



Aggie Bond Beginning Farmer Loan Program

MINNESOTA AGRICULTURAL DEVELOPMENT ACT

PROGRAM SUMMARY & INSTRUCTIONS

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TABLE OF CONTENTS

<u>Section</u>	<u>Topic</u>	<u>Page</u>
	PROGRAM SUMMARY IN BRIEF	1
	BASIC QUALIFICATIONS	1
I	ELIGIBLE ACTIVITIES	2
	1. Agricultural Land.....	2
	2. Agricultural Improvements.....	2
	3. Depreciable Agricultural Property.....	2
II	INELIGIBLE ACTIVITIES	2
	1. Refinancing Existing Debt.....	2
	2. Finance Working Capital.....	2
	3. Finance the Acquisition of Property.....	2
	4. Finance a Contract Sale Between Close Relatives.....	2
	5. Rural Residence.....	3
	6. CRP Land.....	3
	7. Rental of Project.....	3
	8. Ineligible Animals.....	3
III	APPLICANT ELIGIBILITY	3
	1. Age Limits.....	3
	2. First-Time Farmer.....	3
	3. Net Worth.....	3
	4. Residence.....	3
	5. Training and Experience.....	3
	6. Use of Project.....	3
	7. Enrollment in a Farm Business Management Program.....	4
	8. Consult with Board of Water and Soil Resources.....	4
IV	APPLICATION AND PROCEDURES	4
	1. Signing a Purchase Agreement.....	4
	2. Loan Risk / Credit Evaluation.....	4
	3. Submitting an Application.....	4
	A. Application Period.....	5
	B. Complete Application.....	5
	a. Aggie Bond Application Form.....	5
	b. Financial Statement.....	5
	c. Personal History Letter.....	5
	d. Fees.....	5
	4. Additional Procedures.....	5
	A. Terms of Loan.....	5
	B. Maximum Loan Maturity.....	5
	C. Interim Financing.....	6
	D. Public Hearing and Governor's Approval of Bond Issuance.....	6
	5. Loan Closing Procedures.....	6
	A. Preparation of Bond Documents.....	6
	B. Prepare for Loan Closing.....	6
	C. Prepare Final Closing Documents.....	6
	D. Verify Returned Closing Documents are Complete.....	6

TABLE OF CONTENTS – cont.

<u>Section</u>	<u>Topic</u>	<u>Page</u>
	6. Issuance of Bond.....	6
	7. Procedures Following Bond Issuance.....	7
	A. Timing Requirements for Spending Bond Proceeds.....	7
	B. Prepayment of Loans.....	8
	C. Assumption of Loans-Substitution of Collateral and Transfer of Property...	8
	D. Assignment or Sale of Bonds.....	8
	E. Modified Accelerated Cost Recovery System Limitations.....	8
V	DETAILS FOR SALES CONTRACTS.....	9
	1. Sales Contracts and Security Arrangements.....	9
	2. Terms of the Sales Contract.....	9
	3. Payments Under the Sales Contract.....	9
	4. Closing Documents.....	9
VI	BONDHOLDER INFORMATION.....	9
	1. General Tax Exemption of Bonds.....	9
	2. Investments by State Banks.....	9
	3. Investments by National Banks.....	9
	4. Right to Audit.....	10
VII	DEFINITIONS.....	10
	Agricultural Improvements.....	10
	Agricultural Land.....	10
	Application.....	10
	Beginning Farmer.....	10
	Bond Purchaser.....	10
	Depreciable Agricultural Property.....	10
	Farm.....	10
	Farming.....	10
	Lender.....	10
	Low or Moderate Net Worth.....	10
	Net Worth.....	11
	Total Assets.....	11
	Total Liabilities.....	11
	FEDERAL TAX LAW DEFINITIONS.....	11
	First-Time Farmer.....	11
	Indirect Land Ownership.....	11
	Related Person.....	11
	Substantial Farmland.....	11
	CONCLUDING NOTE.....	12
	APPENDIX	
	Aggie Bond Interest Rate Pricing.....	13

PROGRAM SUMMARY

INDIVIDUAL AGRICULTURAL DEVELOPMENT BOND PROGRAM

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THE PROGRAM SUMMARY IN BRIEF

The Agricultural Development Bond Program, more commonly known as Minnesota's Aggie Bond Beginning Farmer Loan Program (the "Program"), is a tax exempt bond program designed to assist Beginning Farmers in the state of Minnesota to acquire agricultural property at lower interest rates.

The Program enables Lenders and Sellers (if financed by a contract for deed) to receive interest that is exempt from Federal and, in some cases, Minnesota income taxation on loans made to Beginning Farmers. The Lender will make the loan by purchasing from the Rural Finance Authority (the "Authority") a federally tax-exempt Private Activity Bond (PAB) in the amount of the loan. The proceeds of that bond will be lent to the Beginning Farmer by the Authority, and that loan and its collateral will be assigned to the Lender as security for the tax exempt bond.

