

Proposed Rules

Federal Register

Vol. 65, No. 144

Wednesday, July 26, 2000

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

FARM CREDIT ADMINISTRATION

12 CFR Parts 614 and 619

RIN 3052-AB93

Loan Policies and Operations; Definitions; Loan Purchases and Sales

AGENCY: Farm Credit Administration (FCA).

ACTION: Proposed rule.

SUMMARY: We propose revisions to our regulations on loan participations to allow Farm Credit System (System or FCS) institutions greater flexibility to buy loan participations from non-System lenders under certain conditions. We propose to remove the existing 10-percent retention requirement when loan servicing remains with a non-System seller. We also propose removing two restrictive definitions of "loan participation" in order to enable System institutions to use their full statutory authority for loan participations. Also, we are proposing technical and clarifying changes related to System institutions' participation authorities.

DATES: You may send us comments by September 25, 2000.

ADDRESSES: Send us your comments by electronic mail to "reg-comm@fca.gov" or through the Pending Regulations section of our Web site at "www.fca.gov." You may also send written comments to Patricia W. DiMuzio, Director, Regulation and Policy Division, Office of Policy and Analysis, Farm Credit Administration, 1501 Farm Credit Drive, McLean, Virginia 22102-5090, or by facsimile transmission to (703) 734-5784. You may review copies of all comments we receive in the Office of Policy and Analysis, Farm Credit Administration.

FOR FURTHER INFORMATION CONTACT: Dennis K. Carpenter, Senior Policy Analyst, Office of Policy and Analysis, Farm Credit Administration, McLean, VA 22102-5090, (703) 883-4498, TDD (703) 883-4444,

or

James M. Morris, Senior Counsel, Office of General Counsel, Farm Credit Administration, McLean, VA 22102-5090, (703) 883-4020, TDD (703) 883-4444.

SUPPLEMENTARY INFORMATION:

I. Objective

The objective of this proposed rule is to increase the availability and efficiency of providing agricultural credit by providing greater flexibility for System institutions to engage in loan participations with other System institutions and non-System lenders. We expect that the proposed rule will promote more cooperative alliances and business ventures with commercial banks and other lenders.

This proposed rule is part of our efforts to carry out the Board's Philosophy Statement of July 14, 1998. Added regulatory flexibility should increase the efficient flow of funds to agriculture and rural America while helping ensure the continued availability of adequate and competitive agricultural credit. The proposed changes should also contribute to diversification of the portfolios of individual System institutions and non-System lenders, enabling them to better withstand stress conditions in agriculture.

II. Summary

The proposed rule would enable FCS institutions to use existing statutory authorities to support rural America through loan participation agreements with System and non-System lenders. The Farm Credit Act of 1971, as amended (Act) does not define the terms "participate" or "participation," other than in a special definition contained in section 3.1(11)(B)(iv) of the Act. We have broad authority to define terms used in the Act, and used our authority to provide a general regulatory definition of the term "loan participation" in present §§ 614.4325(a)(4) and 619.9195. However, the two regulatory definitions contained in §§ 614.4325(a)(4) and 619.9195 are more restrictive than the Act requires. The proposed rule would remove these restrictive definitions and enable System institutions to use their full statutory authority for loan participations with System and non-System lenders.

Other Federal bank regulators have, over the past several years, effectively defined loan participations to include 100-percent interests in loans. In addition, the Board of Governors of the Federal Reserve System, the Federal Deposit Insurance Corporation, the Office of the Comptroller of the Currency (OCC), and the Office of Thrift Supervision adopted an interagency statement providing guidance for 100-percent participations.¹ We propose removing our restrictive definitions to ensure that System institutions have the flexibility to interpret their loan participation authorities in the context of current banking practices. Therefore, we propose removing the existing regulatory definitions of "loan participation" contained in parts 614 and 619. We do not propose any change in the regulatory definition of "participate" and "participation" in § 613.3300(a), which reflects the definition contained in section 3.1(11)(B)(iv) of the Act, pertaining to the "similar entity" participation authorities.

In addition, we propose removing a 10-percent retention requirement that applies to System institutions buying participations from non-FCS institutions when the seller keeps the servicing rights of the loans. Finally, we propose clarifying the authorities for participation agreements between the Federal Agricultural Mortgage Corporation (Farmer Mac) and other FCS institutions or other lenders.

