

U.S. Farm Crisis

Manjula V. Guru
Agricultural Policy Specialist

James E. Horne
President & CEO

The Kerr Center for Sustainable Agriculture
Poteau, Oklahoma

Abstract

It is widely believed in the corporate sector that in this age of virtual business, most banking customers do not need 'brick and mortar' banks once an account has been opened. This belief has paved the way for the saturation of banks, and this in its turn has led to brutal competition and then consolidation of banks in the United States.

The U.S. banking industry has been consolidating at a rapid rate over the last fifteen years, largely because of the liberalization of state geographic restrictions on branching and holding company acquisitions. The banking consolidations over the years have significantly reduced the number of small banks, and because of that the impact of these bank mergers and acquisitions on small business lending has been considerable.

These developments have led to the total supply of bank credit to members of the farming communities falling substantially, the farmers applications for loans being turned down increasingly, and in a substantial rise in the bankruptcy rate among the farming community. The impact of this development has been felt considerably by farmers, as is evident from the increasing number of farm bankruptcies. This report proposes to examine this impact on the US agricultural enterprises, especially as experienced and perceived by small family farmers.

Keywords: Agriculture, farmers, bankruptcy, bankers, corporate.

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The Kerr Center seeks to influence and call to action our acquaintances by both example and education. The Center's Sustainable Rural Development and Public Policy Program was established in 1996. The program assists rural citizens and decision-makers by sharing information about building strong and sustainable communities and the consequences of proposed policies for rural communities and agriculture.

For more information on this and other Kerr Center programs contact:

The Kerr Center for Sustainable Agriculture, Inc.

P.O. Box 588, Poteau, OK 74953

Phone: (918) 647-9123; Fax: (918) 647-8712

Web Site: www.kerrcenter.com

e-mail: mailbox@kerrcenter.com

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Foreword

We are in the midst of another farm crisis. While many remember the dramatic events of the 1980's, when so many farmers lost everything and agriculture was front page news, this new crisis has been quieter. Its impact, however, is just as serious for many farmers.

Crisis is defined as a crucial or decisive point or situation; a turning point. Agriculture is indeed at a turning point. What has happened? The combination of low prices, bad weather, the false notion that exports help farmers become more profitable, and changes in farm policy has resulted in devastatingly low profits. In addition, large corporations have in recent years moved to curtail farmer independence through production contracts and other forms of vertical integration. These moves have included establishment of huge corporate-owned Confined Animal Feeding Operations, where animals are raised without farmers.

These external forces, largely beyond the control of individual farmers, have taken their toll. Farmers go bankrupt or just decide to quit. Too often, farmers who have lost their farms are characterized, even stereotyped, as inefficient. This is unfair. Not only are these external forces the key reasons for failure, they also serve as barriers to those who might want to enter farming.

As older, experienced farmers bite the dust, who will take their place? As we lose farmers, we lose communities, and

we lose stewardship of natural resources. The general public is not sufficiently aware of these losses.

The loss of farmers, rural communities, and natural resources has ramifications beyond rural America. If we lose our diversified system of food production, based on a healthy number of independent, family-operated farms, our national food security is at risk. As large corporations go about their business of patenting the world's food supply, tying farmers to their products of seed, pesticides, and fertilizers, and then serving as the only feasible market, we will witness further degradation of our natural resources, rural infrastructure, and the cultural history of farming in many communities.

James E. Horne, Ph.D.

President and CEO

Kerr Center for Sustainable Agriculture, Inc.

Section 1: Introduction

*It's part of American heritage - family farmers struggling for their community. But the modern reality is different. A handful of giant corporate agribusinesses are squeezing the life from our family farms. It's still the primary vision of American democracy. Our country's heart and soul, rooted in the land, protected by millions of family farmers. They work cooperatively; they feed their communities; they live a rich cultural life. They are America's economic and spiritual backbone. But it's fast becoming a fantasy. Family farmers are being demolished by giant global corporations. And it has nothing to do with "efficiency."*¹

Seventy years ago, there were nearly seven million American farmers. Now there are about two million, even though the general U.S. population has doubled. Between 1987 and 1992, America lost an average of 32,500 farms per year, mostly family farmers. Of those small farmers still on the land, 80% have farm income below the poverty line. They've had to earn most of their income off the farm. This has been the story in America for decades: more bankruptcies, fewer farmers and ever larger farms. 75% of U.S. farm production now comes from only 50,000 farming operations.

The proportion of Americans now engaged in farming has decreased to less than 2% of the population. And the number of counties where agriculture is the primary economic activity has also been shrinking rapidly since World War II. This decline seems to be taking a heavy toll on small towns and rural areas where agriculture has been a dominant force. A select number of farms are getting larger, and not just because big corporations

are buying them up, but because farmers are expanding by buying out their own neighbors.

No one sector of the economic system in the United States has felt the disastrous affects of corporate concentration, power and control more than the nation's family farmers. The five biggest seed suppliers in the world control 75% of the global market for vegetable seeds. The ten biggest agrochemical manufacturers in the world control 85% of the agrochemical market. Just four companies control 69% of North America's seed corn market.

