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DEPARTMENT OF AGRICULTURE

Farm Service Agency

7 CFR Parts 761 and 762

RIN 0560-AH66

Maximum Interest Rates on Guaranteed Farm Loans

AGENCY: Farm Service Agency, USDA.

ACTION: Interim rule.

SUMMARY: The Farm Service Agency (FSA) is issuing this interim rule amending the regulations that specify interest rates on guaranteed farm loans. This rule will tie the maximum interest rate that may be charged on FSA guaranteed farm loans to nationally published indices, specifically the 3-month London Interbank Offered Rate (LIBOR) or the 5-year Treasury note rate, unless the lender uses a formal written risk-based pricing practice for loans, in which case the rate must be at least one risk tier lower than the borrower would receive without the guarantee. These provisions are intended to increase clarity and specificity in the maximum rate requirements, while at the same time setting rates that will work in current credit market conditions.

DATES: Effective Date: **[Insert date 60 days after publication in the FEDERAL REGISTER]**.

Comment Date: We will consider comments that we receive by **[insert date 90 days after publication in the FEDERAL REGISTER]**.

ADDRESSES: We invite you to submit comments on this interim rule. In your comment, please specify RIN 0560-AH66 and include the volume, date, and page

number of this issue of the Federal Register. You may submit comments by either of the following methods:

- Federal eRulemaking Portal: Go to http://www.regulations.gov. Follow the instructions for submitting comments.
- Mail: Director, Loan Making Division, the Farm Loan Program (FLP), FSA, US Department of Agriculture, 1400 Independence Avenue, SW, Stop 0522, Washington DC 20250-0522.

Comments will be available for inspection online at http://www.regulations.gov and in the Office of the Director, Loan Making Division, FSA, USDA, 1400 Independence Avenue, SW, Stop 0522, Washington, DC 20250-0522, between 8 a.m. and 4:30 p.m., except holidays.

FOR FURTHER INFORMATION CONTACT: Trent Rogers; telephone: (202) 720-3889. Persons with disabilities or who require alternative means for communications should contact the USDA Target Center at (202) 720-2600 (voice and TDD).

SUPPLEMENTARY INFORMATION:

Background

FSA guaranteed loans provide credit to farmers whose financial risk exceeds a level acceptable to commercial lenders. Loans are made to assist those eligible farmers as specified in 7 CFR 762.120 who are not able to obtain conventional loans at reasonable rates and terms. FSA provides commercial lenders (for example, commercial banks, mutual savings banks, mortgage banks, Farm Credit System institutions, credit unions) with a guarantee for up to 95 percent of the loss of principal and interest on a

guaranteed loan (see 7 CFR 762.129). In fiscal year 2010, FSA guaranteed over $3.3 billion farm ownership (FO) and operating loans (OL).

The FSA guarantee reduces the lender's risk of loss. FSA believes the borrower should receive some of the benefit of the reduction in the lender's credit cost in the form of a lower interest rate than the borrower would otherwise receive. Therefore, the FSA regulations for the guaranteed loan program limit the amount of interest that a lender may charge guaranteed loan customers. The existing regulations in 7 CFR 762.124(a)(3) tie the rate to that rate charged an "average agricultural loan customer," as defined in 7 CFR 761.2. This rule would not change the core policy of limiting rates on guaranteed loans to allow the borrower to receive some of the benefit of the guarantee, but would make that policy clearer to implement by tying maximum interest rates to widely published indices. The specific maximum rates will also simplify compliance, as it will be easier to demonstrate that a rate was below the maximum on a specific date than demonstrate it was at or below the rate charged an average agricultural loan customer.

This interim rule follows a proposed rule on the same topic that was published on September 30, 2008 (73 FR 56754-56756). The proposed rule included provisions tying maximum rates to widely published indices. The proposed maximum "spread" between the indices and the maximum rates was based on FSA analysis of over 10 years of data on actual guaranteed loan rates and indices. Based on that data, most guaranteed loans made between 1999 and 2010 would have met the requirements in the proposed rule. This interim rule addresses comments made on the proposed rule; substantive changes were made to address the comments.

General Discussion of Comments and Substantive Changes Made in Response to Comments

In response to the proposed rule, FSA received 97 comments from individuals, organizations, banks, Farm Credit System lenders, lending associations, government agencies and FSA employees. Most comments supported the concept of more clear maximum interest rate requirements, but opposed the specifics of the proposed rule, although there was not a consensus on alternative provisions. Many commenters noted that the proposed interest rate benchmarks would not work in the unusual credit environment that was present in late 2008, when the proposed rule was published. Most comments strongly supported eliminating the term "average agricultural loan customer," which was generally considered to be lacking in clarity and enforceability.