III. Revised Definitions of Participations

The Act does not provide a specific definition of a loan participation other than that contained in section 3.1(11)(B)(iv), concerning "similar entity" participations. Nevertheless, we previously provided more narrow regulatory definitions than required by the statute.

Our prior view was that a loan participation had to be a "fractional" undivided interest, something less than 100 percent.² On review of the statutory provisions on participations, we have concluded that the Act does not require this result. Section 1.5 of the Act

¹ "Interagency Statement on Sales of 10% Loan Participations" (April 10, 1997).

² We expressed this position in the preamble of the proposed Lending Authorities regulations of January 1991 (56 FR 2452, Jan. 23, 1991).

provides that Farm Credit Banks, "subject to regulation by the Farm Credit Administration, shall have power to . . . make, participate in, and discount loans" and may "participate with" other financial institutions in loans authorized under the Act. There are no limitations on the percentage of a loan in which a bank may participate. Similarly, sections 2.2 and 3.1 of the Act provide, respectively, that a production credit association "may make and participate in loans" and a bank for cooperatives may "participate in loans," subject to regulation by the FCA. Nowhere does the Act provide that a participation interest must be less than 100 percent.

Therefore, we are proposing to remove the regulatory definitions of loan participation in §§ 614.4325(a)(4) and 619.9195 to provide more flexibility to System institutions to make better use of existing statutory participation authorities. With this proposed rule we recognize the banking industry's understanding of loan participations as including all or some portion of a loan.

In 1984 the OCC issued a banking circular³ that provides that loan participations can include 100 percent of a loan. The OCC issued its banking circular to address safety and soundness concerns associated with loan purchases and participations. In the circular, the OCC described a loan participation as an arrangement in which a bank makes a loan to a borrower and then sells all or a portion of that loan to a purchasing bank. The circular distinguished a participation from a multi-bank loan transaction (syndicated loan).

The other Federal banking regulators issued an interagency statement on sales of 100-percent participations on April 10, 1997. The interagency statement discussed the features of 100-percent loan participations in light of a 1992 court decision⁴ that concluded that such participations did not involve the sale of securities under federal securities laws. The interagency statement also identified and discussed related safety and soundness concerns such as heightened legal, reputation, and compliance risks.

The OCC's banking circular contained loan participation guidelines addressing safety and soundness concerns. We have adopted similar guidelines, including the requirement that a buying participant exercise an independent credit judgment as part of our general

regulatory guidance for loan purchases and participations.

IV. Proposal Removes 10-Percent Retention Requirement

Section 614.4330(b) generally requires that any non-System lender that sells a loan participation to a System institution but continues to service the loan must retain at least 10 percent of the principal amount of the loan, or the seller's legal lending limit, whichever is less. We imposed this regulatory requirement to ensure the non-System seller and servicer would maintain appropriate controls for loans sold to System participants.

Because of changes in the financial markets, the System's growing experience with loan participations, and to enable FCS institutions to effectively use their existing statutory participation authorities, we now propose removing this retention requirement. This change will facilitate the use of 100-percent participations and allow the participation agreement to provide for loan servicing. However, compensating management controls will be needed to mitigate possible increased risk the added flexibility offers.

V. Characteristics of Typical Participations and Loan Purchases

A. Participations and Loan Purchases

Participations are commonly used when a lender makes a loan and then wishes to sell all of or a portion of the loan. In a participation, the originating lender typically sets up the lending relationship with the borrower and obtains the promissory note, loan agreement and supporting security documents in its name. The participating lender receives an interest in the loan and its collateral through a loan participation agreement and participation certificate.

In contrast, in a typical loan purchase, the buyer, through the purchase agreement, is assigned all rights included in the legal documents, security instruments, and rights to collateral. The buyer assumes the legal lender relationship with the borrower and arranges loan repayment, servicing, and as necessary collection, either directly with the borrower or contractually through an agent.

In typical loan participations all documentation for the loan is between the borrower and the originating lender, and the originating lender has the sole contact with the borrower. The borrower and participant have no direct relationship and there is no contract between the two parties. Therefore, the participant normally must rely on the

seller to enforce the terms of the documents between the originating lender and the borrower.

