

**TO:** Rural Development State Directors

**ATTN:** Deputy Administrator of Community Programs  
Area Directors  
CF Loan Specialists  
Housing Program Directors  
State Environmental Coordinators  
State Architects

**FROM:** Tammye Treviño (Signed by Tammye Treviño)  
Administrator  
Housing and Community Facilities Programs

**SUBJECT:** Response to CF MCR findings from the 2011 MCR

**PURPOSE AND INTENDED OUTCOME**

This Administrative Notice (AN) provides guidance on Agency compliance with construction and development requirements as established in RD Instruction 1942-A, that are critical to the success of Community Facilities (CF), Direct Loan, Guarantee Loan and Grant programs. Results from the 2011 Management Control Review (MCR) for CF Programs revealed several areas of concern regarding the design and construction process and the required documentation for projects funded by the CF Programs. This AN shall serve as clarification to the guidance and direction provided in RD Instruction 1942-A, related to construction and the construction process including the need and requirements for 1) Agency contract concurrence, 2) the value and requirements of a builder's warranty and 3) proper documentation of the project process with respect to environmental and architectural requirements.

**COMPARISON WITH PREVIOUS AN**

There is no previous Administrative Notice on this subject.

**EXPIRATION DATE:**  
February 28, 2013

**FILING INSTRUCTIONS:**  
Preceding RD Instruction 1942-A  
& 1940-G

## **IMPLEMENTATION RESPONSIBILITIES**

Field staff involved in the CF Direct Loan, Guaranteed Loan and Grant Programs process should review the construction requirements established in RD Instruction 1942-A and this AN in order to implement the proper procedures and requirements.

**1) Agency contract concurrence: Professional contracts:** The contract could be a Rural Development form or a commercially available document that is considered acceptable by the industry. The language in the contract should be fair to all parties and be adequate to achieve the expected outcome. Very specific language will bring the greatest chance of a successful result. Any requirements that are weak on specifics may open a door for interpretation, risk exclusion from the agreement or cause the need for a contract change order.

Written agreements better protect the owner, Agency and the contractor from misunderstandings, claims and disputes. When possible, the draft contract should be reviewed by the Rural Development Staff prior to the final agreement to assess the adequacy of the documents. The contract documents may include a legal contract with any standard and special conditions addressed and resolved. Rural Development shall be an integral part of the contract document development process for the benefit of the Agency and the applicant. Reference § 1942.17(l) and 1942.18(b) of RD Instruction 1942-A as follows:

1942.17(l)

(1)

*Professional services.*

*Applicants will be responsible for providing the services necessary to plan projects including design of facilities, preparation of cost and income estimates, development of proposals for organization and financing, and overall operation and maintenance of the facility. Professional services of the following may be necessary: [e]ngineer, architect, attorney, bond counsel, accountant, auditor, appraiser, and financial advisory or fiscal agent (if desired by applicant). Contracts or other forms of agreement between the applicant and its professional and technical representatives are required and are subject to [Agency] concurrence. Form [RD] 1942-19, "Agreement for Engineering Services," may be used when appropriate. Guide 20, "Agreement for Engineering Services ([Agency]/EPA - Jointly Funded Projects)," may be used on projects jointly funded by the [Agency] and EPA. Guide 14 may be used in the preparation of the legal services agreement. Guide 27, Attachment 1 to AIA Document B141, 1997 Edition, "Standard Form of Agreement Between owner and Architect," is approved by the Agency and may be used when appropriate.*

1942.18

*(b) Technical services. Owners are responsible for providing the engineering or architectural services necessary for planning, designing, bidding, contracting, inspecting, and constructing their facilities. Services may be provided by the owner's "in house" engineer or architect or through contract, subject to Rural Development concurrence. Architects and engineers must be licensed in the State where the facility is to be constructed.*

**Substantial Completion Certificate:** Substantial Completion is the construction contract end date. The contract duration extends from the Notice to Proceed date to the Substantial Completion date. Once this date is achieved the contractor typically has a reasonable duration to achieve final completion of the project by continuing work on minor items taken from an inspection report or "Punch List". When the construction is determined to be substantially complete the possible assessment of liquidated damages ceases and the warranty period for the contractor's labor, installed materials and equipment begins.

When Guide 27 is used, note that 1942-A Guide 27 Attachment 1 provides:

*2.6.6.1 The Architect shall conduct an inspection prior to the issuance of the Certificate of Substantial Completion and shall submit a written report to the Owner, Agency and the Contractor about Work to be completed prior to final acceptance. Said inspection and Certificate of Substantial Completion shall be provided by the Architect for each Prime Contractor as appropriate. Such services shall be coordinated with the Agency. Prior to submitting the final Certificate for Payment, the Architect shall conduct an inspection, submit a Statement of Completion, receive and forward to the Owner, for the Owner's review and records, written warranties and related documents required by the Contract Documents and assembled by the Contractor.*

**2) The Value and Requirements of a builder's Warranty.** Warranties are critical to the performance of a construction contract. The terms and conditions of the Warranty provide protection to the owner from latent and unexpected failures, as well as, errors and omissions by the contractor. The contractor's performance/workmanship typically is covered for one year following substantial completion of the project.

