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INDIAN FINANCING AMENDMENTS ACT OF 2002

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AUGUST 28, 2002.—Ordered to be printed
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Mr. INOUYE, from the Committee on Indian Affairs,
submitted the following

R E P O R T

[To accompany S. 2017]

The Committee on Indian Affairs, to which was referred the bill (S. 2017) to amend the Indian Financing Act of 1974 to improve the effectiveness of the Indian loan guarantee and insurance program, having considered the same, reports favorably thereon with an amendment and recommends that the bill (as amended) do pass.

PURPOSE

The purpose of S. 2017 is to direct the Secretary of the Interior (Secretary) to establish a secondary market for the Indian Loan Guaranty Fund that is administered through the Bureau of Indian Affairs.

BACKGROUND

Despite a national unemployment rate of 5.6%, the jobless rate in Native American communities hovers around 50%, with some Indian economies experiencing unemployment rates near 80%. These rates are nearly twice that of the national unemployment rate in the Great Depression of the 1930's.

Despite recent success with casino gaming, energy and natural resource development, and other initiatives, most tribal communities still suffer a lack of jobs, high unemployment, intense poverty and a lack of physical infrastructure.

Given the near-complete absence of private sector enterprises in reservation communities, nearly one in three American Indians and Alaska Natives, or 31.2% lives in poverty. The earning capacity of Native communities also lags behind that of other Americans. For every \$100 earned by the average American family, an Indian fam-

ily earns \$62. Additionally, the average annual per capita income for Indians is \$8,284, far less than that for other Americans.

The challenges to economic development in Native communities are legion but one key component is a dearth of financial capital. It is well documented that Native entrepreneurs lack access to capital for both home mortgages and commercial purposes.¹

In the Community Development Banking and Financial Institutions Act of 1994, 12 U.S.C. 4701, Congress found that, “many of the nation’s urban, rural and Native American communities face critical social and economic problems arising in part from the lack of economic growth, people living in poverty, and the lack of employment and other opportunities.”

In response to these findings, the November, 2001, Community Development Financial Institutions (CDFI) Report noted a key factor in Native American communities is the lack of a financial services sector. The CDFI Report found that 61% of Native American respondents to the survey reported that business loans were rated as “impossible” or “difficult” to obtain.

In addition, a recent study by the General Accounting Office (GAO) noted that access to capital is difficult for both Indian tribes and Native people because of, among other reasons, insufficient collateral. Consequently, Natives have difficulty making funds available to meet the matching fund requirements of many Federal economic development programs.²

In response to the need to increase economic development activity on Indian lands, Congress enacted the Indian Financing Act of 1974, Pub. L. 93-262; 25 U.S.C. 1451 et seq. which established the Indian Loan Guaranty and Insurance Fund to provide Native Americans access to private money sources that would otherwise be unavailable.

The loan guaranty mechanism, of course, is not a new creation. The financial community long ago developed a system to respond to the need to encourage capital access. The system is that creation of a secondary market for loans made by originating lenders. This is the cornerstone for the nation’s private mortgage market and the core function of the Federal National Mortgage Association (Fannie Mae) and the Federal Home Loan Mortgage Corporation (Freddie Mac). A secondary market is also an important part of commercial lending.

The IFA’s Loan Guaranty and Insurance Fund program authorizes the Secretary of the Interior to guaranty or insure loans made by private lenders to individual Indians and Indian tribes. The purpose of a Federal loan guaranty is to provide financial incentives to the private lending community to engage clients and customers that are traditionally under-served.

Under the current Indian Loan Guaranty and Insurance program, the investor is not guaranteed payment if the borrower defaults on a small business loan, with little incentive for a secondary market investor to purchase these BIA-backed loans at the present time. So while the originating lender may be protected up to 90%

¹See General Accounting Office (GAO) Report on Access to Capital (December 2001); see also the Report of the “Native Lending Study”, published by the Treasury Department’s Community Development Financial Institutions Fund, November 2001.

²See General Accounting Office (GAO) Report on Economic Development: Federal Assistance Programs for American Indians and Alaska Natives, December 2001.

of the loan value, the secondary market investor is not. The Secretary is authorized to guarantee not more than 90% on any loan.

