

DEPARTMENT OF AGRICULTURE**Rural Utilities Service****7 CFR Parts 1710, 1717 and 1718**

RIN 0572-AB06

Loan Policies and Security Documents for Electric Borrowers

AGENCY: Rural Utilities Service, USDA.

ACTION: Proposed rule.

SUMMARY: The Rural Utilities Service (RUS) hereby proposes to establish new policies and requirements for loan contracts ordinarily required for loans made to electric distribution borrowers. The rule would update and clarify the framework for loan contract provisions, conform loan contract provisions with the new form of mortgage recently approved, and provide greater flexibility in addressing the financial needs of individual borrowers and the credit risks involved with individual lending situations. Conforming amendments to RUS lien accommodation requirements and changes to RUS operational controls are also proposed.

DATES: Written comments must be received by RUS or carry a postmark or equivalent by September 18, 1995.

ADDRESSES: Written comments should be addressed to Mr. F. Lamont Heppe, Jr., Deputy Director, Program Support Staff, U.S. Department of Agriculture, Rural Utilities Service, room 2234-S, Ag Box 1522, 14th Street and Independence Avenue, SW., Washington, DC 20250-1500. RUS requires a signed original and 3 copies of all comments (7 CFR 1700.30 (e)). Comments will be available for public inspection during regular business hours (7 CFR 1.27(b)).

FOR FURTHER INFORMATION CONTACT: Mr. Alex M. Cockey, Jr., Deputy Assistant Administrator—Electric, U.S. Department of Agriculture, Rural Utilities Service, room 4037-S, Ag Box 1560, 14th Street & Independence Avenue, SW., Washington, DC 20250-1500. Telephone: 202-720-9547.

SUPPLEMENTARY INFORMATION: This rule has been determined to be not significant for the purposes of Executive Order 12866, and therefore has not been reviewed by the Office of Management and Budget (OMB). The Administrator of RUS has determined that the Regulatory Flexibility Act (5 U.S.C. 601 et seq.) does not apply to this rule. The Administrator of RUS has determined that this rule will not significantly affect the quality of the human environment as defined by the National Environmental Policy Act of 1969 (42 U.S.C. 4321 et seq.). Therefore, this

action does not require an environmental impact statement or assessment. This rule is excluded from the scope of Executive Order 12372, Intergovernmental Consultation, which may require consultation with State and local officials. A Notice of Final Rule titled Department Programs and Activities Excluded from Executive Order 12372 (50 FR 47034) exempts RUS electric loans and loan guarantees from coverage under this Order. This rule has been reviewed under Executive Order 12778, Civil Justice Reform. This rule: (1) Will not preempt any State or local laws, regulations, or policies, unless they present an irreconcilable conflict with this rule; (2) Will not have any retroactive effect; and (3) Will not require administrative proceedings before any parties may file suit challenging the provisions of this rule.

The program described by this rule is listed in the Catalog of Federal Domestic Assistance Programs under number 10.850 Rural Electrification Loans and Loan Guarantees. This catalog is available on a subscription basis from the Superintendent of Documents, the United States Government Printing Office, Washington, DC 20402-9325.

Information Collection and Recordkeeping Requirements

The existing recordkeeping and reporting burdens contained in this rule were approved by the Office of Management and Budget (OMB) pursuant to the Paperwork Reduction Act of 1980 (44 U.S.C. 3501 et seq.), under control numbers 0572-0032 and 0572-0103.

Send questions or comments regarding these burdens or any other aspect of these collections of information, including suggestions for reducing the burden, to the Office of Information and Regulatory Affairs, Office of Management and Budget, NEOB, Washington, DC 20503. Attention: Desk Officer for USDA.

Background

On September 29, 1994, at 59 FR 49594, the Rural Utilities Service (RUS) published a proposed rule, 7 CFR 1718 Loan Security Documents for Electric Borrowers, Subpart B Mortgage for Distribution Borrowers, which proposed the agency's policies and requirements for mortgages used to secure direct and guaranteed loans made to electric distribution borrowers. The final rule for such mortgages is published elsewhere in this issue of the **Federal Register**.

This proposed rule sets forth proposed amendments to RUS regulations to update the agency's

policies and requirements regarding loan contracts with distribution borrowers. These new policies and requirements are designed to complement the new distribution mortgage. The changes proposed today are in four different segments:

- A new Subpart C—Loan Contracts with Distribution Borrowers, to be added to 7 CFR part 1718. This proposed subpart sets forth agency policies and requirements regarding the scope, content, and usage of new loan contracts with distribution borrowers.

- A new Subpart M—Operational Controls, to be added to 7 CFR part 1717. This proposed new subpart outlines the main operational controls relating to new mortgages and loan contracts of distribution borrowers, and also modifies certain controls relating to existing mortgages and loan contracts of distribution and/or power supply borrowers.

- Proposed revisions to 7 CFR part 1717, Subpart R—Lien Accommodations and Subordinations for 100 Percent Private Financing. These revisions would adapt RUS policies and requirements regarding lien accommodations to the new loan contracts and mortgages.

- A limited number of proposed changes to 7 CFR part 1710 to conform those provisions to the new mortgages and loan contracts.

In addition to inviting written comments from the public on this proposed rule, REA stands ready to meet with interested individuals and organizations to discuss their comments and recommendations. Such meetings would be open to any interested person, and they would be "informal", as opposed to a formal hearing. Although any such meetings will not be transcribed, REA will include a summary of any such meeting in the file for this rulemaking. To facilitate scheduling, it would be better for individuals, especially the large number of borrowers affected by this proposed rule, to form one or more groups to represent their interests at such meetings.

7 CFR Part 1718, Subpart C—Loan Contracts With Distribution Borrowers

This new subpart would establish agency policies and requirements regarding the scope, content, and usage of new loan contracts with distribution borrowers. These policies are intended to complement those for new distribution mortgages, and to reflect changes in the electric industry and the RUS program over the past several years.

Distribution borrowers that obtain a loan or loan guarantee from RUS after the effective date of this rule would be required to execute a new loan contract and mortgage based on the policies and requirements established by the new rules. Distribution borrowers obtaining other financial assistance from RUS after the effective date of this rule may be required by RUS to execute a new mortgage and loan contract. If there are other co-mortgagees on the borrower's existing mortgage, which there are in most cases, the borrower would have to obtain the approval of these co-mortgagees before executing a new mortgage.

Distribution borrowers receiving a loan during the transition period between now and the date the new model loan contract is published in final form in the **Federal Register** may opt to execute the new model mortgage and the proposed model loan contract. Such borrowers will have the further option of executing the final form of the model loan contract after it is published in the **Federal Register**. Distribution borrowers receiving a loan during the period after publication of the final form of the new model loan contract but before its effective date may opt for the final forms of both the model loan contract and the model mortgage.

Other borrowers not obtaining a new loan from RUS could request that a new mortgage and loan contract be executed, for example, in connection with a lien accommodation request or if the borrower is trying to expand its access to future private financing. RUS will attempt to honor these requests, but may be constrained by time and staff limitations.

The policies and requirements proposed in new Subpart C are designed to provide flexibility in dealing with the different financial needs, credit risks and other circumstances of individual borrowers and individual lending situations. This is intended to enable RUS to respond more quickly and effectively to the special and changing needs of individual borrowers, while at the same time meeting the government's need for loan security under different lending circumstances.

Under this approach, RUS and borrowers would have the flexibility to negotiate different loan contract provisions depending on individual circumstances and needs. This would go beyond the current situation where special needs and requirements are dealt with almost exclusively in the "special provisions" section of a loan contract or contract amendment. It is anticipated that the provisions in the model loan contract will be suitable in

most cases. Since drafting and approving customized contract provisions would be more time consuming and could delay approval of a loan, RUS will consider such modifications only when they are needed to address individual needs or problems.

Proposed section 1718.103 sets forth the scope and content of loan contracts to be used with distribution borrowers in combination with new mortgages executed under 7 CFR Part 1718, Subpart B. The proposed section establishes the general requirements for loan contracts, in most cases leaving the specific language of individual provisions to be determined in the drafting of the loan contracts. An example of such a model loan contract is presented in Appendix A. This model represents one example of a loan contract drafted pursuant to this proposed new rule. Other loan contracts could vary substantially from this example in response to the financing needs of individual borrowers and the credit risks involved in those individual lending situations. It is anticipated that individual provisions of the model will be refined over time to reflect experience gained from use of the model and to respond to the rapidly changing electric industry.

Proposed § 1718.103, as reflected in the model contract in Appendix A, attempts to streamline, simplify and clarify loan contract provisions. A substantial number of restrictive covenants, complex provisions, and other outdated requirements contained in the present form of loan contract would be eliminated. Also, RUS is abandoning the practice of using the same loan contract with a series of amendments to cover all RUS loans throughout the lending relationship, which spans more than 50 years in many cases. Instead, RUS intends to use the approach followed by other lenders of using a new loan contract with each loan. This approach is intended to simplify administration for all parties and to guard against the use of outdated loan documentation.

Historically, RUS loan contracts have contained sweeping powers favoring the Administrator. In the absence of any explicit rulemaking authority in the Rural Electrification Act as originally enacted, these contracts together with their related mortgages lay the foundation for most RUS regulations. RUS has administered these loan documents through a variety of methods, including case-by-case determinations, letters from the Administrator to all borrowers or a

group of borrowers, and notice and comment rulemaking.

RUS intends to retain these flexible approaches to program administration, including the practice of establishing the rights and limitations of the lending relationship broadly in the loan documents and subsequently refining them in regulations. Thus many provisions of the proposed model contract are stated in very broad terms which can be fully understood only in the context of the agency's regulations.

For example, most proposed covenants or "operational controls" in the model contract are expressed in broad language, although in some cases the language is narrower and more focused than in existing loan contracts. Such language leaves room for unforeseen circumstances, which can be addressed more specifically through RUS regulations. In most cases RUS intends to cut back the reach of these provisions through its regulations, as it did recently in the publication of the final rule 7 CFR part 1726 on construction policies and procedures (at 60 FR 10151), as well as in the recent publication of proposed revisions to controls on borrowers' investments (at 60 FR 8981). Under today's proposed rule, several additional operational controls would be eliminated from loan contracts, and several others would be cut back, as described below.

Some may argue that the controls and approval rights contained in the RUS loan contract itself ought to be more limited and more narrowly focused than what is being proposed today. RUS recognizes that approach may appear desirable from an individual borrower's standpoint. However, from the standpoint of administering a program serving nearly 1,000 utility systems and responding to the diverse interests of this group, the Congress, the Executive Branch, and other interested parties, RUS believes that the proposed approach is administratively less costly, less time-consuming, more flexible, and better able to respond quickly to changing needs and circumstances.

Certain provisions that had been included in the proposed mortgage for distribution borrowers, but deleted in the final rule, are proposed for inclusion in the loan contract. These provisions include the rate covenant, limitations on retirements of capital credits and other distributions, certain tests for the issuance of debt that had been included in sections 2.01 and 2.02 of the proposed mortgage, and limitations on the issuance of unsecured debt. These changes are discussed in the final rule on the mortgage published elsewhere in this **Federal Register**.

7 CFR part 1717, Subpart M— Operational Controls

Proposed Subpart M of 7 CFR part 1717 serves several purposes. First, it outlines the main operational controls that would apply to distribution borrowers under the proposed new loan contracts. In many cases, such operational controls are further defined in other RUS regulations. Second, it establishes the circumstances under which RUS approval is granted or an exception to a requirement is established with respect to certain controls. Third, it extends these approvals and exceptions to existing loan contracts and mortgages of distribution borrowers and/or power supply borrowers.

Since proposed Subpart M would address only the main operational controls, failure to include an operational control under Subpart M would not invalidate operational controls contained in other RUS regulations. Also, the approvals and exceptions that would be granted by Subpart M would apply only to operational controls normally included in loan contracts and mortgages. They would not apply to special controls and requirements included in loan documents to deal with special circumstances of individual borrowers.

Proposed Subpart M is not intended to exhaust the treatment of operational controls. RUS is continuing to review this matter and will be proposing further changes. For example, proposed revisions to RUS policies and procedures regarding system design and architectural and engineering services are currently being drafted.

Extensions and additions. Under proposed § 1717.603, prior written approval by RUS would be required before a distribution borrower could extend or add to its electric system if the facilities will be financed by RUS (including reimbursements). If they won't be financed by RUS (wholly or partially), approval would not be required except for:

- Construction or procurement of generating facilities of any size.
- Acquisition of existing electric facilities or systems in service.
- Construction or procurement of electric facilities to serve a customer whose annual kWh purchases or maximum annual kW demand is projected to exceed 25 percent of the borrower's total kWh sales or maximum kW demand in the year immediately preceding the acquisition or start of construction.

Prior written approval from RUS would also be required before power

supply borrowers could extend or add to their electric systems if the facilities will be financed by RUS. Approval requirements when the facilities will not be financed by RUS are or will be set forth in other RUS regulations.

Long-range engineering plans and construction work plans. Proposed § 1717.604 would continue to require all borrowers to maintain up-to-date long-range engineering plans and construction work plans (CWP). However, these plans would not be subject to RUS approval if the borrower does not intend to seek RUS financing for the facilities and other purposes covered by the plans. If requested by RUS, borrowers would have to provide a copy of such plans for RUS review. Applications for RUS financing would continue to be required to be supported by a long-range engineering plan and CWP approved by RUS.

Design standards, plans and specifications, construction standards, and list of materials. Proposed § 1717.605 would continue to require all borrowers, regardless of the source of funding, to follow applicable RUS requirements regarding system design, plans and specifications, construction standards, and the use of RUS accepted materials.

Construction contracts, and engineering and architectural services contracts. Under proposed § 1717.606 borrowers would be encouraged to use RUS standard forms of contracts for construction, materials, equipment, engineering services, and architectural services regardless of the source of funding. They would be required to use the standard contract forms only if funding for the construction, procurement, or services is provided by RUS.

Contract bidding requirements. Proposed § 1717.607 would reiterate current policy that RUS requirements regarding bidding for construction, materials and equipment contracts apply only if the construction or procurement will be financed by RUS.

RUS approval of contracts. Proposed § 1717.608 would establish requirements and grant RUS approval with respect to certain contracts. This section is not complete. Further work needs to be done, and RUS will propose additional rules updating contract approval requirements when those decisions are made.

This proposed section would reiterate current policy in 7 CFR part 1726 that RUS approval of contracts for construction, materials, equipment, and architectural and engineering services would be required only if the

construction, procurement or services are financed by RUS.

RUS approval of contracts to sell electric power to retail customers would be required only if the contract is for longer than two years and the kWh sales or kW demand for any year covered by the contract exceeds 25 percent of the borrower's total kWh sales or maximum kW demand for the year immediately preceding execution of the contract.

RUS approval of power supply arrangements, including power supply contracts, interconnection agreements, interchange agreements, wheeling agreements, pooling agreements, and any other similar arrangements would be granted if they have a term of two years or less. Amendments to such arrangements would also be approved if the amendment would not extend the term of the arrangement for more than two years beyond the date of the amendment. The rule would also grant approval for any amendment to a schedule or exhibit contained in any power supply arrangement, which would have the mere effect of either altering a list of interconnection or delivery points or changing the value of a variable term (but not the formula itself) contained in a formula rate or charge.

RUS approval of contracts for the management and operation of a borrower's electric system or for the maintenance of the electric system would be required only if such contracts cover all or substantially all of the electric system.

RUS approval of general manager. Most existing mortgages or loan contracts give RUS the unconditioned right to approve a borrower's general manager and the manager's employment contract. Proposed § 1717.609 would grant RUS approval for all borrowers that are in compliance with all provisions of their loan documents and any other agreements with RUS. It is further proposed that new loan contracts generally will not give RUS unconditioned approval rights over general managers. Under new loan contracts, RUS would have the right to replace the manager or approve a new manager when a vacancy occurs only if the borrower is in default under its mortgage, loan contract, or other agreement with RUS. This should greatly reduce the times when RUS approval of a general manager is required.