In balancing the need to clarify the regulations with the opportunity for public comment on how the amendments would function in more typical market conditions, FSA has decided to publish an interim rule with a 90 day period for additional public comment. The cost benefit analysis done for this rule, which updates the analysis done for the proposed rule, shows that more than 95 percent of guaranteed loans made in 2009 and 2010 would have met the requirements in this interim rule. We find that the substantive changes in this rule fully address the issue raised by commenters regarding effective maximum rates in unusual market conditions. In response to the many comments received on the proposed rule stating that the proposed rates would not work in current credit market conditions, FSA has increased the maximum rates permitted in this rule, and will allow a further increase if the 3-month LIBOR falls below 2 percent.

This rule makes changes to FLP regulations in 7 CFR parts 761 and 762. The changes in 7 CFR part 761, "General Program Administration," remove the definition for "average agricultural loan customer" and add a reference to the abbreviation, LIBOR. The changes in 7 CFR part 762, "Guaranteed Farm Loans," clarify how maximum interest rates will be calculated for various types of guaranteed loans.

The substantive differences in this interim rule as compared to the provisions in the proposed rule are:

- the indices used in this rule are different from those proposed;
- this rule increases the allowable maximum rate "spread" above the indices by 300 basis points (3 percentage points) from what was proposed;
- this rule sets the maximum rate based on the term over which the rate is fixed, rather than purpose of loan (maximum rates are now the same for operating and ownership loans);
- the proposed provisions allowing FSA to set a different, unspecified, rate during extraordinary market conditions are replaced with more specific provisions allowing a 100 basis point higher "spread" if the 3-month LIBOR falls below 2 percent.

As discussed in more detail below, the proposed rule based maximum rate on the New York Prime and the 10-year Treasury note rate indices. This interim rule uses the 3-month LIBOR and the 5-year Treasury note rate as the indices. The proposed rule specified that the maximum rate allowed for guaranteed loans would be a 250 basis point (2.5 percentage points) spread above New York Prime for Operating loans (OL), and a 350 basis point (3.5 percentage points) spread above 10-year Treasury for Farm

Ownership Loans (FO). This interim rule sets the maximum allowable spread at 650 basis points (6.5 percentage points) above 3-month LIBOR for variable rate loans and those fixed for less than five years, and 550 basis points (5.5 percentage points) above 5-year Treasury for loans fixed for five years or more. The rates are the same for FO and OL in this rule.

The proposed rule included a provision that the maximum interest rate limitations could be modified by FSA in times of extraordinary conditions. This interim rule specifies the extraordinary condition (3-month LIBOR falls below 2 percent) that will automatically trigger a specific 100 basis point increase in the allowable spread. If the 3-month LIBOR falls below 2 percent, the maximum allowable spreads will increase by 100 basis points (1 percentage points), to 750 basis points above the 3-month LIBOR for variable rate loans and 650 basis points above the 5-year Treasury note rate for loans fixed for terms of 5 or more years, regardless of the program type.

We are issuing this interim rule in an attempt to provide clarity to borrowers and lenders in this marketplace and to reduce regulatory uncertainty. We do not believe that this change will substantially alter the interest rates available to borrowers, nor is it our intention to do so. In order to ensure that we have selected the right maximum rates, and to ensure that there are no unintended consequences of this action, we will carefully monitor the implementation of this rule. If we receive comments indicating that there is a substantial negative effect on either borrowers or lenders, we will take those comments into account in determining whether to suspend implementation of this rule. We welcome comments on our approach.

Discussion of Comments

The following provides a discussion of the specific public comments received, and FSA's responses, including changes we are making to the regulations in response to the comments.

Comment: FSA should suspend or delay action on this regulation and reconsider it at a later time when credit markets are more stable.

Response: We are publishing this interim rule, with an additional 90 day comment period, rather than proceeding directly to final rule. This provides more opportunity for public comment, and more time for markets to stabilize, while at the same time providing needed clarity to the guaranteed loan program regulations.

Comment: FSA should withdraw its amendments due to the uncertainty and volatility in the current markets.

Response: As mentioned above, we are publishing this interim rule to provide more opportunity for public comment and more time for markets to stabilize.

Comment: FSA should publish an interim rule rather than a final rule because we would like to see how the options USDA implements actually work.

Response: FSA agrees and is issuing an interim rule.

Comment: FSA should let the market dictate what interest rate lenders charge guaranteed borrowers, rather than placing any limits on the rates. Guaranteed borrowers are inherently financially weaker than the lender's typical customer, and are more expensive to service. The guarantee does not reduce lender's risk of borrower default, and they should be permitted to price accordingly.