The creation in the early 1970's of the Government National Mortgage Association (Ginnie Mae) made it possible to provide credit support for Federal Housing Administration (FHA) and Veterans Administration (VA) mortgages. In turn, this made it possible for home mortgage lenders to sell loans into the secondary market. Secondary market investors can purchase a number of these loans, pool them and then auction off pieces of the pool. This tends to spread and minimize the risk of default among a number of investors. Secondary market activities have also grown in the markets for a wide range of other traded securities. It is now common for lenders to sell car loans, credit card notes, lease contracts, and intellectual property royalties.

Lenders report much difficulty in selling Native American small business loans in a secondary market and having vital capital tied up on existing Native American loans without the ability to liquidate them in order to make new loans.

S. 2017 establishes a procedure by which the ownership of portions of BIA loans are transferred from the original lender to the secondary market. The rights and obligations of owning the loan, including the liability for default, are transferred to any person that wishes to pay for the entire loan. Persons who wish to pay only up to 90% of the value of the loan do not incur liability for default, which would continue to rest with the 10% value of the original lender's interest.

Once the loan is sold, the original lender would notify the BIA of the sale of that loan. The lender would remain obligated under the original guarantee agreement between the original lender and the BIA. The original lender would continue to be responsible for servicing the loan and would remain the secured creditor of record.

With every loan that is sold to a secondary investor, the full faith and credit of the United States is provided and serves as a guaranty to the secondary market investor that if the borrower defaults on the loan, the investor will continue to be paid.

SUMMARY OF SUBSTITUTE TO S. 2017

As introduced, S. 2017 establishes a secondary market for the Indian Loan Guaranty Fund authorized by the Indian Financing Act of 1974. A section-by-section description of the changes contained in the substitute amendment follows.

Section 1. Short title

This Act may be cited as the "Indian Financing Amendments Act of 2002".

Section 2. Findings and purposes

This section states the findings and purposes of S.2 017 and notes the reasons why there is a need to establish a secondary market program for both the Indian Loan Guaranty Fund and the Indian Loan Insurance Program.

Section 3. Amendments to the Indian Financing Act

This section sets forth the procedures necessary to establish a secondary market for both the Indian Loan Guaranty Fund and the

Indian Loan Insurance Program. The Indian Loan Guaranty Fund provides Federal guarantees for Indian small business loans by either an individual Indian (up to \$1.5 million) or by an Indian tribe or tribal entity (up to \$5.5 million). The Indian Loan Insurance Program provides Federal guarantees for Individual Indian small business loans (up to \$100,000).

The Indian Loan Insurance Program limitation on loan amounts is changed from \$100,000 to \$250,000.

The full faith and credit clause to guarantee loans in both the Loan Guaranty Fund and the Loan Insurance Program applies to all future loans made under either program. Current loans existing within the program will not fall under this legislation.

LEGISLATIVE HISTORY

The Indian Financing Amendments Act of 2002 (S. 2017) was introduced on March 14, 2002, by Senator Campbell, for himself, and for Senator Inouye. Subsequent to March 14, Senators Domenici, and Johnson were added as co-sponsors. S. 2017 was referred to the Committee on Indian Affairs and a hearing was held on the bill on April 24, 2002. On July 30, 2002, the Committee on Indian Affairs convened a business meeting to consider S. 2017 and other measures that had been referred to it, and on that date, the Committee favorably reported a substitute amendment to S. 2017.

COMMITTEE RECOMMENDATION AND TABULATION OF VOTE

On July 30, 2002, the Committee on Indian Affairs, in an open business session, adopted an amendment in the nature of a substitute to S. 2017 by voice vote and ordered the bill, as amended, reported favorably to the Senate.

COST AND BUDGETARY CONSIDERATION

The cost estimate for S. 2017 as calculated by the Congressional Budget Office, is set forth below:

U.S. CONGRESS,
CONGRESSIONAL BUDGET OFFICE,
Washington, DC, August 27, 2002.

Hon. DANIEL K. INOUE,
Chairman, Committee on Indian Affairs,
U.S. Senate, Washington, DC.

DEAR MR. CHAIRMAN: The Congressional Budget Office has prepared the enclosed cost estimate for S. 2017, the Indian Financing Amendments Act of 2002.

If you wish further details on this estimate, we will be pleased to provide them. The CBO staff contact is Lanette J. Walker.

Sincerely,

BARRY B. ANDERSON
(For Dan L. Crippen, Director).

Enclosure.

