significantly from the species lost, as the county committee determines, the costs may not be reimbursed.

(d) Owners may elect not to replant the entire eligible stand. If so, the county committee shall calculate payment based on the number of qualifying trees, bushes or vines actually replanted.

(e) The cumulative total quantity of acres planted to trees, bushes or vines for which a person may receive assistance shall not exceed 500 acres.

(f) The cumulative amount of TAP payments which any person, as defined in accordance with part 1400 of this title, may receive shall not exceed $75,000 per program year.

(g) If the total of all eligible TAP claims received exceeds the available TAP funds, payments shall be reduced by a uniform national percentage after the imposition of applicable payment limitation provisions.

§ 783.6 Obligations of an owner.

(a) Eligible owners must execute all required documents, comply with all applicable noxious weed laws, and complete the TAP funded practice within 12 months of application approval.

(b) If a person was erroneously determined to be eligible or becomes ineligible for all or part of a TAP payment, the person and/or successor shall refund any payment paid under this part together with interest from the date of disbursement at a rate in accordance with part 1403 of this title.

(c) Participants must allow representatives of FSA to visit the site for the purposes of certifying compliance with TAP requirements.

§ 783.7 Multiple benefits.

Persons eligible to receive payments under this part and another program for the same loss, may receive benefits from only one program and must choose which program benefits they want. If other benefits become available after payment of TAP benefits the owner may refund the TAP payment and receive the other program benefit. If the owner purchased additional coverage insurance, as defined in 7 CFR 400.651, or is eligible for assistance or emergency loans under another Federal program for the same loss, the owner will be eligible for such assistance. In no case shall the total amount received from all sources exceed the amount of the owner's actual loss. Should the total amount of benefits exceed the owner's actual loss, the TAP benefits will be reduced accordingly.

§ 783.8 Miscellaneous.

(a) Any payment or portion thereof due any person under this part shall be allowed without regard to questions of title under State law, and without regard to any claim or lien in favor of any person except agencies of the U.S. Government.

(b) Persons shall be ineligible to receive assistance under this program if they have:

(1) Adopted any scheme or device intended to defeat the purpose of this program;

(2) Made any fraudulent representation; or

(3) Misrepresented any fact affecting a program determination.

(c) TAP benefits paid to a person as a result of misrepresentation shall be refunded to FSA with interest and costs of collection. The party engaged in acts prohibited by this paragraph and the party receiving payment and their successors shall be jointly and severally liable for any amount due. The remedies provided to FSA in this part shall be in addition to other civil, criminal, or administrative remedies which may apply.

(d) Program documents executed by persons legally authorized to represent estates or trusts will be accepted only if such person furnishes evidence of the authority to execute such documents. A minor who is an owner that has met all other eligibility criteria shall be eligible for TAP assistance if:

(1) The minor establishes that the right of majority has been conferred on the minor by court proceedings or by statute; or

(2) A guardian has been appointed to manage the minor's property and the applicable program documents are executed by the guardian; or

(3) A bond is furnished under which the surety guarantees any loss incurred for which the minor would be liable had the minor been an adult.

(d) The regulations regarding reconsiderations and appeals at part 11 of this title and part 780 of this chapter apply to this part.

(e) In lieu of payments in cash, qualifying losses may be compensated by seedlings sufficient to reestablish a stand.

(f) The Deputy Administrator may set such additional conditions and limitations on eligibility as may be needed to reflect limited funding or accomplish program objectives as deemed appropriate by the Deputy Administrator, consistent with governing legislation.

Signed in Washington DC on August 5, 2003.

James R. Little,

Administrator, Farm Service Agency.

[FR Doc. 03–20345 Filed 8–8–03; 8:45 am]

BILLING CODE 3410–05–P

FARM CREDIT ADMINISTRATION

12 CFR Parts 614 and 615

RIN 3052–AB96

Loan Policies and Operations; Funding and Fiscal Affairs, Loan Policies and Operations, and Funding Operations; OFI Lending

AGENCY: Farm Credit Administration.

ACTION: Proposed rule.

SUMMARY: The Farm Credit Administration (FCA, agency, us, or we) proposes to amend its regulations governing other financing institutions (OFIs) and investments in Farmers' notes so it would be easier for Farm Credit System (FCS, Farm Credit, or System) institutions and non-System lenders to work together in providing affordable credit to agriculture and rural America. In addition, the proposed rule would remove provisions in the existing OFI and Farmers' notes regulations that: Impede the flow of credit; are not required by law; or do not enhance safe and sound operations. The FCA also proposes related amendments to its capital regulations.

DATES: You may send us comments by October 10, 2003.

ADDRESSES: Send us your comments by electronic mail to *reg-comm@fca.gov,* through the Pending Regulations section of our Web site at *www.fca.gov,* or through the government-wide Web site, *www.regulations.gov.* You may also submit your comments in writing to S. Robert Coleman, Director, Regulation and Policy Division, Office of Policy and Analysis, Farm Credit Administration, 1501 Farm Credit Drive, McLean, VA 22102–5090, or by facsimile transmission to (703) 734–5785. You may review copies of all comments we receive in the Office of Policy and Analysis, Farm Credit Administration.

FOR FURTHER INFORMATION CONTACT:

Dennis Carpenter, Senior Policy Analyst, Office of Policy and Analysis, Farm Credit Administration, 1501 Farm Credit Drive, McLean, Virginia 22102–5090, (703) 883–4498, TTY (703) 883–4434,

or

Richard A. Katz, Senior Attorney, Office of General Counsel, Farm Credit Administration, 1501 Farm Credit Drive, McLean, Virginia 22102–5090, (703) 883–4020, TTY (703) 883–4020.

SUPPLEMENTARY INFORMATION:

I. Background

This proposed rule is intended to make affordable credit more available to agriculture and rural America by increasing cooperation between System and non-System lenders. This rulemaking began on April 20, 2000, with an advance notice of proposed rulemaking (ANPRM) that asked the public questions about ways to improve the funding and discount relationship between Farm Credit banks and OFIs. *See* 65 FR 21151. FCA staff subsequently conducted telephone and field interviews with interested parties. On August 3, 2001, we held a public meeting in Des Moines, Iowa, where interested parties offered suggestions on how we could facilitate greater cooperation between System and non-System lenders in providing credit to agriculture and rural America. The public meeting addressed both the OFI program and other arrangements where the FCS and non-System lenders could help each other in extending credit to farmers, ranchers, and other eligible borrowers in rural America.

Many of the comments and suggestions that we received from the ANPRM, interviews, and at the public meeting are incorporated in this proposed rule, which would revise both our OFI and Farmers' notes regulations. This preamble also explains other actions that we are taking to facilitate greater cooperation between System and non-System lenders that will ultimately benefit agriculture and other eligible rural residents. OFIs and Farmers' notes are two separate and distinct programs that arise under different provisions of the Farm Credit Act of 1971, as amended (Act). In the first program, Farm Credit Banks (FCBs) and the agricultural credit bank (ACB) (collectively Farm Credit banks) fund and discount short- and intermediate-term loans that OFIs make to eligible farmers, ranchers, aquatic producers and harvesters, farm-related businesses, and non-farm rural homeowners. The Farmers' notes program currently authorizes certain FCS associations to invest in notes, contracts, and other obligations that eligible farmers and ranchers enter into with suppliers. Changes to the OFI and Farmers' notes regulations require conforming amendments to our capital regulations.

This rule complements other efforts by the FCA to increase the flow of credit to agriculture and rural America by promoting greater cooperation between FCS and non-System lenders. System banks and associations have many different powers that enable them to act as a funding source for a wide array of credit products that non-System lenders offer their customers. For example, Farm Credit banks fund and discount short- and intermediate-term loans that OFIs make to eligible borrowers. Separately, Farm Credit banks and associations can provide non-System lenders with long-term funding, in addition to short- and intermediate-term funding, by buying participations up to 100 percent of the principal amount of the loan. Syndications are another method that FCS institutions use to help non-System institutions extend credit, particularly to larger borrowers. As part of its effort to promote partnering arrangements between FCS and non-System lenders, the FCA is currently exploring methods for the System's use of syndications originated by non-System lenders. Today, the FCA is proposing substantial revisions to its Farmers' notes regulations, which if adopted, will expand this program to more non-System lenders, and allow all FCS associations to invest, for the first time, in both long- and short-term loans between these other lenders and eligible farmers and ranchers.

These different authorities give the FCS many powers to meet the varied funding needs of a wide variety of non-System lenders that finance agriculture. These authorities allow non-System lenders to access any one or a combination of FCS funding programs, depending on individual needs. The System fulfills its mission to finance agriculture and other specified credit needs in rural America by serving as a steady source of funding and liquidity for other lenders. This should result in lower credit costs and more credit options for farmers, ranchers, aquatic producers and harvesters, and other eligible rural residents.

II. Other Financing Institutions

A. History of OFIs

Farm Credit banks have discounted production agricultural loans for OFIs since 1923.[1] Since 1930, Farm Credit banks also have made secured loans and advances directly to OFIs.[2] Thus, OFIs could borrow from, and discount production agricultural loans with, Farm Credit banks before Congress created production credit associations (PCAs) as an alternative source of financing the operating needs of farmers and ranchers.[3] Since 1980, the Act has authorized Farm Credit banks to fund and discount for OFIs any loan that PCAs could make. As a result, OFI loans to eligible processing and marketing, farm-related businesses, and non-farm rural homeowners may also be funded or discounted by a Farm Credit bank.