Response: It is not FSA's intent to set interest rates, but rather to establish broad guidelines. While FSA believes the guarantee reduces risk of loss to the lender, we recognize that a guaranteed borrower may still be financially weaker and more expensive to service than their typical customer. This interim rule should provide lenders enough flexibility to set loan rates based on market factors and to reflect a lender's cost, a borrower's risk, and loan characteristics. Therefore, no change is made to the rule in response to this comment.

Comment: Lenders should be able to base the rate on local market rates, not the maximums, if using the maximums would otherwise result in a denial of credit to the borrower.

Response: Lenders using risk-based pricing practices specified in 7 CFR 762.124(a) would not have to use the indexed rate maximum. This interim rule should enable other lenders sufficient flexibility to base rates on local conditions. Lenders will likely price loans based on their cost of funds or competition.

Comment: There should not be any limits on interest rates. We disagree with USDA's assertion that guaranteed loans automatically reduce lender costs. Lenders should be allowed to charge a rate that is reflective of local market conditions.

Response: Part of the intent of the program is for the borrower to receive the benefit of the reduction in the lender's credit cost in the form of a lower interest rate. The interim rule provides broad guidelines that will allow lenders to adjust accordingly.

Comment: The rule should not limit the rate of a variable rate loan throughout the life of the loan.

Response: It was not our intent for the rule to do so. The interest rate maximums in this rule will be applicable only at loan closing or restructuring, but then rates may fluctuate according to the bank policy that applies to other, non-guaranteed loans, without being restricted by any maximums. We have clarified the provisions in this rule for variable rate loans to state that the rate maximum applies only at the time of loan closing or loan restructuring.

Comment: A national index would reduce lenders' ability to control profit margins.

Response: Under the revised rule lenders should have substantial flexibility in loan pricing and, therefore profit margins.

Comment: Rather than implementing the proposed interest rate maximums, the following language should be adopted: "On the date of loan closing, the interest rate charged by the lender to a borrower with a Farm Service Agency guaranty shall not exceed the interest rate the lender charges a non-guarantee borrower of a similar type, term or loan purpose."

Response: A requirement that rates not exceed the interest rate charged a non-guarantee borrower and provides the specific language for loan type, term, loan purpose, and specific date would provide no benefit to the guaranteed borrower. One of the purposes of the amendments is to ensure that borrowers receive some of the benefit from the reduced risk provided by the guarantee, in the form of a lower rate, not the same rate, than a similar non-guarantee borrower. Therefore, no change is made to the rule in response to this comment.

Comment: Eliminate "average agricultural loan customer" from the definitions. We do not have an average agricultural loan customer rate and it is difficult for lenders to apply this definition. The index and maximum spread is a reasonable and appropriate alternative to the ambiguous "average agricultural loan customer."

Response: As proposed, we have removed the term.

Comment: Don't remove the "average agricultural loan customer" definition. The existing regulations are clear and not vague and FSA's proposal to benchmark interest rates to published indices would add more complexity to the current FSA rules, and more compliance regulation for the small agricultural community banks.

Response: The "average agricultural loan customer" implies a flat-rate loan pricing policy through which all farm customers receive the same rate, which is considered inconsistent with current industry practices. We received many comments that the "average agricultural loan customer" term is ambiguous and makes it difficult for lenders to demonstrate compliance, and it is therefore removed. The new rate maximums, which are clearly specified and based on widely published indices, are not complex; there are only two maximum rates in effect at any time, which should simplify compliance for all types of lenders.

Comment: We support the basic concept to allow lenders to use an internal risk-based pricing practice. However, there are concerns with the way the provisions in the proposed rule are specified. The term "moderate risk borrower" is still too vague and should not be used.

Response: In response to this comment, this rule removes the references to a "moderate risk borrower" that were in the proposed rule and instead refers specifically to a lower risk tier than the borrower would otherwise qualify for.

Comment: Provisions under the proposed rule do not allow a risk-based pricing practice to work effectively within the community banking system.

Response: It is not the intent of FSA to require banks to use risk-based pricing practices in order to participate in the guaranteed loan program. Any lender without a written risk-based pricing practice may use any other pricing practices (for example, cost-plus, flat-rate, or market based) to price guaranteed loans, provided the rates do not exceed the required maximums.

Comment: FSA has not established a clear limit for the interest rate that can be charged to a moderate risk borrower, and by not establishing a clear limit for lenders using risk-based pricing practices, there may be wide variances among lenders.

Response: In response to this comment, this rule removes all references to a moderate risk borrower that were in the proposed rule and instead refers specifically to a lower risk tier than the borrower would otherwise qualify for.

