

RD AN No. 4690 (4274-D, 4280-D,
4280-A, 1942-G and 1951-R, 1951-E)

September 16, 2012

TO: State Directors, Rural Development
ATTN: Business Programs Directors
SUBJECT: Revolving Loan Fund Programs
Ultimate Recipient Conflict of Interest

PURPOSE/INTENDED OUTCOME:

This Administrative Notice (AN) is being issued to provide guidance, as it relates to the Intermediary Relending Program, Rural Business Enterprise Grant Program, Rural Economic Development Grant Program and Rural Microentrepreneur Assistance Program, regarding the restrictions on making loans to third parties from the intermediary/grantee in cases where the intermediary/grantee is a tribal entity or public body. The outcome of this revision will clarify how to address and resolve potential conflicts of interest.

COMPARISON WITH PREVIOUS AN:

No previous AN has been issued on this subject.

IMPLEMENTATION RESPONSIBILITIES:

The Agency has frequently received questions regarding the conflict of interest of Indian tribes and public body intermediaries/grantees, and making third party loans to their members, employees, and tribal business entities. This AN will address these questions and provide further clarification on intermediary/grantee lending to members and employees.

The following states requirements, by program, for third party loans (please note the four footnotes):

EXPIRATION DATE:
August 31, 2013

FILING INSTRUCTIONS:
Preceding RD Instructions 4274-D, 4280-A,
4280-D, 1942-G and 1951-R, 1951-E

RD Instruction 4274-D, section 4274.308(b)(4) – Intermediary Relending Program¹

RD Instruction 4280-D, section 4280.323(c) – Rural Microentrepreneur Assistance Program²

RD Instruction 4280-A, sections 4280.27(g) and 4280.30(a) – Rural Economic Development Grant Program³

CFR 3015, section 3015.205(b)(7) – Rural Business Enterprise Grant Program⁴

Lending to Members

The cited regulations noted under the footnotes shall not prevent an intermediary that is organized as an Indian tribe or public body from making a loan to one of its members.

Lending to an Employee

For the purpose of this AN “employee” includes members of governing bodies, boards, committees, contractors, and immediate family members.

¹ To be eligible to receive loans from the IRP RLF, ultimate recipients “Must along with its principal officers (including their immediate family) hold no legal or financial interest or influence in the intermediary. Also, the intermediary and its principal officers (including immediate family) must hold no legal or financial interest or influence in the ultimate recipient.”

² “(c) Assistance that will cause a conflict of interest or the appearance of a conflict of interest including but not limited to: (1) Financial assistance to principals, directors, officers, or employees of the microlender, or their close relatives as defined; and (2) Financial assistance to any entity the result of which would appear to benefit the microlender or its principals, directors, or employees, or their close relatives, as defined, in any way other than the normal repayment of debt.”

³ Zero-interest loans will not be used: “(g) Where there is directly or inadvertently a conflict of interest or the appearance of a conflict of interest in the Project; for Intermediaries this would include a situation in which the Intermediary, its officers, managers, Board of Directors, employees, their spouses, children, or close relatives, have a financial or ownership interest in the Project being funded, including its construction or development;” and “(a) Conflict of Interest. The Intermediary must not own or manage any Ultimate Recipient Project, unless the Project is acquired as a result of servicing a loan made from the Revolving Loan Fund. Conflicts of interest and all appearances of a conflict of interest are not permitted.”

⁴ “ It will establish safeguards to prohibit employees from using their positions for a purpose that is or gives the appearance of being motivated by a desire for private gain for themselves or others, particularly those with whom they have family, business, or other ties.”

A public body or Indian tribe that applies for and administers an Revolving Loan Fund (RLF) is not precluded from lending to one of its employees and their immediate family, provided the employee is not a member of the intermediary/grantee governing body, a member of the board of directors or governing board of the RLF, a member of the RLF lending board or loan committee or an employee of a department or authority that operates or provides administrative services to the RLF.

The members of the intermediary/grantee governing body, members of the board of directors, or governing board of the RLF, members of its lending board or loan committee and employees of a department or authority that operates or provides administrative services of the RLF, including immediate family, may not hold any legal or financial interest or influence in the third party recipient.

To meet the requirements of the regulations, a public body or Indian tribe that applies for an RLF program loan, must in its application, describe its organizational structure and its structure for the administration of the RLF. The intermediary/grantee should have a distinct lending committee and list of dedicated employees by position. In this instance, those members of the board, lending committee, and separate employment duties, are prevented by conflict of interest to be allowed to be the third party recipient.

As an example, the tribe or public body may have an economic development authority or business development department organized under the tribe or public body to administer the RLF. The detailed description of the structure of the authority or department would be included in the approved Lender's Manual, and will include policies and procedures and separation of duties to ensure no conflicts of interest. An employee of a department, separate from the administration of the RLF, the forestry department and their immediate family, may be eligible third party recipients. An employee of the financial department responsible for collection of RLF loan payments and their immediate family are ineligible third party recipients.

Lending to Tribal Entities

An intermediary/grantee organized as an Indian tribe may make RLF loans to entities owned by its tribe only if the entity is organized and governed independently from the tribe. An example of a tribal entity that is an eligible third party recipient is a business organized as a corporation, incorporated and wholly-owned by the tribe and the corporation's board of directors is appointed by the tribe, but governed by the corporation independently of the tribe. Tribal entities governed under the Tribal Government are not eligible third party recipients of an RLF administered by its tribe. (Such entities may be eligible third party recipients of the RLF administered by other intermediaries/grantees).

Work Plan Documentation

Best practices include that the Agency's delegated authority should review the intermediary/grantee organizational documents and the work plan or lending manual as they relate to the oversight and administration of the RLF, to ensure the proper separation of duties. The lending manual will address the organizational structure, clarifying how the lending organization is structured and the RLF is administered. The Lender's Manual will provide the documentation on how the intermediary/grantee will be organized and managed to avoid a conflict of interest. Prior to loan closing, the intermediary/grantee must provide an Agency-approved Lender's Manual documenting the organization structure to ensure that no conflict of interest will exist with the organizations principal officers, loan board, employees, and its members.

Any changes to the lending department must be reflected in the Lender's Manual and approved by the Agency prior to any change.

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If you have any questions on the information provided, please contact the Specialty Programs Division at (202) 720-1400.

(Signed by John C. Padalino)

John C. Padalino
Acting Administrator
Rural Business-Cooperative Service