



Financial Compliance

USDA RUS ReConnect Program



Rural Development



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Agenda

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- Ineligible Costs
- Advance of ReConnect Funds
- Disbursement of ReConnect Funds
- Project Completion
- Affiliated Transactions
- Loan Security
- Grant Security
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- Reporting Requirements
- Records Retention
- Disallowances
- Conditions of Award Documents
- Affirmative Covenants of Award Documents
- Negative Covenants of Award Documents
- RUS Rights

Compliance Resources



Compliance Resources

- ReConnect Funding Opportunity Announcement – Round One (FOA)
- Award Documents (Loan/Grant and Security Agreements)
- ReConnect Program Construction Procedures
- ReConnect Loan and Grant Program Website: <https://www.usda.gov/reconnect>

Cross-Referencing Compliance Resources

- The FOA requires that all project assets must comply with the ReConnect Program Construction Procedures
- The FOA requires Awardees to comply with all terms, conditions, affirmative covenants, and negative covenants contained in the award documents.
- The FOA, ReConnect Program Construction Procedures, and Award documents all reference other regulations that must be followed.

Eligible Costs



Eligible Costs

- FOA
 - Construction or improvements of facilities required to provide broadband service.
 - Reasonable preapplication expenses (limited to 5% of the award)
 - Acquisition of an existing system (Limited to 40% of the amount requested and only financed with 100% loan category)
 - Terrestrial based facilities for providing satellite broadband service
 - All costs are also subject to the cost principles found in 2 CFR part 200 and must be reasonable, allocable, and necessary to the project

Eligible Costs (continued)

- Award Documents (Section 3.4 Project)
 - Solely to finance the broadband infrastructure project specifically described in the RUS approved application.
 - Must have written approval of RUS for any material change to the network design, construction, buildout timeline, delivery of services, and/or objectives of the project
- ReConnect Construction Procedures
 - Only **new** materials and equipment

Ineligible Costs



Ineligible Costs

FOA

- Operating expenses
- Costs incurred prior to the date the application was submitted to RUS (except for approved preapplication expenses)
- Preapplication expenses incurred prior to the publication of the FY2019 FOA (December 14, 2018)
- Acquisitions of an affiliate, or purchases or acquisitions of any facilities or equipment of an affiliate
- Transactions with an affiliate that do not have specific written approval from RUS in advance
- Acquisitions of a system previously funded by RUS
- Purchases or leases of vehicles (except those used primarily in construction or system improvements)

Ineligible Costs (continued)

FOA

- Broadband facilities leased under and operating lease or Indefeasible right of use (IRU) agreement.
- Mergers or consolidations of entities
- Acquiring spectrum as part of an FCC auction or in a secondary market acquisition
- Facilities that provide mobile services
- Acquisitions of systems already providing sufficient broadband access
- Refinancing outstanding debt

ReConnect Construction Procedures

- Material or equipment purchased or construction performed prior to an award offer accepted by the applicant

Advance of ReConnect Funds



Advance of ReConnect Funds

Pledged Deposit Account

- Award Documents (Section 5.4 Deposit of Advances into Pledged Deposit Account)
 - Must open and maintain a deposit account pledged to RUS
 - Insured by FDIC or other federal agency acceptable to RUS
 - Identified by RUS' designation of the Awardee followed by "Pledged Deposit Account"
 - Promptly deposit all advances of award funds
 - Promptly deposit any previous disbursements that have been disallowed by RUS
 - Matching funds as well as other funds must be maintained on deposit in the Pledged Deposit Account unless expended and withdrawn as authorized by RUS
 - First lien on Pledged Deposit Account
 - Awardee consents ACH electronic payments directly into the Pledged Deposit Account

Advance of ReConnect Funds (continued)

Pledged Deposit Account

- ReConnect Construction Procedures
 - Must open and maintain a deposit account pledged to RUS
 - Insured by FDIC or other federal agency acceptable to RUS
 - All advances will be electronically deposited into the Pledged Deposit Account
 - All matching and/or funds required for project completion as stated in the Award Documents must be deposited into the Pledged Deposit Account at award closing
 - RUS may require that other funds be deposited into the Pledged Deposit Account
 - Match, equity or general fund contributions for project completion
 - Proceeds from the sale of property
 - Interest received on award funds and similar types of receipts
- FOA
 - No funds will be disbursed until all other sources of funding have been obtained and any other pre-award conditions have been met.

