June 25, 2010

Branch Chief
Regulations and Paperwork Management Branch
U.S. Department of Agriculture
300 7th Street, SW, 7th Floor
Washington, DC 20024

Delivered via regulations.gov

Re: Value-Added Producer Grant Program (7 CFR Parts 1951 and 4284)
Proposed Rule with Request for Comments – RIN 0570-AA79
(Federal Register Vol. 75, No. 103 at pp. 29920-29932)

Dear Chief:

I am submitting these comments on behalf of the National Sustainable Agriculture Coalition (NSAC) and its member organizations regarding the Proposed Rule for the Value-Added Producer Grant Program (VAPG). NSAC represents 40 family farm, rural development, and conservation organizations from around the U.S. that share a commitment to federal policy that promotes healthy, economically vibrant rural communities, sustainable agricultural production systems, and family-based farms and ranches.

We have been closely involved with the VAPG program since helping secure its passage in 2000. As you know, VAPG was created by the Agricultural Risk Protection Act of 2000 and modified by the 2002 and 2008 Farm Bills. It is designed to provide funding to producers to research, plan, and launch new value-adding enterprises to increase farm income and help improve rural economies.

Value-added products include ones that have:

- Undergone a change in physical state
- Produced in a way that enhances their value
- Is physically segregated from similar crops in a manner that enhances its value
- Is a source of on-farm renewable energy
- Is marketed as a locally-grown food product

VAPG includes two, ten percent reserved funds -- one for beginning or socially disadvantaged farmers and ranchers and the other for the development of mid-tier value chains.

Priority is to be given to applications from beginning or socially disadvantaged farmers and ranchers and small and medium-sized family farms and ranches.

The statute creates two kinds of grants, planning and working capital grants with a maximum grant size of $500,000. The 2008 Farm Bill requires a simplified application for grant applications of less than $50,000.

The program has worked reasonably well for a long time without a regulation. We nonetheless respect the decision to move forward with a rule for the program and are very pleased the proposed rule has finally been issued, albeit a full two years after the farm bill was signed into law. Given its successful nine-year track record, however, it is more difficult to understand why the program is being stopped in its tracks in order to finalize the regulation.

The decision to put the 2010 NOFA on hold until rulemaking is completed is particularly frustrating given the torpid pace of producing the rule. Assuming that there is no turning back from the decision to do so, we urge you to move with great speed to quickly produce the final rule and NOFA in record time. We note the comment period ends just two days prior to the start of the final quarter of the fiscal year. Time is clearly of the essence.

We also note, in advance, that the producer community should not be the ones to suffer from the failure of the government to produce a rule and NOFA within a reasonable time frame. We would strongly advise against shortening the turnaround time for proposals to be written and submitted. The program as a whole will be harmed if government delay results in unrealistic timeframes being forced upon the user community.

Finally, with respect to the rules themselves, it is incredibly important that the final rule fixes several major problems with the proposed rule. The key problems with the proposed rules are several ways in which they create obstacles for participation by the very farmers and ranchers the program is designed to help by:

- restricting their participation in planning grant activities;
- raising the specter of conflict of interest where none exists;
- requiring unreasonable, fantasy levels of beginning farmer membership in producer groups; and
- providing insufficient scoring points for priority groups.

We address each of these major problems in the detailed comments that follow.

Thank you for considering our recommendations in the development of a final rule.

Sincerely,

Ferd Hoefner

Ferd Hoefner
Policy Director
National Sustainable Agriculture Coalition

NSAC Comments and Recommendations
Value-Added Producer Grant Program Proposed Rule
(Federal Register Vol. 75, No. 103 at pp. 29920-29932)

1. As in the proposed rule, the final rule should allow for grant payment and in-kind matching credit for producer participation in the development of business and marketing plans, but also extend the same treatment to feasibility studies.

The 2009 VAPG NOFA for the first time explicitly excluded farmer and rancher time as an allowable in-kind contribution for planning grants, substantially reducing the number of applicants that had the means to apply and reversing almost a decade of understanding in the field of how the VAPG grant works. This was a serious mistake that would do severe damage to the program if left uncorrected.

We are very heartened, therefore, to see this statement in the Proposed Rule's Supplementary Information section (I. Background, B. Nature of the Program, paragraph five):

> *The Agency notes, pursuant to general Federal directives providing guidance on grant usage that the 100 percent matching funds requirement described in the Agriculture Risk and Protection Act of 2000 may include payment for the time of the applicant/producer or the applicant/producer's family members only for the production of the business and marketing plans.*

More importantly, Section 4284.923(a) of the rule itself states in part:

> *In-kind contribution of matching funds to cover applicant participation in development of business plans and/or marketing plans is allowed to the extent that the value of such work can be appropriately valued.*

VAPG grants are at their core producer grants for entrepreneurial producer-based projects. It is vital that producers be able to contribute their sweat equity to building and launching their project. Participation by consultants and outside experts can also be very important. But the program should not ever be viewed primarily as a grant program that passes funding through farmers and ranchers to paid outside consultants. Such a view is contrary to law and contrary to the intent of Congress in designing the program.

In addition to providing grant funds to pay for the time of the applicant or the applicant's family members in the project, it is also critical that producers be able to choose to contribute in-kind services as part of their matching requirements. If they were not allowed to do so, it would tilt the program to only the well-off, those with access to sufficient capital to fully fund their match requirements. Such a result would contradict the very reason for the program's existence.

<u>Therefore, we strongly support the provision at 4284.923(a) cited above and urge that it be retained, but also strengthened, in the final rule.</u>

The final rule on this point should be strengthened in two ways.

First, the statement from the proposed rule's preamble quoted above refers appropriately to both the applicant and the applicant's family. The sentence in 4284.923(a), however, refers only to the

applicant and does not mention the applicant's family. This oversight should be fixed by adding a specific reference to the applicant's family, to match the clear intent as rendered in the preamble.