With such reduced price competition farmers must pay what these corporate giants demand for seed and chemicals. And at the selling end of the cycle, farmers face even greater consolidation from food processing and manufacturing companies. For example, if you are a farmer growing cereal grains, you face four huge companies (Kellogg, General Mills, Phillip Morris, Quaker Oats) that control 84% of cereal manufacturing. This trend is also seen in animal markets. If you raise beef cattle, only three meat-packing companies (Cargill, ConAgra, IBP) control 81% of the market. Similar numbers apply in poultry and hogs.²

From 1982 to 1993, the prices paid by farmers for inputs increased by 23%, while the prices received by farmers rose by only a third of the cost increase. In other words, the situation got steadily worse. In 1997-1998, farmers spent about \$2.64 per bushel to grow corn (according to government estimates), but they were only able to sell on average at \$1.91 per bushel. In 1999, the price went down to \$1.82 per bushel while costs of production continued to rise.³

The shift to giantism in farming is very apparent in hog production. As late as 1993, almost 2/3 of U.S. hog farmers owned fewer than 100 sows. By 2000 corporate "factory farmers" owned 80,000-200,000 hogs each. They raise their animals in confined conditions, adding to problems of disease and pollution from animal waste and toxins. By the last quarter of 1998, hog farmers could only sell hogs to processors at 15¢ per pound. The cost of production was 55-60¢ per pound, thus increasing small farmer foreclosures and bankruptcies.⁴

The trend now is for a farmer with a larger farm to enter into agreement with suppliers and marketers through vertical integration in a way that changes the financial relationships, responsibility, and rewards for the farmers as compared with others in the food system. For example, the supplier, who may provide the farmer with seeds, chemicals, and capital, may also specify the genetic and product characteristics of the farmer's crops. The farmer, on the other hand, assumes less market risk while also earning less of a profit.

The farmer is much less of a free agent under the new arrangement. Thus, concern about family farms is not just concern about whether farmers have enough land to support a family but is now bound up in shift in the economic and social role of the farmer. Under the new rules of the game, the farmer is less of an independent decision-maker. Supplies may no longer be purchased from local dealers, and the loss of a contract with a processor may put a farmer out of business, especially if local markets have disappeared.

Meanwhile, at local supermarkets retail prices to consumers have steadily increased. Where's the money going? Very little goes to the farmers, while most of it goes to the

corporate middlemen who squeeze the farmers at both ends of the cycle.

For a farmer to maintain a steady family income as prices decline, the size of the farm must increase. So while advances in technology drive real prices down, benefitting the consumer, farmers are forced to enlarge the size of their farms by buying out their neighbors. The dilemma of the family farm is that an adequately-sized farm for a family twenty years ago is no longer adequate today.

USDA figures for the 1990s show that average farm operator household earnings from farming activities as percent of average household income was an alarming 11.8%. Because many farmers earn most of their income off the farm, most Americans are not aware of how depressed the farm economy actually is. In reality, farmers are too often impoverished and enslaved by an ever-increasing large, globalized, transnationally-owned and controlled food manufacturing system.

For nearly a century now, the inability of most farmers to receive a consistently fair and equitable return on their investment has left them with three basic options: sell their land and exit from agriculture altogether, attempt to borrow money from public and private lenders in order to remain in farming, or seek employment off the farm in order to economically survive and hopefully retain the family's farm. Their inability, however, to receive a fair and equitable return on their investment (to say nothing of simply being able to meet their production expenses) has little to do today with how efficient they are, but a lot to do with not being paid adequately for what they produce.

Such a dismal situation is resulting more and more in frustrated and helpless farmers calling it “quits” and stepping into the unknown realm of bankruptcy. Many decide to get rid of their lands and make a life away from farming. Yet there are some brave people who make an effort to hold on to their farms and continue with their chosen occupation of farming and their allegiance to the land and its stewardship.

Section 2:
Today’s Increasing Agricultural
Bankruptcies⁵

Legislative and regulatory changes during the 1990s have significantly altered the way banks are supervised and regulated. Banks have justified proposed mergers with anticipated gains in economies of scale through reductions in overhead per dollar revenue, anticipated gains in economies of scope through expansion of bank product lines, and anticipated increases in volume through market expansion. Legislative and regulatory changes have removed restrictions on geographic expansion and expanded the services banks may offer. Interstate banking is old news, as are regulatory changes that now permit banks to buy securities firms.

With the decline in the number of small banks, the impact of bank mergers and acquisitions on small business lending (SBL) has been considerable. Farmer applications for loans are being increasingly turned down, and the ones fortunate enough to get a loan are having their loans increasingly foreclosed upon. The result is a rising bankruptcy rate in farming communities.

Farmer bankruptcies are controversial and emotional. Whether regarded in the general sense of a business closing down or in a narrower legal sense, they are thought to be an indicator of the economic and social well-being of rural communities, as well as the structure of the rural economy. Sometimes bankruptcies are regarded as a measure of the success or failure of various public policies (such as price supports, export subsidies, conservation rules, environmental regulation, and public credit funding), directed at improving the economic status of the farm sector. Public concern over farm policy therefore rises when bankruptcy appears to be taking an inordinate toll on smaller farms.

Bankruptcy generally describes proceedings undertaken in a federal court when a debtor⁶ is unable to pay or to reach agreement for payment with creditors. The bankruptcy code contains four operative chapters (chapters 7⁷, 11⁸, 12⁹, and 13¹⁰), under which personal or business bankruptcy petitions may be filed. The debtor rehabilitation provisions of the code (Chapters 11, 12, and 13) differ from the Chapter 7 proceedings because the debtor looks to rehabilitation and reorganization, rather than liquidation, and the creditors look to future earnings of the debtor, rather than property held by the debtor, to satisfy their claims.

