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A Guide to Borrower Litigation against the Farm Credit System and the Rights of Farm Credit System Borrowers

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A GUIDE TO BORROWER LITIGATION AGAINST THE FARM CREDIT SYSTEM AND THE RIGHTS OF FARM CREDIT SYSTEM BORROWERS†

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I. INTRODUCTION

The farm financial crisis of the 1980's has produced and continues to produce an unprecedented amount of litigation against the lending institutions of the Farm Credit System by the owners of those institutions, their borrowers. Although no single characterization of the substance of the claims made by those borrowers can be all-encompassing, the gist of most claims has been that the Farm Credit System lender behaved imprudently or unfairly in the servicing, including foreclosure, of the borrower's loans. Coinciding with that litigation have been entreaties to Congress to mandate changes in the ways in which Farm Credit System lenders deal with their borrowers. As a result, the 1980's produced dramatic revisions in the organic law governing the Farm Credit System.

This article will survey both the recent litigation against Farm Credit System lenders and the statutory and judicially created rights of the borrowers of those institutions. In doing so, this article's intent is to provide the reader with a succinct, but reasonably complete, primer on its subject. The article is structured topically to facilitate the reader's access to issues of particular interest. Although exhaustive treatment of the myriad issues that have arisen in borrower litigation against the Farm Credit System is beyond the scope of this article, greater attention is devoted to the

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more significant or problematic issues. For those issues in particular, this article references additional sources of guidance or information.[1]

If for no other reason, the legal aspects of the relationship between Farm Credit System lenders and their borrowers are important because, until 1987, the Farm Credit System was the nation's "largest single provider of credit to farmers, ranchers, and their cooperatives."[2] For most of the last decade, Farm Credit System lenders have shared roughly one-third of the farm loan market.[3] Accordingly, the behavior of Farm Credit System lenders has a significant impact on the financial well being of agricultural producers who are permanently or periodically reliant on credit.[4]

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1. At various points in this article, note is made of the unsettled nature of the issue discussed. Because the jurisprudence governing the Farm Credit System continues to develop, the reader is urged to be attentive to developments post-dating this article.

In addition to the usual sources for recent developments, there are at least three periodicals that provide coverage of Farm Credit System litigation. The AGRICULTURAL LAW UPDATE, a monthly publication of the American Agricultural Law Association, is available through membership in the AALA, Robert A. Leflar Law Center, University of Arkansas, Fayetteville, AR 72701. The IOWA AGRICULTURAL LAW REPORTER is available from the Agricultural Law Center, The Law School, Drake University, Des Moines, IA 50311. The FARMERS' LEGAL ACTION REPORT is available from the Farmers' Legal Action Group, Inc., 1301 Minnesota Building, 46 East Fourth Street, St. Paul, MN 55101. A fourth publication, THE AGRICULTURAL CREDIT LETTER, published by Webster Communications Corporation, P.O. Box 9153, Arlington, VA 22209, offers twice monthly coverage of various matters affecting the System. Unlike the first three publications, THE AGRICULTURAL CREDIT LETTER primarily covers institutional developments within the System, and its coverage of litigation is generally limited to cases that affect the System as a whole.

2. H.R. 295 (I), 100th Cong., 1st Sess. 54, *reprinted in* 1987 U.S. CODE CONG. & ADMIN. NEWS 2723, 2726. "In 1987, commercial banks surpassed the Farm Credit System as the principal holder of combined real estate and non-real estate farm debt." ECON. RESEARCH SERV., USDA, PUB. NO. AFO-33, AGRICULTURAL INCOME AND FINANCE: SITUATION AND OUTLOOK REPORT 13 (May 1989)[hereinafter AGRICULTURAL INCOME AND FINANCE].

3. Boehlje & Pederson, *Farm Finance: The New Issues*, CHOICES, Third Quarter 1988, at 16,17 [hereinafter Boehlje & Pederson]. Since 1980, the Farm Credit System has shared close to or over one-third of the farm loan market, although that share is declining. In 1980, the System held a thirty-two percent share of the farm loan market. That share increased to thirty-four percent in 1983. However, in 1986, the System's share declined to twenty-nine percent. By way of comparison, in 1986, commercial banks held a twenty-six percent market share, life insurance companies held six percent, the Farmers Home Administration held fifteen percent, and individuals and others shared twenty-three percent of the farm loan market. *Id. See also* Jensen, *Agricultural Lending in the 1980's: An Insurance Company's Perspective*, 18 MEM. ST. U.L. REV. 353, 354 (1988) (discussing agricultural lending by insurance companies in the 1980s). By 1989, the System's market share had declined to less than twenty-seven percent while the share of commercial banks had increased to thirty-two percent. AGRICULTURAL INCOME AND FINANCE, *supra* note 2, at 13-14. For an account of the recent competition for borrowers between Farm Credit System institutions and commercial banks, see Webster, *Interest Rate Turf Battles: Farm Credit Versus the Commercial Banks*, AGRIFINANCE, Dec. 1989, at 18. *See also* S. 2830, 100th Cong., 2d Sess., 136 CONG. REC. S11,232, S11,314 (1990) (a directive in the Senate version of Food, Agricultural, Conservation, and Trade Act of 1990 (informally referred to as the 1990 farm bill) for a General Accounting Office study of rural credit cost and availability including a review of the interest rates of System lenders).

4. For discussions of the reliance of farmers on debt financing, see *e.g.*, T. FREY & R. BEHRENS, LENDING TO AGRICULTURAL ENTERPRISES (1981); M. STRANGE, FAMILY

In a general sense, the legal aspects of the relationship between Farm Credit System lenders and their borrowers are colored and occasionally complicated or confused by four fundamental attributes of Farm Credit System lenders. First, Farm Credit System lenders are federally chartered.[5] Second, as federally chartered institutions, Farm Credit System lenders are subject to regulation by the Farm Credit Administration [hereinafter FCA], an agency of the federal government with authority and power generally equivalent to other federal financial regulators.[6] Third, Farm Credit System lenders must operate within the confines of the statutory authority underlying their federal charters, the Farm Credit Act of 1971, as amended.[7] Finally, although they are federally chartered entities, regulated by a federal agency, and

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FARMING: A NEW ECONOMIC VISION 104-26 (1988); N. Harl, *The Financial Crisis in the United States*, in IS THERE A MORAL OBLIGATION TO SAVE THE FAMILY FARM? 115-16 (G. Comstock ed. 1987) (a similar discussion can be found at Harl, *The Architecture of Public Policy: The Crisis in Agriculture*, 34 KANSAS L. REV. 425, 426-32 (1986)); Baker, *Structural Issues in U.S. Agriculture and Farm Debt Perspectives*, 34 U. KAN. L. REV. 457 (1986); Boehlje & Pederson, *supra* note 3, at 16-17; Roberts, *Deregulating the Agricultural Industry: A Wise Policy Choice?*, 12 J. CONTEMP. L. 49, 59-61 (1986); Kelley, *Imposing the Duties of Fairness, Good Faith, and Honesty On the Agricultural Lender*, ARK. L. NOTES 18, 18-19 (1987) [hereinafter Kelley].

5. 12 U.S.C.A. §§ 2002(a), 2011(a), 2071(a), 2091(a) (West 1989).

6. 12 U.S.C.A. §§ 2241-74 (West 1989). The FCA is "an independent agency in the executive branch. . . ." 12 U.S.C.A. § 2241 (West 1989). *See also* 12 C.F.R. pt. 600 (1990) (setting forth the organizational structure and the functions of the FCA). For summaries of the current responsibilities of the FCA, see Kayl, *Farm Credit Amendments Act of 1985: Congressional Intent, FCA Implementation, and Courts' Interpretation (And the Effect of Subsequent Legislation on the 1985 Act)*, 37 DRAKE L. REV. 271, 285-300 (1987-88) [hereinafter Kayl]; Dewey, *The Farm Credit System*, 36 FED. B. NEWS & J. 287 (1987) [hereinafter Dewey]. *See also* Massey & Schneider, *Title I of the Agricultural Credit Act of 1987: "A Law in Search of Enforcement"*, 23 U.C. DAVIS L. REV. 589, 613-14 (1990)(criticizing the FCA's lack of enforcement of the rights of System borrowers) [hereinafter Massey & Schneider]; *infra* notes 78-80, 100 and the accompanying text (discussing in greater detail the responsibilities of the FCA).

7. As amended to date, the statutory authority for the Farm Credit System is found at 12 U.S.C.A. §§ 2001-2279 (West 1989 & Supp. 1990). As is discussed in greater detail in various portions of this article, the Farm Credit Act of 1971, Pub. L. No. 92-181, 85 Stat. 583, has been substantially amended four times, specifically by the Farm Credit Act Amendments of 1980, Pub. L. No. 96-592, 94 Stat. 3437; the Farm Credit Amendments Act of 1985, Pub. L. No. 99-205, 99 Stat. 1678; the Omnibus Budget Reconciliation Act of 1986, Pub. L. No. 99-509, 100 Stat. 1874; and the Agricultural Credit Act of 1987, Pub.L. No. 100-233, 101 Stat. 1568-1717 (1988). Technical corrections were made to the Agricultural Credit Act of 1987 by the Agricultural Credit Technical Corrections Act of 1988, Pub. L. No. 100-399, 102 Stat. 989. *See also* Rural Development, Agriculture, and Related Agencies Appropriation Act of 1989, Pub. L. No. 100-460, 102 Stat. 2229, 2266 (1988) (amending section 6.29 of the Farm Credit Act of 1971); Act of Dec. 12, 1989, Pub. L. No. 101-220, 103 Stat. 1876, 1879-81 (amending sections 5.55 and 6.29 of the Farm Credit Act of 1971 and section 646 of the Rural Development, Agriculture, and Related Agencies Appropriations Act of 1989).

This article was prepared prior to the enactment of the 1990 farm bill. The Senate version of that legislation, the Food, Agriculture, Conservation, and Trade Act of 1990, proposes several amendments to the Farm Credit Act of 1971. S. 2830, 101st Cong., 2d Sess., 136 CONG. REC. S11,232, S11,314-316 (1990). Only one of those amendments, a provision for production credit association first liens on borrower stock and participation certificates in the association, directly affects the rights of System borrowers. *Id.* at S11,314.

subject to Congressionally imposed limits of authority and other requirements, Farm Credit System lenders are neither owned nor managed by the federal government. Rather, they are owned on a cooperative basis by their member-borrowers.[8] Those four fundamental attributes must be understood and appreciated for it is their presence and the interplay among them that gives the law governing the relationship between Farm Credit System lenders and their borrowers its uniqueness.

Because the four attributes essentially arise from the statutory purposes, history, and structure of the Farm Credit System, this article begins with a discussion of those purposes and that history and structure. The article next focuses on the unique issues that have arisen in litigation by borrowers against System lenders and the various statutory "borrowers' rights" available to System borrowers. Finally, the article concludes with some thoughts and comments on the future of Farm Credit System lenders and their relationships with their borrowers.

II. THE PURPOSE OF THE FARM CREDIT SYSTEM

The objective of the Farm Credit System has been defined as the satisfaction of ". . . the peculiar credit needs of American farmers and ranchers while encouraging those farmers and ranchers to participate through management, control, and ownership of the

8. Borrower ownership was achieved by conditioning borrowing on the purchase of stock in the local association either making or servicing the loan. In turn, the associations purchased stock in the "upstream," supervisory bank, a federal land bank or federal intermediate credit bank (now merged as district farm credit banks). When the initial capitalization by the federal government was repaid, the System became wholly owned and controlled by its borrowers. *See infra* notes 15-36 and the accompanying text. *See generally* FREY & BEHRENS, *supra* note 4, at 385-97 (describing how the System's borrowers became the owners of the System through the purchase of stock in federal land bank and production credit associations); W. LEE, M. BOEHLJE, A. NELSON, & W. MURRAY, AGRICULTURAL FINANCE 354-69 (7th ed. 1980) (same).

Occasionally, the stock purchase requirement is incorrectly or loosely stated when a federal land bank loan is at issue. For example, in *In re* Massengill, 100 Bankr. 276 (E.D. N.C. 1988), the court referred to the borrower's stock as "Land Bank stock". 100 Bankr. at 278. However, the court also expressly noted that the stock had been purchased in the federal land bank association, not in the federal land bank. 100 Bankr. at 278 & n.1. Other courts have simply stated incorrectly that the borrower had purchased stock in the federal land bank. *E.g.*, *In re* Cansler, 99 Bankr. 758, 759 (W.D. Ky. 1989). At least one court has admitted uncertainty about the stock purchase requirement. *In re* Shannon, 100 Bankr. 913, 916 n.9 (S.D. Bankr. Ohio 1989).