BASIC QUALIFICATIONS

- Net worth of \$851,000 or less.
- May not have previously owned any substantial amount of farmland.
- Property may be purchased from, but not financed by, a related person.
- Program may be used to purchase agricultural land, agricultural improvements, and depreciable agricultural property.
- No more than an aggregate amount of \$543,800 may be borrowed.
- Of the possible \$543,800, no more than \$62,500 can be "used" Property. Also, no more than \$250,000 can be used for purchasing new depreciable farm property.
- There is no minimum loan amount for the Program.
- Labor must be performed by, and management provided by the Beginning Farmer, his or her co-applicant, and/or minor children and may not cash rent or custom hire a majority of the field work or livestock management to be completed.
- Beginning Farmer must be an individual. Loans to corporations, LLC's, etc. are ineligible under the Federal Tax Code. (If a loan is sought with respect to a partnership, each partner must apply separately as individuals).

The Bond Purchaser will make a credit evaluation of the Beginning Farmer, may require any collateral deemed necessary and, with the Beginning Farmer, must arrange the terms of the loan or contract. Neither the loan, the contract, nor the bond will be the Authority's obligation, and the bond will be secured solely by the loan or contract and collateral provided by the Beginning Farmer. The Bond Purchaser will be responsible for the creation and perfection of any security interest deemed necessary for the loan or contract.

A loan made under the Program is funded solely from the bond issued to the Bond Purchaser. The Authority does not provide independent funds to finance the bank loan/contract sale. Therefore, a Beginning Farmer must submit an application with a Bond Purchaser (bank or contract seller) who is able to purchase the Authority's bond to fund the Beginning Farmer's loan. The Authority shall not be liable or responsible for the

failure of a Bond Purchaser to purchase a bond or otherwise perform the functions of a lender. Nor shall the Authority be liable or responsible for the failure of a Beginning Farmer to locate an alternate Bond Purchaser in the event of a failure of performance by the Beginning Farmer's initial Bond Purchaser.

SECTION I

ELIGIBLE ACTIVITIES

Eligible activities (only for persons who are First-Time Farmers) consist of financing purchases of the following:

1. **Agricultural Land** -- The Authority can finance the purchase of land suitable for use in farming.
2. **Agricultural Improvements** -- The Authority can finance the construction or purchase of improvements located on Agricultural Land (which are suitable for use in farming). Examples: Confinement systems for swine, cattle or poultry; barns and other out-buildings; grain storage facilities; silos; improvements to land such as tiling and soil conservation practices which could include, but not be limited to, terraces, farm ponds, erosion control structures, waterways, etc. Agricultural Improvements may be new or used, and may include additions to or renovation of existing buildings or other structures. There are restrictions regarding the financing of a personal residence on a farm.
3. **Depreciable Agricultural Property** -- The Authority can finance the purchase of personal property suitable for use in farming for which an income tax deduction for depreciation is allowed in computing Federal income taxes. Examples: Livestock used for breeding or dairy purposes, farm machinery, trucks, etc. Feeder cattle, feeder pigs, or feeder lambs do not qualify as depreciable property. Within certain limitations, bond proceeds may be used to finance new or used Depreciable Agricultural Property. "Used" livestock are female animals that have produced offspring or are male animals that have been used for breeding purposes. Open or bred heifers, gilts, or lambs would not be considered "used" property under this definition (this class of animals would be considered "new" property). Male animals that have not been used for breeding purposes would also be considered "new" property.

SECTION II

INELIGIBLE ACTIVITIES

The Internal Revenue Service has promulgated many rules and regulations governing the use and sale of tax-exempt bonds, some of which apply to the Authority's Program. The rules that will affect the Program most are those stating that **tax-exempt bond proceeds cannot be used to:**

1. **Refinancing Existing Debt** - that has been incurred by the Beginning Farmer prior to 60 days within the Authority's board approval of a Program application.
2. **Finance Working Capital** - to purchase feed, seed, fertilizer, fuel, etc. (Feeder cattle, feeder pigs or feeder lambs would also fall into this category.)
3. **Finance the Acquisition of Property** - for individuals other than First-Time Farmers.
4. **Finance a Contract Sale between Beginning Farmer and Grandparent, Parent or Sibling** - Federal tax law does not allow tax-exempt bonds to be issued to close relatives. The purchase of land, improvements or equipment from close relatives must be financed through a third party lender in order to be eligible.