Farming is a capital-intensive industry, and farmers rely on credit to finance a significant portion of the assets they employ. The credit needs of farming communities are served by a wide range of lenders. Banks, the Farm Credit System (FCS), the United States Department of Agriculture (USDA), and life insurance companies are the major institutional sources of credit. Surveys of lenders and borrowers suggest that

competition for credit-worthy borrowers has been very intense among agricultural lenders for the past several years (USDA, 1996).

The most visible components of the financial market faced by rural borrowers are the commercial banks located within their communities. Not only are bank offices prominent community landmarks, but they supply most of the credit used by rural borrowers. The rural credit delivery system in the U.S. consists largely of privately-owned banks, providing financial services with the intent of earning profits.

The small size of rural communities and the small size of rural borrowers limit the number of lenders that can profitably compete for rural loans. As a result, many of the rural markets and farming communities are not well-served. In some rural communities (and especially for members of farming communities), the range of available financial services and institutions is too small to ensure an efficient allocation of financial resources.

Farmers in rural America face a number of problems when applying for loans:

1. Risk financing (equity for new businesses, long-term operating loans for businesses and community organizations) is difficult to find;
2. Transaction costs are often higher for rural borrowers whose financial needs are unusually large or complex (by local standards), as they have to shop over a wider geographic area and deal with a broader range of institutions than is typically true in urban settings; and

3. Access to credit and other financial services remains a problem for those who fail to qualify for commercial loans because of low incomes, low skills, and lack of collateral.

Commercial banks in rural areas and Farm Credit Service lenders are both financially sound and able to respond to increases in economic demand. Both groups of lenders have increased their lending in recent years and claim to be prepared to meet future demand for commercial credit. Despite this observation, substantial evidence exists that many rural credit markets remain imperfectly competitive, in the sense that there are not enough banks available for community members to choose between.¹¹ These imperfections often result in operating inefficiencies among some rural borrowers, who are forced to go to the available bank and hence accept the services given even if they are not the best.

Section 3: Popular Perceptions

3.1. What Do the Farmers Say about Bankruptcies?

The Kerr Center conducted case studies of four Oklahoma family farmers who have chosen to file for bankruptcy. They were each asked three questions. Their views are represented without changes. The farms had been in all the farmers' families for at least 100 years. Three of the four farmers studied are college graduates. The guaranteed loan program seems to be at the root of problems for three of the four farmers.¹² All four also commented on the number of farmers who had been bought out recently in their areas, and the purchases of neighboring land by lawyers, doctors and other urban dwellers who might never use it for farming purposes.

The first question we asked was what led the farmers to file for bankruptcy. All four of the farmers said that they were forced into it.

Farmer One, from northeastern Oklahoma, had suffered a high death loss in his cattle herd and had reduced his calf crop due to selenium problems. He was the first in his area to receive a guaranteed loan from what used to be a local bank and believes problems to have started after that. After filing the preliminary loan application, he apparently talked to the banker about needing additional money, as he wanted to take over some of his neighbor's land. The banker agreed to loan him more. However, once the loan application was approved the banker refused to loan him more money. It took him thirteen months to get funds through the local bank. In the process he used up all of his cash reserves to pay for operating costs, to renew leases, and to plant crops. These were all expenses the bank had originally agreed to cover in the loan. Luckily his wife had a regular non-farm job. Under the guaranteed loan Farmer one had made a principal loan, and was given a fixed payment for the next two years. These problems, plus the drought in 1995, led to his filing for bankruptcy.

Farmer Two, from northwestern Oklahoma, had always been successful and had never encountered any major problems throughout his farming career which started almost 50 years ago. According to him, "things were good in the 70's, and it was only in the late 80's that problems arose due to lack of rainfall and bad weather." He had never borrowed any money, and even now owes only the bank, which unfortunately was not locally-owned. He applied for a guaranteed loan. The bank did all the paperwork for him, and while under the loan he was supposed to have money to buy cattle, the banker would not loan him the

money to do so. The bank then wanted to foreclose. As a last minute effort to save his land, he chose to file for bankruptcy.

Farmer Three, from southwestern Oklahoma, is a cattle rancher. The local lender sold the bank to a non-local bank. Before the bank sale was completed, the new owners required the old banker to foreclose on any poorly-performing loans. The new bank decided that Farmer Three's loan was not being paid off quickly enough. Being a non-local bank, the bankers did not have an agricultural background and were more oriented towards investments. When Farmer Three began experiencing financial losses, the bank started charging interest at a quarterly rate. The victim tried reasoning as well as pleading with the bank. The bank finally agreed to help him on the condition that he would give the bank his house and settle for a life interest. When he declined to do so, the bank threatened to foreclose on him. In frustration, he filed for bankruptcy.

Farmer Four, from southwestern Oklahoma, died during the bankruptcy proceedings and was succeeded by his 74-year-old wife and son. They are a hard-working family who had never over-invested in equipment, and were not living beyond their means. Their land had been mortgaged since the 70's, and they had been making their payments on time. Then suddenly, the bank wanted payment by September 1, when they knew that the cotton crop was harvested around November 1. Desperate to save his land, Farmer Four decided to file for bankruptcy. He died the day the bankruptcy papers were received.

The second question was whether their situations would have been different if the regulatory system-- i.e., the banking system-- had been different. All the four farmers agreed instantly.