Comment: The proposed middle risk tier does not represent a typical or moderate strength customer. One risk-based pricing practice used within our institution uses a 14-tier scale, but tier 7 is not "moderate risk." In general, the first 9 tiers map to a Fully Acceptable loan, a 9 would be low Acceptable, 10 would be Special Mention, 11 and 12 would be Substandard and the remaining ratings map to Doubtful and Loss. Under this type of risk-based pricing practice, the moderate risk loan would likely be rated 10 or 11, not the middle tier of 7 and 8 as the FSA proposed rule specified. As an alternative, we

suggest that for loans protected by a guarantee, the lender assign it a risk tier at least one tier lower (representing lower risk and therefore a lower interest rate) than that borrower would receive without a guarantee.

Response: We agree that the suggested alternative of specifying one lower risk tier is a straightforward and objective methodology which accommodates lender pricing practices better than specifying that the middle tier be used. This alternative would satisfy the objective of providing benefit to the borrower with a lower interest rate, and is a clear and unambiguous requirement for lenders. In response to this and other similar comments, this rule removes all references to a moderate risk or middle tier borrower that were in the proposed rule and instead refers specifically to a risk tier one tier lower than the borrower would otherwise qualify for.

Comment: The term "model" implies a much more sophisticated process than is typically used to price loans. A common understanding of a "model" would include pricing resulting from an economic capital model that is a pure form of a risk-based pricing, taking into consideration different levels of risk and the probability of default, exposure to default, and loss given default. That is more detailed analysis than is typically performed to develop loan pricing by agricultural lenders and we suggest that FSA therefore refer to it as a pricing "practice" rather than a pricing "model."

Response: It is our intention to follow lender practices where practical. Therefore, this suggestion is adopted in this interim rule; references to "pricing models" in the proposed rule have been replaced with references to "pricing practices." Additional guidance and examples will be published in FSA internal handbooks of how a risk-based pricing practice may be used to determine the maximum loan rate.

Comment: Our risk-based pricing practice uses detailed actuarial data. FSA should set the policy regarding risk rating without examining or challenging the actuarial detail.

Response: If a risk-based pricing practice is used, the lender must provide FSA with information about its risk-based pricing practices if requested by FSA. That does not necessarily mean that FSA will challenge those practices. The purpose of requesting the information is so that FSA could determine compliance in the context of the lender's specific risk-based pricing practice, rather than to challenge the actuarial detail.

Comment: A bank's pricing matrix is part of an institution's business model and therefore proprietary. FSA should state clearly in the regulation, not just the preamble, that a lender's pricing matrix is not discoverable via a Freedom of Information Act (FOIA) request, and is not otherwise available for public inspection.

Response: FSA understands the concern, but does not feel that a specific provision in the regulation is needed or appropriate. FSA does not intend to release a lender's risk-based pricing practice to any non-government entity or party as a result of a FOIA request. The lender's risk-based pricing practice would be protected under the Privacy Act of 1974 following FSA's normal procedures.

Comment: The proposed interest rate limits and indices are not appropriate and will not allow us to extend credit under current market conditions.

Response: FSA proposed new interest rate limits based on widely recognized indices, with the intent of providing simple, clear, straightforward limits that would not hamper lender participation in the program. As stated in the Supplementary Information section of the proposed rule, the proposed indices and rates were based on a detailed

analysis of 10 years of interest rate data. The proposed rule's comment period occurred during a period of historic financial market disruption. In response to this comment and similar comments, we are publishing this interim rule with different indices and spreads resulting in higher interest rate maximums than in the proposed rule, with an additional provision for an even wider spread in market conditions such as those that existed from 2009 to 2010. As part of the cost benefit analysis for this rule, we determined that more than 95 percent of guaranteed loans made in 2009 and 2010 by lenders of all sizes would meet the requirements in this interim rule.

Comment: The selected indices are not the most appropriate ones. Alternatives include the Farmer Mac Cost of Funds Index (COFI), 3-Month COFI, 1-Year COFI, 5-Year Reset COFI, 10-Year Reset COFI, 15-Year Reset COFI, Federal Farm Credit Banks (FFCB) Funding Corporation Cost Index, LIBOR, LIBOR Swap Curve, Federal Home Loan Bank (FHLB), 5-year Treasury note rate, and 10-year Constant Maturities Treasury (CMT). Farmer Mac II COFI is particularly appropriate because of the availability to sell loans into the secondary market and it is nationally recognized and familiar to FSA.