5. **Rural Residence** - the purchase of only a house is not permitted. However, if the house is a minor part of a farm or acreage purchase it can be included as a part of the loan. No more than 5 percent of the bond proceeds can be used toward the purchase of the house.
6. **CRP Land** - the purchase of farmland that is entirely enrolled in CRP is not permitted. Depending on whether a portion of bond proceeds are financing a house (not to exceed 5 percent) 20-25% of the bond proceeds may be used to purchase CRP acres.
7. **Rental of Project** – labor must be performed by and management provided by the Beginning Farmer, his or her co-applicant, and/or minor children and may not cash rent or custom hire a majority of the field work or livestock management to be completed.
8. **Ineligible Animals** – feeder cattle, feeder pigs, feeder lambs, chickens, or turkeys as they do not qualify as depreciable property and, as a result, are not eligible under the program. Other animals that would be ineligible under the program would include horses and those classified as “exotic” such as llamas, fallow deer, ostriches and emus.

The Beginning Farmer, or any related person, shall not make any expenditures with respect to the acquisition or construction of any part of the Project prior to 60 days of the date the Authority board approves the Application. To do so runs a risk that the IRS would deem the bond transaction an ineligible reimbursement; tax-exempt bond proceeds may not be used for the purpose of an ineligible reimbursement.

Notwithstanding the foregoing, approval of an Application *does not* constitute final bond approval. The Authority reserves the right to cease bond processing at any time or to reduce the permitted bond amount if, prior to bond closing, it is discovered that the Beginning Farmer is refinancing an existing loan, or if due to the implementation of, or changes in federal or State law or regulations, it is determined that the Project is ineligible.

SECTION III

APPLICANT ELIGIBILITY

The basic eligibility requirements for the Program are as follows:

1. **Age Limits** -- A Beginning Farmer must be of legal age to own real property under Minnesota law. There is no upper age limit.
2. **First-Time Farmer** -- All Beginning Farmers must be First-Time Farmers regardless of the purpose of the loan. A First-Time Farmer is an individual who has never had any direct or indirect ownership interest in Substantial Farmland in the operation of which he/she has materially participated. An ownership interest or material participation by an individual’s co-applicant or minor child will be attributed to the individual as well.
3. **Net Worth** -- The Beginning Farmer must meet the net worth requirements.
4. **Residence** -- The Beginning Farmer must be a resident of Minnesota at the time the bond is issued.
5. **Training and Experience** -- The Beginning Farmer must have documented, to the satisfaction of the Lender and the Authority, sufficient education, training or experience in the type of farming operation for which the loan is requested.
6. **Use of Project** – The agricultural land, agricultural improvements, and depreciable agricultural property shall only be used for farming by the individual, the individual’s co-applicant, or the individual’s minor children.

Labor must be performed by, and management provided by, the Beginning Farmer, his or her co-applicant, and/or minor children and may not cash rent or custom hire a majority of the field work or livestock management to be completed.

7. Agree to enroll in a farm business management program approved by the Minnesota Commissioner of Agriculture for at least the first three years of the loan if an approved program is available within 45 miles from the borrower's residence.
8. Agree to consult with a local Board of Water and Soil Resources office and file an approved soil and water conservation plan.
9. May wish to obtain credit life insurance for the amount of the debt incurred to purchase the property.

SECTION IV

APPLICATION AND PROCEDURES

1. Signing a Purchase Agreement

The Beginning Farmer, or any family member, shall not commence acquisition or construction of any part of the Project prior to the date on which the Authority approves the Program Application. To do so runs a risk that the IRS would deem the bond transaction an ineligible reimbursement. Tax-exempt bond proceeds may not be used for the purpose of an ineligible reimbursement. This means that neither the Beginning Farmer nor any family member can enter into any contract or purchase agreement, installment or otherwise, in connection with the project or any part thereof prior to the Authority's approval of the Application.

Therefore, the Beginning Farmer should make application to, and obtain Authority approval, before signing a purchase offer or an offer to buy. However, the Beginning Farmer may sign a purchase offer or other contract prior to obtaining Authority approval, if the following three conditions are met:

- 1) it clearly states the purchase is subject to approval of the Authority;
- 2) the risk of loss remains with the seller; and
- 3) the Authority approval is obtained prior to the Beginning Farmer taking possession of the property.

2. Loan Risk / Credit Evaluation

THE LENDER OR CONTRACT FOR DEED SELLER MUST MAKE THE CREDIT EVALUATION OF THE LOAN, THE BEGINNING FARMER'S NET WORTH AND ABILITY TO REPAY PRINCIPAL AND INTEREST AND THE SUFFICIENCY OF THE SECURITY FOR THE LOAN.