RUS approval of compensation of the board of directors. Most existing mortgages or loan contracts require the borrower to obtain RUS approval of any compensation provided to the members of the borrower's board of directors.

Such approval requirement will not be included in new mortgages or in the proposed loan contract, and proposed § 1717.610 would waive this requirement for existing mortgages and loan contracts.

RUS approval of expenditures for legal, engineering, and supervisory services. Most existing mortgages or loan contracts require borrowers to obtain RUS approval before making expenditures for legal, engineering, and supervisory services, other than "routine" expenditures. Proposed § 1717.611 would grant RUS approval of expenditures for legal and supervisory services regardless of the source of funding, and for engineering services if they are not funded by RUS. Approval requirements for engineering services financed by RUS are set forth in other RUS regulations.

RUS approval of borrower's bank or other depository. Most existing mortgages or loan contracts give RUS the right to approve the bank or other depositories used by a borrower. Proposed § 1717.612 would grant RUS approval of the borrower's bank or other depositories provided that they are insured by the Federal Deposit Insurance Corporation or other Federal agency acceptable to RUS. Proposed new loan contracts would not grant RUS such authority, but would require that funds from loans made or guaranteed by RUS be deposited in a bank or other depository insured by the Federal Deposit Insurance Corporation or other Federal agency acceptable to RUS, unless prior written approval is obtained from RUS.

110 Percent Borrowers. It is recognized that the proposed changes in operational controls applicable to borrowers in general will, if adopted, require some changes in the exceptions to RUS controls applicable to borrowers with a net worth of at least 110 percent of the outstanding debt owed to RUS. The interim final rule on such exceptions was published in the **Federal Register** on January 28, 1994 at 59 FR 3982. After comments are received on the proposed rule published today, RUS will review those comments as well as those received on the interim final rule (7 CFR 1710.7, 7 CFR 1717.860, and 7 CFR 1717.904) and then publish both rules in final form.

7 CFR Part 1717, Subpart R—Lien Accommodations and Subordinations for 100 Percent Private Financing

Changes are proposed to 7 CFR part 1717, subpart R, to adapt RUS policies and requirements for lien accommodations and subordinations to the new distribution mortgage. Most of

these changes are conforming technical changes, a few are substantive in nature.

Section 1717.850 General

Under new mortgages for distribution borrowers, borrowers will be able to issue additional secured debt without the approval of RUS or the other mortgagees if the borrowers meet the criteria in section 2.01 of their mortgages. Also, if they meet the criteria in section 2.02 of their mortgages, borrowers will be able to issue secured debt to refinance existing secured debt without approval of the mortgagees.

If borrowers meet the criteria in section 2.01 or 2.02, debt issued under those sections will automatically be secured under the mortgage and will not require a lien accommodation from RUS or other mortgagees. Thus the lien accommodation regulation, 7 CFR 1717 subpart R, would not apply to such financing. This is true even if approval from RUS is required under the RUS loan contract due to criteria or restrictions included in the loan contract. While the borrower would be required to obtain prior RUS approval in such cases, a lien accommodation would not be required if the financing met the requirements of section 2.01 or 2.02 of the new mortgage.

Several technical amendments are proposed to 1717.850. Paragraph (a) would be revised to indicate, as discussed above, that Subpart R applies only to the issuance of secured debt that does not meet the criteria of section 2.01 or 2.02 of the new mortgage. Paragraph (b) would be revised to include the four community infrastructure purposes eligible under section 2.01 of the new mortgage as also being eligible for a lien accommodation under Subpart R.

Paragraph (f) would be substantially revised to eliminate the requirement that the borrower provide RUS with a written agreement that it will: comply with the National Electric Safety Code; use only RUS accepted materials where applicable; comply with RUS construction standards; follow a CWP approved by RUS; and provide an engineer's certification after completion of construction that the construction was done in compliance with RUS requirements. While this certification would no longer be required, the borrower would continue to be required to comply with RUS standards regarding facility and system planning and design, construction, procurement, and the use of materials accepted and listed by RUS. Elimination of the certification would reduce the administrative burden on borrowers.

A minor technical change would be made to paragraph (g)(1) to conform

with proposed changes to 7 CFR part 1710, subpart F, (discussed later) to the effect that construction work plans would not have to be approved by RUS unless the borrower intends to seek RUS financing for facilities or other purposes covered by the plan. Also, a technical change is proposed to paragraph (h)(2) to eliminate references to sections of the mortgage and loan contract with respect to prior approval or waiver of approval of certain borrower actions granted by paragraphs (g)(1) and (h)(1) of this section. Such references to the loan documents will be confusing as new mortgages and loan contracts are executed with some borrowers, while other borrowers are still operating under the old loan documents. Moreover, as RUS continues to codify more and more of its regulations relating to RUS approvals and controls, references to specific provisions of the loan documents relating to prior approval and waivers granted by such regulations will become less meaningful.

Finally, changes are proposed to paragraph (m) of this section to broaden the requirements and conditions under Subpart R that may be waived by the Administrator of RUS if it's in the financial interests of the government. Also, the meaning of the financial interests of the government would be clarified.

Section 1717.852 Financing Purposes

With two exceptions, all of the proposed changes to § 1717.852 are basically technical changes to conform the section with the new mortgage. A new paragraph (a)(3) would be added to add to eligible lien accommodation purposes the four community infrastructure purposes eligible for financing without mortgagee approval under section 2.01 of the new mortgage. The four purposes are water and waste disposal systems, solid waste disposal systems, telecommunication and other electronic communication systems, and natural gas distribution systems. Other infrastructure and other rural development projects would continue to be eligible for a lien accommodation if the Administrator determines its in the government's financial interests. They would also continue to be eligible for a lien subordination under the terms of § 1717.858, to which no changes are being proposed.

Paragraph (a)(1) would be amended by adding steam power to electric power as an eligible purpose for lien accommodations. RUS has received lien accommodation requests from borrowers where the financing was needed to supply both electric power and steam power to the customer. The

requests have been approved after a special finding by RUS that the accommodation of the government's lien was in the government's financial interest. By adding steam power as an eligible purpose, the special finding would no longer be required, which should expedite the review of such applications.

Existing paragraph (a)(4) would be redesignated (a)(5) and the limit on transaction costs eligible for lien accommodation would be raised from 3.5 percent of loan proceeds to 5 percent. No other changes are proposed to paragraph (a) other than renumbering of the subparagraphs. Minor technical changes would be made to the wording in paragraph (b) to reflect the addition of the four community infrastructure purposes to the purposes generically eligible for a lien accommodation, and to broaden the scope of purposes eligible in connection with cogeneration projects. Also, paragraph (b)(2) would be removed since it would be redundant with the proposed expanded scope of § 1717.850(m).

Section 1717.854 Advance Approval.

Minor technical amendments are proposed to paragraphs (a) and (b) to reflect the proposed addition of the four community infrastructure purposes to the purposes generically eligible for a lien accommodation, and thus eligible for advance approval.

Changes are proposed to paragraph (c) to conform the financial criteria for eligibility for advance approval of a lien accommodation to those contained in section 2.01 of the new mortgage. Thus the existing two-part interest coverage and equity tests in paragraph (c) would be replaced with the interest coverage, equity, and net utility plant tests contained in section 2.01 of the new mortgage. With this change borrowers under the "old" existing mortgage would be subject to the same basic financial tests in qualifying for advance approval of a lien accommodation as borrowers under section 2.01 of the new mortgage in issuing additional secured debt without mortgagee approval. The latter borrowers would not require a lien accommodation, and thus 1717.854 would no longer be relevant for them.

The proposed new tests in paragraph (c) are a Times Interest Earned Ratio (TIER) of at least 1.5 and Debt Service Coverage (DSC) of at least 1.25 in each of the past two years, equity of at least 27 percent after debt issuance, and a ratio of net utility plant to long-term debt of at least 1.0 after debt issuance. In addition, the existing limitation of variable rate debt to 15 percent of all outstanding debt would be eliminated

by removing paragraph (c)(7). This limitation on variable rate debt would also be eliminated from advance approvals of lien accommodations for refinancing loans by removing paragraph (a)(5) from 1717.857.

A few minor technical changes are proposed to § 1717.855 and 1717.856, primarily to conform them with the proposed addition of the four community infrastructure purposes to the purposes generically eligible for a lien accommodation, and to eliminate the certification from borrowers that they will comply with RUS construction standards and CWP requirements.

Finally, no changes are proposed to 7 CFR part 1717, Subpart S, regarding lien accommodations for concurrent supplemental loans. Such loans must continue to meet the same requirements as insured loans made by RUS.

7 CFR Part 1710—General and Pre-Loan Policies and Procedures Common to Insured and Guaranteed Electric Loans

Section 1710.103 Area coverage. A technical change is proposed to delete the statement which could be interpreted that the loan contract must include the exact language of § 1710.103 with respect to area coverage requirements. That never was the intent. The proposed technical change is consistent with the general approach that the loan contract should provide the general authority for a requirement or control, while RUS regulations should provide the specific details and often narrow the focus of the general authority provided in the loan contract.

Section 1710.114 TIER, DSC, OTIER and ODSC requirements. It is proposed that the rate covenant be shifted from the mortgage to the loan contract, and that an Operating Times Interest Earned Ratio (OTIER) and an Operating Debt Service Coverage (ODSC), both set at a minimum of 1.1, be added to the existing TIER and DSC requirements for distribution borrowers. The reasons for these changes are discussed in the background section of the final rule on the distribution mortgage published elsewhere in this issue of the **Federal Register**.

Long-range engineering plans and construction work plans. Under section 1710.250, all borrowers would continue to be required to maintain up-to-date long-range engineering plans and construction work plans, but the plans would not have to be approved by RUS unless the borrower intends to seek RUS financing. Applications for RUS financing would continue to have to be supported by an RUS-approved long-range engineering plan and CWP. RUS

approval of these plans would be with respect to only those facilities to be financed by RUS, and as to whether the plans provide an acceptable basis, from a planning and engineering standpoint, for approving the RUS financing.

A new paragraph (k) would be added to this section authorizing RUS to waive certain requirements with respect to long-range engineering plans and construction work plans if RUS determines that the requirements impose a substantial burden on the borrower and that waiving the requirements will not significantly affect the accomplishment of the objectives of the regulation. For example, RUS could waive certain requirements relating to load growth if the borrower's growth is stagnant or declining.

List of Subjects

7 CFR Part 1710

Electric power, Electric utilities, Loan programs—energy, Rural areas.

7 CFR Part 1717

Administrative practice and procedure, Electric power, Electric utilities, Intergovernmental relations, Investments, Lien accommodation, Lien subordination, Loan programs—energy, Operational controls, Reporting and recordkeeping requirements, Rural areas.

7 CFR Part 1718

Administrative practice and procedure, Electric power, Electric utilities, Loan programs—energy, Loan security documents, Reporting and recordkeeping requirements, Rural areas.

For the reasons explained in the preamble and under the authority of 7 U.S.C. 901 *et seq.*, RUS proposes to amend 7 CFR Chapter XVII as follows:

PART 1710—GENERAL AND PRE-LOAN POLICIES AND PROCEDURES COMMON TO INSURED AND GUARANTEED ELECTRIC LOANS

1. The authority citation for part 1710 is revised to read as follows:

Authority: 7 U.S.C. 901–950b; Public Law 99–591, 100 Stat. 3341–16; Public Law 103–354, 108 Stat. 3178 (7 U.S.C. 6941 *et seq.*).

2. Section 1710.2 is amended in paragraph (a) by adding the following definitions in alphabetical order to read as follows:

§ 1710.2 Definitions and rules of construction.

(a) *Definitions.* * * *

* * * * *

Electric system means all of the borrower's interests in all electric production, transmission, distribution, conservation, load management, general plant and other related facilities, equipment or property and in any mine, well, pipeline, plant, structure or other facility for the development, production, manufacture, storage, fabrication or processing of fossil, nuclear, or other fuel or in any facility or rights with respect to the supply of water, in each case for use, in whole or in major part, in any of the borrower's generating plants, including any interest or participation of the borrower in any such facilities or any rights to the output or capacity thereof, together with all lands, easements, rights-of-way, other works, property, structures, contract rights and other tangible and intangible assets of the borrower in each case used or useful in such electric system.

* * * * *

ODSC means Operating Debt Service Coverage of the electric system calculated as:

$$\text{ODSC} = \frac{A+B+C}{D}$$

where:

All amounts are for the same one-year period and are based on the RUS system of accounts. References to line numbers in the RUS Form 7 refer to the June 1994 version of the form, and will apply to corresponding information in future versions of the form;

A=Depreciation and Amortization Expense of the electric system, which usually equals Part A, Line 12 of RUS Form 7;

B=Interest on Long-term Debt of the electric system, which usually equals Part A, Line 15 of RUS Form 7, except that Interest on Long-term debt shall be increased by 1/3 of the amount, if any, by which the rentals of Restricted Property of the electric system (Part M, Line 3 of RUS Form 7) exceeds 2 percent of Total Margins and Equities (Part C, Line 36 of RUS Form 7);

C=Patronage Capital & Operating Margins of the electric system, which usually equals Part A, Line 20 of RUS Form 7; and

D=Debt Service Billed (RUS+other) which equals all interest and principal billed or billable during the calendar year for long-term debt of the electric system plus 1/3 of the amount, if any, by which the rentals of Restricted Property of the electric system (Part M, Line 3 of RUS Form 7) exceeds 2 percent of Total Margins and Equities (Part C, Line 36 of RUS Form 7).

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OTIER means Operating Times Interest Earned Ratio of the electric system calculated as:

$$\text{OTIER} = \frac{A+B}{A}$$

where:

All amounts are for the same one-year period and are based on the RUS system of accounts. References to line numbers in the RUS Form 7 refer to the June 1994 version of the form, and will apply to corresponding information in future versions of the form;

A=Interest on Long-term Debt of the electric system, which usually equals Part A, Line 15 of RUS Form 7, except that Interest on Long-term debt shall be increased by 1/3 of the amount, if any, by which the rentals of Restricted Property of the electric system (Part M, Line 3 of RUS Form 7) exceeds 2 percent of Total Margins and Equities (Part C, Line 36 of RUS Form 7); and
B=Patronage Capital & Operating Margins of the electric system, which usually equals Part A, Line 20 of RUS Form 7.

* * * * *

§ 1710.103 [Amended]

3. Section 1710.103 is amended by removing in paragraph (b) the sentence "The loan contract shall contain provisions to this effect."

4. Section 1710.114 is revised as follows:

§ 1710.114 TIER, DSC, OTIER and ODSC requirements.

(a) *General.* Requirements for coverage ratios are set forth in the borrower's mortgage, loan contract, or other contractual agreements with RUS. The requirements set forth in this section apply to borrowers that receive a loan on or after February 10, 1992. Nothing in this section, however, shall reduce the coverage-ratio requirements of a borrower that has contractually agreed with RUS to a higher requirement.

(b) *Coverage ratios.* (1) Distribution borrowers. The minimum coverage ratios required of distribution borrowers, whether applied on an annual or average basis, are a TIER of 1.50, DSC of 1.25, OTIER of 1.1, and ODSC of 1.1. OTIER and ODSC shall apply to distribution borrowers that receive a loan on or after [the effective date of the final rule].

(2) The minimum coverage ratios required of power supply borrowers, whether applied on an annual or average basis, are a TIER of 1.05 and DSC of 1.00.

