ICBA
INDEPENDENT COMMUNITY
BANKERS of AMERICA

Formulation of the 2012 Farm Bill: Credit Programs

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Independent Community Bankers of America

House Agriculture Committee
Subcommittee on Department Operations,
Oversight and Credit

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Formulation of the 2012 Farm Bill: Credit Programs

Introduction

Mr. Chairman and members of the subcommittee, thank you very much for the opportunity to testify today on a topic of great interest to this committee, our nation's farmers and ranchers, and the thousands of community banks that serve rural America.

My name is Jeff Gerhart. I am Chairman of the Bank of Newman Grove, Newman Grove, Nebraska. I am testifying today as the Chairman of the Independent Community Bankers of America and I have previously been a member of ICBA's[1] Agriculture-Rural America committee. I am pleased to present ICBA's views and recommendations on credit programs for development of the 2012 Farm Bill.

Bank of Newman Grove, Nebraska

My hometown of Newman Grove, Nebraska is nestled in the rolling hills of southwest Madison County roughly 120 miles north and west of Omaha or Lincoln. The Bank of Newman Grove was established in 1891and continues to provide our agricultural community with banking services that are needed to be a successful farmer in today's agricultural environment.

The Bank of Newman Grove makes farmland loans, machinery loans, crop loans, irrigation pivot loans, livestock loans – whatever the farmer needs to run a successful operation – we have the expertise to make sure our customers are equipped to operate modern day agricultural operations.

We provide our customers with a good financial analysis of their farming operation in order to help them make good decisions to be successful. Our farmers raise corn and soybeans as well as hogs and cattle. Most of our customers are families that have banked with us for several generations. In fact, we have a fifth generation farm customer who has two daughters – making them the sixth generation doing business with us. Community banking for the next generation is important for our farming community and for our country.

In addition to our farmers we also serve many local businesses along our busy Main Street – from the City Café, Barnes Mini Mart, Mid Nebraska Lutheran Home (skilled care and assisted living), a dental office and a medical clinic to name just a few.

We also reopened our local steak house "The Hombre" with about 80 local residents who raised $100,000. The "Hombre" is so busy on the weekends you would be smart to make a reservation before you arrive. That's a nice problem to have.

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[1] **About ICBA**
The Independent Community Bankers of America®, the nation's voice for more than 7,000 community banks of all sizes and charter types, is dedicated exclusively to representing the interests of the community banking industry and its membership through effective advocacy, best- in-class education and high-quality products and services. For more information, visit www.icba.org.

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As I speak, the Bank of Newman Grove is talking with a local couple that is interested in buying our local weekly newspaper that has been in business for over 100 years. These are examples of just a few ways that our bank and community banks in general seek to keep our family farmers passing that farm onto the next generation and in turn keep our rural communities vibrant.

Community Banks Role in the Rural Economy

Community banks continue to play an important role in the nation's economy. There are approximately 7,400 community banks in the U.S. and the vast majority of these are located in communities of 50,000 or fewer residents. Thousands of community banks are in small, rural, and even remote communities.

Community banks have only a little more than 10 percent of all bank assets but make almost 40 percent of all small business loans. This is important since small businesses represent an astounding 99 percent of all employer firms and employ one-half of the private sector workforces. In addition, the more than 26 million small businesses in the U.S. have created 70 percent of the net new jobs over the past decade. Small businesses are important in rural America since many farmers and/or their spouses have off-farm jobs. As small businesses ourselves, Community banks specialize in small business relationship lending. When our customers do well, community banks do well.

Community banks under $500 million in assets extend over 50 percent of all agricultural credit from the banking sector. In addition, commercial banks under $1 billion in asset size extend approximately 56 percent of non-real estate loans to the farm sector and 62 percent of the real estate credit. **Attachment B** of our testimony provides two charts which reflect community bank agricultural lending.

Farm Bill Needed Despite a Healthy Farm Economy

We have experienced a period of historically high prices and farm income levels in U.S. agriculture. According to USDA's February 2012 projections:

- Net farm income is forecast to be $91.7 billion in 2012, down $6.3 billion (6.5 percent) from the 2011 forecast.
- Net cash income is forecast to be $96.3 billion in 2012, down $12.5 billion (11.5 percent) from the 2011 forecast.
- Even so, it would remain $15.9 billion above the 10-year average (2002-2011) of $80.3 billion.
- Crop receipts are expected to experience a slight increase in 2012. A marginal decline is anticipated for 2012 U.S. livestock sales.

Net farm income measures wealth, while net cash income is a measure of solvency, or the ability to pay bills and make payments on debt. Along with income we also keep a close eye on the

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expense side of the equation. Higher commodity prices have led to higher input costs, which have led to a higher level of production expenses for farmers.

