed.

(1) The lender must document and show that all of the collateral has been accounted for and properly liquidated and that liquidation proceeds have been properly accounted for and applied correctly on the loan. The Agency must be satisfied that the lender has accomplished this in the manner set out in this subpart and that the lender has maximized the collections in conducting the liquidation.

(2) The lender must show a breakdown on any protective advance amount as to the payee, purpose of the expenditure, date paid, evidence that the amount expended was proper, and that the amount was actually paid.

(3) The lender must show a breakdown of liquidation expenses as to the payee, purpose of the expenditure, date paid, evidence that the amount expended was proper, and that the amount was actually paid.

(4) Accrued interest should be supported by attachments showing how the amount was accrued by the lender. A copy of the promissory note and ledger will be attached. If the interest rate was a variable rate, the lender must include documentation of changes in the selected base rate and when the changes in the loan rate became effective.

(e) Any net rental or other income that has been received by the lender from the collateral will be applied on the guaranteed loan debt.

(f) Certain reasonable liquidation costs will be allowed during the liquidation process. The liquidation costs will be submitted as a part of the liquidation plan. Such costs will be deducted from gross proceeds received from the disposition of collateral unless the costs have been previously determined by the lender (with Agency concurrence) to be protective advances. If changed circumstances after submission of the liquidation plan require a revision of liquidation costs, the lender will procure the Agency's written concurrence prior to proceeding with the proposed changes. No in-house expenses of the lender will be allowed. In-house expenses include, but are not

limited to, employees' salaries, staff lawyers, travel, and overhead.

(g) In those instances where the lender made authorized protective advances, the lender may claim recovery for the guaranteed portion of any loss of monies advanced as well as interest resulting from such protective advances. These claims shall be included in the final Report of Loss.

(h) After the final Report of Loss has been tentatively approved:

(1) If the actual loss is greater than any estimated loss payment, such loss will be paid by the Agency.

(2) If the Agency conducted the liquidation, it will provide an accounting to the lender and will pay the lender in accordance with the Loan Note Guarantee.

(i) The amount payable by the Agency to the lender cannot exceed the limits contained in the Loan Note Guarantee. If the Agency conducts the liquidation, loss occasioned by accruing interest will be covered by the guarantee only to the date the Agency accepts this responsibility. When the liquidation is conducted by the lender, loss occasioned by accruing interest will be covered to the extent of the guarantee to the date of final settlement provided the lender proceeds expeditiously with the liquidation plan approved by the Agency.

§ 1980.895 Future recovery.

After a loan has been liquidated and a final loss has been paid by the Agency, any future funds which may be recovered by the lender will be pro-rated between the Agency and the lender in accordance with the guaranteed percentage even if the Loan Note Guarantee has been terminated.

§ 1980.896 Termination of Loan Note Guarantee.

The Loan Note Guarantee under this subpart will terminate automatically:

(a) Upon full payment of the guaranteed loan; or

(b) Upon full payment of any loss obligation or negotiated loss settlement except for future recovery provisions; or

(c) Upon written request from the lender to the Agency, provided that the lender holds all of the guaranteed portion and the original Loan Note Guarantee is returned to the Agency.

§§ 1980.897–1980.900 [Reserved]

Dated: September 24, 1997.

Jill Long Thompson,

Under Secretary, Rural Development.

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