(3) When new loan contracts are executed, the Administrator may, case

by case, increase the coverage ratios of distribution and power supply borrowers above the levels cited in paragraphs (b)(1) and (b)(2), respectively, of this section if the Administrator determines that the higher ratios are required to ensure reasonable security for and/or the repayment of loans made or guaranteed by RUS. Also, the Administrator may, case by case, reduce said coverage ratios if the Administrator determines that the lower ratios are required to ensure reasonable security for and/or the repayment of loans made or guaranteed by RUS.

(4) If a distribution borrower has in service or under construction a substantial amount of generation and associated transmission plant financed at a cost of capital substantially higher than the cost of funds under section 305 of the RE Act, then the Administrator may establish, in his or her sole discretion, blended levels for TIER, DSC, OTIER, and ODSC based on the respective shares of total utility plant represented by said generation and associated transmission plant and by distribution and other transmission plant.

(c) *Requirements for loan feasibility.* To be eligible for a loan, borrowers must demonstrate to RUS that they will, on a pro forma basis, earn the coverage ratios required by paragraph (b) of this section in each of the years included in the borrower's long-range financial forecast prepared in support of its loan application, as set forth in subpart G of this part.

(d) *Requirements for maintenance of coverage ratios.*—(1) *Prospective requirement.* Borrowers must design and implement rates for utility service to provide sufficient revenue (along with other revenue available to the borrower in the case of TIER and DSC) to pay all fixed and variable expenses, to provide and maintain reasonable working capital and to maintain on an annual basis the coverage ratios required by paragraph (b) of this section. Rates must be designed and implemented to produce at least enough revenue to meet the requirements of this paragraph under the assumption that average weather conditions in the borrower's service territory will prevail in the future, including average system damage and outages due to weather and the related costs. Failure to design and implement rates pursuant to the requirements of this paragraph shall be an event of default upon notice provided in accordance with the terms of the borrower's mortgage or loan contract.

(2) *Retrospective requirement.* The average coverage ratios achieved by a borrower in the 2 best years out of the 3 most recent calendar years must meet the levels required by paragraph (b) of this section. If a borrower fails to achieve these average levels, it must promptly notify RUS in writing. Within 30 days of such notification or of the borrower being notified in writing by RUS, whichever is earlier, the borrower, in consultation with RUS, must provide a written plan satisfactory to RUS setting forth the actions that will be taken to achieve the required coverage ratios on a timely basis. Failure to develop and implement a plan satisfactory to RUS shall be an event of default upon notice provided in accordance with the terms of the borrower's mortgage or loan contract.

(3) *Fixed and variable expenses,* as used in this section, include but are not limited to: all taxes, depreciation, maintenance expenses, and the cost of electric power and energy and other operating expenses of the electric system, including all obligations under the wholesale power contract, all lease payments when due, and all principal and interest payments on outstanding indebtedness when due.

(e) *Requirements for advance of funds.* (1) If a borrower applying for a loan has failed to achieve the coverage ratios required by paragraph (b) of this section during the latest 12 month period immediately preceding approval of the loan, or if any of the borrower's average coverage ratios for the 2 best years out of the most recent 3 calendar years were below the levels required in paragraph (b) of this section, RUS may withhold the advance of loan funds until the borrower has adopted an annual financial plan and operating budget satisfactory to RUS and taken such other action as RUS may require to demonstrate that the required coverage ratios will be maintained in the future and that the loan will be repaid with interest within the time agreed. Such other action may include, for example, increasing system operating efficiency and reducing costs or adopting a rate design that will achieve the required coverage ratios, and either placing such rates into effect or taking action to obtain regulatory authority approval of such rates. If failure to achieve the coverage ratios is due to unusual events beyond the control of the borrower, such as unusual weather, system outage due to a storm or regulatory delay in approving rate increases, then the Administrator may waive the requirement that the borrower take the remedial actions set forth in this

paragraph, provided that such waiver will not threaten loan feasibility.

(2) With respect to any outstanding loan made on or after February 10, 1992, if, based on actual or projected financial performance of the borrower, RUS determines that the borrower may not achieve its required coverage ratios in the current or future years, RUS may withhold the advance of loan funds until the borrower has taken remedial action satisfactory to RUS.

5. Section 1710.250 is amended by revising paragraphs (b) and (e) and adding a new paragraph (k) to read as follows:

§ 1710.250 General.

* * * * *

(b) Generally, all borrowers are required to maintain up-to-date long range engineering plans approved by their boards of directors. Current CWP's approved by the borrower's board must also be developed and maintained for distribution and transmission facilities and for improvements and replacements of generation facilities. All such distribution, transmission or generation facilities must be included in the respective CWP's regardless of the source of financing.

* * * * *

(e) Applications for a loan or loan guarantee from RUS (new loans or budget reclassifications) must be supported by a current CWP approved by both the borrower's board of directors and RUS. RUS approval of these plans relates only to the facilities, equipment, and other purposes to be financed by RUS, and means that the plans provide an adequate basis from a planning and engineering standpoint to support RUS financing. RUS approval of the plans does not mean that RUS approves of the facilities, equipment, or other purposes for which the borrower is not seeking RUS financing. If RUS disagrees with a borrower's estimate of the cost of one or more facilities for which RUS financing is sought, RUS may adjust the estimate after consulting with the borrower and explaining the reasons for the adjustment.

* * * * *

(k) Upon written request from a borrower, RUS may waive in writing certain requirements with respect to long-range engineering plans and CWP's if RUS determines that such requirements impose a substantial burden on the borrower and that waiving the requirements will not significantly affect the accomplishment of the objectives of this subpart. For example, if a borrower's load is forecast to remain constant or decline during the

planning period, RUS may waive those portions of the plans that relate to load growth.

§ 1710.251 [Amended]

6. Section 1710.251 is amended by removing the words "and RUS" from the first sentence of paragraph (a).

§ 1710.252 [Amended]

7. Section 1710.252 is amended by removing the words "and RUS" from the first sentence of paragraph (a).

PART 1717—POST-LOAN POLICIES AND PROCEDURES COMMON TO INSURED AND GUARANTEED ELECTRIC LOANS

8. The authority citation for part 1717 continues to read as follows:

Authority: 7 U.S.C. 901-950b; Pub. L. 103-354, 108 Stat. 3178 (7 U.S.C. 6941 *et seq.*), unless otherwise noted.

9. Subpart M is added to part 1717 to read as follows:

Subpart M—Operational Controls

Sec.

- 1717.600 General.
- 1717.601 Applicability.
- 1717.602 Definitions.
- 1717.603 RUS approval of extensions and additions.
- 1717.604 Long-range engineering plans and construction work plans.
- 1717.605 Design standards, plans and specifications, construction standards, and RUS accepted materials.
- 1717.606 Standard forms of construction contracts, and engineering and architectural services contracts.
- 1717.607 Contract bidding requirements.
- 1717.608 RUS approval of contracts.
- 1717.609 RUS approval of general manager.
- 1717.610 RUS approval of compensation of the board of directors.
- 1717.611 RUS approval of expenditures for legal, accounting, engineering, and supervisory services.
- 1717.612 RUS approval of borrower's bank or other depository.

Subpart M—Operational Controls

§ 1717.600 General.

(a) *General.* The loan contract and mortgage between the Rural Utilities Service (RUS) and electric borrowers imposes certain restrictions and controls on the borrowers and gives RUS (and other co-mortgagees in the case of the mortgage) the right to approve or disapprove certain actions contemplated by the borrowers. Certain of these controls and approval rights are referred to informally as "operational controls" because they pertain to decisions or actions with respect to the operation of the borrowers' electric systems. The approval authority granted to RUS by the loan contract or mortgage regarding

each decision or action subject to controls is often stated in broad, unlimited terms. This subpart lists the main operational controls affecting borrowers and establishes for each area of control the circumstances under which RUS approval of a decision or action by a borrower is either required or not required. In some cases, only the general principles or general circumstances pertaining to RUS approval or control are presented in this subpart, while the details regarding the circumstances and requirements of RUS approval or control are set forth in other RUS regulations. Since this subpart addresses only the main operational controls, failure to address a control or approval right in this subpart in no way invalidates such controls or rights established by the loan contract, mortgage, other agreements between a borrower and RUS, and RUS regulations.

(b) *Case by case amendments.* Upon written notice to a borrower, RUS may amend or annul the approvals and exceptions to controls set forth in this subpart or other RUS regulations if the borrower is in violation of any provision of its loan documents or any other agreement with RUS, or if RUS determines that loan security and/or repayment is threatened. Such amendment or annulment will apply to decisions and actions of the borrower after said written notice has been provided by RUS.

(c) *Generic notices.* By written notice to all borrowers or a group of borrowers, RUS may grant or waive approval of decisions and actions by the borrowers that are controlled under the loan documents and RUS regulations. RUS may also by written notice withdraw or cut back its grant or waiver of approval of said decisions and actions made by previous written notice, but may not by such notice extend its authority to approve decisions and actions by borrowers beyond the authority granted by the loan documents and RUS regulations.

§ 1717.601 Applicability.

(a) The approvals and exceptions to controls conveyed by this subpart apply only to controls and approval rights normally included in RUS loan documents. They do not apply to special controls and approval requirements included in the loan documents or other agreements executed between a borrower and RUS that relate to individual problems or circumstances specific to an individual borrower.

(b) The provisions of this subpart apply to loan documents entered into

between borrowers and RUS, regardless of whether the documents were executed before, on, or after [the effective date of the final rule].

(c) The approvals and exceptions to controls granted by RUS in this subpart shall not in any way affect the rights of other co-mortgagees under the mortgage or their loan contracts.

§ 1717.602 Definitions.

Terms used in this subpart have the meanings set forth in 7 CFR part 1710. In addition, for the purposes of this subpart:

Default means an event of default as defined in the borrower's loan documents or other agreement with RUS, and furthermore includes any event that has occurred and is continuing which, with notice or lapse of time and notice, would become an event of default.

Financed or funded by RUS means financed or funded wholly or in part by a loan made or guaranteed by RUS, including concurrent supplemental loans required by 7 CFR 1710.110, loans to reimburse funds already expended by the borrower, and loans to replace interim financing.

Interchange agreement means a contractual arrangement that can include a variety of services utilities provide each other to increase reliability and efficiency, and to avoid duplicating expenses. Some examples are: transmission service (the use of transmission lines to move power and energy from one area to another); emergency service (an agreement by one utility to furnish another with power and energy to protect it in times of emergency, such as power plant outages); reserve sharing (contributions to a common pool of generating plant reserves so that each individual utility's reserves can be reduced); and economic exchanges (swapping power and energy from different plants to avoid running the most expensive units).

Interconnection agreement means a contract governing the terms for establishing or using one or more electrical connections between two or more electric systems permitting a flow of power and energy among the systems.

Loan documents means the mortgage (or other security instrument acceptable to RUS), the loan contract, and the promissory note entered into between the borrower and RUS.

Pooling agreement means a contract among two or more interconnected electric systems to operate on a coordinated basis to achieve economies and/or enhance reliability in supplying their respective loads.

Power supply contract means any contract entered into by a borrower for the sale or purchase, at wholesale, of electric energy.

Wheeling agreement means a contract providing for the use of the electric transmission facilities of one electric utility to transmit power and energy of another electric utility or other entity to a third party. Such transmission may be accomplished directly or by displacement.

§ 1717.603 RUS approval of extensions and additions.

(a) *Distribution borrowers.* Prior written approval by RUS is required for a distribution borrower to extend or add to its electric system if the extension or addition will be financed by RUS. For extensions and additions that will not be financed by RUS, approval is hereby given to distribution borrowers to make such extensions and additions to their electric systems, including the use of (or commitment to use) general funds of the borrower, except for the following:

- (1) Construction, procurement, or leasing of generating facilities, regardless of the size of the facilities;
- (2) Acquisition or leasing of existing electric facilities or systems in service; and
- (3) Construction, procurement, or leasing of electric facilities to serve a customer whose annual kWh purchases or maximum annual kW demand in the foreseeable future is projected to exceed 25 percent of the borrower's total kWh sales or maximum kW demand in the year immediately preceding the acquisition or start of construction.

(b) *Power supply borrowers.* Prior written approval by RUS is required for a power supply borrower to extend or add to its electric system if the extension or addition will be financed by RUS. Requirements for RUS approval of extensions and additions that will not be financed by RUS are set forth in other RUS regulations.

(c) *Additional details.* Additional details relating to RUS approval of extensions and additions of a borrower's electric system financed by RUS are set forth in other RUS regulations, e.g., in 7 CFR parts 1710 and 1726.

§ 1717.604 Long-range engineering plans and construction work plans.

(a) All borrowers are required to maintain up-to-date long-range engineering plans and construction work plans (CWPs) in form and substance as set forth in 7 CFR part 1710, subpart F.

(b) Applications for financing from RUS must be supported by a long-range engineering plan and CWP approved by RUS.

(c) RUS approval is not required for long-range engineering plans and CWP's if the borrower does not intend to seek RUS financing for any of the facilities, equipment or other purposes included in those plans. However, if requested by RUS, a borrower must provide an informational copy of such plans to RUS.

§ 1717.605 Design standards, plans and specifications, construction standards, and RUS accepted materials.

All borrowers, regardless of the source of funding, are required to comply with applicable RUS requirements with respect to system design, plans and specifications, construction standards, and the use of RUS accepted materials. These requirements are set forth in other RUS regulations, especially in 7 CFR parts 1724 and 1728.

§ 1717.606 Standard forms of construction contracts, and engineering and architectural services contracts.

All borrowers are encouraged to use the standard forms of contracts promulgated by RUS for construction, materials, equipment, engineering services, and architectural services, regardless of the source of funding for such construction and services. Borrowers are required to use these standard forms of contracts only if the construction, procurement or services are financed by RUS. RUS requirements with respect to such standard forms of contract are set forth in 7 CFR part 1724 for architectural and engineering services, and in 7 CFR part 1726 for construction, materials, and equipment.

§ 1717.607 Contract bidding requirements.

Borrowers must follow RUS requirements regarding bidding for contracts for construction, materials, and equipment only if financing of the construction or procurement will be provided by RUS. These requirements are set forth in 7 CFR part 1726.

§ 1717.608 RUS approval of contracts.

(a) *Construction contracts and architectural and engineering contracts.* RUS approval of contracts for construction and procurement and for architectural and engineering services is required only when such construction, procurement or services are financed by RUS. Detailed requirements regarding RUS approval of such contracts are set forth in 7 CFR part 1724 for architectural and engineering services, and in 7 CFR part 1726 for construction and procurement.

(b) *Large retail power contracts.* RUS approval of contracts to sell electric power to retail customers is required only if the contract is for longer than 2

years and the kWh sales or kW demand for any year covered by the contract exceeds 25 percent of the borrower's total kWh sales or maximum kW demand for the year immediately preceding execution of the contract. This requirement applies regardless of the source of funding of any plant extensions, additions or improvements that may be involved in connection with the contract.

(c) *Power supply arrangements.* (1) Power supply contracts (including but not limited to economy energy sales and emergency power and energy sales), interconnection agreements, interchange agreements, wheeling agreements, pooling agreements, and any other similar power supply arrangements subject to approval by RUS are deemed approved if they have a term of 2 years or less. Amendments to said power supply arrangements are also deemed approved provided that the amendment does not extend the term of the arrangement for more than 2 years beyond the date of the amendment.

(2) Any amendment to a schedule or exhibit contained in any power supply arrangement subject to RUS approval, which merely has the effect of either altering a list of interconnection or delivery points or changing the value of a variable term (but not the formula itself) contained in a formula rate or charge is deemed approved.

(3) The provisions of this paragraph apply regardless of whether the borrower is a seller or purchaser of the services furnished by the contracts or arrangements, and regardless of whether or not a Federal power marketing agency is a party to any of them.

(d) *System management and maintenance contracts.* RUS approval of contracts for the management and operation of a borrower's electric system or for the maintenance of the electric system is required only if such contracts cover all or substantially all of the electric system.