S. 2017—Indian Financing Amendments Act of 2002

S. 2017 would allow lenders of any loans guaranteed or insured under the Indian Financing Act of 1974 to sell such loans to the

secondary market. CBO estimates that implementing this bill would have no significant budgetary impact. Because the legislation could affect direct spending, pay-as-you-go procedures would apply, but CBO estimates that such effects would be insignificant.

Under this bill, loans transferred from lenders to secondary markets would continue to be guaranteed and insured by the federal government. Based on information from the Department of the Interior (DOI), CBO estimates that the annual cost of administering such transfers would be negligible over the 2003–2007 period. Any costs incurred by DOI to administer the program would be subject to the availability of appropriated funds.

S. 2017 also would authorize the Secretary of the Interior to collect a fee for any guaranteed or insured loan being transferred. Allowing the Secretary to impose fees on such transfers could reduce the subsidy cost of the guarantees and insurance the DOI has provided for existing loans under the Indian Financing Act. Based on information from DOI, CBO estimates that the change in direct spending would be negligible, however, because it is unlikely that the department would collect these fees.

S. 2017 contains no intergovernmental or private-sector mandates as defined in the Unfunded Mandates Reform Act and would impose no costs on state, local, or tribal governments.

This estimate was approved by Peter H. Fontaine, Deputy Assistant Director for Budget Analysis. The CBO staff contact for this estimate is Lanette J. Walker.

REGULATORY IMPACT STATEMENT

Paragraph 11(b) of rule XXVI of the Standing Rules of the Senate requires that each report accompanying a bill to evaluate the regulatory paperwork impact that would be incurred in implementing the legislation. The Committee has concluded that enactment of S. 2017 will create only de minimis regulatory or paperwork burdens.

EXECUTIVE COMMUNICATIONS

The Committee has received no official communication from the Administration on the provisions of the bill.

CHANGES IN EXISTING LAW

In compliance with subsection 12 of rule XXVI of the Standing Rules of the Senate, the Committee states that the enactment of S. 2017 will result in the following changes in 25 U.S.C. Sec. 1451 et seq., with existing language which is to be deleted in black brackets and the new language to be added in italic:

Be it enacted by the Senate and House of Representative of the United States of America in Congress assembled,

SHORT TITLE.—This Act may be cited at the “Indian Financing Act Amendments of 2002”.

FINDINGS AND PURPOSE.— * **

(A) FINDINGS.—Congress finds that—

(i) the Indian Financing Act of 1974 (25 U.S.C. 1451 et seq.) was intended to provide Native American borrowers with access to commercial capital sources that,

but for that Act, would not be available through loans guaranteed by the Secretary of the Interior;

(ii) although the Secretary of the Interior has made loan guarantees available, acceptance of loan guarantees by lenders to benefit Native American business owners has been limited;

(iii) 27 years after enactment of the Act, the promotion and development of Native American business remains an essential foundation growth of economic and social stability of Native Americans;

(iv) acceptance by lenders of the loan guarantees may be limited by liquidity and other capital market-driven concerns; and

(v) it is in the best interest of the guaranteed loan program to—

i. encourage the orderly development and expansion of a secondary market for loans guaranteed by the Secretary; and

ii. expand the number of lenders originating loans under that Act.

(B) PURPOSE.—The purposes of this Act are—

(i) to stimulate the use by lenders of secondary market investors for loans guaranteed by the Secretary of the interior;

(ii) to preserve the authority of the Secretary to administer the program and regulate lenders;

(iii) to clarify that a good faith investor in loans guaranteed by the Secretary will receive appropriate payments;

(iv) to provide for the appointment by the Secretary of a qualified fiscal transfer agent to administer a system for the orderly transfer of the loans;

(v) to authorize the Secretary to—

i. promulgate regulations to encourage and expand a secondary market program for loans guaranteed by the Secretary; and

ii. allow the pooling of the loans as the secondary market develops; and

(vi) to authorize the Secretary to establish a schedule for assessing lenders and investors for the necessary costs of the fiscal transfer agent and system.

* * * * *

25 U.S.C. 1485

(a) *IN GENERAL.*—Any loan guaranteed under this subchapter, including the security given for such loan, may be sold or assigned by the lender to any persons.