Second, the major element that is still missing from this provision in Section 4284.923(a) is an allowance for producer participation in planning grants and for in-kind producer matching contributions in the development of a value-added business feasibility study.

The statute is reasonably clear on this matter:

> *A grantee under paragraph (1) shall use the grant -- (A) to develop a business plan or perform a feasibility study to establish a viable marketing opportunity for a value-added agricultural product;*
> (7 U.S.C. 1621 (b)(3)(A))

The statute provides that producers may ***perform*** feasibility studies as part of planning grants. If a producer receiving an award can use the grant to themselves ***perform*** a feasibility study then certainly they should also be able to count portions of their time working on a feasibility study as an in-kind match.

Feasibility studies can be conducted by a qualified consultant, and in many cases should be, but with input and contributions from the producer(s). We note that marketing and business plans are critical components for the feasibility study and the proposed rule at 4284.923(a) already allows producers and their families to count their marketing and business plan development time as part of their in-kind match. It would be logically inconsistent to say they can count time toward the two critical components of the feasibility study, but not the feasibility study per se. Moreover, consultants will be relying on the producer(s) to supply much of the additional information that will provide the basic background and parameters of the feasibility study without which they cannot proceed. For these reasons an explicit reference to feasibility studies must be added to 4284.923(a).

To address both of these issues – family members and feasibility studies -- we recommend that Section 4284.923(a) of the rule be modified as follows:

> *(a) Planning funds may be used* ***by applicants for the costs associated with conducting and developing a feasibility study, business plan, and/or marketing plan associated with the processing and/or marketing of a value-added product, including costs required*** *to pay for a qualified consultant to conduct and develop a feasibility study, business plan, and/or marketing plan associated with the processing and /or marketing of a value-added product.* ~~***Planning funds may not be used for applicant participation in feasibility studies.***~~ *In-kind contribution of matching funds to cover applicant* ***or family members of the applicant*** *participation in development of* ***feasibility studies***, *business plans and/or marketing plans is allowed to the extent that the value of such work can be appropriately valued. Funds may not be used to evaluate the agricultural production of the commodity itself, other than to determine the project's input costs related to the feasibility of processing and marketing the value-added product.*

This is not the only improvement needed to make the rule consistent with itself and with the statute on the issue of feasibility studies. The rule's definition of "feasibility study" contradicts the statute at 7 U.S.C. 1621 (b)(3)(A) and would also contradict the proposed rule at 4284.923(a) once modified as suggested above.

We therefore recommend the following conforming language be added to that definition to provide consistency and clarity:

4284.902 Definitions

Feasibility study. *An analysis* ~~**by a qualified consultant**~~ *of the economic, market, technical, financial, and management capabilities of a proposed project or business in terms of the project's expectation for success.* ***Applicants may use a qualified consultant to perform the feasibility study, in which case applicants and family members of applicants may participate in collecting data and providing input required by the qualified consultant in the development of a feasibility study and may either receive payment for their time or may count their time as an in-kind contribution of matching funds to the extent that the value of such work can be appropriately valued.***

2. Elements of the proposed rule that contradict the statute and the statement in Section 4284.923(a) providing for in-kind matching for participation in development of business and marketing plans should be corrected so the rule as a whole is consistent and clear and does not lead to arbitrary implementation decisions.

We are concerned that a variety of sections in the proposed rule contradict, or at the very least confuse, the otherwise clear directive in the proposed rule that farmers and ranchers are encouraged to write or help write business and marketing plans for their proposed projects and have the time they invest in the work accepted as an eligible in-kind match for a grant.

The statute clearly states that grants will be awarded to:

> *an eligible independent producer (as determined by the Secretary) of a value-added agricultural product to assist the producer—(i) in developing a business plan for viable marketing opportunities for the value-added agricultural product ; or (ii) in developing strategies that are intended to create marketing opportunities for the producer….*
> (7 U.S.C. 1621 (b)(1)(A))

Preserving this producer-centered approach to grants is fundamental to VAPG's success. Our member organizations that have been engaged in education and technical assistance on VAPG grants believe that successful value-added projects are the result of a profound understanding of the complexities of farming businesses that can only be provided by the farmers and ranchers who will be participating in the enterprise. Conversely, projects that fail most often do so because they did not incorporate the insights and experience of the producers the business will rely on for its success. Farmers and ranchers must be central to the work required in planning for a new enterprise.

The proposed rule needs to be fixed to be consistent throughout, clear to understand, and easy to interpret. In the interest of such regulatory consistency, NSAC proposes the following seven changes.

A. Conflict of Interest

In the definition section (4284.902) the term "conflict of interest" is defined as:

A situation in which a person or entity has competing professional or personal interests that make it difficult for the person or business to act impartially. An example is a grant recipient or an employee of a recipient that conducts or significantly participates in conducting a feasibility study for the recipient.

Concern over conflicts of interest began to emerge in VAPG NOFAs several years ago and has now led to an overly restrictive definition. Specifically, the example provided in the second sentence of the definition of conflict of interest cited above implies that farmers and ranchers have an inherent bias in favor of their project ideas that trumps an equally compelling interest in not investing their resources in an idea that will not work. NSAC members' experience, in contrast, shows that successful businesses are those in which participating farmers and ranchers are intimately engaged in all of the planning stages.

Given the example included as part of the conflict of interest definition, the continued references to conflict of interest in the proposed rule give the clear impression that participation by the producer, their family members and/or staff creates huge problems and is prohibited. This undermines the fundamental principle of the VAPG program: that farmers and ranchers should be empowered through these grants to explore creative new businesses that will increase farm income and create or expand rural wealth.