Advance of ReConnect Funds (continued)

General

- FOA
 - All matching funds or cash provided in lieu of loan funds must be expended first, followed by loan funds, and then by grant funds (except approved pre-application expenses)
 - Grant funds will be used for approved pre-application expenses (first advance request only)
- Award Documents
 - Section 4.3 Conditions to Individual Advances: All approved matching funds are to be expended before a request of loan or grant funds (except approved pre-application expenses)
 - Section 4.4 First Advance to Pay Off Pre-Application Expenses: Grant Funds will be used to pay off approved pre-application expenses included on the first advance.

Advance of ReConnect Funds (continued)

RUS Form 481 – Financial Requirement Statement (FRS)

- Award Documents (Section 4.3 Conditions to Individual Advances)
 - Requests for award funds must be made on an FRS
 - Requests should not be submitted more frequently than once per month
 - Advance requests are to be limited to immediate disbursement needs
 - Award advances are on a reimbursement basis, or based on unpaid 3rd party invoices
- ReConnect Construction Procedures
 - To request advances, Awardee must submit FRS
 - All matching funds will be treated as award funds and recorded appropriately on the FRS
 - Shall request funds in the first advance request to pay eligible pre-application expenses
 - Request advances as needed to meet obligations promptly (<60 days)

Disbursement of ReConnect Funds



Disbursement of ReConnect Funds

Award Documents

- Section 5.2 – Use of Advances: Expend award funds only for eligible purposes in accordance with the RUS approved line item project budget and FRS submitted prior to the advance of funds
- Section 5.4 – Deposit of Advances into Pledged Deposit Account: Moneys in the Pledged Deposit Account shall be used solely for the purposes for which advances were made (FRS) - Any exception must be approved in writing

Disbursement of ReConnect Funds (continued)

ReConnect Construction Procedures

- Funds in Pledged Deposit Account shall be used solely for the purposes approved in the application and shall be disbursed for the approved purposes for which they were requested on the FRS
- Funds should be disbursed for the item for which they were advanced
- Interest earned must remain in Pledged Deposit Account and cannot be disbursed without RUS approval

Project Completion



Project Completion

FOA

- Projects must be completed within 5 years from the date funds are first made available
- Build-out is considered complete when the network design has been fully implemented, the service operations and management systems infrastructure is operational, and the awardee is ready to support the activation and commissioning of individual customers to the new system

Award Documents (Section 3.1 Loan and Grant Amounts, Interest Rate, and Expiration Date)

- Expiration date = 5 years from the release of funds date

Affiliated Transactions



Affiliated Transactions

Award Documents (Section 7.13 Affiliated Transactions)

- The Awardee shall not enter into any transaction, contract, or dealing with an Affiliate of the Awardee or with the Awardee's or Affiliate's directors, trustees, officers, managers, members (if the Awardee is a limited liability company), or other corporate officials, without the prior written consent of RUS. RUS' consent to advance loan funds for affiliated transactions will be limited to an amount which is the lower of cost or market rate and which is subject to verification by RUS and its representatives having access to the books and records of the Affiliate

Affiliated Transactions (continued)

Award Documents (Article I – Definitions)

- "Affiliate" or "Affiliated Company" of any specified person or entity means any other person or entity directly or indirectly controlling of, controlled by, under direct or indirect common control with, or related to, such specified person or entity, or which exists for the sole purpose of providing any service to one company or exclusively to companies which otherwise meet the definition of affiliate. This definition includes Variable Interest Entities as described in Financial Accounting Standards Board Interpretation (FIN) No. 46(R), Consolidation of Variable Interest Entities. For the purpose of this definition, "control" means the possession directly or indirectly, of the power to direct or cause the direction of the management and policies of a company, whether such power is exercised through one or more intermediary companies, or alone, or in conjunction with, or pursuant to an agreement with, one or more other companies, and whether such power is established through a majority or minority ownership voting of securities, common directors, officers, or stockholders, voting trust, holding trusts (other than money exchanged) for property or services

