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Cooperative Finance Corporation

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A Touchstone Energy® Cooperative

June 21, 2011

Office of the Comptroller of the Currency
Board of Governors of the Federal Reserve System
Federal Deposit Insurance Corporation
Securities and Exchange Commission
Federal Housing Finance Agency

Re: Credit Risk Retention
RIN 1557-AD40, 7100-AD70, 3064-AD74, 3235-AK96, 2590-AA43

A New Category of "Rural Electric Utility Loans" Should Be Created and Should Be Subject to Discrete Underwriting Criteria to Be Considered "Qualified Assets"

The National Rural Utilities Cooperative Finance Corporation (CFC) appreciates this opportunity to provide these comments on the Credit Risk Retention proposal issued jointly by the Federal Reserve Board, the Office of the Comptroller of the Currency, the Federal Deposit Insurance Corporation, the Securities and Exchange Commission, the Federal Housing Finance Agency, and the Department of Housing and Urban Development (collectively, the Agencies).

CFC is a nonprofit cooperative wholly owned by America's consumer-owned rural electric cooperatives (RECs). We were created by those RECs in 1969 to provide them with financing.

We provide business-purpose loans to the RECs to finance their provision of electric service to residents of rural America. We are the largest non-governmental lender to RECs. While we do not actively organize or initiate securitizations, we do sell whole loans to buyers such as the Federal Agricultural Mortgage Corporation (Farmer Mac), and these whole loans may later be securitized into asset-backed securities (ABS). We therefore could fall within the definition of "originator" in the Agencies' proposed rule. The proposal would require sponsors of ABS to retain at least 5 percent of the credit risk of the assets underlying the securities, except where the ABS are collateralized exclusively by "qualified assets" – loans meeting specified underwriting criteria designed to ensure the loans are very low-risk. In certain circumstances, the sponsor could allocate its risk retention obligations to the originator.

CFC understands the need to ensure that credit risk is prudently managed in loans that are securitized into ABS, and managing credit risk is always a major focus of our lending activities. We welcome this opportunity to discuss the rural electric utility loans we make, and to explain how their risk profile is distinct from that of other types of commercial loans. **Because of such differences, we propose that the Agencies use their authority under Dodd-Frank to establish a new category of "rural electric utility loans," to which discrete underwriting criteria would apply in order to be deemed "qualified assets."** Dodd-Frank explicitly gives the Agencies the authority to create additional classes of assets for purposes of the Credit Risk

Retention rule, including the authority to establish discrete underwriting criteria for any such additional asset classes.[1] The Agencies should use this authority to appropriately address rural electric utility loans, which are different from every other asset class that the Agencies have proposed in this rule, including "commercial loans." [2]

The underwriting criteria the Agencies have proposed for such loans appear designed for loans in other business sectors – certain of the criteria are simply inapplicable to the electric utility sector and to the way rural electric utility loans are made.

In particular, we want to make clear that the rural electric utility loans we make do not raise the concerns underlying the Dodd-Frank Act's risk retention provisions. Indeed, as we discuss in detail in this letter, there are numerous ways in which we – and our loans – are very different from the originators and loans that contributed to the financial crisis.

As a result, additional risk retention criteria are not needed to address the risk posed by our loans underlying ABS or to incentivize us to keep "skin in the game." Risk retention requirements would not change our already prudent behavior or change the way we make loans. They would simply increase our costs by requiring retention of additional capital. In addition, we would face increased administrative burdens related to overseeing and ensuring compliance with any risk retention requirements applicable to us.

Instead, we believe the Agencies should evaluate rural electric utility loans under discrete criteria to be considered "qualified assets" under this rule.

