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Solicitation of articles: All AALA members are invited to submit articles to the Update. Please include copies of decisions and legislation with the article. To avoid duplication of effort, please notify the Editor of your proposed article.

IN FUTURE ISSUES

- USDA—Rural development

Milk marketing order system upheld

The Eighth Circuit has rejected a challenge by the Minnesota Milk Producers Association and others to the Secretary of Agriculture's pricing of "Class I" milk under the milk marketing order system authorized by the Agricultural Marketing Agreement Act of 1937, 7 U.S.C. §§ 601 et seq. *Minnesota Milk Producers Ass'n v. Glickman*, Nos. 97-4145MN, et al., 1998 WL 470361 (8th Cir. Aug. 13, 1998). The decision reversed a holding to the contrary by a federal district court in Minnesota. *Minnesota Milk Producers Ass'n v. Glickman*, 981 F. Supp. 1224 (D. Minn. 1997).

The milk marketing order system authorized by the Agricultural Marketing Agreement Act of 1937 (AMAA) was a response to unstable marketing conditions and low milk prices during the Great Depression.

Although the price support program and milk marketing orders are authorized by separate statutes, the price support program is relevant to the milk marketing order system. Milk marketing orders establish the minimum price that handlers must pay for Class I milk; that is, Grade A milk used for fluid consumption. The determination of the Class I price under milk marketing orders, however, is partially based on the Class III price (the "M-W" price). The Class III price represents the price of hard products, such as cheese and butter. A class known as Class IIIA is the price for nonfat dry milk. Because the price support program supports the price of hard products, it has a tendency to influence Class III prices.

Under the price support program, the federal government will buy, at designated prices, bulk cheese, butter, and nonfat dry milk. As with other price support programs high price supports encourage production. When surpluses result, federal expenditures increase. Under the 1996 farm bill, the price support rate will decline over the period from 1996 through 1999 at the rate of 15 cents per hundredweight per year from $10.35 in 1996 to $9.90 in 1999. Also, the program will terminate at the end of 1999 *See* 7 U.S.C. § 7251. Thus, until the year 2000, milk producers have two markets—the commercial market and the federal government acting through the Commodity Credit Corporation. In recent years, federal purchases have been about 5% of all sales.

Milk marketing orders are voluntary; two-thirds of the producers in a specific region must vote to have a marketing order apply. Currently, thirty-eight marketing orders in various geographical regions cover eighty percent of the nation's fluid milk production; the remainder is subject to state marketing orders (California, for example) or is unregulated. The 1996 farm bill directs the Secretary to reduce the number of marketing orders to not less than ten and not more than fourteen orders

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Commission rates key to successful FLC

In the San Joaquin Valley, the predominant method used by farm labor contractors to charge grower customers is to charge for total wages plus a commission based on a percentage rate applied to that amount. A study by the University of California Agricultural Personnel Management Program in 1992 showed that commission rates in table and raisin grapes for 26 FLCs in the Valley averaged 33%; the minimum reported was 30%, the maximum was 37%.

A Fresno-based farm labor contractor recently met with local representatives to express his concern that he returns to an FLC at a 30% commission rate in the grape industry are very low, or negative, using his own costs as an illustration.

The veteran 20-year FLC says many contractors, particularly new ones do not know their full costs of operation. "Overall, there's a definite need for business management education in the FLC industry. As it is now, many, after only a few years, go out of business, unable to pay the social security and unemployment taxes that are due."

In fact, the Internal Revenue Service, in 1994, formed a Fresno-based "Ag Design Team" of officers that is still working "to address the San Joaquin Valley's biggest compliance problem—an estimated $200 million in unpaid employment taxes from agricultural tax form 943."

And turnover in farm labor contracting is indeed high. About 5 to 6 thousand federal

Continued on page 2

FLC registrations are issued each year by the U.S. Department of Labor in California, Arizona, Oregon, Washington, and Hawaii. About 1,500—25 to 30 percent—are "initial" or new registrations, according to DOL officer Noemi Lucha in San Francisco.

Let's return to this FLC's costs and returns for a one-week period. A crew of 25 men work 8 hours a day for 6 days for $5.75 per hour. A crew boss is paid $70 a day. That's a week's payroll of $7,320. If he accepts a commission rate of 30%, he would have an "inclusive" commission of $2,196 to pay business costs over and above the wages due the workers.

Now the expenses as a percent of payroll. The social security tax (employer share) is 7.65%. His combined federal and state unemployment tax rate is the maximum (and common) 6.2%. Workers' compensation (for grapes) costs him 4.98%, liability insurance is 1%, and his payroll service costs 2% of payroll. Field sanitation (portable toilets and handwashing facilities) is 1.02%, paper cups and ice [illegible], cell phone/pager .68%, and pickup expense (at 33 cents/mile) is 2.22% of payroll.

Not included in his costs are office rent, advertising, business dues, tools, safety program, and the "overlooked" costs of holding the California FLC license ($350 per year) and surety bonding requirement. Also, he himself noted, the "transactional" costs involving in moving from one grower customer to another are ignored in his illustration.