This broad definition of conflict of interest could easily lead to an interpretation that would prohibit farmer or rancher participation in any of the work necessary for planning grants and result in VAPG evolving into a grant program that benefits consultants rather than producers.

We agree that feasibility studies generally should be written by third party professionals but disagree that a conflict of interest exists that should preclude producers from being integral to the research and information collection necessary for a successful feasibility study. The economic realities of the farmer and rancher communities the VAPG program was created to help ameliorate require that the program allow producers' time and expenses be permitted as an allowable match for grant funds. The best businesses -- the ones most likely to succeed -- are those in which producers are most actively engaged in the enterprise's planning. Their involvement should be encouraged and counted as an equally important contribution as cash to the project.

The inclusion of the example in the second sentence of the proposed rule's definition of conflict of interest, when applied to sections of the rule that refer back to the conflict of interest definition, contradicts the statute at 7 U.S.C. 1621 (b)(1)(A) and (b)(3)(A) as well as the allowance made in 4284.923(a) and must be fixed to provide consistency and clarity.

We therefore recommend the example be eliminated from the definition as follows:

A situation in which a person or entity has competing professional or personal interests that make it difficult for the person or business to act impartially. ~~***An example is a grant recipient or an employee of a recipient that conducts or significantly participates in conducting a feasibility study for the recipient.***~~

Without this change, the conflict of interest provision directly contradicts the statute as well as the proposed rule at 4284.923(a), leaving program implementation decisions up to the whim of the grant reviewers as to which section of the law and rule to apply and which to ignore. The example in the

conflict of interest definition therefore must be dropped to conform to the statute, create an internally consistent rule, and avoid fomenting arbitrary and capricious decision making.

B. Marketing Plan

In the definition section (4284.902) the term "marketing plan" is defined as:

> *A plan for the project conducted by a qualified consultant that identifies a market window, potential buyers, a description of the distribution system and possible promotional campaigns.*

The statute 7 U.S.C. 1621 (b)(1)(A) and (b)(3)(A) clearly states that VAPG grants are to assist an eligible producer in developing a business plan for viable marketing opportunities or in developing strategies that are intended to create marketing opportunities for the producer. This definition contradicts the statute by granting consultants exclusive rights to awards for marketing plans. Moreover, this definition also directly contradicts the allowance in Section 4284.923(a) for producers to count their time in developing marketing plans as in-kind matching contributions.

Therefore, NSAC proposes that the definition be fixed to read:

> ***Marketing plan.*** *A plan for the project* ~~**conducted by a qualified consultant**~~ *that identifies a market window, potential buyers, a description of the distribution system and possible promotional campaigns.*

Without this change, the marketing plan definition directly contradicts the statute as well as Section 4284.923(a) of the proposed rule, leaving program implementation decisions up to the whim of the grant reviewers as to which section of the law and rule to apply and which to ignore. Dropping the exclusive reference to qualified consultants must be deleted to conform to the statute, create an internally consistent rule, and avoid potential arbitrary and capricious decision making.

C. Matching Funds

In the definition section (4284.902) the term "matching funds" is defined as:

> *A cost-sharing contribution to the project via confirmed cash or funding commitments from eligible sources without a conflict of interest, that are used for eligible project purposes during the grant period. Eligible matching funds include confirmed applicant cash, loan or line of credit, non-Federal grant sources (unless otherwise provided by law), and third party cash or eligible third-party in-kind contributions. Matching funds must be at least equal to the grant amount, and combined grant and matching funds must equal100 percent of the total project costs. All eligible cash and third-party in-kind matching funds contributions must be spent on eligible expenses during the grant period, and are subject to the same use restrictions as grant funds. Matching funds must be spent at a rate equal to or greater than the rate at which grant funds are expended, and if matching funds are proposed in an amount exceeding the grant amount, those matching funds must be spent at a proportional rate equaling the match-to-grant ratio identified in the budget. Expected program income may not be used to fulfill the matching funds requirement at time of application. Further, funds used for an ineligible purpose, contributions donated outside the proposed grant period, and in-kind contributions that are invalid, overvalued or include potential for a conflict of interest are not acceptable matching funds. All matching funds must be verified by authentic documentation from the source as part of the application.*

First, as an aside, we note that this long paragraph is not, on the whole, a definition but rather a set of substantive rule provisions that probably belong in the body of the rule rather than in the definition section. Mixing detailed operational provisions into a definition is generally not considered good rule writing practice.

Second, and far more importantly, the omission of any mention of producer in-kind matches while specifically referencing third-party in-kind match clearly implies that applicant time is not an eligible match and, combined with the proposed rule's broadly defined conflict of interest definition, will have a chilling effect on potential farmer and rancher applicants.

To be consistent with the allowance in Section 4284.923(a), the rule must clearly state that producer time, travel expenses, purchased materials, and other expenses incurred working on the project are eligible in-kind matching contributions for grants and do not present a conflict of interest.

Therefore, we recommend the following modifications to the definition:

> ***Matching funds.*** *A cost-sharing contribution to the project via confirmed cash or funding commitments* ***or via anticipated in-kind contributions*** *from eligible sources without a conflict of interest that are used for eligible project purposes during the grant period. Eligible matching funds include confirmed applicant cash, loan or line of credit, non-Federal grant sources (unless otherwise provided by law),* ***and eligible in-kind contributions,*** *and third party cash or eligible third-party in-kind contributions. Matching funds must be at least equal to the grant amount, and combined grant and matching funds must equal100 percent of the total project costs. All eligible cash and* ~~third-party~~ *in-kind matching funds contributions must be spent on eligible expenses during the grant period, and are subject to the same use restrictions as grant funds. Matching funds must be spent at a rate equal to or greater than the rate at which grant funds are expended, and if matching funds are proposed in an amount exceeding the grant amount, those matching funds must be spent at a proportional rate equaling the match-to-grant ratio identified in the budget. Expected program income may not be used to fulfill the matching funds requirement at time of application. Further, funds used for an ineligible purpose, contributions donated outside the proposed grant period, and in-kind contributions that are invalid, overvalued or include potential for a conflict of interest are not acceptable matching funds. All matching funds must be verified by authentic documentation from the source as part of the application.*

Without this change, the matching grant definition directly contradicts 4284.923(a), leaving implementation of the program up to the whim of the grant reviewers as to which section of the rule to apply and which to ignore. Inclusion of producer in-kind matching contributions and deletion of exclusive reference to third-party in-kind matching contributions is essential to create an internally consistent rule and to avoid potential arbitrary and capricious decision making.