Background on CFC

CFC is a nonprofit cooperative entity owned by America's consumer-owned RECs, which bring electric power to rural America.[3] It was created by those RECs in 1969 through the National Rural Electric Cooperative Association (NRECA)[4] to provide the RECs with financing to supplement the loan programs of the U.S. Department of Agriculture. Today, our nearly 1,000

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[1] Section 941 of DFA adds the following Section 15G(c)(2) to the Securities Exchange Act of 1934: "ASSET CLASSES.—The [credit risk retention] regulations prescribed under subsection (b) shall establish asset classes with separate rules for securitizers of different classes of assets, including residential mortgages, commercial mortgages, commercial
loans, auto loans, and any other class of assets that the Federal banking agencies and the Commission deem appropriate. (B) CONTENTS.—For each asset class established under subparagraph (A), the regulations prescribed under subsection (b) shall include underwriting standards established by the Federal banking agencies that specify the terms, conditions, and characteristics of a loan within the asset class that indicate a low credit risk with respect to the loan." (Emphasis added.)

[2] Alternatively, the Agencies could choose to amend their proposed underwriting criteria for commercial loans to accommodate other types of loans, such as rural electric utility loans, that would not fit within the criteria the Agencies have proposed. If the Agencies choose to take that approach, we encourage the Agencies to incorporate the criteria for rural utility loans that we propose in this letter.

[3] For additional information on CFC, including our history, current business, and financial reports and securities filings, please see our website, www.nrucfc.coop.

[4] NRECA is the national service organization for more than 900 not-for-profit RECs and public power districts in the rural United States. For additional information on NRECA, please see its website, www.nreca.coop.

members serve 42 million rural consumers living in 47 states. Our loan programs help enable our members to provide electric power services to residents of rural America.[5]

We are not a bank or other depository institution, but we are the largest non-governmental lender to rural electric systems. At February 28, 2011, CFC had loans and guarantees outstanding of $19.1 billion to our REC members.

CFC's Rural Electric Utility Loans

Ever since CFC was created by our member RECs to serve as their financing arm, we have continued to lend primarily to those member RECs. We make loans to our members for purposes related to their business of providing power to rural America. CFC offers both long-term loans and short-term lines of credit for these purposes. Our long-term loans may have terms of up to 35 years, reflecting, among other things, the long lifespan of the property, plant and equipment such loans often finance.

Long-Term Loans

CFC's long-term loans generally have the following characteristics:

• Terms of up to 35 years on a senior secured basis;
• Amortizing or bullet maturity loans with serial payment structures;
• The property, plant and equipment financed by and securing the long-term loan has a useful life equal to or in excess of the loan maturity;
• Flexibility for the borrower to select a fixed interest rate for periods of one to 35 years or a variable rate; and
• The ability for the borrower to select various tranches with either a fixed or variable interest rate for each tranche.

Short-Term Loans

Short-term loans are generally unsecured lines of credit. Line of credit loans are generally advanced at variable interest rates. These variable interest rates may be set on the first day of each month or mid-month.

The principal amount of line of credit loans with maturities of greater than one year generally must be paid down to a zero outstanding principal balance for five consecutive days during each 12-month period.

Line of credit loans are also made available when a member either receives Rural Utilities Service (RUS) approval to obtain interim financing or submits a loan application that is pending approval from RUS (sometimes referred to as "bridge loans"). Advances under these interim facilities must be repaid with advances from RUS long-term loans.

[5] Our member RECs are entities that Congress singled out, in the text of the Dodd-Frank Act, as deserving of a "public interest" waiver from derivatives regulations under Dodd-Frank. In doing so, Congress recognized that "rural electric cooperatives" serve a "public good." *See* Dodd-Frank Act, § 722(f).

The rural electric utility loans that CFC makes to our member RECs do not pose the same risk as residential mortgage loans, auto loans, credit card loans, or small business loans. The loans that CFC makes to the RECs are used to build and maintain the infrastructure required to provide essential electric service to rural customers. The whole loans that we sell to Farmer Mac are secured by a first lien on all assets and revenues of the REC borrower. At February 28, 2011, a total of 96.6% of the $16.3 billion of long term loans outstanding to RECs were secured by a first lien on all assets and revenues.