In any event, the costs, in his case, tota 26.41%, leaving $262.79 profit for the week The self-employment tax (15.3% of r income) reduces effective income $222.58. Based on a 48-hour week, h would make $4.64 per hour—less than th workers—and would, in this writer's opir ion, sooner or later by out of business.

—*Steve Sutter, UC Area Farr Advisor, Berkeley, C*

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AALA Editor ....Linda Grim McCormick
Rt. 2, Box 292A, 2816 C.R. 163
Alvin, TX 77511
Phone (281) 388-0155
FAX (281) 388-1291
E-mail [illegible]@flash net

[illegible] Susan Schneider, University of [illegible] AR; Stephen Carpenter, FLAG, [illegible] MN; Steve Sutter, Berkeley, CA; Christopher [illegible] University of Arkansas, Fayetteville, AR; [illegible] McCormick, Alvin, TX

[illegible] AALA membership information, contact [illegible] Office of the Executive Director, [illegible] Law Center, University of Arkansas, [illegible] AR 72701

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Proposal regarding a name change

During the past few years, the AALA has experienced lower membership. Given this situation, a proposal has come forward to attempt to provide renewed vigor for our Association through reaching out and touching a broader audience. The proposal is for a name change. An Ad Hoc Name Change Committee has been appointed to look into the possibility of changing the name of the AALA to something that (1) would more accurately describe our membership; (2) would more accurately delineate the activities of members; or (3) would enable the AALA to expand our pool of potential members. The Committee consists of Terence J. Centner (Chair), Eldon McAfee, Pat Conover, Leon Geyer, Dona Merg, and Rich Ricketts.

Preliminary thoughts identified two alternative names for our Association: the "Agribusiness and Environmental Law Association" or the "Agricultural and Environmental Law Association." Either would have the acronym "AELA." The proposed names omit the word "American" because "AELA" seems to be a more manageable acronym than "AAELA." Moreover, with an address in the United States, the word "American" is not needed.

Such a fundamental change will not be made without full consideration by the membership. To assist members in considering the proposal, we would like to discuss some advantages and disadvantages of a name change. [illegible] feel free to convey your thoughts and concerns of this proposal to members of the Ad Hoc Committee or to members of the Board of Directors.

Agribusiness

The term "agribusiness" includes agriculture and other activities associated with the agricultural industry. Given that mar agricultural lawyers provide counsel to agribusiness and/or other issues that are not strictly production agriculture, the term agribusiness may be more accurate to describe our Association. The term also could help draw more agribusiness participation.

Conversely, many members see "agricultural" as covering their activities more accurately than "agribusiness." Moreover, the term agribusiness suggests that the Association may be concerned with business at the expense of farmers. Many members of the AALA are small-tow practitioners serving individual farme and others. We do not want to lose you members.

The issue has also been advanced th "agribusiness" and "environmental" a incompatible.

Environmental

The term "environmental" would rec nize what has already occurred at con ence programs, cited literature, and u versity teaching activities. Environm tal issues have been a major part of rec conference programs. Environmental sues are part of the agricultural law b ography of the *Agricultural Law Upd* Analyzing the past four bibliograph listings, over one-half of the titles h involved environmental issues. Fin the teaching activities reported at the AALA conference in Minneapolis by m of our academic members suggest they teaching both environmental and agr tural law.

Production agriculture is going t involved in environmental issues for foreseeable future. We might use this ation to our advantage. Some college agriculture have decided that agricul can best help itself by expanding t base and taking the lead in environme matters. These colleges have taken environmental programs while cont ing to service agricultural needs, argu without detracting from traditional a cultural support. The addition of "e mental" could attract additional mem who have an environmental inetere

Adding the term "environmental" t name comes with a cost. It will be see some as diluting our agricultural intended to focus on agricultural is not environmental. The addition of term may cause our Association to f its most important mission.

The Ad Hoc Name Change Comm would welcome your ideas on this posal. Letters may be sent to the Com tee Chair by e-mail tcentner@agecon.uga.edu or to the fol ing address: Terence J. Centner. Conner Hall, The University of Geor Athens, GA 30602.

Milk Marketing Orders/*Cont. from page 1*
within three years. *Id.* § 7253(a)(1).

Milk marketing orders are binding on the parties to whom they are directed; that is, handlers and processor of milk. They are issued as regulations.

Milk marketing orders set the minimum prices for raw fluid grade milk (Grade A, Class I milk) that processors must pay to producers. They also specify how the returns from milk sales are to be distributed among producers.

Only fluid grade milk is regulated. Ninety percent of all milk produced in the United States is fluid grade, that is, Grade A. About forty-two percent of that milk is used for fluid consumption, the remainder is used for hard and soft products. Grade B milk, produced under lower standards than Grade A milk, can only be used for hard dairy products.

The minimum prices for Grade A milk are established based on how the milk is used in end products. In that regard, there are three basic classes of milk:

Class I (fluid consumption)

Class II (soft products)

Class III (hard products)(Class IIIA covers nonfat dry milk)

Class I and II prices are based on the Class III price. The Class III price is the market price for Grade B milk purchased by processors in Minnesota and Wisconsin (the "M-W" price), as determined by monthly surveys. Because Class III milk is not regulated by marketing orders (only Class I milk is subject to marketing orders), its price is determined by the market, which may be influenced by the price support program price. Because the demand for manufactured dairy products is national, the M-W price generally represents the national market price.

