INTERIOR BOARD OF INDIAN APPEALS

Bonanza Fuel, Inc. v. Director, Office of Economic Development,
Bureau of Indian Affairs

33 IBIA 203 (03/11/1999)

United States Department of the Interior

OFFICE OF HEARINGS AND APPEALS
INTERIOR BOARD OF INDIAN APPEALS
4015 WILSON BOULEVARD
ARLINGTON, VA 22203

BONANZA FUEL, INC., Appellant	:	Order Affirming Decision
v.	:	Docket No. IBIA 97-146-A
DIRECTOR, OFFICE OF ECONOMIC DEVELOPMENT, BUREAU OF INDIAN AFFAIRS, Appellee	:	March 11, 1999

This is an appeal from a May 5, 1997, decision of the Director, Office of Economic Development, Bureau of Indian Affairs (Director; BIA), declining to continue an interest subsidy on a guaranteed loan. 1/ For the reasons discussed below, the Board affirms the Director's decision.

Interest subsidies are addressed in 25 U.S.C. § 1511 and 25 C.F.R. § 103.42. 25 U.S.C. \§ 1511 provides:

> The Secretary is authorized under such rules and regulations as he may prescribe to pay as an interest subsidy on loans which are guaranteed or insured under the provisions of subchapter II of this chapter amounts which are necessary to reduce the rate payable by the borrower to the rate determined under section 1464 of this title.

As relevant to this appeal, 25 C.F.R. § 103.42 provides:

> (a) The Commissioner may pay an interest subsidy to lenders on loans which are guaranteed or insured under this part 103 * * *. Interest subsidy payments by the United States shall be discontinued on such loans * * * when one of the following occurs:
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> * * * * * * *
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> (5) Cash flow form [sic] the business being financed appears sufficient to pay for full debt service based on periodic review by the Commissioner. Cash flow shall

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1/ The Director also declined to approve the subordination of the guaranteed loan to a proposed new loan. Appellant does not challenge that part of the Director's decision.

be deemed sufficient to pay debt service when earnings before interest and taxes, after adjustments for extraordinary items, equal or exceed industry norms. [2/]

On August 30, 1994, the Juneau Area Director approved a 90% loan guaranty for a loan to Appellant in the amount of $2,240,000. The loan was made by the National Bank of Alaska (Bank) for the purpose of financing Appellant's construction of a bulk fuel storage facility in Nome, Alaska. Provision (F)6 of the loan guaranty requires the Bank to conduct an Annual Risk Review on the loan, and Provision (F)3 provides: "An Interest Subsidy will be applied and is to be determined at loan closing. The Annual Risk Review will determine the term of the subsidy, which can not exceed five years."

On March 24, 1997, the Bank wrote to the Juneau Area Credit Officer, stating that Appellant had requested an additional loan in the amount of $350,000 for the purpose of constructing another storage tank, which Appellant needed in order to serve its new customers. The Bank requested that BIA subordinate the existing guaranteed loan to the new loan. It also stated that Appellant "still need[s] your interest subsidy to maintain a positive cash flow."

Because of a memorandum issued by the Director on February 10, 1997, the Area Office was required to submit any request for interest subsidies to the Director for approval. 3/

The Area Credit Officer recommended that Appellant's interest subsidy be continued for another year. His recommendation was based upon a Times Debt Service (TDS) and Surplus Cash analysis of Appellant's 1996 financial reports. 4/ The Area Director forwarded the Area Credit Officer's recommendation to the Director, noting Area Office concurrence.

According to the Director's brief in this appeal, BIA staff in the Director's office analyzed Appellant's financial situation by comparing it to financial data in the Robert Morris Associates Annual Statement Studies for 1996 (RMA), under the category "Wholesalers - Petroleum Bulk Stations and Terminals." On May 5, 1997, the Director sent a memorandum to the Area Director, stating:

2/ Subsection 103.42(a)(5) was added to section 103.42 in 1992 at the same time other changes were made to Part 103. Neither the proposed nor the final rulemaking document discusses this provision, and there were apparently no public comments on it. See 56 Fed. Reg. 48082 (Sept. 23, 1991); 57 Fed. Reg. 46470 (Oct. 8, 1992).

3/ In the Feb. 10, 1997, memorandum, which was addressed to "All Area Directors," the Director noted that there had been problems with the administration of the interest subsidy program. She stated that, "until further notice, [she would] allocate interest subsidy on a case-by-case basis, relying on the Area Director's recommendation for funding allocation."

4/ In her brief in this appeal, the Director states that TDS value is "the amount a debtor has in cash to pay per dollar of annual debt service." Director's Answer Brief at 2.

Our interest subsidy commitment expired in December of 1996.

* * * * * * *

> We cannot approve the request to resume interest subsidy payments because [Appellant's] cash flow is good and sufficient to pay debt service. The regulations (25 CFR 103.42(a)(5)) require that interest subsidy payments be discontinued when earnings before interest and taxes, after adjustment for extraordinary items, equal or exceed industry norms. [Appellant's] adjusted earnings are nine percent of sales compared to the industry norm which is only about two percent.

On June 6, 1997, the Area Credit Officer informed Appellant of its right to appeal the Director's decision to the Board.

In its notice of appeal, Appellant objected to the Director's use of RMA data to identify the "industry norm" for Appellant's business. Appellant contended that it did not fall within the RMA's "wholesaler" category because its business included retailing and delivery as well as wholesale operations. It further contended that it did not fall within any of the categories listed by the RMA.