Electric utility defaults are rare. In a May 2009 report, Moody's Investors Service (Moody's) stated that there were only 6 regulated electric utility bond defaults in the prior 25 years.[6] The report also states that four of the defaults were due to regulators that did not provide timely rate relief to cover costs and that one of the defaults was due to the massive amount of damage caused by hurricane Katrina. In all six cases, the bonds were secured by a lien on the assets of the electric utility, and in all six cases the investors recovered 100% of principal and interest on a nominal basis. In the report, Moody's also indicates that its past practice had been to give a one-notch ratings upgrade to secured debt obligations versus unsecured debt obligations. However, the disparity between the losses experienced on unsecured debt and the losses experienced on debt secured by liens on electric utility assets is so compelling that, at the time, Moody's proposed increasing the upgrade on first mortgage utility bonds to two notches. An April 28, 2011 report from Standard & Poor's also observed that the electric cooperative utilities "passed through the crucible of the recession generally unscathed."[7]

CFC has a comparably strong history with its REC member lending. We have had only 15 payment defaults in our 42 years of lending to our REC members. Our loans outstanding to REC members totaled $18.1 billion at February 28, 2011. To date, we have incurred principal losses totaling $68 million on five of those 15 defaults and no principal loss on the other ten.

One of the key factors limiting the amount of defaults is that the RECs provide an essential electric service to customers. Electricity is one of the last items that consumers decide to go without. In fact, even in foreclosure, the electricity is typically maintained to keep the home warm so that pipes do not burst in the winter or to keep the home cool so that mold does not accumulate in the summer, and there must be electricity on to show the home to prospective buyers. This is consistent with our REC member data showing that even during 2008 and the financial crisis, there was only a median decline of 1.4% in electricity sales by our REC members. In addition, our REC members wrote off only one quarter of one percent of accounts receivable. The REC account receivable writeoffs have remained at this very low level throughout the financial crisis where there were significant defaults on mortgage loans.

This limited default history and limited loss history on our member REC loans is significantly different from what banks and other financial institutions have experienced with residential mortgage loans, auto loans, credit card loans and even small business loans. Over the past few

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[6] "Proposed Wider Notching Between Certain Senior Secured Debt Ratings and Senior Unsecured Debt Ratings for Investment Grade Regulated Utilities," *Moody's Global Infrastructure Finance*, May 2009.

[7] "Despite the Recession and Uncertainty of Regulation, Electric Cooperative Utilities Maintain Good Credit Quality," Standard & Poor's, April 28, 2011.

years there have been huge losses incurred on residential and commercial mortgage loans, credit card loans and auto loans, while CFC has not had any electric system principal losses. During the financial crisis, banks' financial results were severely impacted by the amount of loan loss reserves required to cover the decline in value and the losses experienced on residential mortgage loans, credit card loans, auto loans, home equity loans and small business loans. During that same timeframe, CFC has had only one REC member payment default (related to the cost of attempting to move to a geothermal fuel supply) and no principal writeoffs on REC member loans.

CFC was created for the purpose of providing business financing to our members, and we maintain an ongoing relationship with our borrowers – the RECs that comprise our ownership and membership. Since CFC lends only to its members, CFC has at all times a substantial amount of loans outstanding to the same members whose loans it sells. Through our whole loan sale program with Farmer Mac, we have sold loans from 140 members totalling approximately $825 million as of April 30, 2011, and continue to service those loans. Those same borrowers had a total of just over $2 billion in CFC long-term loans outstanding as of the same date – almost 2.5 times the amount of loan sales outstanding. There were only 5 of those 140 systems that had no CFC loans outstanding on April 30, 2011. We use equally stringent underwriting criteria for loans that we sell as for loans that we hold.

Thus, CFC's REC loans do not pose the same risk to investors or the financial system as do many loans made by financial institutions for residential mortgages, home equity loans, credit card loans, auto loans and small business loans.

CFC's Underwriting, Approval, and Monitoring Process

As we describe below, we have developed a robust system governing our credit process, policies, and ongoing monitoring of the loans we make.