Affiliated Transactions (continued)

ReConnect Construction Procedures

- With regard to the Project, the Awardee shall not enter into any transaction, contract, or dealing with an Affiliate of the Awardee or with the Awardee's or Affiliate's directors, trustees, officers, managers, members (if the Awardee is a limited liability company), or other corporate officials, without the prior written consent of RUS. RUS' consent to advance award funds for affiliated transactions will be limited to an amount which is the lower of cost or market rate and which is subject to verification by RUS and its representatives having access to the books and records of the Affiliate.

Loan Security



Loan Security

FOA

- Secured by all assets of the Awardee
 - RUS given an exclusive first lien on all assets of the Awardee, including all revenues
 - RUS may share first lien on a *pari passu* basis (if security arrangements are satisfactory to RUS)
 - Will not share assets with any related party or affiliate of the Awardee
 - Tribal and Municipalities' security terms will be developed separately
 - All property and facilities purchased with award funds must be owned by the Awardee
- The sale or lease of any portion of the Awardee's facilities must be approved in writing by RUS

Loan Security (continued)

Award Documents (Section 9.1 Collateral)

- Awardee hereby pledges, assigns, and transfers to RUS, and grants to RUS a continuing security interest in ALL ASSETS of the Awardee, whether now owned or hereafter acquired
- Awardee also covenants that it will enter into a mortgage in favor of RUS for any real property that is acquired while any Note is outstanding
- Section 7.4 Additional Indebtedness: No additional indebtedness without prior written consent of RUS
 - Secured or unsecured

Grant Security



Grant Security

FOA

- Exclusive first lien on all grant assets during the service obligation of the grant
- Any sale or disposition of grant assets must comply with 2 CFR part 200
- Must repay the grant if the project is sold, transferred, or merged without RUS approval during the service obligation of the grant
- The sale or lease of any portion of the Awardees facilities must be approved in writing by RUS
- All property and facilities purchased with award funds must be owned by the Awardee

Grant Security (continued)

Award Documents (Section 9.2 Special Security with Respect to Grant Assets)

- Government must be provided with an exclusive first lien on all grant assets during the Service Obligation of the Award
 - Shall not be shared *pari passu* with any other entity
- Any sale or disposition of grant assets must comply with 2 CFR part 200
- Section 9.3 Unapproved Sale of Grant Assets: Must repay all funds advanced under the grant to the government if the Project or Awardee is sold or merged without RUS approval during the Service Obligation of the grant

RUS Right to Inspect



RUS Right to Inspect

FOA

- Awardee must comply with all reasonable Agency requests to support ongoing monitoring efforts
- Awardee shall afford RUS, through its representatives, reasonable opportunity, at all times during business hours and upon prior notice, to have access to and the right to inspect:
 - Broadband system or other property encumbered by the Award Documents
 - Any and all books, records, accounts, invoices, contracts, leases, payrolls, timesheets, cancelled checks, statements, and other documents (Electronic or Paper)
 - Including subsidiaries
 - Make copies or extracts

RUS Right to Inspect (continued)

- **Award Documents (Section 6.2 Rights of Inspection)**
 - The Awardee shall afford RUS, the Office of the Inspector General of USDA, and the Government Accountability Office, through their representatives, reasonable opportunity, at all times during business hours and upon prior notice, to have access to and right to inspect the Project, any other property encumbered by the Security Documents, and any and all books, records, accounts, including electronic books, records, accounts and electronic mail messages, regardless of the physical form or characteristics, invoices, contracts, leases, payroll records, canceled checks, statements, and other documents, and papers of every kind belonging to or in any way pertaining to its property or business, including its Subsidiaries, if any, and to make copies or extracts therefrom

