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FARM CREDIT ADMINISTRATION

12 CFR Parts 614 and 617

RIN 3052–AC04

Loan Policies and Operations; Borrower Rights; Effective Interest Rate Disclosure

AGENCY: Farm Credit Administration.

ACTION: Final rule.

SUMMARY: The Farm Credit Administration (FCA, agency, we, or our) issues this final rule amending its regulations governing disclosure of effective interest rates (EIR) and related information on loans. This final rule clarifies when and how qualified lenders must disclose the EIR and other loan information to borrowers; when and how the cost of Farm Credit System (FCS or System) borrower stock must be disclosed to borrowers; and how loan origination charges and other loan information must be disclosed to borrowers. The final rule requires lenders to use a discounted cash flow method in determining the EIR to provide meaningful disclosures to borrowers but does not prescribe detailed calculation procedures. To make the regulations easy to understand and use by borrowers, lenders, and other users, we have rewritten the existing regulations in part 614, subpart K, Disclosure of Loan Information, in a question-and-answer format and moved them to part 617, Borrower Rights.

EFFECTIVE DATE: This regulation will be effective 30 days after publication in the **Federal Register** during which either or both Houses of Congress are in session. We will publish a notice of the effective date in the **Federal Register**.

FOR FURTHER INFORMATION CONTACT:

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SUPPLEMENTARY INFORMATION:

I. Objectives

Our objectives for this rule are to:

- Ensure that borrowers receive meaningful and timely disclosure of the EIR and related information on loans;
- Promote consistency in the method used to determine the EIR; and
- Make the regulations easy to understand and use by borrowers, lenders, and other users.

II. Background

As discussed in the preamble to the proposed rule (*See* 68 FR 5587, February 4, 2003), section 4.13(a) of the Farm Credit Act of 1971, as amended (Act),[1] requires the FCA to enact regulations requiring ''qualified lenders'' [2] to provide borrowers, not later than the time of loan closing, with meaningful and timely disclosure of:

- The current rate of interest on the loan;
- The amount and frequency of interest rate adjustments and the factors that the lender may take into account in adjusting rates for adjustable or variable rate loans;
- The effect of any loan origination charges or purchases of stock or participation certificates on the rate of interest on the loan;
- A statement indicating that stock purchased is at risk; and
- A statement indicating the various types of loan options available to borrowers.

The requirements of section 4.13 of the Act are applicable to all loans made by ''qualified lenders'' not subject to the Truth in Lending Act (TILA).[3] Under section 4.13(a) of the Act, qualified lenders must give borrowers notice of any change in the interest rate applicable to a borrower's loan within a ''reasonable time'' after the change. In addition, section 4.13(b) of the Act requires qualified lenders that offer more than one rate of interest to borrowers, at the request of a borrower, to: (1) Provide a review of the loan to determine if the proper rate has been established; (2) explain to the borrower, in writing, the basis for the interest rate charged; and (3) explain to the borrower, in writing, how the credit status of the borrower may be improved to receive a lower interest rate on the loan.

Current FCA regulations (initially adopted in 1988) implement the disclosure requirements of the Act, but contain limited guidance on several key issues. In recent years, new stock purchase requirements, new loan programs, and varied methodologies for calculation of effective interest rates has meant that compliance with current EIR disclosure regulations has become more challenging and led to inconsistent disclosure among qualified lenders. This final rule rewrites our existing regulations to provide more guidance in a user-friendly format.

The final rule is the second component of our current rulemaking on borrower rights. This final rule amends part 617, Borrower Rights, which was rearranged by the Distressed Loan Restructuring rule adopted by the FCA Board on February 10, 2004, and published in the **Federal Register** on March 9, 2004 (*See* 69 FR 10901). Consequently, part 617 will contain all regulations on borrower rights after both rules become effective.

III. Comments

We received comments on the proposed rule from the Farm Credit Council (Council), two Farm Credit banks, and 10 Farm Credit System associations. In general, commenters expressed support for FCA's efforts to clarify its EIR rules. However, a number of the comments raised general and specific objections to various parts of the proposed rule. FCA's responses to these comments are discussed in our section-by-section analysis below.