Response: Our analysis for the proposed rule showed that the Wall Street Journal Prime Rate and 10 year Treasury rate most closely tracked to guaranteed loan rates, using 10 years of data from 1999 to 2008. However, given the input from commenters, we have done additional analysis using more recent 2009 and 2010 data. Based on the comments, FSA reviewed lending practices and the various indices and determined that the 3-month LIBOR was the most reflective of lender funding costs for variable rate loans or fixed rate loans with rates fixed for terms of less than 5 years regardless of

program type. Similarly, the 5-year Treasury note rate was the most reflective for loans with rates fixed for 5 years or more. The use of these commonly used indices should not restrict the ability of lenders to sell loans into the secondary market. We also conducted an analysis, including a comparison to our proposed rule, to determine an appropriate maximum spread over these indices in a normal interest rate environment. Based on this analysis, we determined that for variable rate loans and loans with rates fixed for less than 5 years, the maximum rate will be 650 basis points (6.5 percentage points) over the 3-month LIBOR, regardless of program type. Loans with rates fixed for 5 years or longer will be limited to no more than 550 basis points (5.5 percentage points) over the 5-year Treasury note rate, regardless of program type. The spread may increase by 100 basis points when the 3-month LIBOR is below 2 percent, as it is now. These spreads result in higher maximum rates than those in the proposed rule. As noted earlier, more than 95 percent of guaranteed loans made in 2009 and 2010 by lenders of all sizes would meet the requirements in this rule.

Comment: With the rates in the proposed rule, lenders would be prevented from making fixed rate loans to their farm customers, regardless of term or type, due to the fluctuation in yield curves and the availability to book or sell loans into the secondary market. With variable rate loans, at some time in the future, the effective interest rate, if based on the Treasury note rate or New York Prime rate, could increase, which would increase the payment amount and could place the borrower into a negative cashflow.

Response: As noted earlier, this interim rule includes higher maximum rates for both fixed and variable rate loans than were in the proposed rule, in response to comments and continued atypical credit market conditions. It was not the intent to

require that variable rate loans be pegged to the indices for the duration of the loan. This rule clarifies that variable rate loans must have an initial rate below a certain maximum at the time the loan is made or restructured, but that the rate can vary over the term of the loan. As with all variable rate loans, guaranteed or not, the rate may rise or fall in the future.

Comment: The 10-year Treasury note rate, or any single rate, would eliminate most of the available long term fixed financing, particularly for operating loans.

Response: The interim rule uses the 5-year Treasury note rate as the index for loans with rates fixed for five years or greater, and permits rates up to 5.5 percentage points greater than the index. For example, if the 5-year Treasury note rate is 2.5 percent, lenders may charge up to 8 percent on a guaranteed loan fixed for a term of 5 or more years. Lenders that use risk-based pricing practices do not have to use the indexed maximum rate, they may provide guaranteed loans at a rate that is at least one risk tier lower than the borrower would otherwise qualify for. This offers some flexibility for lenders who do not feel that the specified maximum rate fits their needs.

Comment: The rule does not include provisions to ensure that interest rate adjustments made after loan origination on variable rate loans are reasonable.

Response: Variable rates can fluctuate according to the bank's internal practices for similar, non-guaranteed loans and this rule specifies the lender must provide FSA with these rate adjustment policies, if requested. Our objective is to follow standard lender practices when practical and we have determined that this is an adequate control and will result in rates that are similar to those charged to other customers without the FSA guarantee.

Comment: The rates or the indices used should be tied to the lenders' cost of funds rather than historical data.

Response: The decision to use the 3-month LIBOR and 5-year Treasury rates as indices in the interim rule was that they more closely reflected a lenders' cost of funds. As discussed later, the cost benefit analysis explains that these indices did closely track rates on guaranteed loans charged by lenders' over the 1999 through 2010 time period.

Comment: If maximum spreads are included in the regulations, banks should be allowed to raise the spreads 100 basis points if necessary to extend credit. This would allow lenders to react as necessary to unusual financial marketplace disruptions such as are now being witnessed.

Response: That change has been made in this rule. If the 3-month LIBOR is below 2 percent, the maximum spreads are now 100 basis points higher than is permitted under more normal market conditions.

Comment: FSA should consider using LIBOR or LIBOR swap curve index for loans beyond short term variable and increase the spread to 400 basis points.

Response: FSA changed the rule, to add the LIBOR index and to increase the allowable spread for loans with rates fixed for less than 5 years.

Comment: The spreads used to determine maximum rates should be larger.

Response: FSA changed the rule in response to this comment. As a result of changing the indices and increasing spreads, the maximum rates in this interim rule averaged 200 basis points higher than in the proposed rule (193 basis points for loans fixed for less than 5 years; 225 basis points for loans fixed for 5 or more years) over the 1999 through 2010 period.

Comment: There should not be any type of ceiling for interest rates because if interest rates were to rise, the interest rate compression with an interest rate ceiling could lead to lender inability to use this program.