Prior to the effective date of the Agricultural Credit Act of 1987, borrowers who obtained federal land bank funds had to apply for a loan through a federal land bank association and purchase stock in the association. *See* 12 U.S.C.A. § 2016 (West 1980). Currently, borrowers who reside in an area not served by a federal land bank association may borrow directly from the successor to the federal land bank in each district, the farm credit bank, after purchasing stock in the respective farm credit bank. 12 U.S.C.A. §§ 2017, 2021(b) (West 1989). *See also infra* notes 119-34 and the accompanying text (discussing the restructuring of the System resulting from the Agricultural Credit Act of 1987).

system."[9] The Congressional expression of the policy and objectives of the Farm Credit System is as follows:

> (a) It is declared to be the policy of the Congress, recognizing that a prosperous, productive agriculture is essential to a free nation and recognizing the growing need for credit in rural areas, that the farmer-owned cooperative Farm Credit System be designed to accomplish the objective of improving the income by furnishing sound, adequate, and constructive credit and closely related services to them, their cooperatives, and to selected farm-related businesses necessary for efficient farm operations.
>
> (b) It is the objective of this chapter to continue to encourage farmer- and rancher-borrowers participation in the management, control, and ownership of a permanent system of credit for agriculture which will be responsive to the credit needs of all types of agricultural producers having a basis for credit, and to modernize and improve the authorizations and means for furnishing such credit and credit for housing in rural areas made available through the institutions constituting the Farm Credit System as herein provided.
>
> (c) It is declared to be the policy of Congress that the credit needs of farmers, ranchers, and their cooperatives are best served if the institutions of the Farm Credit System provide equitable and competitive interest rates to eligible borrowers, taking into consideration the creditworthiness and access to alternative sources of credit for borrowers, the cost of funds, including any costs of defeasance under section 4.8(b), the operating costs of the institution, including the costs of any loan loss amortization under section 5.19(b), the cost of servicing loans, the need to retain earnings to protect borrowers' stock, and the volume of net new borrowing. Further, it is declared to be the policy of Congress that Farm Credit System institutions take action in accordance with the Farm Credit Act Amendments of 1986 in such manner that borrowers from the institutions derive the greatest

9. Daley v. Farm Credit Admin., 454 F. Supp. 953, 954 (D. Minn. 1978).

> benefit practicable from that Act: *Provided*, That in no case is any borrower to be charged a rate of interest that is below competitive market rates for similar loans made by private lenders to borrowers of equivalent creditworthiness and access to alternative credit.[10]

The policy and objectives assigned to the Farm Credit System reflect that the System was created as a result of a need by farmers for "dependable sources of adequate credit, on terms suited to the particular needs of agriculture, from lenders who understood their problems."[11]

III. THE HISTORY AND STRUCTURE OF THE FARM CREDIT SYSTEM

A. THE EUROPEAN COOPERATIVE MODEL

In response to difficulties faced by farmers in obtaining credit in the early 1900's, two commissions, one appointed by President Taft and the other created by a private organization, undertook studies of the European rural credit systems.[12] Three different proposals for responding to the credit needs of American farmers were generated from the combined work of the commissions:

1. obtaining loan funds through the sale of bonds to investors;
2. organizing cooperatives; and
3. making direct government loans to farmers.[13]

The first proposal, the realization of funds through the sale of bonds to investors, was based on the method used by the German

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10. 12 U.S.C.A. § 2001 (West 1989).

11. W. HOAG, THE FARM CREDIT SYSTEM: A HISTORY OF FINANCIAL SELF-HELP 1 (1976) [herinafter HOAG]. *See also* McGowan & Noles, *The Cooperative Farm Credit System*, 4 MERCER L. REV. 263, 263 (1953) [hereinafter McGowan & Noles] ("[The System] is a complete, dependable and permanent system for the furnishing to farmers on a cooperative basis of various types of sound agricultural credits at reasonable rates of interest and costs."). *See generally* 11 N. HARL, AGRICULTURAL LAW, ch. 100 (1986) (describing the purposes of the System); 2 J. DAVIDSON, AGRICULTURAL LAW, ch. 10 (1981) (same); K. MEYER, D. PEDERSON, N. THORSON & J. DAVIDSON, AGRICULTURAL LAW: CASES AND MATERIALS, 269-74 (1985) (same); J. JUERGENSMEYER & J. WADLEY, AGRICULTURAL LAW § 14.3 (1982)(same).

12. HOAG, *supra* note 11, at 211-12. The commissions especially focused on the successful *Landshaft* system that had been functioning for 100 years in Germany. *Id. See also* FEDERAL LAND BANK OF ST. PAUL, DOWN THE ROAD TOGETHER 6 (1967) (describing the commissions' studies and asserting that "there is some reason to believe that the German Landshafts were patterned on early agricultural credit programs which originated in the American colonies").

13. HOAG, *supra* note 11, at 212.

Landschaften banks.[14] It ultimately became the method adopted by the federal land banks, the banks for cooperatives, and the federal intermediate credit banks.[15] Those Farm Credit System institutions currently obtain loan funds by selling bonds and debentures on the money markets.[16]

The cooperative approach was based on the organization of the European *Raiffeisen* banks. This form was adopted by the local federal land bank associations and production credit associations.[17] The third approach, direct governmental loans to farmers, was incorporated into the Farmers Home Administration programs.[18]

B. THE FEDERAL LAND BANKS (FLB)

Acting on the recommendations contained in the commission reports, Congress, in 1916, enacted the Federal Farm Loan Act of 1916[19] authorizing the establishment of federal land banks for the purpose of making long-term loans secured by real estate.[20] Each federal land bank was initially capitalized by federal government subscription of the institution's stock, and supervision of the banks was placed in a five-member Federal Farm Loan Board serving under the Treasury Department.[21] However, the Act provided that the government owned stock was to be eventually retired

14. *Id.* at 213.
15. *Id.*
16. *See* 12 U.S.C.A. §§ 2153, 2160 (West 1989) (authorizing System banks to borrow and to issue notes, bonds, and other obligations and creating the Federal Farm Credit Banks Funding Corporation to serve as the marketing agent for those obligations, replacing the System's Fiscal Agency which had previously served that function). *See also* 12 C.F.R. pt. 615, subpts. A, C, D, O (1990) (relating to the funding of the System and the issuance of notes, bonds, and other obligations); 55 Fed. Reg. 24,861, 24,887 (1990) (revising the authority for 7 C.F.R. pt. 615).
17. HOAG, *supra* note 11, at 213.
18. Brake, *A Perspective On Federal Involvement In Agricultural Credit Programs*, 19 S.D.L. REV. 567, 568-69 (1974) [hereinafter Brake]. *See also* HOAG, *supra* note 11, at 209-17; 11 N. HARL, AGRICULTURAL LAW 100.01[2] (1986) (discussing the historical development of the System); J. KNAPP, THE ADVANCE OF AMERICAN COOPERATIVE ENTERPRISE: 1920-1945 246-87 (1973) (same, with an emphasis on the cooperative nature of the System); M. ABRAHAMSEN, COOPERATIVE BUSINESS ENTERPRISE 323-37 (1976) (same, also with an emphasis on the cooperative nature of the System); McGowan & Noles, *supra* note 11, at 263-65 (same); Horne, *Sources of Agriculture Financing With an Emphasis on the Farm Credit System*, AGRIC. L.J. 15 (1980-81) (same). Although a discussion of the lending programs administered by the Farmers Home Administration (FmHA) is beyond the scope of this article, excellent explanatory materials on those programs are available from the Farmers' Legal Action Group, Inc., 1301 Minnesota Building, 46 East Fourth Street, St. Paul, MN 55101. *See also* Lancaster, *Current Issues in FmHA Loan Servicing*, 23 U.C. DAVIS L. REV. 713 (1990) (discussing the application of the Agricultural Credit Act of 1987 to FmHA borrowers).
19. Pub. L. No. 64-158, ch. 245, 39 Stat. 360 (1916) (repealed 1923).
20. *Id.* at 362-63.
21. *Id.* at 360-63.

through farmer-borrower purchases so that the federal loan banks would eventually be solely owned by farmers.[22] Since 1947, the federal land banks have been completely farmer owned.[23]

Pursuant to the Farm Loan Act of 1916, the Federal Farm Loan Board created twelve federal land bank districts.[24] In addition, national farm loan associations, later renamed federal land bank associations, were established to act as agents for the regional federal land bank associations.[25] Farmer-borrower purchases of stock in local federal land bank associations which, in turn, purchased stock in the federal land banks, ultimately achieved farmer ownership of both entities.[26]

C. THE FEDERAL INTERMEDIATE CREDIT BANKS (FICB)

In 1923, pursuant to the Agricultural Credit Acts,[27] the federal intermediate credit banks were created to discount the notes of other lenders made for short or intermediate term farm loans.[28] Although initially capitalized by the federal government in a manner similar to the capitalization of the federal land banks, the federal intermediate credit banks did not make direct loans to farmers as did the federal land banks.[29] Rather, the initial function of the federal intermediate credit banks was to purchase notes made by other lenders.[30]

D. THE PRODUCTION CREDIT ASSOCIATIONS (PCA)

Because existing lenders did not make substantial use of the federal intermediate credit banks, regional production credit corporations were authorized in 1933.[31] The Farm Credit Act of 1933[32] created twelve regional production credit corporations, twelve regional banks for cooperatives, and the Central Bank for Cooperatives.[33] The banks for cooperatives were established to

22. *Id.* at 364-65.
23. HOAG, *supra* note 11, at 254.
24. *Id.* at 214. For a map of the federal land bank districts, now the farm credit bank districts, see Appendix C to this article. *See also* 12 U.S.C.A. §§ 2002(b), 2252(a) (West 1989) (providing that there shall not be more than twelve farm credit districts and authorizing the merger of districts).
25. *Id.* at 216.
26. Brake, *supra* note 18, at 570-72; HOAG, *supra* note 11, at 213-17.
27. Pub. L. No. 67-503, ch. 252, 42 Stat. 1454 (1923) (repealed 1933).
28. *Id.* at 1455-56.
29. HOAG, *supra* note 11, at 25. The Federal Intermediate Credit Banks stopped using government capital in 1956. *Id.*
30. Brake, *supra* note 18, at 572; HOAG, *supra* note 11, at 231-43.
31. HOAG, *supra* note 11, at 237.
32. Pub. L. No. 73-75, 48 Stat. 257 (1933) (repealed 1953).
33. *Id.* at 257-64.

make loans to farmer cooperatives.[34]

The Farm Credit Act of 1933 also authorized the establishment of local production credit associations modeled after the federal land bank associations.[35] However, unlike federal land bank associations, the production credit associations were not merely agents of the regional production credit corporations.[36] Rather, they made direct loans that were discounted by the regional corporations.[37] Later, in 1956, the federal intermediate credit banks assumed the discounting function for production credit associations, and the assets of the twelve regional production credit corporations were transferred to the federal intermediate credit banks.[38]

E. THE FARM CREDIT ADMINISTRATION AND THE DEPARTMENT OF AGRICULTURE

The Farm Credit Act of 1933 created the Farm Credit Administration to coordinate all federal lending activities.[39] For the first six years of its existence, the Farm Credit Administration operated as an independent agency of the executive branch.[40] However, in 1939, an executive order placed the agency in the Department of Agriculture.[41] The Farm Credit Administration remained within the Department of Agriculture until the Farm Credit Act of 1953[42] re-established its independent status.[43]

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34. *See* Brake, *supra* note 18, at 572-73; HOAG, *supra* note 11, at 231-43.

35. Farm Credit Act of 1933, Pub. L. No. 73-76, 48 Stat. 257, 259 (1933) (repealed 1953).

36. HOAG, *supra* note 11, at 46-48.

37. *Id.* at 50-53.

38. Brake, *supra* note 18, at 569. For a detailed account of the early history of the Farm Credit System, see McGowan & Noles, *supra* note 11.

39. Farm Credit Act of 1933, Pub. L. No. 73-76, 48 Stat. 257, 262-64 (1933) (repealed 1953). *See also* HOAG, *supra* note 11, at 233, 234 (discussing the Farm Credit Act of 1933). The functions and powers transferred to the Farm Credit Administration included the following: the Federal Land Bank, National Farm Association and Federal Intermediate Credit Bank supervision from the Federal Farm Loan Board in the Treasury Department; loans to cooperatives from Agricultural Marketing Revolving Fund from the Federal Farm Board; Regional Agricultural Credit Corporations supervision from the Reconstruction Finance Corporation; Crop Production and Seed Loan Offices supervision from the Secretary of Agriculture; and the Fund for Investments in Stock of Agricultural Credit Corporations from the Secretary of Agriculture. *Id.* at 234.

40. HOAG, *supra* note 11, at 233.

41. Reorganization Plan No. 1 of 1939, 53 Stat. 1423, 1429 (April 25, 1939) (repealed 1953).

42. Pub. L. No. 83-202, 67 Stat. 390 (1953) (repealed 1971).

43. *Id.* at 390-94.

F. DECENTRALIZATION OF THE SYSTEM — THE FARM CREDIT ACT OF 1953

Not only did the Farm Credit Act of 1953 re-establish the independent status of the Farm Credit Administration, it redefined and redirected the Farm Credit System, moving it toward decentralization, farmer ownership and control, and cooperative development.[44] The 1953 Act created the Federal Farm Credit Board as the policy making body of the Farm Credit Administration.[45] In addition, the Farm Credit Administration, with its Governor responsible to the Board rather than the President, was accorded supervisory authority over the regional banks, the federal land banks [hereinafter FLBs] and federal intermediate credit banks [hereinafter FICBs], and their local associations, the federal land bank associations [hereinafter FLBAs], and production credit associations [hereinafter PCAs] respectively.[46] Farmer participation and control was increased by giving farmer members the authority to elect six of the seven members on each of the twelve district farm credit boards.[47] Also, recommendations were sought for retiring all of the remaining government capital in the system.[48] Further, the impetus of the Farm Credit Act of 1953 contributed to the repayment of all government capital in the Farm Credit System by the end of 1968.[49]

G. THE MODERN SYSTEM — THE FARM CREDIT ACT OF 1971

The Farm Credit Act of 1971[50] continued the trend toward decentralization by authorizing that more decisions be made at local district levels.[51] To implement decentralization, lending authority was expanded in three areas by the authorization of the following: long term mortgage loans for rural housing;[52] loans to

44. *See generally* HOAG, *supra* note 11, at 231-43 (identifying and describing the broad themes of the Farm Credit Act of 1953).

45. Farm Credit Act of 1953, Pub. L. No. 83-202, 67 Stat. 390 (1953) (repealed 1971).

46. HOAG, *supra* note 11, at 257-58. The restoration of the Farm Credit Administration to the status of an independent agency after fourteen years as an agency within the United States Department of Agriculture was primarily motivated by a desire to insulate it from political influence. *Id.*

47. *Id.* at 121.

48. *Id.* at 259.

49. Brake, *supra* note 18, at 574-76; HOAG, *supra* note 11, at 257-61.

50. Pub. L. No. 92-181, 85 Stat. 583 (1971) (codified as amended at 12 U.S.C.A. §§ 2001—2279aa-14 (West 1989 & Supp. 1990).

51. *Id.* at 584-86 (FLBs), 590-97 (FICBs). *See generally* Kayl, *supra* note 6, at 275-77 (discussing the major features of the Farm Credit Act of 1971).