The legislative history of the various Farm Credit Acts reveals that the primary purpose of the OFI program is to address the scarcity of operating credit for farmers and ranchers.[4] Over the years, Congress has responded to the changing credit needs of farmers, ranchers, and other rural residents by expanding the lending authority of the FCS, and giving Farm Credit banks more authority to fund OFIs.[5] These statutory changes have ensured that the FCS could continue as a source of affordable and reliable credit to agriculture and rural America on both a wholesale and retail level.

OFIs, historically, have established funding or discount relationships with Farm Credit banks when the cost of FCS funds is significantly lower than other funding sources. The OFI program reached its peak in the 1970s and early 1980, when market interest rates were at historically high levels. In 1982, approximately 300 OFIs borrowed approximately $914 million from various Farm Credit banks. By December 31, 2002, Farm Credit banks lent only $291 million to 31 OFIs.

Much of the decline in the OFI program can be attributed to the farm crisis of the mid and late 1980s. Declining land values and commodity prices meant that many farmers were unable to repay their loans, which caused the FCS to experience significant financial stress between 1984 and 1989. During this time, many OFIs terminated their funding and discount relationships with Farm Credit banks for a variety of reasons. One reason for the decline of the OFI program was that Farm Credit banks were in a weakened financial position and, therefore, could no longer offer OFIs competitive rates. Additionally, the merger or consolidation among many commercial bank OFIs improved their liquidity and

[1] *See* The Agricultural Credits Act of 1923, Pub. L. 503, 42 Stat. 1454 (March 4, 1923).

[2] *See* Federal Farm Loan Act Amendments, Pub. L. 439, 46 Stat. 816 (June 26, 1930).

[3] *See* Farm Credit Act of 1933, Pub. L. 75–73D, title II, 48 Stat. 257, 259 (June 16, 1933).

[4] *See* H. R. Rep. No. 1712, 67th Cong., 1st. Sess. (February 25, 1923), p. 17; H.R. Rep. No. 96–1287, 96th Cong., 2nd Sess. (September 4, 1980), p.21.

[5] From 1923 until 1988, OFIs funded and discounted short- and intermediate-term loans with the former Federal Intermediate Credit Banks. Section 410 of the Agricultural Credit Act of 1987 (1987 Act) created the FCBs through the mandatory merger of the Federal Land Bank and the Federal Intermediate Credit Bank in each Farm Credit district. See Pub. L. 100–233, section 410, 101 Stat. 1568, 1637 (January 6, 1988). Section 7.0 of the Act authorizes FCBs to merge with banks for cooperatives to form an ACB. According to section 7.2 of the Act, an ACB has all of the powers and obligations of its constituent banks.

resulted in lower-cost funding for their agricultural loans.

The FCS has regained its financial strength over the past decade. As a result, FCBs and the ACB are once again in a strong financial position to fulfill their statutory mission of increasing the availability of affordable and dependable credit for agriculture and other rural credit needs by assisting both FCS associations and non-System lenders, including OFIs. The FCA has consistently promoted various efforts to improve cooperation among System and non-System lenders so agriculture and rural America will always have adequate credit. In this context, we propose regulatory amendments that will provide OFIs with greater access to the funding and discount services of Farm Credit banks within the confines of the Act.

B. The Act and OFIs

Currently, section 1.7(b)(1) of the Act authorizes Farm Credit banks to offer funding, discounting, and other similar financial services to OFIs so they can make short- and intermediate-term loans to eligible agricultural and aquatic producers, farm-related business, and rural homeowners. Section 1.7(b)(1)(B) of the Act allows national banks, State banks, trust companies, agricultural credit corporations, incorporated livestock loan companies, certain agricultural credit cooperatives, and corporations that lend to aquatic producers and harvesters to become OFIs. Section 1.7(b)(4) requires the FCA to enact regulations that assure that loans, discounts, and other similar financial assistance from Farm Credit banks are available on a reasonable basis to any OFI that:

1. Is significantly involved in lending for agricultural or aquatic purposes;

2. Demonstrates a continuing need for supplementary sources of funds to meet the credit requirements of its agricultural or aquatic borrowers;

3. Has limited access to national or regional capital markets; and

4. Does not use its relationship with its Farm Credit bank to extend credit to persons and for purposes that are not authorized by title II of the Act.

C. FCA's Rulemaking Efforts

This proposed rule is designed to help restore the vitality of the OFI program by making it easier for OFIs to obtain funding from Farm Credit banks. Between 1996 and 1998, the FCA conducted a rulemaking that overhauled the OFI regulations by removing numerous regulatory requirements that were not required by law, or did not promote safety and soundness.[6] The express purpose of our earlier rulemaking was to ''substantially expand access to System funding so OFIs can provide more short- and intermediate-term credit to parties who are eligible to borrow under sections 2.4(a) and (b) of the Act.'' [7]

After the earlier rulemaking concluded, Farm Credit banks and OFIs brought to our attention other problems that impeded OFI access to System funding. In response to these concerns, the FCA started this rulemaking in April 2000. The ANPRM sought input on the following issues:

1. The appropriate risk weighting of Farm Credit bank loans to OFIs;

2. Removing regulatory restrictions on funding OFIs located in the chartered territory of another Farm Credit bank;

3. Public disclosure of the identities of OFIs; and

4. Other ways to improve the ability of Farm Credit banks to fund OFIs.

The FCA received 37 comment letters in response to the ANPRM. Of this total, comments were received from six Farm Credit banks and associations, 18 commercial banks, and four non-bank entities. Nine (9) banking trade associations also submitted comments on behalf of their members. Most commenters favored: (1) Lowering the risk weighting on most System bank loans to OFIs; (2) removing territorial restrictions on FCS bank loans to OFIs; and (3) disclosing the identity of OFIs. The commenters also offered us helpful suggestions for improving the funding and discounting relationship between OFIs and their System funding banks. We will discuss these comments in greater detail below when we explain how the proposed rule addresses specific issues.

The responses to the ANPRM indicated that we needed more public input, not only on OFIs, but also on other approaches that would enable the FCS to provide funding to non-System lenders that finance agriculture and other specified needs in rural America. The FCA gained additional information and advice about these issues in the summer of 2001, when staff conducted telephone and field interviews with all Farm Credit banks, an FCS association, and three OFIs in Wisconsin, and Oklahoma. These field interviews were supplemented by telephone interviews with other lenders. In all interviews, the staff asked the questions that we originally raised in the ANPRM and sought additional information about the hurdles that existing and potential OFIs faced in their relationships with FCS funding banks.

The FCA Board also decided to solicit additional guidance from interested parties by convening a public meeting in Des Moines, Iowa, on August 3, 2001. Fifteen (15) representatives from Farm Credit banks and associations, trade associations, commercial banks, OFIs, investment bankers, and farm groups presented testimony at or as follow-up to the public meeting. In addition to discussing the OFI program, commenters at the public meeting also asked the FCA to explore other arrangements where non-System lenders that do not qualify as OFIs could obtain credit services from both Farm Credit banks and associations. The comments that we received from the ANPRM, field and telephone interviews, and the public meeting, helped us develop the rule that we propose today.

D. Regulatory Issues

As we explained earlier, the purpose of this rule is to make it easier for OFIs to obtain funding from Farm Credit banks for their short- and intermediate-term loans to agricultural and aquatic producers, farm-related business, and rural homeowners. Improving OFI access to the funding and discount services of Farm Credit banks could make affordable credit more available to farmers, ranchers, and other eligible borrowers. Farm Credit banks fulfill their missions as a Government-sponsored enterprise by enhancing the liquidity of OFIs, thereby lowering the cost of funding agriculture.

Commenters identified several regulatory issues pertaining to the OFI program. The FCA proposes to address some of the issues by amending the OFI regulations. In other cases, the FCA will explain how the commenters' concerns are addressed by the existing regulations, which means that a regulatory amendment is unnecessary.

1. Assured Access

Section 1.7(b)(4)(B)(i) of the Act requires FCA regulations to assure that the funding and discount services of Farm Credit banks are available on a reasonable basis to any OFI that is significantly involved in lending for agricultural and aquatic purposes. Currently, § 614.4540(b)(1) [8] states that Farm Credit banks must ''fund, discount, or provide other similar financial assistance to any creditworthy OFI that * * * maintains at least 15 percent of its loan volume at a seasonal peak in loans and leases to farmers,

[6] *See* 61 FR 24907 (May 17, 1996); 62 FR 38223 (July 17, 1997); 63 FR 36541 (July 7, 1998).

[7] *See* 63 FR 36541 (July 7, 1998).

[8] *See* 46 FR 51886 (October 22, 1981).

ranchers, aquatic producers and harvesters.'' Section 1.7(b) of the Act and § 614.4540 of the regulations allow OFIs that do not meet this 15-percent threshold to fund and discount their short- and intermediate-term loans at Farm Credit banks, but they are not assured access if credit becomes scarce.