In addition to comments on specific proposals, the Council urged FCA, in light of the dramatic change in the nature and extent of System stock purchase requirements since the 1980s, to ''evaluate the benefit (if any) members receive from these disclosures

[1] 12 U.S.C. 2199(a).

[2] ''Qualified lenders'' include System lenders (except for a bank for cooperatives), and non-System lenders (other financing institutions (OFIs)) for loans that OFIs make with funding from a Farm Credit bank. *See* 12 U.S.C. 2202a(a)(6).

[3] 15 U.S.C. 1601, *et seq.* TILA applies to consumer loans and specifically exempts agricultural loans.

in the context of the costs incurred by the associations in making the disclosures and their value to the customers (given the minimal purchase requirements).'' Regardless of FCA's view of the benefit of EIR disclosures, Congress mandated (in section 4.13 of the Act) that qualified lenders make these disclosures. Therefore, FCA has sought, in this rule, to make the required statutory disclosures as meaningful as possible to borrowers without adding unnecessary regulatory burden to qualified lenders.

After carefully considering the comments, we are adopting the final rule as proposed with only one substantive and several technical changes. Specifically, we are deleting proposed § 617.7115(b) and § 617.7130(a)(5), which would have required qualified lenders to separately disclose to borrowers all fees not included in ''loan origination charges'' that borrowers are required to pay to obtain a loan. Also, we are eliminating the proposed definitions of ''loan'' and ''qualified lender'' and other changes to the existing parts 611, 612, 614, and 617 from this rule because they have been implemented by the Distressed Loan Restructuring rule.

IV. FCA's Section-by-Section Response to Comments

Subpart A—General

Section 617.7000—Definitions

One association suggested FCA add a definition for ''covered loan,'' which would establish a maximum dollar amount for loans subject to EIR disclosure regulations. However, section 4.13 of the Act requires lenders to make disclosures to borrowers for ''all loans'' not subject to TILA. We received no other comments on the definitions. As a result, we eliminate the proposed definitions of ''loan'' and ''qualified lender'' from this rule because they have been implemented by the Distressed Loan Restructuring rule and adopt other definitions as proposed.

Subpart B—Disclosure of Effective Interest Rates

Section 617.7100—Who Must Make and Who Is Entitled To Receive an Effective Interest Rate Disclosure?

One Farm Credit bank and six of its affiliated associations objected to proposed § 617.7100(b), which provides what a lender must do when there is more than one borrower obligated on a loan. As explained below, we adopt proposed § 617.7100 as final without change.

Current § 614.4367(d) allows the lender to satisfy the disclosure requirements by providing the disclosure to any one of the primary obligors on the loan. The final rule will give borrowers the opportunity to designate, in writing, the person they wish to receive the disclosures. If the borrowers do not designate a particular recipient, the lender must provide the disclosures to at least one borrower primarily liable for repayment of the loan. The objecting commenters asserted:

(1) There is no basis in the Act authorizing this designation;

(2) The regulation would create an unnecessary burden on System lenders, including requiring lenders to prepare and maintain documentation of the borrowers' designation choice; and

(3) In a default situation, a lender may be unable to locate or contact the designee and, therefore, the regulation could be raised as a legal impediment to a System lender's collection or foreclosure actions.

First, while a strict reading of the Act would require that each borrower receive disclosure, we believe that where there is one loan, allowing disclosure to one borrower complies with the Act and is less burdensome to lenders. We also believe that the proposed rule—giving borrowers an opportunity to designate an EIR disclosure recipient—is consistent with Congress's intent in creating ''borrower rights'' in the Act. Second, we do not believe that the new regulation will be unduly burdensome because all it requires is that qualified lenders honor the borrowers' written designation request, if one is made. Many System associations already allow borrowers to designate an EIR disclosure recipient without reported incident or undue burden. Third, § 617.7100 applies only to EIR disclosures that are primarily made at or before loan closing.