52. 12 U.S.C.A. §§ 2014, 2018 (West 1980). In amending the Farm Credit Act of 1971, the Agricultural Credit Act of 1987, Pub. L. No. 100-233, 101 Stat. 1568, 1572-1662 (1988),

persons furnishing custom services to farmers;[53] and financial services to farmers including financial management, record keeping, and estate planning.[54]

1. *FLBs and FLBAs*

After the Farm Credit Act of 1971, the Farm Credit System was entirely farmer owned for the last government subscription had been retired in 1968.[55] Long-term mortgage credit was provided through the FLBs and the FLBAs.[56] Although each FLB and each FLBA were separate corporations, each FLBA owned a portion of the stock of the regional FLB.[57] Farmers who sought FLB funds made application through their local FLBA.[58]

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restructured the system. The previously separate FLBs and FICBs were required to merge into district farm credit banks. Although FLBAs and PCAs were permitted, with limited exceptions, to remain separate, the 1987 Act also allowed FLBAs and PCAs to merge as agricultural credit associations. *See infra* notes 125-27 and the accompanying text. However, the authority of the farm credit banks and the PCAs to make loans for rural housing was retained. 12 U.S.C.A. §§ 2019(b), 2075(b) (West 1989). *See also* 12 C.F.R. § 613.3040 (1990) (rural resident loan program); 55 Fed. Reg. 24,861, 24,878 (1990) (to be codified at 12 C.F.R. § 613.3040) (same). A FLBA can also make direct loans for rural housing if that authority has been delegated to it by the district farm credit bank. *See* 12 U.S.C.A. § 2013(18) (West 1989); 55 Fed. Reg. 24,861, 24,881 (1990) (to be codified at 12 C.F.R. 614.4030(a)(3)).

53. 12 U.S.C.A. § 2016 (West 1980). As with the authority to make housing loans to rural residents, the authority to make loans for persons furnishing custom services to farmers has been retained under the current amended version of the Farm Credit Act of 1971. 12 U.S.C.A. §§ 2019(c), 2075(a)(3) (West 1989). *See also* 12 C.F.R. § 613.3050 (1990) (farm-related businesses); 55 Fed. Reg. 24,861, 24,878 (1990) (to be codified at 12 C.F.R. § 613.3050) (same).

54. 12 U.S.C.A. §§ 2019, 2076 (West 1980). Under the current version of the Farm Credit Act of 1971, "technical assistance" may be provided by System lenders to their borrowers. 12 U.S.C.A. §§ 2020(a), 2076 (West 1989). *See also* 12 C.F.R. § 618.8000 (1990) (technical assistance); 55 Fed. Reg. 24,861, 24,888 (1990) (revising the authority for 12 C.F.R. § 618).

55. *See supra* note 49 and the accompanying text.

56. 12 U.S.C.A. § 2093 (West 1980). Currently, as a result of the Agricultural Credit Act of 1987, the authority formerly possessed by FLBs is held by the district farm credit banks (FCBs). 12 U.S.C.A. § 2015(a) (West 1989). *See also* 55 Fed. Reg. 24,861, 24,800 (1990) (to be codified at 12 C.F.R. § 614.4000) (long-term real estate lending authority of farm credit banks). Lending for long-term real estate purposes is still provided through a FLBA unless there is not an active association in the lending area. 12 U.S.C.A. § 2021(a)-(b) (West 1989). *See also* 55 Fed. Reg. 24,861, 24,881 (1990) (to be codified at 12 C.F.R. § 614.4030) (long-term real estate lending authority of federal land credit associations). However, a farm credit bank may delegate its direct lending authority to an association. 12 U.S.C.A. § 2013(18) (West 1989). When direct lending authority for long-term real estate loans is transferred to a FLBA, the association is referred to as a "federal land credit association." 55 Fed. Reg. 24,861, 24,889 (1990) (to be codified at 12 C.F.R. § 519.9155). *See also infra* notes 119-27 and the accompanying text (discussing the changes in lending authority occasioned by the 1987 Act).

57. 12 U.S.C.A. § 2093 (West 1980). Under the current version of the Farm Credit Act of 1971, FLBAs still subscribe to the stock of their respective farm credit bank. 12 U.S.C.A. § 2093(10) (West 1989).

58. 12 U.S.C.A. § 2020 (West 1980). Currently, borrowers seeking long-term loans for real estate purposes still apply for those funds through a FLBA if there is an association serving the prospective borrower's area. To obtain the funds, the prospective borrower must purchase stock in the association. 12 U.S.C.A. § 2017 (West 1989). If there is not an

The farmer borrower of FLB funds was required to purchase capital stock in the FLBA in an amount at least equal to five percent of the face value of his loan.[59] With the purchase of stock, the borrower became a voting member of the FLBA, and the FLBA purchased a like amount of stock in the regional FLB.[60] Each stockholder was entitled to only one vote.[61] Further, the FLB and FLBA held a first lien on the borrower's stock.[62]

The primary source of FLB funds was derived from the sale of consolidated federal land bank bonds which were joint obligations of the twelve district FLBs.[63] However, the United States bears no liability on the bonds.[64]

2. *FICBs and PCAs*

PCAs under the Farm Credit Act of 1971 made short and intermediate term loans that were, in turn, discounted by the regional FICBs.[65] The capital stock of the FICBs was owned by

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association serving the prospective borrower's area, the loan may be obtained directly from the district farm credit bank, and stock must be purchased in the district farm credit bank. 12 U.S.C.A. § 2021(b), (c) (West 1989).

59. 12 U.S.C.A. § 2034(a) (West 1980). For a discussion of current requirements regarding the amount of stock that must be purchased, *see infra* notes 131 and 132 and the accompanying text. *See also In re* Massengill, 100 Bankr. 276, 278 & n. 1 (E.D. N.C. 1988) (describing in detail the stock purchase requirements under the Farm Credit Act of 1971 prior to its amendment by the Agricultural Credit Act of 1987).

60. 12 U.S.C.A. § 2034 (West 1980). The voting shareholders of each FLBA continue to elect the association's board of directors. 12 U.S.C.A. § 2092 (West 1989). *See also supra* note 58 (discussing the current requirements for the purchase of stock). Under current law, when a FLBA has merged with a PCA, the stock purchased would be that of the agricultural credit association formed as a result of that merger. *See infra* notes 125-27 and the accompanying text.

61. *Id.* The one vote principle still applies. Thus, irrespective of the number of shares owned, a shareholder in a System institution has only one vote. *See* 12 C.F.R. § 615.5230(a)(1)(i) (1990).

62. 12 U.S.C.A. § 2054 (West 1980). Under the current law, FLBAs continue to be entitled to a first lien on borrower's stock and participation certificates issued by the association. 12 U.S.C.A. § 2097 (West 1989).

63. 12 U.S.C.A. § 2155 (West 1980). *See also* 12 U.S.C.A. §§ 2153, 2155 (West 1989) (the System continues to issue notes, bonds, debentures, and other obligations for which each bank in the System is jointly liable).

64. 12 U.S.C.A. § 2155(c) (West 1989). For an extensive and highly critical study of the Farm Credit System's funding of loans with long-term, non-callable, fixed rate bonds during the early 1980's, see GENERAL ACCOUNTING OFFICE, PUB. NO. GGD-86-150 BR, FARM CREDIT SYSTEM: ANALYSIS OF FINANCIAL CONDITION (1986). *See also* Barry, *Financial Stress For the Farm Credit Banks: Impacts On Future Loan Rates For Borrowers*, 46 AGRIC. FINANCE REV. 27 (1986) (discussing the effect on loan rates resulting from the financial distress experienced by the System in the mid-1980s).

65. 12 U.S.C.A. §§ 2096, 2072(6) (West 1980). Under the Farm Credit Act of 1971, as currently amended, PCAs largely retain the same status and function that they assumed under the 1971 Act. PCAs continue to extend short- and intermediate-term credit. 12 U.S.C.A. § 2075(a) (West 1989). However, the functions formerly performed by FICBs are now the responsibility of the district farm credit banks. Those functions include the discounting of PCA loans. 12 U.S.C.A. § 2015(b)(A) (West 1989). *See also infra* notes 119-27 and the accompanying text (discussing the lending authority of System lenders under the Agricultural Credit Act of 1987).

PCAs.[66] The FICBs obtained funds through the sale of consolidated debentures.[67] As was required of FLBA and FLB borrowers, PCA borrowers also were required to purchase stock in an amount equal to at least five percent of the face value of the loan.[68]

3. *Board of Directors*

Each PCA and FLBA had a board of directors elected by its members.[69] Similarly, each of the twelve farm credit districts had a board of directors consisting of seven members.[70] Prior to the enactment of the Farm Credit Amendments Act of 1985,[71] one director was appointed by the Governor of the Farm Credit Administration and the remaining six were elected by the district's FLBAs, PCAs, and borrowers from the bank of cooperatives, with each of the three System institutions electing two directors.[72] Under the 1985 Act, the seventh member of the district board was elected by the "borrowers at large in a district," a phrase defined as follows:

> (i) a voting shareholder of a Federal land bank association and a direct borrower, and a borrower through an agency, from a Federal land bank;
> (ii) a voting shareholder of a production credit association; and
> (iii) a voting shareholder or subscriber to the guaranty fund of a bank for cooperatives.[73]

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66. 12 U.S.C.A. § 2073 (West 1980). Currently, PCAs continue to subscribe to stock in the "upstream" bank. However, that bank is now the district farm credit bank rather than the district FICB. 12 U.S.C.A. § 2073(7) (West 1989).

67. 12 U.S.C.A. § 2094 (West 1980). As a result of the Agricultural Credit Act of 1987, the successors to the district FICBs, the farm credit banks, are responsible for obtaining funds through the sale of obligations for which all of the System banks are liable. 12 U.S.C.A. §§ 2013(10), 2153, 2155(a) (West 1989).

68. 12 U.S.C.A. § 2094 (West 1980). Currently, prospective borrowers still must purchase stock in the PCA making the loan. 12 U.S.C.A. § 2017 (West 1989). For a discussion of the current requirements regarding the amount of stock that must be purchased, see *infra* notes 131-32 and the accompanying text.

69. 12 U.S.C.A. §§ 2092, 2032 (West 1980). Under the current law, each PCA's shareholders continue to elect the PCA's board of directors. 12 U.S.C.A. § 2072 (West 1989).

70. 12 U.S.C.A. § 2222 (1980). Currently, the number of directors serving on the board of directors of the district farm credit banks is dictated by the respective bank's bylaws. *See* 12 U.S.C.A. § 2012 (West 1989). *See also* 12 C.F.R. §§ 611.310-611.340 (1990) (relating to the election of bank and association directors).

71. *See infra* notes 74-92 and the accompanying text.

72. 12 U.S.C.A. § 2223 (West 1980) (repealed 1988).

73. 12 U.S.C.A. § 2223(a) (West Supp. 1986) (repealed 1988). Currently, the only statutory requirement concerning the qualification of a director is that "at least one member shall be elected by the other directors, which member shall not be a director, officer, employee, or stockholder of a System institution." 12 U.S.C.A. § 2012 (West 1989). A

H. THE FARM CREDIT AMENDMENTS OF 1985

The Farm Credit Amendments Act of 1985[74] also made structural changes in levels above the district board of directors. Prior to the 1985 Act, the Federal Farm Credit Board was a part-time board consisting of thirteen members, one nominated by each of the twelve districts and appointed by the President and one appointed by the Secretary of Agriculture as his representative.[75] The 1985 Act renamed the board the Farm Credit Administration Board and reduced its membership to three full-time members.[76] The three members are appointed by the President with the advice and consent of the Senate.[77]

The shift in the responsibilities of the Farm Credit Administration was a second major structural change caused by the 1985 Act.[78] Under prior law, the Farm Credit Administration directly participated in the supervision and management of the System.[79] Under the 1985 Act, the Farm Credit Administration assumed the function of an independent regulatory agency.[80] The enumerated powers of the Farm Credit Administration included the power to modify the boundaries of farm credit districts, approve the merger of districts, and promulgate regulations.[81] In addition, the Farm Credit Administration was directed to examine System institutions in the same manner as followed by examiners under the National Bank Act, the Federal Reserve Act, and the Federal Deposit Insur-

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concise description of the System as it existed under the 1971 Act is found in Rosantrater, *Farm Credit: An Overview*, 15 COLO. LAW. 1594 (1981).

74. Pub. L. No. 99-205, 99 Stat. 1678 (1985) (codified as amended in scattered sections of 12 U.S.C.A. (West 1989 & Supp. 1990)).

75. 12 U.S.C.A. § 2242 (West 1980).

76. 12 U.S.C.A. § 2242 (West 1989).

77. *Id.*

78. The significance of this change and its consequences are analyzed in Kayl, *supra* note 6, at 279-94, and Dewey, *supra* note 6, at 287-89.

79. *See* Dewey, *supra* note 6, at 287 (describing the selection process for the former, part-time, Federal Farm Credit Board, a process in which twelve of the thirteen members were nominated by the twelve farm credit districts, as a "process in which directors could place allegiances to their individual district's interests above their responsibilities to the federal regulatory body"). *See also* Kayl, *supra* note 6, at 288 ("the situation was the classic 'tail wagging the dog' wherein the FCA was intimidated by the FCS members").

80. *See* 12 U.S.C.A. §§ 2243, 2252 (West 1989) (setting forth the authority of the FCA board and the powers and duties of the FCA). *See also* Dewey, *supra* note 6, at 287-88 ("The 1985 Amendments recognized the wisdom in establishing the FCA as a non-captive agency which could carry out its governmental functions free of institutions' influence."); Kayl, *supra* note 6, at 286 ("Stronger independent regulation is an euphemism for greater control of the FCS by the FCA."); Bailey v. Federal Intermediate Credit Bank, 788 F.2d 498, 499 n. 3 (8th Cir. 1986) ("the concern of Congress was with decreasing the FCA's day-to-day involvement and increasing its role as an 'arm's length' regulator of the farm credit system" (citations omitted)), *cert. denied*, 479 U.S. 915 (1986); *In re* Hoag Ranches, 846 F.2d 1225, 1229 (9th Cir. 1988) ("The role of the Farm Credit Administration has been changed from supervisor to arms-length regulator").