Several commercial bank and System commenters believe that this 15-percent threshold is too onerous, and they asked the FCA to reduce or eliminate it. These commenters erroneously claim that the requirement that agricultural loans always comprise 15 percent of an OFI's loan portfolio discourages potential OFIs and deters existing OFIs from depending on Farm Credit banks as their primary source of agricultural funding. The FCA seeks to dispel the misconception that § 614.4540(b)(1) requires OFIs to always maintain at least 15 percent of their loan portfolio in farm loans in order to maintain assured access. Instead, this regulation requires such OFIs to maintain at least 15 percent of their volume at a seasonal peak in farm loans and leases.

At this time, the FCA does not propose to change the 15-percent threshold as the factor that determines whether an OFI is significantly involved in agricultural lending, and thus assured access to funding from a System bank. In reaching this decision, the FCA examined how two of the other Federal bank regulatory agencies determine if a bank engages in substantial agricultural lending. The FCA's research revealed that the Federal Deposit Insurance Corporation (FDIC) classifies banks as agricultural banks if at least 25 percent of their loans are to farmers or ranchers. The Board of Governors of the Federal Reserve System (Federal Reserve Board) classifies a bank as agricultural if its ratio of farm loans to total loans exceeds the unweighted average of the average of all banks on a given date. Based on this formula, the Federal Reserve Board most recently classified banks as agricultural banks if farm loans comprise at least 14.97 percent of their loan portfolios. Thus, the standard that the FCA uses to determine if a non-System lender is substantially involved in agricultural lending is significantly more permissive than the FDIC's benchmark and comparable to the measure used by the Federal Reserve Board.

The current regulatory threshold also seems to strike a fair balance between the needs of small rural lenders and larger institutions. Agricultural loans usually comprise a larger percentage of the loan assets of small rural lenders. However, larger institutions may extend more overall credit, in dollar terms, to farmers, although agricultural loans are a much smaller percentage of their loan portfolios. Additionally, § 614.4540(b)(1) continues to forbid Farm Credit banks from including the loan volume of an OFI's parent, affiliates, or subsidiaries in determining compliance with this 15-percent threshold. In practice, most lenders establish a separate OFI affiliate to access System bank funding and, therefore, the 15-percent threshold should not be onerous to OFIs. As noted earlier, failure to meet the 15-percent threshold does not prohibit FCS bank funding to creditworthy OFIs unless credit is scarce.

Because the FCA wants to make the OFI program more attractive to eligible agricultural lenders, we invite your comments on alternatives that reasonably demonstrate that an OFI is significantly involved in agricultural lending, as section 1.7(b)(4)(B)(i) of the Act requires.

2. Place of Discount

Non-System lenders and many Farm Credit banks have long considered place of discount restrictions as a major reason why the OFI program has not been widely used by commercial banks and other agricultural lenders. Historically, OFIs borrowed from the Farm Credit bank that serves the territory where such OFIs maintain their headquarters or makes the most of their loans. As a result, OFIs have maintained a funding or discount relationship with a System bank that is owned and controlled by their competitors.

In 1998, the FCA sought to remedy this problem by adopting § 614.4550, which established new place-of-discount rules for OFIs. Under this regulation, every OFI must apply first to the Farm Credit bank that serves the territory where the OFI operates. If the bank denies funding, or otherwise fails to approve a completed application within 60 days, the OFI may apply to any other FCB or the ACB. Additionally, the regulation allows a Farm Credit bank to consent to another System bank funding or discounting loans for an OFI.

We received 28 comments about place of discount in response to the ANRPM, and another five comments about this issue during the interviews and public meeting. Specifically, we received comments on this issue from 12 commercial banks and seven commercial bank trade associations. Additionally, six Farm Credit banks and one FCS association commented on this issue. All commercial bank and bank trade association commenters, five Farm Credit banks, and the one FCS association favored repealing regulatory restrictions on place of discount so OFIs could choose their System funding bank. One Farm Credit bank opposed repealing § 614.4550, so FCS associations would not be placed at a competitive disadvantage.

In response to these comments, the FCA proposes allowing OFIs to apply for funding and discount services from any FCS bank. However, the proposed rule will require a Farm Credit bank to notify another System bank in writing within five (5) business days of receiving an application from an OFI that maintains its headquarters or has more than 50 percent of its loan volume in the territory of the other Farm Credit bank. This notice will give the bank in whose territory the OFI is located ample opportunity to contact the applicants and offer them funding and discount services. Under the proposed rule, no OFI may borrow from two or more Farm Credit banks at the same time. Farm Credit banks extend wholesale credit to OFIs, and they hold the OFIs' retail loans and other collateral as security. Allowing two or more Farm Credit banks to simultaneously fund the same OFI could pose safety and soundness risks to the funding banks if the OFI experienced financial stress and disputes arose over collateral pledged.

Our new regulatory approach would resolve the difficulties that often arise when OFIs must borrow from a Farm Credit bank that is owned and controlled by their competitors. When Farm Credit banks compete for OFI credit, the OFI can lower its funding costs, which it can then pass on to its agricultural borrowers. Additionally, this approach frees Farm Credit banks from potential association pressure not to lend to their competitors. If a Farm Credit bank is concerned about another System bank funding OFIs in its territory, written notice gives it ample opportunity to seek the relationship with the OFI.

3. Borrower Rights

Section 4.14A(a)(6)(B) of the Act expressly requires OFIs to adhere to borrower rights, ''but only with respect to loans discounted or pledged under section 1.7(b)(1).'' The borrower rights that apply to loans that OFIs discount or pledge with a Farm Credit bank are: (1) Effective Interest Rate (EIR) disclosures; (2) notice of adverse credit decision; (3) the right to appeal adverse credit decisions to the lender's credit review committee; (4) receiving copies of certain documents; and (5) the right to restructure distressed loans. Existing § 614.4560(d) implements section 4.14A(a)(6)(B) of the Act by requiring OFIs to comply with borrower rights on

those loans that Farm Credit banks fund or discount.

During this rulemaking, the FCA received numerous comments from existing and potential OFIs and a Farm Credit bank that borrower rights are a significant disincentive to the success of this program. Borrower rights are a statutory requirement for OFIs; therefore, the FCA cannot repeal § 614.4560(d).

Recently, a Farm Credit bank and some of its affiliated OFIs asked the FCA to reconsider its interpretation of section 4.14A(a)(6)(B) of the Act. The FCB and its OFIs interpret section 4.14A(a)(6)(B) to mean that borrower rights apply to OFI loans only during the time they are actually pledged as collateral to the funding bank. Under this interpretation, OFI loans would be exempt from most borrower rights requirements because many of these rights apply before or after the time an OFI's loans are actually pledged to the FCB or ACB. Examples of borrower rights that usually apply before an OFI actually pledges loans to a Farm Credit bank are: (1) Most EIR disclosures; (2) written notice that the borrower's credit application has been denied; and (3) appeals of adverse credit decisions to the lender's credit review committee. An example of a right that applies when a loan is no longer pledged to a System bank is the right of borrowers under section 4.14A of the Act to restructure distressed loans. Borrowers usually seek to restructure a distressed loan after the Farm Credit bank instructs the OFI to remove it from collateral. Under the suggested interpretation, section 4.13A of the Act would be the only borrower rights provision of the Act that would always apply to OFI borrowers. This provision enables System and OFI borrowers to obtain copies of: (1) All loan documents they sign or deliver; (2) loan appraisals on their assets that the lender uses in making credit decisions; and (3) the lender's articles of incorporation and bylaws.

The FCB and its affiliated OFIs advocate an interpretation of section 4.14A(a)(6)(B) of the Act that emphasizes the timing of certain events over how an OFI loan is funded. However, our analysis leads us to conclude that Congress intended section 4.14A(a)(6)(B) of the Act to apply whenever an OFI uses a Farm Credit bank rather than another source (such as deposits or other lines of credit) to fund the borrower's loan. Originally, the provisions of the Act that govern EIR disclosures, written notice of credit denials, and appeal of adverse credit decisions only applied to Farm Credit banks and associations that operate under title I or II of the Act. The 1987 Act amended these statutory provisions so these rights and protections would also apply to OFI borrowers.[9] The 1987 Act also added section 4.14A to the Act so that farmers, ranchers, and aquatic producers and harvesters [10] who borrowed from either the FCS or an OFI would have the right to restructure distressed loans.[11] These statutory amendments clearly demonstrate that Congress intended to grant OFI borrowers whose loans were funded by a Farm Credit bank all of the rights and protections described above, regardless of when certain events occurred.

The FCB and its OFIs believe that Congress's use of the word ''pledged'' in section 4.14A(a)(6)(B) indicates that borrower rights apply only during the period of time when an OFI loan serves as collateral for the Farm Credit bank loan. However, they are reading the word ''pledged'' out of context with the rest of the statute. Section 4.14A(a)(6) refers to ''loans discounted or pledged under section 1.7(b)(1)'' of the Act. However, section 1.7(b)(1) of the Act describes the services that Farm Credit banks are authorized to provide certain FCS associations and OFIs, not the timing of when such associations and OFIs pledge collateral to the bank. Therefore, the term ''pledged'' in section 4.14A(a)(6)(B) covers those loans that a Farm Credit bank funds under its authority in section 1.7(b)(1), not the time when such loans are pledged.