Farmer One says that the problems with bankruptcies have to do with "...undue extra costs and requirements...providing a lot of employment opportunities to bankers." He feels that the prevailing system favors "hammering" people who have guaranteed loans. Noting that local officials didn't want to talk at all, he adds that while local bankers were aware of his problems, they, like the big bank, didn't care about the farmer's problems. He concedes that the Farmers Home Administration (FHA) has been helpful, but he doesn't like working with them because they aren't always available. The Farm Bureau, according to him, talks a lot about what's good, but doesn't do much in the way of help. Furthermore, he blames the government for telling the people "facts about the Farm Bills once the term is about to finish."

Farmer Two believes that the bank could have worked with him but chose not to. The bankers, according to him, have "a bad attitude." He has never paid much attention to the Farm Bills, but mourns the loss of the family farms and says, "the biggies are buying out us small farms."

Farmer Three maintains that the whole banking industry has changed and is now pretty ruthless. He doesn't think that he would have ever needed the bankruptcy option had he been given a chance by the bank. The banker could have analyzed the case and helped him through, but chose not to. A majority of the bankers don't know their clients anymore and very few banks are agricultural lenders today. There are also no big banks in the county anymore, and definitely none that are local. Furthermore, the Federal Land Bank System and the Farm Credit Corporation (FCC) have changed since the 1980's. Bankers now appear to want enterprises with less risk involved,

and community-based investment such as agriculture does not fall into this category.

Farmer Four's family says that the banks are not meant for the farmers any more. "It is as though they have decided that once you start paying up the principal amount of the loan, then they would need to cash you out and give the land to someone else. It no longer profits them to continue with their loan agreement." They believe the existing situation is a classic case of the carrot-and-stick approach. The bank's strategy is to tempt you with money and a prosperous future and then show you the stick once you deviate from their planned path. Further, the FHA is seen as no longer helping the small farmers. The Extension Service is also perceived as ineffective.

The third and last question was whether the farmers felt that they should have proceeded differently? And again there was a consensus opinion, which this time was "NO."

Farmer One doesn't feel that under the circumstances he could not have acted any differently. "Bankruptcy was the only thing to do....However, I have learnt a lot from banking in the last few years....Anytime you owe money you make yourself a slave." He chose Chapter 12 and not Chapter 7 because "the land is my life and I didn't want to leave it." And he says that he would again choose Chapter 12 if he were faced with a similar situation.

Farmer Two cannot think of any other way he could have proceeded. According to him, this was a classic example of "big corporations buying out farmers." The situation forced them to file bankruptcy. While Chapter 12 seemed the only way to proceed, Chapter 7 is beginning to now loom in the background.

He comments that the situation shouldn't be like this, but "the reality is, it is." He reflects that contract farming is like still being a farmer but working for someone else. He concludes by saying: "It's a hard old road. But its going to get worse."

"Bankruptcy is not easy," says Farmer Three. He didn't want to file for bankruptcy but was forced into it. However, he feels that if faced with a similar situation again, he would most likely proceed in the same way. However, he comments that he's a lot smarter now and if he wants money again, he would go to the Farm Credit Services (FCS). He feels that he wasn't given a fair chance, and that his failure was due to a number of factors—the main one being the banker. "I worked long and hard to pay off the debts, but there was no way to do that. The more I worked, the more everything failed."

Farmer Four's family maintains that even if faced with a similar situation they would still select Chapter 12. For, as his widow says, "...when you work a lifetime, you don't walk off and give it to someone else." Bankruptcy, according to them, is a lot easier and has less paperwork involved than dealing with the FHA or with the Federal Land Bank directly.

3.2. What Do Bankers Say about Farmer Bankruptcies?

We spoke to two bankers in Oklahoma, one of whom is a farmer, to find out how they viewed the prevailing crisis. We were struck by the difference in perceptions between the two bankers.

Our first question was whether the bankers felt that there really was a farm crisis.

“Everybody talks of the farm crisis. But I feel there is none,” says Banker One (non-farmer) from northwestern Oklahoma. According to him, farming is a business. “Farming should be managed just like any other business.” Yet he acknowledges that there are some that make it work and are doing well, and others who are suffering financially and going into bankruptcy. If there really is a crisis, according to him, nobody would be able to make it. He says that prices and weather are the two variables that affect farming, and these two factors are the same for all those in farming.

“There’s no doubt that there’s farm crisis going on. But, its not an evenly distributed one,” says Banker Two (a farmer), also from northwestern Oklahoma. According to him, every time money is involved a difference in success is possible. As a farmer himself, he says that, “farmers today don’t set their own prices, but are instead cost-payers.”

Our second question was why the bankers are viewed as the bad guys by most family farmers today.

According to Banker One, making the farmers realize their problems or getting them out of trouble is the first step. They have to look at the economics of each situation, and have to be stern and “hard-headed.” They then have to push the farmers to move away from handing out operating expenses. Bankers have to try to make the farmers understand that they can only borrow certain amounts of money, and that they have to work hard to make their payments. In other words, the payments have to be made. “The farmers have to learn to manage the budget available to them. They cannot just overspend the money given and then want to borrow more.”

They have to be more accountable for their debts and have to learn to make their business (i.e., farming) work.