(e) *Other contracts.* [Reserved]

§ 1717.609 RUS approval of general manager.

(a) If a borrower's mortgage or loan contract grants RUS the unconditioned right to approve the employment and/or the employment contract of the general manager of the borrower's system, such approval is hereby granted provided that the borrower is in compliance with all provisions of its loan documents and any other agreements with RUS.

(b) If a borrower is in default with respect to any provision of its loan documents or any other agreement with RUS:

(1) Such borrower, if directed in writing by RUS, shall replace its general manager within 30 days after the date of such written notice; and

(2) Such borrower shall not hire a general manager without prior written approval by RUS.

§ 1717.610 RUS approval of compensation of the board of directors.

If a borrower's mortgage or loan contract requires the borrower to obtain approval from RUS for compensation provided to members of the borrower's board of directors, such requirement is hereby waived.

§ 1717.611 RUS approval of expenditures for legal, accounting, engineering, and supervisory services.

(a) If a borrower's mortgage or loan contract requires the borrower to obtain approval from RUS before incurring expenses for legal, accounting, supervisory (other than for the management and operation of the borrower's electric system, see § 1717.608(d)), or other similar services, such approval is hereby granted. However, while expenditures for accounting do not require RUS approval, the selection of a certified public accountant by the borrower to prepare audited reports required by RUS remains subject to RUS approval.

(b) If a borrower's mortgage or loan contract requires the borrower to obtain approval from RUS before incurring expenses for engineering services, such approval is hereby granted if such services will not be financed by RUS. Approval requirements with respect to engineering services financed by RUS are set forth in other RUS regulations.

§ 1717.612 RUS approval of borrower's bank or other depository.

(a) If a borrower's mortgage or loan contract gives RUS the authority to approve the bank or other depositories used by the borrower, such approval is hereby granted provided that the bank or other depositories are insured by the Federal Deposit Insurance Corporation or other Federal agency acceptable to RUS.

(b) Without the prior written approval of RUS, a borrower shall not deposit funds from loans made or guaranteed by RUS in any bank or other depository that is not insured by the Federal Deposit Insurance Corporation or other Federal agency acceptable to RUS.

10. Section 1717.850 is amended by revising paragraphs (a), (b), (f), (g)(1)(ii), (h)(2), and (m) to read as follows:

§ 1717.850 General.

(a) *Scope and applicability.* (1) This subpart R establishes policies and

procedures for the accommodation, subordination or release of the Government's lien on borrower assets, including approvals of supporting documents and related loan security documents, in connection with 100 percent private sector financing of facilities and other purposes. Policies and procedures regarding lien accommodations for concurrent supplemental financing required in connection with an RUS insured loan are set forth in subpart S of this part.

(2) This subpart and subpart S of this part apply only to debt to be secured under the mortgage, the issuance of which is subject to the approval of the Rural Utilities Service (RUS) by the terms of the borrower's mortgage with respect to the issuance of additional debt or the refinancing or refunding of debt. If RUS approval is not required under such terms of the mortgage itself, a lien accommodation is not required. If the loan contract or other agreement between the borrower and RUS requires RUS approval with respect to the issuance of debt or making additions to or extensions of the borrower's system, such required approvals do not by themselves result in the need for a lien accommodation.

(b) *Overall policy.* (1) Consistent with prudent lending practices, the maintenance of adequate security for RUS's loans, and the objectives of the Rural Electrification Act (RE Act), it is the policy of RUS to provide effective and timely assistance to borrowers in obtaining financing from other lenders by sharing RUS's lien on a borrower's assets in order to finance electric facilities, equipment and systems, and certain other types of community infrastructure. In certain circumstances, RUS may facilitate the financing of such assets by subordinating its lien on specific assets financed by other lenders.

(2) It is also the policy of RUS to provide effective and timely assistance to borrowers in promoting rural development by subordinating RUS's lien for financially sound rural development investments under the conditions set forth in § 1717.858.

(f) *Safety and performance standards.* (1) To be eligible for a lien accommodation or subordination from RUS, a borrower must comply with RUS standards regarding facility and system planning and design, construction, procurement, and the use of materials accepted by RUS, as required by the borrower's mortgage, loan contract, or other agreement with RUS, and as further specified in RUS regulations.

(2) RUS "Buy American" requirements shall not apply.

(g) * * *

(i) * * *

(ii) Obtain a certification from a registered professional engineer, for each year during which funds from the separate subaccount are utilized by the borrower, that all materials and equipment purchased and facilities constructed during the year from said funds comply with RUS safety and performance standards, as required by paragraph (f) of this section, and are included in an CWP or CWP amendment approved by the borrower's board of directors;

* * * * *

(h) * * *

(2) To the extent that provisions in a borrower's loan contract or mortgage in favor of RUS may be inconsistent with paragraphs (g)(1) and (h)(1) of this section, paragraphs (g)(1) and (h)(1) of this section are intended to constitute an approval or waiver under the terms of such instruments, and in any regulations implementing such instruments, with respect to facilities financed with debt obtained entirely from non-RUS sources without an RUS guarantee.

* * * * *

(m) *Waiver authority.* Consistent with the RE Act and other applicable laws, any requirement, condition, or restriction imposed by this subpart, or subpart S of this part, on a borrower, private lender, or application for a lien accommodation or subordination may be waived or reduced by the Administrator, if the Administrator determines that said action is in the Government's financial interest with respect to ensuring repayment and reasonably adequate security for loans made or guaranteed by RUS.

* * * * *

11. Section 1717.851 is amended by removing the definitions for "ODSC" and "OTIER" and by adding the following definitions in alphabetical order to read as follows:

§ 1717.851 Definitions.

* * * * *

Natural gas distribution system means any system of community infrastructure whose primary function is the distribution of natural gas and whose services are available by design to all or a substantial portion of the members of the community.

* * * * *

Solid waste disposal system means any system of community infrastructure whose primary function is the collection and/or disposal of solid waste and

whose services are available by design to all or a substantial portion of the members of the community.

Telecommunication and other electronic communication system means any system of community infrastructure whose primary function is the provision of telecommunication or other electronic communication services and whose services are available by design to all or a substantial portion of the members of the community.

* * * * *

Water and waste disposal system means any system of community infrastructure whose primary function is the supplying of water and/or the collection and treatment of waste water and whose services are available by design to all or a substantial portion of the members of the community.

* * * * *

12. In § 1717.852, paragraphs (a)(1) introductory text and (a)(1)(ii) are amended by adding the words "and/or steam" before the word "power", paragraphs (a)(3) through (a)(7) and paragraph (b) are revised, and paragraph (a)(8) is added to read as follows:

§ 1717.852 Financing purposes.

(a) * * *

(3) The following types of community infrastructure substantially located within the electric service territory of the borrower: water and waste disposal systems, solid waste disposal systems, telecommunication and other electronic communications systems, and natural gas distribution systems;

(4) Front-end costs, when and as the borrower has obtained a binding commitment from the non-RUS lender for the financing required to complete the procurement or construction of the facilities;

(5) Transaction costs included as part of the cost of financing assets or refinancing existing debt, provided, however, that the amount of transaction costs eligible for lien accommodation or subordination normally shall not exceed 5 percent of the principal amount of financing or refinancing provided, net of all transaction costs;

(6) The refinancing of existing debt secured under the mortgage;

(7) Interest during construction of generation and transmission facilities if approved by RUS, case by case, depending on the financial condition of the borrower, the terms of the financing, the nature of the construction, the treatment of these costs by regulatory authorities having jurisdiction, and such other factors deemed appropriate by RUS; and

(8) Lien subordinations for certain rural development investments, as provided in § 1717.858.

(b) *Purposes ineligible.* The following financing purposes are not eligible for a lien accommodation or subordination from RUS:

(1) Working capital, including operating funds, unless in the judgment of RUS the working capital is required to ensure the repayment of RUS loans and/or other loans secured under the mortgage;

(2) Facilities, equipment, appliances, or wiring located inside the premises of the consumer, except:

(i) Certain load-management equipment (see 7 CFR 1710.251(c));

(ii) Renewable energy systems and RUS-approved programs of demand side management and energy conservation; and

(iii) As determined by RUS on a case by case basis, facilities included as part of certain cogeneration projects to furnish electric and/or steam power to end-user customers of the borrower;

(3) Investments in a lender required of the borrower as a condition for obtaining financing; and

(4) Debt incurred by a distribution or power supply borrower to finance facilities, equipment or other assets that are not part of the borrower's electric system or one of the four community infrastructure systems cited in paragraph (a)(3) of this section, except for certain rural development investments eligible for a lien subordination under § 1717.858.

* * * * *

13. Section 1717.854 is amended by revising the section heading and paragraphs (a), (b), (c)(1) and (c)(2), removing paragraph (c)(7), redesignating paragraphs (c)(3) through (c)(6) as paragraphs (c)(4) through (c)(7), adding a new paragraph (c)(3), adding "and" at the end of newly designated paragraph (c)(6)(vi), and removing "; and" at the end of newly designated paragraph (c)(7) and adding a period in its place to read as follows:

§ 1717.854 Advance approval—100 percent private financing of distribution, subtransmission and headquarters facilities, and certain other community infrastructure.

(a) *Policy.* Requests for a lien accommodation or subordination from distribution borrowers for 100 percent private financing of distribution, subtransmission and headquarters facilities, and for community infrastructure listed in § 1717.852(a)(3), qualify for advance approval by RUS if they meet the conditions of this section and all other applicable provisions of

this subpart. Advance approval means RUS will approve these requests once RUS is satisfied that the conditions of this section and all other applicable provisions of this subpart have been met.

(b) *Eligible purposes.* Lien accommodations or subordinations for the financing of distribution, subtransmission, and headquarters facilities and community infrastructure listed in § 1717.852(a)(3) are eligible for advance approval, except those that involve the purchase of existing facilities and associated service territory.

(c) * * *

(1) The borrower has achieved a TIER of at least 1.5 and a DSC of at least 1.25 for each of 2 calendar years immediately preceding, or any 2 consecutive 12 month periods ending within 180 days immediately preceding, the issuance of the debt;

(2) The ratio of the borrower's equity, less deferred expenses, to total assets, less deferred expenses, is not less than 27 percent, after adding the principal amount of the proposed loan to the total assets of the borrower;

(3) The borrower's net utility plant as a ratio to its total outstanding long-term debt is not less than 1.0, after adding the principal amount of the proposed loan to the existing outstanding long-term debt of the borrower;

* * * * *

14. Section 1717.855 is amended by revising the section heading and paragraph (a) to read as follows:

§ 1717.855 Application contents: Advance approval—100 percent private financing of distribution, subtransmission and headquarters facilities, and certain other community infrastructure.

* * * * *

(a) A certification by an authorized official of the borrower that the borrower and, as applicable, the loan are in compliance with all conditions set forth in § 1717.854(c) and all applicable provisions of §§ 1717.852 and 1717.853;

* * * * *

15. Section 1717.856 is amended by revising the section heading, the introductory text, the introductory text of paragraph (a), and paragraph (c)(3) to read as follows:

§ 1717.856 Application contents: Normal review—100 percent private financing.

Applications for a lien accommodation or subordination for 100 percent private financing for eligible purposes that do not meet the requirements of § 1717.854 must include the following information and documents:

(a) A certification by an authorized official of the borrower that:

* * * * *

(c) * * *

(3) The borrower has achieved the TIER and DSC and any other coverage ratios required by its mortgage or loan contract in each of the two most recent calendar years; and

* * * * *

§ 1717.857 [Amended]

16. Section 1717.857 is amended by removing paragraph (a)(5), by adding "and" at the end of paragraph (a)(3), and by removing "; and" at the end of paragraph (a)(4)(ii) and adding a period in its place.

PART 1718—LOAN SECURITY DOCUMENTS FOR ELECTRIC BORROWERS

17. The authority citation for part 1718 continues to read as follows:

Authority: 7 U.S.C. 901–950b; Pub. L. 103–354, 108 Stat. 3178 (7 U.S.C. 6941 *et seq.*).

18. Subpart C is added to part 1718 to read as follows:

Subpart C—Loan Contracts With Distribution Borrowers

Sec.

- 1718.100 General.
- 1718.101 Applicability.
- 1718.102 Definitions.
- 1718.103 Loan contract provisions.
- 1718.104 Availability of model loan contract.

Appendix A to Subpart C of Part 1718—Model Form of Loan Contract for Electric Distribution Borrowers

Subpart C—Loan Contracts With Distribution Borrowers

§ 1718.100 General.

(a) *Purpose.* The purpose of this subpart is to set forth the policies, requirements, and procedures governing loan contracts entered into between the Rural Utilities Service (RUS) and distribution borrowers or, in some cases, other electric borrowers.

(b) *Flexibility for individual circumstances.* The intent of this subpart is to provide the flexibility to address the different needs and different credit risks of individual borrowers, and other special circumstances of individual lending situations. The model loan contract contained in Appendix A of this subpart provides an example of what a loan contract with an "average" or "typical" distribution borrower may look like under "average" or "typical" circumstances. Depending on the credit risks and other circumstances of individual loans, RUS may execute loan contracts with

provisions that are substantially different than those set forth in the model. RUS may develop alternative model loan contract provisions. If it does, such provisions will be made available to the public.

(c) *Resolution of any differences in contractual provisions.* If any provision of the loan contract appears to be in conflict with provisions of the mortgage, the loan contract shall have precedence with respect to the contractual relationship between the borrower and RUS with respect to such provision. If either document is silent on a matter addressed in the other document, the other document shall have precedence with respect to the contractual relationship between the borrower and RUS with respect to such matter.

(d) *Loan contract provisions subject to subsequent rule making.* The provisions of all loan contracts executed pursuant to this subpart shall be subject to amendment and modification pursuant to subsequent rule making. Such amendments and modifications may not exceed the authority granted to RUS in the loan contract entered into with the borrower.

§ 1718.101 Applicability.

(a) *Distribution borrowers.* The provisions of this subpart apply to all distribution borrowers that obtain a loan or loan guarantee from RUS on or after [the effective date of the final rule]. Distribution borrowers that obtain a lien accommodation or any other form of financial assistance from RUS after [the effective date of the final rule] may be required to execute a new loan contract and new mortgage. Moreover, any distribution borrower may submit a request to RUS that a new loan contract and new mortgage be executed. Within the constraints of time and staff resources, RUS will attempt to honor such requests. Borrowers must first obtain the concurrence of any other mortgagees on their existing mortgage before a new mortgage can be executed.

(b) *Other borrowers.* Borrowers other than distribution borrowers may also submit requests for execution of a new loan contract pursuant to this subpart and a new mortgage pursuant to subpart B of this part. RUS may approve such requests if it determines that it is in the government's financial interest. If other mortgagees are on the borrower's existing mortgage, their concurrence would be required before a new mortgage could be executed.

§ 1718.102 Definitions.

For the purposes of this subpart:

Borrower means any organization that has an outstanding loan made or

guaranteed by the Rural Utilities Service (RUS) or its predecessor, the Rural Electrification Administration, for rural electrification, or that is seeking such financing.

Distribution borrower means a borrower that sells or intends to sell electric power and energy at retail in rural areas, the latter being defined in 7 CFR 1710.2.

Loan documents means the mortgage (or other security instrument acceptable to RUS), the loan contract, and the promissory note entered into between the borrower and RUS.

§ 1718.103 Loan contract provisions.