81. 12 U.S.C.A. § 2252(a)(1), (2), (9) (West 1989).

ance Act.[82] Further, the Farm Credit Administration was given broad enforcement powers under the 1985 amendments including the authority to issue cease and desist orders[83] and to suspend or remove System institution directors and officers.[84] Finally, the chairman of the Farm Credit Administration Board also serves as the chief executive officer of the Farm Credit Administration under the 1985 Act.[85]

The Farm Credit Amendments Act of 1985 also centralized the power to raise and distribute funds within the System.[86] The Act created the Farm Credit System Capital Corporation which, in turn, was granted the authority to require all of the System institutions to purchase its stock, to pay assessments to it, and to contribute to its capital.[87] The purposes of the Capital Corporation included the following functions:

1. provide financial assistance to System institutions;
2. acquire from and participate with other System institutions the nonperforming assets of those institutions;
3. "hold, restructure, collect, and otherwise administer nonperforming assets required from or participated in with other Farm Credit System institutions, and guarantee performing and nonperforming assets held by other Farm Credit institutions"; and
4. provide technical and other services to other System institutions relating to their loan portfolios.[88]

Probably the most controversial of the powers accorded to the Capital Corporation was the authority to draw funds from stronger districts to buttress weaker ones.[89] The Corporation's attempts to exercise that authority spawned numerous lawsuits initiated by district banks and local associations.[90]

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82. 12 U.S.C.A. § 2254(a) (West 1989).
83. 12 U.S.C.A. §§ 2261-63 (West 1989).
84. 12 U.S.C.A. §§ 2264-74 (West 1989).
85. 12 U.S.C.A. § 2244 (West 1989).
86. One of the goals of the 1985 amendments was to "[g]ive the Farm Credit System broader authority to use its own resources to shore up weak system units". Kayl, *supra* note 6, at 285 (citing H.R. REP. NO. 425, 99th Cong., 1st Sess. *reprinted in* 1985 U.S. CODE CONG. & ADMIN. NEWS 2587).
87. 12 U.S.C.A. §§ 2216-16k, 2152 (West Supp. 1986) (repealed 1988).
88. 12 U.S.C.A. § 2216 (West Supp. 1986) (repealed 1988).
89. 12 U.S.C.A. § 2216(f)(a)(14) (West Supp. 1986) (repealed 1988).
90. *E.g.*, Federal Land Bank of Springfield v. Farm Credit Admin., 676 F. Supp. 1239 (D. Mass. 1987); Sikeston Production Credit Ass'n v. Farm Credit Admin., 647 F. Supp. 1155 (E.D. Mo. 1986). For general discussions of the issues presented in the litigation, see Webster, *Joined in Battle: Who Will Control the Farm Credit System?* AGRIFINANCE, March 1987, at 6; Taylor, *Big Trouble at Farm Credit*, FARM J., Nov. 1986, at 20; Kayl, *supra* note 6, at 289-305 (citing additional cases).

The Farm Credit Amendments Act of 1985 also gave the Secretary of the Treasury the authority to provide financial assistance to the system on a "certification . . . [of] need" by the Farm Credit System.[91] Finally, as will be discussed in greater detail later in this article, the 1985 Act granted to System borrowers certain rights not previously afforded to them.[92]

I. THE FARM CREDIT ACT AMENDMENTS OF 1986

The mid-1980's saw continuing deterioration in the financial condition of the Farm Credit System.[93] The Congressional response, contained in the Farm Credit Act Amendments of

91. 12 U.S.C.A. § 2216 (West Supp. 1986). A good, but brief, discussion on the structural changes mandated by the 1985 Act is contained in Note, *The Congressional Response To A Crisis In Agricultural Credit: The 1985 Farm Credit Amendments*, 31 S.D.L. REV. 471 (1986). *See also* Duncan, *Farm Credit System — Current Matters*, 38 ALA. L. REV. 537, 539 (1987) (discussing the 1985 Act); Kayl, *supra* note 6, at 279-305 (same). *See generally* GENERAL ACCOUNTING OFFICE, PUB. NO. RCED-86-126BR, FARM FINANCE: FARM DEBT, GOVERNMENT PAYMENTS, AND OPTIONS TO RELIEVE FINANCIAL STRESS (1986) (discussing the agricultural economy at the time of the 1985 Act and the options available to improve that economy).

92. 12 U.S.C.A. § 2199(a) (disclosure of interest rates), 2199(b) (forbearance), 2200 (access to loan documents and other information), 2201 (prompt action on loan applications), 2202 (reconsideration of action on loan applications) (West Supp. 1986) (some of the borrower rights currently found in sections 2199-2202 were added by the Agricultural Credit Act of 1987, Pub. L. No. 100-233, tit. I, 101 Stat. 1568, 1572-85 (1988)). *See infra* notes 340-434 and the accompanying text.

In addition to the codified protections for System borrowers, the 1985 Act also contained an uncodified provision mandating that System lenders review all loans that had been placed in "non-accrual" status "based on changes in the circumstances of such institutions as the result of this Act and the amendments made by this Act. . . ." Borrowers were to be notified in writing of the results of that review. Farm Credit Amendments Act of 1985, Pub. L. No. 99-205, 307, 99 Stat. 1678, 1709 (1985).

Perhaps the most significant of the borrower protections contained in the 1985 Act was the requirment that System lenders develop forbearance policies. 12 U.S.C.A. § 2199(b) (West Supp. 1986). Previously, there had been no statutory requirement for such policies. Rather, the only directive for such policies was contained in the regulations at 12 C.F.R. § 614.4510 (1985). Section 614.4510 merely required that the banks and associations have policies providing a "means of forbearance for cases when the borrower is cooperative, making an honest effort to meet the conditions of the loan contract, and is capable of working out of the debt burden."

The imposition of a statutory mandate for the development of forbearance policies, though itself not specific regarding the availability and means of forbearance, reflected Congressional displeasure with the System's prior procedures and attitudes toward forbearance. *See* H.R. REP. NO. 99-425, 99 CONG., 1ST SESS., *reprinted in* 1985 U.S. CODE CONG. & ADMIN. NEWS 2587, 2598. *See also* Kayl, *supra* note 6, at 287 ("Testimony before House and Senate committees [considering the 1985 legislation] dealt with borrowers' perceptions that they had been treated high-handedly by FCS member institutions" (citations omitted)). Later, with the passage of the Agricultural Credit Act of 1987, Congress became more specific in its directives to the System regarding its treatment of its member-borrowers. *See infra* notes 340-434 and the accompanying text.

93. GENERAL ACCOUNTING OFFICE, PUB. NO. RCED-89-33BR, FARM FINANCE: FINANCIAL CONDITION OF AMERICAN AGRICULTURE AS OF DECEMBER 31, 1987, 66-73 (1988); GENERAL ACCOUNTING OFFICE, PUB. NO. RCED-88-26BR, FARM FINANCE: FINANCIAL CONDITION OF AMERICAN AGRICULTURE AS OF DECEMBER 31, 1986, 64-71 (1987). *See also* Guebert, *Confessions of a Farm Credit Regulator*, TOP PRODUCER, June-July 1987, at 15 (discussing the deteriorating financial condition of the System); Taylor, *Day of Reckoning for Farm Credit*, FARM J., March 1987, at 26 (same).

1986,[94] was to partially decentralize authority by giving district banks the power to set interest rates and to implement new "regulatory accounting practices" (RAP) that, among other things, allowed System institutions to amortize for up to twenty years the additions to their loss reserves.[95]

J. THE AGRICULTURAL CREDIT ACT OF 1987

The Agricultural Credit Act of 1987[96] was signed by the President on January 6, 1988.[97] The 1987 Act operates in two ways that have resulted or will result in structural changes to the System. First, it makes available up to four billion dollars of federal funds to improve the financial condition of System institutions.[98] Second, it mandates the merger of certain System institutions and provides for the voluntary consolidation of others.[99]

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94. Pub. L. No. 99-509, 1031-1037, 100 Stat. 1874, 1877-79 (1986) (codified as amended in scattered sections of 12 U.S.C.A. (West 1989 & Supp. 1990)).

95. *Id.*, 1035-1037, 100 Stat. at 1878-79. *See generally* Banner & Barry, *RAPPING The Farm Credit System: Spreading Costs to the Future*, CHOICES, First Quarter 1988, at 31 (discussing the economics of the new regulatory accounting practices); *How the Farm Credit System Could Harvest a Big Profit*, WASH. POST NAT. WEEKLY ED., Oct. 27, 1986, at 20, col. 1 (same); Kayl, *supra* note 6, at 309-10 (discussing the 1986 Act in general). The "regulatory accounting practices" regulations are currently found at 12 C.F.R. § 624 (1990).

96. Pub.L. No. 100-233, 101 Stat. 1568-1718 (1988) (codified in scattered sections of Titles 7, 12, & 14 of 12 U.S.C.A. (West 1988, 1989 & Supp. 1990)).

97. The 1987 Act substantially changed the loan servicing procedures for the loan programs administered by the Farmers Home Administration (FmHA) and made minor changes to other agricultural programs, including the Conservation Reserve Program. *See generally* Hayes, *Farmers Home Administration: What the New Law Provides*, 3 FARMERS' LEGAL ACTION REP. 6 (1988) (discussing, in detail, the changes made by the 1987 Act to FmHA loan servicing procedures); Hertzler, Jr., *The Agricultural Credit Act of 1987—A View from the Farmers Home Administration*, 2 J. AGRIC. LENDING 17 (1988) (briefly describing how the 1987 Act affected the FmHA); McEowen & Harl, *A Look at the Conservation Reserve Program (CRP) and How It Affects Owners and Tenants of Marginal Land*, 12 J. AGRIC. TAX'N & L. 121 (1990) (discussing the Conservation Reserve Program).

98. 12 U.S.C.A. § 2278b-6 (West 1989).

99. An uncodified provision of the 1987 Act required the merger of the FLB and FICB in each district within six months of the Act's enactment. Pub. L. No. 100-203, 410, 101 Stat. 1568, 1637 (1988). *See also* 12 U.S.C.A. § 2011 (West 1989) (setting forth in the annotations the terms of section 410). *See generally* 12 U.S.C.A. §§ 2279a-2279a-3 (West 1989) (authorizing the merger of banks within a district).

In addition, another uncodified provision of the 1987 Act required each FLBA and PCA sharing substantially the same geographic territory to submit to their respective shareholders a plan for merging the associations within six months after the merger of the district FLB and FICB. Pub. L. No. 100-203, 411, 101 Stat. 1568, 1638 (1988). *See also* 12 U.S.C.A. § 2071 (West 1989) (setting forth in the annotations the terms of section 411). *See generally* 12 U.S.C.A. § 2279c-1 (West 1989) (authorizing the merger of associations).

Finally, the 1987 Act also required the development of a proposal for the consolidation of farm credit districts, Pub. L. No. 100-203, 412, 101 Stat. 1568, 1638-39 (1988), and the voluntary merger of the banks for cooperatives, Pub. L. No. 100-203, 413, 101 Stat. 1568, 1639-42 (1988). *See also* 12 U.S.C.A. §§ 2221, 2121 (West 1989) (setting forth in the annotations the terms of sections 412 and 413, respectively).

1. *Financial Assistance to System Institutions*

Under the 1987 Act, the Farm Credit Administration remains the regulatory authority over System institutions.[100] However, a new threefold approach to financial assistance is undertaken. First, the Capital Corporation, a creation of the 1985 Act, has been abolished.[101] In its place, an entity known as the Farm Credit System Assistance Board has been created to certify financially distressed institutions.[102] Once certified, an institution can issue preferred stock and receive financial assistance.[103] If the book value of the stock of a System institution is less than seventy-five percent of the par value of the stock, that is, if its value is less than $3.75 per share, the institution is required to seek certification.[104]

Second, the 1987 Act also created an entity known as the Financial Assistance Corporation.[105] That entity is authorized to issue federally guaranteed bonds and to purchase the preferred stock of System institutions that have been certified as eligible to issue preferred stock, thereby funnelling the federal "bail-out" funds to those institutions.[106] The Financial Assistance Corporation will terminate on the maturity and full payment of its

100. *See generally* Dewey, *supra* note 6, at 289 (discussing the role of the FCA under the 1987 Act).

101. Pub. L. No. 100-233, 207(a)(3), 101 Stat. 1568, 1607 (1988). The assets and liabilities of the Capital Corporation were assumed by the Farm Credit System Assistance Board. 12 U.S.C.A. § 2278a-9 (West 1989).

102. 12 U.S.C.A. § 2278a (West 1989). The mission of the Assistance Board is to protect borrower's stock and "to assist in restoring System institutions to economic viability. . . ." 12 U.S.C.A. § 2278a-1 (West 1989). The Board has three directors, one appointed by the Secretary of the Treasury, one by the Secretary of Agriculture, and the third member, who is to be an agricultural producer "experienced in financial matters", is appointed by the President with the advice and consent of the Senate. 12 U.S.C.A. § 2278a-2 (West 1989).

The Assistance Board is granted broad powers with which to fulfill its mission. *See* 12 U.S.C.A. § 2278a-3 (West 1989). Those powers include the authority to issue regulations without complying with the Administrative Procedure Act, and the Board is not subject to regulation by the FCA. 12 U.S.C.A. § 2278a-10(a), (b) (West 1989).

103. 12 U.S.C.A. § 2278a-4, 2278a-5 (West 1989). The preferred stock issued by certified institutions is purchased by the Financial Assistance Corporation using funds the Corporation obtained by issuing federally guaranteed bonds. *See infra* note 106 and the accompanying text.

104. 12 U.S.C.A. § 2278a-4(b) (West 1989). The $3.75 per share figure assumes that the stock had a par value of $5.00, which it usually did prior to the 1987 Act. *See* 12 U.S.C.A. §§ 2034(a), 2094(f) (West 1980). *See also In re* Massengill, 100 Bankr. 276, 278 & n. 1 (E.D. N.C. 1988) (discussing the stock purchase requirements in effect prior to the 1987 Act).

105. 12 U.S.C.A. § 2278(b) (West 1989). The purpose of the Financial Assistance Corporation is the provision of capital to financially distressed System institutions. 12 U.S.C.A. § 2278b-1 (West 1989). The board of directors of the Financial Assistance Corporation consists of the Board of Directors of the Federal Farm Credit Banks Funding Corporation. 12 U.S.C.A. § 2278b-2(a) (West 1989).