D. Planning Grant

In the definition section (4284.902) the term "planning grant" is defined as:

> *A grant to facilitate the development of a defined program of economic planning activities to determine the viability of a potential value-added venture, and specifically for the purpose of paying for a qualified (third-party) consultant to conduct and develop a feasibility study, business plan, and/or marketing plan associated with the processing and/or marketing of a value-added agricultural product.*

This definition makes clear that planning grants are to be used to develop a feasibility study which may include a business and/or marketing plan. The statute provides for two types of grants – one to perform feasibility studies and one for working capital. Clearly what the agency and the proposed rule refers to as planning grants are the first of the two statutory grant strategies. As discussed in our point number one above, the statute directs the agency to make grants to producers to perform feasibility studies and develop business plans. Thus the statute requires the agency to make planning grants to producers who in turn will perform feasibility studies and development business plans.

The "planning grant" definition must be changed to conform to the statute at 7 U.S.C. 1621 1621(b)(1)(A) and (b)(3)(A) and to clarify that these grants are designed to benefit producers who by statute may perform the feasibility study. We support the notion that use of a "qualified (third-party) consultant" may be strongly encouraged. Applicant producers should have the option to hire consultants, and should in fact be encouraged to do so, but they cannot be required to do so by rule. Otherwise the rule is in direct conflict with the statute.

NSAC therefore recommends the following definition:

> ***Planning grant:*** *A grant to facilitate the development of a defined program of economic planning activities to determine the viability of a potential value-added venture,* ~~***and specifically for the purpose of paying for a qualified (third-party) consultant***~~ **including** *to conduct and develop a feasibility study, business plan, and/or marketing plan associated with the processing and/or marketing of a value-added agricultural product.* ***A planning grant may be used in whole or in part for the purpose of paying for a qualified third party consultant. Use of third party consultants is strongly encouraged.***

Without this change, the planning grant definition directly contradicts 7 U.S.C. 1621 (b)(1)(A) and (b)(3)(A) as well as Section 4284.923(a) of the proposed rule, leaving program implementation decisions up to the whim of the grant reviewers as to which section of the law and rule to apply and which to ignore. Dropping the reference to mandatory, exclusive use of qualified consultants is critical to conform to the statute, create an internally consistent rule, and avoid potential arbitrary and capricious decision making.

E. Project Eligibility

Section 4284.922 (b)(5) of the proposed rule states:

> *(5) Working capital applications must include a feasibility study and business plan completed specifically for the proposed value-added project by a qualified consultant. The Agency must concur in the acceptability or adequacy of the feasibility study and business plan for eligibility purposes.*

This is the first of the operational provisions of the proposed rule that is in conflict with 7 U.S.C. 1621 (b)(1)(A) and (b)(3)(A) as well as Section 4284.923(a) of the proposed rule. To be in accord with the statute, the use of consultants may be encouraged but cannot be required. To be consistent with the producer in-kind contribution of the proposed rule, producer in-kind matching contributions must be recognized in this paragraph to avoid it seeming to override 4284.923(a).

NSAC members do not believe that a good business plan must always or only be written by a third party. To the contrary, they believe that the producer or producer group members planning the

enterprise often have the *"knowledge, expertise, and experience to perform the specific task required in an efficient, effective, and authoritative manner"* -- the Proposed Rule's definition for *qualified consultant*.

Furthermore, the rule gives the Agency the right and responsibility to assess the merits of the feasibility study and business plan, which removes any possible justification for having them done solely by non-producers. In addition, grant applications are reviewed at the local, state and national level and proposal feasibility is a criterion for funding. Potential inadequacies with proposals can be determined in this review process without resorting to sweeping disqualifications that will make VAPG grants less accessible to the producers who need them most.

NSAC recommends the following simple modification of this provision:

> *(5) Working capital applications must include a feasibility study and business plan completed specifically for the proposed value-added project* ***~~by a qualified consultant~~****. The Agency must concur in the acceptability or adequacy of the feasibility study and business plan for eligibility purposes.*

Without this change, paragraph (5) of the program eligibility section of the proposed rule directly contradicts 7 U.S.C. 1621 (b)(1)(A) and (b)(3)(A) as well as Section 4284.923(a) of the proposed rule, leaving program implementation decisions up to the whim of the grant reviewers as to which section of the law and rule to apply and which to ignore. Dropping the reference to mandatory, exclusive use of qualified consultants is critical to conform to the statute, create an internally consistent rule, and avoid potential arbitrary and capricious decision making.

F. Ineligible uses of grant and matching funds

Section 4284.924 of the proposed rule states:

> *(p) Pay for any goods or services provided by a person or entity that has a conflict of interest or an appearance of a conflict of interest. Also, note that in-kind matching funds may not be provided by a person or entity that has a conflict of interest or an appearance of a conflict of interest.*

This is a second operational provision of the proposed rule that is in conflict with the provision at 4284.923(a). The emphasis on conflict of interest or an appearance of conflict of interest is misplaced in reference to in-kind matching funds. All matching contributions must be verifiable and the time, or "sweat equity", that farmers, ranchers and/or their families invest to design and develop these value-added enterprises are necessary to their success, as the rule otherwise provides in 4284.923(a).

