

RD AN No. 3994 (4279-B)  
June 24, 2004

SUBJECT: Business and Industry Guaranteed Loan Program  
Purchase of Cooperative Stock

TO: State Directors, Rural Development

ATTN: Business Programs Directors

PURPOSE/INTENDED OUTCOME:

The purpose of this Administrative Notice (AN) is to clarify and provide guidance in determining the procedure for handling inquiries and accepting Business and Industry (B&I) Guaranteed Loan applications for the purchase of cooperative stock.

COMPARISON WITH PREVIOUS AN:

This AN updates and replaces RD AN No. 3872 (4279-B) dated June 12, 2003.

IMPLEMENTATION RESPONSIBILITIES:

RD Instruction 4279-B, section 4279.113(i), authorizes the issuance of loan guarantees for the purchase of startup cooperative stock by a family-sized farm where commodities are produced by the farm to be processed by the cooperative. The Farm Security and Rural Investment Act of 2002 (Farm Bill) modified some of the original authorizing legislation. These changes will become effective 30 days after the Interim Final Rule is published in the Federal Register. Because law prohibits the Agency from disclosing the specific changes prior to publication, this AN does not address those changes. We will provide additional guidance when the rule is published.

Any inquiries or applications received that may be consistent with the modified authorizing legislation and not currently part of the published regulation should be referred to the National Office.

EXPIRATION DATE:  
June 30, 2005

FILING INSTRUCTIONS:  
Preceding RD Instruction 4279-B

1. Eligibility requirements.
  - a. Any farmer/rancher eligible for the Farm Service Agency (FSA) Guaranteed Loan Program will be considered a family-sized farm for the purposes of this program. Eligibility criteria for the FSA Guaranteed Loan Program can be found in the 2-FLP Guaranteed Loanmaking and Servicing Handbook published by FSA. This handbook may be found on FSA's website at [www.fsa.usda.gov](http://www.fsa.usda.gov). Applications received from farmers not meeting this definition will be considered on a case-by-case basis with documentation, acceptable to the Agency, as to why it should be considered a family-sized farm.
  - b. For purposes of the Cooperative Stock Purchase Program, a cooperative is an entity incorporated under the State Cooperative Incorporation Law. A processing facility that is a wholly-owned subsidiary of a cooperative is considered to be a part of the cooperative.
  - c. The cooperative and any wholly-owned processing facility must be a start-up.
  - d. The cooperative must have been organized for the purpose of processing an agricultural commodity that was produced by its members.
2. Feasibility study requirements. In accordance with RD Instruction 4279-B, section 4279.150, a feasibility study by a qualified independent consultant may be required by the Agency for start-up businesses or existing businesses when the project will significantly affect the borrower's operation. A feasibility study is required to be completed for the cooperative, in accordance with the above-cited program regulations, and will provide for a consistent evaluation of the potential success of the business upon which the stock purchase loans are based. The feasibility of the cooperative will determine the viability of the business and not the individual farm operators. Feasibility studies of the individual borrowers (farmers/ranchers) are not necessary.
3. Equity requirements. We expect that virtually every applicant (farmer/rancher) will be an existing business entity. Consequently, the minimum tangible balance sheet equity requirement would be 10 percent. New farmers/ranchers would need 20 percent equity.

4. Environmental review requirements. Cooperative stock purchase loans should be considered categorical exclusions under the provisions of RD Instruction 1940-G. However, there is a financial soundness link between the stock purchase loan and the environmental soundness of the cooperative that issues the stock. Since the interests of the Agency are directly tied to the successful operation of the cooperative, you should include the following requirement in all Conditional Commitments for cooperative stock loans: “The cooperative will provide the lender with all required Federal, State, and local permits and other clearances involving the environmental aspects for review and approval.” If the lender requests the Loan Note Guarantee to be issued prior to the cooperative becoming operational, the lender must certify to the Agency that the above requirement will be met.
5. Collateral requirements. Existing program regulations require that collateral be sufficient to protect the interests of the lender and the Agency. The Agency will not require the lender to secure the loan with more than a lien on the stock acquired with loan funds, an assignment of any patronage refund, and the full and unconditional personal or corporate guarantee of the borrower. The lender will otherwise determine the sufficiency of collateral in accordance with its established lending practices.

The borrower and lender must realize that the borrower is fully liable for the entire debt, regardless of the success or failure of the cooperative. In the event of default, the stock will very likely not be sufficient to pay the stock purchase loan in full. The lender will be expected to maximize the recovery on each stock purchase loan, including collection of the personal or corporate guarantees.

6. Annual financial reporting requirements (for guaranteed loans for the purchase of cooperative stock). The Agency has determined that commercial agricultural lenders do not require financial statements prepared in accordance with Generally Accepted Accounting Principles (GAAP) from farmers and ranchers. The Farm Bill requires the Agency to accept financial information from a farmer or rancher in the manner generally required by commercial agricultural lenders in the area. Until the Agency issues more definitive guidance, the Agency will accept the farmer or rancher’s financial information provided by the lender as being in the manner generally required by commercial agricultural lenders in the area.

7. Lender analysis.
  - a. The lender must complete a credit analysis of each stock purchase loan in accordance with RD Instruction 4279-B, section 4279.131.
  - b. Because of the financial link between the stock purchase loans and the cooperative, the lender is expected to provide the Agency with a complete credit analysis of the cooperative prior to making its first stock purchase loan.
  
8. Loan concurrence/approval. State Directors are not authorized to approve or make any commitment on any request for the purchase of cooperative stock until the National Office has reviewed the cooperative's feasibility study/proposal and provided direction. The State Director should work with the cooperative in obtaining an independent feasibility study. When a feasibility study/proposal is presented, the State Director is to forward the information, along with a written summary and a recommendation, to the National Office.
  
9. Lead State Office responsibilities. When you are working with a cooperative with members in more than one State, it will be easier for the cooperative to channel all of its questions and concerns through a single State Office. The lead State Office will coordinate issues involving the lender and cooperative concerning policy and procedural issues and promote a standardized methodology for loan processing and servicing.

The lead State Office will be the State in which the processing facility is located, unless otherwise designated by the National Office. The individual loans will be processed, approved, and serviced in the State in which that borrower resides, regardless of where the processing facility is located.
  
10. When to close the loan. Closing the stock purchase loan prior to the cooperative becoming operational is a means of capitalizing the cooperative. The cooperative's lender may require the cooperative to have the funds from the stock sale under the cooperative's control and shown on its financial statement as a condition for loan approval. This would require the stock purchase loan to the farmer to be closed prior to the cooperative becoming operational, as would be expected in a proposal of this type. Therefore, when necessary, you may issue the Loan Note Guarantee when the lender closes the individual loan for the stock purchase, even though the cooperative may not yet be operational.

11. Loan guarantee limits. The loan amount and percentage of guarantee are limited by RD Instruction 4279-B, section 4279.119.

If you have any questions, please contact the B&I Division, (202) 690-4103.

*(Signed by William F. Hagy, III) for*

JOHN ROSSO  
Administrator  
Rural Business-Cooperative Service