106. 12 U.S.C.A. §§ 2278b-6(a), 2278b-7(b) (West 1989). Interest must be paid on the federally guaranteed bonds. *See* 12 U.S.C.A. §§ 2278b-6(c), 2278b-8 (West 1989). Although the Secretary of the Treasury bears some initial responsibility for interest payments, the System is ultimately obligated to repay the Secretary up to the sum of $2,000,000,000 for interest payments. 12 U.S.C.A. §§ 2278b-6(c), 2278b-8(b) (West 1989).

bonds.[107] The bonds will have a fifteen year maturity period.[108]

In addition to creating an "assistance fund" through the issuance of federally guaranteed bonds, the 1987 Act created a "trust fund" funded solely from the proceeds from a one-time required purchase of Financial Assistance Corporation stock by the PCAs and Farm Credit Banks.[109] The creation of the "trust fund" already has been challenged as an unconstitutional taking under the fifth amendment.[110]

Third, the 1987 Act also creates the Farm Credit System Insurance Corporation.[111] The Corporation's function is to create an insurance fund by assessing and collecting premiums from System institutions.[112] The fund is intended to protect System institutions, investors, and stockholders beginning in 1993 by satisfying defaults on payments of bonds, preferred stock, and borrower stock.[113]

The 1987 Act also created, as part of the Farm Credit System, the Federal Agricultural Mortgage Corporation to oversee a new agricultural mortgage secondary market.[114] Lenders other than System lenders will be eligible to participate in the secondary

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107. 12 U.S.C.A. § 2278b-11 (West 1989). The System is required to pay the bond obligations. 12 U.S.C.A. § 2278b-6(c) (West 1989).

108. 12 U.S.C.A. § 2278b-6(a) (West 1989). For an excellent discussion of the federal "bailout" provisions of the 1987 Act, see Massey, *Farm Credit System: Structure and Financing Under the New Act*, 3 FARMERS' LEGAL ACTION REP. 52, 58-64 (1988) [hereinafter Massey] (includes flow chart diagrams of the "bailout" mechanisms).

109. 12 U.S.C.A. §§ 2278b-5(b), 2278b-9 (West 1989 & Supp. 1990). The purpose of the "trust fund" is to provide intermediate security for each System institution's share of interest and principal repayment on the "assistance fund" bonds. *See* Massey, *supra* note 108, at 63-64.

110. Colorado Springs Production Credit Ass'n v. Farm Credit Admin., 695 F. Supp. 15 (D.D.C. 1988) (order denying in part and granting in part motion to dismiss).

111. 12 U.S.C.A. § 2277a-1 (West 1989).

112. *Id. See also* Massey, *supra* note 108, at 65-68 (discussing purposes and functions of the Farm Credit System Insurance Corporation); Federal Farm Credit Banks Funding Corp. v. Farm Credit Admin., 731 F. Supp. 217, 219-20 (E.D. Va. 1990) (briefly describing the Insurance Corportation and the Insurance Fund).

113. *See* 12 U.S.C.A. § 2277a-9(a), (c) (West 1989).

114. 12 U.S.C.A. §§ 2279aa - 2279aa-14 (West 1989). *See generally* Pariser, *Agricultural Real Estate Loans and Secondary Markets*, IV AGRIC. & HUMAN VALUES 29 (1987) (discussing the possible effects of the secondary market on the Farm Credit System); GENERAL ACCOUNTING OFFICE, PUB. NO. RCED-90-118, FEDERAL AGRICULTURAL MORTGAGE CORPORATION: SECONDARY MARKET DEVELOPMENT AND RISK IMPLICATIONS (1990) (discussing a variety of issues presented by the secondary market); GENERAL ACCOUNTING OFFICE, PUB. NO. RCED-88-55FS, FARM FINANCE: PROVISIONS FOR SECONDARY MARKETS FOR FARM REAL ESTATE LOANS IN H.R. 3030 (1987) (same); AMERICAN BANKERS ASSOC., FINANCING FARM REAL ESTATE: A COMPREHENSIVE TRAINING MANUAL FOR THE SECONDARY MARKET FOR AGRICULTURE (1988) (a lender's guide to the secondary market created by the 1987 Act); D. FRESHWATER & D. TRECHTER, NEW APPROACHES TO FINANCING LONG-TERM FARM DEBT (Econ. Res. Serv., USDA, Agric. Info. Bull. No. 511, March 1987) (discussing secondary agricultural mortgage markets in general); Killebrew, *The Case for the Secondary Market*, 1 J. AGRIC. LENDING 6 (1987) (a commercial lender's argument for a secondary agricultural mortgage market).

market.[115]

In addition, the Federal Farm Credit Banks Funding Corporation was created as the System's fiscal agent for the marketing of System bonds. In addition to marketing System bonds, the Funding Corporation will determine the terms and other conditions of those bonds.[116]

Questions have already been raised about the efficacy of the federal "bail-out."[117] Moreover, on Friday, May 20, 1988, the Federal Land Bank of Jackson was closed and placed in a receivership by the Farm Credit Administration after examiners determined that an additional infusion of federal funds would be "futile."[118]

2. *Merger of System Institutions*

The 1987 Act mandated the merger of the federal land bank and the federal intermediate credit bank in each district within six months after January 6, 1988.[119] The merged FLB and FICB within each district are now known as the Farm Credit Banks.[120]

The Farm Credit Banks, acting through FLBAs, will continue to provide real estate loans.[121] However, the Farm Credit Banks can transfer direct loan making authority to an FLBA.[122]

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115. 12 U.S.C.A. § 2279aa-5(2) (West 1989).

116. 12 U.S.C.A. § 2160 (West 1989).

117. Bullock & Dodson, *The Farm Credit System: It Was A New Lease On Life, But . . .*, CHOICES, First Quarter 1988, at 32.

118. 53 Fed. Reg. 18,812 (1988) (order appointing receiver) (the order has been amended at least twice, 53 Fed. Reg. 47,762 (1988), 55 Fed. Reg. 3,644 (1990)). *See also* Wall St. J., May 23, 1988, at 4, col. 1 (reporting on the receivership order); GENERAL ACCOUNTING OFFICE, PUB. NO. GGD-90-16, FARM CREDIT: BASIS FOR DECISION NOT TO ASSIST JACKSON FEDERAL LAND BANK (1989) (critical study of the decision to place the Jackson FLB in receivership); *Behind The Takeover of Jackson Farm Credit*, AGRIFINANCE NEWS, July 1988, at 1 (discussing the Jackson FLB receivership); Hughes, *Jackson FLB In Receivership*, AGRIC. OUTLOOK, July 1988, at 20 (same). Subsequently, the loans of the Jackson FLB were sold to the Farm Credit Bank of Texas, and the three states formerly served by the Jackson FLB, Alabama, Mississippi, and Louisiana, are now served by the Farm Credit Bank of Texas. FARM CREDIT ADMIN., 4 FCA BULL. 2-3 (1989). Some of the events leading up to the placing of the Jackson FLB in receivership are discussed in Federal Land Bank of Jackson in Receivership v. Federal Intermediate Credit Bank (of Jackson), 727 F. Supp. 1055, 1056-57 (S.D. Miss. 1989). *See also* Grant v. Federal Land Bank of Jackson, 559 So.2d 148, 150-55 (La. Ct. App. 1990) (discussing the Jackson FLB's receiver's liability under the *"D'Oench* doctrine" [D'Oench, Duhme & Co. v. Federal Deposit Insurance Corp., 315 U.S. 676 (1942)] in a lender liability action), *cert. denied*, 563 So.2d 886, 887 (La. 1990); Note, *Borrower Beware: D'Oench, Duhme and Section 1823 Overprotect the Insurer When Banks Fail*, 62 S. CAL. L. REV. 253 (1988) (discussing the *"D'Oench* doctrine").

119. Pub. L. No. 100-233, 401, 101 Stat. 1568, 1622 (1988). *See also supra* note 99 (discussing the mandatory merger of district FLBs and FICBs into district farm credit banks).

120. 12 U.S.C.A. § 2011 (West 1989).

121. 12 U.S.C.A. §§ 2015, 2013(18), 2021(a), 2091, 2093(9) (West 1989). Where there is no active association, the Farm Credit Bank may make the loan directly. 12 U.S.C.A. § 2021(b) (West 1989).

122. 12 U.S.C.A. § 2013(18) (West Supp. 1989). When the direct lending authority has been delegated to a FLBA, the association is referred to as a "Federal land credit

PCAs will continue to provide short and intermediate term loans.[123] Those loans may be discounted by the Farm Credit Banks, and associations, including both federal land bank and production credit associations, will continue to be supervised by the Farm Credit Banks.[124]

Under the 1987 Act, a PCA and an FLBA may merge.[125] If a merger occurs, the Farm Credit Banks must transfer the direct lending authority for long-term real estate mortgage loans to the FLBA.[126] Further, merged associations are referred to as "agricultural credit associations" (ACAs).[127]

The Act also required the twelve banks for cooperatives and the Central Bank for Cooperatives to consider consolidation into one national bank for cooperatives.[128] The St. Paul, Springfield, Jackson, and Spokane Banks recently voted not to consolidate; the remaining eight banks will consolidate into one national bank.[129]

The 1987 Act removed the requirement that a borrower must purchase stock in the amount of five percent of the face value of the loan.[130] A borrower now must purchase stock in an amount as set by the lender, subject to FCA regulation.[131] The FCA has

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association". 55 Fed. Reg. 24,861, 24,889 (1990) (to be codified at 12 C.F.R. § 619.9155). *See also* 55 Fed. Reg. 24,861, 24,881 (1990) (to be codified at 12 C.F.R. § 614.4030) (lending authority for federal land credit associations).

123. 12 U.S.C.A. §§ 2073(13), 2075 (West 1989).

124. 12 U.S.C.A. §§ 2013(6), (13), (17)-(21) (West Supp. 1989). *See also* 55 Fed. Reg. 24,861, 24,882-83 (to be codified at 12 C.F.R. subpt. C) (final rules relating to the farm credit bank/association relationship) (The FCA still has not adopted in final form other rules relating to loan policies and operations proposed on November 3, 1988, at 53 Fed. Reg. 44,438-44,456 (1990)). *See* 55 Fed. Reg. 24,861, 24862 (1990)).

125. 12 U.S.C.A. § 2279c-1 (West 1989). The 1987 Act directed that, not later than six months after the merger of the FLBs and FICBs into district farm credit banks, the board of directors of the FLBAs and PCAs were to submit to their respective association's shareholders a proposal to merge the FLBAs and PCAs serving the same geographical area. Pub. L. No. 10-233, 411, 101 Stat. 1568, 1368 (1988). *See also* 12 U.S.C.A. § 2071 (West 1989) (setting for section 411 in the annotations). The 1987 Act also permits "like" associations to merge, i.e., a PCA may merge with another PCA. 12 U.S.C.A. § 2279f-1 (West 1989).

126. 12 U.S.C.A. § 2279b(b) (West 1989). *See also* 55 Fed. Reg. 24,861, 24,882 (1990) (loan authority for the "agricultural credit associations" formed by the merger of "unlike" associations).

127. 55 Fed. Reg. 24,861, 24,888 (1990) (to be codified at 12 C.F.R. § 619.9015).

128. Pub. L. No. 100-233, 413, 101 Stat. 1568, 1639-42 (1988). *See also* 12 U.S.C.A. § 2121 (West 1989) (setting forth the terms of section 413 in the annotations).

129. *National Bank for Cooperatives Formed by Merger Vote*, AGRIFINANCE NEWS, August 1988, at 4. A bank for cooperatives may merge with district farm credit bank. 12 U.S.C.A. § 2279f(a) (West 1989). When such a merger occurs, the resulting bank is known as an "agricultural credit bank". 55 Fed. Reg. 24,861, 24,888 (1990) (to be codified at 12 C.F.R. § 619.9020). *See generally* Hopkin, Sporleder, Padberg & Knutson, *Evaluation of Restructuring Alternatives for the Banks for Cooperatives*, 3 J. AGRIC. COOPERATION 71 (1988) (discussing the consolidation alternatives for the banks of cooperatives).

130. 12 U.S.C.A. §§ 2034, 2294 (West 1980). *See supra* notes 59 & 68 and the accompanying text.

131. 12 U.S.C.A. §§ 2074, 2094 (West Supp. 1989).

issued regulations providing that the amount of stock required to be purchased must be not less than two percent of the loan amounts or $1,000, whichever is less.[132]

Finally, the 1987 Act also requires the Farm Credit Administration to propose a plan for the merger of the twelve districts into no less than six districts.[133] The various Farm Credit Banks are to submit the proposed merger affecting it to its members for their approval.[134]

K. "FARM CREDIT SERVICES" AS A TRADE NAME, THE FEDERAL FARM CREDIT CORPORATION OF AMERICA, AND THE FARM CREDIT COUNCIL

As has been briefly described above and is discussed elsewhere in this article, the Farm Credit System consists of various "System institutions," most notably the district Farm Credit Banks, Banks For Cooperatives, and various federal land bank associations and production credit associations within each district. Each System institution is a federally-chartered instrumentality and, as such, is a separate legal entity.[135] However, the various institutions often hold themselves out as being, or being a part of, "Farm Credit Services." "Farm Credit Services" is a trade name;

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132. 12 C.F.R. § 614.5220(d) (1990).

133. Pub. L. No. 100-203, 412, 101 Stat. 1568, 1638-39 (1988). *See also* 12 U.S.C.A. § 2002 (West 1989) (setting forth the terms of section 412 in the annotations).