After surpassing the $300 billion figure for the first time in 2011, total production expenses are forecast to increase $12.5 billion in 2012 to $333.8 billion. While not as large as the increase in 2011, this forecast is the second consecutive increase of over $10 billion. In six of the last eight years, the increase in expenses has been double-digit. As in 2011, the 2012 figure will set both nominal and inflation-adjusted records[2].

Some members of the media, Congress and the general public have been asking why a new farm bill is even necessary in an era of ongoing higher prices and record farm income levels. Those of us who have been involved in agriculture and lending to agriculture for many decades know that change is the only constant in farming. Booms are often followed by busts and the euphoria of high prices can be met head-on by the nerve wracking challenges of extremely low prices.

Let me offer a word of caution when looking at income and expense numbers. They do not always move together. The farmer does not always make a profit when a crop is planted, harvested and sold or when livestock is sold. Farmers don't directly set their own prices. There are no guarantees.

The cyclical nature of agriculture and the uncontrollable risks of severe adverse weather combined with unknown commodity prices and costs of production require a continued safety net for farmers and ranchers.

A strong farm program also supports lenders in their decisions to extend loans to the farm community with some assurance that the loans will be repaid. A strong farm program helps to support our local communities – rural and non-rural. From Newman Grove to Omaha and similarly from small towns to larger cities across America, our success depends upon a strong agricultural industry.

Importance of Crop Insurance

Before commenting specifically on the credit title, I would stress the importance of the crop insurance program to the farm bill from a lender's perspective and as a crop insurance agent in my community. On the main street of Newman Grove, there are three competitive insurance agencies that provide our farmers with quality insurance products.

Crop insurance is important to the adequate supply of credit to farmers and ranchers as it provides assurance that farmers will be able to repay their operating loans in the event of weather related or price related calamities. Crop insurance is a good risk management tool that our farm customers have learned to use to better manage the risk that exists in farming today.
The dramatic evolution of crop insurance in meeting the needs of most of our nation's farmers has been truly impressive. The use of crop insurance by U.S. farmers has grown sharply, from

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[2] 2012 Farm Sector Income Forecast, Revised Feb. 13, 2012, www.ers.usda.gov/Briefing/FarmIncome/nationalestimates.htm

45 million insured acres in 1981 to 262 million in 2011. The amount of insured liability rose from $6 billion in 1981 to more than $113 billion in 2011[3].

Estimates are that crop insurance will have paid out over $11 billion to farmers and ranchers for 2011, a record level of indemnity payments. The fact that there were not calls for a multi-billion dollar emergency disaster bill during the past year is significant.

Texas, Oklahoma, Kansas and other states experienced the worst drought in their history and we really don't know what this year will bring. But, crop insurance is a testimony to the risk management needs of the farmers and ranchers. Crop insurance is a risk management tool that works and has provided stability to our agricultural economy.

ICBA urges Congress to maintain existing levels of funding for crop and revenue insurance programs, particularly if they are to be the foundation of the next farm bill.

ICBA Recommendations: Credit Title

Mr. Chairman, ICBA has made detailed recommendations suggesting adjustments that can be made to USDA guaranteed loan programs that could stretch existing dollars further. These recommendations cover USDA's guaranteed farm loan programs and the agency's Business and Industry (B&I) program.

While we believe that additional funds should be added to these programs, at the very least there should be no cuts to these programs. The program multiplies a very minimal amount of federal dollars into billions of dollars of loan volume in rural America.

Our full recommendations are attached as **Attachment A**. A summary of these recommendations follow.

Guaranteed Farm Loan Recommendations:

- **Remove Term Limits on Farm Ownership (FO) Loans.**

  Rationale – Fees have been increased and this program is now self-funding. There is no reason to limit eligibility for this self-funded program. Community banks extend the funds for guaranteed farm loans, not the government. Commodity programs do not have term limits and these programs can have significant budgetary costs.

- **Significantly Increase the Size of Guaranteed Loan Limits**

  Rationale – The costs of farmland and production expenses have risen significantly in recent years. The current loan limit ($1.2 million) has not kept pace with the costs of financing today's farmland values and the program is at risk of becoming largely irrelevant for financing the needs of family farmers.

[3] Crop Insurance and the Future Farm Safety Net, Keith Collins and Harun Bulut, 4th Quarter 2001, *Choices Magazine*

Let me give you an example: This past winter 160 acres of non-irrigated land sold for $8,000 per acre just northwest of Newman Grove. One hundred sixty acres of dry land is now selling for $1.28 million. If the land had irrigation, the price would be higher. A 160 acre farm would not be viable in our area and could not cash flow. Even a farm twice that size would not be profitable in our area. Our farmers average between 750 to 1,000 acres.

Congress should direct USDA to test a pilot project that allows producers to choose to pay higher fees for even larger loan limits above whatever a new and higher loan limit would be set at for all producers. This would help accommodate individual family farmers' needs for operating loans. Real estate loans should also be included in the pilot program.