B. Advantages of Participations

Some of the principal advantages of participations are:

- Lending limit relief for the seller,
- Increased liquidity for the seller,
- Reduced concentration risk for both the buyer and seller through greater portfolio diversification,
- Increased fee income opportunities,
- Access to external credit expertise and new and diverse markets,
- Improved capital adequacy management for both the buyer and seller, and
- Better use of the buyer's excess funds.

C. Controlling Risk of Participations

There are risk control issues that can arise with loan participations. Some of these are typical of any credit arrangement. However, expanding the definition of a loan participation to include 100-percent participations can increase certain types of risks if not controlled and managed appropriately.

Therefore, we believe that System institutions should take extra care in developing the policies and procedures for their participation programs if they intend to buy 100-percent participations. An institution's policies and procedures and participation agreements should, at a minimum, address the following risks:

1. *Credit risk*—The participant depends on the originating lender to obtain, develop, and evaluate the relevant information about the borrower and the structure of the credit.

2. *Legal risk*—The originating lender typically prepares the documentation for the loan and perfects any security interests. The participant generally has a share of the rights of the originating lender. If deficiencies exist, the participant's rights may be limited.

3. *Administrative risk*—Typically, the participant must rely on the originating lender to (a) service, monitor, and control the credit relationship with the borrower, (b) provide information about the borrower, and (c) remit payments received from the borrower. However, all of the aforementioned administrative actions must be addressed in the participation agreement as well as the parties' duties and responsibilities.

A participant's administrative risk increases when the originating lender has no direct financial interest in the loan. The proposed removal of the 10-percent retention requirement increases this risk. The participation agreement should specifically address whether the

³ OCC-BC-181 "Purchases of Loans in Whole or in Part Participations" (August 2, 1984).

⁴ *Banco Espanol De Credito v. Security Pacific National Bank*, 973 F.2d 51 (2nd Cir. 1992).

seller has the ability, and under what circumstances, to transfer or sell the note or agreement to a third party without concurrence by the participant.

D. Managing Portfolio Risk

Our current regulations require each System institution involved in loan participation activities to develop and implement policies and procedures for such programs, including establishing appropriate portfolio limits to control portfolio risk.

While participations offer a number of advantages to an institution's portfolio (especially as risk diversification tools) they also carry additional risks not common to a normal borrower/lender relationship. We believe policy direction from a System institution's board of directors becomes even more important with these proposed changes. Portfolio limitations should be reviewed by the institution's board to ensure loan participations are appropriately integrated into the institution's overall business plan and risk management strategies.

VI. Farmer Mac Related Participation Authorities

In response to a question raised by Farmer Mac,⁵ we propose a change in the authorities contained in part 614, subpart A, of the regulations. The Act provides that banks and associations can enter into participation arrangements with other System institutions, which by definition includes Farmer Mac. However, our present regulations do not reflect this fact. Farmer Mac was given authority to buy, sell, hold, or assign loans after the present regulations were written. Therefore, we propose to revise the authority regulations in part 614, subpart A, to clarify the loan participation authorities of System banks and associations and Farmer Mac.

VII. Technical and Conforming Changes

We are also proposing certain technical and conforming changes to the regulations.

List of Subjects

12 CFR Part 614

Agriculture, Banks, Banking, Flood insurance, Foreign trade, Reporting and recordkeeping requirements, Rural areas.

12 CFR Part 619

Agriculture, Banks, Banking, Rural areas.

For the reasons stated in the preamble, we propose to amend parts 614 and 619 of chapter VI, title 12 of the Code of Federal Regulations 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 A—Lending Authorities

2. Amend § 614.4000 as follows:
a. Remove the word “and” at the end of paragraph (d)(1);
b. Remove the “.” and add “; and” at the end of paragraph (d)(2); and
c. Add paragraph (d)(3) to read as follows:

§ 614.4000 Farm Credit Banks.

(d)(3) The Federal Agricultural Mortgage Corporation to the extent provided in § 614.4055.

3. Amend § 614.4010 as follows:
a. Remove the word “and” at the end of paragraph (e)(1);
b. Remove the “.” and add “; and” at the end of paragraph (e)(2); and
c. Add paragraph (e)(3) to read as follows:

§ 614.4010 Agricultural credit banks.