This rule would not apply to any other notices required by the Act or otherwise and therefore has no plausible relationship to a loan default situation. When a qualified lender determines that a loan is, or has become, distressed, provisions in subpart E of part 617 regarding distressed loan restructuring apply. Under § 617.7410(d), the lender must notify all primary obligors. If the obligors identify one party to receive notices, the qualified lender should send the original notice to that person and send copies to the other obligors.

Section 617.7105—When Must a Qualified Lender Disclose the Effective Interest Rate to a Borrower?

Section 617.7105 revises the criteria that establish the circumstances in which EIR disclosure is necessary. Paragraph (b) of this section provides that a qualified lender must provide a new EIR disclosure to existing borrowers on or before the date the borrower:

(1) Executes a new promissory note or other comparable evidence of indebtedness;

(2) Purchases additional stock or participation certificates as a condition of obtaining new funds from the qualified lender; or

(3) Pays an additional loan origination charge to the qualified lender as a condition of obtaining new funds.

The Council commended this clarification and stated that the new rule will benefit System institutions. One association requested that FCA state in the rule or preamble that no new EIR disclosure is required for a ''loan servicing action.'' However, ''loan servicing action'' is not defined in the Act or our regulations, and required disclosure is not based on whether an action is described as a ''loan servicing action.'' Instead, § 617.7105 requires that if any loan action does not result in a new note, purchase of new stock, or new loan origination charges as a condition of obtaining new funds, no new disclosure is required. If it does, new disclosure is required. We believe that proposed § 617.7105 provides clarity to qualified lenders and adopt it as final.

Section 617.7110—How Should a Qualified Lender Disclose the Cost of Borrower Stock or Participation Certificates?

Section 617.7110 provides that the cost of borrower stock or participation certificates must be included in the EIR calculation only at the time the stock or participation certificates is purchased in connection with a loan transaction, whether purchased with cash, included in a promissory note, or otherwise paid. For subsequent loans to existing borrowers, only the cost of new stock or participation certificates, if any, purchased in connection with the transaction must be included in the EIR calculation. We received no comments on this proposed provision and adopt it as final.

Section 617.7115—How Should a Qualified Lender Disclose Loan Origination and Other Charges?

Many commenters commended FCA for clarifying in proposed § 617.7115(a)

exactly what ''loan origination charges'' must be included in the EIR calculation, indicating that the new rule should reduce regulatory burden and result in greater accuracy in reflecting the true cost of credit to the borrower.

We received negative comments from a Farm Credit bank and a number of associations on proposed § 617.7115(b), which provides that all other payments that a borrower is required to make to obtain a loan, but not included as a loan origination charge in the EIR calculation, must be disclosed separately at the time of loan closing. Objections to the proposal included:

(1) Requiring a separate list of all fees not included as loan origination charges in the EIR calculation goes far beyond FCA's authority;

(2) The new rule would mirror TILA and Regulation Z [4] requirements, which are not applicable to agricultural loans;

(3) Developing a new automated form to include these items would be costly to implement;

(4) A lender may have no knowledge of certain amounts a borrower pays directly to third parties for items such as taxes or insurance.

Upon consideration of the comments, we are deleting the proposed requirements of §§ 617.7115(b) and 617.7130(a)(5).

Section 4.13(a)(3) of the Act requires qualified lenders to disclose the effect of ''loan origination charges'' on the effective rate of interest. Proposed § 617.7115(a) identified what ''loan origination charges'' must be disclosed for purposes of implementing section 4.13(a)(3). The Act does not specifically require disclosure of any other fees or costs not constituting ''loan origination charges.'' Additionally, as we discussed in the preamble to the proposed rule, Congress specifically exempted agricultural loans from TILA coverage and its more extensive disclosure requirements. For these reasons, we are eliminating proposed paragraph (b) of this section in order to avoid adding unnecessary regulatory burden to qualified lenders.