To clear up the inconsistency, NSAC recommends the deletion of the second sentence as follows:

> *(p) Pay for any goods or services provided by a person or entity that has a conflict of interest or an appearance of conflict of interest.* ***~~Also, note that in-kind matching funds may not be provided by a person or entity that has a conflict of interest or an appearance of a conflict of interest.~~***

G. Application Package

Section 9284.931 of the proposed rule at paragraph (b)(4) states:

Verification of cost-share matching. Using the format prescribed by the application package, the applicant must provide authentic documentation from the source to confirm the eligibility and availability of both cash and in-kind contributions that meet the following requirements:

…

(v) Matching funds must be provided in the form of confirmed applicant cash, loan, or line of credit; or confirmed third-party cash or eligible third-party in-kind contribution.

(vi) Examples of ineligible matching funds include funds used for an ineligible purpose, contributions donated outside the proposed grant period, third-party in-kind contributions that are over-valued, expected program income at time of application or instances where the potential for a conflict of interest exists, including applicant in-kind contributions in 4284.923(a).

These two subparagraphs represent a third operational provision of the proposed rule in conflict with the allowance provided in 4284.923(a). Although the proposed rule at 4284.923(a) states that applicant producer's time is an acceptable in-kind contribution, these two provisions each contradict that statement. Omitting mention of applicant time or other in-kind match in subparagraph (v) and (vi) while including a specific reference to eligible third-party contributions implies that the only kind of match that applicants can provide are in the form of cash.

Also, subsection (vi) unnecessarily raises the specter of rejecting the in-kind contributions of producers permitted by 4284.923(a) by cross-reference to the conflict of interest definition we address is A. above.

NSAC recommends these subparagraphs be rewritten as follows:

Verification of cost-share matching. Using the format prescribed by the application package, the applicant must provide authentic documentation from the source to confirm the eligibility and availability of both cash and in-kind contributions that meet the following requirements:

…

(v) Matching funds must be provided in the form of confirmed applicant cash, loan, or line of credit, ***and may include payment for the time of the applicant/producer or the applicant producer's family members to the extent that the value of such work can be appropriately valued;*** *or confirmed third-party cash or eligible third-party in-kind contribution.*

(vi) Examples of ineligible matching funds include funds used for an ineligible purpose, contributions donated outside the proposed grant period, third-party ***or applicant*** *in-kind contributions that are over-valued, expected program income at time of application or instances where the potential for a conflict of interest exists*~~,~~ ~~**including applicant in-kind contributions in 4284.923(a)**~~.

Without this change, the matching fund language in the application package section of the proposed rule directly contradicts 4284.923(a) of the proposed rule, leaving implementation of the program up to the whim of the grant reviewers as to which section of the rule to apply and which to ignore.

Inclusion of producer in-kind matching contributions is essential to create an internally consistent rule and to avoid potential arbitrary and capricious decision making.

3. The final rule should facilitate applications from projects benefiting beginning farmers and ranchers.

Supporting projects that contribute to increasing opportunities for beginning farmers and ranchers is a statutory priority for the VAPG program. The statute also provides for a 10 percent reserved fund set-aside for projects that benefit beginning farmers or ranchers or socially disadvantaged farmers or ranchers. The specific wording of these two statutory provisions is very important:

> *(b)(6) PRIORITY.—In awarding grants under this subsection, the Secretary shall give priority to projects* ***that contribute to*** *increasing opportunities for—*
>
> *(A) beginning farmers or ranchers;*
>
> …
>
> *(7)(C)(i) IN GENERAL.—The Secretary shall reserve 10 percent of the amounts made available for each fiscal year under this paragraph to fund projects* ***that benefit*** *beginning farmers or ranchers or socially disadvantaged farmers or ranchers.*
>
> ***(emphasis added)***

The agency is to give priority to projects that ***contribute*** to farming opportunities for beginning farmers and is to reserve funds for projects that ***benefit*** beginning farmers. No where does the statute say that such priority projects must exclusively benefit beginning farmers and no one else. By statute it is sufficient that the priority projects contribute to new farming opportunities and benefit beginning farmers.

In implementing the clear intent of Congress, the agency needs to provide guidance in regulation and/or in guidance to grant reviewers as to what constitutes a significant enough contribution or benefit to beginning farmers as to qualify a proposal as meeting the program priority or access to the reserved fund.

Stipulating the criteria in the rule has the negative effect of locking the criteria in place for all the years the rule remains in place. The alternative -- dealing with the issue in the annual NOFA and/or grant review criteria -- has the benefit of allowing for an iterative process to refine and fine tune the criteria based on actual experience.

Our preference would be providing for iterative annual adjustments as needed to ensure the intent of Congress in creating the beginning farmer priority is actually achieved in the reality of program implementation. If, however, it is going to be stipulated in the rule, it is all the more urgent that the rule gets it right, since there will be no turning back.

In the case of individual farmer/rancher grants there is no problem. The individual farmer or rancher is either a beginner or not. However, group proposals are an entirely different matter.

The proposed rule's beginning farmer definition dictates that all members of the farmer group, coop, business, or other entity must be beginning farmers or ranchers, an extremely unlikely situation in the real world. In essence, the proposed rule completely negates the express will of Congress in creating the priority and reserved fund in the first place by creating a stipulation that renders the directive effectively null and void.

Even if a 100 percent beginning farmer member coop or business or farm group existed somewhere in the real world, requiring a new farm business made up multiple farmers be 100 percent beginners will preclude mentoring opportunities with more experienced farmers and increase risk of failure. Hence it would tend to defeat the purpose of the program.