(e)(3) The Federal Agricultural Mortgage Corporation to the extent provided in § 614.4055.

4. Amend § 614.4020 as follows:
a. Remove the “.” and add “; and” at the end of paragraph (b)(2); and
b. Add paragraph (b)(3) to read as follows:

§ 614.4020 Banks for cooperatives.

(b)(3) The Federal Agricultural Mortgage Corporation to the extent provided in § 614.4055.

5. Amend § 614.4030 as follows:

a. Remove the word “and” at the end of paragraph (b)(1);
b. Remove the “.” and add “; and” at the end of paragraph (b)(2); and
c. Add paragraph (b)(3) to read as follows:

§ 614.4030 Federal land credit associations.

* * * * *

(b)(3) The Federal Agricultural Mortgage Corporation to the extent provided in § 614.4055.

* * * * *

6. Amend § 614.4040 as follows:
a. Remove the word “and” at the end of paragraph (b)(1);
b. Remove the “.” and add “; and” at the end of paragraph (b)(2); and
c. Add paragraph (b)(3) to read as follows:

§ 614.4040 Production credit associations.

* * * * *

(b)(3) The Federal Agricultural Mortgage Corporation to the extent provided in § 614.4055.

* * * * *

7. Amend § 614.4050 as follows:
a. Remove the word “and” at the end of paragraph (c)(1);
b. Remove the “.” and add “; and” at the end of paragraph (c)(2); and
c. Add paragraph (c)(3) to read as follows:

§ 614.4050 Agricultural credit associations.

* * * * *

(c)(3) The Federal Agricultural Mortgage Corporation to the extent provided in § 614.4055.

* * * * *

8. Add a new § 614.4055 to read as follows:

§ 614.4055 Federal Agricultural Mortgage Corporation loan participations.

Subject to the requirements of subpart H of this part 614:

(a) Any Farm Credit System bank or direct lender association may buy from, and sell to, the Federal Agricultural Mortgage Corporation, participation interests in “qualified loans.”

(b) The Federal Agricultural Mortgage Corporation may buy from, and sell to, any Farm Credit System bank or direct lender association, or lender that is not a Farm Credit System institution, participation interests in “qualified loans.”

(c) For purposes of this section, “qualified loans” means qualified loans as defined in section 8.0(9) of the Act.

Subpart H—Loan Purchases and Sales

9. Amend § 614.4325 by:
a. Removing paragraph (a)(4);

⁵ Farmer Mac, in a letter dated October 26, 1999, requested that we modify our regulations to recognize Farmer Mac authority to sell loan participations to System Institutions.

b. Redesignating paragraphs (a)(5), (a)(6), and (a)(7) as paragraphs (a)(4), (a)(5), and (a)(6), respectively; and revising newly designated paragraph (a)(4) to read as follows:

§ 614.4325 Purchase and sale of interests in loans.

* * * * *

(a)(4) *Participating institution* means an institution that purchases a participation interest in a loan originated by another lender.

* * * * *

§ 614.4330 [Amended]

10. Amend § 614.4330 as follows:

a. Remove the words “an undivided” and add in their place the words “a participation” in paragraph (a)(9); and

b. Remove paragraph (b) and redesignate existing paragraph (c) as paragraph (b).

Subpart J—Lending and Leasing Limits

§ 614.4358 [Amended]

11. Amend § 614.4358 as follows:

a. Remove paragraph (b)(4)(i); and
b. Redesignate paragraphs (b)(4)(ii) and (b)(4)(iii) as paragraphs (b)(4)(i) and (b)(4)(ii), respectively.

PART 619—DEFINITIONS

12. The authority citation for part 619 continues to read as follows:

Authority: Secs. 1.7, 2.4, 4.9, 5.9, 5.12, 5.17, 5.18, 7.0, 7.6, 7.7, 7.8 of the Farm Credit Act (12 U.S.C. 2015, 2075, 2160, 2243, 2246, 2252, 2253, 2279a, 2279b, 2279b–1, 2279b–2).

§ 619.9195 [Removed and Reserved]

13. Remove and reserve § 619.9195.

Dated: July 20, 2000.