- **Significantly Increase Guaranteed Loan Volume Caps**

  Rationale – With an increase in loan limits, USDA would need to increase the amount or volume of dollars that are extended to ensure an equal or larger number of FO loans can be made. USDA should be given flexibility to accomplish this since the guaranteed FO program is self-funding.

- **Expand Eligible Borrowers to Meet Planning Needs**

  Rationale – While USDA has flexibility to meet most demand for guaranteed FO loans based on types of entities, eligibility needs to be expanded to allow guaranteed FO loans to borrowers who either own or operate family farms instead of requiring them to both own and operate a family farm.

  Today's farms often have different entities for tax and estate planning purposes, not all of which are owned by both parents and children. Protections need to be in place to ensure these loans do not go to large corporations that form various types of entities while providing flexibility to access both farm real estate and operating loans.

Guaranteed B & I Loans – Modify how the Subsidy Rate is Calculated

- **Disallow Loss Calculations Above Current Loan Limits**

  Rationale – Losses should not be calculated based on loans that USDA no longer guarantees, as such calculations do not reflect the true risks of how the program is operated.

- **Limit Loss Calculations to a Fifteen to Twenty-Year Timeframe**

  Rationale – Many changes have been made since the program's inception in 1974 and loss calculations should reflect a time period that is more representative of how the program has evolved and how it has been managed in recent history.

- **Increase/remove caps on amount of lending in "zero subsidy" categories**

  Rationale – Various categories or types of B&I loans have had no losses (e.g. health care, etc.). Allowing these categories to have significantly more loans and volume than currently allowed would generate higher fee revenues to USDA. The additional revenues could finance more loans in other B&I categories (e.g. manufacturing).

Additional options would include raising the guarantee percentage from 80 percent to 90 percent and lowering the origination fee from 2 percent to 1 percent on small B&I loans – loans up to $5 million or a loan size determined by the Secretary - and reducing paperwork. These changes, however, would require raising fees on the largest loan categories to offset reduced revenues from the lower fees on smaller loans. Congress should ask USDA what changes could be accommodated for smaller B&I loans in this manner while being revenue neutral.

Mr. Chairman, all of these recommendations for USDA guaranteed loan programs would very likely extend currently limited dollars into many more loans and significantly higher guaranteed loan volumes without requiring any new government funding.

We must seek to think creatively and outside of the box when dealing with scarce federal dollars.

The ability of USDA's guaranteed loan programs to multiply the impact of very few federal dollars to such an enormous degree should serve as a model of efficiency for many other government programs.

Farmer Mac

Farmer Mac has proposed legislation to expand their ability to act as a secondary market. This authority would allow Farmer Mac to purchase business loans, operating loans, short term loans and USDA guaranteed loans, and remove limits on the size of loans on acreages of less than 1,000 acres and other changes.

ICBA bankers and staff have discussed these changes with Farmer Mac and will continue discussing these issues in an effort to fully understand and assess these proposals and their potential for enhancing the activities of community banks in rural America.

Are Farmland Prices a Bubble?

There have been suggestions that current farmland prices represent a "bubble" that could burst causing economic harm in rural America much like the housing bubble that burst causing much devastation in the national economy.

Even some federal banking agencies, not wanting to be caught unaware or unprepared, as they may have been with subprime mortgages and the activities of the nation's largest financial institutions, have suggested that the farm economy is in or nearly in a bubble. Ag banks are watching this closely and have conservative underwriting standards in place to protect both their banks and their customers.

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On the other side of this debate, various ag economists and likewise some ag bankers do not believe we are in a farmland bubble at this time. Many suggest farmland values could drop, and perhaps significantly, without causing great harm to the farm economy, although such an outcome is not at all desirable. There are several reasons for this thinking.

First, community banks have been conservative in their farmland lending, basing those decisions on the ability of the land to cash flow at much lower price levels than exist today. In addition, the down payment required is often fairly significant approaching levels of 40 percent or more. Many farmers, due to the current high commodity prices and abundant harvests of recent years, are flush with cash and have made farmland purchases with cash borrowing little if anything. Further, interest rates are at historic lows, making this an excellent time to lock in low-cost, fixed rate financing.

Survey Results of ICBA's Agriculture-Rural America Committee

ICBA conducted a survey of its Agriculture-Rural America committee last summer to determine what the impact would be to the farm economy if commodity prices and farmland values began to fall. ICBA's Agriculture-Rural America committee consists of twenty-five bankers from every geographical region of the U.S. representing most agricultural commodities produced in the United States. I used the results of this survey as the basis for my remarks at the Kansas City Federal Reserve Bank's symposium "*Recognizing Risks in Global Agriculture.*[4]"

Our committee's bankers were asked at what price would corn and soybeans have to fall before farmers started showing signs of stress? The consensus from the various agricultural bankers was that it would stress the farmers' cash flow if the price of corn was between $3.50 and $5 a bushel. Soybeans falling to the price of $8 per bushel would cause problems in most portfolios.