Banker 2 says that farmers will, in the future, have to take on more responsibility. “The banker does not mandate the farmers buying and selling anything. Its finally a choice of the farmers themselves.” Oftentimes a venture appears like a good situation to farmers, and then because of some economic problem, it becomes a bad proposition and blame falls on the farmer. “Agriculture is such an emotional industry. And the farmers take bankruptcy so emotionally. And that is the reason they have to somehow shift the responsibility onto someone else.”

The next question was what the bankers felt about the guaranteed loan program.

Banker One said that his bank has moved a lot of people into the guaranteed loan program, and that most of his bank’s loans are 90% guaranteed. This program is favored by them as it affords the bank very limited exposure. He commented that the program requires record books to be maintained in a systematic fashion for a number of categories such as money to be spent for fertilizer, for machinery, and for feed. As a banker he has to be very stern in certain situations because farmers have to show at each and every stage that there is a regular cash flow. Once the farmers use money from any one of these categories, then they should not take money from any other category.

Banker Two’s bank has a very limited number of FSA guaranteed loans. While they did many historically, they realized that “any guarantee is only as good as it can be.” He

feels that a lot of the credibility that these loans commanded in the past is no longer applicable and that the program works well only in cases of real estate. This is so because while production increased under these loans, the total revenue receipt declined. He adds that his counterparts at the bank do not feel very confident about guaranteed loans. This is because the lender would like to keep his guarantee intact, and when the borrower wants to borrow extra money, the feeling of security is threatened. While the FSA maintains that, if required, additional money can be applied for, such is not the case. The banker gets caught in a bad spot with farmers who believe that, while FSA is prepared to help them, the bankers are unwilling.

Our fourth question was about the path their banks would be treading in the years to come.

Banker One's bank, which is locally-based is now looking for different branches and strategies to allow the bank to diversify away from agriculture. While the bank will not leave agriculture totally, it doesn't see how else "it can survive in the years to come."

Banker Two, whose bank is a national bank, says that his bank will continue to help farmers "within practical limits." He feels bad about not being able to lend to all farmers and acknowledges that such inaction will lead to an increase in contract farming. But he also acknowledges that even though he may not like that scheme of banking, "the banks have to do what's bankable."

3.3. What Does FSA Say about Guaranteed Loans?

According to an FSA agent located in southeastern Oklahoma who deals mainly with the guaranteed loan program (90% of their loans are guaranteed) and is in constant touch with bankers: When the FSA makes a guaranteed loan to a bank, the banks do well with the guaranteed loans. He thinks the program gives the banks a lot more lending authority. He says that if he were a banker he would not hesitate in using these loans, for if the bankers know the application process well, then they're bound to do well with them.

The FSA agent adds that guaranteed loans cover all agricultural as well as non-agricultural enterprises. Normally a 4% subsidy is given to the borrowers and this 4% is actually for the farmers. He comments that the wheat farms out in the West often use this.

He acknowledges that there are some abuses in the guaranteed loan system, as the farmer does not always receive the full amount. He's heard of banks which start the contract with farmers at the base rate and then increasingly hike up the interest. However, he says that there have been no defaults by either the bankers or the farmers in LeFlore County as far as he knows.

3.4. Where Do the Trustees¹³ Stand in this Crisis?

All four of the farmers interviewed by us were positively and favorably inclined towards their bankruptcy trustees. All praised their trustees for being very helpful and conscientious.

Banker Two commented that from the bank's perspective the trustee is there to protect the interests of the creditors and debtors; personally, he feels that the trustees lean more in favor

of the farmers, and don't care for the bankers. But then he goes on to say, that the trustees never want to put in too much effort into any one case, as "they take on far more than they can effectively handle."

According to a retired Commissioner of the Federal Mediation and Conciliation Service, "... in 90 out of 100 bankruptcy cases, the trustee is an attorney, and finds someone to buy the farmer out in order to get their 11.1%." By law the trustees get 11.1% if they liquidate or manage the farmers' affairs. "By facilitating the sale of the farmer's property, the trustee gets his/her 11.1% up front, and therefore there is no motivation left to help the farmers." According to the Commissioner, under new revisions, the person who handles the foreclosure can also bid on the land. The trustees, says the Commissioner, "... troddle behind closed doors and come up with bankruptcy plans, and never think it necessary to consult with the farmers on their plans."

Section 4: So Whose Fault Is This Crisis?

With the farmers, bankers, and FSA agents pushing the responsibility and blame for the prevailing plight of family farmers on to one another, the question arises: Whose fault is it really, and who should now take constructive action to repair the situation?

The situation is desperate. Farming was once the most diversified and democratic economic sector in America, but today it's among the most narrowly concentrated and anti-competitive. The effect on small farmers is to make them nearly extinct.