Kelly Mikel Williams,

Secretary, Farm Credit Administration Board.
[FR Doc. 00–18873 Filed 7–25–00; 8:45 am]

BILLING CODE 6705–01–P

DEPARTMENT OF TRANSPORTATION

Federal Aviation Administration

14 CFR Part 39

[Docket No. 2000–NM–133–AD]

RIN 2120–AA64

Airworthiness Directives; Empresa Brasileira de Aeronautica S.A. (EMBRAER) Model EMB–120 Series Airplanes

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 EMBRAER Model EMB–120 series airplanes. This proposal would require a one-time inspection to detect wear of the hydraulic pump hoses, and corrective action, if necessary. This proposal would also require relocation of the clip that secures the left forward hold-open rod of both nacelles. This action is necessary to prevent chafing and consequent rupture of the hydraulic line and loss of hydraulic pressure, which could result in reduced controllability of the airplane. This action is intended to address the identified unsafe condition.

DATES: Comments must be received by August 25, 2000.

ADDRESSES: Submit comments in triplicate to the Federal Aviation Administration (FAA), Transport Airplane Directorate, ANM–114, Attention: Rules Docket No. 2000–NM–133–AD, 1601 Lind Avenue, SW., Renton, Washington 98055–4056. Comments may be inspected at this location between 9:00 a.m. and 3:00 p.m., Monday through Friday, except Federal holidays. Comments may also be sent via the Internet using the following address: 9-anm-nprmcomment@faa.gov. Comments sent via the Internet must contain “Docket No. 2000–NM–133–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 for Windows or ASCII text.

The service information referenced in the proposed rule may be obtained from Empresa Brasileira de Aeronautica S.A. (EMBRAER), P.O. Box 343—CEP 12.225, Sao Jose dos Campos—SP, Brazil. This information may be examined at the FAA, Transport Airplane Directorate, 1601 Lind Avenue, SW., Renton, Washington; or at the FAA, Small Airplane Directorate, Atlanta Aircraft Certification Office, One Crown Center, 1895 Phoenix Boulevard, suite 450, Atlanta, Georgia.

FOR FURTHER INFORMATION CONTACT:

Robert Capezzuto, Aerospace Engineer, Systems and Flight Test Branch, ACE–116A, FAA, Small Airplane Directorate, Atlanta Aircraft Certification Office, One Crown Center, 1895 Phoenix Boulevard, suite 450, Atlanta, Georgia 30349; telephone (770) 703–6071; fax (770) 703–6097.

SUPPLEMENTARY INFORMATION:

Comments Invited

Interested persons are invited to participate in the making of the proposed rule by submitting such written data, views, or arguments as they may desire. Communications shall identify the Rules Docket number and be submitted in triplicate to the address specified above. All communications received on or before the closing date for comments, specified above, will be considered before taking action on the proposed rule. The proposals contained in this notice may be changed in light of the comments received.

Submit comments using the following format:

- Organize comments issue-by-issue. For example, discuss a request to change the compliance time and a request to change the service bulletin reference as two separate issues.
- For each issue, state what specific change to the proposed AD is being requested.
- Include justification (e.g., reasons or data) for each request.

Comments are specifically invited on the overall regulatory, economic, environmental, and energy aspects of the proposed rule. All comments submitted will be available, both before and after the closing date for comments, in the Rules Docket for examination by interested persons. A report summarizing each FAA-public contact concerned with the substance of this proposal will be filed in the Rules Docket.

Commenters wishing the FAA to acknowledge receipt of their comments submitted in response to this notice must submit a self-addressed, stamped postcard on which the following statement is made: “Comments to Docket Number 2000–NM–133–AD.” The postcard will be date stamped and returned to the commenter.

Availability of NPRMs

Any person may obtain a copy of this NPRM by submitting a request to the FAA, Transport Airplane Directorate, ANM–114, Attention: Rules Docket No. 2000–NM–133–AD, 1601 Lind Avenue, SW., Renton, Washington 98055–4056.

Discussion

The Departamento de Aviação Civil (DAC), which is the airworthiness authority for Brazil, notified the FAA that an unsafe condition may exist on certain EMBRAER Model EMB–120 series airplanes. The DAC advises that it has received a report of one case of rupture of an engine-driven pump hydraulic hose, possibly due to its friction against the clip that secures the