Our bankers were also asked how far farmland values would have to fall before the farmers would face serious challenges. While responses varied depending on crop, location, and other factors, bankers said a decline of 30 percent or more would be significant. Their answers also depended on what land value farmers have on their balance sheets or how much land they've bought recently with credit. Many of our borrowers have conservative land values in their calculations.

I was invited to participate in a panel entitled "*Weathering Unexpected Downturns in Agriculture.*[5]" This panel discussed what degree of downturn it would take to cause financial distress in agriculture and I encourage the committee to review this document to perhaps gain an even broader perspective on views of ag lenders on the rural economy.

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[4] Kansas City Fed symposium: Recognizing Risk in Global Agriculture, www.kansascityfed.org/publications/research/rscp/rscp-2011.cfm

[5] Kansas City Fed: symposium panel: Weathering Unexpected Downturns, pg 43, http://www.kansascityfed.org/publicat/rscp/Session3.pdf

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A few relevant observations:

- Each year our bank stress tests our customers' land values to determine farmers' ability to withstand "shocks" to the farm economy;
- With the infusion of cash from a strong farm economy, farmers have been working to reduce their debt loads;
- Most bankers feel the land values shown on their farmers' financial statements are conservative;
- Most bankers feel their farm customers can handle a modest correction in both commodity prices and farmland values;
- Farmers have been updating their equipment over the past couple years;
- These considerations should serve to help make farmers more efficient during future times of potential stress.

Potential Factors Negatively Influencing Farmland Values

Factors that could come into play that would negatively impact farmland prices would be if the Federal Reserve began to raise interest rates sharply to deal with rising inflation in the general economy. This would particularly affect those borrowers who may be highly leveraged, although the number of these borrowers should hopefully be relatively low.

Also, rising production expenses and falling commodity prices would squeeze the ability of producers to have positive cash flows.

There may be particular problems in store for farmers whose non-bank lenders have conducted their own internal farmland appraisals and raised the appraised values of farmland on loan applications just to justify extending loans to farmers.

The House Agriculture Committee should not allow lenders under their jurisdiction to continue making in-house appraisals on loans above $250,000 but should rather require farmland appraisals to be made by outside, independent appraisers. Community banks use independent appraisers on loans over $250,000 as a prudent and sound underwriting practice.

We should also closely watch what is happening in other countries that are major purchasers of U.S. farm commodities. China has been a big influence on our domestic farm prices. Its economy is slowing and some suggest it could be in for a hard landing economically. The Euro zone countries, a larger cumulative economic base than the U.S. economy, has also witnessed many of its countries slipping into recession, as has the United Kingdom, a member of the European Union but not the Euro zone. European countries purchase 20 percent of overall U.S. exports.

In addition, many of the ten largest global economies outside of the U.S. and Europe, including China, Japan, Russia, Brazil, and India, are already in significant market corrections although their economies are not slowing as significantly as the European countries. If the world's economic problems persist and deepen, the stage could be set for much lower demand for U.S.

farm commodities. Significantly lower demand could lower commodity prices and farmland values. The issues warrant close monitoring and Congressional attention where appropriate.

Comparisons to the 1980s Implosion in Farmland Values

Most ag economists and ag bankers view the current strong farmland values as quite different from the situation that existed in the 1980's farm credit crisis for the reasons stated above.

One question that lenders were asked to be prepared to answer for the symposium mentioned previously was "how would banks respond to smaller profits in agriculture?" I asked a follow up question that I suggest many banks would view as more important: "How would regulators respond to smaller profits in agriculture?"

The regulators are really the tail that wags the dog. The banker's ability to work with his customer is influenced – and heavily at times – by the examiner's position and decisions on the banks farm loan portfolios.

During the 1980s agricultural credit crisis, we were able to restructure debt for farmers when they needed help. The banking examiners at that time were willing to work along with the banker who was working along with the farmer.

The question we ask ourselves is whether a loan will be classified even though it has been re-written to accommodate a more realistic cash flow and repayment plan. If individual loans are classified, those decisions will do the most damage in the quickest timeframe to a bank's farm loan portfolio.

If there are times of stress in the farm economy in the future, it will be essential for the regulatory environment to acknowledge bankers' ability to work through problem loans as was done in the 1980's farm credit crisis so that bankers can see farmers through tough times.

The 1980s agricultural crisis was our bank's toughest time since the Great Depression. It was also the toughest time for our farmers. Together we worked through those challenges. Our bank was fortunate not to lose any farmers through bankruptcy or foreclosure during those years. Many banks were not so fortunate.

I still remember the day that one of the first agricultural banks in Nebraska failed and was closed. Because I knew the family, I looked in the mirror and reminded myself that, if we weren't careful, this could happen to us.
Between bankers and farmers, there were many sleepless nights – and also for the local agribusinesses. In the end, working together, we worked through the challenges surrounding us.