134. *Id.* A more detailed explanation of the structural changes occasioned by the 1987 Act can be found in a FARMERS' LEGAL ACTION GROUP, INC., SPECIAL REPORT ON THE AGRICULTURAL CREDIT ACT OF 1987 (1988), available from the Farmers' Legal Action Group, Inc., 1301 Minnesota Building, 46 East Fourth Street, St. Paul, Minnesota, 55101. *See also* Davidson, *Agricultural Credit Act of 1987*, AGRIC. L. UPDATE, Feb. 1988, at 7 (surveying the provisions of the 1987 Act); M. HUGHES, RECENT DEVELOPMENTS AT THE FARM CREDIT SYSTEM (Econ. Res. Serv., USDA, Agric. Inf. Bulletin No. 572, 1989) (summarizing the structural changes in the System resulting from the 1987 Act); Koenig & Hiemtra, *More Than A Facelift for FCS*, AGRIC. OUTLOOK, March 1988, at 22 (same); Kayl, *supra* note 6, at 311-18 (same); Duncan, *The Agricultural Credit Act of 1987—A View from the Farm Credit Administration*, 2 J. AGRIC. LENDING 7 (1988) (same); Lugar, *The Agricultural Credit Act of 1987 — A View from the Hill*, 2 J. AGRIC. LENDING 12 (1988) (same); Harl, *Policy Considerations Related to Further Intervention in the Farm Credit System*, 2 J. AGRIC. COOPERATION 57 (1987) (written before the passage of the 1987 Act, this article highlights many of the policy considerations underlying the provisions that were enacted). Appended to this article as Appendix B is a flow chart of the Farm Credit System current as of July 1989.

The 1987 Act also contained significant new "borrowers' rights" provisions. Those provisions are discussed later in this article. *See infra* notes 340-434 and the accompanying text. *See also* Massey & Schneider, *supra* note 6, at 589-624 (focusing exclusively on the "borrowers' rights" provisions of the 1987 Act); Hambright, *The Agricultural Credit Act of 1987*, 17 COLO. LAW. 611 (1988) (same); Saxowsky, *Government Response to Financial Stress: The Farm Experience*, 3 NAT. RESOURCES & ENV'T 28 (1989) (surveying the governmental response to the farm credit crisis of the 1980s, including the changes legislatively imposed on the System).

135. *See infra* note 150 and the accompanying text.

it is not a legal entity. Accordingly, "Farm Credit Services," as such, is not capable of suing or being sued.

The various Farm Credit System banks are authorized to create organizations to perform certain functions or services for the banks.[136] Two such organizations have been organized under charters issued by the FCA. The first, initially established in July, 1985, by the district banks, is the Farm Credit Corporation of America (FCCA) located in Denver, Colorado.[137] Among other things, the FCCA provides centralized financial and management guidance to the district banks.[138] The second, the Farm Credit Council, is the trade association of the System banks and associations.[139] Essentially a lobbying organization, its offices are in Washington, D.C.[140]

III. LITIGATION INVOLVING THE FARM CREDIT SYSTEM

A. FEDERAL JURISDICTION

Federal jurisdiction over FLBAs and PCAs is limited. Unless diversity of citizenship exists to satisfy the requirement of 28 U.S.C. § 1332,[141] the only other currently possible bases for federal jurisdiction over FLBAs and PCAs are federal question jurisdiction under 28 U.S.C. § 1331,[142] premised on the theory that the Farm Credit Act, as amended, implies a private cause of action;[143] the Racketeer Influenced and Corrupt Organizations Act;[144] and the Equal Credit Opportunity Act.[145] As will be discussed later in this article, the prevailing view is that the Farm Credit Act of 1971 does not create an implied private cause of action.[146] Further, it also appears that claims based on the Farm Credit Amendments Act of 1985 may not satisfy 28 U.S.C. § 1331. The Eighth Circuit and the Minnesota Court of Appeals have recently held that the

136. 12 U.S.C.A. § 2211 (West 1989). *See also* 12 C.F.R. § 611.1135 (1990) (providing for the incorporation of service organizations).

137. *See generally The Farm Credit System: New Players, New Goals* (Interview with Brent Beesley, President and Chief Executive Office of the FCCA), LANDOWNER, Aug. 25, 1986, at 3 (discussing the history of the FCCA).

138. *Id.*

139. *Id.*

140. *Id.* In late 1989, plans were underway to disband the Farm Credit Corporation of America (FCCA) and to divide its functions between the Farm Credit Council (FCC) and the Federal Farm Credit Banks Funding Corporation. *See Farm Credit System Aims for New Year Start of New Farm Credit Council*, AGRIC CREDIT LETTER, Dec. 15, 1989, at 1.

141. 28 U.S.C.A. § 1332 (West 1966 & Supp. 1990).

142. 28 U.S.C.A. § 1331 (West 1966 & Supp. 1990).

143. *See infra* notes 184-267 and the accompanying text.

144. 18 U.S.C.A. §§ 1961-1968 (West 1984 & Supp. 1990).

145. 15 U.S.C.A. §§ 1691-1691f (West 1982 & Supp. 1990).

146. *See infra* notes 184-94 and the accompanying text.

1985 Act did not create an implied private right of action for damages.[147] Whether the Agricultural Credit Act of 1987 implies a private right of action also appears to be headed for a negative resolution. The Ninth, Tenth, and Eighth Circuits have held that there is no implied private cause of action for injunctive relief under the 1987 Act.[148] The Eighth Circuit's decision, one reached by the court sitting *en banc*, vacated an earlier panel decision finding an implied cause of action for injunctive relief to remedy the failure of System lenders to follow a procedural directive in the 1987 Act.[149]

1. *Status as Federally Chartered Instrumentalities*

The mere status of the FCBs, FLBAs, and PCAs as federally chartered instrumentalities of the United States does not create federal court jurisdiction. FLBAs and PCAs are federally chartered instrumentalities of the United States.[150] In that regard, 29 U.S.C. § 1349[151] provides as follows:

> The district courts shall not have jurisdiction of any civil action by or against any corporation upon the ground that it was incorporated by or under an Act of Congress, unless the United States is the owner of more than one-half of its capital stock.[152]

Further, 28 U.S.C. § 1349 has been held to preclude federal court jurisdiction over a claim against a FLB premised on an allegation

147. The following cases have found that there is no implied right of action for damages in the 1985 Act: Redd v. Federal Land Bank of St. Louis, 851 F.2d 219 (8th Cir. 1988); Mendel v. Production Credit Ass'n of the Midlands, 862 F.2d 180 (8th Cir. 1988); Ebenhoh v. Production Credit Ass'n of Southeast Minnesota, 426 N.W.2d 490 (Minn. Ct. App. 1988). *See also* Hillesland v. Federal Land Bank Ass'n of Grand Forks, 407 N.W.2d 206, 208-10 (N.D. 1987) (finding no implied action in a wrongful discharge action and holding that a member of Congress's statements made during the debate on the 1985 Act were irrelevant to determining whether Congress intended to create an implied cause of action under the 1971 Act).

148. Harper v. Federal Land Bank of Spokane, 878 F.2d 1172 (9th Cir. 1989), *cert. denied*, 110 S. Ct. 867 (1990); Griffin v. Federal Land Bank of Wichita, 902 F.2d 22 (10th Cir. 1990); Zajac v. Federal Land Bank of St. Paul, No. 88-5353ND (8th Cir. July 31, 1990) (*en banc*) (1990 U.S. App. LEXIS 12932).

149. Zajac v. Federal Land Bank of St. Paul, 887 F.2d 844 (8th Cir. 1989), *vacated on grant of reh'g en banc*, Dec. 7, 1989 (1989 U.S. App. LEXIS 18809).

150. 12 U.S.C.A. §§ 2011(a) (FCBs), 2091(a) (FLBAs), 2071(a) (PCAs) (West 1989).

151. 28 U.S.C.A. § 1349 (West 1976).

152. *Id.* The United States does not own stock in the Farm Credit System, the last federal government stock having been retired in 1968. Brake, *supra* note 18, at 576; *In re* Hoag Ranches, Inc., 846 F.2d 1225, 1228 (9th Cir. 1988). The "bail out" provisions of the Agricultural Credit Act of 1987 did not involve the acquisition of System institution stock by the United States. *See generally supra* notes 105-08 and the accompanying text (discussing the "bail out" provisions of the 1987 Act).

that the FLB was a federally chartered instrumentality.[153]

Also, System institutions are generally not considered foreign corporations under state certificate of authority statutes. This is because

> [i]t is well settled that "[c]orporations created by the authority of the United States are not foreign corporations but have legal existence in every state in which they may transact business pursuant to the authority conferred upon them by Congress."[154]

Thus, the status as federally chartered instrumentalities does not create federal court jurisdiction.

2. *Citizenship*

For purpose of diversity and other jurisdictional bases, a System institution is "deemed to be a citizen of the State, commonwealth, or District of Columbia in which its principal office is located."[155]

3. *Fifth Amendment*

There is no federal question jurisdiction under 28 U.S.C. § 1331 against an FLBA or PCA based on a claim arising under the fifth amendment to the United States Constitution because those

153. Federal Land Bank of Columbia v. Cotton, 410 F. Supp. 169, 170 (N.D. Ga. 1975) (also holding that the FLB was not an agency within the meaning of 28 U.S.C.A. §§ 451 & 1349 (West 1976) *Id.* at 171) (In subsequent litigation involving the same parties, 28 U.S.C. § 1349 was cited for the proposition that "[t]he mere fact that defendant is federally chartered does not support federal jurisdiction". Cotton v. Federal Land Bank of Columbia, 647 F. Supp. 37, 38 n. 1 (M.D. Ga. 1986), *aff'd*, 887 F.2d 1091 (11th Cir. 1989)). *Accord* Federal Land Bank of St. Louis v. Keiser, 628 F. Supp. 769, 771 (C.D. Ill. 1986). *See also* Franklin v. Federal Land Bank of St. Louis, 96 Bankr. 929, 931-34 (W.D. Mo. 1989) (holding that a FLB's status as a federally chartered instrumentality is not sufficient to support procedural due process claim or federal question jurisdiction); LPR Land Holdings v. Federal Land Bank of St. Paul, 651 F. Supp. 287, 289-92 (E.D. Mich. 1987) (same, rejecting the argument that Federal Land Bank of St. Paul v. Bismarck Lumber Co., 314 U.S. 95 (1941), and Greene County Nat'l Farm Loan Ass'n v. Federal Land Bank of Louisville, 152 F.2d 215 (6th Cir. 1945), stand for the contrary proposition); Hill v. Farm Credit Bank of St. Louis, 726 F. Supp. 1201, 1208 (E.D. Mo. 1989) (same, citing additional cases); *In re* Hoag Ranches, 846 F.2d 1225, 1227-28 (9th Cir. 1988) (PCA not an "agency" within the meaning of Fed. R. App. P. 4(a)(1)).

154. Federal Land Bank of St. Paul v. Gefroh, 390 N.W.2d 46, 47 (N.D. 1986) (quoting Federal Land Bank of Omaha v. Felt, 368 N.W.2d 592, 595 (S.D. 1985)). *See also* Federal Land Bank of St. Paul v. Anderson, 410 N.W.2d 709, 713 (N.D. 1987) (holding that a FLB is not subject to state registration requirements); Kolb v. Naylor, 658 F. Supp. 520, 526 (N.D. Iowa 1987) (same); Federal Land Bank of St. Paul v. Bagge, 394 N.W.2d 694, 696 (N.D. 1986) (same, relying on *Gefroh*).

155. 12 U.S.C.A. § 2258 (West 1989). *See also* Engelmeyer v. Production Credit Ass'n of the Midlands, 652 F. Supp. 1235, 1237 (D.S.D. 1987) (citing section 2258; Cotton v. Federal Land Bank of Columbia, 647 F. Supp. 37, 38-39 (D. Ga. 1986)); and Apple v. Miami Valley Production Credit Ass'n, 614 F. Supp. 119, 122 (D. Ohio 1985)).

entities are private rather than governmental.[156] However, the Eighth Circuit has found a "colorable basis" for jurisdiction for a fifth amendment claim against a PCA based on the "pervasive involvement of the federal government in the creation and operation of the production credit associations."[157]

4. *Federal Common Law*

There is no 28 U.S.C. § 1331 jurisdiction under the federal common law based on a claim of breach of fiduciary duty.[158] The fiduciary obligations of FLBAs and PCAs will be discussed in greater detail later in this article.[159]

5. *Section 1983*

Federal instrumentalities are not "persons" subject to section 1983 liability.[160] Thus, there is no 28 U.S.C. § 1343 jurisdiction based on a claim arising under 42 U.S.C. § 1983.

6. *Tucker Act*

Unless there is at issue a claim based on a substantive right, there is no jurisdiction under the Tucker Act.[161] In addition, the

156. *E.g.*, Birbeck v. Southern New England Production Credit Ass'n, 606 F. Supp. 1030, 1034-35 (D. Conn. 1985) (citing DeLaigle v. Federal Land Bank of Columbia, 568 F. Supp. 1432, 1439 (S.D. Ga. 1983), *overruled on other grounds sub nom.* Smith v. Production Credit Ass'n, 777 F.2d 1544, 1548 n. 1 (11th Cir. 1985)); Federal Land Bank of Wichita v. Jost, 761 P.2d 270, 271 (Colo. Ct. App. 1988) (relying on *DeLaigle* and Federal Land Bank v. Read, 703 P.2d 777, 78-81 (Kan. 1985)). *See also supra* note 153 (citing other cases).

157. Schlake v. Beatrice Production Credit Ass'n, 596 F.2d 278, 281 (8th Cir. 1979) (citing Duke Power Co. v. Carolina Environmental Study Group, Inc., 438 U.S. 59 (1978)). *But see* Hill v. Farm Credit Bank of St. Louis, 726 F. Supp. 1201, 1208 (E.D. Mo. 1989) (declining to follow *Schlake*); Franklin v. Federal Land Bank of St. Louis, 96 Bankr. 929, 934 (W.D. Mo. 1989) (declining to follow *Schlake* and citing Boyster v. Roden, 628 F.2d 1121 (8th Cir. 1980), in support of the assertion that "[e]ven the Eighth Circuit Court of Appeals has treated *Schlake* as an aberration"); LPR Land Holdings v. Federal Land Bank of St. Louis, 651 F. Supp. 287, 291 (E.D. Mich. 1987) (declining to follow *Schlake*); Birbeck v. Southern New England Production Credit Ass'n, 606 F. Supp. 1030, 1034 n. 1 (D. Conn. 1985) (criticizing *Schlake*); United States v. Haynes, 620 F. Supp. 474, 477 (M.D. Tenn. 1985) (declining to follow *Schlake*); *In re* Hoag Ranches, 846 F.2d 1225, 1228-29 (9th Cir. 1988) (same).