Appellant did not pursue this argument in its opening brief and, in fact, based its argument in part on figures in the RMA. The Director made note of this in her answer brief, stating that she "interpret[ed] this change of position to mean that [Appellant] has conceded that the RMA is an appropriate tool of reference for purposes of applying section 103.42(a)(5)." Director's Answer Brief at 5 n.4. Appellant did not refute the Director's statement in its reply brief and again relied on figures in the RMA to support its argument. Accordingly, the Board concludes that Appellant has abandoned its objection to the RMA.

In its opening and reply briefs, Appellant argues that its cash flow is insufficient to pay for full debt service. The Director's decision does not explain the method she used to reach her conclusion about Appellant's cash flow. Nor does anything in the administrative record explain her methodology. It was not until she filed her answer brief that she described the process by which she reached her conclusion. 5/ She explains that BIA considered the RMA term "opera-

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5/ Normally, when neither the BIA decision nor the administrative record shows how BIA reached its conclusion, the Board remands the matter to BIA. See, e.g., Reed v. Minneapolis Area Director, 19 IBIA 249 (1991); S & H Concrete Construction, Inc. v. Acting Phoenix Area Director, 19 IBIA 69 (1990). In this case, the Director has explained her reasoning in her brief on appeal, and Appellant has had an opportunity to respond. Further, as discussed below, this case turns on the interpretation of a regulation, and thus the Board has more extensive review authority here than it does in the usual case arising under the Indian Financing Act, 25 U.S.C. §§ 1451-1543. Therefore, the Board will review the merits of this matter.

The Director is reminded, however, that it is her responsibility to explain the basis of her decision and to ensure that the administrative record supports that decision.

ting profit" to be the equivalent of the term "earnings before interest and taxes" (EBIT) in 25 C.F.R. § 103.42(a)(5). Because the RMA shows "operating profit" as a percentage of total value of sales and assets, BIA made corresponding calculations from the figures shown in Appellant's financial statements. BIA found that, for businesses of the type and size of Appellant, the industry norm operating profit, as a percentage of assets, was 1.4%, and Appellant's adjusted EBIT, 6/ as a percentage of assets, was 7.3%. It also found that, for businesses of Appellant's type with similar sales, the industry norm operating profit, as a percentage of sales, was 2.1%, and Appellant's adjusted EBIT, as a percentage of sales, was 9.4%.

Appellant does not dispute these calculations. It contends, however, that the Director's methodology does not comply with 25 C.F.R. § 103.42(a)(5) because it does not analyze Appellant's cash flow and thus does not properly determine Appellant's ability to service debt. Appellant contends, inter alia, that "[t]he calculation used by the Director would not be used by a private lending institution as a measure of a business's ability to service debt." Appellant's Reply Brief at 5.

In its opening brief, Appellant advocates the use of two "coverage ratios" applied in the RMA and described therein as "measur[ing] a firm's ability to service debt." RMA Introduction at 18. These two ratios are "(1) earnings before interest and taxes divided by annual interest expense (EBIT/Interest), and (2) net profit plus depreciation, depletion, and amortization expenses, divided by the current portion of long term debt (Net Profit + Dep., Amort./Cur.Mat. L/T/D)." Appellant's Opening Brief at 7. 7/ Appellant contends that these ratios provide a better measure of Appellant's ability to service debt and that, by application of either ratio, Appellant's cash flow is shown to be insufficient to service debt and is also shown to be below the industry norm. In its reply brief, Appellant discusses only the first of the two ratios, conceding that "[t]he regulation requires the use of EBIT." Appellant's Reply Brief at 3.

The Director contends that neither ratio may be used because "[t]he implementing regulations neither direct nor permit BIA to factor in interest expenses or the amount of debt to be paid in a given year." Director's Answer Brief at 7.

Appellant focuses upon the first sentence of 25 C.F.R. § 103.42(a)(5), without taking into account the mandatory nature of the second sentence. While the first sentence calls for BIA analysis of a business's cash flow in order to evaluate its ability to service debt, the second sentence states unequivocally that, where adjusted EBIT equal or exceed industry norms, cash flow shall be deemed sufficient to pay for full debt service. When the two sentences are read together, it becomes clear that it is only when adjusted EBIT do not equal or exceed industry norms that any further analysis is either necessary or appropriate.

6/ I.e., EBIT after adjustments for extraordinary items. See 25 C.F.R. § 103.42(a)(5).

7/ Appellant states that the second ratio is the same as the Area Credit Officer's TDS calculation. Opening Brief at 8.

Appellant clearly believes that the measure described in the second sentence of 25 C.F.R. § 103.42(a)(5) is inadequate to assess a business's ability to service debt. Even assuming Appellant is correct in this regard, it would not matter here. The Board has no authority to disregard the clear import of the regulation and must apply the regulation as written. Cf., e.g., Danard House Information Services Division, Ltd. v. Sacramento Area Director, 25 IBIA 212, 218 (1994), and cases cited therein (The Board lacks authority to declare a duly promulgated regulation invalid).

Appellant does not contend that its adjusted EBIT do not equal or exceed industry norms. Thus, Appellant has not shown that the Director erred in declining to continue its interest subsidy.

Therefore, pursuant to the authority delegated to the Board of Indian Appeals by the Secretary of the Interior, 43 C.F.R. § 4.1, the Director's May 5, 1997, decision is affirmed.

//original signed
Anita Vogt
Administrative Judge

//original signed
Kathryn A. Lynn
Chief Administrative Judge