If members of Congress wonder how some banking examiners are treating banks today, simply ask community bankers in your district if bank examiners are being overly harsh or overly accommodative or just right with bank examinations. You'll no doubt get an earful.

Farm Credit System (FCS) Abuses

Although the Farm Credit System is under the authority of the Farm Credit Act (Act), and is therefore not part of the credit title of the Farm Bill, many bankers are complaining about the abuses being facilitated by the FCS and its captive regulator, the Farm Credit Administration (FCA). These abuses include predatory pricing practices and cherry picking of prime customers utilizing their tax and funding advantages as a government sponsored enterprise (GSE). They also include allowing FCS institutions to skirt the legal constraints of the Act through various "pilot programs" to engage in non-farm lending or simply turning a blind eye to instances where System institutions are engaging in activities not authorized by the Act.

ICBA would strongly oppose any farm bill provisions that allow either the FCS or the FCA to further expand the powers of the FCS. ICBA believes that Congress should thoroughly investigate the activities of the FCS and shed light on attempts to circumvent the law and their activities in general. Such investigations would be extremely appropriate at a time when Congress is considering reforming the housing GSE. The FCS is also a GSE that is greatly in need of reform, transparency and accountability. A number of reforms targeting the FCS should be considered.

We respect the committee's desire not to get into a heated debate on this topic as part of this hearing. However, we believe future congressional hearings devoted to this topic are warranted. ICBA would be happy to work with the committee towards this end.

Conclusion

Mr. Chairman and subcommittee members, thank you again for devoting time today to discuss the important topic of agricultural credit and its role in the development of the 2012 Farm Bill. We believe there are a number of ways the committee could adjust USDA authorities under the CONACT and/or through the Farm Bill that would stretch existing dollars further, resulting in more loans and more credit extended without increasing federal budget outlays. The result would be more jobs in rural America and a healthier rural economy. We urge your support for the recommendations made in our testimony.

Thank you. I would be pleased to answer any questions.

Attachment A

Detailed Recommendations for USDA Guaranteed Loan Programs
(Further Explanation of Testimony Recommendations)

Guaranteed Farm Loans – The U.S. Department of Agriculture's (USDA) Farm Service Agency (FSA) has increased user fees in order to essentially make guaranteed farm ownership (FO) program self funding and the operating loan (OL) program much closer to a self-funding level. Therefore, we support the following changes:

- **Remove Term Limits** – ICBA supports removing term limits on guaranteed farm operating loans. Whether a producer needs a guaranteed loan or not is a decision best made between the farmer and his local lender and should not be based on arbitrary timeframes established in Washington. The program is now self-funding due to higher fees. Other farm programs do not have term limits even though they have significant costs in terms of budget outlays.

- It has been estimated that over 4,500 farmers and ranchers nationwide have become ineligible for loan guarantees. An additional 1,500 producers are expected to lose eligibility in 2012 followed by an additional 2,200 operators in 2013. Over 8,200 family farmers and ranchers either have lost or will lose access to FO loans since January 1, 2011.

- **Significantly Increase the Size of Guaranteed Loan Limits** – ICBA would support significantly increasing the size of the current loan limits, now $1.214 million, to accommodate larger-sized family farmers and to meet rising farmland and production expenses. Land values have risen substantially in recent years. For example, farmland values for 2011 escalated 22 percent in the seven-state Seventh Federal Reserve District (Chicago Fed)—the biggest annual increase since 1976. Similarly, cropland values increased 25 percent in 2011 from 2010 levels in the ten-state Kansas City Federal Reserve District.

- In addition, USDA estimated farm production expenses increased by $32.5 billion in 2011, reaching a record of $318 billion. The higher level of production expenses in 2011 represented an increase of over 11 percent from the previous year. Increases in the current loan limit are pegged to the "Prices Paid by Farmers Index" as of the end of August each year. Current projections based on March numbers would increase the loan limit to $1.288 million, a 6% increase.

- The current rate of increase in the loan size of guaranteed farm loan programs does not appear adequate to keep pace with sharp upward spikes in land values or production expenses. This situation, if continued throughout the life of the farm bill, combined with the potential for lower farm income in some years, would exacerbate the potential higher demand for credit as producers seek to keep pace with higher costs.

- Providing USDA the flexibility to raise the loan limit size as necessary would have no budgetary impact on program costs for the FO loan program at this time. However, there may also be ways to increase the size limit for OL loans as discussed below without budgetary costs and for FO loans in a year(s) where there may otherwise be a cost due to a rise in the default rate.

- Since the OL loan program is not totally self-funding, Congress could direct USDA to develop a pilot program to enable individual producers, at their option, to choose a higher loan limit above the regular loan limit for both FO and OL loans if they are willing to pay higher fees, if necessary in a particular year, to offset any additional program costs. This approach could allow some family farmers a choice of a larger loan size to fit their individual farm needs without imposing higher fees on the overall universe of borrowers using the programs. This approach could also be combined with the ability to transfer funds into these programs, if needed, from other FSA farm loan programs with unused or surplus funds.

