

The Government Changes the Rules Mid-Game

An Explanation of the Credit Provisions of the FAIR Act

Part Two — Preservation Loan Servicing Program and Inventory Property Changes

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Part Two of this series of articles on the Credit Title of the Federal Agricultural Improvement and Reform Act (the FAIR Act) discusses amendments to the Farm Service Agency's (FSA) preservation loan servicing programs and handling of inventory lands.

I. Preservation Loan Servicing—Farmland Leaseback/Buyback Program

The FAIR Act made significant changes to the FSA preservation loan servicing programs.

A. Elimination of the Farmland Leaseback/Buyback Program

The FAIR Act eliminates the farmland leaseback/buyback program.¹

1. What is the Farmland Leaseback/Buyback Program?

The farmland leaseback/buyback program was first authorized in 1985. It is one of two preservation loan servicing programs.² It offered farmers who had lost their farmland to FSA through foreclosure, bankruptcy, or voluntary conveyance a chance to reacquire that land. The farmer could reacquire the land through an immediate purchase or could enter a lease that contained an option to purchase the land during the lease period.³

FSA farmer-borrowers could apply for the farmland leaseback/buyback program at two different times. A farmer could apply before FSA took the land into inventory and/or within 180 days after FSA took the property into inventory.⁴ If the application was made before FSA took title to the property, the farmer would have to agree to convey the land to FSA in exchange for a purchase agreement or a

¹ Federal Agriculture Improvement and Reform Act of 1996, Pub. L. No. 104-127 (Apr. 4, 1996), 110 Stat. 888-119 (Fair Act).

² The other preservation loan servicing program is the homestead protection program discussed below at pages 28-29.

³ See 7 C.F.R. § 1951.911(a) (1996).

⁴ *Id.*

lease with option to purchase. This is referred to as “pre-acquisition” farmland leaseback/buyback. If the farmer applied for the program after FSA had already taken title to the farmland, it would be referred to as an application for “post-acquisition” farmland leaseback/buyback.

2. Will FSA Process Applications Made Before the Law Was Changed?

The FAIR Act eliminates FSA’s authority for the farmland leaseback/buyback program.⁵ However, some applications for the program that had been submitted before the Act became law may still be processed. The amendment eliminating the farmland leaseback/buyback program was included in Section 638 of the FAIR Act. The Act also includes a special transition provision which states that “[t]he amendments made by sections 638 . . . shall not apply with respect to a complete application to acquire inventory property submitted prior to the date of enactment of this Act.”⁶

On April 5, 1996, FSA interpreted this provision to allow continued processing of applications only for those farmers who:

- Had already conveyed property to FSA under a written agreement that the agency would provide leaseback/buyback consideration;
- Had an application for acquisition of inventory property on April 4, 1996, if the application contained all of the information FSA needed to complete the sale; or
- Were exercising the option to purchase the property in accordance with the terms of a lease agreement that was in effect as of April 4, 1996.⁷

FSA had interpreted the Act to prohibit processing of all other “pre-acquisition” and “post-acquisition” applications for leases with options to purchase that were pending on April 4, 1996.⁸

On behalf of the National Family Farm Coalition, FLAG sent a letter to Secretary of Agriculture Dan Glickman asking that he reinterpret the transition provision of the Act. FLAG requested that FSA continue processing all applications for the farmland leaseback/buyback program, including all applications for leases with options to purchase, that farmers had submitted before April 4, 1996.⁹

⁵ FAIR Act, § 638.

⁶ FAIR Act, § 663(c).

⁷ FSA Notice FC-37, pp. 1-2.

⁸ FSA Notice FC-37, p. 2.

⁹ FLAG’s letter to the Secretary explains how he could legally reinterpret the transition provision of the Act to allow processing of all farmland leaseback/buyback applications pending on the date of enactment of the Act. It includes a request that he continue to consider farmers for farmland leaseback/buyback if they submitted a complete application in response to the FSA Notice of Availability of Primary and Preservation Loan Servicing Programs (1951-S notice) but were denied primary loan servicing.

On August 8, 1996, in response to FLAG's letter, FSA changed its policy on processing applications that were submitted before enactment of the FAIR Act.¹⁰ According to this new policy statement, FSA will continue to process all complete applications for pre-acquisition leaseback/buyback that it received before April 4, 1996. A complete application for pre-acquisition leaseback/buyback includes a complete application for primary and preservation loan servicing, commonly known as a 1951-S application.¹¹

By submitting a 1951-S application, a farmer-borrower applies for both primary and preservation loan servicing programs. Farmland leaseback/buyback is a preservation loan servicing program. However, before a farmer is considered for the leaseback/buyback program pursuant to a 1951-S application, there is a lengthy process for consideration of eligibility for the primary loan servicing or debt restructuring programs. Eligibility for preservation loan servicing, including the leaseback/buyback program, is considered only after determining that the borrower is not eligible for any of the primary loan servicing programs. Because of this processing time, a farmer's 1951-S application may have been submitted long before the FAIR Act was passed, even though the farmer had not yet been considered for leaseback/buyback. Under FSA's new policy, these 1951-S applications will continue to be processed through leaseback/buyback consideration, despite the FAIR Act's elimination of the program.