For these reasons, OFIs must comply with borrower rights on all loans that they fund or discount through a Farm Credit bank. Borrower rights, however, do not apply to loans that an OFI funds through other sources. Thus, OFIs that always use the funding or discounting services of a Farm Credit bank to make all of its short- and intermediate-term agricultural and aquatic loans must comply with all borrower rights requirements.

Some flexibility may exist, however, for those OFIs that actually use several sources of funding, including Farm Credit banks, to make loans to farmers, ranchers, and aquatic producers and harvesters. In some cases, an OFI genuinely may not know how it will fund a particular borrower's loans until after closing. In such cases, an OFI may decide not to give the borrower an EIR disclosure, written notification about the denial of credit, or the right to appeal the credit denial to a credit review committee because the OFI plans to use deposits or another line of credit to fund the borrower's loan. If the OFI subsequently decides to draw on its credit line with its Farm Credit bank to fund this loan, borrower rights would apply to all future actions on this loan. For example, a borrower who did not receive an EIR disclosure at closing would be entitled to an EIR disclosure at a later date if the OFI funds or discounts the loan with the Farm Credit bank and then adjusts the borrower's interest rate. The OFI must also give the borrower written notice and the right to appeal adverse credit actions to a credit review committee once it funds or discounts a seasoned loan with a Farm Credit bank. OFIs must also honor the rights of borrowers to restructure distressed loans even if the Farm Credit bank removed such loans from collateral after their credit quality declined. Once a Farm Credit bank funds or discounts a loan, borrower rights attach to it for the duration of the loan. This is the same approach that the FCA follows for loans that FCS institutions sell to non-System lenders.[12]

The FCA proposes a technical correction to § 614.4560(d). Currently, this provision erroneously states that section 4.36 of the Act applies to all loans that an OFI funds or discounts through an FCB or ACB. In fact, the plain language in section 4.36 of the Act states that the right of first refusal applies only to the borrowers of FCS institutions that operate under title I or II of the Act. As a result, OFIs are subject to some, but not all, of the regulations in subpart N of part 614. Accordingly, the FCA proposes to omit the reference to section 4.36 from § 614.4560(d) and to further amend this regulatory provision so it refers to §§ 614.4516, 614.4517, 614.4518, and 614.4519, which are the only regulations in subpart N of part 614 that apply to OFIs.[13]

4. Equitable Treatment

In 1998, the FCA adopted § 614.4590, which requires Farm Credit banks to treat OFIs and FCS associations

[9] Pub. L. 100–233, Sections 103, 104, 105, and 106, 101 Stat. 1568, 1579–81 (January 6, 1988).

[10] Borrower rights do not apply to loans that are subject to the Truth-in-Lending Act, 15 U.S.C. 1601 *et seq*. The Truth-in-Lending Act applies to consumer credit. Non-farm rural home loans and consumer loans to farmers are subject to the Truth-in-Lending Act, not the borrower rights provisions of the Act. *See* Act, §§ 4.13 and 4.14A(a)(5). Also, borrower rights do not apply to loans that the ACB makes under title III of the Act. *See* Act §§ 4.14A(a)(6)(A).

[11] Pub. L. 100–233, Sections 102, 101 Stat 1568, 1574 (January 6, 1988).

[12] 12 CFR 614.4336.

[13] The FCA recently proposed to move all borrower rights regulations to part 617. *See* 68 FR 5587, February 4, 2003. If the FCA adopts this change the final OFI rule will revise the cross-references to borrower rights regulations in § 614.4560(d).

equitably. More specifically, § 614.4590(a) states that Farm Credit banks must apply comparable and objective loan underwriting standards and pricing requirements to both OFIs and FCS associations. Under § 614.4590(b), the total charges that a System bank assesses its OFIs must be comparable to the total charges it imposes on its affiliated associations. This regulation also states that any variation between the overall funding costs that OFIs and FCS associations are charged by the same funding bank must result from differences in credit risk and administrative costs to the FCB or ACB.

Many responses to the ANPRM and several speakers at the public meeting expressed the view that Farm Credit banks do not treat OFIs equitably with FCS associations, which own and control each System bank. According to these commenters, the perception of unfair treatment discourages potential OFIs from establishing a funding and discount relationship with an FCB or ACB. Many commenters informed us that existing OFIs often feel that Farm Credit banks favor the associations.

Many commercial bank commenters suggested that our regulations should mandate equal, rather than equitable, treatment of OFIs and FCS associations. These commenters believe that the disparity of treatment is especially evident in the price of funding that Farm Credit banks charge their OFIs and FCS associations. Several commenters want us to require Farm Credit banks to disclose to OFIs exactly how they price their loans to both OFIs and FCS associations. Several commercial bank trade associations asked the FCA to require Farm Credit banks to identify the specific components that make up their cost of funds to OFIs and the amount of these components in terms of basis points. Commercial banks and their trade associations also requested that the FCA enact regulations that expressly prohibit Farm Credit banks from charging OFIs fees that are not charged to FCS associations. Some commenters asked the FCA to require Farm Credit banks to pay dividends or patronage to OFIs.

The FCA sought to address many of these concerns in the rulemaking that ended in 1998 by adopting § 614.4590, which requires Farm Credit banks to treat OFIs and FCS associations equitably. The FCA notes that the OFI program has not significantly expanded since 1998, but many of the same complaints about disparate treatment by Farm Credit banks of OFIs and FCS associations have surfaced once again. The FCA has decided to address these concerns by proposing amendments to § 614.4590 that would strengthen regulatory requirements concerning equitable treatment.

Fundamental differences between OFIs and direct lender associations mean that regulations can only require Farm Credit banks to treat OFIs and FCS direct lender associations equitably, but not equally. The following are some of the fundamental differences between these two types of financial institutions that preclude identical treatment:

- OFIs have access to several funding sources whereas direct lender associations do not.
- FCS associations have invested significant amounts of capital in the funding bank, while most OFIs have not.
- A direct lender association pledges all of its loans to the Farm Credit bank, whereas OFIs do not.
- FCS associations are members of a cooperative credit system that shares gains and losses, whereas OFIs have limited exposure to such losses.
- Administrative costs for funding a direct lender association and an OFI differ because OFIs are not required to maintain a long-term commitment with a System funding bank.

These fundamental differences mean that OFIs expose Farm Credit banks to different credit risks and administrative costs than direct lender associations. As a result, some disparity in cost of funds that an FCB or ACB charges FCS associations and OFIs may be justified. For this reason, § 614.4590 requires that Farm Credit banks treat OFIs comparably, but not identically, to FCS associations in pricing loans. In fact, § 614.4590(b) states that the total charges that an FCB or ACB assesses an OFI through capitalization requirements, interest rates, and fees shall be comparable to the charges that the same Farm Credit bank imposes on its direct lender associations. This regulation also specifies that any variation in the overall funding costs that the same FCS funding bank charges OFIs and direct lender associations must be attributed to differences in credit risk and administrative costs to the bank.

The current regulation, however, does not require Farm Credit banks to explain and justify variations in the cost of funds to existing OFIs and OFI applicants. As a result, it is difficult to ascertain whether Farm Credit banks are pricing credit comparably for OFIs and FCS associations, as § 614.4590(b) requires. Commercial bank commenters have repeatedly asked the FCA to resolve this problem by requiring Farm Credit banks to disclose to OFIs how they price funding for both OFIs and associations. In 1998, we reasoned that disclosing such pricing information was unnecessary because the regulation did not compel Farm Credit banks to charge identical rates to OFIs and System associations.[14] The comments that we received during this rulemaking have persuaded us to propose a change on this issue. Disclosing pricing information will make the OFI program more transparent and address concerns by existing and potential OFIs that they are not treated fairly. The FCA hopes that this change will attract more agricultural lenders to this program and, therefore, make affordable credit more available for farmers, ranchers, and other eligible rural residents.

The FCA plans to achieve this objective by proposing to add two new provisions to § 614.4590. Proposed § 614.4590(c) would require each FCB or ACB to provide any OFI or OFI applicant, upon request, a copy of its policies, procedures, loan underwriting standards, and pricing guidelines for OFIs. This provision would also specify that the pricing guidelines must identify the specific components that make up the cost of funds for OFIs and the amount of these components in basis points. We believe this requirement is consistent with the information that is available to the associations, and is analogous to EIR disclosures that associations provide to retail borrowers.

Proposed § 614.4590(d) would require each FCB or ACB to explain in writing the reasons for any variation in the overall funding costs it charges OFIs and FCS associations if such information is requested by an OFI or OFI applicant. This provision would require a Farm Credit bank to compare the costs that it charges OFIs and FCS associations as groups or, if possible, variations between groups of OFIs and FCS associations that are of a similar size. However, proposed § 614.4590(d) would expressly prohibit System funding banks from disclosing financial or confidential information about individual FCS associations. Such information is confidential and proprietary information affecting the bank and its other customers and, therefore, it cannot be disclosed to OFIs.

