National Sustainable Agriculture Coalition

July 24, 2012

Robert Bonnet, Director
Loan Making Division (LMD)
Farm Service Agency - USDA
1400 Independence Avenue, SW, Stop 0522
Washington, DC 20250-0522

Re: Comment: FSA RIN 0560-AI17 Fed. Reg. 31220 (Vol. 77, May 25, 2012)

Dear Mr. Bonnet:

The National Sustainable Agriculture Coalition (NSAC) is grateful for the opportunity to submit comments on the Farm Service Agency (FSA) Proposed Rule to modify the Operating Loan (OL) program by allowing FSA to make microloans to qualified borrowers, including young, beginning, and small farmers, and those serving local and regional food markets.

NSAC is an alliance of grassroots organizations that advocates for federal policy reform to advance the sustainability of agriculture, food systems, natural resources, and rural communities. Our vision of agriculture is one where a safe, nutritious, ample, and affordable food supply is produced by family farmers who make a decent living pursuing their trade, while protecting the environment, and contributing to the strength and stability of their communities. Many NSAC organizations include small, beginning, and diversified producers who serve local and regional markets among their members, and would greatly benefit from FSA's proposed microloan program.

We applaud FSA for this innovative new loan program that will allow USDA to better meet the credit needs of non-traditional borrowers who often face difficulty in obtaining commercial credit, and who often rely on credit cards with high interest rates for many of their smaller-budget farm expenses.

The Need for Microloans

In a national survey of young and beginning farmers, capital was cited as the number one barrier to farming. Loan requests by young farmers fall into the same pool as all other FSA borrowers, including well-established, larger, and higher-grossing operations. Within FSA's Direct Operating Loans portfolio, young, beginning and small farmers compete for a limited pool of annual appropriations, and are currently required to abide by the same rules and complete the same application process as applicants that are applying for much larger loans, up to the DOL loan limit of $300,000. However, for many young farmers, all the capital they may need is a much smaller amount and may need the loan on a fast turnaround time, with no other financial resources to fall back on, aside from high-interest credit cards and limited assets. While technically FSA can make smaller loans, busy field agents are often unwilling or less responsive to these loan requests, as they are more accustomed to working with larger requests.

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FSA's proposed microloan program will make affordable capital more easily accessible to farmers of all ages, and is especially suited to meet the credit needs of young, beginning, and diversified farmers who grow a variety of crops on a small-scale and who primarily serve local and regional markets.

The farmers that make up this segment of potential borrowers are distinct from traditional borrowers that FSA has historically lent to, and likely many local FSA loan officers may therefore be less familiar with the unique challenges and specific needs of smaller, high-value, diversified production systems. It is absolutely critical that FSA becomes more capable over time of enhancing current levels of outreach to these traditionally underserved markets, and are able to offer appropriate financial products and services that are tailored to this distinct borrower pool, including smaller loans made under the proposed microloan program when these alternative enterprises are just getting started.

Recommendations

NSAC supports FSA's efforts to better serve the needs of non-traditional borrowers, including small and beginning farmers and those growing for local markets, and would ask that in implementing the proposed microloan program that you consider the following recommendations.

1. Provide training and resources to local FSA field offices to ensure loan officers have the expertise needed to make loans to non-traditional borrowers.

Loan officers who are usually accustomed to making larger loans for more traditional borrowers, may be less familiar with less conventional operations, including small, diversified operations selling through direct or alternative marketing channels or using sustainable, organic, or other less conventional production practices. As such, they may find it difficult to assess the financial risks, projected yields and profitability of these types of smaller, more diversified operations when reviewing a prospective microloan application.

Providing formal training to local FSA loan officers is one potential option FSA should consider in order to address this knowledge gap. Other resources should also be available and accessible to FSA field offices from both state FSA offices and agricultural organizations that are familiar with these types of operations. Loan officers should be encouraged to request assistance from state offices and other local agricultural resources when necessary to have appropriate information and knowledge base to respond when approached by small and diversified producers and be able to sufficiently process their microloan applications. Examples of organizations that could serve as a resource to ensure accurate and reliable profit calculations could include regional distributors, organic marketing companies, and sustainable agriculture farm organizations. Similarly, FSA field offices with greater experience with making these types of loans could help FSA field offices with less experience. Not only does this help FSA field offices make smaller loans, but will also help them with larger loans as these farmers graduate or as other farmers at larger scales seek financing.

Also, to the extent practicable, USDA should encourage local loan officers to work with other organizations to help "broker" these capital flows – such as the Carrot Project in Massachusetts or California FarmLink – who are already engaged in intermediary microlending programs for farmers. We strongly support the pending House farm bill provision encouraging the further use of intermediaries with respect to microloans (more on that below in point #11).