FSA county offices are required to notify all farmers who had submitted complete farmland leaseback/buyback applications before April 4, 1996, of their possible eligibility for the program.¹² Pursuant to FC-37, these farmers had previously been notified that their applications could no longer be processed because the FAIR Act eliminated the leaseback/buyback program. Farmers should have been notified of the reopening of their applications by September 30, 1996.¹³ However, if a farmer has *not* received such a notice *and* had submitted a complete 1951-S application before April 4, 1996, *and* had not yet been considered for pre-acquisition leaseback/buyback, he or she should immediately contact FSA and request consideration for the program.

3. Can Farmers Apply for Farmland Leaseback/Buyback in the Future?

Farmers will not be allowed to apply for the farmland leaseback/buyback program after April 4, 1996, because the FAIR Act eliminated all authority for FSA to grant a preference for sale or lease to the previous owner of the farmland.¹⁴

¹⁰ See FC-66.

¹¹ See "The Government Changes the Rules Mid-Game: An Explanation of the Credit Provisions of the FAIR Act, Part One" at page 16 above for further explanation of the primary loan servicing programs.

¹² See FC-71.

¹³ See FC-71

¹⁴ FAIR Act, § 638.

II. Preservation Loan Servicing—Homestead Protection Program

Unlike the farmland leaseback/buyback program, the FAIR Act did *not* eliminate the authority for the second preservation loan servicing program—the homestead protection program. However, the Act did reduce the time during which farmers may apply for this program after FSA takes the property into inventory.¹⁵

A. What Is the Homestead Protection Program?

The homestead protection program is designed to allow farmers to reacquire their home if FSA takes it into its inventory through voluntary conveyance, foreclosure, or bankruptcy.¹⁶ Under this program, farmers may reacquire their principal residence and up to ten adjoining acres of land. There may be a reasonable number of farm service buildings useful to the farm family on that adjoining land. Farmers may enter into a lease containing an option to purchase or a direct purchase agreement with FSA under the homestead protection program.

FSA farmer-borrowers may apply for the homestead protection program at two different times. A farmer may apply for homestead protection before FSA takes the property into inventory,¹⁷ in which case the farmer would have to agree to convey the homestead property to FSA in exchange for a purchase agreement or a lease with option to purchase. This is referred to as “pre-acquisition” homestead protection. A farmer may also apply for the homestead protection program after FSA takes the homestead property into inventory. This is known as an application for “post-acquisition” homestead protection.

The FAIR Act changes only apply to the time for filing an application for “post-acquisition” homestead protection. The FAIR Act did not change the “pre-acquisition” homestead protection program.

B. What Is the New Time Period for Application?

The FAIR Act requires farmers to apply for the post-acquisition homestead protection program within 30 days of the date the property is taken into FSA inventory.¹⁸ Prior to the FAIR Act, farmers had 90 days from the date FSA took the property into inventory to apply for homestead protection.

C. When Must FSA Notify Farmers of the Homestead Protection Program?

The FAIR Act requires FSA to send a notice of the availability of the post-acquisition homestead protection program to the previous borrower-owner of property containing the borrower’s principal residence by the date on which FSA acquires the property.¹⁹ This notice should advise the farmer that he or she has 30 days from the date FSA acquires the property to apply for the homestead protection program.

¹⁵ FAIR Act, § 644.

¹⁶ 7 U.S.C. § 2000.

¹⁷ 7 C.F.R. § 1951.911(b) (1996).

¹⁸ FAIR Act, § 644.

¹⁹ FAIR Act, § 644.

III. Sale or Lease of FSA Inventory Farmland

A. Elimination of Priorities for the Sale or Lease of FSA Inventory Farmland

The FAIR Act made significant changes to the procedures FSA must use to dispose of farmland in its inventory.

The FAIR Act has also eliminated many of the priorities for sale or lease of FSA inventory farmland. Before the FAIR Act, certain farmers were entitled to priority consideration for purchase or lease of FSA inventory farmland. The previous order of priority for sale or lease was to:

1. The farmer-borrower who owned the farmland before it was taken into FSA - inventory;²⁰
2. The spouse or child of the farmer-borrower who owned the property before it was taken into FSA inventory or a stockholder in the corporation if the previous borrower-owner was a corporation owned exclusively by the members of the same family;
3. The operator of land when it was taken into FSA inventory if this was a different person than the previous owner;
4. Qualified beginning farmers or ranchers;
5. Farmers operating not larger than family-size farms.²¹

Under the FAIR Act amendments, the only farmers who will be given priority consideration for purchases of inventory farmland are qualified beginning farmers and ranchers.