The Class II price is determined by adding, on average, 15 cents to the Class III price.The Class I price (except in some western states) is based on the following:

a. The Class III price;

b. + $1.04 (the Grade A differential); and

c. + about 15 cents for every 100 miles from Eau Claire, Wis. (the distance differential).

Why the Grade A differential? The Grade A differential was established in the 1960s to encourage "deficit" regions (e.g., the Southeast and Southwest) to develop their own dairy industry. At one time, the differential equaled the additional cost of producing Grade A instead of Grade B milk. Not surprisingly, it no longer does; Grade A milk can be produced at less cost than the differential. A 1986 study found that the additional cost is now about 15 cents; but the differential remains at $1.04.

Why the distance differential? The distance differential was established to encourage "surplus" regions (i.e., the upper Midwest) to ship milk to "deficit" regions to avert shortages that might develop. The distance differential was intended to represent the cost of transporting "surplus" milk to these "deficit" regions. Thus, the Class I price generally increases in relation to the distance from Eau Claire, Wisconsin, and the distance differential is what really bothers Upper Midwest producers.

The Class I price is not the price the producer receives. Determining the prices for each of the three classes of milk is only a preliminary step in determining the price the producer receives. The next steps are determining the following:

a. The usage of milk, by class, in each marketing order region; and

b. The monthly average or "blend" price on the basis of usage under each marketing order.

Here is how this works: The "blend" price is equal to the percentage utilization for each class times the respective class price. The total of the three classes becomes the overall "blend" price. That overall "blend" price is the price the producer receives.

"Blend" prices vary according to usage. Marketing order regions having high usages of Class I milk have higher blend prices than regions where Class II and III usage predominates. Since Class I prices partially depend on distance from Eau Claire, the real "winners" are regions, such as Florida, that are a great distance from Eau Claire *and* that have high Class I milk usage. In 1995, for example, the blend price in Florida was $16.07/cwt, while the blend price in Eau Claire was $12.32/cwt.

As one might guess, producer enthusiasm for the current system varies by region. Some Upper Midwest producers want to scrap marketing orders in favor of a free market. Wisconsin, for example, is mostly a manufacturing state. In other words its usage is mostly Class II and III. To the extent that marketing orders stimulate production in other regions, the excess production usually ends up in Class II and III products, thus driving down the M-W price. Also, Wisconsin obviously does not benefit from the distance differential. Among the producers who have benefited the most are those in the Southwest, where costs of production are relatively low. Once a deficit region, the Southwest now ships milk to the Upper Midwest because it lacks the manufacturing capacity for Class II and III products. By "dumping" its surplus milk in the Upper Midwest, the Southwest depresses Upper Midwest prices.

In light of this background, the residence of the plaintiffs in the *Minnesota Milk Producers* litigation should come as no surprise. In their 1990 complaint to the district court, the plaintiffs challenged the distance differential as violative of AMAA section 608c(18). That section, in essence, requires the differentials to reflect economic conditions in each order region.

During the protracted course of the litigation, which included an intermediate appeal to the Eighth Circuit, the Secretary held a series of hearings on the pricing structure. For his part, the Secretary concluded that the pricing structure satisfied the AMAA. For its part, the district court concluded that the Secretary had failed to support his conclusions with substantial evidence. Exasperated with the Secretary's apparent unwillingness or inability to explain his decision, the district court invalidated the Class I pricing structure, but upheld the M-W component of that price. Both sides appealed to the Eighth Circuit.

The district court's decision caused considerable apprehension in the dairy industry. That decision, however, was stayed pending the outcome of the cross-appeals. The stage was nonetheless set for a showdown over Class I pricing.

For anyone expecting pyrotechnics from the Eighth Circuit, the court's decision is a disappointment. In the end, the case turned on the application of the "*Chevron* deference doctrine" announced in *Chevron v. Natural Resources Council, Inc.*, 467 U.S. 837 (1984). Under that doctrine, a court must defer to an agency's permissible interpretation of a statute if the statute fails to speak directly to the precise question at issue. Though the district court had concluded that the AMAA spoke precisely to the question at issue by imposing a duty on the Secretary to monitor pricing in compliance with section 608c(18), the Eighth Circuit disagreed. Based on its own construction of the statute, the Eighth Circuit concluded that the Secretary had to comply with section 608c(18) only when he decided to change a marketing order, something he had not done here. In other words, the Secretary was not constrained by that section in maintaining the status quo.

Having concluded that the text of the AMAA did not support the plaintiffs' position, the Eighth Circuit justified its deference to the Secretary's position on several grounds, including the fact that Congress had codified the then-existing differentials in 1985. *See* 7 U.S.C. § 7253. The Eighth Circuit also upheld the Secretary's determination as to the validity of the M-W price under the AMAA. As a result, the debate over marketing orders has, for the time being, has left the courts and returned to the Secretary who is currently considering proposals for the consolidation of marketing orders as required by the 1996 farm bill.