This crisis in rural America is responsible for the loss of over one million small to medium-sized farms since 1980. Indeed, in one twelve-month period in the late 1980's, more than one million people were forced from their land. In 1996 alone, thousands of families in Oklahoma lost their farms through bankruptcies and foreclosure. And that's not all. For those who manage to hold on, it often means holding on in grinding, unending poverty and a constant struggle just to meet the day-to-day necessities of life. The fact is, while only 20-25% of the U.S. population live in rural areas, 38% of all people living in poverty live in rural areas. Furthermore, 67% of the nation's substandard housing is rural, and 27% of the children in rural America are growing up hungry, forced to live in destitution even though the parents of most of them work.¹⁴

Many people assume that when a farm goes bankrupt, the land vanishes and the farmer dies. What actually happens in a farm bankruptcy is that the farm is simply turned over to another individual (now usually to a corporation), who then attempts to make a profit from the same land. This is proven by the fact that the amount of crop land in the United States has changed little over the past sixty years despite a decrease in the number of farmers.¹⁵

Corporate farmers say that the trend to big farms happened because small farmers are "less efficient." But the reality is that small farmers are actually more efficient than big ones, especially if you quantify or calculate the environmental and social costs from factory farming, now subsidized by the government, with the costs passed on to taxpayers. The reality is also that consolidations and mergers are increasingly taking place at both ends of the farming cycle – on the inputs side which is where the farmer has to buy (seeds, fertilizers,

chemicals), as well as on the outputs side which controls what the farmer receives at the selling end. Both ends are increasingly controlled by corporate giants, aided by government policy. Small farmers are caught in the middle.

This enormous market power, which has made agribusiness corporations the most profitable industrial sector in the United States over the past five years, is measured by returns to stockholder equity. One way in which these corporations have used this power has been to push down the prices received by the independent farmer, who now functions merely as a producer of raw materials for a corporate-dominated food manufacturing system. Unable to make a fair return, farmers are forced to rely on borrowed money and government handouts. Resulting bankruptcies have led to a massive consolidation of U.S. farmland.

Under these circumstances, farmers badly need the help of bankers. The farmers need the advice and assistance of people who are not emotionally involved in the process, and whose lives and occupations are not at stake. Unlike most other professions, farming is greatly influenced by forces of nature, which are beyond the control of the farmers.

According to the Commissioner quoted earlier, “three people who can shut you off as a farmer are the county supervisor, the sheriff, and the banker. The bankers often phoney up loans, push the blame onto the farmers, and then foreclose. And in the process they sure make a lot of money. It’s a system problem, and every time the Congress passes money for the farmers, the bankers get it and keep it. They thus structure the farmers for poverty.”

Banker One told us that farming as a business needs good management like any other business. Following this idea, it is possible to see that the farming crisis is a result simply of lack of good business skills. Farmers borrow with the thought that if they increase their machine inventory, if they increase the land that they work, the money will come back to them. Borrowing increases while the actual price of crops goes down. Often farmers borrow money because they are told by the large corporations they contract with, that new machinery or new animal houses are needed. Before the farmers know what has hit them, the farm is swimming so deeply in debt that it seems impossible to break free, and the only way out is to file for bankruptcy.

It is a well-known fact today that loan applications are usually approved for farmers who produce under a contract production agreement with large agricultural corporations, while farmers who chose not to put themselves into a contract relationship are not even considered for new agricultural loans. Is that fair treatment?

The inability of farmers to make a profit is often not related to the way the farms are managed. The culture under which farms operated in the past has simply changed. In the past, agriculture was thought to be a way of life. Agriculture has now become a business that requires proper and hard-headed management skills only.

Section 5: Why The Need For A Chapter 12?

Chapter 12, the Family Farmer Bankruptcy Act of 1986, was enacted in response to the farm financial crisis of the early

to mid 1980's. Chapter 12 was passed to deal with the then existing farm financial crisis and was not intended at that time to be permanent. Today, more than a decade after its passage there are arguments for and against farmer special provisions under bankruptcy code. A key issue is whether maintenance of a special chapter for family farms is warranted.

Some arguments in favor of Chapter 12 are based on the belief that farms are small businesses subject to considerable risks stemming from weather, pests, markets, and other considerations because of a long biological process necessary to produce most agricultural commodities. This view includes the belief that farms operate under unique circumstances. Therefore the delays and uncertainties commonly linked with Chapter 11 bankruptcy generate substantial problems.

Moreover, the number of farmer bankruptcies is likely to be small compared with the bankruptcies filed by large urban firms. Support of special consideration could stem from the belief that the nation is best served by having a comparatively large number of family farms as opposed to a comparatively few large corporate farms. A special bankruptcy provision is one policy tool that can help maintain farm numbers. Also, farmers need protection from the relatively greater economic power of bankers and other lenders.

It should be remembered that Chapter 12 is very important for providing the family farmer with access to bankruptcy reorganization, and to reforming the process to accommodate the more distinctive nature of farming. Chapter 12 bankruptcy has been a viable option for family farmers nationwide. It has allowed family farmers to reorganize their

assets in a manner which balances the interests of creditors and the future success of the involved farmer.

If Chapter 12 bankruptcy provisions are not extended for family farmers, this will have a drastic impact on an agricultural sector already reeling from low commodity prices. Not only will many family farmers have to end their operations, but also land values will likely plunge downward. Such a decrease in land values will affect both the ability of family farmers to earn a living and the manner in which banks, making agricultural loans, conduct their lending activities.

The arguments against special bankruptcy treatment for farmers focus largely on efficiencies and costs. Some question why farmers should receive bankruptcy treatment different from other small businesses, i.e., what is so special about the modern farm? Regarding protecting the number of farms and, hence, slowing change in farm-sector structure, one would have to show that farm businesses receiving special bankruptcy treatment recover and survive, and would not have done so otherwise. Often the question is raised regarding the cost to lenders and to society in general stemming from the money lost or written off in farm bankruptcy procedures. Lastly, there is some concern that prospects of dealing with a farmer under Chapter 12 may discourage lenders from making credit available to farmers who are poorer credit risks.