THE AUTHORITY WILL NOT MAKE AN INDEPENDENT EVALUATION OF THE BEGINNING FARMER'S ABILITY TO REPAY THE LOAN, OR DETERMINE THE BEGINNING FARMER'S NET WORTH. THE AUTHORITY AND ITS COUNSEL WILL NOT REVIEW AND WILL MAKE NO WARRANTIES OR REPRESENTATIONS WITH RESPECT TO THE LEGAL SUFFICIENCY OR VALIDITY OF THE LOAN OR THE SALES CONTRACT. IN SETTING THE TERMS AND DRAFTING THE LOAN OR SALES CONTRACT, THE BEGINNING FARMER AND BOND PURCHASER ARE STRONGLY ENCOURAGED TO CONSULT THEIR LEGAL COUNSEL AND TAX CONSULTANTS.

Lenders/bondholders should use their own financial statement and other forms deemed necessary to document the eligibility of the Beginning Farmer and his or her ability to repay principal and interest payments.

3. Submitting an Application

A Beginning Farmer and Lender/Bondholder must jointly prepare and submit an Application to the Authority. (Spouse must sign, if appropriate).

- A. **Application Period** -- An application must be received by 4:00 p.m. on the Friday prior to the RFA Board meeting. The RFA Board meets the 1st Wednesday of each month. The application should be in the Authority's office by the close of business Friday before that particular Board meeting.
- B. **A Complete Application** includes the following:

Aggie Bond Application Form -- Application forms are available from the Authority. **The Application should be completed by the Beginning Farmer and Lender/Bondholder and submitted to the Authority.** Applicants and Lenders are encouraged to contact the Authority if they have questions in completing the Application.

Financial Statement -- A copy of the Beginning Farmer's signed financial statement (taken within 60 days preceding Application submission). If a loan is sought with respect to a partnership, separate Applications and financial statements must be submitted by each partner, and an aggregated financial statement covering the partnership and all partners must also be submitted.

NOTE: If the Beginning Farmer and/or spouse are involved in a business, partnership, corporation, etc., either related or unrelated to his/her farming operation, a financial statement from this entity must also be submitted with the Application.

Personal History Letter -- A personal history letter signed by the applicant/s explaining the Beginning Farmer's background with respect to his or her education and experience in the type of farming operation for which a loan is sought. The letter should also outline the Beginning Farmer's access to machinery, if the loan is for land; or his or her access to land, if the loan is for Agricultural Improvements or Depreciable Agricultural Property. The letter should also state where the Beginning Farmer will obtain operating capital, if needed.

Fees -- The Beginning Farmer or Lender/Bondholder must include the following fees:

A bond allocation fee:

\$20.00	loans up to \$149,999
40.00	loans from \$150,000 to \$249,999
60.00	loans from \$250,000 to \$349,999
80.00	loans from \$350,000 to \$449,999
100.00	loans from \$450,000 to \$543,800

In addition, a loan origination fee equal to 1 1/2% of the amount of the loan, but not less than \$200, must be paid at loan closing. The loan origination fee may be paid by either party or 2% of bond proceeds can be used towards the origination fee.

The completed Application will be reviewed and considered by the Authority at the first board meeting after it is received. After the application has received the final approval by the Authority board, documents will be prepared and mailed by the Authority staff for signatures of the Beginning Farmer and Lender.

4. **Additional Procedures**

- A. **Terms of Loan** -- The Beginning Farmer and Lender must agree on terms of the loan such as interest rate, length of loan, prepayment options, service fees and repayment schedule. The Authority reserves the right to withhold approval for a loan containing onerous provisions.
- B. **Maximum Loan Maturity** -- Federal law provides that the weighted average maturity of an Authority bond can be no more than 120% of the average reasonably expected economic life of the project being financed with the proceeds of the bond (except land).

- C. **Interim Financing (does not apply to contract sales)** -- As noted above, a Beginning Farmer must not commence acquisition or construction of any part of the Project prior to the date the Authority approves the Application. If this were to occur, the bond transaction could be deemed an ineligible reimbursement. However, once the Application has been approved, the Project may move forward with either construction or possession. If necessary, the Lender may then interim finance the loan prior to bond issuance. The interim financing (principal only) will be paid with the proceeds of the bond when issued.

The documents also provide for prepayment at the option of the Beginning Farmer under terms and conditions which are to be agreed upon between the Beginning Farmer and the Lender. The documents setting forth optional prepayment contain blanks which need to be completed by the Beginning Farmer and the Lender.

It should be noted that the bond documents may be prepared to provide for a prepayment at the option of the Lender. The terms of this type of prepayment will need to be agreed upon by the Beginning Farmer and the Lender. This prepayment option should be used where a Lender may be willing to extend the initial term of a loan, but wants the ability to review the situation at various points in time and to end the loan if the Beginning Farmer's progress is unsatisfactory (call option).

- D. **Public Hearing and Governor's Approval of Bond Issuance** -- Federal law requires that a public hearing must be held before any Authority bond is issued. A legal notice will be published by the Authority in a newspaper of general circulation at least 14 days prior to the hearing. In addition, any individual may file a written request with the Authority at or prior to the scheduled hearing requesting that a local hearing be held in the area where the project is located.

Generally, these public hearings will be conducted by members of the Authority's staff. A hearing need not be held prior to an Application being approved, but it must be held before the bond documents are approved.

The Governor of Minnesota, after receiving a report on the results of the public hearing, may then approve or disapprove the bond. An allocation of the State's bonding authority must then be received for the bond. Once the final approval from the Governor and the bonding allocation are received, the loan may proceed to closing.

5. **Loan Closing Procedures**

After the Application has received the preliminary and final approval from the Board, and preliminary Bond Counsel attorney's approval, the following steps are needed to complete the loan closing process:

- A. **Preparation of Bond Documents** -- A set of bond documents must be prepared for each loan. These documents will be mailed to the Bond Purchaser for signatures from both the Bond Purchaser and Beginning Farmer. They need to be returned to RFA for Department of Agriculture signatures. Once all necessary signatures have been obtained, the set of bond documents is mailed to the Bond Counsel attorney's office for review and final approval.
- B. **Prepare for Loan Closing** -- When final documents are returned from Bond Counsel and final approval is obtained, the Bond Purchaser or other appropriate individuals are contacted regarding the loan closing date.
- C. **Prepare Final Closing Documents** -- The bond documents and closing papers are dated and finalized. The documents are then sent promptly so they are received prior to the closing date.
- D. **Verify Returned Closing Documents are Complete** -- After loan closing, certain documents need to be returned to the Authority's office.

- 6.. **Issuance of Bond** -- In the case of an institutional or individual lender: In simultaneous transactions the Lender purchases the Bond from the Authority; the Authority makes the loan to the Beginning

farmer from the proceeds of the Bond issue; and the Authority assigns the promissory note and lien it receives from the Beginning Farmer to the Lender as security for the Bond.

In the case of a sales contract (contract for deed): in a simultaneous transaction, the Lender seller will enter into a sales contract with the Authority, the Authority will deliver its Bond to the Lender to evidence the Authority's obligation under the sales contract and the Beginning Farmer will assume the Authority's obligations under the sales contract.

A loan made under the program is funded solely from the bond sold to the Lender. The Authority has no funds to fund a loan. Therefore, a Beginning Farmer must submit an application with a Lender who is able to purchase the Authority's bond to fund the Beginning Farmer's loan. The Authority shall not be liable or responsible for the failure of a Lender to purchase a bond or otherwise perform the functions of a Lender. Nor shall the Authority be liable or responsible for the failure of a Beginning Farmer to locate an alternate Lender in the event of a failure of performance by the Beginning Farmer's initial Lender.

The principal and interest on the bond are limited obligations, payable solely out of the revenue derived from the debt obligation, collateral, or other security furnished by or on behalf of the Beginning Farmer. A guarantor, letter of credit or alternative credit enhancement on the debt is permissible. A guarantor may be a Related Person. **The Bond, which is issued by the Authority and purchased by the Lender, is a non-recourse obligation. The principal and interest on the Bonds ARE NOT secured by a pledge of the credit or the taxing power of the state of Minnesota of the Authority.** It should also be noted that any recording or filing fees or transfer taxes associated with the loan will be paid by the Beginning Farmer or Lender and not the Authority. **Additionally, the Authority will have no responsibility with respect to the preparation, execution, or filing of any Declaration of Value or Groundwater Hazard Statements.**

****IRS Tax Form 8038: "Information Return for Tax-Exempt Private Activity Bond Issues" is filed with the IRS by the Bond Counsel Attorney's Office on behalf of the Bond Holder for both a contract sale and lender loan. This form will need to be provided to your tax preparer as proof of the tax exemption on the interest income earned on the loan when filing taxes. A copy is provided to the Bond Holder once the form is filed. ****

7. **Procedures Following Bond Issuance** -- No bond proceeds may be used for a non-qualified purpose or by a non-qualified user. Following disbursement of the bond proceeds, the Lender and Beginning Farmer must certify that: (i) the Project be used by a "first-time farmer" for a qualified purpose so long as the Bond is outstanding; (ii) the Borrower keeps records relating to the use of proceeds of the bond and to make any rebate payments required to be made under the tax code if proceeds of the Bond are not expended within six months of the bond issuance date; and (iii) the Borrower and the Lender will notify the Authority of any noncompliance and to take any remedial action required to be taken in the event of noncompliance.
 - A. **Timing Requirements for Spending Bond Proceeds** -- Federal tax law restrictions generally do not permit the investment of bond proceeds in securities which bear an interest rate higher than that on the bond.

Under the current rules, the period of time during which bond proceeds may be invested in an unrestricted yield has been effectively shortened to six months. Unless all "Gross Proceeds" of a tax-exempt bond are spent on the project being financed within six months after the date the bond is issued, the parties to the bond issue will be subject to some very onerous Federal reporting requirements and will be required to pay any profits earned on bond proceeds to the Federal government.

To avoid subjecting any of the Authority's bonds to these reporting and payment requirements, it is the policy of the Authority not to issue a bond for a Project until the Authority can be assured that all bond proceeds will be expended on the Project within six months of the date of the bond issuance. In the closing documents the Beginning Farmer and Lender are required to certify that the use of the proceeds will comply with this policy.

LENDERS PLEASE NOTE: IT IS THE LENDER'S RESPONSIBILITY TO INSURE THAT ANY SECURITY AGREEMENTS, MORTGAGES, GUARANTEES OR OTHER SECURITY DOCUMENTS WHICH THE LENDER REQUIRES IN A TRANSACTION HAVE BEEN COMPLETED AND SIGNED; AND THAT ANY FINANCING STATEMENTS HAVE BEEN FILED, MORTGAGES RECORDED OR ANY OTHER NECESSARY STEPS TAKEN TO PROTECT THE BOND PURCHASER'S INTERESTS. THE AUTHORITY MAKES NO WARRANTIES OR REPRESENTATIONS WITH RESPECT TO THE EFFECTIVENESS, VALIDITY OR PRIORITY OF ANY LIENS OR SECURITY INTERESTS, WHICH A LENDER HAS, OR BELIEVES HE/SHE MAY HAVE, WITH RESPECT TO A PARTICULAR PROJECT.

- B. **Prepayment of Loans** -- Under the Authority's documents, the Beginning Farmer's payment obligations are subject to mandatory prepayment: (a) in the event the interest income on the bond becomes includable in gross income for purposes of federal or Minnesota income taxation; (b) in the event that the loan agreement entered into by the Beginning Farmer becomes void or unenforceable, and; (c) to the extent any bond proceeds remain following completion of the acquisition or construction of the Project. In addition, the documents provide for optional prepayment from insurance of condemnation proceeds (at the discretion of the Lender) in the event of damage, destruction, or condemnation of all or any part of the project.
- C. **Assumption of Loans - Substitution of Collateral and Transfer of Property** -- Loans and sale contracts may not be assumed without the prior approval of the Authority, and then only if the purchaser of the property will qualify as a First-Time Farmer. Equipment and other depreciable property may be exchanged or traded in on similar property, and other property such as breeding livestock may be added or substituted as collateral at the discretion of the Lender without the prior approval of the Authority. The benefits of the Authority bond must remain with a qualified First-time Farmer, and no person to whom property is traded or otherwise transferred may obtain the benefits of the bond.
- E. **Assignment or Sale of Bonds** -- The Authority does not place any restrictions on the Lender's/Contract Sellers ability to participate out, assign or sell a bond issued under the Program. It should be noted there are laws that prevent certain sales and participations, or at least seriously restrict them. Therefore, Lenders/Contract Sellers should consult with their legal counsel to determine if any of these laws or regulations will be violated before selling, assigning, or participating out a bond. In addition, there are certain adverse tax consequences if the bond is assigned, participated out or sold to a Related Person of the Beginning Farmer. Servicing of the loan may also be assigned, but must at all times be with a participating Lender as defined in Rules of the Authority. The Authority must be notified in writing prior to assignment of servicing of the loan.
- E. **Modified Accelerated Cost Recovery System Limitations** -- Lenders and Beginning Farmers should be aware that Federal law limits the application of the Modified Accelerated Cost Recovery System (MACRS) with respect to facilities financed with the Authority's bonds. If an item is financed with the proceeds of a bond, the Beginning Farmer must use an alternative MACRS method where deductions are computed by applying the straight line method, the applicable averaging convention, and the applicable longer recovery period for such item (12 years for personal property with no class life, 40 years for real property, and the class life for all other property).

NOTE: Beginning Farmers should contact their tax consultant regarding the specific effect this change in the MACRS will have on their operations or Project.

SECTION V

DETAILS FOR SALES CONTRACTS

NOTE: This section applies specifically to transactions involving a sales contract from the contract seller to the Beginning Farmer. This section should be disregarded if the Bond Purchaser is a lender.

1. **Sales Contracts and Security Arrangements** – The Program involves the Bond Purchaser, Beginning Farmer and the Authority. After an Application has been submitted and approved, the Bond Purchaser and the Authority will enter into a sales contract and the Bond Purchaser will receive a bond to evidence the Authority's obligations under the contract. The Beginning Farmer assumes the payments and other obligations of the Authority under the contract.
2. **Terms of the Sales Contract** – It must be clearly stated in the sales contract as to the portion of the payments constituting principal and the portion constituting interest (the "Tax-Exempt Rate"). *(Contact RFA for a copy of the Aggie Bond contract for deed form used for your review.)*
3. **Payments Under the Sales Contract** – The Beginning Farmer's payment obligations and rights and obligations to prepay principal and interest under the sales contract shall be determined by the Beginning Farmer and Bond Purchaser and included in the sales contract.
4. **Closing Documents** – The Authority will have no responsibility with respect to the preparation, execution, or filing of any declaration of value statements, groundwater hazard statements, or any other forms or documents as may be required to finalize the transaction.

SECTION VI

BONDHOLDER INFORMATION

1. **General Tax Exemption of Bonds** -- Under Federal tax law, an Authority bond is classified as a Qualified Small Issue Bond. Therefore, if all the provisions of the state and federal law continue to be complied with by the Beginning Farmer and Lender, the interest on an Authority bond will not be included in the bondholder's gross income for federal income tax purposes or taxable net income of individuals, estates or trusts for Minnesota income tax purposes.

Notwithstanding the preceding paragraph, interest on the bonds is includable in taxable income of corporations and financial institutions for purposes of the Minnesota franchise tax, is an item of tax preference includable in alternative minimum taxable income for purposes of the federal alternative minimum tax applicable to all taxpayers and the Minnesota alternative minimum tax applicable to individuals, estates and trusts, and is includable in adjusted current earnings of corporations in determining alternative minimum taxable income for purposes of the federal alternative minimum tax imposed on corporations.

2. **Investments by State Banks** -- Minnesota Statutes contain certain limitations on the investments of state banks and trust companies. State banks and trust companies should review such limitations to assure themselves they are authorized to participate in the Program.
3. **Investments by National Banks** -- A national bank may not invest in bonds issued under the Program on behalf of any one Beginning Farmer in an amount greater than its lending limits as set forth in 12 U.S.C. 84 (generally this is 30% of the bank's capital structure). This investment limit is separately applied to each Beginning Farmer as a separate obligor. An Authority loan will count against a Beginning Farmer's lending limit with a national bank.

4. **Right to Audit** -- The Authority shall, at any time, have the right to audit or monitor records of the Lender and the Beginning Farmer relating to a loan and bond to insure the bond proceeds were used for qualified purposes by a qualified user.

SECTION VII

DEFINITIONS

"Agricultural Improvements" means improvements, buildings, structures or fixtures suitable for use in farming located on Agricultural Land. Agricultural Improvements as defined in Minnesota Statutes, Section 41C.02 include a single family dwelling located on Agricultural Land that is or will be occupied by the Beginning Farmer and structures attached to or incidental to the use of the dwelling.

NOTE: The ability to finance a personal residence with the Program is severely limited due to federal regulations governing the use of the Authority's bonds; therefore, except in certain circumstances (e.g., when the value of the residence is clearly less than 5% of the amount of the loan or the amount of contract financed), it will be necessary to finance a personal residence separately.

"Agricultural Land" means land suitable for use in farming and which is, or will be, operated as a farm located in the state of Minnesota.

"Application" means a completed instrument on a form approved by the Authority. Each application must include the following: Beginning Farmer's name, address, financial data, description of anticipated use of loan proceeds, amount of loan, down payment amount (if any), statement of Beginning Farmer's net worth determined in accordance with Authority rules, a summary of proposed loan terms and certain certifications of the Beginning Farmer and Bond Purchaser.

"Beginning Farmer" means an individual or partnership with a low or moderate net worth that engages in farming or plans to engage in farming.

"Bond Purchaser" means any individual, lender, corporation, government or governmental subdivision or agency, business trust, estate, trust, partnership or association, or any other legal entity that obtains an Authority bond under the Program in connection with a contract sale or loan to a Beginning Farmer.

"Depreciable Agricultural Property" means personal property suitable for use in farming for which an income tax deduction for depreciation is allowable in computing federal income tax under the Internal Revenue Code of 1986, as amended.

"Farm" means a farming enterprise which is recognized in the community as a farm rather than a rural residence.

"Farming" means the cultivation of land for the production of agricultural crops, the raising of poultry, the production of eggs, the production of milk, the production of fruit or other horticultural crops, grazing, the production of livestock, aquaculture, hydroponics, the production of forest products, or other activities designated by the Authority's rules.

"Lender" means a bank, credit union, savings and loan association, insurance company, or other financial institution that is authorized to do business in Minnesota, which the Authority determines has sufficient personnel and other resources to efficiently and properly originate and service qualified agricultural loans or an individual may be a Lender in the Program.

"Low or Moderate Net Worth" means:

- a. For an individual, an aggregate net worth of the individual and the individual's spouse and minor children of less than \$851,000;

- b. For a partnership, an aggregate net worth of all partners, including each partner's net capital in the partnership, together with each partner's spouse and minor children of less than \$1,633,600. However, the aggregate net worth of each partner and that partner's spouse and minor children may not exceed \$851,000.

"Net Worth" means total assets minus total liabilities as determined in accordance with generally accepted accounting principles with appropriate exceptions and exemptions reasonably related to an equitable determination of the Beginning Farmer's or partnerships net worth. Assets shall be valued at fair market value.

"Total Assets" shall include, but not be limited to, the following: cash crops or feed on hand; livestock held for sale; breeding stock; marketable bonds and securities; securities (not readily marketable); accounts receivable; notes receivable; cash invested in growing crops; net cash value of life insurance; machinery and equipment; cars and trucks; farm and other real estate including life estates and personal residence; value of a beneficial interest in a trust; government payments or grants; and other assets. Total assets shall not include items used for personal, family or household purposes by the applicant, but in no event shall such property be excluded to the extent a deduction for depreciation is allowable for Federal income tax purposes. All assets shall be valued at fair market value by the participating Lender. Such value shall be what a willing buyer would pay a willing seller in the locality. A deduction of ten percent may be made from fair market value of farm and other real estate.

"Total Liabilities" shall include, but not be limited to, the following: accounts payable, notes or other indebtedness owed to any source, taxes, rent, amount owed on a real estate contract or real estate mortgages, judgments, accrued interest payable, any other liabilities. Liabilities are to be determined on the basis of generally accepted accounting principles.

The Federal tax law contains definitions which affect the Program and Beginning Farmers. They are as follows:

"First-Time Farmer" (This is different than a Beginning Farmer) is a person who has never had any direct or indirect ownership interest in "Substantial Farmland" in the operation of which he or she has materially participated. An ownership interest or material participation by a person's spouse or minor child will be attributed to the person as well.

However, the Federal tax law also provides that a person's prior ownership interest in farmland will be disregarded if:

- a. Such farmland was disposed of while the person was insolvent; and
- b. Section 108 of the Internal Revenue Code applied to indebtedness with respect to such farmland; that is, the person was not required to recognize any income for Federal tax purposes from the cancellation of the indebtedness on the farmland.

"Indirect Land Ownership" - If a person holds a minimal interest in a family farm corporation, a limited partnership, a trust, or any other type of entity which in turn owns farmland in an amount which is greater than 30 percent of the median size of a farm in the county in which the farm is located and the person materially participates in the operation of such farmland, then the person will not qualify as a First-Time Farmer.

"Related Person", according to the IRS, includes grandfather, grandmother, father, mother, brother or sister (whether whole or half-blood), child, grandchild, or spouse. It also includes certain corporations and partnerships. Certain in-laws may be eligible.

"Substantial Farmland" - Any parcel of land is Substantial Farmland unless:

- a. The parcel is smaller than 30 percent of the median size of a farm in the county where the parcel is located. (Note: If applicants previously purchased land jointly with another party, they need to report

the number of gross acres of the entire tract and not their proportion of acres purchased. To be eligible, the total amount of acres of the combined purchase must fall below 30% of the median size farm in the respective county.)

CONCLUDING NOTE: The Authority recognizes some of the provisions in this Program Summary may be confusing to the Beginning Farmer or Lender. The Authority will provide whatever assistance it can in answering questions or completing documents. Beginning Farmers and Lenders are encouraged to visit with the Authority staff early in the application process to make the entire transaction as simple as possible.

01/19

AGGIE BOND INTEREST RATE PRICING

The tax-exempt interest income earned by lenders and contract sellers enables them to charge the beginning farmers a lower interest rate.

Comparative Pricing – Bond vs. Conventional

Step 1

First, calculate net after tax yield on a conventional loan

Conventional Rate	8.50%
Minus Cost of funds	4.50%*
Equals Gross Margin	4.00%
Times (1-tax rate)	.66
Equals net after tax yield	2.64%

*Cost of funds as a percent of assets

Step 2

Add net after tax yield to cost of funds to determine Tax-exempt Equivalent*

Net after tax yield	2.64%
Plus Cost of Funds	4.50%*
Equals Tax-exempt Equivalent	7.14%

Aggie Bonds are considered “non-bank qualified”. Therefore, the interest expense of carrying the bond is disallowed from lender’s ordinary expenses for income tax purposes. Lenders are advised to check with their tax consultants.