The FCA also proposes a conforming amendment to § 614.4540(c) that would require each FCB or ACB to establish objective policies, procedures, pricing guidelines, and loan underwriting standards for determining the creditworthiness of each OFI applicant. Currently, § 614.4540(c) does not mention procedures or pricing guidelines.

[14] *See* 63 FR 35541 (July 7, 1998).

The proposed rule does not require Farm Credit banks to pay dividends or patronage to their OFIs. It is not appropriate in this instance for FCA regulations to impose business practices on FCS institutions in the absence of a compelling safety and soundness reason.

The proposed amendments to § 614.4590 should ensure that Farm Credit banks treat their OFIs and associations equitably. If information that a Farm Credit bank discloses about how it prices funding for OFIs and FCS associations continues to raise concerns about equitable treatment, an OFI or OFI applicant could pursue this matter with the FCA Ombudsman.

5. Ombudsman

Many commercial banks and their trade associations asked us to appoint an Ombudsman to assist OFI applicants and existing OFIs in establishing and maintaining good relations with System funding banks. On February 25, 2003, the FCA Board established the Office of the Ombudsman. According to the public announcement, ''The Office of the Ombudsman will be an effective, neutral and confidential resource and liaison for the public.'' Addressing the concerns of OFIs will be one of many duties of the Office of the Ombudsman. More information about how the Ombudsman will assist existing and potential OFIs will be forthcoming.

6. Disclosure of OFI Identities

In the ANPRM, we asked you whether we should amend our regulations so Farm Credit banks could disclose the identities of the OFIs that they fund. Our current regulations on releasing information prohibit FCS institutions from releasing information about their borrowers and stockholders to the public.[15] However, these prohibitions apply only to retail borrowers, such as farmers, ranchers, aquatic producers and harvesters, and rural homeowners. We have never interpreted these regulations as prohibiting the release of names of FCS associations that borrow from Farm Credit banks. In fact, information about the identities of FCS associations is widely available because it is contained in financial statements that Farm Credit banks release to the public.

The ANPRM explained why we believe that the reasons for protecting the identity of retail borrowers do not apply to financial institutions that fund and discount loans with a Farm Credit bank. Retail borrowers often are individual consumers, and keeping their identities confidential shields them from unwanted marketing solicitations or publicity involving their personal financial business. In contrast, OFIs could benefit from the disclosure of their identity because it could make prospective retail borrowers aware of other credit options.

We received 33 comments about the disclosure of OFI identities. Twenty-five (25) comments on this issue came from commercial banks or their trade associations; two comments were received from a non-bank entity and an OFI, while six comments came from Farm Credit banks and associations. Reaction was mixed, and neither commercial banks nor System institutions took unified positions on this issue. Most commenters believe that there is no valid justification to prohibit or otherwise restrict Farm Credit banks from disclosing the names of their OFIs. These commenters assert that disseminating this information promotes the OFI program and informs farmers, ranchers, and rural homeowners of their other credit options. These commenters also believe that the FCA regulations should treat FCS associations and OFIs the same when it comes to disclosing their identities to the public. However, other commenters opposed the disclosure of identifying information about OFIs to the public. These commenters believe that requiring such disclosures are an unwarranted intrusion by the FCA into private business transactions. Other commenters expressed the view that OFIs should advertise for customers if they want to expand market penetration, rather than relying on Farm Credit banks to inform potential borrowers of their other credit options. Some commenters suggested a compromise that would allow Farm Credit banks to disclose only the identities of OFIs that consent.

The FCA proposes a new rule, § 614.4595, which would allow Farm Credit banks to disclose to the public the names, addresses, telephone numbers, and Internet Web site addresses of those OFIs that consent in writing. The proposed regulation also requires each Farm Credit bank to adopt policies and procedures for: (1) Obtaining and maintaining the consent of its OFIs; and (2) disclosing this information to the public. Similarly, the financial statements of Farm Credit banks should disclose the identity of an OFI only with its consent. The FCA believes that this regulatory approach empowers each OFI to make the decision whether disclosure of its name, address, telephone number, and Web site address to the public is in its best interest.

7. Associations Acting as Farm Credit Bank Agents

Both System and non-System commenters suggested that FCS associations could serve as an effective conduit for funding OFIs. These commenters pointed out that associations often have established relationships with local OFIs and other commercial lenders. In many cases, FCS associations and existing and potential OFIs already have entered into joint financing arrangements for common borrowers.

The Act allows only Farm Credit banks that operate under title I of the Act, not FCS associations, to establish funding and discount relationships with OFIs. However, section 1.5(18) of the Act allows a Farm Credit bank to delegate to associations such functions as the bank deems appropriate. Similarly, section 2.2(19) of the Act allows a direct lender association to perform functions delegated to it by its funding bank. We believe that this authority allows FCS associations to act as point-of-contact or servicing agents for the Farm Credit bank in its lending relationship with its OFIs.

While associations could not directly fund OFIs, they could help make this program more successful by acting as intermediaries or servicing agents on loans from the Farm Credit banks to OFIs. Such arrangements could help promote new, and support existing, local relationships between the associations and potential and existing OFIs. Origination and servicing fees earned by the associations as agents for the banks can also serve to increase the associations' earnings potential. Such arrangements could also serve to reduce the servicing costs for smaller OFIs. A precedent for this approach is that FCS associations acted as servicing agents on loans that the former regional banks for cooperatives made to small, local, farmer cooperatives. In this capacity, FCS associations provided efficient and effective loan administration for the banks on loans they could have made themselves.

Agreements between the parties can establish these arrangements and, therefore, no new regulation is necessary. The FCA Board supports associations serving as agents for the Farm Credit banks in establishing and maintaining funding relationships between Farm Credit banks and existing or new OFIs.

[15] 12 CFR part 618, subpart G.

8. ''Similar Financial Assistance'' for OFIs

Section 1.7(b)(1) of the Act expressly authorizes Farm Credit banks to ''extend other similar financial assistance'' to both OFIs and FCS associations that extend short- and intermediate-term credit to their customers. Several commenters asked us to clarify exactly what constitutes ''similar financial assistance.'' Similar financial assistance includes lease financing, the issuance of guarantees, surety bonds, and the issuance of standby letters of credit. These all are services that Farm Credit banks routinely provide to their direct lender associations and; therefore, they are also acceptable forms of financial assistance that Farm Credit banks may offer their OFIs. Our explanation is consistent with guidance that we previously offered Farm Credit banks on this issue. At this time, no regulatory amendment is necessary to clarify the meaning of ''similar financial assistance'' in section 1.7(b)(1) of the Act.

9. Establishment of OFI Lending Limits

In 1998, former § 614.4565 was repealed, which imposed a lending limit on the amount of credit that any OFI could extend to a single credit risk with FCS funds. At the time, we acknowledged that certain OFIs would remain subject to lending limits that their primary regulator imposes under applicable Federal or state law. The preamble to the final rule stated that we expect each Farm Credit bank to prudently manage risk exposures to concentrations in OFI loan portfolios through underwriting standards and the general financing agreements (GFAs) executed with the OFIs.[16]

After the FCA repealed former § 614.4565, some Farm Credit banks considered imposing a lending limit on both FCS associations and OFIs that is lower than the lending limit that: (1) Section 614.4353 establishes for System direct lender associations; and (2) Federal or state laws place on depository institutions. During this rulemaking, two commenters asked us to enact a new regulation that would forbid Farm Credit banks from imposing a lending limit on OFIs that is lower than the limit established by applicable Federal or state law. The FCA declines this request because it is inconsistent with safety and soundness. Each Farm Credit bank may establish, by underwriting standards and GFAs, limits on its exposure to concentrations in the loan portfolios of both FCS associations and OFIs that are more stringent than lending limits imposed by statute or regulation, as long as it does not favor FCS associations over OFIs.

10. Eligible Collateral Pledged To Support an OFI's Discounting Arrangements With a Farm Credit Bank

Currently, § 614.4570 requires a secured lending relationship between each Farm Credit bank and every OFI. Under § 614.4570(b)(2), each FCB or ACB must perfect its security interest in any and all obligations and the proceeds thereunder that the OFI pledges as collateral, in accordance with applicable state law. Additionally, § 614.4570(c) allows each FCB and ACB to require its OFIs to pledge supplemental collateral to support the lending relationship.

These commenters asked the FCA to amend § 614.4570(b) so OFIs could pledge long-term agricultural mortgage loans as primary collateral to their FCS funding bank. According to the commenters, this approach would provide OFIs with an additional source of funding for agricultural mortgages.

The FCA denies this request because it is incompatible with section 1.7(b) of the Act, which requires OFIs to use funds from a Farm Credit bank only for the purpose of extending short- and intermediate-term credit to eligible borrowers for authorized purposes under section 2.4(a) and (b) of the Act. OFIs may, however, pledge agricultural mortgages to Farm Credit banks as supplemental, but not primary, collateral under § 614.4570(c).