*1942A Guide 19 Attachment 9:*

*29.1 The CONTRACTOR shall guarantee all materials and equipment furnished and WORK performed for a period of one (1) year from the date of SUBSTANTIAL COMPLETION. The CONTRACTOR warrants and guarantees for a period of one (1) year from the date of SUBSTANTIAL COMPLETION of the system that the completed system is free from all defects due to faulty materials or workmanship and the CONTRACTOR shall promptly make such corrections as may be necessary by reason of such defects including the repairs of any damage to other parts of the system resulting from such defects. The OWNER will give notice of observed defects with reasonable promptness. In the event that the CONTRACTOR should fail to make such repairs, adjustments, or other WORK that may be made necessary by such defects, the OWNER may do so and charge the CONTRACTOR the cost thereby incurred. The Performance BOND shall remain in full force and effect through the guarantee period*

### **3) Proper documentation of the project process with respect to environmental requirements.**

#### **A) Wetland Impact**

#### **ConAct Prohibition of**

The MCR review revealed that in some cases, the following ConAct prohibitions were not being adhered to. Please make a note of the following wetland impact prohibitions for the CF Program.

Section 363 of the Consolidated Farm and Rural Development Act (the ConAct) (7 U.S.C. 2006e) prohibits “. . . any loan to drain, dredge, fill, level, or otherwise manipulate a wetland (as defined in . . . 16 U.S.C. 3801(a)(16)) or to engage in any activity that results in impairing or reducing the flow, circulation, or reach of water, except in the case of activity related to the maintenance of previously converted wetlands, or in the case of such activity that is already commenced before November 28, 1990. This section shall not apply to a loan made or guaranteed under [the Con Act] for a utility line.”

However, please also note that the Consolidated and Further Continuing Appropriations Act, 2012 recently modified section 363 of the ConAct by providing a fiscal year 2012 waiver from the above wetland prohibition for CF programs only. This waiver states:

*Sec. 744.* For fiscal year 2012, section 363 of the Consolidated Farm and Rural Development Act (7 U.S.C. 2006e) shall not apply to a project funded under the community facilities programs authorized under such Act if such project is also subject to approval of a permit issued under section 404 of the Federal Water Pollution Control Act (33 U.S.C. 1344). This provision only applies for FY 2012.

## **B) FEMA Form 81-93 - Flood Insurance Requirements**

The MCR review revealed that in some cases, the FEMA Form 81-93 and documentation of flood insurance was not included in the project file. RD Instruction 1806-B requires and AN 4562 specifies that a FEMA Form 81-93 Form be completed and included in the project file and flood insurance is required “. . .*whenever federal agency lender financing, including **direct** or **guaranteed loans**, is secured by a lien on improved real estate, where a building is or will be located, within the 100-year floodplain (or Special Flood Hazard Area (SFHA)) (from AN 4562).*”

*Some exceptions to this requirement, from AN 4562, are as follows:*

- **Grants.** *All grants are excluded from the mandatory purchase requirement according to the provisions of the NFIRA of 1994.*
- **Land Only.** *The National Flood Insurance Program does not insure land and the law does not address mortgages secured by land alone (without buildings);*
- **Inventory.** *Flood insurance is not required for a loan financing inventory where the secured collateral is stored in a building located in a 100-year floodplain and the building is not security for the loan; flood insurance for personal property is not required by law for residential loans in the SFHA, flood insurance for personal property or inventory for commercial loans in the SFHA is not required by law unless the personal property/inventory, in addition to a building, secures the loan.*
- **Small loans.** *If the original outstanding principal balance is \$5,000 or less with a repayment term of 1 year or less, the SFHDF and flood insurance is not required. The dual criteria must be met in order for this exemption to apply; and*
- **Federal/State Owned Property.** *If the security property is Federal or State-owned property and covered by adequate policies of self-insurance (refer to the list at 44 CFR, Chapter 1, Part 75), flood insurance is not required. This does not apply to county- or city-owned property.*

As specified in AN 4562 the FEMA Form 81-93 is required to determine if flood insurance will be required on a particular “building”. *“The mandatory purchase provisions of the NFIRA of 1994 direct federally regulated lenders and Federal agency lenders to not make, increase, renew, or extend any loan on applicable property unless flood insurance is purchased and maintained to protect that property securing loans in a SFHA. The statutory requirements apply when improved real property (e.g., a building) or manufactured (mobile) home is taken as security for financing.”*

Further note that RD Instruction 1806-B states: *“In addition to an applicant meeting the requirements for the type of financial assistance requested, the following requirements for eligibility of applicants for financial assistance for acquisition and construction purposes in designated special flood and mudslide-prone areas must be met:*

- A. If flood insurance is available, to be eligible after March 1, 1974, the applicant must have purchased a flood insurance policy at the time the loan or grant is closed.*
- B. Applicants will not receive financial assistance in those communities that have been notified as having special flood and mudslide-prone areas and where flood insurance is not available within 1 year after such notification, or by July 1, 1975, whichever is later.”*

**C) Preliminary and Final Public Notice, and Private Party Notice of Important Resource Impact**

The MCR review revealed that in some cases, the preliminary and final public notice requirements and the private party notice requirements were not being adhered to when the proposal contained impacts to floodplains, wetlands, important farmlands, or historic properties as required by 1940-G Exhibit C. Please make a note of the following requirements and ensure inclusion in the project file.