- Larger loans should target family farmers and the fees should not be unduly burdensome. Additional fees should be a voluntary option to the borrower based on their needs.

- **However, if the loan sizes were increased to better reflect rising production costs and farmland values, USDA would also need a simultaneous increase in the volume of loans they can guarantee.** This is necessary to keep pace with the demand for the same number of loans as currently provided. Therefore, ICBA recommends a significant increase in the volume caps for USDA guaranteed loans (see below).

- **Significantly Increase Guaranteed Loan Volume Caps** – Congress should stipulate that USDA's guaranteed loan programs that are self-funding should either not have volume caps or USDA should have flexibility to raise them significantly above current levels. This will ensure greater credit availability in rural America without unnecessary limitations. Since the guaranteed farm ownership program is now self-funding in terms of program costs, it provides no budget savings to cap the loan volume for this program. In fact, the program may make money in some years. Last year the FSA farm ownership program guaranteed almost $2 billion in loans. With this change, a higher volume could be achieved to satisfy loan demand without having to transfer funds from other programs.

- **Expanding Eligible Borrowers to Meet Planning Needs** – We urge the committee to expand who is eligible for guaranteed FO (<u>ownership /real estate</u>) loans from the FSA while ensuring such loans continue to go to family farmers. Currently, a borrower must be <u>both the owner and operator</u> of the family farm to be eligible for guaranteed FO loans. This requirement does not reflect the evolving structures of how some family farms are managed today for tax planning, inheritance, asset transfers and other managerial purposes.

- For example, the real estate of the family farm may be owned in a trust by the parent(s), while the equipment and other farm assets may be owned in a limited liability company (LLC) with the children. This family farm would be ineligible for a real estate loan even if the children were totally responsible for operating the family farm and would one day receive

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the assets of the farm – simply because the children do not currently both own and operate the farm.

- This situation also can cause a problem when a child or children want to purchase the farm from a parent but are unable to qualify for a farm ownership loan even though they have been operating the farm and will continue to do so. By contrast, individuals are eligible for guaranteed farm operating loans if they are either owners or operators of a family farm.

- Eligibility should be expanded to allow instances where operating entities of family sized farms may receive a real estate loan when the real estate is owned by family members who are directly or indirectly members of the operating entity. Protections should ensure that large corporations which own various farm entities do not hide behind vaguely worded family farm, ownership or control definitions.

Guaranteed Business and Industry (B & I) Loans – The OMB's subsidy rate calculations appear to over inflate the costs of administering USDA's B & I loan program which reduces the loan volume available for lenders and their customers. For example, OMB calculates the subsidy rate for B&I loans based on failed loans no longer made (i.e. 1980's ethanol loans of $50 to $100 million) and in size increments no longer permitted. OMB also calculates losses over the entire history of the B & I program dating back to 1974 even though USDA has significantly altered programs during that time to minimize risks. For example, USDA now limits its ethanol loan guarantees for the B&I program to $10 million.

In addition, several loan categories within the B&I program have never had defaults or losses and they therefore amount to "zero-subsidy" loan programs. If USDA were provided flexibility under the CONACT to raise or remove volume caps on these zero-subsidy categories of loan programs, more loans could be made in these no-risk categories. This would allow USDA to apply fees towards other important economic sectors or loan types resulting in an overall increase of guaranteed loan volume without any costs to the federal government. This would also increase the number of jobs provided in rural America.