2. Build in evaluation for this new loan program in order to assess borrower participation and the extent to which this program is sufficiently meeting their credit needs.

In order to ensure that this new loan program is adequately meeting the needs of the intended borrowers (as identified in the preamble to the Proposed Rule), FSA should track and publish information on the use of this program on an annual basis. This could prove especially useful in understanding how the new loan program is being implemented at the local level, and whether there are specific states or regions of the country that are facing barriers in effectively implementing this program and offering microloans to their borrowers. Information that could be collected by FSA which might aid program analysis and evaluation includes type of operation, gross sales or revenue, direct or local market sales, number of years farming, total farm acreage, and geographic classification (i.e. rural, urban, suburban), in addition to a more thorough state-by-state analysis of how many microloans are processed, how many applications are received, how much funding is obligated under this new program, how many loan officers are trained in making microloans, etc. This analysis and evaluation activity will provide valuable information and statistics on who is using and benefitting from this program to inform future implementation of the program to better meet borrower needs.

3. Ensure the microloan application is available online.

Many young, beginning and small farmers are accustomed to receiving and processing information online. Posting the microloan application online would greatly reduce the number of trips a farmer has to make off their farm to their local FSA office. Additionally, microloan applicants should be able to submit the initial loan application online, and ideally, be able to check on the status of their application as well. By making these materials available electronically, this would not only reduce paperwork and minimize administrative expenses within FSA, but also allow loan officers to sufficiently review each loan application prior to meeting in person to approve the loan, and inform the applicant if there are any additional materials that might be required. If additional information is required, this supplemental information should also be able to be submitted electronically.

The online application should be easy to find from FSA's main home page, and any background materials or application instructions should be displayed in a user-friendly manner in plain language that is easy to comprehend by someone who has likely never applied for a loan before. FSA should consult with organizations currently involved in microlending to provide feedback on the online format to ensure it is easily accessible for the intended borrowers. Having these application materials and program information online and easily accessible to potential applicants will also aid in outreach efforts, and allow agricultural and community-based organizations that work directly with farmers to easily link to and refer farmers to FSA's online microloan application.

4. Require mentor signature on loan applications to prevent fraud and abuse of program.

While we agree that the loan application process should not be unnecessarily time-consuming or burdensome in the documentation required, there should be some degree of documentation that is required to ensure that the loan applicant is indeed involved in an apprenticeship or mentorship program (see more about this in point #6 below). We recommend that FSA require the signature or the mentor or apprenticeship supervisor on the narrative materials submitted by the applicant documenting their experience. We do not feel that this is overly burdensome, and would be fairly easy for the applicant to maintain, especially in the case of a mentorship or apprenticeship in which the applicant is in frequent contact and communications with their mentor or supervisor. However, at the same time, loan officers should be given some flexibility in determining what documentation is required if a loan applicant is unable to obtain a signature in a timely fashion in order to prevent delays in processing their loan.

5. Establish a process to allow new farm businesses to use this program.

Under the Proposed Rule, an applicant must include all financial and production records for the most recent production cycle as part of their microloan application. There should be some standardized process that is in place to allow applicants with no yield history to make use of this program, and to ensure this program supports the growth of new farm businesses as well as help established farmers continue or expand their operations. This is especially important for applicants who qualify for the farm experience requirement by serving as an apprentice on someone else's farm and where past yields of the apprenticeship farm may not accurately reflect projected yields for their own operation. This process should be clarified and explained in the Final Rule, and communicated to local field offices to ensure new farmers are not wrongly turned away from this program.

6. Modify eligibility requirements to require one full season of farm production experience and clarify expanded managerial experience requirement.

While we praise FSA's efforts to include added flexibility to microloan eligibility requirements, we would request more clarity in what is considered an "agriculture-related organization" as mentioned in the new requirement "(1) a past association with an agriculture- related organization, such as 4-H Club or Future Farmers of America (FFA), that demonstrates experience in a related enterprise." We do have some hesitations that a past association by itself, without any prior actual on-farm experience or education, may not sufficiently allow FSA loan officers to assess the managerial capabilities for an individual who wishes to apply for a microloan to start their own farm enterprise.

In discussing loan eligibility requirements with several of our member groups who work directly with young and beginning farmers in the field, our consensus recommendation is that microloan applicants should be required to either show at least one full-season of on-farm experience in order to qualify for a microloan or qualify through existing eligibility criteria which includes education or training as well as experience.

The Proposed Rule includes the following added eligibility requirement for microloans (emphasis added):

> (ii) A written description of a *self directed apprenticeship* for the *first operating cycle*. The applicant will agree as a condition of the loan to seek, receive, and apply guidance, during the first production cycle of production and marketing typical to the applicant's specific operation, with an individual who is knowledgeable of production and marketing practices that are pertinent to the applicant's operation and will provide a developmental partnership to share knowledge, skills, information, and perspective of agriculture to foster professional growth. The intent of this apprenticeship is to provide the applicant with the skills and knowledge necessary to manage their operation on their own. They may continue the apprenticeship beyond the first operating cycle, but they are not required to do so.