There are two operative provisions in the proposed rule related to beginning farmers and ranchers. The first is in reference to the reserved funds (Section 4284.922) and states:

> *(d)(1) If the applicant is applying for beginning farmer or rancher, or socially-disadvantaged farmer or rancher reserved funds, the applicant must provide documentation demonstrating that the applicant meets one of these definitions.*

The second is a very indirect reference in the evaluation criteria and scoring of applications section, where up to 15 points are awarded for "Type of applicant."

In the final analysis, therefore, everything in the rule hinges on the definition of beginning farmer or rancher in the definition section of the rule:

> *Beginning farmer or rancher. This term has the meaning given it in section 343(a) of the Consolidated Farm and Rural Development Act (7 U.S.C. 1991(a)) and is an entity in which none of the individual owners have operated a farm or a ranch for more than 10 years. For the purposes of this subpart, a Beginning Farmer or Rancher must currently own and produce the agricultural commodity to which value will be added.*

This language indicates that proposals from individual beginning farmers or ranchers as well as applications from an agricultural producer group, coop, and business must include exclusively beginning farmers or ranchers to qualify for the beginning farmer or rancher category. As it applies to group proposals, this definition flies in the face of the statutory language that projects simply contribute to beginning farmer opportunities and benefit beginning farmers.

There are two remedies for this disregard of the statute and disregard of real world considerations. One would be to change the definition. The other would be to leave the definition as is but add an operative provision elsewhere in the rule to ensure the rule complies with the law and common sense.

<u>If the first alternative is chosen, NSAC recommends the definition of beginning farmer and rancher be amended as follows</u>:

> *Beginning farmer or rancher. This term has the meaning given it in section 343(a) of the Consolidated Farm and Rural Development Act (7 U.S.C. 1991(a)) and is an entity in which none of the individual owners have operated a farm or a ranch for more than 10 years.* ***<u>In the event that there are multiple</u>***

farmer or rancher owners of the applicant group, at least 25 percent of the ownership must be held by Beginning Farmers or Ranchers. *For the purposes of this subpart, a Beginning Farmer or Rancher must currently own and produce the agricultural commodity to which value will be added.*

If the second alternative is chosen, NSAC recommends the following language be added to 4284.920:

Under Section 4284.920 -- Applicant eligibility -- add a new (c) as follows and re-letter the rest of the section accordingly –

(c) Beginning farmers or ranchers. To qualify for the priority for projects that contribute to opportunities for beginning farmers or ranchers or for the reserved fund for projects that benefit beginning farmers or ranchers, an applicant that is an agricultural producer group, a farmer or rancher cooperative, or a majority-controlled producer-based business venture must be comprised of at least 25 percent beginning farmers or ranchers.

One or both of these options are required to fix a very serious problem with the proposed rule.

We note that the definition of socially-disadvantaged farmers and ranchers includes a 51 percent threshold for group applications. While there are a number of producer cooperatives that are made up exclusively or almost exclusively of socially disadvantaged farmers and ranchers, NSAC does not know of any cooperatives or businesses that consist exclusively of beginning producers. The needs and realities of the two groups are distinct. A majority of members of socially disadvantaged producer groups and coops often have many years of agricultural experience and can work with any beginning producers in the group.

So while a 51 percent standard makes sense for socially-disadvantaged groups, it does not make sense for beginning farmers and ranchers. Rules, to be effective, must reflect the facts on the ground and not some non-existent ideal world. Moreover, mentoring by more experienced farmers is a need and an opportunity specific to enterprises including beginning farmers and ranchers which also makes the 25 percent threshold for beginners an appropriate measure to qualify a project for this reserved fund.

Again, our preference would be to leave the specific threshold to the annual, iterative NOFA process, so the agency and the public can learn from experience about what works best to ensure the intent of Congress is fulfilled. If that route is chosen, the language of the NOFA must be crystal clear about the 25 percent standard. If, however, the rule is going to preclude a reasonable result by way of a super restricted definition and there is to be no countervailing measure in the NOFA, then we would insist on one of the fixes proposed above.

4. The final rule should give proper acknowledgement of the statutory VAPG priorities by strengthening the grant evaluation criteria and scoring section.

The Food, Conservation, and Energy Act of 2008 (2008 Farm Bill) amended the VAPG program in several important ways, including identifying priority groups for funding and establishing two

program reserved funds. NSAC believes that these program modifications are significant and should be addressed in the preamble to the rule in the Summary section and in the Supplemental Information section. Most importantly, the proposal evaluation criteria and scoring applications section (4284.942) needs to be strengthened to make the statutory priorities actual programmatic priorities.

The 2008 Farm Bill authorized granting priority for projects that increase opportunities for (1) beginning farmers or ranchers, (2) socially disadvantaged farmers or ranchers, and (3) operators of small- and medium-sized family farms and ranches structured as family farms.

The 2008 Farm Bill also established two, ten percent reserved funds within the VAPG program to support (1) mid-tier value chain projects, and (2) projects that benefit beginning or socially disadvantaged farmers or ranchers.

The statutory priorities and set-asides are clearly intended to ensure that these producer groups and this type of rural development marketing model are more likely to be supported with VAPG grant funds.

Since the language changes in the 2008 Farm Bill fundamentally address the character of the VAPG grant program Congress intended to create, NSAC believes that they should be clearly referenced in the discussion of the rule. We find the omission of such a discussion in the preamble to the proposed rule to be quite glaring.