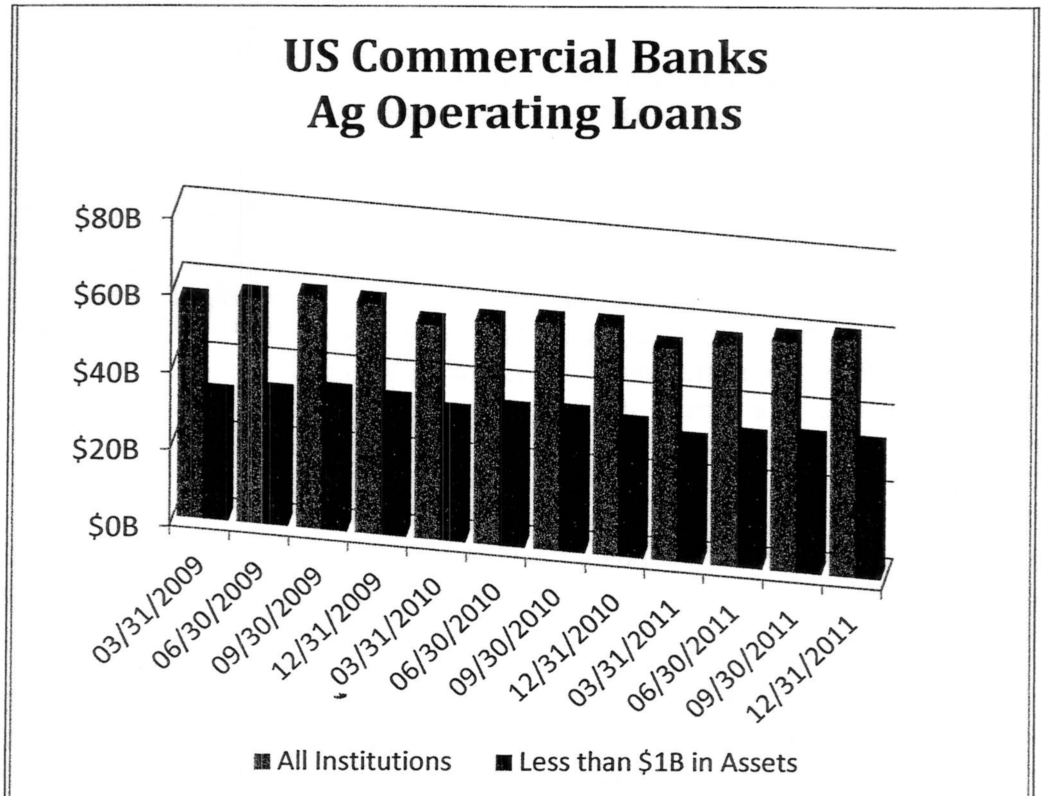
Therefore, our recommendations would be as follows:

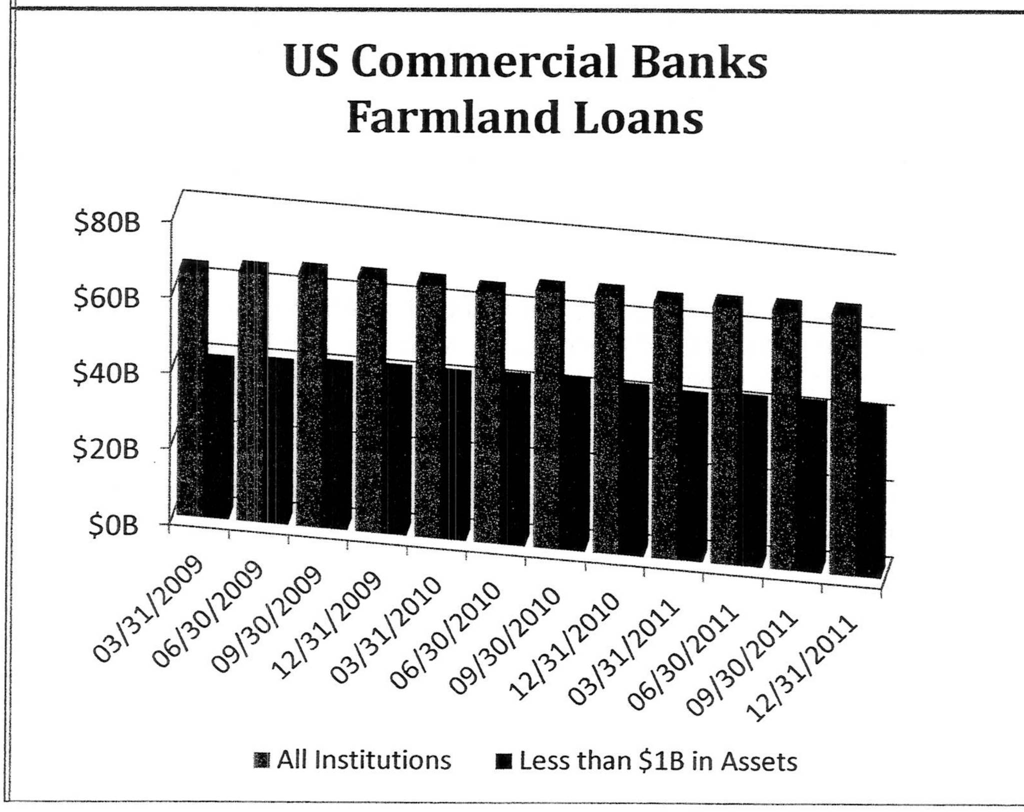
- Amend the CONACT to mandate the B & I subsidy rate calculation not include loans with size limits above those currently being made by USDA (to address the old ethanol loan issues);

- Require subsidy calculations be based on loans and loan types extended no longer than two decades ago. A fifteen to twenty year timeframe would be more relevant to USDA's current activities and would reflect adjustments that USDA has made to minimize risks;

- Provide USDA flexibility to increase or remove volume caps for "zero-subsidy" loan categories within the B&I program with a track record of having no defaults or loan losses. This change will increase fee revenue to USDA and allow for new loans in other categories, thus increasing the amount of lending made in rural America through the B&I program.