—Christopher R. Kelley, Assistant Professor of Law, University of Arkansas, Of Counsel, Vann Law Firm, Camilla, GA

Farm Service Agency Guaranteed Loan servicing

By Susan A. Schneider and Stephen Carpenter

Farmers' Legal Action Group, Inc. (FLAG), recently published two books authored by FLAG staff attorney Stephen Carpenter explaining the Farm Service Agency (FSA) guaranteed loan programs. The first is the *Farmers' Guide to Getting a Guaranteed Loan*, which as the title indicates, analyzes the process of applying for and obtaining a guaranteed loan. The second book, entitled the *Farmers' Guide to Guaranteed Loan Servicing* addresses the often misunderstood process of servicing a guaranteed loan when the borrower experiences financial distress. This article reviews the *Guide to Guaranteed Loan Servicing* and then provides an excerpt from it.

For a number of years, the focus of the FSA farm loan program has shifted from direct lending to providing guaranteed loans. Congress reaffirmed its commitment to this shift in the 1996 farm bill, and the move from direct to guaranteed loans has continued to be reflected in USDA loan appropriations. Under the FSA guaranteed loan program, the farmer-borrower does not obtain the loan from the FSA. Rather, the loan is from another lender, usually a commercial bank or a Farm Credit System lender. As an inducement to the lender, FSA provides a guarantee of up to 95% of the amount of the loan.

This rather unusual three way arrangement between the farmer, the lender, and the FSA has frequently given rise to misconceptions about the relationships between the parties. For example, many borrowers as well as many lenders have erroneously believed that traditional loan servicing tools were unavailable in resolving a distressed loan. Lenders may have feared that providing this type of assistance to a borrower would jeopardize their loan guarantee. The *Farmers' Guide to Loan Servicing* addresses this misconception head on by presenting a complete analysis of each loan servicing tool available. The book specifically discusses seven major categories of loan servicing tools: debt consolidation, loan restructuring, reamortization, deferrals, debt write down, interest rate assistance, and the transfer and assumption of debt. It also addresses the difficult issue of a guaranteed borrower's rights and the administrative appeal process. The book is written in an easy to read style that will be appealing to non-lawyers, yet it is footnoted to provide complete citations to the relevant statutes and regulations. It is well organized and thorough, and it should be invaluable to attorneys who work with farm borrowers or lenders involved in the guaranteed loan program.

The following excerpt from The Farmers Guide to Guaranteed Loans discusses the loan servicing options of debt consolidation and loan rescheduling.

Review by Susan A. Schneider, Assistant Professor of Law, University of Arkansas School of Law, Fayetteville, AR; Excerpt by Stephen Carpenter, Staff Attorney, Farmers Legal Action Group, Inc., St. Paul, MN.

Consolidation of Guaranteed Loans

Consolidation is the simplest and most manageable loan servicing option for guaranteed loans. Consolidation takes two or more loans from a lender and combines the outstanding principal and interest into a single loan.

Guaranteed Loans made for operating purposes may be consolidated

The following types of FSA guaranteed operating loans may be consolidated.

Operating (OL) Loans

In general, two or more guaranteed operating loans may be consolidated.[1] Guaranteed OL loans may only be consolidated with other guaranteed OL loans.[2]

Operating (OL) lines of credit

An existing guaranteed operating (OL) line of credit may be consolidated with a new guaranteed OL line of credit. The terms of the line of credit must be consistent with the terms of the original line of credit agreement between the farmer and the lender.[3] For this purpose, the terms of the line of credit cover both the time limits for making advances and the final maturity date of the line of credit.

Emergency (EM) Loans made for operating purposes

Guaranteed Emergency (EM) loans made for operating purposes may also be consolidated.[4] These loans may only be consolidated with other guaranteed EM loans made for operating purposes.[5]

Limitations on consolidation of Guaranteed Loans

Several requirements limit the availability of guaranteed loan consolidation.

No consolidation of loans secured by real estate

Guaranteed OL loans may not be consolidated if they are secured by real estate.[6]

No consolidation for Interest Assistance Loans

Guaranteed operating loans and lines of credit with outstanding Interest Assistance Agreements or Interest Rate Buydown Agreements may not be consolidated.[7] Interest assistance is discussed in detail below.

No consolidation for loans subject to Shared Appreciation Agreements

Guaranteed OL loans and lines of credit may not be consolidated if they are subject to an outstanding Shared Appreciation Agreement.[8] Shared Appreciation Agreements are discussed in the Write-down section below.

Multiple consolidations possible

There is no limit on the number of times a farmer may consolidate guaranteed loans.[9]

Repayment periods for Consolidated Loans

A consolidated note or line of credit will have a limited repayment period.