<u>We suggest adding the following language to the Summary section when issuing the final rule</u>:

> **SUMMARY:** *The Food, Conservation, and Energy Act of 2008 (the Act), amends section 231 of the Agricultural Risk Protection Act of 2000, which established the Value-Added Producer Grant Program. This program will be administered by the Rural Business-Cooperative Service. Under the proposed program, grants will be made to help eligible producers of agricultural commodities enter into or expand value added activities including the development of feasibility studies, business plans, and marketing strategies. The program will also provide working capital for expenses such as implementing an existing viable marketing strategy.* ***<u>The program provides a priority for funding for projects that contribute to opportunities for beginning farmers or ranchers, socially disadvantaged farmers or ranchers, and operators of small- and medium-sized family farms and ranches. Further, it creates two reserved funds each of which will include 10 percent of program funds each year to support applications that support opportunities for beginning and socially disadvantaged farmers and ranchers and for proposed projects that develop mid-tier value marketing chains.</u>*** *The Agency proposes to implement the program to meet the goals and requirements of the Act.*

<u>Likewise, we suggest the addition of the following language to the Supplementary Information section</u>:

> **SUPPLEMENTARY INFORMATION:**
> **I. Background**
> *B. Nature of the Program*

This subpart contains the provisions and procedures by which the Agency will administer the Value-Added Producer Grant (VAPG) Program. The primary objective of this grant program is to help Independent Producers of Agricultural Commodities, Agriculture Producer Groups, Farmer and Rancher Cooperatives, and Majority-Controlled Producer-Based Business Ventures develop strategies to create marketing opportunities and to help develop Business Plans for viable marketing opportunities regarding production of bio-based products from agricultural commodities. As with all value-added efforts, generating new products, creating expanded marketing opportunities, and increasing producer income are the end goal.

Eligible applicants are independent agricultural producers, farm and rancher cooperatives, agricultural producers groups, and majority-controlled producer-based business ventures.

The program includes priorities for projects that contribute to opportunities for beginning farmers or ranchers, socially disadvantaged farmers or ranchers, and operators of small- and medium-sized family farms and ranches. Applications from these priority groups will receive additional points in the scoring of applications. In the case of equally ranked proposals, preference will be given to applications that more significantly contribute to opportunities for beginning farmers and ranchers, socially disadvantaged farmers and ranchers, and operators of small- and medium-sized family farms and ranches.

Further, the program includes two reserved funds each of which will include ten percent of program funds each year to support applications that support projects that benefit beginning and socially disadvantaged farmers and ranchers and that develop mid-tier value marketing chains.

Beyond these preamble statements, the operative provision in the rule itself for the priority categories needs to be significantly strengthened to make them actual priorities rather than minor preferences.

We recommend that Section 4284.942 – Proposal evaluation criteria and scoring applications -- be strengthened as follows:

(b) Scoring applications. The maximum number of points that will be awarded to an applicant is 100, plus an additional 10 points if the project is located in a rural area. The criteria specified in paragraphs (b)(1) through (7) of this section will be used to score each application. The Agency will specify how points are awarded for each criterion in a Notice published each fiscal year.

(1) Nature of the proposed project (maximum ~~***25***~~ ***20*** *points).*
(2) Personnel qualifications (maximum 20 points).
(3) Commitments and support (maximum 10 points).
(4) Work plan/budget (maximum 20 points).
(5) ~~***Type of applicant***~~ ***Contribution to priority beneficiaries*** *(maximum* ~~***15***~~ ***25*** *points).*
(6) Administrator priority categories and points (maximum ~~***10***~~ ***5*** *points).*
(7) Rural or rural area location (10 points may be awarded).

(c) Priority groups. In the event of applications equally ranked but in which one application substantially serves one or more of the priority groups and the other does not, or one serves a priority group or groups to a significantly greater degree than the

other, the one that better serves the priority group shall be the higher ranked proposal.

It is difficult to see how the intent of Congress has been met in a proposed rule that proposes to provide just 15 points out of 110 points to proposals which fulfill the statutory priority. In our view there needs to be a more substantial weighting of the ranking criteria to create a real priority. Assuming the agency prefers to keep the point total constant, we have adjusted the numbers to give more weight to the statutory priority while not doing damage to the overall construct of the scoring system.

Also, the "type of applicant" phrase in the proposed rule's scoring system is vague and potentially very misleading. We recommend that clear and unambiguous language be substituted to tie these points directly to the statutory priorities.

Language should also be added to the final rule to make clear that "priority" means among other things that if applications are otherwise equally ranked but one application substantially serves one or more of the priority groups and the other does not, or one does so to a significantly greater degree than the other, the one that better serves the priority group is the higher ranked proposal.

5. The final rule should provide a more reasonable definition of medium-sized farms and ranches.

The proposed rule defines the medium-sized farms and ranches as those with average annual sales between $250,000 and $700,000. NSAC recommends that the sales limit should be raised to $1,000,000.

According to USDA data, all sales classes above $5,000 and below $1,000,000 are declining in numbers. The proposed rule defines small farms as those with sales below $250,000. The sales classes between $250,000 and $1,000,000 are the so-called "disappearing middle" of agriculture that Secretary Vilsack has so eloquently addressed in his public speeches.

This is the segment of agriculture perfectly tailored for the VAPG program and its value-added income opportunities. While nearly 60 percent of the total value of agricultural production is captured by farms of over $1 million in sales, the disappearing middle still represents a substantial amount of production – 25 percent but declining -- and a large number of total producers.

They are well-situated, as the Secretary repeatedly points out, to take advantage of value-added opportunities in local and regional food systems and in bioenergy and bioproducts. While their ability to compete in the raw, undifferentiated commodity market is unlikely to be a path to survival and prosperity without further farm consolidation and the lost economic opportunity that goes with it, competing in the value-added market can be a good bet for these farms.

Average profit margins are lower on farms under $1 million in gross farm income than for those over $1 million, and lower on farms of less than $250,000 than on farms between $250,000 and $1 million. However, the most successful small and medium-sized farms, those most likely to remain in business and shore up rural farming communities and economies, actually have comparable profit margins to the largest farms. While specific value-added statistics are not readily available, it is

reasonable to expect that those farms with successful value-adding enterprises are more likely than others to be in that higher profit margin category. From a family farm and rural development perspective, policy, including the VAPG program, should do everything it can to increase their numbers.