Under the existing circumstances when farmers are increasingly turning towards bankruptcy proceedings the need for Chapter 12 is all the more crucial. In the words of Neil Harl, from Iowa State University, "It took us almost three years to bring into force a Chapter 12 when immediate enforcement was the need of the hour. If Chapter 12 were to be wiped out

completely now, I don't know how many more years it would take to enforce it again when it'll be needed."

Section 6: Conclusion

While there have been tremendous advances in the science and technology of food production—advances that have enabled the United States to lead the world in the Green Revolution, they have come at the high price of human participation in agriculture and damage to natural resources. The principles of stewardship of the land and the common good of all are absent in the current development of agriculture policy. Instead, we see ever increasing concentrations of land and the means of production into fewer and fewer hands.

Contrary to most beliefs, the economic forces which are at the root of rural America's problems are not "natural" ones, or ones which are necessarily even technologically-driven. They are, instead, problems which are largely the creation of human beings themselves, and which are being driven by the same greed which is today driving the world's financial markets.¹⁶

The system which has now been imposed on rural America is so malignant that normal men and women should be excused for thinking that some kind of plot must be at the bottom of what's going on. It's difficult to believe that people could be so driven by greed and avarice that they would think nothing of the consequences of what they are doing. But that's exactly what's happening. As difficult as it is for ordinary people to comprehend, we are (for the most part) dealing with people whose only real concern centers around greed.

That is hard to accept for people who have lived right, invested all they had, and believed that the American dream would come by the sweat of their brows, only to find themselves driven to the wall by impersonal and incomprehensible forces. Some in rural America cannot overcome their deep sense of personal failure. They are ending their lives at a rate that has made suicide overtake accidents as the leading cause of death on America's family farms. According to the manager of a Farmer Hotline Crisis Center in Oklahoma, "The farmer suicide rate is still climbing. The farmers have been under pressure for so long and have been extended the invitation to die. Unfortunately, they have accepted that invitation to die – until some measure is taken to stop foreclosing on farmers...this increase will continue."¹⁷

However, the need for family farms cannot be disputed, even though it has to be acknowledged that corporate agriculture may have its advantages. A highly diversified system of agriculture is preferable to a concentrated one for a number of reasons. First, it enables many more people to make a living from the land. Second, it ensures better diversity in plant and animal life, reducing the possibility of catastrophic disease or pests destroying herds or acreage. Third, a family farmer generally thinks of passing the farm on to future generations and often has a greater reverence for the land and interest in the community and its economic well-being. A corporation, on the other hand, has profit as its primary motive, has fewer ties to the community, and is less likely to make decisions in the long-term interest of the community.

Because today's agricultural production system is so capital intensive, it has saddled family farmers with tremendous debt. The burden that led to thousands of bankruptcies and

foreclosures in the mid-1980's continues today as the high costs of production rise for nearly every commodity, while prices drop to historic lows.

Farmers today are still willing to farm and it cannot be emphasized enough that America still needs family farmers. But because of the increasing concentration, bank mergers and acquisitions and a general indifference towards farmers among bankers today, society is soon going to lose these farms. Effort therefore has to be made to keep these farms and to preserve them. When farmers are willing to try a second time and make their farms function more economically, it should be a societal goal to assist them since effective and sustainable farming practices will result in healthy food and a healthy environment.

The need for a Chapter 12 cannot be disputed now and in the foreseeable future due to the serious situation being faced by our nation's farm families, for although the U.S. economy is generally healthy, it is clear that the agricultural sector is hurting. However, even with a continued Chapter 12, effort should be made to make the entire bankruptcy system more "farmer friendly," and more receptive to the needs of the farmers.

In light of the concerns regarding the extinction of family farms, we need to explore new ways to make markets more transparent to family farmers and create new opportunities to increase the remaining small and moderate-sized family-owned and operated farms. Such measures may include a guaranteed price so farmers will always meet reasonable costs of production and make a modest profit, have better access to instruments for ownership and operating credit, encouraging conservation and

sustainable farming methods, and funneling more research dollars into sustainable farming techniques.

Section 7: The Kerr Center's Policy Recommendations

First, it is imperative that Congress make Chapter 12 of the Bankruptcy Code a part of the permanent law. This Chapter was created exclusively for farmers, and while not perfect, attempts to address the peculiarities of farming as a business. If Chapter 12 were not to exist, the number of farmers and ranchers choosing liquidation (Chapter 7) would increase.

Second, since one of the reasons why there is an increasing number of farm bankruptcies is the rising tide of corporate-controlled markets, Congress should take immediate steps to address the impact of an ever-consolidating marketplace on independent farms and the communities within which they reside. The Department of Justice (DOJ) possesses the authority to take legal action to break-up large mega-processing firms, and it should take those steps immediately. DOJ should also strengthen its review of agricultural mergers and enforce existing antitrust authority. Congress should pass an immediate moratorium on mergers and consolidations within the agricultural processing sector.

Third, Congress should take action to address the effects of agricultural concentration on family farmers and the relationships between producers and corporate entities. And finally, the Packers and Stockyards Act should be fully and aggressively enforced and amendments should be pursued to

strengthen the government's ability to monitor corporate agricultural practices.

Fourth, Congress and the various state legislatures must become more active in addressing the market disadvantages of small producers. One means of doing so is through greater encouragement of the use of cooperatives for marketing. Cooperatives, properly organized and managed, offer producers an alternative to the corporate controlled marketing structure. New start-ups need professional assistance. This is one area in which the states can have substantial impact through the passage of initiatives designed to bolster the family farm, provide professional training and assistance for niche marketing and cooperative marketing, and providing incentives to move away from corporate controlled marketplaces.