Loan Underwriting

CFC maintains separate, dedicated lending staff to underwrite loans of different types. Our members contact the applicable lending staff to discuss the member's need for funding. Our lending staff then evaluates the member's request to determine whether the requested loan represents an acceptable credit risk. The lending staff's evaluation of the proposed credit will include, but is not limited to:

- The size of the loan requested
- The intended use of proceeds
- Whether collateral is required and if so, whether there is sufficient collateral
- The member's risk profile as measured by financial ratios and other risk characteristics
- Other factors that might be applicable to the type of borrower or the specific loan request being considered

If our lending staff determines that the credit is acceptable, they will work with the member to structure the loan based on the various options we offer and prepare a credit recommendation for review by lending staff management, as discussed further below under *Loan Approval.*

We maintain an internal member risk rating system which includes a borrower rating and a facility rating. The borrower risk rating measures risk of default for each borrower based on both quantitative and qualitative measurements specific to the particular business line of the borrower. The borrower risk rating is used to assess the credit quality of each of our members and to establish credit limitations, and is a factor in determining applicable credit approval levels. The facility risk rating measures risk of loss in the event of default for a particular facility based on the collateral or guarantee associated with the loan.

The member risk ratings are updated at least annually by our lending staff upon the receipt of audited financial information and are reviewed in connection with any new credit request. Annually, an outside banking consultant conducts a review of the risk rating process for compliance with policy and consistency in application and reports to CFC's management and Board of Directors (Board). In addition, we compare our internal ratings to the publicly available ratings for our members that have public ratings.

Loan Approval

Our Board establishes our loan policies, which include a credit approval matrix. The credit approval matrix specifies the required level of approval applicable to any proposed loan based on factors such as the amount of the loan, the borrower risk rating, whether credit limitations are exceeded and whether the loan is to a member associated with any of our current directors. Through the approval matrix, the Board has delegated the authority to approve certain loans to the CEO, the Corporate Credit Committee, and lending staff management, while retaining sole authority to approve certain loans.

In order to maintain our ability to consider and approve loans and other extensions of credit on a timely basis, the Board has established a loan committee, made up of Board members, that is authorized to approve loans that require Board approval. Loans that require Board approval are considered either at scheduled Board meetings or by the loan committee between regularly scheduled Board meetings.

Loans that require approval at a more senior level than lending staff management are forwarded to the Corporate Credit Committee for review. The Corporate Credit Committee is a cross-functional group that includes staff with distribution, power supply and telecommunications lending experience, legal experience, accounting experience, regulatory experience and financial industry experience. Lending staff will present the credit recommendation and answer any questions posed by the committee. The Corporate Credit Committee will then approve or reject the loan. Loans that require CEO or Board approval will be forwarded with documentation and a credit recommendation by the lending staff management and Corporate Credit Committee. The CEO or Board (or the loan committee of the Board) will review the credit recommendation, ask questions of staff if necessary, and either approve or reject the loan request.

Board policy requires that any exceptions to applicable credit limitations and any loan or extension of credit to a member that has one of our Directors as a director or officer must be approved by the Board or the loan committee of the Board; the director associated with the member requesting the loan will be recused from discussions and voting. Still, the CEO has the authority to approve emergency and certain other lines of credit, including where a director is either a director or officer of the member receiving such credit. Such lines of credit must meet specific qualifying criteria and must be underwritten in accordance with the prevailing standards and terms.

Approval of Advances on Previously Approved Loan Facilities

Certain of our loan facilities allow our members to draw down the loan amount over a period of time. To advance an amount under an approved loan facility, a member must be in compliance with all terms and conditions of their facility. The majority of our loans allow us to deny an advance if there has been a material adverse change in the financial condition of the borrower since the time the facility was approved.

Monitoring Process

Annually, members submit to us standard industry financial and statistical reports and covenant compliance certificates, and borrowers are required to provide us with audited financial statements. Risk ratings are updated annually or more often if there are credit events. The Corporate Credit Committee reviews extensions of credits requiring special attention. The credit process is audited annually by internal audit staff. In addition, an independent third party performs an annual credit review of a majority of loans in the portfolio, reviews the accuracy of our internal risk rating system, monitors credit extension practices and reports to management. The results of the audit and independent credit review are communicated to CFC's Board along with any recommendations for improvement.