Section 614.4570(c) requires each FCB and the ACB to develop policies and loan underwriting standards that establish uniform and objective requirements for determining the need and amount of supplemental collateral or other credit enhancements that each OFI must pledge to its System funding bank as a condition for obtaining credit. The amount, type, and quality of supplemental collateral or other credit enhancements specified by such policies and procedures must be proportional to the level of risk that the OFI poses to the System funding bank. Provisions in the GFA or the security agreement govern collateral pledged by each OFI to its System funding bank.

11. Improving the Relationship Between Farm Credit Banks and OFIs

Several commenters offered various suggestions for improving the relationship between Farm Credit banks and prospective and existing OFIs. These suggestions are confidence-building measures that will attract more OFIs to rely on Farm Credit banks as a source of funding and liquidity. These ideas could improve relations between existing OFIs and their funding banks and encourage prospective OFIs to establish funding and discount relationships with Farm Credit banks.

New regulations or policies promulgated by the FCA are not required to implement these ideas for improving the OFI program. Instead, these suggestions request Farm Credit banks to take the initiative and reach out to existing and prospective OFIs. The FCA uses this opportunity to convey the commenters' ideas to Farm Credit banks and provide them with guidance about measures that could make this program more appealing to OFIs. The FCA encourages Farm Credit banks to develop internal programs and initiatives that:

a. Establish outreach programs for contacting prospective OFIs and providing them with information about the bank's services;

b. Routinely publish updated information about its products and services for OFIs, and its underwriting standards, funding terms and conditions, and pricing guidelines for OFI loans;

c. Allow OFI representatives to observe meetings of the bank's board of directors;

d. Promote better communication through roundtable discussions, focus groups, and public discussions that bring OFIs, associations, and other interested parties together to discuss issues of mutual interest;

e. Work with OFIs to identify and remove administrative barriers that hinder OFI access;

f. Allow FCS associations to act as intermediaries and servicing agents on extensions of credit from the funding bank to OFIs, as discussed earlier; and

g. Identify best practices for OFIs.

The FCA is strongly committed to the success of the OFI program. OFIs are an important component of the mission of Farm Credit banks to finance agriculture. By adopting the internal programs and initiatives described above, Farm Credit banks can attract more OFIs to rely on the FCS as a source for funding and liquidity which, in turn, will provide eligible farmers, ranchers, aquatic producers and harvesters, farm-related businesses, and rural homeowners with more plentiful and affordable credit, as Congress intended. The FCA may provide additional guidance to Farm Credit banks about improving the OFI program through bookletters, informational memoranda, and the Office of the Ombudsman.

[16] *See* 63 FR 36541, 36545 (July 7, 1998).

E. Statutory Issues

Many FCS and non-System commenters identified other factors that they view as impediments to the success of the OFI program. Several commenters believe that OFIs should be able to fund or discount long-term mortgage loans on agricultural land and rural homes with Farm Credit banks. Other commenters observed that OFIs cannot hold voting stock in their System funding banks and; therefore, they are not represented on the banks' boards of directors. One commenter opposed the prohibition on Farm Credit banks extending additional credit to OFIs when the aggregate of their liabilities exceeds ten times their paid-in and unimpaired capital and surplus. Several commenters expressed the view that the OFI program should be modeled after the Federal Home Loan Bank System. These restrictions on the OFI program are imposed by the Act, not FCA regulations.

III. Investments in Farmers' Notes

Our public meeting notice asked interested parties for input on both OFIs and ''other types of partnering relationships between System and non-System lending institutions that would increase the availability of funds to agriculture and rural America.'' *See* 66 FR 35428 (July 5, 2001). At the public meeting, many commenters encouraged us to promote other arrangements, in addition to the OFI program, that make it easier for Farm Credit banks and associations to provide funding and liquidity to non-System financial institutions and merchants that extend credit to agriculture. Many commenters expressed their desire for more flexible and informal arrangements between FCS and non-System institutions.

The FCA is exploring a variety of different options that could improve cooperation between FCS and non-System lenders that, in turn, would increase the flow of credit to agriculture and rural America. For example, we are currently reviewing the regulatory treatment of loan syndications. Future rulemakings may suggest other regulatory approaches for enhancing partnering arrangements between FCS and non-System lenders.

Our efforts in this rulemaking focus on the Farmers' notes program. The FCA originally approved this program in 1966. The purpose of the Farmers' notes program is to provide liquidity to private dealers and cooperatives that sell farm machinery, supplies, equipment, home appliances, and other items of a capital nature to eligible farmers and ranchers. The Farmers' notes regulation, § 615.5172, allows PCAs and agricultural credit associations to purchase, as investments, notes, conditional sale contracts, and obligations that evidence the sale of the items, described above to farmers and ranchers.

The authority to purchase Farmers' notes derives from section 2.2(10) of the Act, which permits certain associations to invest their funds as may be approved by their funding bank under FCA regulations. Because Farmers' notes are investments, the regulation places a portfolio cap of 15 percent and a concentration limit of 50 percent of capital and surplus on association investments in Farmers' notes. Additionally, § 615.5172(d) requires participating dealers and cooperatives to endorse Farmers' notes that they sell to these associations with full recourse. The full recourse requirement is designed as a credit enhancement, which is consistent with the treatment of Farmers' notes as investments. Finally, the existing regulation requires associations to contact those notemakers who meet their credit underwriting standards, and encourage them to become FCS borrowers.

The Farmers' notes regulation has become outmoded. The FCA proposes substantial revisions to § 615.5172 that should reinvigorate this program. The proposed revisions should enable this program to evolve as agricultural credit markets continually change, so that FCS associations can help non-System lenders meet the credit needs of farmers. However, the purpose of this program remains the same, namely that FCS associations will continue to provide funding and liquidity to other agricultural creditors.

The FCA proposes four major changes to the Farmers' notes regulation so that this program will be more responsive to the needs of other creditors and their customers. First, all entities that routinely extend agricultural or aquatic credit in the normal course of their business may participate in this program. In the past, this program was restricted to private dealers and cooperatives. Now, merchants and all types of creditors will be able to sell Farmers' notes to FCS associations. Second, the FCA proposes to expand this program to long-term loans. Third, all FCS direct lenders may now invest in Farmers' notes, whereas this program was previously limited to FCS associations that had only short- and intermediate-term lending authorities. Fourth, FCS associations will be allowed to invest in notes from aquatic producers and harvesters and farm-related businesses. All these proposed changes are reflected in proposed § 615.5172(a) and (b).

Other provisions of the proposed rule ensure that FCS direct lender associations continue to treat Farmers' notes as investments. Several provisions of the proposed rule contain various requirements that are designed to enhance the credit quality of Farmers' notes. For example, proposed § 615.5172(b) reaffirms that FCS associations may invest in Farmers' notes that are secured by specified collateral that the underlying debtor pledges to creditors. The FCA also proposes to retain the 15-percent portfolio cap and the 50-percent concentration limit in § 615.5172(c). All proposed revisions to § 615.5172(c) would either conform this provision to amendments in § 615.5172(a) and (b) or are stylistic changes that enhance the clarity of this regulation. Current § 615.5172(d) requires the seller to endorse all Farmers' notes with full recourse. The FCA proposes to update this requirement by allowing other types of credit enhancements, such as guarantees, insurance, reserves of cash or marketable securities, subordinated interests, or a combination of such credit enhancements that would adequately cover the principal amount of the association's investment in Farmers' notes.

The purpose of the portfolio cap, the concentration limit, and the credit enhancements in proposed § 615.5172(d) is to ensure that Farmers' notes are treated as investments. FCS associations are credit cooperatives, and the portfolio cap and concentration limit ensure that most assets in association portfolios are loans to members. The full recourse requirement and the other credit enhancements in § 615.5172(d) lessens the credit risk that FCS associations assume from Farmers' notes.

The FCA proposes to delete the provision in § 615.5172 that currently requires associations to contact the farmers or ranchers who are indebted on these Farmers' notes, and encourage them to become FCS borrowers. This requirement may be an impediment to the success of the Farmers' notes program. Other creditors may be reluctant to sell Farmers' notes to FCS associations as long as the regulation requires such associations to lure away their customers.

The proposed revisions to the Farmers' notes regulation would give the System a greater role in providing funding and liquidity to those who extend credit to agriculture during the normal course of business. The Farmers' notes program complements the OFI

program. Farm Credit banks provide funding and liquidity to OFIs, whereas FCS direct lender associations provide these services through the Farmers' notes program. In both programs, the FCS acts as a source of funding and liquidity to agricultural creditors who need these services so they can meet the credit needs of their customers. As a result, the System fulfills its mission to finance agriculture and related activities in rural America, as Congress intended. From the FCA's perspective, agriculture benefits when System and non-System lenders cooperate to make affordable credit more available for farmers, ranchers, aquatic producers and harvesters, farm-related businesses, and rural homeowners.

IV. Capital Risk Weighting

We have previously interpreted our regulations as requiring funding banks to risk weight loans to OFIs at 100 percent. In contrast, existing § 615.5210(f)(2)(ii)(I) allows Farm Credit banks to risk weight loans to System associations at 20 percent. This means Farm Credit banks currently hold more capital (at a minimum) for loans to OFIs than loans to System associations, which in many cases have similar structures and financial conditions as OFIs.