Consolidated OL Loans—usually 15 Years

In general, a consolidated operating loan note must be repaid within 15 years from the date of the consolidation.[10] If the note was made solely for recreation or nonfarm enterprise purposes, it will have a maximum repayment period of seven years from the consolidation.[11]

Consolidated OL line of credit—no longer than original line of credit

The repayment period for a new OL line of credit agreement that was created after consolidating an existing line of credit cannot exceed the terms of the existing line of credit.[12]

Combining consolidation with loan rescheduling

Consolidation, used by itself, does not reduce the principal or interest on a guaranteed loan. Consolidation can, however, be used in combination with another loan servicing option—rescheduling. If a consolidated loan is also rescheduled, the requirements for rescheduling discussed in the next section of this book must be met.[13]

Time limits for repayment may be extended

·· a consolidated loan is also resched- :. the time allowed for repayment . be extended for a certain period.[14]

Interest rates may be changed

›nsolidation, by itself, does not change borrower's interest rate. If a consoli- ·.›n is combined with a rescheduling, ·.ever, the interest rate may some- ·.s be changed.[15] Generally, the inter- · rate for a consolidated OL loan or line ·edit is negotiated by the farmer and .ender. FSA sets some limits on inter- · rates that may be charged.[16]

Rescheduling of Guaranteed Loans

.Vhen a guaranteed loan is resched- .i its terms are rewritten.[17] For ex- ple, a rescheduled loan may have the · .th of the repayment period extended, · :ch can lower monthly payments, and .y have the interest rate changed.

:ranteed Loans made for operating ·poses may be rescheduled

In general, guaranteed FSA loans and ·.s of credit made for operating pur- ·es may be rescheduled.[18] These in- .de: (1) guaranteed OL loans; (2) guar- :eed OL lines of credit; and (3) guaran- ·d EM loans made for operating pur- ·es.

Rescheduling is similar to re-amorti- :ıon, which is discussed in the next tıon of this book. The main difference ·ween the two is that rescheduling is · loans that are made for operating .rposes and reamortization is for loans .at are made for real estate purposes.

:ow rescheduling works

Rescheduling can lower guaranteed .an payments by changing the repay- ent terms. This section gives a general :escription of how the loan terms may be nanged.

Interest rates for rescheduled loans

FSA regulations may have some effect ›n the interest rates that are charged on ·escheduled guaranteed loans.

Interest rates generally

Generally, the interest rate on a guar- anteed OL loan is negotiated between the lender and the borrower. The same is usually true for guaranteed loans that are being rescheduled.[19] FSA does set some limits on the interest rate that can be charged on a guaranteed loan.[20]

If Interest Assistance Agreement is in effect

If the rescheduled OL loan or line of credit has an outstanding Interest Assistant Agreement, the interest rate after rescheduling may not be more than the rate under the original Interest Assistance Agreement.[21] Interest assistance is discussed in detail in a later section of this book.

Repayment periods for rescheduled loans

FSA regulations set limits on the allowable repayment period for a rescheduled guaranteed loan or line of credit.

Rescheduled OL Loans—usually 15 years

In general, a rescheduled note must have a repayment period of not more than 15 years from the date of the rescheduling, unless the loan is for recreational and/or nonfarm enterprise purposes, in which case the maximum repayment period is seven years.[22]

Rescheduled OL Line of Credit—usually seven years

A rescheduled OL line of credit must have a repayment period of not more than seven years from the date of the rescheduling.[23]

Uneven payments for rescheduled loans possible

According to FSA regulations, a rescheduled guaranteed loan may, in some cases, have unequal payments.

Unequal installments possible

In some cases, a guaranteed loan can be rescheduled into unequal amortized installments.[24] Uneven payments can only be used if one of the three following conditions is true.

(1) New enterprise

An uneven payment schedule is possible if the farmer is establishing a new enterprise.[25] A new enterprise, for this purpose, is not defined by FSA regulations. If the farmer is moving into a new type of production, such as adding a cow-calf operation to the farm, this likely counts as establishing a new enterprise.

(2) Farm is being developed

An uneven repayment schedule is permitted if the farm is being developed.[26] FSA regulations do not define development.

(3) Recovering from economic reverses

An uneven repayment schedule is permitted if the farmer is recovering from economic reverses.[27] FSA regulations do not define economic reverses. For this particular aspect of the regulations, the cause of the economic reverse should not affect FSA's decision to allow uneven payments.

Balloon payments not allowed

Although unequal installments may be possible, balloon payments are not allowed for rescheduled guaranteed loans.[28]

Capitalizing interest on rescheduled Guaranteed Loans

As a result of a 1995 change in FSA regulations, interest on a rescheduled guaranteed note may be capitalized.[29] Capitalization of interest means that the interest which has accumulated on the debt is turned into principal. Rescheduling a note or line of credit agreement can, therefore, increase the total amount of principal owed by the borrower.[30]

Not all interest can be capitalized

Not all interest on a rescheduled loan can be capitalized. FSA regulations create the following restrictions.

(1) Interest must have accrued at original rate on note

Only interest that has accrued at the interest rate shown on the farmer's original promissory note may be capitalized.[31]

(2) No late fees or default penalties

Many lenders charge late payment fees or default interest penalties if the borrower does not make payments on time. FSA regulations do not permit this form of interest to be capitalized.[32]

Maximum principal limits apply

FSA regulations set a maximum dollar amount of principal that can be owed at one time by a farmer. Usually, this limit affects only the amount of money that the farmer seeks to borrow. In addition, however, borrowers will not be allowed to capitalize interest to the point that total principal including capitalized interest is greater than this maximum amount.[33] Maximum amounts of principal that may be owed are as follows.