Covenant Compliance

Borrowers are required to maintain certain financial ratios throughout the life of the loan. To be in compliance with the covenants in the loan agreement and eligible for loan advances, distribution systems generally must maintain an average modified debt service coverage ratio, as defined in the loan agreement, of 1.35 or greater. Similarly, power supply systems generally must maintain an average modified debt service coverage ratio, as defined in the loan agreement, of 1.0 or greater. CFC may make long-term loans to distribution and power supply systems, on a case-by-case basis, that do not meet these general criteria.

In addition, members with long-term loans outstanding are generally required to provide us with certain information and documentation on an annual basis, including, but not limited to, audited financial statements and a certificate of management confirming compliance with all covenants.

The Proposed Rule's Treatment of "Commercial Loans"

The Agencies' proposed rule would require sponsors of ABS to retain at least 5 percent of the credit risk of the underlying assets and would permit a sponsor to allocate some or all of its risk retention obligations to one or more originators of the assets, with the agreement of the affected originator(s).

As required by the Dodd-Frank Act, the proposal also provides that certain ABS would *not* be subject to these risk retention requirements, including ABS that are collateralized exclusively by loans that are deemed "qualified assets." "Qualified assets" would include, among other types of loans, "commercial loans" meeting certain underwriting standards. The stated purpose for requiring such underwriting standards is to ensure that the loans backing the ABS are of very low credit risk.

The proposed rule defines a "commercial loan" as any secured or unsecured loan to a company or an individual for business purposes, other than a loan to purchase or refinance a one-to-four family residential property, a loan for the purpose of financing agricultural production, or a loan for which the primary source (that is, 50 percent or more) of repayment is expected to be derived from rents collected from persons or entities that are not affiliates of the borrower.

This proposed definition of "commercial loan" – which is quite general – does describe the basic structure of the loans that CFC makes to its members. However, the underwriting criteria the Agencies have proposed for commercial loans to be considered "qualified assets" are not appropriate for every type of commercial loan. Only some of the Agencies' proposed criteria would be appropriate to apply to rural electric utility loans. Therefore, we propose that rural electric utility loans be subject to a discrete set of underwriting criteria, which would include some of the criteria the Agencies have proposed for commercial loans, as well as other criteria specific to the rural electric utility sector.

- **We also request that the Agencies clarify the proposed criterion that the loans must "not permit reinvestment periods"** (Proposed §___.18(a)(2)). It is unclear from the proposal what this provision is meant to prohibit. The proposed rule does not define "reinvestment periods," and that term potentially could have a number of meanings.

<u>The Agencies' Final Rule Should Create a New Category of "Rural Electric Utility Loans," to Which Discrete Underwriting Criteria Should Apply</u>

The Agencies have been given explicit authority under Dodd-Frank to add additional asset classes to the Credit Risk Retention rule, and to establish discrete underwriting criteria for any such additional asset classes. We urge the Agencies to use this authority to give appropriate treatment to rural electric utility loans. As we have discussed, rural electric utility loans are very different from other types of commercial loans. Not only do they pose much lower credit risk than many other types of loans, but the way they are made – the typical length of the loan term and typical loan covenants, for instance – differs as well. The standards we use for underwriting rural electric utility loans have worked well, and there is no need to impose additional criteria that more aptly apply to other types of loans.

We realize that, in drafting the proposed underwriting standards for each type of loan under this rule, the Agencies expressly wanted to establish standards more stringent than those typical in the lending industry. As stated in the proposal,

> The Agencies recognize that many prudently underwritten CRE, commercial and automobile loans will not meet the underwriting standards set forth in Sec. __.18 to Sec. __.20 of the proposed rules. For example, the Agencies note that the proposed standards are significantly more prudent and conservative than those required to attain a 'pass' credit under the Federal banking agencies' supervisory practices. Sponsors of ABS backed by loans that do not meet the underwriting standards will be required to retain some of the credit risk of the securitized loans in accordance with the proposed regulation (unless another exemption is available).