The ANPRM acknowledged that many OFIs, particularly commercial banks or their affiliates might pose no greater risk to their FCS funding bank than System associations. However, unregulated non-bank OFIs could expose their System funding bank to greater risk than FCS associations and regulated OFIs. The preamble to the ANPRM explained, in detail, the risk-reducing features of FCS associations that justified a 20-percent risk weighting.[17]

Furthermore, as the preamble to the ANPRM observed, the risk-weighting categories in the FCA's capital regulations are patterned after the risk-weighting categories in the 1988 Basel Accord, which the other Federal bank regulatory agencies adopted and applied to all depository institutions. As a result, many, but not all, OFIs have the same risk-reducing features as FCS associations. The ANPRM asked several questions about whether and how we should amend our capital regulations to address the risk weighting of OFI loans by Farm Credit banks.

We received 38 comments on this issue during the ANPRM comment period and as part of the public meeting testimony from 28 commercial banks, two non-bank entities and OFIs, five Farm Credit banks, and two associations. The overwhelming majority of the commenters supported the concept of differentiating the risk weighting of OFI loans based on the structure and risk-mitigating characteristics of the OFIs. Under this approach, OFIs that are Federal- or state-regulated depository institutions or their affiliates would be risk-weighted at 20 percent, while unregulated non-bank OFIs might be risk weighted at a higher percentage. One unregulated OFI opposed any change to the risk weighting of OFI loans by Farm Credit banks. Three commenters, including two FCBs, suggested that Farm Credit banks apply the same risk weight to all OFI and FCS association loans.

The FCA proposes amendments to § 615.5210 that would permit Farm Credit banks to risk weight their loans to OFIs that are Federal- or state-regulated depository institutions, or their affiliates, at 20 percent. Under this proposal, Farm Credit banks would continue to risk weight loans to OFIs that are unregulated, or exhibit a higher risk profile at either 50 or 100 percent, depending on certain factors, which are explained below. Although we received no comments about how to risk weight Farmers' notes, the proposed rule would establish similar risk weights for these investments.

The proposed rule would establish a 20-percent risk weighting for OFIs or Farmers' notes sold by entities that are either: (1) An equivalent to an OECD[18] bank (Federal- or state-regulated depository institution); (2) subsidiaries of OECD equivalent banks or bank holding companies and carry full guarantees from such parent entities; or (3) an institution that carries one of the three highest ratings from a nationally recognized statistical rating organization (NRSRO).[19]

Additional criteria for a 20-percent risk weighting is that the obligation must have full recourse or another form of credit enhancement. Under § 614.4570(a), OFIs must pledge full recourse on all loans they fund or discount with a Farm Credit bank. Proposed § 615.5172(d) requires full recourse or another form of credit enhancement for Farmers' notes as described in the proposed rule.

Proposed § 615.5210 would establish a 50-percent risk weighting for OFIs or Farmers' notes sold by entities that: (1) Are not OECD banks but otherwise meet similar capital and operational standards; and (2) carry an investment grade or higher NRSRO rating. Again, full recourse or another appropriate credit enhancement is a condition for the 50-percent risk weighting. The proposed rule establishes a 100-percent risk weighting for all OFIs and Farmers' notes that do not qualify for the 20-percent or 50-percent risk weight categories.

Applying lower risk weightings for OFIs that are considered less risky would allow the FCBs to hold less capital to support such loans. This approach is consistent with the direction from the proposed Basel Accord revisions, which are currently under consideration. Lowering the capital requirements for OFI loans will lower the operating costs of the OFI program to Farm Credit banks, which in turn should lower the cost of funds to OFIs and ultimately reduce interest rates charged to OFI borrowers. These outcomes would advance the System's public mission to provide affordable credit on a consistent basis to agriculture and rural America. Greater flexibility for the risk weighting of OFI loans should provide the Farm Credit banks additional incentives to expand their lending to both existing and new OFIs.

V. Regulatory Flexibility Act

Pursuant to section 605(b) of the Regulatory Flexibility Act (5 U.S.C. 601 *et seq.*), the FCA hereby certifies that the proposed rule will not have a significant economic impact on a substantial number of small entities. Each of the banks in the System, considered together with its affiliated associations, has assets and annual income in excess of the amounts that would qualify them as small entities. Therefore, System institutions are not ''small entities'' as defined in the Regulatory Flexibility Act.

List of Subjects

12 CFR Part 614

Agriculture, Banks, banking, Foreign trade, Reporting and recordkeeping requirements, Rural areas.

[17] *See* 65 FR 21151 (April 20, 2000).

[18] *OECD* means the group of countries that are full members of the Organization for Economic Cooperation and Development, regardless of entry date, as well as countries that have concluded special lending arrangements with the International Monetary Fund's General Arrangement to Borrow, excluding any country that has rescheduled its external sovereign debt within the previous 5 years. For purposes of United States banking operations, all Federally regulated depository institutions are considered the equivalent of OECD banks.

[19] Nationally recognized statistical rating organization means an entity recognized by the Division of Market Regulation of the Securities and Exchange Commission (or any successor Division) (Commission) as a nationally recognized statistical rating organization for various purposes, including the Commission's uniform net capital requirements for brokers and dealers.

12 CFR Part 615

Accounting, Agriculture, Banks, banking, Government securities, Investments, Rural areas.

For the reasons stated in the preamble, parts 614 and 615, chapter VI, title 12 of the Code of Federal Regulations are proposed to be amended as follows:

PART 614—LOAN POLICIES AND OPERATIONS

1. The authority citation for part 614 continues to read as follows:

Authority: 42 U.S.C. 4012a, 4104a, 4104b, 4106, and 4128; secs. 1.3, 1.5, 1.6, 1.7, 1.9, 1.10, 1.11, 2.0, 2.2, 2.3, 2.4, 2.10, 2.12, 2.13, 2.15, 3.0, 3.1, 3.3, 3.7, 3.8, 3.10, 3.20, 3.28, 4.12, 4.12A, 4.13, 4.13B, 4.14, 4.14A, 4.14C, 4.14D, 4.14E, 4.18, 4.18A, 4.19, 4.25, 4.26, 4.27, 4.28, 4.36, 4.37, 5.9, 5.10, 5.17, 7.0, 7.2, 7.6, 7.8, 7.12, 7.13, 8.0, 8.5 of the Farm Credit Act (12 U.S.C. 2011, 2013, 2014, 2015, 2017, 2018, 2019, 2071, 2073, 2074, 2075, 2091, 2093, 2094, 2097, 2121, 2122, 2124, 2128, 2129, 2131, 2141, 2149, 2183, 2184, 2199, 2201, 2202, 2202a, 2202c, 2202d, 2202e, 2206, 2206a, 2207, 2211, 2212, 2213, 2214, 2219a, 2219b, 2243, 2244, 2252, 2279a, 2279a–2, 2279b, 2279c–1, 2279f, 2279f–1, 2279aa, 2279aa–5); sec. 413 of Pub. L. 100–233, 101 Stat. 1568, 1639.

Subpart P—Farm Credit Bank and Agricultural Credit Bank Financing of Other Financing Institutions

2. Revise § 614.4540(c) to read as follows: § 614.4540 *Other financing institution access to Farm Credit Banks and agricultural credit banks for funding, discount, and other similar financial assistance.*

* * * * *

(c) *Underwriting standards.* Each Farm Credit Bank and agricultural credit bank shall establish objective policies, procedures, pricing guidelines, and loan underwriting standards for determining the creditworthiness of each OFI applicant. A copy of such policies and guidelines shall be made available, upon request to each OFI and OFI applicant.

* * * * *

3. Revise § 614.4550 to read as follows:

§ 614.4550 Place of discount.

A Farm Credit Bank or agricultural credit bank may provide funding, discounting, or other similar financial assistance to any OFI applicant. However, a Farm Credit Bank or agricultural credit bank cannot fund, discount, or extend other similar financial assistance to an OFI that maintains its headquarters, or has more than 50 percent of its outstanding loan volume to eligible borrowers who conduct agricultural or aquatic operations in the chartered territory of another Farm Credit bank unless it notifies such bank in writing within five (5) business days of receiving the OFI's application for financing. Two or more Farm Credit banks cannot simultaneously fund the same OFI.

4. Revise § 614.4560(d) to read as follows:

§ 614.4560 Requirements for OFI funding relationships.

* * * * *

(d) The borrower rights requirements in part C of title IV of the Act, and the regulations in subparts K, L, and §§ 614.4516, 614.4517, 614.4518, and 614.4519 of subpart N of part 614 shall apply to all loans that an OFI funds or discounts through a Farm Credit Bank or agricultural credit bank, unless such loans are subject to the Truth-in-Lending Act, 15 U.S.C. 1601 *et seq.*

* * * * *

5. Amend § 614.4590 by adding new paragraphs (c) and (d) to read as follows:

§ 614.4590 Equitable treatment of OFIs and Farm Credit System associations.

* * * * *

(c) Upon request, each Farm Credit Bank or agricultural credit bank must provide each OFI and OFI applicant a copy of its policies, procedures, loan underwriting standards, and pricing guidelines for OFIs. The pricing guidelines must identify the specific components that make up the cost of funds for OFIs and the amount of these components in basis points.