(1) OL Loans—up to $400,000

The total outstanding principal on FSA guaranteed and direct operating loans and lines of credit can be no more than $400,000.[34]

(2) OL lines of credit—ceiling in Contract of Guarantee

The total amount of principal outstanding at any time on a guaranteed line of credit can never be more than the ceiling set out in the FSA Contract of Guarantee.[35]

Capitalization of interest on Interest Assistance Loans

If the borrower is rescheduling a guaranteed loan with an outstanding Interest Assistance Agreement, additional restrictions apply to the capitalization of inter-

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GUARANTEED LOANS/*Cont. from page 5*

est.[36] Changes in loan terms, aside from the interest rate, can take place as a part of the rescheduling and are not affected by interest assistance. Interest assistance is discussed in detail in a later section of this book.

(1) Capitalize at farmer's effective rate of interest

As noted above, only interest accrued at the rate indicated on the original loan note may be capitalized. If the farmer is receiving interest assistance, however, only the interest accrued at what FSA calls the borrower's "effective" rate of interest may be capitalized.[37] The farmer's effective rate of interest is the rate on the note minus any interest assistance.[38]

(2) Changing interest rates

As noted above, a rescheduling may change the rate of interest charged the borrower. If, however, the farmer is receiving interest assistance—that is, if an Interest Assistance Agreement is in effect—interest rate changes may only take place at certain times.[39] Specifically, if the farmer is receiving interest assistance, interest rate changes may only be made on either the annual [illegible] date or the annual review date. If the lender is rescheduling the loan at some other time, the interest rate cannot be changed.

Repeated rescheduling

There is no limit on the number of times a borrower may reschedule a guaranteed loan.[40]

Combining rescheduling with consolidation

Borrowers can reschedule and consolidate guaranteed loans at the same time.[41]

Borrower eligibility for Guaranteed Loan rescheduling

FSA regulations establish the following eligibility requirements for guaranteed loan rescheduling.

Meet eligibility requirements for original loan

Farmers must continue to meet the eligibility requirements for the type of loan to be serviced. For example, if a guaranteed OL loan is to be rescheduled, the borrower must meet the original eligibility requirements for getting a guaranteed OL loan.[42]

Any delinquency due to circumstances beyond borrower's control

Farmers are eligible for rescheduling whether or not their loans are delinquent. If there is a delinquency, however, it must be due to circumstances beyond the control of the borrower. For this particular purpose, such circumstances are limited by FSA regulations to include only certain reductions in income and certain increases in expenses.[43]

Reduction in farm income

The delinquency may be due to a decline in farm income. Some such declines will be considered to be beyond the control of the farmer—but not all. In deciding whether a decline in farm income is due to circumstances beyond the control of the farmer, FSA focuses on the farmer's financial management decisions.

(1) Inadequate or poor financial management

In order to be eligible for rescheduling, the decline in farm income must not have been due to "inadequate or poor financial management decisions" by the farmer.[44] FSA regulations do not explain what is meant by inadequate or poor financial management decisions. The regulations do state that if the decline in farm income is due to "untimely marketing practices," such as when a farmer forward contracts and the crop price continues to rise, any resulting decline in income is considered to be within the farmer's control. As a [illegible] cause a decline in farm income and this decline in farm income causes a delinquency, the farmer will be ineligible for guaranteed loan reamortization.[45]

(2) Other causes of a decline in farm income

If the reduction in farm income that led to a delinquency is due to any cause other than inadequate or poor financial management decisions by the farmer, the reduction of income should be considered by FSA to be beyond the control of the borrower.[46]

Unforeseen essential farm expenses

If the delinquency is due to unforeseen but essential farm expenses, the delinquency is considered by FSA to be due to circumstances beyond the control of the farmer.[47] For this purpose, FSA regulations do not define an essential farm expense.[48]

Unforeseen essential family living expenses

If the delinquency is due to unforeseen but essential family living expenses, the delinquency is considered by FSA to be beyond the control of the borrower.[49] For this purpose, FSA regulations do not define *unforeseen* essential family living expenses.[50]

Natural disaster

If the delinquency is due to a natural disaster, such as a drought or flood, FSA considers the delinquency to be beyond the borrower's control. An official disaster declaration or designation in the farm's area is not needed for the disaster to qualify as beyond the control of the borrower.[51]

Borrower acted in good faith

In order to be eligible for rescheduling, the farmer must have acted in good faith, demonstrating sincerity and honesty in meeting agreements with and promises made to the lender and FSA.[52]

Although this requirement sounds vague and open to interpretation, FSA regulations suggest that it should only be used to deny loan servicing in very narrow circumstances.[53] For the purpose of this requirement, acting in good faith means two things. Nothing in the FSA regulations suggests that the FSA may use any other factors when determining whether a borrower has acted in good faith.

Cooperate in servicing and maintaining security

The farmer must have cooperated in servicing the account and maintaining the security.[54]

The farmer must have sat[illegible] completed borrower training if it was required.[55] Borrower training is required for most guaranteed loan borrowers.[56]

Positive cash flow requirements

FSA regulations include detailed cash flow requirements for rescheduling and other guaranteed loan servicing options.

Need rescheduling to cash flow

To be eligible for rescheduling, the farmer must need the loan servicing to develop a positive cash flow. This requirement has two parts.

