

Eligibility criteria are established according to statute and RUS program requirements. To be eligible to participate in the program, a guaranteed lender must be a bank or other lending institution organized as a private, not-for-profit cooperative association or otherwise on a non-profit basis and be able to demonstrate to the Secretary that it possesses the appropriate expertise, experience and qualifications to make loans for electrification or telephone purposes. To be eligible to receive a guarantee, a guaranteed lender must furnish the Secretary with a certified list of the principal balances of concurrent loans then outstanding evidencing that such aggregate balance is at least equal to the sum of the proposed principal amount of guaranteed bonds to be issued, and any previously issued guaranteed bonds outstanding. Also, the guaranteed bonds to be issued by the guaranteed lender must receive an underlying investment grade rating from a Rating Agency, without regard to the guarantee and the final maturity of the guaranteed bonds may not exceed 15 years.

The rules establish an application process where the applicant is required to submit eligibility data and certifications for on-going review. The application information includes background information, a term sheet summarizing the proposed terms and conditions of the guarantee agreement, a statement as to how the proceeds are to be used and the financial benefit it anticipates deriving from participating in the program, a pro-forma cash flow projection or business plan for the next five years, consolidated financial statements of the guaranteed lender for the previous three years, evidence of having been assigned an investment grade rating on the debt obligations for which it is seeking the guarantee, without regard to the guarantee; and other application documents deemed necessary by the Secretary for the evaluation of applicants.

Each application will be reviewed by the Secretary to determine whether it meets the eligibility requirements. The application is then evaluated based upon the extent to which the proposed provisions indicate the applicant will be able to repay the guaranteed bonds, the adequacy of the proposed provisions to protect the Federal government, the applicant's demonstrated performance of financially sound business practices; the extent to which providing the guarantee to the applicant will help reduce the cost and/or increase the supply of credit to rural America, and the amount of fee income available to be

deposited into the Rural Economic Development Subaccount.

After the guarantee is approved, other conditions must be met prior to receiving final endorsement by the Secretary. Bond documents must be executed by the applicant and the applicant must certify to the Secretary that the guaranteed bonds proceeds will be applied to fund eligible new loans under the RE Act, to refinance concurrent loans, or to refinance existing debt instruments of the guaranteed lender used to fund eligible loans. The applicant must also provide a final certified list of concurrent loans and their outstanding balances as of the date the guarantee is issued. Counsel to the applicant must furnish an opinion as to the applicant being legally authorized to issue the guaranteed bonds and enter into the bond documents. No material adverse change can occur between the date of the application and date of execution of the guarantee. The Chairman of the Board and the Chief Executive Officer of the applicant (or other senior management acceptable to the Secretary) must certify acknowledging the applicant's commitment to submit to the Secretary an annual credit assessment of the applicant by a Rating Agency and acknowledging the guaranteed lender's commitment to deliver annual consolidated financial statements audited by an independent certified public accountant for each year during which the guaranteed bonds are outstanding. It should be emphasized that the Secretary will not issue the guarantee if, in the sole judgment of the Secretary, there has occurred a material adverse change in the condition (financial or otherwise) or prospects of the guaranteed lender or its subsidiaries.

The rule establishes an annual fee for the guarantee equal to 30 basis points (0.3 percent) of the amount of the unpaid principal of the guaranteed bond. The fee is deposited into the Rural Economic Development Subaccount maintained under section 313(b)(2)(A) of the RE Act. The Secretary also has the authority to structure the schedule for payment of the annual fee, with the consent of the lender, so that sufficient funds are available to pay the subsidy costs for the guarantee.

As long as any guaranteed bonds remain outstanding, the guaranteed lender agrees to provide the Secretary on an annual basis consolidated financial statements and accompanying footnotes, audited by independent certified public accountants, pro forma projections of the guaranteed lender's balance sheet, income statement, and

statement of cash flows over the ensuing five years, a credit assessment issued by a Rating Agency, a review and certification of the security of the government guarantee that is audited by an independent certified public accounting firm or federal banking regulator, a review and certification of the lender's capital adequacy utilizing the capital adequacy standards of FIRREA by a reputable, independent certified public accounting firm or federal banking regulator, and other such information requested by the Secretary. Additionally the bond documents will specify such bond monitoring and financial reporting requirements as deemed appropriate by the Secretary.

Economic Impact

The Guarantees for Bonds and Notes Issued for Electrification and Telephone Purposes Program (the "Program") facilitates the continued improvement of electric and telephone service in rural America, by providing Federal loan guarantees on debt issued by non-profit, cooperative and other rural lending institutions (the "Lenders"). However, by providing bond guarantees under the Program, financial default risk is transferred to the Federal government. Under the most likely scenario, the fees collected from the Lenders would offset all of the expected credit subsidy costs of the Program. As a result, the expected cost to taxpayers would be zero. However, there is a possibility that the Lender could default, which, depending on the timing of the default, could expose the government to a maximum liability of approximately \$3 billion. Based on historical experience for unsecured corporate bonds of this quality, the government could be expected to recover at least one-half of the defaulted amounts, making it more likely that the government's maximum exposure is approximately \$1.5 billion. The exposure may be even less depending upon the annual appropriation by Congress to fund guarantees through this program.

Without this new program lenders would continue to obtain debt financing at prices that reflect the financial risk of uninsured bonds. The higher rates associated with this financing as compared to Federally guaranteed debt would be passed on to the cooperatives and other borrowers and eventually to the consumers in rural America in the form of higher electric or telephone rates. Under the proposed Rule lenders could refinance outstanding debt at a lower rate and pass the savings in one form or another on to its borrowers