Response: There is no fixed ceiling specified in this rule; the maximum rate "floats" with the indices. If interest rates rise, the maximum rate rises. For example, if the 3-month LIBOR rises from 3 percent to 4 percent, the maximum allowable rate on a guaranteed variable rate loan as specified in this rule rises from 9.5 percent to 10.5 percent.

Comment: Lenders typically charge less than the proposed maximum rates. Lenders would raise their rates to match these maximums, resulting in no benefit to the guaranteed loan borrower from the reduced risk of loss with a guarantee.

Response: Competition should prevent lenders from raising their rates to match the maximum rate if that maximum is higher than the market rate. In nearly all regions of the country, FSA guarantees represent only a small overall market share (4 percent nationwide), and would be expected to have little influence on market rates. Therefore, it would be expected that guaranteed lenders who systemically attempt to price above the market rate would face substantive competitive pressure.

Comment: The proposed indices and spreads are a good idea, as it is difficult to determine what the average farm customer receives. The New York prime rate plus 3 percent is reasonable for larger and more solid OLs, however loans to higher risk borrowers requesting loans of $50,000 or less should have a spread up to New York Prime rate plus 4 percent. The maximums should be the same for all FOs, regardless of size.

Response: This interim rule allows up to 650 basis points above the index for variable rate loans or fixed rate loans with rates fixed for less than 5 years and 550 basis points above the index for loans fixed for more than 5 years, regardless of size or purpose (FO vs. OL) of loan. Consequently, the maximum rates in this rule are 200 basis points higher than they would have been in the proposed rule. The size and purpose of loan are not used to determine which maximum rate applies, in part because FSA wanted to make the regulations clear and simple to implement. Since maximum rates are based on the term over which the rate is fixed, a shorter term FO could have a different rate than a longer term FO.

Comment: If FSA imposes maximum spreads over the proposed indices, lenders should be able to set a "floor" in times of unusual financial market disruptions, in order for lenders to cover cost of lending and institutions operating expenses. The floor should be between 5 percent to 8 percent. Without a floor, lenders may not be able to extend credit to farmers in times of very low rates.

Response: Lenders may set a floor (minimum rate), so long as it is at or below the maximum rates set in this rule, but lenders are not required by this rule to set such a floor. This rule addresses the issue of appropriate spreads in times of unusual market conditions by allowing higher maximum rates above the indices (650 basis points for variable rate loans and 750 basis points for fixed rate loans) if the 3-month LIBOR is below 2 percent. This is considered less arbitrary than allowing lender to set "floors" during unusual financial times. (If the 3-month LIBOR were literally zero, that would allow maximum rates of 6.5 percent and 7.5 percent, which is within the range suggested by this comment.) This provision allows lenders to charge less than that maximum. FSA

is concerned that a mandatory "floor" provision which prohibited lenders from charging interest rates below a certain minimum rate could discourage borrowers from using FSA loans in times of extraordinary market conditions, particularly if the floor was above market rates. FSA did not include a mandatory floor in the interim rule. Lenders are free to set any floor they want.

Comment: Instead of the provisions for moderate risk borrowers, interest rates should be based on a point system like the one used by the Small Business Administration (SBA).

Response: It is not clear what regulatory alternative is suggested with this comment. If this comment refers to SBA loan regulations that provide different loan rate maximums based on the size, purpose, and type of the loan, the goal in revising the FLP regulations was to make them as clear and simple to implement as possible. We feel that the simple structure of only two maximum levels, independent of the size or purpose of the loan, serves that goal.

Executive Orders 12866 and 13563

Executive Order 12866, "Regulatory Planning and Review," and Executive Order 13563, "Improving Regulation and Regulatory Review," direct agencies to assess all costs and benefits of available regulatory alternatives and, if regulation is necessary, to select regulatory approaches that maximize net benefits (including potential economic, environmental, public health and safety effects, distributive impacts, and equity). Executive Order 13563 emphasized the importance of quantifying both costs and benefits, of reducing costs, of harmonizing rules, and of promoting flexibility.

The Office of Management and Budget (OMB) designated this rule as significant under Executive Order 12866, "Regulatory Planning and Review," and has reviewed this rule. A summary of the cost benefit analysis is provided below and is available at http://www.regulations.gov and from the contact information listed above.

Clarity of the Regulation

Executive Order 12866, as supplemented by Executive Order 13563, requires each agency to write all rules in plain language. In addition to your substantive comments on these proposed rules, we invite your comments on how to make them easier to understand. For example:

- Are the requirements in the rule clearly stated? Are the scope and intent of the rule clear?
- Does the rule contain technical language or jargon that is not clear?
- Is the material logically organized?
- Would changing the grouping or order of sections or adding headings make the rule easier to understand?
- Could we improve clarity by adding tables, lists, or diagrams?
- Would more, but shorter, sections be better? Are there specific sections that are too long or confusing?
- What else could we do to make the rule easier to understand?