Further, the Agencies state that "the standards for a qualifying commercial loan use measures that are consistent with, but more prudent and conservative than, industry standards for evaluating the financial condition and repayment capacity of a borrower."

At the same time, though, we encourage the Agencies to recognize that the worthy objective of minimizing risk in ABS may be achieved through underwriting standards that do not include every component listed in the proposal, at least for certain types of loans.

Indeed, in a May 26, 2011 letter to the Agencies, a bipartisan group of 39 U.S. Senators cautioned the Agencies not to implement overly stringent underwriting criteria through this rule, stating that the Agencies' proposed criteria go beyond Congressional intent. While the Senators' letter focuses on the standards for "qualified residential mortgages" (QRMs), the concerns it articulates are equally relevant to commercial loans: "The statute requires the QRM definition to be based on 'underwriting and product features that historical loan performance data indicate result in a lower risk of default'....The proposed regulation goes beyond the intent and language of the statute by imposing unnecessarily tight down payment restrictions."[8] Likewise, the Agencies' proposed criteria for commercial loans exceed what is needed to ensure that certain loans are of low credit risk – certainly in the case of rural electric utility loans.

<u>CFC's Proposed Definition for "Rural Electric Utility Loans"</u>

We believe a new category of loan is needed to appropriately address the unique aspects of rural electric utility loans. As we have discussed, rural electric utility loans do not pose the same level of credit risk as do other types of commercial loans, and therefore should not be subject to all the underwriting criteria proposed by the Agencies for commercial loans. We propose the following new definition of "rural electric utility loan," which would be subject to its own underwriting criteria to be deemed a "qualified asset":

- "*Rural electric utility loan* means:
  - a secured or unsecured loan to a company or an individual for business purposes,
  - that is made to a nonprofit entity that is primarily engaged in the business of distributing, generating, or transmitting electric power to rural areas.

[8] May 26, 2011 letter from Sens. Landrieu et al.

- For purposes of this section, *rural area* has the same meaning as in the Rural Electrification Act of 1936."[9]

CFC's Proposed Underwriting Criteria Applicable to "Rural Electric Utility Loans"

We agree with the inclusion of many of the criteria that the Agencies have proposed for commercial loans. However, other proposed criteria would be inappropriate to apply to rural electric utility loans, because they do not recognize the way such loans are made, such as the typical terms of such loans and the nature of typical collateral, as well as the way rural electric utilities operate.

The criteria we propose here, tailored to rural electric utility loans, include a number of the criteria the Agencies have proposed for commercial loans. Our proposed criteria are designed to ensure that the rural electric utility loans underlying ABS pose very low credit risk.

We would be pleased to meet with you to discuss these criteria and the purposes underlying them, and to provide any supplementary information that could help your review of our proposed criteria. The Agencies appear not to have considered the rural electric utility sector in drafting criteria for "commercial loans," and we would welcome the opportunity to give additional details about this sector.

➢ ***CFC's proposed underwriting standards for qualifying rural electric utility loans.***

(1) Origination.

Prior to origination of the loan, the originator:

- Verified and documented the financial condition of the borrower:
  - As of the end of the borrower's two most recently completed fiscal years; and
  - During the period, if any, since the end of its most recently completed fiscal year.

- Determined that the primary source of repayment for the loan will be revenue from the business operations of the borrower.

- Conducted an analysis of the borrower's ability to service its overall debt obligations during the next two years, based on reasonable projections.

- Determined that, based on the average of the previous two years' actual performance, the borrower had:
  - For loans to rural electric distribution systems:
    - A modified debt service coverage (MDSC)[10] ratio of 1.35 or greater; and
    - Equity to total assets of 20 percent or greater.
  - For loans to generation and transmission cooperatives:

[9] *See* 7 USC § 913.

[10] The MDSC ratio is a measurement of a system's ability to generate sufficient operating funds to cover its cash requirements.

- MDSC of 1.1 or greater; and
- Equity to total assets of 10 percent or greater.

The ratios we have proposed are cash-based ratios that work effectively to ensure that a rural electric cooperative borrower will be able to service its debt. These ratios have been accepted by our investors as useful measures that are appropriate to the rural electric utilities sector.