Loan contracts executed pursuant to this subpart shall contain such provisions as RUS determines are appropriate to further the purposes of the RE Act and to ensure that the security for the loan will be reasonably adequate and that the loan will be repaid according to the terms of the promissory note. Such loan contracts will contain provisions addressing, but not necessarily limited to, the following matters:

(a) Description of the purpose of the loan;

(b) Specification of the interest to be charged on the loan, including the method for determining the interest rate if it is not fixed for the entire term of the loan;

(c) Specification of the method for repaying the loan principal, including the final maturity of the loan;

(d) The conditions under which the loan may be prepaid before its maturity date, including but not limited to requirements regarding the prepayment of loans made concurrently by RUS and another secured lender;

(e) The method for making scheduled payments on the loan;

(f) Accounting principles and system of accounts, and RUS authority to approve the accountant used by the borrower;

(g) The method and time period for advancing loan funds and the conditions precedent to the advance of funds;

(h) Representations and warranties by the borrower as a condition of obtaining the loan, including but not limited to: the legal authority of the borrower to enter into the loan contract and operate its system; that the loan documents will be a legal, valid and binding obligation of the borrower enforceable according to their terms; compliance of the borrower in all material respects with all federal, state, and local laws, regulations, codes, and orders; existence of any pending or threatened legal actions that could have a material adverse effect on the

borrower's ability to perform its obligations under the loan documents; the accuracy and completeness of all information provided by the borrower in the loan application and with respect to the loan contract, and the existence of any material adverse change since the information was provided; and the existence of any material defaults under other agreements of the borrower;

(i) Representations, warranties, and covenants with respect to environmental matters;

(j) Reports and notices required to be submitted to RUS, including but not limited to: annual financial statements; notice of defaults; notice of litigation; notice of orders or other directives received by the borrower from regulatory authorities; notice of any matter that has resulted in or may result in a material adverse change in the condition or operations of the borrower; and such other information regarding the condition or operations of the borrower as RUS may reasonably require;

(k) Annual written certification that the borrower is in compliance with its loan contract, note, mortgage, and any other agreement with RUS, or if there has been a default in the fulfillment of any obligation under said agreements, specifying each such default and the nature and status thereof;

(l) Requirement that the borrower design and implement rates for utility services to meet certain minimum coverage of interest expense and/or debt service obligations;

(m) Requirement that the borrower maintain and preserve its mortgaged property in compliance with prudent utility practice and all applicable laws, which may include certain specific actions and certifications set forth in the borrower's loan contract or mortgage;

(n) Requirement that the borrower plan, design and construct its electric system according to standards and other requirements established by RUS, and if directed by the Administrator, that the borrower follow RUS planning, design and construction standards and requirements for other utility systems constructed by the borrower;

(o) Limitations on extensions and additions to the borrower's electric system without approval by RUS;

(p) Limitations on contracts and contract amendments that the borrower may enter into without approval by RUS;

(q) Limitations of the transfer of mortgaged property by the borrower;

(r) Limitations on dividends, patronage refunds, and cash distributions paid by the borrower;

(s) Limitations on investments, loans, and guarantees made by the borrower;

(t) Authority of RUS to approve a new general manager and to require that an existing general manager be replaced if the borrower is in default under its mortgage, loan contract, or any other agreements with RUS;

(u) Description of events of default under the loan contract and the remedies available to RUS;

(v) Applicability of state and federal laws;

(w) Severability of the individual provisions of the loan documents;

(x) Matters relating to the assignment of the loan contract;

(y) Requirements relating to federal laws and regulations, including but not limited to the following matters: area coverage for electric service; civil rights and equal employment opportunity; access to buildings and other matters relating to the handicapped; design and construction standards relating to earthquakes; the National Environmental Policy Act of 1969 and other environmental laws and regulations; flood hazard insurance; debarment and suspension from federal assistance programs; and delinquency on federal debt; and

(z) Special requirements applicable to individual loans, and such other provisions as RUS may require to ensure loan repayment and reasonably adequate loan security.

§ 1718.104 Availability of model loan contract.

Single copies of the model loan contract (RUS Informational Publication 1718 C) are available from the Administrative Services Division, Rural Utilities Service, United States Department of Agriculture, Washington, DC 20250-1500. This document may be reproduced.

Appendix A to Subpart C of Part 1718—Model Form of Loan Contract for Electric Distribution Borrowers

Loan Contract

Table of Contents

Recitals

Article I—Definitions

Article II—Representations and Warranties

Section 2.1. Representations and Warranties.

Article III—Loan

Section 3.1. Advances.

Section 3.2. Interest Rate and Payment.

Section 3.3. Prepayment.

Article IV—Conditions of Lending

Section 4.1. General Conditions.

Section 4.2. Special Conditions.

Article V—Affirmative Covenants

Section 5.1. Generally.

Section 5.2. Annual Certificates.

Section 5.3. Simultaneous Prepayment of Contemporaneous Loans.

Section 5.4. Rates to Provide Revenue Sufficient to Meet Coverage Ratios Requirements.

Section 5.5. Depreciation Rates.

Section 5.6. Property Maintenance.

Section 5.7. Financial Books.

Section 5.8. Rights of Inspection.

Section 5.9. Area Coverage.

Section 5.10. Real Property Acquisition.

Section 5.11. "Buy American" Requirements.

Section 5.12. Power Requirements Studies.

Section 5.13. Long Range Engineering Plans and Construction Work Plans.

Section 5.14. Design Standards, Plans and Specifications, Construction Standards, and List of Materials.

Section 5.15. Construction.

Section 5.16. Standard Forms of Construction Contracts, and Engineering and Architectural Services Contracts.

Section 5.17. Contract Bidding Requirements.

Section 5.18. Nondiscrimination.

Section 5.19. Financial Reports.

Section 5.20. Miscellaneous Reports and Notices.

Section 5.21. Special Construction Account.

Section 5.22. Additional Affirmative Covenants.

Article VI—Negative Covenants

Section 6.1. General.

Section 6.2. Limitations on System Extensions and Additions.

Section 6.3. Limitations on Expenses for Legal, Engineering and Supervisory Services.

Section 6.4. Limitations on Employment and Retention of Manager.

Section 6.5. Limitations on Certain Types of Contracts.

Section 6.6. Limitations on Mergers and Sale, Lease or Transfer of Capital Assets.

Section 6.7. Limitations on Acquisition, Construction or Procurement of Generating Facilities, Existing Facilities or Utility Systems.

Section 6.8. Limitation on Distributions.

Section 6.9. Limitations on Loans, Investments and Other Obligations.

Section 6.10. Depreciation Rates.

Section 6.11. Historic Preservation.

Section 6.12. Rate Reductions.

Section 6.13. Limitations on Additional Indebtedness.

Section 6.14. Limitations on Issuing Additional Indebtedness Secured Under the Mortgage.

Section 6.15. Impairment of Contracts Pledged to RUS.

Section 6.16. Limitations on Using non FDIC-insured Depositories.

Section 6.17. Additional Negative Covenants.

Article VII—Default

Section 7.1. Events of Default.

Article VIII—Remedies

Section 8.1. Generally.

Section 8.2. Suspension of Advances.

Article IX—Miscellaneous

Section 9.1. Notices.

Section 9.2. Expenses.

Section 9.3. Late Payments.

Section 9.4. Filing Fees.

Section 9.5. No Waiver.

Section 9.6. Governing Law.

Section 9.7. Holiday Payments.

Section 9.8. Rescission.

Section 9.9. Successors and Assigns.

Section 9.10. Complete Agreement; Amendments.

Section 9.11. Headings.

Section 9.12. Severability.

Section 9.13. Right of Setoff.

Section 9.14. Right of RUS to Appoint Supervisor.

Section 9.15. Schedules and Exhibits.

Section 9.16. Prior Loan Documents.

Section 9.17. Term.

Schedule 1

Schedule 2—Existing Liens

Schedule 3—Additional Contracts

Exhibit A: Form of Promissory Note

Exhibit B: Equal Opportunity Contract Provisions

Exhibit C-1: Manager's Certificate Required Under Loan Contract Section 6.14 for Additional Notes

Exhibit C-2: Manager's Certificate Required Under Loan Contract Section 6.14 for Refinancing Notes

Loan Contract

AGREEMENT, dated _____, 199_____, between _____ ("Borrower"), a corporation organized and existing under the laws of the State of _____ (the "State") and the UNITED STATES OF AMERICA acting by and through the Administrator of the Rural Utilities Service ("RUS").

Recitals

The Borrower has applied to RUS for a loan for the purpose(s) set forth in Schedule 1 hereto.

RUS is willing to make such a loan to the Borrower pursuant to the Rural Electrification Act of 1936, as amended, on the terms and conditions stated herein.

THEREFORE, for and in consideration of the premises and the mutual covenants hereinafter contained, the parties hereto agree and bind themselves as follows:

Article I—Definitions

Capitalized terms that are not defined herein shall have the meanings as set forth in the Mortgage. The terms defined herein include the plural as well as the singular and the singular as well as the plural.

"Act" shall mean the Rural Electrification Act of 1936 etc.

"Advance" or "Advances" shall mean advances by RUS to Borrower pursuant to the terms and conditions of this Agreement.

"Agreement" shall mean this Loan Contract together with all schedules and exhibits and also any subsequent supplements or amendments.

"Business Day" shall mean any day that RUS is open for business.

"Contemporaneous Loan" shall mean a loan made pursuant to a loan agreement providing for a loan secured by a mortgage on which RUS was also a mortgagee, the making of which was conditioned upon the making of a loan, therein described, by another lender, and shall also mean any loan which the Borrower has used to satisfy RUS Regulations requiring that supplemental financing be obtained in order to qualify for a loan from RUS. Any loan used to refinance or refund a Contemporaneous Loan is also considered to be a Contemporaneous Loan.

"Coverage Ratios" shall mean, collectively, the following financial ratios pertaining to the Electric System: (i) TIER of 1.5; (ii) Operating TIER of 1.1; (iii) DSC of 1.25; and Operating DSC of 1.1.

"DSC" shall have the meaning as defined in the Mortgage.

"Distributions" shall mean for the Borrower to, in any calendar year, declare or pay any dividends, or pay or determine to pay any patronage refunds, or retire any patronage capital or make any other cash distributions, to its members, stockholders or consumers; *provided, however*, that for the purposes of this Agreement a "Cash Distribution" shall be deemed to include any general cancellation or abatement of charges for electric energy or services furnished by the Borrower, but not the repayment of a membership fee upon termination of a membership [and not the rebate of an abatement of costs incurred by the Borrower, such as a reduction of wholesale power cost previously incurred].

"Electric System" shall have the meaning as defined in the Mortgage.

"Equity" shall mean the Borrower's total margins and equities computed pursuant to RUS Accounting Requirements but excluding any Regulatory Created Assets.

"Event of Default" shall have the meaning as defined in Section [7.1].

"Interest Expense" shall mean the interest expense of the Borrower computed pursuant to RUS Accounting requirements.

"Loan" shall mean the loan described in Article II which is being made pursuant to the RUS Commitment in furtherance of the objectives of the Act.

"Loan Documents" shall mean, collectively, this Agreement, the Mortgage and the Note.

"Long-Term Debt" shall mean the total of all amounts included in the long-term debt of the Borrower pursuant to RUS Accounting Requirements.

"Maturity Date" shall have the meaning as defined in the Note.

"Monthly Payment Date" shall have the meaning as defined in the Note.

"Mortgage" shall have the meaning as described in Schedule 1 hereto.

"Mortgaged Property" shall have the meaning as defined in the Mortgage.

"Net Utility Plant" shall mean the amount constituting the total utility plant of the Borrower, less depreciation, computed in accordance with RUS Accounting Requirements.

"Note" shall mean a promissory note executed by the Borrower in the form of Exhibit A hereto, and any note executed and delivered to RUS to refund, or in substitution for such a note.

"Operating DSC" or "ODSC" shall mean Operating Debt Service Coverage calculated as:

$$\text{ODSC} = \frac{A+B+C}{D}$$

where:

All amounts are for the same one-year period and are computed pursuant to RUS Accounting Requirements;

A=Depreciation and amortization expense of the Electric System;

B=Interest Expense on all Long-term Debt of the Electric System, except that Interest Expense shall be increased by 1/3 of the amount, if any, by which the rentals of Restricted Property of the Electric System exceed 2 percent of total margins and equities;

C=Patronage capital & operating margins of the Electric System, which equals operating revenue and patronage capital of Electric System operations, less total cost of electric service (including Interest Expense on all Long-Term Debt of the Electric System); and

D=Debt service billed which equals all interest and principal billed or billable to the Borrower during the year for all Long-Term Debt of the Electric System, plus 1/3 of the amount, if any, by which the rentals of Restricted Property of the Electric System exceed 2 percent of total margins and equities.

"Operating TIER" or "OTIER" shall mean Operating Times Interest Earned Ratio calculated as:

$$\text{OTIER} = \frac{A+B}{A}$$

where:

All amounts are for the same one-year period and are computed pursuant to RUS Accounting Requirements;

A=Interest Expense on all Long-term Debt of the Electric System, except that Interest Expense shall be increased by 1/3 of the amount, if any, by which the rentals of Restricted Property of the Electric System exceed 2 percent of total margins and equities; and

B=Patronage capital & operating margins of the Electric System, which equals operating revenue and patronage capital of Electric System operations, less total cost of electric service (including Interest Expense on all Long-Term Debt of the Electric System).

"Payment Notice" shall mean a notice furnished by RUS to Borrower that indicates the precise amount of each payment of principal and interest and the total amount of each payment.

"Permitted Debt" shall have the meaning as defined in Section [6.13].

"Regulatory Created Assets" shall mean the sum of any amounts properly recordable as unrecovered plant and regulatory study costs or as other regulatory assets, computed pursuant to RUS Accounting Requirements.

"RUS Accounting Requirements" shall mean any system of accounts prescribed by RUS Regulations as such RUS Accounting Requirements exist at the date of applicability thereof.

"RUS Commitment" shall have the meaning as defined in Schedule 1 hereto.

"RUS Regulations" shall mean regulations published by RUS from time to time in the **Federal Register** as they exist at the date of applicability thereof, and shall also include any regulations of other federal entities which RUS is required by law to implement.

"Subsidiary" shall mean a corporation that is a subsidiary of the Borrower and subject to the Borrower's control, as defined by RUS Accounting Requirements.

"Termination Date" shall have the meaning as defined in the Note.

"TIER" shall have the meaning as defined in the Mortgage.

"Total Assets" shall mean an amount constituting the total assets of the Borrower as computed pursuant to RUS Accounting Requirements, but excluding any Regulatory Created Assets.

"Total Utility Plant" shall mean the amount constituting the total utility plant of the Borrower computed in accordance with RUS Accounting Requirements.

"Utility System" shall have the meaning as defined in the Mortgage.

Article II—Representations and Warranties

Section 2.1. Representations and Warranties. To induce RUS to make the Loan, and recognizing that RUS is relying hereof, the Borrower represents and warrants as follows:

(a) *Organization; Power, Etc.* The Borrower: (i) is duly organized, validly existing, and in good standing under the laws of its state of incorporation; (ii) is duly qualified to do business and is in good standing in each jurisdiction in which the transaction of its business makes such qualification necessary; (iii) has all requisite corporate and legal power to own and operate its assets and to carry on its business and to enter into and perform the Loan Documents; (iv) has duly and lawfully obtained and maintained all licenses, certificates, permits, authorizations, approvals, and the like which are material to the conduct of its business or which may be otherwise required by law; and (v) is eligible to borrow from RUS.

(b) *Authority.* The execution, delivery and performance by the Borrower of this Agreement and the other Loan Documents and the performance of the transactions contemplated thereby have been duly authorized by all necessary corporate action and will not violate any provision of law or of the Articles of Incorporation or By-Laws of the Borrower or result in a breach of, or constitute a default under, any agreement, indenture or other instrument to which the Borrower is a party or by which it may be bound.

(c) *Consents.* No consent, permission, authorization, order, or license of any governmental authority is necessary in connection with the execution, delivery, performance, or enforcement of the Loan Documents, except (i) such as have been obtained and are in full force and effect and (ii) such as have been disclosed on Schedule 1 hereto.

