

RD AN No. 3957 (4287-B)
March 23, 2004

SUBJECT: Business and Industry Guaranteed Loan Program
Liquidation Expenses, Protective Advances, and the Final Report of Loss

TO: State Directors, Rural Development

ATTN: Business Programs Directors

PURPOSE/INTENDED OUTCOME:

The purpose of this Administrative Notice (AN) is to share findings from a recent Nationwide Office of Inspector General audit on Business and Industry (B&I) loan liquidations and to issue guidance to the State Offices regarding authorized protective advances and erroneous and unsupported information on Form RD 449-30, "Loan Note Guarantee Report of Loss."

COMPARISON WITH PREVIOUS AN:

There is no previous AN on this subject.

IMPLEMENTATION RESPONSIBILITIES:

The audit found that Business Programs personnel authorized protective advances that the lenders were not eligible to claim. The claims occurred when the borrowers had voluntarily conveyed collateral securing the loan to the lender in full satisfaction of the debt. The lender claimed protective advances for expenses incurred protecting the collateral. Once the collateral is conveyed to the lender, expenses incurred thereafter are liquidation expenses. Protective advances are an indebtedness of the borrower and are secured by the security instruments. Sound judgment must be exercised in determining that the protective advance preserves collateral and recovery is actually enhanced by making the advance.

EXPIRATION DATE:
March 31, 2005

FILING INSTRUCTIONS:
Preceding RD Instruction 4287-B

RD Instruction 4287-B, section 4287.156 provides the following: protective advances and interest thereon at the note rate will be guaranteed at the same percentage of loss as provided in the Loan Note Guarantee. “Protective advances must constitute an indebtedness of the borrower to the lender...Agency written authorization is required when cumulative protective advances exceed \$5,000.@ In addition, the maximum loss to be paid by the Agency will never exceed the original principal plus accrued interest regardless of any protective advances made.@ This maximum loss statement should be put in writing to the lender once the decision to liquidate is made.

The Final Report of Loss calculations are usually completed by the lender. Some States conduct a final loss audit of the lender=s loan ledgers. A final loss audit is recommended, although not required by regulation. RD Instruction 4287-B, section 4287.158(c)(4) specifically states: “The lender will show a breakdown of liquidation expenses as to the payee, purpose of the expenditure, date paid, and evidence that the amount expended was proper and that payment was actually made. *The Agency should review all liquidation expenses to determine if the expenses were proper, reasonable, and in accordance with the approval given by the Agency.* Liquidation expenses are recoverable only from collateral proceeds.” It is the responsibility of Agency personnel to ensure that the Final Report of Loss calculations are correct and justifiable in our role of monitoring and oversight responsibility. In addition, the Agency must complete Appendix B, “Final Loss Settlement Checklist@ of RD Instruction 4287-B. Appendix B is a useful tool to assist in determining if the loan was administered as intended; i.e., type of security, source of liquidation proceeds, liquidation costs, etc. Appendix B provides a format to walk you through the entire loan from its inception to the Final Report of Loss. Once Appendix B is accurately completed, documentation is on file to support whatever questions may arise later.

Please direct any questions to the B&I Division Servicing Branch, (202) 690-4103.

(Signed by John Rosso)

JOHN ROSSO
Administrator
Rural Business-Cooperative Service