Reporting Requirements



Reporting Requirements

FOA

- Annual comparable audited financial statements
 - Report on compliance and on internal control over financial reporting
 - Management letter (7 CFR 1773)
- Quarterly balance sheets, income statements, statements of cash flow, rate package summaries, number of customers taking broadband service (per community)
 - Due 30 days after calendar quarter
 - Using RUS' on-line reporting system
 - Loan amortization period or economic life of the facilities funded for 100% grant
- Annual service area maps through RUS mapping tool
- Final service area map showing all construction complete
 - May require portion of the award to be rescinded or paid back if not fully constructed
- Semi annual reports for 3 years after completion of project

Reporting Requirements

Award Documents (Sections 6.3 Annual Audit and 6.4 Reporting)

- Annual comparable audited financial statements (Due 120 days after fiscal year end)
 - Report on compliance and on internal control over financial reporting
 - Management letter (7 CFR 1773)
 - CPA must meet requirements of 7 CFR 1773.4
 - Non-Federal entities (expending \$750,000 or more in federal awards per fiscal year are subject to 2 CFR part 200 subpart F. (Due 9 months after fiscal year end)
- Quarterly balance sheets, income statements, statements of cash flow, rate package summaries, number of customers taking broadband service (per community) completion status of the build out. In addition, other reports as RUS may request
 - Due 30 days after calendar quarter
 - Using RUS' on-line reporting system

Reporting Requirements

Award Documents (Sections 6.3 Annual Audit and 6.4 Reporting)

- Annual service area maps through RUS mapping tool
 - Until entire funded service area can receive the broadband service
- Close out report
 - Due 90 days after the expiration or termination of the award or expenditure of all award funds
 - Includes reporting on various aspects of the project and also a final buildout map on the RUS mapping tool
 - May require portion of the award to be rescinded or paid back if not fully constructed
- Semi annual reports for 3 years after completion of project
 - Beginning the first January 31st after project completion
 - Using RUS' online reporting system

Accounting Requirements

FOA

- US GAAP, acceptable to RUS
- System of Accounting (RUS Bulletin 1770B-1)
- 2 CFR 200
 - “Grant recipient” = “loan recipient” and “loan/grant” recipient
- Must adopt a system of accounts acceptable to RUS (7 CFR 1770,B)

Award Documents (Sections 6.1 and Definitions in Article I)

- US GAAP, acceptable to RUS
- 2 CFR 200
- System of Accounting (RUS Bulletin 1770B-1)

Records Retention



Records Retention

FOA

- Retained and preserved in accordance with 7 CFR 1770 A
 - Construction – retained until audited and approved by RUS
 - Plant in service – retained until facilities are permanently removed from utility service
 - Life and mortality study data supporting depreciation – retained 25 years or for 10 years after plant is retired, which ever is longer

Award Documents (Section 6.1 Financial Records)

- The Awardee shall maintain, at its premises, such books, documents, papers, or other records and supporting documents, including, but not limited to, invoices, receipts, payroll records and bills of sale, adequate to identify the purposes for which, and the manner in which Loan, Grant, and other funds were expended on the Project. The Awardee shall at all times keep, and safely preserve, proper books, records and accounts in which full and true entries shall be made of all dealings, business, and affairs of the Awardee and its Subsidiaries, in accordance with its system of accounts
- The Awardee shall maintain copies of all documents submitted to RUS in connection with the Award until the longer of (i) the Loan being paid in full and all audits have been completed, (ii) the term of this Agreement or (iii) three years subsequent to close-out of the Award

Records Retention (continued)

ReConnect Construction Procedures

- Records supporting all assets financed by RUS shall be retained until audited and approved by RUS. Records must be sufficient to document the cost and location of all expenditures and to support advances and disbursement of award funds. The support records must include, but not limited to, contracts, third party invoices, timesheets, payroll records, material records, and overhead allocation records and summary schedules.
- Records related to plant-in-service must be retained until the facilities are permanently removed from utility service, all removal and restoration activities are completed, and all costs are retired from the accounting records unless accounting adjustments resulting from reclassification and original costs studies have been approved by RUS or other regulatory body having jurisdiction.