Summary of Costs and Benefits

In the cost benefit analysis, rates charged on FSA guarantees over the 1999 through 2010 period were analyzed and compared with different indices. While the analysis indicated a substantial variability in rates charged on guaranteed loans, rates were generally consistent with similar purpose unguaranteed farm loans made at the same time by commercial banks. It was determined that if the interim rule had been in effect from 1999 through 2010, over 95 percent of the guaranteed loans would have been under the maximum. While lower thresholds were considered, it was determined that these could be disruptive, as lenders might be inclined to make fewer guaranteed loans. That could result in an increase in demand for FSA direct loans, which are more costly to the Federal government.

While most lenders and borrowers will benefit from the changes in this interim rule, a few farmers may be unable to obtain guaranteed loans and may turn to direct loans for capital. Since direct programs as more expensive to administer, this would impose a slight cost on taxpayers ($1 to $5 million). These costs must be considered in light of expected benefits, many of which are intangible. Elimination of the unclear "average agricultural loan customer" designation should benefit borrowers and lenders alike. Lenders with risk pricing procedures should find compliance easier. Other lenders will be free to use their existing loan pricing procedures, as long as the rates do not exceed the maximum. While implementation of absolute maximum rates could result in some farmers not being able to obtain guaranteed loans, our analysis suggests that this number would be very small. Also, guaranteed loans which lenders consider so risky that they require rates of 100 or more basis points above the maximum should probably be made as

direct loans. As a direct loan, the easier terms would enable the borrower to have a greater chance of success.

Regulatory Flexibility Act

The Regulatory Flexibility Act (5 U.S.C. 601-612), as amended by the Small Business Regulatory Enforcement Fairness Act of 1996 (SBREFA), generally requires an agency to prepare a regulatory flexibility analysis of any rule subject to the notice and comment rulemaking requirements under the Administrative Procedure Act (5 U.S.C. 553) or any other statute, unless FSA certifies that the rule will not have a significant economic impact on a substantial number of small entities. FSA has determined that this rule will not have a significant impact on a substantial number of small entities for the reasons explained below. Consequently, FSA has not prepared a regulatory flexibility analysis.

This rule is not expected to change the ability of applicants, borrowers, or lenders to participate in the FSA guaranteed loan program, and would not increase the costs of compliance with the program for entities of any size. All applicants or borrowers affected by this rule are small entities. Many lenders are considered small entities, using the SBA size standard of less $175 million in assets. However, changes in this rule will be applied to all affected entities equally, without regard to their size. No comments were received on the proposed rule regarding significant impact on a substantial number of small entities. Our analysis, which is explained in more detail in the cost benefit analysis, shows that less than 0.3 percent of guaranteed loans made by small banks in 2009 and 2010 had interest rates above those specified in this rule, so this rule will not

have a significant effect on small lenders. By setting specific maximum rates, this rule will reduce compliance complexity for entities of all sizes.

Environmental Evaluation

The environmental impacts of this rule have been considered in a manner consistent with the provisions of the National Environmental Policy Act (NEPA, 42 U.S.C. 4321-4347), the regulations of the Council on Environmental Quality (40 CFR parts 1500-1508), and the FSA regulations for compliance with NEPA (7 CFR parts 799 and 1940, subpart G). FSA concluded that this rule will not have a significant impact on the quality of the human environment either individually or cumulatively and therefore categorically excluded and not subject to environmental assessments or environmental impact statements in accordance with 7 CFR 1940.310(e)(3).

Executive Order 12372

Executive Order 12372, "Intergovernmental Review of Federal Programs," requires consultation with State and local officials. The objectives of the Executive Order are to foster an intergovernmental partnership and a strengthened Federalism, by relying on State and local processes for State and local government coordination and review of proposed Federal Financial assistance and direct Federal development. This rule neither provides Federal financial assistance nor direct Federal development; it does not provide either grants or cooperative agreements. Therefore this program is not subject to Executive Order 12372.

Executive Order 12988

This rule has been reviewed in accordance with Executive Order 12988, "Civil Justice Reform." This rule would not preempt State and or local laws, and regulations, or policies unless they present an irreconcilable conflict with this rule. Before any judicial action may be brought regarding the provisions of this rule, the administrative appeal provisions of 7 CFR parts 11 and 780 must be exhausted.

Executive Order 13132

This rule has been reviewed under Executive Order 13132, "Federalism." The policies contained in this rule do not have any substantial direct effect on States, the relationship between the Federal government and the States, or the distribution of power and responsibilities among the various levels of government. Nor does this interim rule impose substantial direct compliance costs on State and local governments. Therefore, consultation with the States is not required.