(1) Cannot cash flow without rescheduling

The farmer must not be able to develop a positive [illegible] the pr[illegible] repayment schedule.[58]

(2) Can cash flow with rescheduling

The farmer must be able to develop a positive cash flow with changes in the repayment schedule.[59]

Defining and calculating positive cash flow

For the purposes of a guaranteed loan FSA regulations require that a positive cash flow include a ten percent surplus. Two specific calculations are required by FSA to calculate a positive cash flow. FSA calls these formulas the Term Debt and Capital Lease Coverage Ratio and the Capital Replacement and Term Debt Repayment Margin.[61]

Lender determines cash flows

The regulations say that the lender makes these cash flow calculations.[62]

Farmer will be able to continue the operation

FSA has a general requirement that rescheduling must insure that the farmer will be able to continue the operation.[63] In theory, this requirement is separate from and in addition to the cash flow requirement.

Other requirements for rescheduling of Guaranteed Loans

FSA regulations set several other requirements for rescheduling a guaranteed loan. First, the security position of the lender may not be hurt by rescheduling.[64] Second, the rescheduling must assist in the orderly collection of the loan.[65] Third, in general, the rescheduling must be in the best interests of the borrower and the lender.[66] Fourth, rescheduling requires prior approval from FSA.[67] Fifth, in some cases, the lender will have assigned part of the borrower's loan to what is known as a holder—usually a bank.[68] Any holder must agree in writing to the rescheduling.[69]

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[1] 7 C.F.R. § 1980.124(b)(1) (1997).

[2] 7 C.F.R. § 1980.124(b)(3) (1997).

[3] 7 C.F.R. § 1980.124(b)(1) (1997).

[4] 7 C.F.R. § 1980.124(b)(1) (1997).

[5] 7 C.F.R. § 1980.124(b)(3) (1997). This includes guaranteed EM loans for annual operating purposes and guaranteed EM major adjustment loans for operating purposes. Guaranteed EM loans for actual losses and EM major adjustment loans for real estate purposes may not be consolidated.

[6] 7 C.F.R. § 1980.124(b)(5) (1997).

[7] 7 C.F.R. § 1980.124(b)(5) (1997).

[8] 7 C.F.R. § 1980.124(b)(5) (1997).

[9] 7 C.F.R. § 1980.124(b)(6) (1997).

[10] 7 C.F.R. § 1980.124(b)(10) (1997).

[11] 7 C.F.R. § 1980.124(b)(10) (1997).

[12] 7 C.F.R. § 1980.124(b)(10) (1997). Terms, for this purpose, includes both the making of advances as well as the final maturity date.

[13] For example, limitations on balloon payments for rescheduling apply when a loan is both consolidated and rescheduled.

[14] 7 C.F.R. § 1980.124(b)(10) (1997).

[15] 7 C.F.R. § 1980.124(b)(9) (1997). For the rules regarding guaranteed EM loans, see 7 C.F.R. § 1980.124(b)(8) (1997).

[16] These limits can be found in 7 C.F.R. § 1980.175(e) (1997). 7 C.F.R. § 1980.124(b)(9). These limits are also discussed in FLAG's *Farmers' Guide to Getting a Guaranteed Loan.* See the FLAG order form at the end of this book.

[17] 7 C.F.R. § 1980.124(b)(2) (1997).

[18] 7 C.F.R. § 1980.124(b)(2) (1997).

[19] 7 C.F.R. § 1980.124(b)(9) (1997). For the rules regarding guaranteed EM loans, see 7 C.F.R. § 1980.124(b)(8) (1997).

[20] 7 C.F.R. § 1980.124(b)(9) (1997). The limits are found in 7 C.F.R. § 1980.175(e) (1997). They are discussed in detail in FLAG's *Farmer's Guide to Getting a Guaranteed Loan.* See the FLAG order form at the end of this book.

[21] 7 C.F.R. § 1980.124(b)(9) (1997). The same requirement applies for Interest Rate Buy-down Agreements.

[22] 7 C.F.R. § 1980.124(b)(10) (1997).

[23] 7 C.F.R. § 1980.124(b)(10) (1997).

[24] 7 C.F.R. § 1980.124(b)(10) (1997).

[25] 7 C.F.R. § 1980.124(b)(10) (1997).

[26] 7 C.F.R. § 1980.124(b)(10) (1997).

[27] 7 C.F.R. § 1980.124(b)(10) (1997).

[28] 7 C.F.R. § 1980.124(b)(10) (1997).

[29] 7 C.F.R. § 1980.124(a)(7) (1997). See also 7 C.F.R. pt. 1980, subpt. A, app. A, Loan Note Guarantee, par. 15 (1997).

[30] 7 C.F.R. § 1980.124(a)(7), (e) (1997).

[31] 7 C.F.R. § 1980.124(a)(8) (1997).

[32] 7 C.F.R. § 1980.124(a)(8) (1997).

[33] 7 C.F.R. § 1980.124(e) (1997).

[34] 7 C.F.R. § 1980.175(d)(2) (1997) (redesignated as 7 C.F.R. § 1980.175(d)(3) by 62 Fed. Reg. 9351, 9358 (1997)).

