UNITED STATES DEPARTMENT OF AGRICULTURE
Farm Service Agency
Washington, DC 20250

Notice FLP-745

2-FLP

For: State and County Offices

Guaranteed Loan Narrative Q&A's

Approved by: Deputy Administrator, Farm Loan Programs

1 Overview

A Background

The Loan Making Division (LMD), Guaranteed Loan Branch conducted online webinar sessions regarding loan narratives used by FSA's guaranteed lenders in May 2016. Each webinar session reviewed the necessary content of loan narratives to provide for more consistency within this aspect of guaranteed loan applications. Questions were submitted by participants of each session. The questions, and their respective answers, from all of the sessions have been compiled in this notice.

B Purpose

This notice provides questions and answers from all of the Guaranteed Loan Narrative webinar sessions.

C Contact

If there are questions about this notice:

- lenders may contact their local County Office or State Office
- County Offices shall contact their State Office
- State Offices shall contact Matt Henderson, LMD, Guaranteed Loan Branch, by either of the following:
  - e-mail to **matthew.henderson2@wdc.usda.gov**
  - telephone at 202-720-5847.

Disposal Date	**Distribution**
June 1, 2017	State Offices; State Offices relay to County Offices

2 Action

A State Office Action

The National Office will distribute this notice to guaranteed lenders via GovDelivery.

State Offices shall:

- distribute this notice to guaranteed lenders in their State
- ensure that all FSA employees with loan approval authority have reviewed this notice and are reviewing guaranteed loan narratives according to this guidance, as appropriate.

B County Office Action

County Office staff with loan approval authority shall review this notice and review guaranteed loan narratives according to this guidance, as appropriate.

Guaranteed Loan Narrative Webinars Q&A's

The following questions and answers were compiled from all sessions of FSA's Guaranteed Loan Narrative Refresher Webinar conducted in May 2016.

Q 1: Why are tax ID numbers needed in the narrative when there are places for those items to be provided on the application form?

A 1: There is limited space on the application form for tax ID numbers. If there are more entity members or co-applicants than there are spaces available on the application form, the tax ID number needs to be included in the loan narrative.

Also, the loan narrative should be used to provide information about the entity members including ownership shares as well as a description of the responsibilities of each member. See 2-FLP, subparagraph 66 I for more information.

Q 2: What additional information is needed in the lender's narrative when the loan purpose is to refinance debt already incurred?

A 2: If a lender is refinancing their own debt, the loan narrative needs to address several points. First, it must explain how the refinancing benefits the applicant. The purpose of the guarantee can't be simply to transfer the risk of a loss over to the government. The lender needs to explain how the refinancing is in the applicant's best interest and will improve the applicant's financial position.

FSA can only refinance debt incurred for an authorized loan purpose. Therefore, the narrative must explain what the original debt was used for.

Additionally, if the debt being refinanced has an existing FSA guarantee, the lender must explain why the various restructuring and servicing options weren't utilized. FSA requires that lenders utilize servicing options in these scenarios as much as possible. Consequently, in order to justify a guaranteed loan for this purpose, the lender must explain why servicing the existing guaranteed loans does not provide the same benefit to the applicant.

See 2-FLP, subparagraphs 122 B, 122 E, 123 B, and 152 H for more detail.

Q 3: Should nonessential assets be addressed in the loan narrative?

A 3: Nonessential assets must be considered by FSA officials when reviewing an applicant's ability to obtain credit without a guarantee. If nonessential assets exist, the lender should address and explain what those assets are so that FSA can determine how the eligibility requirements apply in each situation. A nonessential asset is an asset which does not contribute to the farm operation or the payment of other living expenses. An example of such an asset would be a vacation home owned by an applicant who does not use it as a primary residence and does not generate essential family living income from it.

See 2-FLP, subparagraph 108 J and Exhibit 2 for more information.

Guaranteed Loan Narrative Webinars Q&A's (Continued)

Q 4: Should livestock numbers be addressed in the loan narrative?

A 4: Yes. If an applicant has any kind of livestock operation, the details of such, including livestock numbers, should be addressed in the loan narrative. This is important so that FSA can evaluate the size and scope of the operation. Additionally, this information is needed to determine what level of environmental review may be necessary.

See 2-FLP, subparagraph 66 C and 208 F for more detail.

Q 5: Is there a known correlation between the length of a guaranteed loan narrative and the default rate of FSA loans?

A 5: The National Office has not conducted such a study. The primary concern is the quality of the content within the narrative. It is more likely the default rate will correlate to the quality of the analysis and narrative; and the length of the narrative will correlate to the complexity of the farm operation and loan request.

Q 6: Should risk based pricing practices be addressed in the loan narrative?

A 6: If a lender uses risk based pricing practices, FSA regulations require that a guaranteed loan applicant receive an interest rate one tier better than they would receive without the guarantee. This should be addressed in the section where the lender describes the loan purposes and the proposed rates and terms so FSA can ensure that the lender's proposal is in compliance with the regulations.

If a lender does not use risk based pricing practices, the narrative should state what the proposed rate will be.

See 2-FLP, subparagraph 66 C and paragraph 135 for more detail.

Q 7: Does the "no agency loss" eligibility requirement apply to direct loans, guaranteed loans, or both?

A 7: The "no agency loss" eligibility requirement applies to both direct and guaranteed loans. If a loan applicant has indicated that they cannot certify that they have not caused the Agency a loss, the lender should contact FSA before proceeding. FSA can then verify if a loss to the Agency has occurred that would render the applicant ineligible.

See 2-FLP, subparagraph 108 C for more information.

Guaranteed Loan Narrative Webinars Q&A's (Continued)

Q 8: How old of an appraisal does FSA accept as "current"?