**Preliminary Notice 1940-G Exhibit C (2)(b)(3)(b)**

*(b) Inform the Public - The Departmental Regulation requires us in Section 6, Responsibilities, to notify the affected landholders at the earliest time practicable of the proposed action and to provide them an opportunity to review the elements of the action and to comment on the action's feasibility and alternatives to it. This notification requirement only applies to Class I and Class II actions and not to categorical exclusions that lose their status as an exclusion for any of the reasons stated in §1940.317(e) of this subpart. The notification will be published and documented in the manner specified in §1940.331 of this subpart and will contain the following information:*

- (i) A brief description of the application or proposal and its location;*
- (ii) The type(s) and amount of important land resources to be affected;*
- (iii) A statement that the application or proposal is available for review at an FmHA . . . field office (specify the one having jurisdiction over the project area); and*
- (iv) A statement that any person interested in commenting on the application or proposal's feasibility and alternatives to it may do so by providing such comments to FmHA . . . within 30 days following the date of publication. (Specify the FmHA . . . office processing the application or proposal for receipt of comments.) Further consideration of the application or proposal must be delayed until expiration of the public comment period. Consequently, publication of the notice as early as possible in the review process is both in the public's and the applicant's interest. Any comments received must be considered and addressed in the subsequent Agency analysis of alternatives and mitigation measures. It should be understood that scheduling a public information meeting is not*

*required but may be helpful based on the number of comments received and types of issues raised.*

**Final Notice 1940-G Exhibit C (3)(d)**

*d. Additional Notification Requirement.*

*(1) Final Notice - Where it is not possible to avoid an impact to a floodplain or wetland and after all practicable mitigation measures have been identified and agreed to by the prospective applicant, a final notice of the proposed action must be published. This notice will either be part of the notice required for the completion of a Class II assessment or a separate notice if a Class I assessment or an EIS has been completed for the action. The notice will be published and distributed in the manner specified in §1940.331 of this subpart and contain the following information.*

- (a) A description of the proposed action, its location, and the surrounding area;*
- (b) A description of the floodplain or wetland impacts and the mechanisms to be used to mitigate them;*
- (c) A statement of why the proposed action must be located in a floodplain or a wetland;*
- (d) A description of all significant facts considered in making this determination;*
- (e) A statement indicating whether the actions conform to applicable State or local floodplain protection standards; and (f) A statement listing other involved agencies and individuals.*

*(2) Private Party Notification- For all actions to be located in floodplains or wetlands in which a private party is participating as an applicant, purchaser, or financier, it shall be the responsibility of the approving official to inform in writing all such parties of the hazards associated with such locations.*

**D) Signed Finding of No Significant Impact (FONSI)**

The MCR review revealed that in some cases, a signed FONSI notice (1940-G Exhibit I) as specified in 1940.318 (j) and 1940.319 (j) were not included in the project file. Please make a note of the following requirements and ensure inclusion in the project file.

***1940.318 (j) The approving official will review the environmental file and recommendations. The official will then execute the environmental impact determination and findings. If the conclusions reached are that there is no significant impact and there is compliance with the listed requirements, the format contained in Exhibit I of this subpart will be used. If a significant impact is determined, the steps specified in §1940.320 of this subpart will be initiated for the preparation of the EIS. If a determination is made that the proposed action does not comply with the environmental requirements that are explained in this subpart and listed in Item 10b of Form FmHA . . . 1940-21 for a Class I action or Item XXlb of Exhibit H of this subpart for a Class II action and there are no feasible alternatives (practicable alternatives when required by specific provisions of this subpart), modifications, or mitigation measures which could comply, the action will be denied or disapproved. If the approving official's determination or findings differ from the recommendations of the preparer,***

*concurring official or the SEC, this difference will be addressed in the manner specified in §1940.316 of this subpart.*

***1940.319 (j) Exhibit I will be completed by the approval official in the same instances for a Class I assessment as for a Class II assessment. However, public notification of FmHA's . . . finding of no significant environmental impact will not be required for a Class I assessment. Also, special provisions for completing a Class I assessment for an action that is normally categorically excluded but loses its classification as an exclusion are contained in §1940.317(g) of this subpart. With the exception of the two preceding sentences, all other procedural requirements of the assessment process, such as the timing of the assessment and the limitations on the applicant's actions, apply to a Class I assessment.***

### **POINT OF CONTACT**

Please direct all questions pertaining to this AN to your State Architect or the National Office Program Support Staff: William Downs, Program Support Staff, at (202) 720-1499 or email: [william.downs@wdc.usda.gov](mailto:william.downs@wdc.usda.gov).