However, while we are not imposing this additional disclosure as a requirement, we continue to believe, as one association commenter stated, ''disclosure of such fees at or prior to loan closing is sound lending practice.'' This is particularly true for inexperienced borrowers, such as beginning farmers. Therefore, we encourage additional voluntary disclosure by qualified lenders in loan transactions.

[4] Federal Reserve Board regulation that implements TILA.

Section 617.7120—How Should a Qualified Lender Present the Disclosures to a Borrower?

Proposed § 617.7120 was intended to provide reasonable assurance that qualified lenders provide user-friendly, meaningful disclosures to borrowers. We received no comments on proposed § 617.7120 and adopt it as final.

Section 617.7125—How Should a Qualified Lender Determine the Effective Interest Rate?

One association objected to the requirement of § 617.7125(a) that the EIR be calculated using a discounted cash flow methodology. That association asserted:

(1) This is an inappropriate TILA-style requirement;

(2) This will impose an increased burden since there are a variety of payment schedules employed to accommodate borrowers' agricultural needs and non-FCS lenders do not have such a requirement.

As we discussed in the preamble to the proposed rule, while the proposal is conceptually similar to the formula prescribed in Regulation Z for determination of the annual percentage rate (APR) on loans subject to TILA, a discounted cash flow is also the standard accepted methodology used in the financial services industry as the best measurement of the cost of credit over time and to develop loan amortization schedules. As we also noted in the proposed rule preamble, although the discounted cash flow method involves somewhat complex mathematical computations, the FCA does not believe a requirement to use this method would cause undue burden to lenders. A survey of System lender disclosures we conducted in the spring of 2002 indicated that a substantial majority (more than 80 percent) of FCS lenders have already incorporated discounted cash flows in their EIR calculations. In addition, a variety of computer-based tools for calculating effective interest rates are readily available in the market place at a reasonable cost.

Additionally, another association requested that we add a provision establishing a tolerance level—similar to the Regulation Z provision—for the accuracy of the EIR disclosure. Regulation Z provides that an annual percentage rate is considered accurate (and the lender is not in violation of Regulation Z) if the rate disclosed is within a tolerance level. We considered, but rejected, that approach because, unlike Regulation Z, our rules provide for flexibility in calculating the EIR. FCA believes that the complexity of agricultural lending requires a more flexible disclosure approach than provided for under Regulation Z. Therefore, instead of a fixed formula mandated by FCA, we provide in § 617.7125(c) that lenders must establish policies and procedures for disclosing the effect of the cost of borrower stock (or participation certificates) and loan origination charges on the interest rate of a loan. Qualified lenders will also be required to establish policies and procedures for determining the major assumptions used in calculating the EIR, such as for calculating the EIR for adjustable rate loans, revolving or open-end lines of credit, or other loans where key terms may vary or may not be fixed. The rule places responsibility on a qualified lender to use due diligence in calculating the EIR. Redisclosure would only be necessary if a lender made a material error in the original calculation.

A third association opposed the requirement that the cost of the required stock purchase be included as a ''borrowing expense'' with no assumption of retirement at loan payoff allowed in the calculation of the EIR, stating that the risk of loss of stock is extremely minimal and to ''make the assumption that stock will not be recovered is to raise unfounded concern on the part of the borrower that such loss is anticipated.'' While the commenter may be factually correct in asserting that the borrower's risk of loss of stock is minimal, we believe the Act requires this result.

Congress provided in section 4.13(a)(3) of the Act that the purchase of borrower stock must be disclosed as a cost of the credit in determining the effective rate of interest on a loan. In other parts of the Act, Congress further provided that borrower stock is an ''at-risk'' equity investment. Assumption of stock retirement in the EIR calculation is contrary to the at-risk feature of borrower stock. While purchase of stock is a prerequisite for obtaining a loan, section 4.3A of the Act [5] precludes automatic retirement of borrower stock upon loan payoff. Therefore, a qualified lender cannot explicitly or implicitly guarantee or assume stock retirement.

One association also objected to the requirement of proposed § 617.7125(c) that qualified lenders must develop policies and procedures establishing criteria on how the cost of borrower stock and loan origination charges are assigned among multiple loans obtained simultaneously. The association asserts that the requirement will be

[5] 12 U.S.C. 2154a.

burdensome and limits the association's flexibility. However, we believe that policies and procedures establishing criteria are necessary to ensure fairness and consistency in disclosure to borrowers and to prevent misleading information. We continue to believe that the proposed rule will allow an association to adopt policies and procedures broad enough to allow some discretion and flexibility on a case-by-case basis. For all the reasons discussed above, we adopt proposed § 617.7125 as final with one conforming change to reference § 617.7115 in paragraph (b)(3) of this section.

Section 617.7130—What Initial Disclosures Must a Qualified Lender Make to a Borrower?

As discussed in the preamble to the proposed rule, the Council previously stated that existing § 614.4367(a)(3), which requires the computation of EIR to be made on a transaction-specific basis, goes beyond the requirement of § 4.13(a)(3) of the Act. The Council made the same comment about proposed § 617.7130 (which keeps the existing requirement), stating that the statutory requirement could be satisfied by using a representative example based on a generic transaction and recommended that FCA allow disclosure through the use of a standard example.

As we stated in the proposed rule preamble (and in all prior rulemakings in this area), we disagree with this approach and believe that in order for borrower disclosure to be ''meaningful,'' as is required by statute, the disclosure should take into account the specific loan for which the disclosure is being provided. The EIR disclosed should be derived from the interest rate and related charges applicable to the loan being made to the borrower. However, for adjustable or revolving loans where the terms and conditions are not fixed or are subject to change, a disclosure of the EIR based on the terms and conditions known at the inception of the loan, coupled with representative examples showing the effect of changes in any of the cost elements of the loan, *e.g.*, borrower stock, loan origination charges, or interest rate, on the EIR would be appropriate under the circumstances. We received no other comments on proposed § 617.7130 and adopt it as final with only one change to remove proposed paragraph (a)(5) of this section in conformance with the change to proposed § 617.7115.

Section 617.7135—What Subsequent Disclosures Must a Qualified Lender Make to a Borrower?

As discussed in the proposed rule preamble, the Council recommended that where an interest rate is based on a widely publicized external index plus a spread, disclosure of a change of interest rate should not be required when the index changes but should be required only when the change in rate is caused by a change in the spread. The Council, a Farm Credit bank, and five associations also reiterated this position in their comments on proposed rule § 617.7135. However, as we discussed in the earlier preamble, we believe eliminating the notice of interest rate changes for index rate loans is not appropriate. The Act requires notice of ''any change in the interest rate applicable to the borrower's loan.''[6] While the contract rate (index plus spread) may not have changed, it is clear that when the index changes, the rate of interest the borrower pays on the loan has changed. There is nothing in the legislative history of the Act to suggest that Congress intended to exempt index rate loans from the disclosure requirement. Furthermore, we believe it is important to remind borrowers that interest rate changes will affect their payment amounts.

In the preamble to the proposed rule, we indicated that any form of correspondence to borrowers could satisfy the required written notice, including a newsletter. The Council urged FCA to specifically authorize that any required disclosure may be made on a System institution's Web site or by calling a telephone information line. While sending an e-mail to an individual borrower (in compliance with any applicable e-commerce requirement, including the parties' agreement) would satisfy the notice requirement of this section, we do not believe posting information on a Web site or telephone information line would satisfy statutory requirements. The Act requires that qualified lenders provide ''notice to the borrower'' of a change in the borrower's interest rate.[7] However, a ''widely publicized external index'' does not provide notice directly to a borrower, and information available to borrowers on the Web or by telephone does not provide such notice. For these reasons, we adopt § 617.7135 as final without change.

[6] 12 U.S.C. 2199(a)(4).

[7] 12 U.S.C. 2199(a)(4).

Subpart C—Disclosure of Differential Interest Rates

Section 617.7200—What Disclosures Must a Qualified Lender Make to a Borrower on Loans Offered With More Than One Rate of Interest?

We did not receive any comments on this section and adopt it as final.

V. Regulatory Flexibility Act

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

List of Subjects

12 CFR Part 614

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

12 CFR Part 617

Banks, banking, Criminal referrals, Criminal transactions, Embezzlement, Insider abuse, Investigations, Money laundering, Theft.

■ For the reasons stated in the preamble, parts 614 and 617 of chapter VI, title 12 of the Code of Federal Regulations, are amended as follows:

PART 614—LOAN POLICIES AND OPERATIONS

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

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

Subpart K—[Removed]

■ 2. Remove subpart K, consisting of §§ 614.4365 through 614.4368.

PART 617—BORROWER RIGHTS

■ 3. The authority citation for part 617 continues to read as follows:

Authority: Secs. 4.13, 4.13A, 4.13B, 4.14, 4.14A, 4.14C, 4.14D, 4.14E, 4.36, 5.9, 5.17 of the Farm Credit Act (12 U.S.C. 2199, 2200, 2201, 2202, 2202a, 2202c, 2202d, 2202e, 2219a, 2243, 2252(a)(9)).

Subpart A—General

■ 4. Amend § 617.7000 by adding the following definitions alphabetically to read as follows:

§ 617.7000 Definitions.

* * * * *

Adjustable rate loan means a loan where the interest rate payable over the term of the loan may change. This includes adjustable rate, variable rate, or other similarly designated loans.

Effective interest rate means a measure of the cost of credit, expressed as an annual percentage rate, that shows the effect of the following costs, if any, on the interest rate on a loan charged by a qualified lender to a borrower:

(1) The amount of any stock or participation certificates that a borrower is required to buy to obtain the loan; and

(2) Any loan origination charges paid by a borrower to a qualified lender to obtain the loan.

Interest rate means the stated contract rate of interest.

* * * * *

■ 5. Amend part 617 by adding new subparts B and C to read as follows:

Subpart B—Disclosure of Effective Interest Rates

Sec.

617.7100 Who must make and who is entitled to receive an effective interest rate disclosure?
617.7105 When must a qualified lender disclose the effective interest rate to a borrower?
617.7110 How should a qualified lender disclose the cost of borrower stock or participation certificates?
617.7115 How should a qualified lender disclose loan origination charges?
617.7120 How should a qualified lender present the disclosures to a borrower?
617.7125 How should a qualified lender determine the effective interest rate?
617.7130 What initial disclosures must a qualified lender make to a borrower?
617.7135 What subsequent disclosures must a qualified lender make to a borrower?

Subpart B—Disclosure of Effective Interest Rates

§ 617.7100 Who must make and who is entitled to receive an effective interest rate disclosure?

(a) A qualified lender must make the disclosures required by subparts B and C of this part to borrowers for all loans not subject to the Truth in Lending Act.

(b) For a single loan involving more than one borrower, a qualified lender is required to provide only one set of disclosures to borrowers. All borrowers may designate, in writing, one person who will receive the effective interest rate disclosure. If the borrowers do not designate a particular recipient, the lender may provide the disclosure to at least one of the borrowers who is primarily liable for repayment of the loan.

§ 617.7105 When must a qualified lender disclose the effective interest rate to a borrower?

(a) *Disclosure to prospective borrowers.* A qualified lender must provide written effective interest rate disclosure for each loan no later than the time of loan closing.

(b) *Disclosure to existing borrowers.*

(1) A qualified lender must provide a new effective interest rate disclosure to an existing borrower on or before the date:

(i) The borrower executes a new promissory note or other comparable evidence of indebtedness;

(ii) The borrower purchases additional stock or participation certificates as a condition of obtaining new funds from the qualified lender; or

(iii) The borrower pays an additional loan origination charge to the qualified lender as a condition of obtaining new funds.

(2) A qualified lender is not required to provide a new effective interest rate disclosure when it advances new funds to an existing borrower if none of the conditions of paragraph (b)(1) of this section apply and the advance is made pursuant to a preexisting contract that specifically provides for future advances.

§ 617.7110 How should a qualified lender disclose the cost of borrower stock or participation certificates?

The cost of borrower stock or participation certificates must be included in the effective interest rate calculation at the time the stock or participation certificate is purchased in connection with a loan transaction. For subsequent loans to existing borrowers, only the cost of new stock or participation certificates, if any, purchased in connection with a new loan or advance of new funds must be included in the effective interest rate calculation for the transaction.

§ 617.7115 How should a qualified lender disclose loan origination charges?

Any one-time charge paid by a borrower to a qualified lender in consideration for making a loan must be included in the effective interest rate as a loan origination charge. These include, but are not limited to, loan origination fees, application fees, and conversion fees. Loan origination charges also include any payments made by a borrower to a qualified lender to reduce the interest rate that would otherwise be charged, including any charges designated as ''points.''

§ 617.7120 How should a qualified lender present the disclosures to a borrower?

A qualified lender must:

(a) Disclose the effective interest rate and other information required by subparts B and C of this part clearly and conspicuously in writing, in a form that is easy to read and understand and that the borrower may keep; and

(b) Not combine the disclosures with any information not directly related to the information required by §§ 617.7130 and 617.7135.

§ 617.7125 How should a qualified lender determine the effective interest rate?

(a) A qualified lender must calculate the effective interest rate on a loan using the discounted cash flow method showing the effect of the time value of money.

(b) For all loans, the cash flow stream used for calculating the effective interest rate of a loan must include:

(1) Principal and interest;

(2) The cost of stock or participation certificates that a borrower is required to purchase in connection with the loan; and

(3) Loan origination charges described in § 617.7115.

(c) A qualified lender must establish policies and procedures for EIR disclosures that clearly show the effect of the cost of borrower stock (or participation certificates) and loan origination charges on the interest rate of a loan. A qualified lender must also establish policies and procedures for determining major assumptions used in calculating the effective interest rate, *e.g.,* criteria on how the cost of borrower stock (or participation certificates) and loan origination charges are assigned or allocated among multiple loans obtained by a borrower simultaneously.

§ 617.7130 What initial disclosures must a qualified lender make to a borrower?

(a) *Required disclosures—in general.* A qualified lender must disclose in writing:

(1) The interest rate on the loan;

(2) The effective interest rate of the loan;

(3) The amount of stock or participation certificates that a borrower is required to purchase in connection with the loan and included in the calculation of the effective interest rate of the loan;

(4) All loan origination charges included in the effective interest rate;

(5) That stock or participation certificates that borrowers are required to purchase are at risk and may only be retired at the discretion of the board of the institution; and

(6) The various types of loan options available to borrowers, with an explanation of the terms and borrower rights that apply to each type of loan.

(b) *Adjustable rate loans.* A lender must provide the following information for adjustable rate loans in addition to the requirements of paragraph (a) of this section:

(1) The circumstances under which the rate can be adjusted;

(2) How much the rate can be adjusted at any one time and how much the rate can be adjusted during the term of the loan;

(3) How often the rate can be adjusted;

(4) Any limitations on the amount or frequency of adjustments; and

(5) The specific factors that the qualified lender may take into account in making adjustments to the interest rate on the loan.

§ 617.7135 What subsequent disclosures must a qualified lender make to a borrower?

(a) *Notice of interest rate change.*

(1) A qualified lender must provide written notice to a borrower of any change in interest rate on the borrower's existing loan, containing the following information:

(i) The new interest rate on the loan;

(ii) The date on which the new rate is effective; and

(iii) The factors used to adjust the interest rate on the loan.

(2) If the borrower's interest rate is directly tied to a widely publicized external index, a qualified lender must provide written notice to the borrower of the rate change within forty-five (45) days after the effective date of the change.