(d) Upon request of any OFI or OFI applicant, each Farm Credit Bank or agricultural credit bank must explain in writing the reasons for any variation in the overall funding costs it charges to OFIs and direct lender associations. The written explanation must compare the cost of funds that the Farm Credit Bank or agricultural credit bank charges the aggregate of its OFIs and affiliated direct lender associations. When possible, the written explanation shall compare the costs of funding that the bank charges several OFIs and FCS associations that are similar in size. However, the Farm Credit Bank or agricultural credit bank must not disclose financial or confidential information about any individual FCS association.

6. Amend part 614, subpart P by adding a new § 614.4595 to read as follows:

§ 614.4595 Public disclosure about OFIs.

A Farm Credit Bank or agricultural credit bank may disclose to members of the public the name, address, telephone number, and Internet Web site address of any affiliated OFI only if such OFI, through a duly authorized officer, consents in writing. Each Farm Credit Bank and agricultural credit bank must adopt policies and procedures for obtaining and maintaining the consent of its OFIs and for disclosing this information to the public.

PART 615—FUNDING AND FISCAL AFFAIRS, LOAN POLICIES AND OPERATIONS, AND FUNDING OPERATIONS

7. The authority citation for part 615 continues to read as follows:

Authority: Secs. 1.5, 1.7, 1.10, 1.11, 1.12, 2.2, 2.3, 2.4, 2.5, 2.12, 3.1, 3.7, 3.11, 3.25, 4.3, 4.3A, 4.9, 4.14B, 4.25, 5.9, 5.17, 6.20, 6.26, 8.0, 8.3, 8.4, 8.6, 8.7, 8.8, 8.10, 8.12 of the Farm Credit Act (12 U.S.C. 2013, 2015, 2018, 2019, 2020, 2073, 2074, 2075, 2076, 2093, 2122, 2128, 2132, 2146, 2154, 2154a, 2160, 2202b, 2211, 2243, 2252, 2278b, 2278b-6, 2279aa, 2279aa-3, 2279aa-4, 2279aa-6, 2279aa-7, 2279aa-8, 2279aa-10, 2279aa-12); sec. 301(a) of Pub. L. 100–233, 101 Stat. 1568, 1608.

Subpart F—Property, Transfers of Capital, and Other Investments

8. Revise § 615.5172 to read as follows:

§ 615.5172 Investments by associations in Farmers' notes.

(a) In accordance with policies prescribed by the board of directors of the Farm Credit Bank or agricultural credit bank that funds it and each direct lender association, each direct lender association may invest in notes, sales contracts, and other similar obligations (hereafter Farmers' notes) that eligible farmers, ranchers, producers and harvesters of aquatic products, and farm-related businesses give to entities that routinely extend credit in the normal course of their business.

(b) Farmers' notes must be secured by:

(1) Collateral of a capital nature that eligible farmers, ranchers, producers and harvesters of aquatic products use in their agricultural or aquatic operations or for their household needs;

(2) Collateral of a capital nature that eligible farm-related businesses use in providing farm-related services to eligible farmers and ranchers.

(c) The total amount that an association may invest in Farmers' notes, at any one time, must not exceed 15 percent of the balance of its loans outstanding at the close of the association's preceding fiscal year. In addition, the total amount that an association may carry as investments in Farmers' notes originated by any one selling entity must not exceed 50

percent of the association's capital and surplus.

(d) All Farmers' notes in which an association invests shall have at least one or a combination of the following credit enhancements:

(1) The selling entity must endorse these Farmers' notes with full recourse;

(2) A guarantee by a creditworthy third party covers the full principal amount of the Farmers' note;

(3) Acceptable insurance covers the principal amount of each Farmers' note;

(4) The selling entity or a third party maintains a reserve of cash or marketable securities in an amount that equals or exceeds 10 percent of the principal amount of each Farmers' note;

(5) The selling entity or a third party holds a subordinated interest that equals or exceeds 10 percent of the principal amount of each Farmers' note; or

(6) The entire principal amount of the Farmers' notes is covered by a combination of credit enhancements listed in this section.

Subpart H—Capital Adequacy

9. Amend § 615.5210 by adding new paragraphs (f)(2)(ii)(M) and (N); (f)(2)(iii)(C); and (f)(2)(iv)(E) and (F) to read as follows:

§ 615.5210 Computation of the permanent capital ratio.

* * * * *

(f) * * *

(2) * * *

(ii) * * *

(M) Claims on other financing institutions provided that:

(*1*) The other financing institution qualifies as an OECD bank or it is owned and controlled by an OECD bank that guarantees the claim, or

(*2*) The other financing institution has a rating in one of the highest three investment-grade rating categories from a NRSRO or the claim is guaranteed by a parent company with such a rating, and

(*3*) The other financing institution has endorsed all obligations it pledges to its funding Farm Credit bank with full recourse.

(N) Investments in Farmers' notes that:

(*1*) Provide the Farm Credit System direct lender association full recourse against a seller or has other acceptable credit enhancements specified in § 615.5172(d), and

(*2*) Are guaranteed by an OECD bank or other institution that qualifies for a 20-percent risk weight under this section, or

(*3*) Are sold by entities that:

(*i*) Are rated in one of the highest three investment-grade rating categories from a NRSRO or the investment is guaranteed by a parent company with such a rating. If the entity has more than one NRSRO rating the lowest rating shall apply.

(*ii*) Maintain capital to total assets of at least 9 percent.

(iii) * * *

(C) Claims on other financing institutions that:

(*1*) Are not covered by the provisions of paragraph (f)(2)(ii)(M) of this section, but otherwise meet similar capital, risk identification and control, and operational standards, or

(*2*) Carry an investment-grade or higher NRSRO rating, and

(*3*) The other financing institution has endorsed all obligations to its Farm Credit funding bank with full recourse.

(D) Investments in Farmers' notes that:

(*1*) Provide the Farm Credit System direct lender association full recourse against a seller or has other acceptable credit enhancements specified in § 615.5172(d), and

(*2*) The seller is not covered by the provisions of paragraph N (20-percent risk weight), but otherwise meets similar capital, risk identification and control, and operational standards, or

(*3*) The credit provider carries an investment-grade or higher NRSRO rating.

(iv) * * *

(E) Claims on other financing institutions that do not otherwise qualify for a lower risk weight category under this section.

(F) Investments in Farmers' notes that do not otherwise qualify for a lower risk weight under this section.

* * * * *

Dated: August 6, 2003.

Jeanette C. Brinkley,

Secretary, Farm Credit Administration Board.

[FR Doc. 03–20360 Filed 8–8–03; 8:45 am]

BILLING CODE 6705–01–P

DEPARTMENT OF TRANSPORTATION

Federal Aviation Administration

14 CFR Part 39

[Docket No. 2002–NM–173–AD]

RIN 2120–AA64

Airworthiness Directives; Boeing Model 747–400, –400D, and –400F Series Airplanes Equipped With General Electric (GE) or Pratt & Whitney (P&W) Series Engines

AGENCY: Federal Aviation Administration, DOT.

ACTION: Notice of proposed rulemaking (NPRM).

SUMMARY: This document proposes the adoption of a new airworthiness directive (AD) that is applicable to certain Boeing Model 747–400, –400D, and –400F series airplanes; equipped with GE or P&W series engines. This proposal would require modifications and functional tests of the wiring of the wire integration unit and the air supply control test unit (ASCTU) of the engine bleed air distribution system. This action is necessary to prevent inadvertent commanded shutdown of the engine bleed air distribution systems due to an erroneous ASCTU command. Such a shutdown could cause depressurization of the airplane and subsequent ice build-up on the engine inlets during descent, which could result in ingestion of ice into the engine(s) and consequent loss of thrust on one or more engines. This action is intended to address the identified unsafe condition.

DATES: Comments must be received by September 25, 2003.

ADDRESSES: Submit comments in triplicate to the Federal Aviation Administration (FAA), Transport Airplane Directorate, ANM–114, Attention: Rules Docket No. 2002–NM–173–AD, 1601 Lind Avenue, SW., Renton, Washington 98055–4056. Comments may be inspected at this location between 9 a.m. and 3 p.m., Monday through Friday, except Federal holidays. Comments may be submitted via fax to (425) 227–1232. Comments may also be sent via the Internet using the following address: *9-anm-nprmcomment@faa.gov.* Comments sent via fax or the Internet must contain ''Docket No. 2002–NM–173–AD'' in the subject line and need not be submitted in triplicate. Comments sent via the Internet as attached electronic files must be formatted in Microsoft Word 97 or 2000 or ASCII text.

The service information referenced in the proposed rule may be obtained from Boeing Commercial Airplane Group, P.O. Box 3707, Seattle, Washington 98124–2207. This information may be examined at the FAA, Transport Airplane Directorate, 1601 Lind Avenue, SW., Renton, Washington.

FOR FURTHER INFORMATION CONTACT: Don Eiford, Aerospace Engineer, Systems and Equipment Branch, ANM–130S, FAA, Seattle Aircraft Certification Office, 1601 Lind Avenue, SW., Renton, Washington 98055–4056; telephone (425) 917–6465; fax (425) 917–6590.

SUPPLEMENTARY INFORMATION: