

# Getting to Zero Subsidy & the Farm Bill

**Bill Broydrick**

Broydrick & Associates

# Getting to Zero Subsidy

The background features abstract, overlapping geometric shapes in various shades of green, ranging from light lime to dark forest green. The shapes are primarily triangles and polygons, creating a dynamic, layered effect. The overall composition is clean and modern, with the text centered on a white background.

# Letter to the Conferees, Nov. 21, 2018

November 21, 2018

The Honorable Pat Roberts  
Chairman  
Senate Committee on Agriculture, Nutrition & Forestry  
328A Russell Senate Office Building  
Washington, DC, 20510

The Honorable Debbie Stabenow  
Ranking Member  
Senate Committee on Agriculture, Nutrition &  
Forestry  
328A Russell Senate Office Building  
Washington, DC, 20510

The Honorable K. Michael Conaway  
Chairman  
House Committee on Agriculture  
1301 Longworth House Office Building  
Washington, DC 20515

The Honorable Collin C. Peterson,  
Ranking Member  
House Committee on Agriculture  
1301 Longworth House Office Building  
Washington, DC 20515

Dear Chairman Roberts, Ranking Member Stabenow, Chairman Conaway and Ranking Member Peterson,

On behalf of the National Rural Lenders Association, Rural Lenders Roundtable, the American Bankers Association and the Independent Community Bankers of America, we urge you to include the attached language which is similar to Senator David Perdue's non-controversial "Rural Development Loan Study" amendment in the Committee Conference Report.

The proposed amendment would require a study of zero-subsidy programs for the Rural Energy for America Program and the Business and Industry loan program and a determination of alternative financing mechanisms. The zero-subsidy methodology was established 30 years ago for the Small Business Administration ("SBA") and the size of their portfolio has considerably expanded, providing credit to small businesses with the participation of the lending community.


This Rural Development Zero Subsidy Study amendment is crucial to harmonize the differences in both chambers' Farm bills in their attempt to move the Community Facilities Lending Program, and other guaranteed loan programs to a zero-subsidy basis. For instance, two sections, Sec. 6203 in the Engrossed House bill and Sec. 6117 in the Engrossed Senate amendment, are both written to address fees for Guaranteed Loans, in the hopes of reaching zero-subsidy status. However, these pieces of legislation have differences that go beyond simple style or formatting. Sec. 6203(a) directs the Secretary of the Department of Agriculture to collect fees from "*the recipient of the insured or guaranteed loan*" whereas Sec. 6117(a) directs the Secretary to collect those same fees from "*the lender.*" This same discrepancy appears in Sec. 6203(b) and Sec. 6117(b). While the recipient of the insured or guaranteed loan described in 6203 can be, and is likely meant as, the same entity as the lender in 6117, it is unclear under a plain-meaning reading of the statute. The word "recipient" could mean the lender who receives the loan from the U.S. government, but it could also mean the rural borrower who is the ultimate recipient of the loan. This ambiguity is likely to lead to confusion, perhaps even litigation, and must be resolved.

The Rural Development Zero Subsidy Study would review current policies and procedures and revise as required in order to reduce losses and budget authority through professionalization of credit decisions. Special attention should be given to the flexibility and alternatives in both initial and annual fees for borrowers and lenders. Other avenues of provisions should be researched for management and retention of the zero subsidy that would improve the marketability and flow of funds to rural communities. Additionally, the study should explain, in detail, how the subsidy rate is formulated for each individual guaranteed lending program and how the formulation may be improved or changed to reflect the actual performance of each program. Special care should be given to policies that will enhance the robustness of secondary markets to increase liquidity.

Additionally, to obtain an informed and vigorous understanding of the viability of transitioning to zero subsidy, rural stakeholders should also play an integral role in the study and report. The Secretary should consult with all stakeholders—especially trade associations that represent lender and rural communities. The Department should conduct a series of public forums to gather input from rural communities, municipalities, non-profits, and other borrowers.

To properly comprehend the viability of transitioning Rural Development Guaranteed Loan programs to zero-subsidy and to harmonize existing provisions in both chambers' bill, we ask that this language, which is similar to Senator Perdue's "Rural Development Loan Study" amendment, be included in the Committee Conference Report.

Respectfully,



Thomas Kimsey  
President, National Rural Lenders' Roundtable



Mark Scanlan  
Senior Vice President, Independent Community Bankers America



Stuart McCalman  
Representing National Rural Lenders Association



Ed Eilfmann  
Senior Vice President, American Bankers Association

# Getting to Zero Subsidy

*Basic Subsidy Rate Calculation:*

**Losses-Fees Income= Subsidy Costs**

*Current B&I Subsidy Rate: 2.32%*

## **How to Reduce the Subsidy Rate?**

1. Reduce Losses; or
2. Increase Fees

# Parameters of Increasing Fees to Reduce Subsidy Rate

1. **Offsetting the entire subsidy of 2.32%:** Increase the **origination fee** from 3% to 5.7% (by approx. 270 basis points)
2. **Offsetting the entire subsidy of 2.32%:** Increase the **annual renewal fee** by approx. 60-70 basis points from 50 basis points (0.5%) to 110-120 basis points (1.1 – 1.2%)
3. **Offsetting the subsidy of 2.32%:** Increase **both** the **origination fee and annual renewal fee**, at mid-points:
  - a. Increase the origination fee by 1.0% to 4.0%; and
  - b. Increase the annual renewal fee by 30 basis points to .8%

# DRAFT Rural Development Loan Study Amendment

No later than September 30, 2019, the Secretary shall submit to the Committee on Agriculture of the House of Representatives and the Committee on Agriculture, Nutrition and Forestry of the Senate a report analyzing guaranteed lending under Community Facilities, Water and Waste, Broadband, B&I, and REAP to determine—

- i. the level to which the origination fee and annual renewal fees would need to be raised in order to:
  - a. achieve a zero-subsidy level
  - b. reduce the subsidy rate to optimize the value of the program for rural communities.
- ii. The projected loan volume and the projected appropriations amount necessary to support that program level for each program under the fee structures described in (i);
- iii. whether such fees would prevent participation by smaller lenders and borrowers;
- iv. whether participation under a zero-subsidy structure could be increased by charging higher fees for larger loans and lower fees for smaller loans and, if so, what level of fees and loan sizes would achieve higher participation;
- v. how subsidy rates are formulated for individual guaranteed lending programs and how to enhance subsidy rate formulation to reflect performance of each program;
- vi. differences between USDA and SBA loan processes and whether USDA could expedite loan processing and ensure consistency between area service centers, states and national offices.
- vii. whether a transition period is necessary to shift USDA's guaranteed programs to a zero-subsidy structure without diminishing existing loan volume.
- viii. Other actions the department could take to reduce the subsidy cost of running guaranteed lending programs, besides increasing fees, including a quantification of the estimated effects of such changes.

# DRAFT Rural Development Loan Study Amendment Report Language

*Guaranteed lending programs are important to meeting credit needs of rural borrowers who are unable to qualify for conventional credit. The Managers believe a modest increase in fees can achieve a zero-subsidy rate and potentially minimize or eliminate the need for future appropriations while increasing the volume of loans extended to rural businesses. However, the Managers are also mindful that guaranteed lending under the Community Facilities, Water and Waste, and Broadband programs serves a public policy purpose and encourages the Secretary to work with the Committees on Appropriations to establish a fee structure, annual appropriations amount, and program level appropriate to achieve that purpose.*

*To assist in determining the appropriate fee structure and to examine the potential to reduce subsidy rates under other guaranteed lending programs, the Managers direct the Secretary conduct a study of several guaranteed lending programs to clarify the extent of necessary fee increases; the impact on loan volume; whether fee increases could be structured to minimize impact on smaller lenders and borrowers; and how to better enhance credit terms for future borrowers, lenders and secondary market participants. In conducting the study, the Secretary shall consult with a range of stakeholders utilizing each program from across the rural lending community, including: rural community leaders, borrowers, rural Banking institutions, rural Credit Unions, Farm Credit institutions, secondary market participants, and other interested stakeholders.*

# The Farm Bill

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# ***House & Senate:*** Changes to the definition of “rural”?

**Rural is still defined as** a “community with a population under 50,000”

***So what did change?*** Some programs have **eliminated** their “community population eligibility cap of 20,000” so, now **every** rural community (under 50k) is eligible

**Which programs are no longer capped?** Community Facilities Guaranteed Loans, Water & Waste and Broadband Programs

# Communities Between 20,000-50,000 Population= **New Lending Opportunities**

## **Georgia: ~34 Communities** between 20-50k<sup>1</sup>

*Cartersville, Union City, Acworth, Griffin, Sugar Hill, Candler-McAfee, Pooler, Decatur, McDonough, Carrollton, Canton, Stockbridge, Chamblee, Duluth, Lawrenceville, LaGrange, Statesboro, Woodstock, Hinesville, Douglasville, Dalton, Redan, Evans, Kennesaw, Tucker, Peachtree City, East Point, Martinez, Rome, Mableton, Newnan, Milton, Gainesville, Peachtree Corners, Dunwoody*

## **Wisconsin: ~26 Communities** Between 20-50k<sup>2</sup>

*Pleasant Prairie, South Milwaukee, Watertown, Mequon, Muskego, Caledonia, De Pere, Neenah, Superior City, Stevens Point, Mount Pleasant, Fitchburg, West Bend, Manitowoc, Sun Prairie, Franklin, Oak Creek, Beloit, Greenfield, Menomonee Falls, Brookfield, Wausau, New Berlin, Fond du Lac, Wauwatosa, Sheboygan*

# ***House & Senate:*** What does the “cap” elimination mean for Community Facilities?

**Because Community Facilities is no longer capped, the gov’t must increase available resources available...how?**

- ▶ ***Senate § 6116 and House § 6203 authorize the Secretary to charge guaranteed loans a fee to offset subsidy costs***

# *House v. Senate: Guaranteed Loan Fees*

**House § 6203(a)** directs the Secretary of the Department of Agriculture to collect fees from **'the recipient** of the insured or guaranteed loan'

**VS.**

**Senate § 6116(a)** directs the Secretary to collect those same fees **from 'the lender.'**

**Issue:** While the recipient of the insured or guaranteed loan described in § 6203 can, and usually will, be the same entity as the lender in § 6117, there is a **substantive difference** between the recipient of the guaranteed loan and the lender of the guaranteed loan

***Best option?***

Leave it to the marketplace to decide who will pay for the subsidy

# *House & Senate: Community Facilities, Health Crisis and Prioritization (1/2)*

The Secretary has the authority to announce a **renewable, one-year, temporary reprioritization** for certain rural development loan and grant applications to assist rural communities in responding to a specific rural health emergency

Prioritizes **loan and grant funding** for development of community facilities that provide **substance use disorder prevention, treatment, and recovery services**

*House: § 6001. Prioritizing projects to meet health crises in rural America.*

*Senate: § 6105. Community Facilities **Direct Loans and Grants** for Substance Use Disorder Treatment Services*

# *House & Senate:* Community Facilities, Health Crisis and Prioritization (2/2)

The Secretary must issue an announcement specifying the emergency, and providing notice to the relevant congressional committees and the Secretary of HHS (House § 6001(b))

## **The “crisis” prioritization would expire either when:**

- ▶ (1) the Secretary has determined that the emergency has ended; or
- ▶ (2) 360 days after the announcement, whichever date is earlier (House § 6001(e))

# *Senate:* Rural Energy for America Program

§ 9107 amends § 9007 of the Farm Security and Rural Investment Act of 2002 to:

- ▶ 1. Reauthorize the Rural Energy for America Program at **\$50 million for each year 2019-2023**; and
- ▶ 2. Maintain mandatory baseline funding of **\$50 million per year**

# *House:* Rural Energy for America Program

§ 6407 amends § 9007(g) of the Farm Security and Rural Investment Act of 2002 by:

- ▶ 1. Authorizing **appropriations of \$20,000,000 per fiscal year**; and
- ▶ 2. Reauthorizing the program through 2023.



# *House & Senate:* Tribal college and university essential community facilities

Provides grant funding to entities that are tribal colleges to provide the federal share of the cost of developing specific tribal college or university essential community facilities

- ▶ Senate § 6104 amends § 306 (a) (25) (C) of the Consolidated Farm and Rural Development Act to **reauthorize** the Tribal College and University Essential Community Facilities Program through 2023

**vs.**

- ▶ House § 6207 amends § 306(a)(25)(C) of the Consolidated Farm and Rural Development Act by **decreasing the authorization** of appropriations to **\$5,000,000** for each fiscal year and reauthorizes the program until 2023

# *House:* Association Health Plans

- ▶ \$65 million in loans and grants to help organizations establish agricultural-related “association” type health plans
- ▶ the secretary of Agriculture may grant **up to 10** loans of **no more than \$15 million** each to existing agricultural associations

**Questions?**