Disallowances



Disallowances

Award Documents (Section 8.3 Disallowed Expenditures)

- If RUS determines that the Awardee did not expend award funds on eligible purposes in accordance with approved line item budget and Form(s) 481 approved by RUS prior to the advance of funds, RUS may, in its sole discretion:
 - Disallow all or a part of the expenditures and disbursements
 - Require a deposit into the pledged deposit account to be used for other RUS approved purposes
 - Require reimbursement of the Government directly
 - Suspend future Advances
 - Take any other action RUS determines to be necessary

Disallowances

Award Documents (Section 5.3 Unused and Disallowed Advances)

- The Awardee shall reimburse RUS for any advanced funds whose original expenditure has been disallowed by and RUS loan and grant audit.
 - Satisfied as directed by RUS
 - Administrative offset against other approved purposes on Form(s) 481
 - Repaying the disallowed amount directly to the United States Treasury
 - Interest
 - Beginning on date RUS delivers a written demand for payment
 - Interest rate at the disallowed advance or US Treasury rate
 - Closeout of the Loan and/or grant will not affect the right of RUS to disallow expenditures and recover in full any amount based on a subsequent audit or other review

Conditions of Award Documents



Conditions of Award Documents

Section 4.1 Conditions Precedent to Closing

- Legal Matters
- Loan-Grant Agreement
- Filed and Recorded Security Documents, Articles of Incorporation, Charter Bylaws and Organizational Documents
- Authorizations
- Approvals
- Title Evidence
- Management, Service, and Operating Agreements
- Opinion of Counsel
- Additional Conditions

Conditions of Award Documents (continued)

Section 4.2 General Conditions Precedent to RUS' Obligations to Release Funds for Advance

- Service Rate Evidence
- Fidelity Bond or Theft Insurance Company
- Current Financial Information and Certificate of Authority
- Deposited Funds
- Additional Conditions

Conditions of Award Documents (continued)

Section 4.3 Conditions to Individual Advances

- Continuing Representations and Warranties
- Expenditure of Funds
- Material Adverse Affect
- Event of Default
- Requisitions and Supporting Documentation
- Flood Insurance
- Current Financial Information
- Compliance with Buildout Timeline and Reporting Requirements
- Compliance with Loan/Grant Agreement
- Permits, Licenses and Franchises
- Deposited Funds
- Additional Documents
- Additional Conditions

Affirmative Covenants of Award Documents



Affirmative Covenants of Award Documents

Section 5.5 Additional Project Funding

- Must have adequate funding in place to complete the project
- Must have prior written approval from RUS when obtaining additional indebtedness

Section 5.6 Miscellaneous Notices

- Notice of other Defaults
- Notice of Litigation
- Regulatory and Other Notices
- Material Adverse Effect
- Corporate Document Changes
- Other Information

Affirmative Covenants of Award Documents (continued)

Section 5.7 Rates and Financial Performance Criteria

- Must design, charge, and maintain rates to meet the following Financial Requirements:
- Section 5.8 Financial Requirements
 - At least two of the following:
 - Minimum TIER of 1.2
 - Minimum DSCR of 1.2
 - Minimum Current Ratio of 1.2
 - Positive cash flow from operations at the end of the fifth year of the award
 - Positive ending cash balance as reflected on the cash flow statement for each year of the forecast period
- Section 5.9 Corrective Action
 - Must submit corrective action plan to RUS if fail to meet requirements above
 - Within 30 days of sending the financial reports
 - Within 30 days of being notified by RUS
 - Which ever is earlier

Affirmative Covenants of Award Documents (continued)

Section 5.10 Service Obligation

- Must provide the level of broadband service described in approved application
 - From project completion to the longer of:
 - Composite Economic Life of the facilities financed (Specified on Schedule 1)
 - As long as the note is outstanding
- Grant portions
 - Failure to meet full service obligation
 - Government has claim to all or part of the federal grant
 - Proportionate to number of years grant assets were in service
 - As determined by RUS

Affirmative Covenants of Award Documents (continued)