[35] 7 C.F.R. § 1980.175(d)(2) (1997) (redesignated as 7 C.F.R. § 1980.175(d)(3) by 62 Fed. Reg. 9351, 9358 (1997)).

[36] This circumstance is not discussed in FSA regulations. An FSA Notice, however, permits the capitalization of interest on interest assistance loans. FSA Notice FC-185, Capitalizing Interest and Interest Assistance for Guarantee Loans (Apr. 28, 1998) (set to expire on Apr. 1, 1999).

[37] FSA Notice FC-185, Capitalizing Interest and Interest Assistance for Guaranteed Loans, at 2 (Apr. 28, 1998) (set to expire on Apr. 1, 1999).

[38] FSA Notice FC-185, Capitalizing Interest and Interest Assistance for Guaranteed Loans, at 2 (Apr. 28, 1998) (set to expire on Apr. 1, 1999).

[39] FSA Notice FC-185, Capitalizing Interest and Interest Assistance for Guaranteed Loans, at 2 (Apr. 28, 1998) (set to expire on Apr. 1, 1999).

[40] 7 C.F.R. § 1980.124(b)(6) (1997).

[41] 7 C.F.R. § 1980.124(b)(7) (1997).

[42] 7 C.F.R. § 1980.124(a)(1) (1997). For eligibility requirements see 7 C.F.R. §§ 1980.175(b), 1980.176 (1997). These requirements are also discussed in FLAG's *Farmers' Guide to Getting a Guaranteed Loan.* See the FLAG order form at the end of this book.

[43] 7 C.F.R. § 1980.124(a)(3) (1997).

[44] 7 C.F.R. § 1980.124(a)(3)(i) (1997).

[45] 7 C.F.R. § 1980.124(a)(3)(i) (1997).

[46] 7 C.F.R. § 1980.124(a)(3)(i) (1997).

[47] 7 C.F.R. § 1980.124(a)(3)(ii) (1997).

[48] FSA regulations for direct loans do provide a definition for essential expenses. According to these regulations essential expenses are those which are "basic, crucial or indispensable." 7 C.F.R. § 1962.17(b)(2)(ii) (1997). In addition, the regulations provides a list of items that are to serve as a guideline to what "normally may be considered essential family living and operating expenses." These expenses include: household operating, food, clothing and personal care; health and medical expenses; house repair and sanitation; school and church; transportation; furniture; hired labor; machinery, farm building and fence repair; interest on loans and credit or purchase agreements; rent on equipment, land and buildings; feed for animals; seed, fertilizer, pesticides, herbicides, and spray materials; other farm supplies; livestock expenses, including medical supplies, and veterinarian bills; machinery hire; fuel and oil; personal, property, and real estate taxes; water charges; personal, property, and crop insurance; auto and truck expenses; utility payments; payments on contracts or loans secured by farmland, necessary farm equipment, livestock, or other chattels; and essential farm machinery (an item of essential farm machinery which is beyond repair may be replaced).

[49] 7 C.F.R. § 1980.124(a)(3)(ii) (1997). Family living expenses are calculated only for individual borrowers and for the partners, joint operators, stockholders, or members who operate the farm of an entity borrower.

[50] See, however, footnote 50.

[51] 7 C.F.R. § 1980.124(a)(3)(iii) (1997).

[52] 7 C.F.R. § 1980.124(a)(4) (1997).

[53] 7 C.F.R. § 1980.124(a)(4) (1997).

[54] 7 C.F.R. § 1980.124(a)(4) (1997).

[55] 7 C.F.R. § 1980.124(a)(4) (1997).

[56] See 7 C.F.R. § 1980.191 (1997).

[57] 7 C.F.R. § 1980.124(a)(5) (1997).

[58] 7 C.F.R. § 1980.124(a)(5) (1997).

[59] 7 C.F.R. § 1980.124(a)(5) (1997).

[60] 7 C.F.R. § 1980.106(b), "Positive cash flow" (1997). These calculations are summarized in Appendix A of this book.

[61] 7 C.F.R. § 1980.106(b), "Positive cash flow" (1997). These calculations are summarized in Appendix A of this book.

[62] 7 C.F.R. § 1980.124(a)(5) (1997).

[63] 7 C.F.R. § 1980.124(a)(2) (1997).

[64] 7 C.F.R. § 1980.124(a)(1) (1997).

[65] 7 C.F.R. § 1980.124(a) (1997). The exact nature of this requirement is not explained in the regulations.

[66] 7 C.F.R. § 1980.124(b)(4) (1997). The nature of this requirement is not explained in the regulations.

[67] 7 C.F.R. § 1980.124(a) (1997).

[68] 7 C.F.R. §§ 1980.124(a)(6), 1980.6(a), "Holder" (1997).

[69] 7 C.F.R. § 1980.124(a)(6) (1997).

Federal Register *in brief*

The following is a selection of items that were published in the *Federal Register* from July 27 to September 4, 1998.

1. FCIC; Basic provisions, various crop insurance provisions; effective date: 7/1/98. 63 Fed. Reg. 40632.

2. IRS; Estate and gift tax marital deduction; QTIP; effective date 8/19/98. 63 Fed. Reg. 44391.

—Linda Grim McCormick, Alvin, TX

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