Finally, Congress and the states should increase the support for research geared toward sustainable agriculture, sustainable rural communities and sustainable marketplaces.

Afterword

In preparing this paper we spent considerable time with four farmers who were forced into bankruptcy. To get the full story, we also interviewed people from various lending institutions, both private and public. It became obvious that the teamwork often found in locally-owned banks, that used to keep lenders working with their farmers and for their community, is almost gone. When local banks are absorbed by chains, the need to satisfy stockholders and investors that live outside the community is far greater than the need to build communities. As we lose our passion for the land, we depersonalize our food system and it becomes nothing more than an input-output production model with the common denominator being dollars. I'm not sure that we can sustain ourselves with such a model.

As an economist, I understand the conventional notions and arguments that are based on the efficiency model, as well as its merits. However, as a person, I have come to care about many of the intangibles of life that are ultimately more important. Efficiency models do not take into account issues of topsoil loss, degradation of water quality, the human health consequences of industrial agriculture, issues of justice, distribution of income, hunger, or the value of a community. When any model of agriculture negatively impacts any of these, there is a cost. That cost may be easily counted or it may be as subtle as the barn depreciating. At some point, we all will pay.

The farm crisis is real and it has real costs that will be borne by this and future generations. If we want agriculture to sustain us, then we must make sure that our system is based on fairness and adequate returns for those tending the land. It must be based on sound ecological principles that will ensure that our

natural resources are adequate to meet the needs of future generations. We are at a turning point. If we address these elements of sustainability, then we will see a decentralized food system that is resilient, where competition is healthy, where research is done for the public good, and the landscape will hold many farmers tending their farms with an eye to the future.

James Horne
President and CEO
Kerr Center for Sustainable Agriculture

Notes

¹ *America's last family farms*. [Available at: <http://www.turnpoint.org/lastfarms.txt>].

² Wirtz, R.A. *Farm crisis: Here we go again?* Federal Gazette, October, 1999.

³ *America's last family farms*. [Available at: <http://www.turnpoint.org/lastfarms.txt>].

⁴ *Id.*

⁵ **Bankruptcy** is a non-technical term for a legal state of insolvency. **Insolvency** is a term used to describe a firm that is failing; generally it means that a firm's liabilities exceed its assets or that it is unable to satisfy its obligations as they come due. [Epstein, David G. Bankruptcy and Other Debtor-Creditor Laws, In a Nutshell. Fifth edition. St. Paul, Minn. West Publishing Co. 1995].

⁶ A **debtor** is the entity seeking protection from creditors under the bankruptcy laws. *Id.*

⁷ **Chapter 7** - liquidation proceedings; generally assets are sold by a trustee and the company ceases operation. (Individuals may file Chapter 7 also). *Id.* p.134.

⁸ **Chapter 11** - reorganization proceedings, generally for business entities; the debtor retains control of the business in Chapter 11 (unless the Court appoints a trustee). *Id.* p.135, 331, 334.

⁹ **Chapter 12** - family farmer bankruptcies; created by Congress in 1986 (Chapter 12 became effective on November 26, 1986); only a family owned farm business can qualify for Chapter 12 and it must have debt less than \$1.5 million and have 50% of its income from farming operations. *Id.* p.360.

¹⁰ **Chapter 13** - bankruptcy proceedings for an individual with the intention of rescheduling the individual's debt (rather than liquidating the individual's assets and debt. Chapter 13 is referred to as wage-earner bankruptcy, personal bankruptcy or consumer bankruptcy. Chapter 13 cannot be used by a partnership or a corporation; it can be used by a sole proprietorship. *Id.* p.135, 367, 370-1.

¹¹ USDA/ ERS. Are Farmer Bankruptcies A Good Indicator of Rural Financial Stress? Agriculture Information Bulletin No. 724-06. December 1996.

¹² See Appendix A. According to an FSA agent, under the guaranteed loan program the bank is actually FSA's customer. FSA has a loan application and the banks have a loan application. The bank supplies all the borrowers information to FSA. 1% of the fees under the guaranteed loan is paid to FSA. There are three types of lenders in this case: the standard eligible lender, the certified lender, and the higher preferred lender. The last of these categories was started in September of 1999. The applications are very short, and easy to complete.

¹³ A **trustee** is an agent of the court who manages the property of the debtor for the benefit of the creditors. The court appoints a trustee in most Chapter 7 cases and in Chapter 11 cases when it determines that the debtor's management should not remain in control. This type of trustee should be distinguished from the **U.S. Trustee**, who plays an administrative role in all bankruptcy cases. [Epstein, David G. Bankruptcy

and Other Debtor-Creditor Laws, In a Nutshell. Fifth edition. St. Paul, Minn. West Publishing Co. 1995, p.28].

¹⁴ Dyer, Joel. Harvest of Rage. P.78.

¹⁵ Bovard, James. *The Farm Credit Quagmire*. Policy Analysis No. 122. July 27, 1989.

¹⁶ Shearer, S.R. *A Growing Rage in America's Heartland*. [Available at: <http://www.isrp.org/journals/april/rage.html>].

¹⁷ For further details email Mona Lee Brock at mlbrock@trinex.net