Section 5.11 Obligations with Respect to the Construction, Operation and Maintenance of the Project

- Project Management and Operation
- Construction in accordance with Network Design and Buildout Timeline
- General Insurance Requirements
- Contracting
- Commencement and Completion of the Project
 - Begin within 180 days
 - Complete within 5 years of Release of Funds Date

Affirmative Covenants of Award Documents (continued)

- Section 5.12 Preservation of Existence and Rights
- Section 5.13 Compliance with Laws
- Section 5.14 Equal Opportunity Requirements
- Section 5.15 Purchases with Award Funds
 - Must be purchased outright. (No leasing)
- Section 5.16 Awardee to Defend Title and Remove Liens
- Section 5.17 Further Assurances
- Section 5.18 Buy American (7 CFR 1787)
- Section 5.19 Additional Affirmative Covenants (Schedule 1)

Negative Covenants of Award Documents



Negative Covenants of Award Documents

- Section 7.2 Merger, Consolidation, Transfer of Property, or Change in Control
- Section 7.3 Covenants for LLC's and Similar Awardees
 - No dissolutions
 - Supported by Organizational and cannot be amended without RUS written consent
 - No changes in membership affecting 49% or more without RUS written consent
- Section 7.4 Additional Indebtedness
 - No additional debt (Secured or Unsecured)
 - Exceptions (not to exceed 5% of consolidated total assets)
 - Purchase money security interests
 - Unsecured trade indebtedness
 - Other debt arising in ordinary course of business

Negative Covenants of Award Documents (continued)

- Section 7.5 Negative Pledge
 - No encumbrance on RUS' security interest in property
- Section 7.6 Contracts
 - Must have prior RUS written consent to enter into management and operational contracts
- Section 7.7 Salaries
 - Must be reasonable and conform to usual practice of similar entities
- Section 7.8 Extension of Credit
 - Cannot advance payments or make loans to related parties or affiliates

Negative Covenants of Award Documents (continued)

Section 7.9 Distributions or Withdrawals

- No distributions or withdrawals (dividends, stock, capital, profit allocations, membership, unit, other), except:
 - Annual distribution
 - Not to exceed 25% of prior year net income or margins, If after such, net worth is at least 1% of total assets
 - Not to exceed 50% of prior year net income or margins, if after such, net worth is at least 20% of total assets
 - Not to exceed 75% of prior year net income or margins, if after such, net worth is at least 30% of total assets
 - No limit if after such, net worth is at least 40% of total assets
- Subject to any additional restrictions on distributions and withdrawals included on Schedule 1

Negative Covenants of Award Documents (continued)

- Section 7.10 Changing Principal Place of Business, Place of Conducting Business, or Type of Organization
- Section 7.11 Changing name or Place of Incorporation or Organization
- Section 7.12 Historic Preservation
- Section 7.13 Affiliated Transactions (already discussed)
- Section 7.14 Preferred Stock
- Section 7.16 Restrictions on Changes to Line Item Budget
 - No changes are allowed without RUS prior written approval

Negative Covenants of Award Documents (continued)

Section 7.15 Restrictions on Transfers of Property

- No sales, leases, or transfers of Collateral
- If not in default on RUS award
 - May sell or dispose of property that is no longer necessary to, nor useful for, the operation of the Awardees business or if obsolete, worn out, damaged, or otherwise unsuitable for the purposes of the Awardee
 - Replace the same with other property of the same kind and nature, or substitute thereof
 - Apply proceeds if any to replacement thereof or prepayment of the indebtedness on the outstanding notes
 - Proceeds must immediately be used to prepay RUS debt or be deposited into the Pledged Deposit Account
 - Proceeds in Pledged Deposit Account can only be used as directed by RUS

RUS Rights



RUS Rights

- Section 8.1 Termination of Award Offer
- Section 8.2 Audits and Compliance Reviews
- Section 8.3 Disallowed Expenditures
- Section 8.4 Suspension of Advances
- Section 8.5 Payment Extensions
- Section 8.6 Right to Expend Money
- Section 8.7 Right to File Financing Statements





Rural Development