(d) *Binding Agreement.* Each of the Loan Documents is, or when executed and delivered will be, the legal, valid, and binding obligation of the Borrower,

enforceable in accordance with its terms, subject only to limitations on enforceability imposed by applicable bankruptcy, insolvency, reorganization, moratorium, or similar laws affecting creditors' rights generally.

(e) *Compliance With Laws.* The Borrower is in compliance in all material respects with all federal, state, and local laws, rules, regulations, ordinances, codes, and orders (collectively, "Laws"), the failure to comply with which could have a material adverse effect on the condition, financial or otherwise, operations, properties, or business of the Borrower, or on the ability of the Borrower to perform its obligations under the Loan Documents, except as the Borrower has disclosed on Schedule 1 attached hereto.

(f) *Litigation.* There are no pending legal, arbitration, or governmental actions or proceedings to which the Borrower is a party or to which any of its property is subject which, if adversely determined, could have a material adverse effect on the condition, financial or otherwise, operations, properties, or business of the Borrower, or on the ability of the Borrower to perform its obligations under the Loan Documents, and to the best of the Borrower's knowledge, no such actions or proceedings are threatened or contemplated, except as the Borrower has disclosed on Schedule 1 attached hereto.

(g) *Title to Property.* The Borrower holds good and marketable title to all of its real property and owns all of its personal property free and clear of any lien or encumbrance except the liens and encumbrances specifically identified on Schedule 2 attached hereto (the "Existing Liens"), and liens or other interests permitted under the Mortgage.

(h) *Financial Statements; No Material Adverse Change; Etc.* All financial statements submitted to RUS in connection with the application for the Loan or in connections with this Agreement fairly and fully present the financial condition of the Borrower and the results of the Borrower's operations for the periods covered thereby and are prepared in accordance with RUS Accounting Requirements consistently applied. Since the dates thereof, there has been no material adverse change in the financial condition or operations of the Borrower. All budgets, projections, feasibility studies, and other documentation submitted by the Borrower to RUS are based upon assumptions that are reasonable and realistic, and as of the date hereof, no fact has come to light, and no event or transaction has occurred, which would cause any assumption made therein not to be reasonable or realistic.

(i) *Principal Place of Business; Records.* The principal place of business and chief executive office of the Borrower is at the address of the Borrower shown on Schedule 1 attached hereto.

(j) *Location of Properties.* All property owned by the Borrower is located in the counties identified in Schedule 1 hereto.

(k) *Subsidiaries.* The Borrower has no subsidiary, except as the Borrower has disclosed on Schedule 1 attached hereto.

(l) *Defaults Under Other Agreements.* The Borrower is not in default under any agreement or instrument to which it is a

party or under which any of its properties are subject that is material to its financial condition, operations, properties, profits, or business.

(m) *Survival.* All representations and warranties made by the Borrower herein or made in any certificate delivered pursuant hereto shall survive the making of the Advances and the execution and delivery to RUS of the Note.

Article III—Loan

Section 3.1. *Advances.* RUS agrees to make, and the Borrower agrees to request, on the terms and conditions of this Agreement, Advances from time to time in an aggregate principal amount not to exceed the RUS Commitment. On the Termination Date, RUS may stop advancing funds and limit the RUS Commitment to the amount advanced prior to such date. The obligation of the Borrower to repay the Advances shall be evidenced by the Note in the principal amount of the unpaid principal amount of the Advances from time to time outstanding. The Borrower shall give RUS written notice of the date on which each Advance is to be made.

Section 3.2. *Interest Rate and Payment.* The Note shall be payable and bear interest as follows:

(a) *Payments and Amortization.* Principal will be amortized in accordance with the method stated in Schedule 1 hereto and more fully described in the form of Note attached hereto as Exhibit A.

(b) *Application of Payments.* Each payment shall be applied first to any charges then due on the Note, second to interest accrued on the principal amount to the due date of such payment on the Note, and the balance to the reduction of principal against the Note in inverse order of maturity.

(c) *Electronic Funds Transfer.* Except as otherwise prescribed by RUS, the Borrower shall make all payments on the Note utilizing electronic funds transfer procedures as specified by RUS.

(d) *Fixed or Variable Rate.* The Note will bear interest at either a fixed or variable rate in accordance with the method stated in Schedule 1 hereto and as more particularly described in the form of Note attached hereto as Exhibit A.

Section 3.3. *Prepayment.* The Borrower has no right to prepay the Note in whole or in part except such rights, if any, as are expressly provided for in the Note. However, prepayment of the Note (and any penalties) shall be mandatory under Section [5.3] hereof if the Borrower has used a Contemporaneous Loan in order to qualify for the RUS Commitment, and later prepays the Contemporaneous Loan.

Article IV—Conditions of Lending

Section 4.1. *General Conditions.* The obligation of RUS to make any Advance hereunder is subject to satisfaction of each of the following conditions precedent on or before the date of such Advance:

(a) *Legal Matters.* All legal matters incident to the consummation of the transactions hereby contemplated shall be satisfactory to counsel for RUS.

(b) *Loan Documents.* That RUS receive duly executed originals of this Agreement and the other Loan Documents.

(c) *Authorization.* That RUS receive evidence satisfactory to it that all corporate documents and proceedings of the Borrower necessary for duly authorizing the execution, delivery and performance of the Loan Documents have been obtained and are in full force and effect.

(d) *Approvals.* That RUS receive evidence satisfactory to it that all consents and approvals (including without limitation the consents referred to in Section [2.1(c)] of this Agreement) which are necessary for, or required as a condition of, the validity and enforceability of each of the Loan Documents have been obtained and are in full force and effect.

(e) *Event of Default.* That no Event of Default specified in Article VII and no event which, with the lapse of time or the notice and lapse of time specified in Article VII would become such an Event of Default, shall have occurred and be continuing or will have occurred after giving effect to the Advance on the books of the Borrower.

(f) *Continuing Representations and Warranties.* That the representations and warranties of the Borrower contained in this Agreement be true and correct on and as of the date of such Advance as though made on and as of such date.

(g) *Opinion of Counsel.* That RUS receive an opinion of counsel for the Borrower (who shall be acceptable to RUS) in form and content acceptable to RUS.

(h) *Mortgage Filing.* The Mortgage shall have been duly recorded as a mortgage on real property, including after-acquired real property, and duly filed, recorded or indexed as a security interest in personal property, including after acquired personal property, wherever RUS shall have requested, all in accordance with applicable law, and the Borrower shall have caused satisfactory evidence thereof to be furnished to RUS.

(i) *Wholesale Power Contract.* That the Borrower shall not be in default under the terms of, or contesting the validity of, any contract that has been pledged by any entity to RUS as security for the repayment of any loan made or guaranteed by RUS under the Act.

(j) *Material Adverse Change.* That there has occurred no material adverse change in the business or condition, financial or otherwise, of the Borrower and nothing has occurred which in the opinion of RUS materially and adversely affects the Borrower's ability to meet its obligations hereunder.

(k) *Requisitions.* That the Borrower will requisition all Advances by submitting its requisition to RUS in form and substance satisfactory to RUS. Requisitions shall be made only for the purpose(s) set forth herein. The Borrower agrees to apply the proceeds of the Advances in accordance with its loan application with such modifications as may be mutually agreed.

(l) *Flood Insurance.* That for any Advance used in whole or in part to finance the construction or acquisition of any building in any area identified by the Secretary of Housing and Urban Development pursuant to the Flood Disaster Protection Act of 1973 (the "Flood Insurance Act") or any rules, regulations or orders issued to implement the Flood Insurance Act ("Rules") as any area

having special flood hazards, or to finance any facilities or materials to be located in any such building, or in any building owned or occupied by the Borrower and located in such a flood hazard area, the Borrower has submitted evidence, in form and substance satisfactory to RUS, or RUS has otherwise determined, that (i) the community in which such area is located is then participating in the national flood insurance program, as required by the Flood Insurance Act and any Rules, and (ii) the Borrower has obtained flood insurance coverage with respect to such building and contents as may then be required pursuant to the Flood Insurance Act and any Rules.

(m) *RUS Regulations.* That the Advance will be in accordance with all applicable RUS Regulations.

Section 4.2. Special Conditions. The obligation of RUS to make any Advance hereunder is also subject to satisfaction, on or before the date of such Advance, of each of the special conditions, if any, listed in Schedule 1 hereto.

Article V—Affirmative Covenants

Section 5.1. Generally. Unless otherwise agreed to in writing by RUS, while this Agreement is in effect, whether or not any Advance is outstanding, the Borrower agrees to duly observe each of the affirmative covenants contained in this Article:

Section 5.2. Annual Certificates.

(a) *Performance under Loan Documents.* The Borrower will duly observe and perform all of its obligations under each of the Loan Documents.

(b) *Annual Certification.* Within ninety (90) days after the close of each calendar year, commencing with the year following the year in which the initial Advance hereunder shall have been made, the Borrower shall deliver to RUS a written statement signed by its General Manager, stating that during such year the Borrower has fulfilled all of its obligations under the Loan Documents throughout such year or, if there has been a default in the fulfillment of any such obligations, specifying each such default known to said person and the nature and status thereof.

Section 5.3. Simultaneous Prepayment of Contemporaneous Loans. If the Borrower shall at any time prepay the Contemporaneous Loan described on Schedule 1, it shall prepay the RUS Note correspondingly to maintain the ratio that the Contemporaneous Loan bears to the RUS Commitment. If the RUS Note calls for a prepayment penalty or premium, such amount shall be paid but shall not be used in computing the amount needed to be paid to RUS under this section to maintain such ratio. In the case of Contemporaneous Loans and RUS Notes existing prior to the date of this Agreement under previous agreements, prepayments shall be treated as if governed by this section. Provided, however, in all cases prepayments associated with refinancing or refunding a Contemporaneous Loan pursuant to Article II of the Mortgage are not considered to be prepayments for purposes of this Agreement provided that the principal amount of such refinancing or refunding loan is not less than the amount of loan principal being refinanced, and the

weighted average life of the refinancing or refunding loan is materially equal to the weighted average remaining life of the loan being refinanced.

Section 5.4 Rates to Provide Revenue Sufficient to Meet Coverage Ratios Requirements.

(a) *Prospective Requirement.* The Borrower shall design and implement rates for utility service furnished by it to provide sufficient revenue (along with other revenue available to the Borrower in the case of TIER and DSC) (i) to pay all fixed and variable expenses when and as due, (ii) to provide and maintain reasonable working capital, and (iii) to maintain, on an annual basis, the Coverage Ratios. In designing and implementing rates under this paragraph, such rates should be capable of producing at least enough revenue to meet the requirements of this paragraph under the assumption that average weather conditions in the Borrower's service territory will prevail in the future, including average Utility System damage and outages due to weather and the related costs.

(b) *Retrospective Requirement.* The average Coverage Ratios achieved by the Borrower in the 2 best years out of the 3 most recent calendar years must be not less than any of the following:

TIER=1.5
DSC=1.25
OTIER=1.1
ODSC=1.1

(c) *Prospective Notice of Change in Rates.* The Borrower shall give thirty (30) days prior written notice of any proposed change in its general rate structure to RUS if RUS has requested in writing that it be notified in advance of such changes.

(d) *Routine Reporting of Coverage Ratios.* Promptly following the end of each calendar year, the Borrower shall report, in writing, to RUS the TIER, Operating TIER, DSC and Operating DSC levels which were achieved during that calendar year.

(e) *Reporting Non-achievement of Retrospective Requirement.* If the Borrower fails to achieve the average levels required by paragraph (b) of this section, it must promptly notify RUS in writing to that effect.

(f) *Corrective Plans.* Within 30 days of sending a notice to RUS under paragraph (e) of this section, or of being notified by RUS, whichever is earlier, the Borrower in consultation with RUS, shall provide a written plan satisfactory to RUS setting forth the actions that will be taken to achieve the required Coverage Ratios on a timely basis.

(g) *Noncompliance.* Failure to design and implement rates pursuant to paragraph (a) of this section and failure to develop and implement the plan called for in paragraph (f) of this section shall constitute an Event of Default under this Agreement in the event that REA so notifies the Borrower to that effect under section [7.1(c)] of this Agreement.

Section 5.5. Depreciation Rates. The Borrower shall adopt as its depreciation rates only those which have been previously approved for the Borrower by RUS.

Section 5.6. Property Maintenance. The Borrower shall maintain and preserve its Utility System in compliance with the provisions of the Mortgage, RUS Regulations and all applicable laws.

Section 5.7. Financial Books. The Borrower shall at all times keep, and safely preserve, proper books, records and accounts in which full and true entries will be made of all of the dealings, business and affairs of the Borrower and its Subsidiaries, in accordance with any applicable RUS Accounting Requirements.

Section 5.8. Rights of Inspection. The Borrower shall afford RUS, through its representatives, reasonable opportunity, at all times during business hours and upon prior notice, to have access to and the right to inspect the Utility System, any other property encumbered by the Mortgage, and any or all books, records, accounts, invoices, contracts, leases, payrolls, canceled checks, statements and other documents and papers of every kind belonging to or in the possession of the Borrower or in anyway pertaining to its property or business, including its Subsidiaries, if any, and to make copies or extracts therefrom.

Section 5.9. Area Coverage. The Borrower shall make diligent effort to extend electric service to all unserved persons within the service area of the Borrower who (i) desire such service and (ii) meet all reasonable requirements established by the Borrower as a condition of such service. To the extent required by RUS, the Borrower shall provide electric service without a contribution in aid of construction.

Section 5.10. Real Property Acquisition. In acquiring real property, the Borrower shall comply with the provisions of the Uniform Relocation Assistance and Real Property Acquisition Policies Act of 1970 (the "Uniform Act"), as amended by the Uniform Relocation Act Amendments of 1987, and 49 CFR part 24, referenced by 7 CFR part 21, to the extent the Uniform Act is applicable to such acquisition.

Section 5.11. "Buy American" Requirements. The Borrower shall use or cause to be used in connection with the expenditures of funds advanced on account of the Loan only such unmanufactured articles, materials, and supplies as have been mined or produced in the United States, Mexico, or Canada, and only such manufactured articles, materials, and supplies as have been manufactured in the United States, Mexico, or Canada substantially all from articles, materials, and supplies mined, produced or manufactured, as the case may be, in the United States, Mexico, or Canada, except to the extent RUS shall determine that such use shall be impracticable or that the cost thereof shall be unreasonable.

Section 5.12. Power Requirements Studies. The Borrower shall prepare and use power requirements studies of its electric loads and future energy and capacity requirements in conformance with RUS Regulations.

Section 5.13. Long Range Engineering Plans and Construction Work Plans. The Borrower shall develop, maintain and use up-to-date long-range engineering plans and construction work plans in conformance with RUS Regulations.

Section 5.14. Design Standards, Plans and Specifications, Construction Standards, and List of Materials. The Borrower shall use design standards, plans and specifications,

construction standards, and lists of acceptable materials in conformance with RUS Regulations.

Section 5.15. Construction. The Borrower shall acquire and construct the Electric System in conformance with RUS Regulations.

Section 5.16. Standard Forms of Construction Contracts, and Engineering and Architectural Services Contracts. The Borrower shall use the standard forms of contracts promulgated by RUS for construction, procurement, engineering services and architectural services in conformance with RUS Regulations.

Section 5.17. Contract Bidding Requirements. The Borrower shall follow RUS contract bidding procedures in conformance with RUS Regulations when contracting for construction or procurement.

Section 5.18. Nondiscrimination.

(a) *Equal Opportunity Provisions in Construction Contracts.* The Borrower shall incorporate or cause to be incorporated into any construction contract, as defined in Executive Order 11246 of September 24, 1965 and implementing regulations, which is paid for in whole or in part with funds obtained from RUS or borrowed on the credit of the United States pursuant to a grant, contract, loan, insurance or guarantee, or undertaken pursuant to any RUS program involving such grant, contract, loan, insurance or guarantee, the equal opportunity provisions set forth in Exhibit B hereto entitled Equal Opportunity Contract Provisions.