158. *Birbeck*, 606 F. Supp. at 1039-44. *See also* Boyster v. Roden, 628 F.2d 1121, 1125 (8th Cir. 1980) (holding that the fiduciary obligations of System institutions are governed by state law, not federal law).

159. *See infra* notes 300-39 and the accompanying text.

160. *Birbeck*, 606 F. Supp. at 1044-45. *See also* Harper v. Federal Land Bank of Spokane, 878 F.2d 1172, 1178 (9th Cir. 1989) (holding that section 1983 is not available because of the absence of state action), *cert. denied*, 110 S. Ct. 867 (1990); Walker v. Federal Land Bank of St. Louis, 726 F. Supp. 211, 214 (C.D. Ill. 1989) ("the FCB is, itself, not a state actor, and thus is not a 'person' for purposes of 1983"); Kolb v. Naylor, 658 F. Supp. 520, 524 (N.D. Iowa 1987) (the "use of state law to foreclose is not sufficient to allege a claim under section 1983").

161. 28 U.S.C.A: §§ 1346(a)(2), 1491(a)(1) (West Supp. 1990). The Tucker Act gives the federal district courts and the United States Claims Court jurisdiction over claims against the United States founded on the United States Constitution, an Act of Congress, a

Tucker Act does not create substantive rights.[162] Also, the Tucker Act does not extend to entities in which the United States has no proprietary interest, and, thus, it does not apply to System lenders.[163]

7. *Truth In Lending*

Credit transactions primarily for agricultural purposes are exempt from the disclosure requirements of the Truth-In-Lending Act.[164] Thus, in virtually all instances, FLB and PCA loans will be exempt from disclosure requirements of the Truth-In-Lending Act.[165]

8. *Federal Tort Claims Act*

The correct rule is that FLBAs and PCAs are not agencies for purposes of the Federal Tort Claims Act (FTCA).[166] However, the Montana Supreme Court recently took the opposite position on this issue, although it later reversed its position in the same case and withdrew its earlier decision. In its initial decision in *Tooke v. Miles City Production Credit Association*,[167] the Montana Supreme Court held that PCAs were subject to the FTCA.[168] In *Tooke*, the Tookes brought suit against the PCA in state court alleging that the PCA had breached its fiduciary duties to them and committed fraud in considering the Tookes' loan application.[169] The court found that the case should have been brought under the FTCA for two reasons.[170] First, the PCA was a federal instrumentality under the test set out in *Lewis v. United States*,[171]

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regulation of an executive department, an express or implied contract with the United States, or an other basis for liquidated or unliquidated damages not sounding in tort. The district court's jurisdiction is limited to claims up to $10,000 and does not include certain claims under the Contract Disputes Act. 28 U.S.C.A. § 1346(a)(2) (West Supp. 1990).

162. *Birbeck*, 606 F. Supp. at 1045.

163. *Id.*

164. 15 U.S.C.A. § 1603(1) (West 1982).

165. *See* Gregory v. Federal Land Bank of Jackson, 515 So. 2d 1200, 1203 (Miss. 1987). *See also* Felt v. Federal Land Bank Ass'n of Belle Fourche, 760 F.2d 209, 210-11 (8th Cir. 1985) (affirming dismissal of claim under the Truth in Lending Act on grounds that the action was time-barred and because of the agricultural purpose exemption).

166. 28 U.S.C.A. §§ 2671-2680 (West 1965 & Supp. 1990); South Central Iowa Production Credit Ass'n v. Scanlon, 380 N.W.2d 699, 700-03 (Iowa 1986); Kolb v. Naylor, 658 F. Supp. 520, 525-26 (N.D. Iowa 1987).

167. Tooke v. Miles City Production Credit Ass'n, No. 87-409 (Mont. March 3, 1988) (Westlaw, MT-CS database, 1988 WL 27167) [hereinafter *Tooke I*], *withdrawn*, 763 P.2d 1111 (Mont. 1988).

168. That holding was reversed when the initial opinion was withdrawn by Tooke v. Miles City Production Credit Ass'n, 763 P.2d 1111 (Mont. 1988).

169. *Tooke I*, slip op. at 3.

170. *Id.*

171. 680 F.2d 1239 (9th Cir. 1982). *Lewis* described the test to determine whether an entity was a federal agency within the meaning of the FTCA as follows: the entity must

and, as a federal instrumentality, it was subject to the FTCA unless the FTCA specifically exempted it from coverage.[172] Second, while the FLB and the FICB were specifically exempted from the FTCA,[173] PCAs were not; thus, they were subject to the FTCA.[174]

The decision was unsound. In essence, it was premised on the notion that the federal government exercises "control over the . . . [PCA's] detailed physical performance and day to day operation."[175] Although recent federal legislation governing the Farm Credit System has been increasingly prescriptive, and the FCA has acquired the status of an independent regulator, PCAs continue to be farmer-owned cooperatives with considerable autonomy.[176] Fortunately, although it claimed to base its change of opinion on "new authority" and not its initial faulty reasoning, the Montana Supreme Court subsequently withdrew its initial opinion in *Tooke* and substituted it with one holding that the PCA was not a federal agency for purposes of the FTCA.[177]

9. *Securities Act*

FLBA and PCA Class B stock is not subject to the Securities Act of 1933[178] or the Securities Exchange Act of 1934.[179] Thus,

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have federal government control over detailed physical performance and daily operation of the entity. *Id.* at 1240. Other factors considered include whether the entity is an independent corporation, whether the government is involved in the entity's finances, and whether the mission of the entity furthers the policy of the United States. *Id.* at 1240-41.

172. *Tooke I*, slip op. at 7.

173. 28 U.S.C.A. § 2680(n) (West 1965).

174. *Tooke I*, slip op. at 7.

175. *Id.*

176. *See generally* HOUSE COMM. ON GOVERNMENT OPERATIONS, FARM CREDIT ADMINISTRATION'S ROLE IN THE SYSTEM'S CRISIS, H. REP. NO. 99-561, 99th Cong., 2nd Sess. 3 (recommending that the FCA implement its new functions under the Farm Credit Amendments Act of 1985, Pub. L. No. 99-205, 99 Stat. 1678 (1985), so as to "zealously guard the cooperative principles of FCS so that as much authority as possible can be exercised at the lowest possible level of the system"); Federal Land Bank of Springfield v. Farm Credit Admin., 676 F. Supp. 1239, 1241 (D. Mass. 1987) (characterizing Farm Credit System banks and associations as "autonomous and locally-oriented," while also being "interdependent and financially interrelated"); Central Kentucky Production Credit Ass'n v. United States, 846 F.2d 1460, 1461 (D.C. Cir. 1988) ("The FCA is an independent regulatory agency that does not itself make, subsidize, or guarantee agricultural loans. Instead, borrowers obtain credit from a national network of privately owned banks and associations"). The autonomy of some PCAs allowed them to prosper while other System institutions were floundering in the 1980s. *See* Sikeston Production Credit Ass'n v. Farm Credit Admin., 647 F. Supp. 1155 (E.D. Mo. 1986); Colorado Springs Production Credit Ass'n v. Farm Credit Admin., 695 F. Supp. 15 (D.D.C. 1988).

177. Tooke v. Miles City Production Credit Association, 763 P.2d 1111, 1114-16 (Mont. 1988) (The court relied heavily on the analysis followed in *In re* Hoag Ranches, 846 F.2d 1225 (9th Cir. 1988), which concluded that a PCA was not a government agency under Fed. R. App. P. 4(a)(1)).

178. 15 U.S.C.A. §§ 77a-77bbbb (West 1981 & Supp. 1990).

179. 15 U.S.C.A. § 771 (West 1981); Dau v. Federal Land Bank of Omaha, 627 F. Supp. 346, 348-49 (N.D. Iowa 1985); Seger v. Federal Intermediate Credit Bank of Omaha, 850 F.2d 468, 469 (8th Cir. 1988); Wiley v. Federal Land Bank of Louisville, 657 F. Supp. 964,

farm borrowers are denied any remedies under the Securities Act.

10. *Federal Indenture Act*

FLBA and PCA stock is exempt under the Federal Indenture Act,[180] thus preventing farm borrowers from seeking any remedies under the Act.

11. *Equal Credit Opportunity Act*

Farm Credit System institutions are subject to the Equal Credit Opportunity Act.[181] Therefore, Farm Credit Institutions must not violate the Equal Credit Opportunity Act regulations.

12. *Fair Debt Collection Practices Act*

In virtually all instances, FLBAs and PCAs will be exempt from the Fair Debt Collection Practices Act[182] because the debt was not incurred for "personal, family, or household purposes."[183] Thus, farm borrowers cannot look to the Fair Debt Collection Practices Act for relief.

13. *Implied Cause of Action Under the Farm Credit Act of 1971 and the Farm Credit Amendments Act of 1985*

Claims of an implied private right of action under the Farm Credit Act of 1971 as the Act existed prior to the effective date of the 1985 amendments have been unsuccessful.[184] In virtually all of those cases, the borrowers were seeking the benefit of the loan

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966 (S.D. Ind. 1987) (also holding that System institutions are not subject to the National Bank Act, 12 U.S.C. §§ 85, 86).

180. 15 U.S.C.A. §§ 78a-78kk (West 1981 & Supp. 1990); *Dau*, 627 F. Supp. at 349 (also rejecting a claim under the federal Real Estate Settlement Procedures Act, 12 U.S.C.A. §§ 2601-17 (West 1980 & Supp. 1990), because of the exemptions for parcels in excess of 25 acres).

181. 15 U.S.C.A. §§ 1691-1691f (West 1982 & Supp. 1990).

182. 15 U.S.C.A. §§ 1692-1693r (West 1982 & Supp. 1990).

183. 15 U.S.C.A. §§ 1692a(5) (West 1982 & Supp. 1990); Munk v. Federal Land Bank of Wichita, 791 F.2d 130, 132 (10th Cir. 1986).

184. The following cases have rejected a private cause of action under the Farm Credit Act of 1971: Bowling v. Block, 785 F.2d 556 (6th Cir. 1985), *cert. denied*, 479 U.S. 829 (1986); Smith v. Russellville Production Credit Ass'n, 777 F.2d 1544 (11th Cir. 1985); Aberdeen Production Credit Ass'n v. Jarrett Ranches Inc., 638 F. Supp. 534 (D.S.D. 1986); Corum v. Farm Credit Services, 628 F. Supp. 707 (D.Minn. 1986); Spring Water Dairy Inc. v. Federal Intermediate Credit Bank of St. Paul, 625 F. Supp. 713 (D. Minn. 1986); Apple v. Miami Valley Production Credit Ass'n, 614 F. Supp. 119 (S.D. Ohio 1985), *aff'd*, 804 F.2d 917 (6th Cir. 1986); Hartman v. Farmers Production Credit Ass'n of Scottsburg, 628 F. Supp. 218 (S.D. Ind. 1983); Yankton Production Credit Ass'n v. Jensen, 416 N.W.2d 860 (S.D. 1987); Production Credit Ass'n of Worthington v. Van Iperen, 396 N.W.2d 35 (Minn. Ct. App. 1986); and Johansen v. Production Credit Ass'n of Marshall-Ivanhoe, 378 N.W.2d 59 (Minn. Ct. App. 1985).

servicing regulations[185] promulgated pursuant to the Act.

As it existed prior to the regulations promulgated under the 1985 amendment, those loan servicing regulations provided, in relevant part, that System banks and associations that were originating lenders were to "adopt loan servicing policies and procedures to assure that loans will be serviced fairly and equitably for the borrower while minimizing the risk for the bank and associations."[186] Also, the regulations provided that the "policy shall provide a means of forbearance for cases when the borrower is cooperative, making an honest effort to meet the conditions of the loan contract and is capable of working out of the debt burden."[187]

At the risk of oversimplifying the issue, the courts that have rejected the argument that the Farm Credit Act of 1971 implies a private cause of action have done so on two basic grounds. First, with the exception of one federal district court, courts have refused to find that the forbearance policies contemplated by the former loan servicing regulations are substantive rules having the force and effect of law.[188] Rather, the forbearance rules have been found to be merely general statements of agency policy and therefore did not provide a basis for an implied cause of action.[189]

The second ground for rejecting assertions of an implied cause of action under the Farm Credit Act of 1971 has been the absence of any legislative history reflecting a Congressional intent to imply a federal remedy.[190] In applying the fourfold test for ascertaining the existence of an implied cause of action in a federal statute enunciated in *Cort v. Ash*,[191] the courts have tended to focus on the legislative intent prong of the test. The conclusion of the court in *Bowling v. Block*[192] is representative:

> It is readily apparent that the Farm Credit Act

185. 12 C.F.R. § 614.4510 - .4512 (1986) (removed 51 Fed. Reg. 39,486, 39,502 (1986)).
186. 12 C.F.R. § 614.4510 (1986) (removed 51 Fed. Reg. 39, 486, 39,502 (1986).
187. 12 C.F.R. § 614.4510(d)(1), (2) (1986) (removed 51 Fed. Reg. 39,486, 39,502 (1986).
188. *Compare* DeLaigle v. Federal Land Bank of Columbia, 568 F. Supp. 1432, 1436-38 (S.D. Ga. 1983) (concluding that section 614.4510 has the "force and effect of law") *with* Smith v. Russellville Production Credit Ass'n, 777 F.2d at 1457-58 ("we disapprove of DeLaigle v. Federal Land Bank of Columbia, *supra*, to the extent that it may be inconsistent with this opinion").
189. Smith v. Russellville Production Credit Ass'n, 777 F.2d at 1548; Federal Land Bank of Springfield v. Saunders, 108 A.D.2d 838, 485 N.Y.Supp. 2d 342 (N.Y. App. Div. 1985), *appeal denied*, 479 N.E.2d 827.
190. *See, e.g.*, Bowling v. Block, 602 F. Supp. 667 (S.D. Ohio 1985), *aff'd*, 785 F.2d 556 (6th Cir.), *cert. denied*, 479 U.S. 829 (1986).
191. 422 U.S. 66, 78 (1975).
192. 602 F. Supp. 667, 670-71 (S.D. Ohio 1985), *aff'd*, 785 F.2d 556 (6th Cir.), *cert. denied*, 479 U.S. 829 (1986).