Apprentices generally do not participate in on-farm operations of an apprenticeship at the same time as running their own farm business. What is described in (ii) seems to more accurately reflect a mentorship relationship, rather than what is typically considered an apprenticeship – which usually involves an exchange of supervised farm labor for room and board, generally some sort of stipend or compensation, and informal, intensive training and experience in farming. The definition provided in the Proposed Rule for an "apprentice" also more accurately describes a mentorship relationship, rather than an apprenticeship.

We therefore recommend that (ii) be clarified in the Final Rule to more accurately reflect the mentorship relationship it describes and be modified to require a full season of on-farm experience (either through an apprenticeship or under the guidance of a mentorship) in order to be eligible to apply for a microloan. We would propose you amend the rule as follows:

> § 761.2 Abbreviations and definitions.
> ~~Apprentice~~ **Mentorship** means **an established, formal relationship between** an individual who receives applied guidance and input from another individual with the skills and knowledge pertinent to the successful operation of the farm enterprise being financed.
>
> § 764.101 General eligibility requirements.
>
> (4) <u>Alternatives for ML</u>. ML applicants also may demonstrate managerial ability by one of the following:
> …
>
> (ii) A written description of a self directed ~~apprenticeship~~ **mentorship** for the first operating cycle**, provided the applicant has at least one full season of farm experience, such as through an apprenticeship program**. The applicant will agree as a condition of the loan to seek, receive, and apply guidance, during the first production cycle of production and marketing typical to the applicant's specific operation, with an individual who is knowledgeable of production and marketing practices that are pertinent to the applicant's operation and will provide a developmental partnership to share knowledge, skills, information, and perspective of agriculture to foster professional growth. The intent of this ~~apprenticeship~~ **mentorship** is to provide the applicant with the skills and knowledge necessary to manage their operation on their own. They may continue the ~~apprenticeship~~ **mentorship** beyond the first operating cycle, but they are not required to do so.

7. Make special note that farm cooperatives and coop members are eligible to apply for microloans.

Farm cooperatives are eligible for direct operating loans provided the majority owners meet the eligibility criteria, and hence would also be eligible for microloans. There are nearly 3,000 farmer cooperatives in the country, including production and marketing cooperatives that produce, handle, process, and market agricultural products grown collectively by farmer members. Under the Agricultural Marketing Agreement Act of 1937, farmer-owned cooperatives are specifically defined as farmers or producers. This recommendation would serve to both encourage cooperative activity and to benefit farmers.

Specifically in direct-marketing channels, farm co-ops are especially useful to small farmers who wish to grow for local and regional markets, but want to take advantaged of pooling resources and reducing costs by marketing their products with other farmers. Alternatively, small farmers may want to form cooperatives for the shared purchases of inputs or services. In some cases, these businesses are new farm businesses made up of young, beginning, and small farmers and those selling to direct and regional markets, and many of their members or potential members and even in some limited cases the co-op itself, could serve to benefit from small loans which can be used to purchase shared inputs or services or to collectively invest in distribution and marketing functions that can give farmers more power in the market place and reduce the risks of production and sales of their products. FSA should encourage cooperative activity and development at a small scale through the implementation of its new microloan program. It would be helpful in the preamble to the Final Rule to discuss this issue and clarify that coops and coop members are eligible and perhaps provide examples of ways in which microloans might be relevant to farm coops.

8. Allow a co-signer on the security requirement.

We support the proposed modifications to the security requirements that require only 100 percent collateral for the proposed microloan application process, versus 150 percent for other direct operating loans. We agree that this is a more reasonable amount to require a new borrower to put up in collateral, and particularly benefits young and beginning farmers who typically have fewer assets to use towards loan security requirements.

In order to better serve these new borrowers, especially young farmers, we recommend that FSA modify the rule to allow a co-signer on the security requirement, in the event that a young farmer who is just getting started in agriculture does not have access to sufficient capital or assets to meet the 100 percent security requirement. This would ensure that new farmers have the greatest flexibility when applying for their first loan to start their new farm business.

9. FSA should require that technical assistance is available for all microloan borrowers.

Technical assistance is absolutely critical for new farmers and first-time borrowers. The background section of the Proposed Rule states that this new loan program was designed to not only meet the needs of small farmers with smaller credit needs, but also of borrowers transitioning from youth loans to larger direct operating and ownership loans. The Proposed Rule also states that (emphasis added):

> "While the ML requirements will reduce the burden on loan applicants, it will not reduce the level of counseling and supervision provided by FSA. In fact, the reduced documentation will allow FSA personnel to *devote more time to loan analysis and to provide technical assistance to borrowers*."