(b) *Equal Opportunity Contract Provisions Also Bind the Borrower.* The Borrower further agrees that it will be bound by such equal opportunity clause in any federally assisted construction work which it performs itself other than through the permanent work force directly employed by an agency of government.

(c) *Sanctions and Penalties.* The Borrower agrees that it will cooperate actively with RUS and the Secretary of Labor in obtaining the compliance of contractors and subcontractors with the equal opportunity clause and the rules, regulations and relevant orders of the Secretary of Labor, that it will furnish RUS and the Secretary of Labor such information as they may require for the supervision of such compliance, and that it will otherwise assist the administering agency in the discharge of RUS's primary responsibility for securing compliance. The Borrower further agrees that it will refrain from entering into any contract or contract modification subject to Executive Order 11246 with a contractor debarred from, or who has not demonstrated eligibility for, Government contracts and federally assisted construction contracts pursuant to Part II, Subpart D of Executive Order 11246 and will carry out such sanctions and penalties for violation of the equal opportunity clause as may be imposed upon contractors and subcontractors by RUS or the Secretary of Labor pursuant to Part II, Subpart D of Executive Order 11246. In addition, the Borrower agrees that if it fails or refuses to comply with these undertakings RUS may cancel, terminate or suspend in whole or in part this contract, may refrain from extending any further assistance under any of its

programs subject to Executive Order 11246 until satisfactory assurance of future compliance has been received from such Borrower, or may refer the case to the Department of Justice for appropriate legal proceedings.

Section 5.19. Financial Reports. The Borrower will cause to be prepared and furnished to RUS from time to time pursuant to RUS Regulations, a full and complete annual report of its financial condition and of its operations in form and substance satisfactory to RUS, audited and certified by Independent certified public accountants satisfactory to RUS and accompanied by a report of such audit in form and substance satisfactory to RUS. The Borrower shall also furnish to RUS from time to time such other reports concerning the financial condition or operations of the Borrower, including its Subsidiaries, as RUS may reasonably request or RUS Regulations require.

Section 5.20. Miscellaneous Reports and Notices. The Borrower will furnish to RUS:

(a) *Notice of Default.* Promptly after becoming aware thereof, notice of: (i) the occurrence of any default; and (ii) the receipt of any notice given pursuant to the Mortgage with respect to the occurrence of any event which with the giving of notice or the passage of time, or both, could become an "Event of Default" under the Mortgage.

(b) *Notice of Non-Environmental Litigation.* Promptly after the commencement thereof, notice of the commencement of all actions, suits or proceedings before any court, arbitrator, or governmental department, commission, board, bureau, agency, or instrumentality affecting the Borrower which, if adversely determined, could have a material adverse effect on the condition, financial or otherwise, operations, properties or business of the Borrower, or on the ability of the Borrower to perform its obligations under the Loan Documents.

(c) *Notice of Environmental Litigation.* Without limiting the provisions of section [5.20(b)] above, promptly after receipt thereof, notice of the receipt of all pleadings, orders, complaints, indictments, or other communications alleging a condition that may require the Borrower to undertake or to contribute to a cleanup or other response under laws relating to environmental protection, or which seek penalties, damages, injunctive relief, or criminal sanctions related to alleged violations of such laws, or which claim personal injury or property damage to any person as a result of environmental factors or conditions, or which, if adversely determined, could have a material adverse effect on the condition, financial or otherwise, operations, properties or business of the Borrower, or on the ability of the Borrower to perform its obligations under the Loan Documents.

(d) *Notice of Change of Place of Business.* Promptly in writing, notice of any change in location of its principal place of business or the office where its records concerning accounts and contract rights are kept.

(e) *Regulatory and Other Notices.* Promptly after receipt thereof, copies of any notices or other communications received from any governmental authority with respect to any matter or proceeding, the effect of which

could have a material adverse effect on the condition, financial or otherwise, operations, properties, or business of the Borrower, or on the ability of the Borrower to perform its obligations under the Loan Documents.

(f) *Material Adverse Change.* Promptly, notice of any matter which has resulted or may result in a material adverse change in the condition, financial or otherwise, operations, properties, or business of the Borrower, or the ability of the Borrower to perform its obligations under the Loan Documents.

(g) *Other Information.* Such other information regarding the condition, financial or otherwise, or operations of the Borrower as RUS may, from time to time, reasonably request.

Section 5.21. Special Construction Account. The Borrower shall hold all moneys advanced to it by RUS hereunder in trust for RUS and shall deposit such moneys promptly after the receipt thereof in a bank or banks which meet the requirements of Section [6.16] of this Agreement. Any account (hereinafter called "Special Construction Account") in which any such moneys shall be deposited shall be designated by the corporate name of the Borrower followed by the words "Trustee, Special Construction Account." Moneys in any Special Construction Account shall be used solely for the construction and operation of the Utility System and, subject to Section [9.14] of this Agreement, may be withdrawn only upon checks, drafts, or orders signed on behalf of the Borrower and countersigned by an executive officer thereof.

Section 5.22. Additional Affirmative Covenants. The Borrower also agrees to comply with any additional affirmative covenant(s) identified in Schedule 1 hereto.

Article VI—Negative Covenants

Section 6.1. General. Unless otherwise agreed to in writing by RUS, while this Agreement is in effect, whether or not any Advance is outstanding hereunder, the Borrower will duly observe each of the negative covenants set forth in this Article.

Section 6.2. Limitations on System Extensions and Additions. The Borrower will not extend or add to its Electric System either by construction or acquisition without the prior written approval of RUS.

Section 6.3. Limitations on Expenses for Legal, Engineering and Supervisory Services. If RUS shall require, the Borrower will not incur any expenses for legal, engineering or supervisory services without the prior written approval of RUS.

Section 6.4. Limitations on Employment and Retention of Manager. At any time any Event of Default, or any occurrence which with the passage of time or giving of notice would be an Event of Default, occurs and is continuing the Borrower will not employ any general manager of the Electric System or any person exercising comparable authority to such a manager unless such employment shall first have been approved by RUS. If any Event of Default, or any occurrence which with the passage of time or giving of notice would be an Event of Default, occurs and is continuing and RUS requests the Borrower to terminate the employment of any such manager or person exercising comparable

authority, or RUS requests the Borrower to terminate any contract for operating the Electric System, the Borrower will do so within thirty (30) days after the date of such notice. All contracts in respect of the employment of any such manager or person exercising comparable authority, or for the operation of the Electric System, shall contain provisions to permit compliance with the foregoing covenants.

Section 6.5. Limitations on Certain Types of Contracts. Without the prior approval of RUS in writing, the Borrower shall not enter into any of the following contracts:

(a) *Construction Contracts.* Any contract for construction or procurement or for architectural and engineering services in connection with its Electric System;

(b) *Large retail power contracts.* Any contract to sell electric power and energy for periods exceeding two (2) years if the kWh sales or kW demand for any year covered by such contract will exceed 25 percent of the Borrower's total kWh sales or maximum kW demand for the year immediately preceding the execution of such contract;

(c) *Wholesale power contracts.* Any contract to sell electric power or energy for resale and any contract to purchase electric power or energy that has a term exceeding two (2) years;

(d) *Power supply arrangements.* Any interconnection agreement, interchange agreement, wheeling agreement, pooling agreement or similar power supply arrangement that has a term exceeding two (2) years;

(e) *System management and maintenance contracts.* Any contract for the management and operation of all or substantially all of its Electric System; or

(f) *Other contracts.* Any contracts of the type described on Schedule 3.

Section 6.6. Limitations on Mergers and Sale, Lease or Transfer of Capital Assets. The Borrower shall not consolidate with, or merge, or sell all or substantially all of its business or assets, to another entity or person except to the extent it is permitted to do so under the Mortgage.

Section 6.7. Limitations on Acquisition, Construction or Procurement of Generating Facilities, Existing Facilities or Utility Systems. The Borrower shall not acquire, construct or procure any generating facilities, existing facilities or utility systems, or portions thereof, without the prior written approval of RUS.

Section 6.8. Limitation on Distributions. Without the prior written approval of RUS, the Borrower shall not in any calendar year make any Distributions (exclusive of any Distributions to the estates of deceased natural patrons) to its members, stockholders or consumers except as follows:

(a) *Equity above 30%.* If, after giving effect to any such Distribution, the Equity of the Borrower will be greater than or equal to 30% of its Total Assets; or

(b) *Equity above 20%.* If, after giving effect to any such Distribution, the aggregate of all Distributions made during the calendar year when added to such Distribution will be less than or equal to 25% of the prior year's margins.

Provided however, that in no event shall the Borrower make any Distributions if there is

unpaid when due any installment of principal of (premium, if any) or interest on its Notes, if the Borrower is otherwise in default hereunder or if, after giving effect to any such Distribution, the Borrower's current and accrued assets would be less than its current and accrued liabilities.

Section 6.9. Limitations on Loans, Investments and Other Obligations. The Borrower shall not make any loan or advance to, or make any investment in, or purchase or make any commitment to purchase any stock, bonds, notes or other securities of, or guaranty, assume or otherwise become obligated or liable with respect to the obligations of, any other person, firm or corporation, except as permitted by the Act and RUS Regulations.

Section 6.10. Depreciation Rates. The Borrower shall not file with or submit for approval of regulatory bodies any proposed depreciation rates which are inconsistent with RUS Regulations.

Section 6.11. Historic Preservation. The Borrower shall not, without approval in writing by RUS, use any Advance to construct any facilities which will involve any district, site, building, structure or object which is included in, or eligible for inclusion in, the National Register of Historic Places maintained by the Secretary of the Interior pursuant to the Historic Sites Act of 1935 and the National Historic Preservation Act of 1966.

Section 6.12. Rate Reductions. The Borrower shall not decrease its rates if it has failed to achieve all of the Coverage Ratios for the calendar year prior to such reduction.

Section 6.13. Limitations on Additional Indebtedness. Except as expressly permitted by Article II of the Mortgage and subject to the further limitations expressed in the next section, the Borrower shall not incur, assume, guarantee or otherwise become liable in respect of any debt for borrowed money and Restricted Rentals (including Subordinated Indebtedness) other than the following: ("Permitted Debt")

(a) Additional Notes issued in compliance with Article II of the Mortgage;

(b) Purchase money indebtedness in non-Utility System property, in an amount not exceeding 10% of Net Utility Plant;

(c) Restricted Rentals in an amount not to exceed 5% of Equity during any 12 consecutive calendar month period;

(d) Unsecured lease obligations incurred in the ordinary course of business except Restricted Rentals;

(e) Unsecured indebtedness for borrowed money, except when the aggregate amount of such indebtedness exceeds 15% of Net Utility Plant and after giving effect to such unsecured indebtedness the Borrower's Equity is less than 30% of its Total Assets;

(f) Debt represented by dividends declared but not paid; and

(g) Subordinated Indebtedness approved by RUS.

PROVIDED, However, that the Borrower may incur Permitted Debt without the consent of RUS only so long as there exists no Event of Default hereunder and there has been no continuing occurrence which with the passage of time and giving of notice could become an Event of Default hereunder.

PROVIDED FURTHER, by executing this Agreement any consent of RUS that the Borrower would otherwise be required to obtain under this Section is hereby deemed to be given or waived by RUS by operation of law to the extent, but only to the extent, that to impose such a requirement of RUS consent would clearly violate federal laws or RUS Regulations.

Section 6.14. Limitations on Issuing Additional Indebtedness Secured Under the Mortgage. (a) The Borrower shall not issue any Additional Notes under the Mortgage without the prior written consent of RUS unless the following additional requirements are met in addition to the requirements set forth in the Mortgage for issuing Additional Notes without the prior consent of any Mortgagee:

(1) the maturity of the loan evidenced by such Notes does not exceed the weighted average of the expected remaining useful lives of the assets being financed;

(2) the principal of the loan evidenced by such Notes is amortized at a rate that will yield a weighted average life that is not greater than the weighted average life that would result from level payments of principal and interest;

(3) the principal of the loan being evidenced by such Notes has a maturity of not less than 5 years; or, in the case of Additional Notes issued to refund or refinance Notes; and

(4) the weighted average life of any such Additional Notes is not greater than the weighted remaining life of the Notes being refinanced.

(b) Any request for consent from RUS under this section, shall be accompanied by a certificate of the Borrower's manager substantially in the form attached to this Agreement as Exhibit C-1 in the case of Notes being issued under Section [2.01] of the Mortgage and C-2 in the case of Notes being issued under Section [2.02] of the Mortgage.

Section 6.15. Impairment of Contracts Pledged to RUS. The Borrower shall not breach any obligation to be paid or performed by the Borrower on any contract, or take any action which is likely to materially impair the value of any contract, which has been pledged as security to RUS by the Borrower or any other entity.

Section 6.16. Limitations on Using non-FDIC Insured Depositories. The Borrower shall not place any Mortgaged Property in the custody of any banking institution or other depository, other than a Mortgagee, unless deposits at such institution are insured by the Federal Deposit Insurance Corporation, or other Federal agency acceptable to RUS. Without the prior written approval of RUS, the Borrower shall not place the proceeds of the Loan or any loan which has been made or guaranteed by RUS in the custody of any bank or other depository that is not insured by the Federal Deposit Insurance Corporation or other federal agency acceptable to RUS.

Section 6.17. Additional Negative Covenants. The Borrower also agrees to comply with any additional negative covenant(s) identified in Schedule 1 hereto.

Article VII—Default

Section 7.1. Events of Default. The following shall be Events of Default under this Agreement:

(a) *Representations and Warranties.* Any representation or warranty made by the Borrower in Article II hereof or any certificate furnished to RUS hereunder shall prove to have been incorrect in any material respect at the time made and shall at the time in question be untrue or incorrect in any material respect and remain uncured;

(b) *Payment.* Default shall be made in the payment of or on account of interest on or principal of the Note when and as the same shall be due and payable, whether by acceleration or otherwise, which shall remain unsatisfied for five (5) Business Days;

(c) *Other Covenants.* Default by the Borrower in the observance or performance of any other covenant or agreement contained in any of the Loan Documents, which shall remain unremedied for 30 calendar days after written notice thereof shall have been given to the Borrower by RUS;

(d) *Corporate Existence.* The Borrower shall forfeit or otherwise be deprived of its corporate charter, franchises, permits, easements, consents or licenses required to carry on any material portion of its business;

(e) *Other Obligations.* Default by the Borrower in the payment of any obligation, whether direct or contingent, for borrowed money or in the performance or observance of the terms of any instrument pursuant to which such obligation was created or securing such obligation;

(f) *Bankruptcy.* A court having jurisdiction in the premises shall enter a decree or order for relief in respect of the Borrower in an involuntary case under any applicable bankruptcy, insolvency or other similar law now or hereafter in effect, or appointing a receiver, liquidator, assignee, custodian, trustee, sequestrator or similar official, or ordering the winding up or liquidation of its affairs, and such decree or order shall remain unstayed and in effect for a period of ninety (90) consecutive days or the Borrower shall commence a voluntary case under any applicable bankruptcy, insolvency or other similar law now or hereafter in effect, or under any such law, or consent to the appointment or taking possession by a receiver, liquidator, assignee, custodian or trustee, of a substantial part of its property, or make any general assignment for the benefit of creditors; and

(g) *Dissolution or Liquidation.* Other than as provided in the immediately preceding subsection, the dissolution or liquidation of the Borrower, or failure by the Borrower promptly to forestall or remove any execution, garnishment or attachment of such consequence as will impair its ability to continue its business or fulfill its obligations and such execution, garnishment or attachment shall not be vacated within 30 days. The term "dissolution or liquidation of the Borrower", as used in this subsection, shall not be construed to include the cessation of the corporate existence of the Borrower resulting either from a merger or consolidation of the Borrower into or with another corporation following a transfer of all or substantially all its assets as an entirety, under the conditions permitting such actions.