If the land is located within the boundaries of an Indian reservation, there are special priorities rules that apply. See page 8 for further discussion of these priorities.

B. Elimination of Most of FSA's Leasing Authority

The FAIR Act also eliminates much of FSA's authority to lease inventory farmland.²² After April 4, 1996, FSA will only be allowed to lease inventory farmland in the following situations:

1. To a qualified beginning farmer who is eligible for a credit sale, a direct farm ownership loan, or a guaranteed loan to buy the land when funds are not available for these programs;²³
2. Land that is within the boundaries of an Indian reservation and acquired from an Indian tribe or an Indian member of the tribe, if it is leased to

²⁰ This priority lasted for 180 days after the farmland was taken into FSA inventory. *See* 7 U.S.C.A. § 1985(e)(1)(A) (West Supp. 1996).

²¹ 7 U.S.C.A. § 1985(e)(1)(C) (West Supp. 1996).

²² FAIR Act, § 638.

²³ The term of the lease to the qualified beginning farmer will run until the earliest of (1) 18 months, or (2) when the credit sale or loan funds become available. FAIR Act, § 638.

- (a) a member of an Indian tribe with jurisdiction over the reservation within which the property is located, (b) an Indian corporate entity, or (c) the Indian tribe;²⁴ or
3. The primary residence and up to ten adjoining acres of land, including a reasonable number of farm service buildings, to the former FSA farmer-borrower under the homestead protection program.²⁵

C. New Rules for Disposal of FSA Inventory Farmland

Following is an outline of the new procedures for sale of FSA inventory farmland:²⁶

Step One

Within 15 days after taking farmland into inventory, FSA must advertise it for sale.

Step Two

For the first 75 days after taking farmland into inventory, FSA must attempt to sell the property to qualified beginning farmers or ranchers.²⁷

²⁴ FSA Notice FC-37 indicates that FSA does not recognize its continuing authority to lease inventory farmland located within Indian reservation boundaries. FC-37 states that within 90 days of acquisition of such farmland, the property shall be offered *only for sale* according to the stated priorities. This policy statement appears to be contrary to the statutory authority to lease or sell such farmland. The statutory authority to lease or sell existed before the FAIR Act. 7 U.S.C.A. § 1985(e)(1)(G) (West Supp. 1996). The FAIR Act did not amend this explicit authority to lease such farmland located within the boundaries of an Indian reservation. Therefore, there is a good legal argument that FSA retains its authority to lease land obtained from Indian borrowers that is located within an Indian reservation.

²⁵ See 7 U.S.C. § 2000 and 7 C.F.R. § 1951.911(b) (1996).

²⁶ FAIR Act, § 638.

²⁷ A qualified beginning farmer or rancher is one who meets the following criteria:

- (1) Meets the general FSA loan eligibility criteria (see “The Government Changes the Rules Mid-Game: An Explanation of the Credit Provisions of the FAIR Act, Part One” at page 8 above);
- (2) Never has operated a farm or ranch or has operated a farm or ranch for less than ten years;
- (3) Individually or with his or her immediate family materially and substantially participates in the day-to-day operations of the farm or ranch, consistent with the practices in the state or county;
- (4) Agrees to participate in loan assessment, borrower training, and financial management program as FSA may require;
- (5) Does not own, directly or indirectly through a family farm corporation, land in an amount that exceeds 25 percent of the median acreage of the farms or ranches in the county; and
- (6) Demonstrates that the applicant’s and his or her spouse’s available resources are not sufficient to farm or ranch on a viable scale.

In case of cooperative, corporation, partnership, or other business entity, all entity members must be beginning farmers. 7 U.S.C.A. § 1991 (West Supp. 1996) as amended by Section 638 of the FAIR Act.

Purchase Price. A beginning farmer must pay the current market value to purchase the property.

State Director Review. If FSA determines that the applicant is not a beginning farmer, the applicant may ask for an expedited review of that determination from the state director of FSA. The state director's decision will be final. No further appeal is allowed.

More Than One Qualified Beginning Farmer. If more than one qualified beginning farmer offers to purchase the property, the Secretary must select among the applicants on a random basis. This random selection is final. It is not an appealable decision.²⁸

Lease. FSA may lease inventory land to a beginning farmer or rancher who qualifies for a credit sale, direct farm ownership loan, or guaranteed loan when funds are not available. The lease term will be 18 months or until the credit sale or loan funds become available, whichever occurs first.