(2) Security Interests.

If the loan is originated on a secured basis:

- The originator obtained a security interest on all of the property pledged to collateralize the loan, with the originator's lien superior to or *pari passu* with any other security interest on that collateral.

- The loan contains covenants:
  - Prohibiting the creation or existence of any superior security interest with respect to any of the collateral;
  - Requiring the borrower to pay taxes, charges, fees, and claims, where non-payment might give rise to a lien on any collateral;
  - Requiring the borrower to take any action required to perfect or protect the security interest of the originator or any subsequent holder of the loan in the collateral or the priority thereof, and to defend the collateral against claims adverse to the lender's interest;
  - Requiring the borrower to permit the originator or any subsequent holder of the loan, and the servicer of the loan, to inspect the collateral; and
  - Requiring the borrower to maintain the physical condition of any collateral for the commercial loan.

(3) Review of Financial Statements and Other Records.

The loan documentation must include covenants that require the borrower to:

- Provide to the originator or subsequent holder, and the servicer, the borrower's financial statements and supporting schedules on at least an annual basis; and
- Allow the originator or subsequent holder, and the servicer, to inspect and review the books and records of the borrower upon reasonable request.

Inapplicable Criteria

The Agencies have proposed a number of criteria for commercial loans that we have not included in our above list.. We have omitted such criteria because they would be inapplicable to rural utility loans. Those criteria include the following:

- *Requiring the borrower and any other party that pledges collateral for the loan to maintain insurance that protects against loss on any collateral for the commercial loan at least up to the amount of the loan.*
    - This criterion should be deleted for rural electric utility loans, as it would not be appropriate to require insurance up to the amount of the loan on collateral that typically consists of electric utility infrastructure. Under prudent utility insurance practices, the borrower REC would be required to maintain insurance on buildings, director and officer liability insurance, and hazard insurance, except where the collateral consists of poles and wires.

- *Loan payments required under the loan agreement must be based on straight-line amortization of principal and interest that fully amortize the debt over a term that does not exceed five years from the date of origination, and must be made no less frequently than quarterly over a term that does not exceed five years.*
    - The Agencies' proposed 5-year timeframe would seem to have been proposed with a different industry in mind – certainly, it would not work for loans in the rural electric utility industry. Rural electric utility loans are typically made for a length of time up to the useful life of the assets being financed, and utility assets are long-lived assets. Thus, we typically have 30-to 35-year terms for our loans. These loans finance plant construction and other long-term activities, and thus it would be inappropriate to require repayment within 5 years. Doing so would require passing on costs to the consumers that pay for the RECs' services – meaning skyrocketing rates for those consumers.

- *The loan was funded within the six (6) months prior to the closing of the securitization transaction.*
    - It is unclear what connection there would be between how recently the loan was funded and the credit risk that loan would pose. CFC makes loans that may later be securitized after we sell them as whole loans. While the securitization typically happens soon after the whole loan sale, it is possible that it could occur later. We do not believe that that fact increases the concerns over risk in the loans underlying the ABS. In fact, securitization that takes place soon after funding could raise concerns that the originator made the loans with the intent to quickly securitize them – in contrast to the way we make loans to our members, which is with the intent to hold the loans and maintain a relationship with the borrower.

- *Covenants must prohibit payments-in-kind.*
    - This criterion does not make sense for the rural electric utilities sector – payments-in-kind are not at issue in rural electric utility loans.

In contrast to the criteria we suggest deleting, our proposed underwriting criteria take into account the unique qualities of rural electric utility loans. They are based on criteria that have, to date, ensured that rural electric utility loans present extremely low credit risk – low enough to make risk retention requirements unnecessary.

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CFC appreciates the Agencies' consideration of our comments on the Credit Risk Retention proposal. We would welcome the opportunity to further discuss our views and the rural electric utilities sector. Please do not hesitate to contact Richard E. Larochelle, CFC's Senior Vice President of Corporate Relations, at (703) 709-6700 should you wish to discuss any of our comments or need additional information.