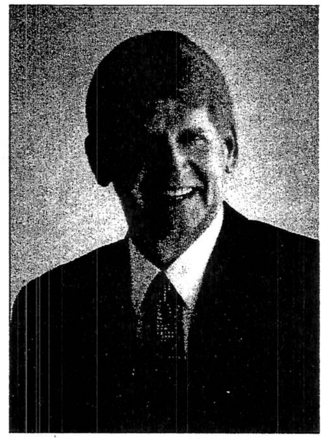
Attachment B





Jeffrey Gerhart

Chairman



Jeffrey L. Gerhart is chairman of the Independent Community Bankers of America (ICBA), the only national trade association that exclusively represents community banks.

Chairman of the Bank of Newman Grove, Neb., and a fourth-generation banker, Gerhart has served ICBA and the community banking industry for many years. He is a member of the ICBA Executive Committee and chairman of the Strategic Planning Committee. He has served as a member of a variety of ICBA committees, including Education, Congressional Affairs, Payments and Technology, Regulatory Review and Strategic Planning, and as chairman of the Policy Development Committee.

He has also served as chairman and board member for the Nebraska Independent Community Bankers. From 1999 to 2004, he was a Class A board member of the Federal Reserve Bank of Kansas City.

Gerhart is president and owner of Gerhart Insurance Agency in Newman Grove. He is president and manager of Marbu Inc., a family-farming operation. He is a member and past officer of the Newman Grove Community Club, treasurer of the Newman Grove Medical Clinic, co-chairman of the Newman Grove Community Foundation, and a member of the Vision/Newman Grove economic group, the Newman Grove United Methodist Church and the Newman Grove Masonic Lodge #305.

Gerhart attended the University of Kansas from 1971 to 1973 and received his bachelor's degree in business from the University of Nebraska in 1975. He is a graduate of the Colorado Graduate School of Banking.

Both community banking and ICBA service are a family tradition. Gerhart's parents, H.L. "Bud" Gerhart Jr. (bank director) and Georgianne, were active in ICBA for many years, with Bud serving a term as ICBA president in 1972. Three generations of Gerharts serve as directors of First Newman Grove Bankshares and the Bank of Newman Grove.

He lives in Newman Grove, Neb., with his wife, Becky; they have two adult children, son Patrick and daughter Kyle.

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Committee on Agriculture
U.S. House of Representatives
Information Required From Nongovernmental Witnesses

House rules require nongovernmental witnesses to provide their resume or biographical sketch prior to testifying. If you do not have a resume or biographical sketch available, please complete this form.

1. Name: Jeffrey L Gerhart

2. Organization you represent: Independent Community Bankers of America

3. Please list any occupational, employment, or work-related experience you have which add to your qualification to provide testimony before the Committee:
   Community banker
   Insurance Agent/Owner
   Farm manager

4. Please list any special training, education, or professional experience you have which add to your qualifications to provide testimony before the Committee:
   35 years as a community banker, insurance agent, farm manager

5. If you are appearing on behalf of an organization, please list the capacity in which you are representing that organization, including any offices or elected positions you hold: ICBA Chairman

PLEASE ATTACH THIS FORM OR YOUR BIOGRAPHY TO EACH COPY OF TESTIMONY.

Committee on Agriculture
U.S. House of Representatives
Required Witness Disclosure Form

House Rules* require nongovernmental witnesses to disclose the amount and source of Federal grants received since October 1, 2009.

Name: ______________________________

Organization you represent (if any): ______________________________

____

1. **Please list any federal grants or contracts (including subgrants and subcontracts) you have received since October 1, 2009, as well as the source and the amount of each grant or contract. House Rules do NOT require disclosure of federal payments to individuals, such as Social Security or Medicare benefits, farm program payments, or assistance to agricultural producers:**

Source: ______________________ **Amount:** ____________

Source: ______________________ **Amount:** ____________

2. **If you are appearing on behalf of an organization, please list any federal grants or contracts (including subgrants and subcontracts) the organization has received since October 1, 2009, as well as the source and the amount of each grant or contract:**

Source: ______________________ **Amount:** ____________

Source: ______________________ **Amount:** ____________

Please check here if this form is NOT applicable to you: X

Signature: ______________________

* Rule XI, clause 2(g)(5) of the U.S. House of Representatives provides: *Each committee shall, to the greatest extent practicable, require witnesses who appear before it to submit in advance written statements of proposed testimony and to limit their initial presentations to the committee to brief summaries thereof. In the case of a witness appearing in a nongovernmental capacity, a written statement of proposed testimony shall include a curriculum vitae and a disclosure of the amount and source (by agency and program) of each Federal grant (or subgrant thereof) or contract (or subcontract thereof) received during the current fiscal year or either of the two previous fiscal years by the witness or by any entity represented by the witness.*

PLEASE ATTACH DISCLOSURE FORM TO EACH COPY OF TESTIMONY.