Interestingly, according to the 2008 ARMS survey, the percentage of household income derived from farming is slightly higher for farms with sales of $500,000 to $1 million than it is for farms of over $1 million, and nearly as high for farms between $250,000 and $500,000 in sales. All three of these sales classes come in close to a three-quarters reliance on farm income, considerably higher than farms with sales of $100,000 to $250,000 for which a bare majority of household income is derived from farming sources. And that larger small farm sales class of $100,000 to $250,000 in sales is considerably higher than all the smaller sales classes in which a small minority of household income comes from farming sources.

The higher the reliance on on-farm income, the more important value-adding strategies become. In our view, therefore, targeting the program's small and medium-sized family farm priority toward the larger small farm class plus the disappearing middle makes a great deal of sense. These farms rely on farm income for a majority of household income, but need to tap into value-adding enterprises and markets to secure a long-term financial future.

Creating a single farm size threshold for all of agriculture is a difficult proposition given the great diversity of U.S. agriculture. For instance, specialty crop and dairy farms have a much higher percentage of farms over the $1 million sales threshold than the rest of agriculture and for both the vast majority of production comes from those largest farms. While the $700,000 threshold in the proposed rule might be roughly adequate for grain farms, and far more than adequate for poultry farms, it is significantly too low for dairy and produce farms. While one could imagine a more complex rule with thresholds that vary by type of farm, if the final rule sticks with a single threshold, it is important that it works and makes sense for agriculture as a whole. While not perfect, the $1 million threshold is more defensible than the proposed rule's $700,000, for all of the reasons cited above.

NSAC therefore recommends the following amendment to the medium-sized farm definition:

> *Medium-sized farm. A farm or ranch that has averaged between $250,001 and* ~~***$700,000***~~ ***$1,000,000*** *in annual gross sales of agricultural products in the previous three years.*

6. The final rule should make small improvements to the mid-tier value chain provisions to ensure maximum responsiveness and effectiveness.

The concept of a mid-tier value chain is new to the VAPG program as a result of the 2008 Farm Bill. It is important that the rules are written in a way that is properly descriptive of what characterizes these marketing relationships without inadvertently precluding non-traditional marketing alliance that achieve the desired result of increasing markets for producers and improving their ability to achieve fair prices.

For instance, mid-tier value chains may include non-profit organizations that provide aggregation, processing, or transportation services for producers to facilitate sales to local institutions and

markets. Community supported agriculture (CSA) projects are sometimes organized by an individual producer acting on behalf of and with the support of allied farmers or ranchers to market of their aggregated product to institutional and other emerging markets. Since various kinds of mid-tier value chains like those above are still emerging the final rule should be as inclusive and flexible as possible.

NSAC proposed the following small adjustments to the local or regional supply network definition and the mid-tier value chain definition:

> *Local or regional supply network. An interconnected group of entities through which agricultural based products move from production through consumption in a local or regional area of the United States. Examples of participants in a supply network may include agricultural producers,* ***aggregators,*** *processors, distributors, wholesalers, retailers, consumers, and entities that organize or provide* ***facilitation services and*** *technical assistance for development of such networks.*
>
> *Mid-tier value chain. Local and regional supply networks that link independent producers with businesses and cooperatives that market value- added agricultural products in a manner that:*
>
> *(1) Targets and strengthens the profitability and competitiveness of small and medium-sized farms and ranches that are structured as a family farm; and*
> *(2) Obtains agreement from* ***eligible individual producers or*** *an eligible agricultural producer group, farmer or rancher cooperative, or majority controlled producer-based business venture that is engaged in the value chain on a marketing strategy.*
> *(3) For mid-tier value chain projects the Agency recognizes that, in a supply chain network, a variety of raw agricultural commodity and value-added product ownership and transfer arrangements may be necessary. Consequently, applicant ownership of the raw agricultural commodity and value-added product from raw through value-added is not necessarily required, as long as the mid-tier value chain proposal can demonstrate an increase in customer base and an increase in revenue returns to the applicant producers supplying the majority of the raw agricultural commodity for the project.*

In addition, the reserved funds eligibility section (4284.922) at (d)(2)(ii) would be improved by the following addition:

> (d)(2)*(ii) Describe at least two alliances, linkages or partnerships within the value chain that link independent producers with* ***other independent producers or with*** *businesses and cooperatives that market value-added agricultural products in a manner that benefits small or medium-sized farms and ranches that are structured as a family farm, including the names of the parties and the nature of their collaboration;*

7. The agency needs to make good on creating a simplified application for small grants of less than $50,000.

The 2008 Farm Bill explicitly calls on Rural Development to offer a simplified application for small grants of less than $50,000 as recognition that the proposal process is so cumbersome that many excellent, inexpensive projects do not get the support they deserve. The FY 2009 NOFA, however, did not offer a substantive improvement in this regard, and the proposed rule contains nothing more than a one sentence reference that says *"Applicants requesting less than $50,000 will be allowed to*

submit a simplified application, the contents of which will be announced in an annual notice issued pursuant to Section 4284.915." (Section 4284.932)

This issue deserves serious attention and we trust will be dealt with in the soon to be released 2010 NOFA. Given the missed opportunity last year and the lack of any substantive proposal in the proposed rule, we want to flag this issue and to suggest, if necessary, that Rural Development staff work with other agencies, including AMS, FSA, and NIFA, that currently use simplified application forms in a variety of grant and loan programs, to adopt lessons learned about grants and loan documents that are user-friendly for under-resourced groups but still provide necessary assurances of merit or credit worthiness.