

# Module: Compliance

## Section: Borrower Rights - Protection of Borrowers

### EM-622

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#### Authority and Purpose

The Farm Credit Act of 1971, as amended by the Agricultural Credit Act of 1987, provides Farm Credit System (System) borrowers with protection from System lenders taking action on loans for which the borrowers have met all loan obligations.

The purpose of Section 4.14D of the Act and FCA Regulation 12 CFR § 614.4514 is to set forth restrictions against foreclosure, accelerated reduction in the principal balance, accelerated repayment due to past delinquencies, and adverse action based on placing any loan in nonaccrual and not notifying the borrower of the action or the reasons for the action.

#### Applicability and Exemptions

This subpart applies to loans and restructurings made by qualified lenders. For the purposes of this subpart, a loan is defined to mean a loan to a farmer, rancher, or producer or harvester of aquatic products for any agricultural or aquatic purpose or other credit needs of the borrower. The restrictions imposed on System lenders to protect borrowers who have met all obligations include:

- A qualified lender may not foreclose on any loan because of failure of the borrower to provide additional collateral as long as all accrued principal, interest, and penalty payments with respect to the loan have been made.
- A qualified lender may not require the borrower to reduce the principal balance of a loan by any amount that exceeds the regularly scheduled payment schedule unless:
  - The borrower disposed of part or all of the collateral and the proceeds were not applied to the loan; or
  - The parties agree otherwise in a written agreement.

**NOTE:** The institution should consider initiating criminal referral proceedings when the borrower has disposed of or diverted collateral.

- After the borrower has made all accrued payments of principal, interest, and penalties, a qualified lender may not enforce acceleration of the borrower's repayment schedule due to the borrower's poor repayment history.
- If a qualified lender places a loan in nonaccrual status and, as a result, an adverse action is taken against the borrower, the lender must document the change of status and promptly notify the borrower in writing of the action and the reasons for the action. If the borrower is not delinquent and the borrower's request to have the loan placed back in accrual status is denied, the borrower may request (within 30 days after receipt of the notice) a review of the decision by the credit review committee.

The above requirements have a unique application to loans in the process of foreclosure. Specifically, a qualified lender must accept late payments from a borrower being foreclosed on if foreclosure has not been completed. System institutions cannot refuse such payments and continue the foreclosure if the payment amounts are sufficient to cure the delinquent status, including any penalty amounts.

Such borrowers might still be in default under other nonmonetary covenants in a loan agreement. Nonmonetary default covenants could include required casualty insurance coverage, property tax payments, or other specified actions required to maintain collateral or the avoidance of other liens on the borrower or collateral.

The lender can request additional principal payments on an otherwise current loan if the lender has reasonable grounds to believe that asset dissipation, diversion, or destruction is occurring. If the borrower is unable or unwilling to comply, the loan would no longer be considered current and the regulation would no longer prevent foreclosure.

### **Examination Objectives**

Determine whether adequate policies, procedures, and internal controls have been established that provide reasonable assurance of compliance with FCA Regulation 12 CFR § 614.4514.

Obtain corrective action when violations are identified or when deficiencies are noted.

### **Examination Procedures**

The following procedures are provided to facilitate an evaluation of the protection of borrowers who have met all loan obligations. Consistent with risk-based examination principles, examiners should add, delete, or modify procedures as needed based on the particular circumstances of the institution.

1. Coordinate compliance examination activities with other members of the examination team and the examiner-in-charge (EIC). Emphasis should be on identifying violations of law and regulation in other areas (e.g., eligibility, scope of financing, lending limits, etc.); integrating those findings with the examination of consumer protection, borrower rights, and financial reporting; and concluding on management's compliance with laws and regulations.
2. Review and evaluate the adequacy of policies, procedures, and internal controls that are in place to ensure compliance with the requirements of FCA Regulation 12 CFR § 614.4514.
3. When reviewing loan files, be alert to correspondence indicating that the lender has requested additional collateral or principal payments.
4. Review a sample of loans transferred to nonaccrual to determine if adverse actions were taken and, if so, if borrower rights were provided.
5. Determine through discussions with management and appropriate institution personnel and a review of pertinent files whether proper notifications were given when loans were placed in nonaccrual status that resulted in adverse action being taken.
6. Complete workpaper FCA 6060, if necessary, in conjunction with the evaluation of compliance with the requirements of this regulation.
7. Utilize discussions with institution managers as needed to gather information and discuss procedures and practices followed by institution personnel to ensure compliance with laws and regulations.
8. Conclude whether the institution is adequately complying with FCA Regulation 12 CFR § 614.4514. If not, ascertain whether the conclusion of noncompliance is supported by adequate documentation of the specific noncompliance.
9. Consider the possibility of issuing a borrower rights directive or imposing civil money penalties if significant, repeated, and uncorrected violations are surfaced.
10. Discuss tentative conclusions and examination findings with the examiner(s) responsible for

evaluating management.

11. Discuss items of concern, scope of work performed, and conclusions with the EIC and with the appropriate institution manager. Obtain a response regarding the cause(s) of deficiencies or weaknesses and anticipated corrective actions.
12. Organize and compile, if necessary, violations of law and regulation into an appendix for the Report of Examination.
13. Prepare a leadsheet or other summary document to provide workpaper support for the work performed and the conclusions reached.