We recommend that FSA not only encourage local loan officers to provide technical assistance and hands-on loan servicing to microloan borrowers, but that they are actually required to do so. This will result in better financial and credit management skills on behalf of the farmers applying and repaying these loans, and will reduce the probability for defaulting on these small loans. In addition to technical assistance and credit counseling, financial management and borrower training is of the utmost importance in ensuring the success of new borrowers (more on this topic in point #10 below).

10. Coordinate borrower training loan requirement with financial training programs funded through the Beginning Farmer and Rancher Development Program.

All FSA borrowers, including microloan borrowers, are required to participate in a qualified production and financial management borrower training program as a condition of their eligibility for all new direct and guaranteed loans. FSA should, to the greatest extent possible, coordinate this borrower training requirement with financial management training programs funded through the Beginning Farmer and Rancher Development Program (BFRDP). BFRDP is a competitive grants program administered by NIFA which provides grants to institutions and organizations that provide education, training and development programs for new farmers – including business management and financial management training, strategies that enhance financial viability of beginning farmers and ranchers, and tax and risk management education. Beginning farmers and new producers who have already participated in one of these financial management training courses funded through BFRDP at the time they apply for a microloan should not be required to take on the added time and expenses to complete a similar borrower training program if the BFRDP course can be recognized by FSA as meeting this requirement.

Instead, there should be a process in place, and increased coordination between FSA and NIFA, to ensure that BFRDP funded projects that include a primary focus on financial management are able to meet FSA's borrower training loan requirement. In fact, increased coordination between the two agencies and specifically between the microloan program and BFRDP – both of which are targeted to new producers – would serve to benefit both programs. FSA microloan officers should be knowledgeable about new farmer training programs (including those funded through BFRDP) in their area, and be able to provide information to and refer potential microloan borrowers to these new farmer resources.

11. Allow microloans to be made within FSA's guaranteed operating loan portfolio by establishing an intermediary relending program.

Both direct and guaranteed loans have funding limits set annually by Congress, and typically direct loan funds are exhausted more quickly than guaranteed funds. We therefore recommend that microloans also be made available within FSA's guaranteed loan portfolio. This would ensure farmers have more timely access and greater flexibility when seeking capital. While we recognize the statutory limits on what activities FSA is authorized to undertake, we fully support the creation of an intermediary relending program that would facilitate FSA's efforts to make small loans available to first-time borrowers and small farmers.

There is currently a provision included in the House Farm Bill (H.R.6083) that would allow FSA to establish a cooperative lending pilot project within the new microloan program, and we encourage FSA to implement this provision expediently if it does become law to allow non-profit organizations, banks, foundations, and other investors who are already involved in microlending to actively participate in FSA's new microloan program and contribute to its successful implementation. Among other things, FSA should consider contracting with these intermediary lenders to not only make and service loans to borrowers, but also to support technical assistance and to provide business, financial, marketing, and credit management services to borrowers.

Additional Considerations

We feel that the maximum loan limit of $35,000 is a reasonable loan limit to place on this new category. However, with the proposed elimination of the simplified Lo-Doc application process for all loans made under $50,000, we have concerns that borrowers that fall in between these two loan thresholds will now face more rigorous application requirements as a result. This issue should be addressed in the Final Rule.

Finally, although the Proposed Rule does not specifically mention limited resource farmers and ranchers, we would assume that the reduced interest rate for these borrowers within FSA's Direct Operating Loan program would also apply to limited resource farmers applying for a microloan. Similarly, we would also assume that the target participation rates for beginning and socially disadvantaged farmers and ranchers would also apply to the new microloan program, although we would request further clarification in the Final Rule to explain how this target rate would be met (i.e. would the target participation rate be applied to both the direct operating loan portfolio as a whole, and also for the microloan loan category, or just to the former?). Both of these issues should be clarified in the Final Rule.

In closing, NSAC fully supports this Proposed Rule, and encourages the swift implementation of FSA's new microloan program. Obviously, ensuring that sufficient outreach is conducted to potential borrowers will be critical in the success of this new program, and in launching this new program option, FSA should create targeted marketing for those potential borrowers who may not be familiar with FSA credit programs, including the young beginning farmer community. NSAC looks forward to working with FSA in this capacity to facilitate the process of getting the word out to the farm community. We are hopeful that this new loan program will improve access to credit for non-traditional borrowers and expand agricultural opportunities for a growing number of young, beginning, and small farmers and ranchers, as well as those growing food for local and regional markets, as well as other traditionally underserved markets.

Thank you for considering our viewpoint and positions on the Proposed Rule. We would be happy to provide additional assistance as requested on this program.

Sincerely,

Ferd Hoefner
Policy Director

Juli Obudzinski
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