Step Three

If no beginning farmer purchases the farmland, FSA must sell it at a public sale within 30 days after the 75-day beginning farmer preference period.

Buying at Public Sale. FSA is not required to attempt to sell the property to farmers at the public sale. Anyone may buy the property at this sale.

Form of Sale. The public sale may be either a sealed bid process or a public auction.

Step Four

If no acceptable bid is received at the public sale, FSA may negotiate a sale of the property for the highest price it can obtain.

D. Conservation Easements

In the past, FSA has been required to place conservation easements on certain types of inventory farmland before it is sold.²⁹ The FAIR Act limited the types of inventory land on which FSA would be required to place conservation easements.³⁰

After April 4, 1996, wetland conservation easements will *not* be placed on land that: (1) was considered a prior converted or frequently farmed wetland on the date the property was taken into inventory; or (2) had been farmed at any time during the five years prior to the date the property was taken into inventory.

However, FSA will continue to place conservation easements on farmland located in a flood plain. Also, if there was a conservation easement on the land when it entered FSA inventory, that easement will remain on the property when it is sold.

²⁸ FAIR Act, § 638(2).

²⁹ 7 U.S.C.A. § 1985(g) (West Supp. 1996).

³⁰ FAIR Act, § 639.

E. Special Rules for Indian-Owned Lands on Indian Reservations

In an attempt to prevent the loss of Indian ownership of farmland located on Indian reservations, Congress enacted a law in 1985 that set special rules for sale or lease of Indian-owned lands that were taken into FSA inventory.³¹ The FAIR Act retained these special rules and added additional procedures that would allow transfer of land directly to Indian tribes or the assignment of FSA debts to the Department of Interior, Bureau of Indian Affairs. If these new procedures are used, FSA will not take the property into its inventory.³²

1. New FAIR Act Provisions

The FAIR Act requires that before FSA begins foreclosure proceedings, it must offer an Indian borrower whose land is located within an Indian reservation an opportunity to (a) have FSA assign the loan and security instruments to the Department of Interior, or (b) convey the Indian land to the Indian tribe that would assume the borrower's debt.

Assignment to Department of Interior. For FSA to be able to assign the debt and security instruments to the Department of Interior, the Secretary of Interior must agree to release FSA of all responsibility to collect on the loan secured by the land.

Transfer and Assumption by Indian Tribe. If the tribe accepts the conveyance of the Indian borrower's land, it must agree to pay off a loan equal in amount to (a) the current market value of the land, or (b) the outstanding principal and interest on the Indian borrower's debt, whichever is less. The assumed loan will be treated as though it were an Indian land acquisition loan.³³

2. Notice

Both the tribe and the Indian borrower must be given notice of these new FAIR Act provisions at least 30 days before FSA may begin foreclosure proceedings.

F. Sale or Lease of Indian Lands in FSA Inventory

There are special rules for how FSA must dispose of inventory land located within Indian reservations. These special rules apply when the borrower from whom FSA acquired the land is either (1) an Indian tribe with jurisdiction over the reservation where the land is located, or (2) a member of the tribe with jurisdiction over that reservation.

³¹ 7 U.S.C.A. § 1985(e)(1)(D) (West Supp. 1996).

³² FAIR Act, § 638.

³³ The Indian land acquisition loan program regulations are located at 7 C.F.R. pt. 1823, subpart N.

The special rules apply without regard to how FSA acquired the land. They apply if FSA acquired the land through bankruptcy, voluntary conveyance, foreclosure, or any other procedure.³⁴

The special rules are that within 90 days after acquiring land within an Indian reservation, FSA must offer to lease or sell the property according to the following order of priority: (1) to a member of the Indian tribe having jurisdiction over the reservation where the property is located; (2) to an Indian corporate entity; (3) to the Indian tribe. The tribe may change this order of priority. It may also restrict eligibility for leases or sales of the land to: (1) members of the tribe; (2) Indian corporate entities that are authorized by the tribe to lease or purchase lands within the boundaries of the reservation; or (3) the Indian tribe itself.

IV. Conclusion

The FAIR Act changes to the preservation loan service programs and procedures for sale of FSA inventory land will make it much more difficult for farmers who have lost their farmland to FSA to regain possession and will encourage land sales to non-family-size farmers. While farm organizations have persuaded the Administration to change its interpretation of some of the Act's provisions to help farmers preserve their farming operations, more changes in policy are needed to ensure that FSA's commitment to family farming is preserved through its handling of inventory farmland.

³⁴ 7 U.S.C.A. § 1985(e)(1)(D), as amended by § 638 of the FAIR Act. FSA may not acquire the land if someone bids higher at the foreclosure sale. If FSA does not acquire the land, the special rules will not apply. See also footnote 24 above regarding lease authority.