(3) If the borrower's interest rate is not directly tied to a widely publicized external index, a qualified lender must send written notice to the borrower of the rate change within ten (10) days after the effective date of the change.

(b) *Notice of increase in stock purchase requirement.* If a qualified lender increases the amount of stock (or participation certificates) a borrower must own during the term of a loan, the lender must send a written notice to the borrower at least ten (10) days prior to the effective date of the increase. The notice must state:

(1) The new effective interest rate on the outstanding balance for the remaining term of the borrower's loan;

(2) The date on which the new rate is effective; and

(3) The reason for the increase in the borrower stock (or participation certificates) purchase requirement.

Subpart C—Disclosure of Differential Interest Rates

Sec.

617.7200 What disclosures must a qualified lender make to a borrower on loans offered with more than one rate of interest?

Subpart C—Disclosure of Differential Interest Rates

§ 617.7200 What disclosures must a qualified lender make to a borrower on loans offered with more than one rate of interest?

A qualified lender that offers more than one rate of interest to borrowers must notify each borrower of the right to request a review of the interest rate charged on his or her loan no later than the time of loan closing. At the request of a borrower, the lender must:

(a) Provide a review of the loan to determine if the proper interest rate has been established;

(b) Explain to the borrower in writing the basis for the interest rate charged; and

(c) Explain to the borrower in writing how the credit status of the borrower may be improved to receive a lower interest rate on the loan.

Dated: March 23, 2004.

Jeanette C. Brinkley,

Secretary, Farm Credit Administration Board.

[FR Doc. 04–6968 Filed 3–29–04; 8:45 am]

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FARM CREDIT ADMINISTRATION

12 CFR Parts 614, 620, 630

RIN 3052–AC07

Loan Policies and Operations; Disclosure to Shareholders; Disclosure to Investors in Systemwide and Consolidated Bank Debt Obligations of the Farm Credit System

AGENCY: Farm Credit Administration.

ACTION: Final rule.

SUMMARY: The Farm Credit Administration (FCA, agency, we, or our) issues this final rule amending our regulations governing the Farm Credit System's (System) mission to provide sound and constructive credit and services to young, beginning, and small farmers and ranchers and producers or harvesters of aquatic products (YBS farmers and ranchers or YBS). Additionally, with this final rule, the agency amends the System's disclosure to shareholders and investors to include reporting on its service to YBS farmers and ranchers.

EFFECTIVE DATE: This regulation will be effective 30 days after publication in the **Federal Register** during which either or both Houses of Congress are in session. We will publish a notice of the effective date in the **Federal Register**.

FOR FURTHER INFORMATION CONTACT: Robert E. Donnelly, Senior Accountant, Office of Policy and Analysis, Farm Credit Administration, McLean, VA 22102–5090, (703) 883–4498, TTY (703) 883–4434,

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SUPPLEMENTARY INFORMATION:

I. Objective

The objective of this rule is to ensure that the System provides sound and constructive credit and services [1] to YBS farmers and ranchers.[2] To accomplish this objective, the rule amends our existing regulations to provide:

1. Clear, meaningful, and results-oriented guidelines for System YBS policies and programs; and

2. Enhanced reporting and disclosure to the public on the System's performance and compliance with its statutory YBS mission (YBS mission or mission).

Through these amendments, the public will be better able to measure the

[1] The term ''services'' includes leases and related services to YBS farmers and ranchers.

[2] The Farm Credit Act of 1971 (1971 Act) gave the production credit associations and the banks for cooperatives the authority to finance ''producers or harvesters of aquatic products'' in addition to financing ''farmers and ranchers.'' The 1980 amendments to the 1971 Act gave the Federal land banks expanded authority to finance ''producers or harvesters of aquatic products'' and put such producers and harvesters on the same footing as ''farmers and ranchers.'' Thus, in accordance with the amendments to the 1971 Act, whenever we refer to ''YBS farmers and ranchers'' or ''YBS borrowers'' in this rule, we are including ''producers or harvesters of aquatic products.''