Executive Order 13175

This rule has been reviewed for compliance with Executive Order 13175, "Consultation and Coordination with Indian Tribal Governments." The USDA Office of Tribal Relations has concluded that the policies contained in this rule do not have Tribal implications that preempt Tribal law. FSA continues to consult with Tribal officials to have a meaningful consultation and collaboration on the development and strengthening of FSA regulations.

Unfunded Mandates Reform Act of 1995

Title II of the Unfunded Mandate Reform Act of 1995 (UMRA, Pub. L. 104-4) requires Federal agencies to assess the effects of their regulatory actions on State, local, or Tribal governments or the private sector. 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 of $100 million or more in any 1 year for State, local, or Tribal governments, in the aggregate, or to the private sector. UMRA generally requires agencies to consider alternatives and adopt the more cost effective or least burdensome alternative that achieves the objectives of the rule. This rule contains no Federal mandates as defined by Title II of UMRA for State, local, or Tribal governments or for the private sector. Therefore, this rule is not subject to the requirements of sections 202 and 205 of UMRA.

Federal Assistance Programs

The title and number of the Federal assistance programs, as found in the Catalog of Federal Domestic Assistance, to which this rule applies are:

10.406-Farm Operating Loans

10.407-Farm Ownership Loans

Paperwork Reduction Act of 1995

The provisions in this interim rule require no revisions to the information collection requirements that were previously approved by OMB under control number 0560-0155.

E-Government Act Compliance

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

List of Subjects

7 CFR Part 761

Accounting, Loan programs-agriculture, Rural areas.

7 CFR Part 762

Agriculture, Credit, Loan programs – agriculture, Reporting and recordkeeping requirements.

For the reasons set out in the preamble, this rule amends 7 CFR parts 761 and 762 as follows:

PART 761—GENERAL PROGRAM ADMINISTRATION

1. The authority citation for part 761 continues to read as follows:

Authority: 5 U.S.C. 301 and 7 U.S.C. 1989.

2. Amend § 761.2 as follows:

a. In paragraph (a), add, in alphabetical order, the abbreviation “LIBOR” to read as follows, and

b. In paragraph (b), remove the definition of “average agricultural loan customer”.

§ 761.2 Abbreviations and definitions.

* * * * *

(a) * * *

LIBOR London Interbank Offered Rate.

* * * * *

PART 762—GUARANTEED FARM LOANS

3. The authority citation for part 762 continues to read as follows:

Authority: 5 U.S.C. 301, 7 U.S.C. 1989.

4. Amend § 762.124 as follows:

a. Revise paragraphs (a)(2) and (a)(3) to read as set forth below,

b. Redesignate paragraphs (a)(4) and (a)(5) as (a)(5) and (a)(6), and

c. Add new paragraph (a)(4) to read as set forth below:

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

(a) * * *

(2) If a variable rate is used, it must be tied to an index or rate specifically agreed to between the lender and borrower in the loan instruments and the rate adjustments must be in accordance with normal practices of the lender for unguaranteed loans. Upon request, the lender must provide the Agency with copies of its written rate adjustment practices.

(3) At the time of loan closing or loan restructuring, the interest rate on both the guaranteed portion and the unguaranteed portion of a fixed or variable rate OL or FO loan may not exceed the following, as applicable:

(i) For lenders using risk-based pricing practices, the risk tier at least one tier lower (representing lower risk) than that borrower would receive without a guarantee. The lender must provide the Agency with copies of its written pricing practices, upon request.

(ii) For lenders not using risk-based pricing practices, for variable rate loans or fixed rate loans with rates fixed for less than five years, 650 basis points (6.5 percentage points) above the 3-month LIBOR.

(iii) For lenders not using risk-based pricing practices, for loans with rates fixed for five or more years, 550 basis points (5.5 percentage points) above the 5-year Treasury note rate.

(4) In the event the 3-month LIBOR is below 2 percent, the maximum rates specified in paragraph (a)(3) of this section do not apply. In that case, at the time of loan closing or loan restructuring, the interest rate on both the guaranteed portion and the unguaranteed portion of an OL or FO loan may not exceed 750 basis points above the 3-month LIBOR for variable rate loans and 650 basis points above the 5-year Treasury rate for fixed rate loans.

* * * * *

5. Amend § 762.150 by revising paragraph (g) to read as follows:

§ 762.150 Interest assistance program.

* * * * *

(g) Rate of interest. The lender interest rate will be set according to § 762.124(a).

* * * * *

Signed on February 12, 2013.

Juan M. Garcia,
Administrator,
Farm Service Agency.

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