A 8: FSA regulations state that an appraisal, chattel or real estate, must be no more than 12 months old to be considered current. However, if the market conditions have remained stable or improved; the property remains in the same or better condition; and the value of the property has remained the same or increased, FSA may allow a real estate appraisal older than 12 months to be used. FSA would recommend that use of a real estate appraisal over 12 months be discussed with the local FSA loan official.

See 2-FLP, subparagraphs 182 A and 183 B for more information.

Q 9: **Is it acceptable to use form FSA-2006 "Property Owned and Leased" to provide the location of all farmed land?**

A 9: Yes, lenders may use this form to provide the location of all farmed land rather than writing it out in the loan narrative. If a lender decides to utilize this form, they should note in the narrative that the FSA loan official should see the attached form for the location of the farmed land.

Q 10: Do all of the applicant eligibility criteria need to be restated in the loan narrative when they are certified to on the application form?

A 10: For the most part, lenders do not need to restate eligibility. There are only three main eligibility criteria that need to be expanded upon in the narrative: the test for credit or the applicant's inability to obtain the loan without the guarantee, the applicant's credit history, and the applicant's status as a qualified alien (if the applicant is not a U.S. Citizen). First, the lender needs to give an explanation of the specific reason(s) the loan could not be made without the guarantee. Second, the lender needs to address and analyze the acceptability of the applicant's credit history (more than just providing the credit score). Finally, if the applicant is not a U.S. citizen, the lender needs to explain what status the applicant holds as a qualified alien so that FSA can determine if they are eligible for a guaranteed loan.

See 2-FLP, paragraph 108 for more detail.

Q 11: The checklist for SEL and CLP lenders requires the lender to provide the proposed loan agreement and a plan for servicing. What specifically is required for these items?

A 11: The proposed loan agreement includes an explanation of any proposed atypical conditions the applicant will need to agree to obtain the loan requested. With regard to a servicing plan, the lender needs to explain to FSA how the lender plans to conduct routine servicing activities such as security inspections, farm visits, annual analyses, collection of income and expenses, collection of tax returns, etc.

See 2-FLP, paragraphs 66, 67, and part 11 for more detail.

Guaranteed Loan Narrative Webinars Q&A's (Continued)

Q 12: In what scenarios should "typical" cash flow projections be used?

A 12: Typical cash flow projections should be used in scenarios where the cash flow in the first year will not be representative of a normal operating cycle. This could be caused by several circumstances such as a new operation starting up, recovery from a natural disaster, recovery from an economic reversal, etc.

In these situations, the narrative needs to address why a typical plan was used, what is different about the typical plan compared to the first year, what the lender is doing to help the applicant reach the typical year (interest only payments, deferrals, etc.), and how a structure such as this will help the applicant succeed.

See 2-FLP, Exhibit 2 for more information.

Q 13: What is the benefit for a Standard Eligible Lender (SEL) to become a Preferred Lender (PLP)?

A 13: With the PLP, FSA's trusts its most experienced lenders to manage their agricultural lending activities using their own policies and procedures. The major benefit is the lender does not need to keep track of separate application, underwriting, and servicing rules – they can originate and service guaranteed loans in much the same way they do any other loan in their portfolio.

PLP lenders collect the same documentation and apply the same underwriting standards for all their loans. They can also perform many of the same routine servicing activities and have more flexibility in handling such things as partial releases, additional loans, emergency advances, and defaulted loans.

Further benefits to PLP status are an abbreviated application and faster approval time. PLP lenders are typically only required to submit an application form and loan narrative. In return, PLP lenders can expect FSA to make an approval decision a within 14 days (in most situations much faster) or the application will be automatically approved.

See 2-FLP paragraphs 52 through 54 for more detail.

Guaranteed Loan Narrative Webinars Q&A's (Continued)

Q 14: How much environmental information needs to be included in a loan narrative?

A 14: At minimum, the lender needs to answer the environmental questions on the application form and provide a description of the loan purpose(s) and farming operation. If the lender believes that an advanced level of environmental review is necessary, they should contact the local FSA office.

Loans for building construction and large livestock operations typically require a more in-depth level of environmental assessment. In those cases, the lender will work closely with the local FSA staff throughout the process. All narratives should include a discussion of any potential problems detected during due diligence farm visit.

See 1-EQ and 2-FLP, paragraphs 70 and 208 for more information.

Note: Environmental questions and answers here are subject to change based on forthcoming revisions of FSA's environmental quality handbooks.

Q 15: How does a lender know if an approved guaranteed loan application has been funded?

A 15: The lender and loan applicant are notified of the approval decision in writing. If the loan has been funded, FSA-2232 "Conditional Commitment" will be included with the approval notification.

If funding is not available, the notification will indicate the request has been approved subject to the availability of funds along with instruction to the lender that the loan should not be closed until they receive the Conditional Commitment.

See 2-FLP, subparagraph 244 C for more detail.

Guaranteed Loan Narrative Webinars Q&A's (Continued)

Q 16: Are balloon payments acceptable for an FSA guaranteed loan?

A 16: Balloon payments are acceptable for Guaranteed FO and OL loans if the following conditions are met:

- the extended repayment schedule is necessary to accomplish a specific goal, such as establishing a new enterprise, developing a farm, or recovering from an economic reversal
- the loan will have adequate collateral at the time the balloon installment comes due
- the borrower is projected to be able to refinance the remaining debt at the time the balloon payment comes due based on the expected financial condition of the operation, the depreciated value of the collateral, and the principal balance on the loan.

FSA expects the lender's loan narrative to provide supporting assumptions describing how the projected collateral value was determined. Some consideration may be given to replacement of collateral over time if the borrower has a history of replacing breeding livestock or upgrading equipment assuming the cash flow includes adequate capital asset replacement funds.

See 2-FLP, subparagraph 137 F for more detail.