Article VIII—Remedies

Section 8.1. Generally. If any of the Events of Default listed in Article VII hereof shall occur after the date of this Agreement and shall not have been remedied, then RUS may pursue all rights and remedies available to RUS that are contemplated by this Agreement or the Mortgage in the manner, upon the conditions, and with the effect provided in this Agreement or the Mortgage, including, but not limited to, a suit for specific performance, injunctive relief or damages. Nothing herein shall limit the right of RUS to pursue all rights and remedies available to a creditor following the occurrence of an Event of Default listed in Article VII hereof. Each right, power and remedy of RUS shall be cumulative and concurrent, and recourse to one or more rights or remedies shall not constitute a waiver of any other right, power or remedy.

Section 8.2. Suspension of Advances. In addition to the rights, powers and remedies referred to in the immediately preceding section, RUS may, in its absolute discretion, suspend making Advances hereunder if (i) any Event of Default, or any occurrence which with the passage of time or giving of notice would be an Event of Default, occurs and is continuing; (ii) there has occurred a change in the business or condition, financial or otherwise, of the Borrower which in the opinion of RUS materially and adversely affects the Borrower's ability to meet its obligations under the Loan Documents, or (iii) RUS is authorized to do so under RUS Regulations.

Article IX—Miscellaneous

Section 9.1. Notices. All notices, requests and other communications provided for herein including, without limitation, any modifications of, or waivers, requests or consents under, this Agreement shall be given or made in writing (including, without limitation, by telecopy) and delivered to the intended recipient at the "Address for Notices" specified below; or, as to any party, at such other address as shall be designated by such party in a notice to each other party. Except as otherwise provided in this Agreement, all such communications shall be deemed to have been duly given when transmitted by telecopy or personally delivered or, in the case of a mailed notice, upon receipt, in each case given or addressed as provided for herein. The Address for Notices of the respective parties are as follows:

Rural Utilities Service, United States
Department of Agriculture, Washington,
DC 20250-1500, Fax: (202) xxxxxxxx
Attention: [Administrator]
The Borrower: The address set forth in
Schedule 1 hereto

Section 9.2. Expenses. To the extent allowed by law, the Borrower will pay all costs and expenses of RUS, including reasonable fees of counsel, incurred in connection with the enforcement of the Loan Documents or with the preparation for such enforcement if RUS has reasonable grounds to believe that such enforcement may be necessary.

Section 9.3. Late Payments. If payment of any amount due hereunder is not received at

the United States Treasury in Washington, DC, or such other location as RUS may designate to the Borrower within five (5) Business Days after the due date thereof or such other time period as RUS may prescribe from time to time in its policies of general application in connection with any late payment charge (such unpaid amount being herein called the "delinquent amount", and the period beginning after such due date until payment of the delinquent amount being herein called the "late-payment period"), the Borrower will pay to RUS, in addition to all other amounts due under the terms of the Note, the Mortgage and this Agreement, any late-payment charge as may be fixed by RUS Regulations from time to time on the delinquent amount for the late-payment period.

Section 9.4. Filing Fees. To the extent permitted by law, the Borrower agrees to pay all expenses of RUS (including the fees and expenses of its counsel) in connection with the filing or recordation of all financing statements and instruments as may be required by RUS in connection with this Agreement, including, without limitation, all documentary stamps, recordation and transfer taxes and other costs and taxes incident to recordation of any document or instrument in connection herewith. Borrower agrees to save harmless and indemnify RUS from and against any liability resulting from the failure to pay any required documentary stamps, recordation and transfer taxes, recording costs, or any other expenses incurred by RUS in connection with this Agreement. The provisions of this subsection shall survive the execution and delivery of this Agreement and the payment of all other amounts due hereunder or due on the Note.

Section 9.5. No Waiver. No failure on the part of RUS to exercise, and no delay in exercising, any right hereunder shall operate as a waiver thereof nor shall any single or partial exercise by RUS of any right hereunder preclude any other or further exercise thereof or the exercise of any other right.

Section 9.6. GOVERNING LAW. EXCEPT TO THE EXTENT GOVERNED BY APPLICABLE FEDERAL LAW, THE LOAN DOCUMENTS SHALL BE DEEMED TO BE GOVERNED BY, AND CONSTRUED IN ACCORDANCE WITH, THE LAWS OF THE STATE [IN WHICH THE BORROWER IS INCORPORATED].

Section 9.7. Holiday Payments. If any payment to be made by the Borrower hereunder shall become due on a day which is not a Business Day, such payment shall be made on the next succeeding Business Day and such extension of time shall be included in computing any interest in respect of such payment.

Section 9.8. Rescission. The Borrower may elect not to borrow all or any portion of the RUS Commitment in which event RUS shall release the Borrower from its obligations hereunder, provided the Borrower complies with such terms and conditions as RUS may impose for such release.

Section 9.9. Successors and Assigns. This Agreement shall be binding upon and inure to the benefit of the Borrower and RUS and their respective successors and assigns,

except that the Borrower may not assign or transfer its rights or obligations hereunder without the prior written consent of RUS.

Section 9.10. Complete Agreement; Amendments. Subject to RUS Regulations, this Agreement and the other Loan Documents are intended by the parties to be a complete and final expression of their agreement. No amendment, modification, or waiver of any provision hereof or thereof, and no consent to any departure of the Borrower herefrom or therefrom, shall be effective unless approved by RUS and contained in either a RUS Regulation or other writing signed by or on behalf of RUS, and then such waiver or consent shall be effective only in the specific instance and for the specific purpose for which given.

Section 9.11. Headings. The headings and sub-headings contained in the titling of this Agreement are intended to be used for convenience only and do not constitute part of this Agreement.

Section 9.12. Severability. If any term, provision or condition, or any part thereof, of this Agreement or the Mortgage shall for any reason be found or held invalid or unenforceable by any governmental agency or court of competent jurisdiction, such invalidity or unenforceability shall not affect the remainder of such term, provision or condition nor any other term, provision or condition, and this Agreement, the Note, and the Mortgage shall survive and be construed as if such invalid or unenforceable term, provision or condition had not been contained therein.

Section 9.13. Right of Setoff. Upon the occurrence and during the continuance of any Event of Default, RUS is hereby authorized at any time and from time to time, without prior notice to the Borrower, to exercise rights of setoff or recoupment and apply any and all amounts held or hereafter held, by RUS or owed to the Borrower or for the credit or account of the Borrower against any and all of the obligations of the Borrower now or hereafter existing hereunder or under the Note. RUS agrees to notify the Borrower promptly after any such setoff or recoupment and the application thereof, provided that the failure to give such notice shall not affect the validity of such setoff, recoupment or application. The rights of RUS under this section are in addition to any other rights and remedies (including other rights of setoff or recoupment) which RUS may have. Borrower waives all rights of setoff, deduction, recoupment or counterclaim.

Section 9.14. Right of RUS to Appoint Supervisor. If the construction of any portion of the Electric System shall not proceed in accordance with the terms of the Loan Documents, RUS may appoint a supervisor (hereinafter called the "Supervisor") for the Electric System. Upon the appointment of a Supervisor, the employment of all superintendents and managers of the Electric System and of all associate and assistant superintendents and managers thereof shall be forthwith terminated. The Borrower shall comply with all reasonable instructions of the Supervisor incident to the carrying out of the obligations of the Borrower hereunder.

Section 9.15. Schedules and Exhibits. Each Schedule and Exhibit attached hereto and

referred to herein is each an integral part of this Agreement.

Section 9.16. Prior Loan Contracts. It is understood and agreed that with respect to all loan agreements previously entered into by and between RUS and the Borrower (hereinafter being referred to as "Prior Loan Contracts") the Borrower shall be required, after the date hereof, to meet affirmative and negative covenants as set forth in this Agreement rather than those set forth in the Prior Loan Contracts. In addition, any remaining obligation of RUS to make additional advances on promissory notes of the Borrower that have been previously delivered to RUS under Prior Loan Contracts shall, after the date hereof, be subject to the conditions set for in this Agreement. In the event of any conflict between any provision set forth in a Prior Loan Contract and any provision in this Agreement, the requirements as set forth in this Agreement shall apply. In the event of any conflict between the provisions set forth in this Agreement and any RUS Regulations now or hereafter in effect from time to time, the RUS Regulations apply. Nothing in this section shall, however, eliminate or modify any special condition, special affirmative covenant or special negative covenant, if any, unless specifically agreed to in writing by RUS.

Section 9.17. Term. This Agreement shall remain in effect until one of the following two events has occurred:

- (a) the Borrower and RUS replace this Agreement with another written agreement or
- (b) all of the Borrower's obligations under the prior loan contracts and this Agreement have been discharged and paid.

IN WITNESS WHEREOF, the parties hereto have caused this Agreement to be duly executed as of the day and year first above written.

(Name of Borrower)

(SEAL)

By _____

President

Attest: _____

Secretary

RURAL UTILITIES SERVICE

By _____

Administrator

Schedule 1

[citations subject to change]

- 1. The purpose of this loan is _____.
- 2. The Mortgage shall mean the Restated Mortgage and Security Agreement, dated as of _____, between the Borrower and RUS, as it may have been or shall be supplemented, amended, consolidated, or restated from time to time.
- 3. The governmental authority referred to in Section [2.1(c)] is _____.
- 4. The exception being taken to the representations in Section [2.1(e)] concerning material compliance with laws is as follows: _____.
- 5. The litigation referred to in Section [2.1(f)] is described as follows: _____.
- 6. The date of the Borrower's financial information referred to in Section [2.1(h)] is _____.

7. The principal place of business of the Borrower referred to in Section [2.1(i)] is _____.

8. All of the property of the Borrower is located in the counties of _____.

9. The subsidiary (or subsidiaries) referred to in Section [2.1(k)] is (are): _____.

10. The Contemporaneous Loan referred to in Section [5.3] is described as follows: _____.

Lender: _____

Amount: _____

Year of Final Maturity: _____

11. The RUS Commitment referred to in the definitions means a loan in the principal amount of \$ _____ which is being made by RUS to the Borrower at the _____ Hardship Rate _____ Municipal Rate (CHECK ONE) pursuant to the Rural Electrification Act and RUS Regulations.

12. Amortization of Advance shall be based upon the method indicated below:

- _____ level principal
- _____ level debt service
- _____ other

13. The SPECIAL condition(s) referred to in Section [4.2] is (are): _____.

14. The additional AFFIRMATIVE covenant(s) referred to in Section [5.22] is (are) as follows: _____.

15. The additional NEGATIVE covenant(s) referred to in Section [6.17] is (are) as follows: _____.

16. The address of the Borrower referred to in Section [9.1].

is _____.

Schedule 2—Existing Liens

The Existing Liens referred to in Section [2.1(g)] are as follows:

[INSERT DESCRIPTION OF EXISTING LIENS, IF ANY, HERE]

Schedule 3—Additional Contracts

The additional contracts referred to in Section [6.5(e)] are described as follows:

[INSERT LIST OF ANY ADDITIONAL CONTRACTS HERE]

Exhibit A—Form of Promissory Note

[INSERT EITHER MUNICIPAL or HARSHIP RATE PROMISSORY NOTE FORM HERE]

Exhibit B—Equal Opportunity Contract Provisions

During the performance of this contract, the contractor agrees as follows:

- (a) The contractor will not discriminate against any employee or applicant for employment because of race, color, religion, sex or national origin. The contractor will take affirmative action to ensure that applicants are employed, and that employees are treated during employment without regard to their race, color, religion, sex or national origin. Such action shall include, but not be limited to the following: employment, upgrading, demotion or transfer, recruitment or recruitment advertising; layoff or termination; rates of pay or other forms of compensation; and selection for training, including apprenticeship. The contractor agrees to post in conspicuous places, available to employees and applicants for employment, notices to be provided setting forth the provisions of this nondiscrimination clause.

(b) The contractor will, in all solicitations or advertisements for employees placed by or on behalf of the contractor, state that all qualified applicants will receive consideration for employment without regard to race, color, religion, sex or national origin.

(c) The contractor will send to each labor union or representative of workers with which he has a collective bargaining agreement or other contract or understanding, a notice to be provided advising the said labor union or workers' representative of the contractor's commitments under this section, and shall post copies of the notice in conspicuous places available to employees and applicants for employment.

(d) The contractor will comply with all provisions of Executive Order 11246 of September 24, 1965, and of the rules, regulations and relevant orders of the Secretary of Labor.

(e) The contractor will furnish all information and reports required by Executive Order 11246 of September 24, 1965, and by the rules, regulations and orders of the Secretary of Labor, or pursuant thereto, and will permit access to his books, records and accounts by the administering agency and the Secretary of Labor for purposes of investigation to ascertain compliances with such rules, regulations and orders.

(f) In the event of the contractor's noncompliance with the non-discrimination clauses of this contract or with any of the said rules, regulations or orders, this contract may be cancelled, terminated or suspended in whole or in part and the contractor may be declared ineligible for further Government contracts or federally assisted construction contracts in accordance with procedures authorized in Executive Order 11246 of September 24, 1965, and such other sanctions may be imposed and remedies invoked as provided in said Executive Order or by rule, regulation or order of the

Secretary of Labor, or as otherwise provided by law.

(g) The contractor will include the provisions of paragraphs (a) through (g) in every subcontract or purchase order unless exempted by rules, regulations or orders of the Secretary of Labor issued pursuant to section 204 of Executive Order 11246, dated September 24, 1965, so that such provisions will be binding upon each subcontractor or vendor. The contractor will take such action with respect to any subcontract or purchase order as the administering agency may direct as a means of enforcing such provisions, including sanctions for noncompliance: Provided, however, that in the event a contractor becomes involved in, or is threatened with, litigation with a subcontractor or vendor as a result of such direction by the agency, the contractor may request the United States to enter into such litigation to protect the interests of the United States.

Exhibit C-1—Manager's Certificate Required Under Loan Contract Section 6.14 for Additional Notes

On behalf of [Name of Borrower] I hereby certify that the Additional Note or Notes to be issued under Section [2.01] of the Mortgage on or about [Date Note or Notes are to be Signed] meet all of the requirements of Section [6.14] of the Loan Contract, namely:

(a) The maturity of the loan evidenced by such Notes (___ years) does not exceed the weighted average of the expected remaining useful lives of the assets being financed (___ years) as evidenced by the attached calculation of said weighted average.

(b) The principal of the loan evidenced by such Notes will either be [check one and provide evidence in the second case]:

___ (1) repaid based on level payments of principal and interest throughout the life of the loan, or

___ (2) amortized at a rate that will yield a weighted average life that is not greater

than the weighted average life that would result from level payments of principal and interest throughout the life of the loan as evidenced by the attached analysis of said weighted average lives.

___ (3) The principal of the loan evidenced by such Notes has a maturity of not less than 5 years.

[Signed] _____
[Dated] _____
[Name] _____
[Title] _____
[Name and Address of Borrower] _____

Exhibit C-2—Manager's Certificate Required Under Loan Contract Section 6.14 for Refinancing Notes

On behalf of [Name of Borrower] I hereby certify that the Additional Note or Notes to be issued under Section [2.02] of the Mortgage on or about [Date Note or Notes are to be Signed] meet the requirement of Section [6.14] of the Loan Contract that the weighted average life of such Notes is not greater than the weighted remaining life of the Notes being refinanced, as evidenced by the attached calculation of said weighted average lives.

[Signed] _____
[Dated] _____
[Name] _____
[Title] _____
[Name and Address of Borrower] _____

Dated: June 29, 1995.

Michael V. Dunn,

Acting Under Secretary, Rural Economic and Community Development.

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