(b) *TRANSFER OF LOANS AND UNGUARANTEED PORTIONS OF LOANS.*—

(1) *TRANSFER.*—

(A) *IN GENERAL.*—The lender of a loan guaranteed under this title may transfer to any person—

(i) all of the rights and obligations of the lender under the loan, or in an unguaranteed portion of the loan; and

(ii) the security given for the loan or unguaranteed portion.

(B) REGULATIONS.—A transfer under subparagraph (A) shall be consistent with such regulations as the Secretary shall promulgate under subsection (g).

(C) NOTICE.—A lender that completes a transfer under subparagraph (a) shall give notice of the transfer to the Secretary (or a designee of the Secretary).

(2) EFFECT OF TRANSFER.—On any transfer under this subsection, the transferee shall—

(A) be considered to be the lender under this title;

(B) become the secured party of record; and

(C) be responsible for—

(i) performing the duties of the lender; and

(ii) servicing the loan or portion of the loan, as appropriate, in accordance with the terms of guarantee of the Secretary of the loan or portion of the loan.

(D) TRANSFER OF GUARANTEED PORTIONS OF LOANS.—

(i) TRANSFER.—

i. IN GENERAL.—The lender of a loan guaranteed under this title, and any subsequent transferee of all or part of the guaranteed portion of the loan, may transfer to any person—

(i) all or part of the guaranteed portion of the loan; and

(ii) the security given for the guaranteed portion transferred.

ii. REGULATIONS.—A transfer under subparagraph (A) shall be consistent with such regulations as the Secretary shall promulgate under subsection (g).

iii. NOTICE.—A lender that completes a transfer under subparagraph (A) shall give notice of the transfer to the Secretary (or a designee of the Secretary).

iv. ACKNOWLEDGEMENT.—On receipt of notice of a transfer under subparagraph (C), the Secretary (or a designee of the Secretary) shall issue to the transferee the acknowledgement of the Secretary of—

(i) the transfer; and

(ii) the interest of the transferee in the guaranteed portion of a loan that was transferred.

(ii) EFFECT.—Notwithstanding any other provision of law, with respect to any transfer under this subsection, the lender shall—

i. remain obligated under the guarantee agreement between the lender and the Secretary;

ii. continue to be responsible for servicing the loan in a manner consistent with the guarantee agreement; and

iii. remain the secured creditor of record.

(E) FULL FAITH AND CREDIT.—

(i) **IN GENERAL.**—*The full faith and credit of the United States is pledged to the payment of all loan guarantees made under this title.*

(ii) VALIDITY.—

i. **IN GENERAL.**—*Except as provided in subparagraph (B), the validity of a guarantee of a loan under this title shall be incontestable if the guarantee is held by a transferee of a guaranteed obligation whose interest in a guaranteed loan has been acknowledged by the Secretary (or a designee of the Secretary) under subsection (c)(1)(D).*

ii. **FRAUD OR MISREPRESENTATION.**—*Subparagraph (A) shall not apply in a case in which the Secretary determines that a transferee of a loan or a portion of a loan transferred under this section has actual knowledge of fraud or misrepresentation, or participates in or condones fraud or misrepresentation, in connection with the loan.*

(F) DAMAGES.—*The Secretary may recover from a lender any damages suffered by the Secretary as a result of a material breach of an obligation of the lender under the guarantee of the loan.*

(G) FEE.—*The Secretary may collect a fee for any loan or guaranteed portion of a loan transferred in accordance with subsection (b) or (c).*

(H) REGULATIONS.—*Not later than 180 days after the date of enactment of this subsection, the Secretary shall promulgate such regulations as are necessary to facilitate, administer, and promote the transfer of loans and guaranteed portions of loans under this section.*

(I) CENTRAL REGISTRATION.—*On promulgation of final regulations under subsection (g), the Secretary shall—*

(i) *provide for the central registration of all loans transferred under this section; and*

(ii) *contract with a fiscal transfer agent—*

i. *to act as a designee of the Secretary; and*

ii. *on behalf of the Secretary—*

(i) *to carry out the central registration and paying agent functions; and*

(ii) *to issue acknowledgements of the Secretary under subsection (c)(1)(D).*

(J) POOLING.—

(i) **IN GENERAL.**—*Nothing in this title prohibits the pooling of whole loans, or portions of loans, transferred under this section.*

(ii) **REGULATIONS.***The Secretary may promulgate regulations to effect orderly and efficient pooling procedures under this title.*

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