> merely established the machinery by which its purpose, to augment the amount of credit available to the farming community, would be effected. It does not create specific enforceable rights which would necessitate the existence of a private right of action. Further, the Act intimates that the specific entities it creates for the purpose or providing the needed credit — the production credit associations, the federal land bank associations and the banks for cooperatives — are to be operated much like any other private lending institution. Therefore, whatever disputes arise between plaintiffs and the nonfederal defendants must be resolved in the same manner that such a dispute would be resolved if the defendants were common banks or savings and loans.[193]

Thus, the issue of whether the Farm Credit Act of 1971, prior to its 1985 amendment, creates an implied cause of action appears to be firmly resolved in the negative. In light of recent decisions, the same also may be said for the issue of whether the Act, as amended in 1985, created an implied cause of action.

The enactment of the 1985 amendments arguably strengthened arguments for an implied cause of action in at least two respects. First, the availability of forbearance became no longer solely a matter of institutional policy. It was a congressional mandate.[194] Second, the legislative history of the 1985 amendments appeared to support the argument in favor of an implied cause of action.[195] In particular, during the floor debate in the House, Representative De La Garza, the Chairman of the House Committee on Agriculture and sponsor of the House bill[196] that formed the basis for the Act stated that ". . . it would be my understanding that the rights . . . [in the Act] shall be enforceable in courts of law."[197]

The test for determining whether one has an implied cause of action for relief under a federal statute was articulated by the United States Supreme Court in *Cort v. Ash*.[198] Those factors are as follows:

> First, is the plaintiff "one of the class for whose *espe-*

193. *Id.*
194. 12 U.S.C.A. § 2199(b) (West Supp. 1986) (amended 1988).
195. 131 CONG. REC. H11518-19 (daily ed. Dec. 10, 1985).
196. H.R. 3792, 99th Cong., 1st Sess. (1985).
197. 131 CONG. REC. H11518-19 (daily ed. Dec. 10, 1985).
198. 422 U.S. 66 (1975).

> *cial* benefit the statute was enacted . . . that is, does the statute create a federal right in favor of the plaintiff? Second, is there any indication of legislative intent, explicit or implicit, either to create such a remedy or to deny one? . . . Third, is it consistent with the underlying purposes of the legislative scheme to imply such a remedy for the plaintiff? . . . And finally, is the cause of action one traditionally relegated to state law, in an area basically the concern of the States, so that it would be inappropriate to infer a cause of action based solely on federal law?[199]

Shortly after the enactment of the 1985 amendments, two courts offered, in dicta, observations as to whether the 1985 amendments to the Farm Credit Act would support a private cause of action.[200] However, in both cases, the court did not need to resolve the issue because the plaintiff was asserting claims based on the Farm Credit Act arising prior to its amendment in 1985.[201]

In the first case to be reported, *Aberdeen Production Credit v. Jarrett Ranches, Inc.*,[202] the court noted the remarks on the House floor by Representative De La Garza.[203] However, because the acts challenged by the plaintiff occurred prior to the enactment of 1985 amendments, the court's remarks were limited to the following:

> This Court does not read this statement to indicate that all regulations of the Farm Credit System were intended to be enforceable in courts of law. The statement was expressly made in reference to "borrowers' rights" established in Title III, 301 et seq. of the 1985 Farm Credit Amendments Act — the "rights" of disclosure and access to documents. The defendants are not claiming any violation of rights allegedly established under the 1985 amendments. Therefore, this Court is not required to consider the significance of the 1985 Farm Credit Amendments Act in determining the existence of a private cause of action.[204]

In the second case, *Production Credit Association of Worth-*

199. Cort v. Ash, 422 U.S. at 78 (emphasis in original) (citations omitted).
200. *See infra* notes 204-10 and the accompanying text.
201. *Id.*
202. 638 F. Supp. 534 (D.S.D. 1986).
203. Aberdeen Production Credit Union v. Jarrett Ranches, 638 F. Supp. 534, 536-37 (D.S.D. 1986).
204. *Jarrett Ranches*, 638 F. Supp. at 537.

ington v. Van Iperen,[205] the court also found it unnecessary to resolve the issue of whether the 1985 amendments created a private cause of action.[206] A decision was unnecessary because "the amendments referred to by the [appellants] were not effective until after the contract date between the parties herein."[207] In passing over the question, however, the court correctly noted that the "substance of the Act" must also be examined and that exclusive reliance could not be made on the statements of Representative De La Garza.[208] The same court later held that no implied private cause of action exists under the 1985 Act.[209]

In subsequent actions where the issue was squarely presented, two federal district courts rejected contentions that the borrowers's rights provisions of the Farm Credit Amendments Act of 1985 created an implied cause of action in favor of Farm Credit System borrowers.[210] In the first of the two cases to be subsequently decided an appeal, *Redd v. Federal Land Bank of St.*

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205. 396 N.W.2d 35 (Minn. Ct. App. 1986).

206. Production Credit Ass'n of Worthington v. Van Iperen, 396 N.W.2d 35, 37 (Minn. Ct. App. 1986).

207. *Id.* at 38.

208. *Id.*

209. Ebenhoh v. Production Credit Ass'n of Southeast Minnesota, 426 N.W.2d 490 (Minn. Ct. App. 1988).

210. Redd v. Federal Land Bank of St. Louis, 661 F. Supp. 861 (E.D. Mo. 1987), *aff'd*, 851 F.2d 219 (8th Cir. 1988); Mendel v. Production Credit Ass'n of the Midlands, 656 F. Supp. 1212 (D.S.D. 1987), *aff'd*, 862 F.2d 180 (8th Cir. 1988). However, addressing a related issue, the North Dakota Supreme Court held that an FLB's failure to comply with the System's forbearance regulations may afford a basis for an equitable defense to a foreclosure action notwithstanding the absence of an implied cause of action. Federal Land Bank of St. Paul v. Overboe, 404 N.W.2d 445, 447-50 (N.D. 1987). *See also* Federal Land Bank of St. Paul v. Bosch, 432 N.W.2d 855, 858 (N.D. 1988) (following *Overboe* in the application of the "equitable defense"); Federal Land Bank of St. Paul v. Asbridge, 414 N.W.2d 596, 597 (N.D. 1987) (same); Federal Land Bank of St. Paul v. Huether, 454 N.W.2d 710, 715 (N.D. 1990) (same).

Unlike the issues in *Redd* and *Mendel*, the issue presented to the North Dakota Supreme Court in *Overboe* assumed that the Farm Credit Act did not afford borrowers a right of action. In *Overboe*, the question was whether, in the absence of a private right of action, a borrower could assert a federal land bank's failure to follow the System's forbearance regulations as a defense to a foreclosure action. 404 N.W.2d at 447. Relying on a line of cases that have allowed a mortgagee's failure to follow HUD mortgage servicing regulations promulgated under the National Housing Act to be asserted as an affirmative defense notwithstanding the absence of a private cause of action under that Act, the court resolved the issue in favor of the borrower. *Id.* at 450.

The administrative forbearance defense permitted by the *Overboe* court permits judicial consideration of both the procedural and substantive aspects of the System institution's action. In that regard, the initial inquiry is whether the institution "has established a general policy of forbearance and whether it applied that policy in arriving at its decision to seek foreclosure. *Id.* at 450. If the trial court finds that the borrower's qualifications were considered by the institution in accordance with its procedures, the court's review of the merits of that consideration must be confined to whether the institution abused its discretion. *Id.* In other words, to prevail, the borrower must show that the institution acted in an "arbitrary, capricious, unreasonable or unconscionable manner." *Id.* The *Overboe* court indicated that the appellate review of a trial court's determination of the substantive issue will be guided by the standard of whether the abuse

Louis,[211] the district court relied on the House Report's discussion of the rejection of an amendment to the 1985 legislation that would have held "directors and officers of the System personally and individually liable for damages suffered when they knowingly violate . . . [the] Act, or any rate regulation or order issued thereunder" as indicating an absence of any intention to create a private cause of action.[212] It bolstered its reliance on the House Report by concluding that the Act's granting of cease and desist powers to the Farm Credit Administration reflected a Congressional intention to so limit the remedy available for violations of the Act.[213] The court discounted Representative De La Garza's statement that the Act created a private cause of action[214] by finding that understanding to be inconsistent with the Act's creation of a remedy in favor of the Farm Credit Administration.[215]

The Eighth Circuit affirmed the district court's decision in *Redd* by finding that the second and third tests under *Cort v. Ash* were not met.[216] The Eighth Circuit agreed with the district court that the remarks of Representative De La Garza were not binding on the court in determining whether an implied cause of action exists.[217] The court looked at the "substance of the amendment to determine whether a cause of action should be implied, rather than the comments of committee persons as they field questions about the bill."[218] The Eighth Circuit reasoned that Congress was aware of the enforcement problems in the Act, but the court found that Congress had answered the problem by granting the FCA broad cease and desist powers.[219] The granting of such broad regulatory powers suggested to the court that Congress did not intend to grant borrowers a private right of action.[220]

The third test under *Cort v. Ash* also provided grounds for the

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of discretion standard of review "appears to have been misapprehended or grossly misapplied." *Id.*

The *Overboe* decision is discussed in greater detail later in this article. See *infra* notes 454-74 and accompanying text.

211. 661 F. Supp. 861 (E.D. Mo. 1987), *aff'd*, 851 F.2d 219 (8th Cir. 1988).

212. H.R. REP. No. 425, 99th Cong., 1st Sess. 44, *reprinted in* 1985 U.S. CONG. & ADMIN. NEWS 2587, 2631.

213. Redd v. Federal Land Bank of St. Louis, 661 F. Supp. at 863 (citing 12 U.S.C.A. §§ 2261, 2264, 2267(b), 2268(a) and (g), and 2269 (West Supp. 1986)).

214. See *supra* note 197 and the accompanying text.

215. *Redd*, 661 F. Supp. at 863-64 (citing 131 CONG. REC. H11518-19 (daily ed. Dec. 10, 1985)).

216. *Redd*, 851 F.2d at 221-22. *See supra* notes 198-99 and the accompanying text for a discussion of the *Cort v. Ash* test.

217. *Id.* at 222.

218. *Id.*

219. *Id.*

220. *Id.*

Eighth Circuit to determine no implied cause of action exists.[221] The court found that the purpose of the 1985 Act was to strengthen the financial condition of the System.[222] Thus, the court reasoned that granting money damages to the Redds would deplete the already diminishing resources of the System and defeat the legislation's purpose.[223]

In the second case to be decided on appeal, also by the Eighth Circuit, *Mendel v. Production Credit Association of the Midlands*,[224] the district court disagreed with the *Redd* court's dismissal of Representative De La Garza's remark.[225] The *Mendel* court found that Representative De La Garza's statement was sufficient to demonstrate intention to create a private remedy.[226] Nevertheless, the district court in *Mendel* also found that the underlying purpose of the 1985 amendments was to "shore up" the finances of the System, and that allowing recovery of monetary damages against a System institution would be inconsistent with that purpose.[227] On that basis, the court in *Mendel* invoked the third element of the *Cort v. Ash* test to deny a private right of action.[228] Relying on its earlier decision in *Redd*, the Eighth Circuit affirmed the result reached by the district court.[229]

14. *Implied Cause of Action Under the Agricultural Credit Act of 1987*

The 1987 Act also does not expressly provide a private cause of action against institutions of the Farm Credit System. However, shortly after System lenders began to implement the 1987 Act, borrowers began asserting that the 1987 Act created an implied private cause of action.[230]

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221. *Id.* *See supra* notes 198-99 and the accompanying text for a discussion of the *Cort v. Ash* test.

222. *Id.* at 222.

223. *Id.* at 222-23.

224. 656 F. Supp. 1212 (D.S.D. 1987), *aff'd*, 682 F.2d 180 (8th Cir. 1988).

225. *Mendel*, 656 F. Supp. at 1216.

226. *Id.*

227. *Id.*

228. *Id.*

229. Mendel v. Production Credit Ass'n of the Midlands, 862 F.2d 180 (8th Cir. 1989). The *Mendel* court repeated the court's earlier holding in *Redd* that the 1985 Amendments to the Farm Credit Act did not create an implied right of damages. *Id.* at 182.

230. Zajac v. Federal Land Bank of St. Paul, No. 88-5353ND (8th Cir. July 31, 1990) (*en banc*) (1990 U.S. App. LEXIS 12932) (no implied cause of action); Griffin v. Federal Land Bank of Wichita, 902 F.2d 22 (10th Cir. 1990) (no implied cause of action); Harper v. Federal Land Bank of Spokane, 692 F. Supp. 1244 (D. Or. 1988), *rev'd*, 878 F.2d 1172 (9th Cir. 1989), *cert. denied*, 110 S. Ct. 867 (1990) (no implied cause of action); Walker v. Federal Land Bank of St. Louis, 726 F. Supp. 211 (C.D. Ill. 1989) (no implied cause of action); Renick Bros., Inc. v. Federal Land Bank Ass'n of Dodge City, 721 F. Supp. 1198 (D. Kan. 1989) (no implied cause of action); Stoppel v. Farm Credit Bank of Wichita, No. 89-1221-C (D. Kan.

The early reception by the federal district courts to those assertions was mixed. In *Martinson v. Federal Land Bank of St. Paul*,[231] *Harper v. Federal Land Bank of Spokane*,[232] and *Leckband v. Naylor*,[233] the Agricultural Credit Act of 1987 was found to have implied a private cause of action. However, in *Zajac v. Federal Land Bank of St. Paul*,[234] *Wilson v. Federal Land Bank of Wichita*,[235] and *Neth v. Federal Land Bank of Jackson*[236] no implied cause of action was found.

When the issue reached the courts of appeals, the reception ceased to be mixed. Of the three courts of appeals to have reached the issue to date, all have found against an implied cause of action. In those cases, *Harper v. Federal Land Bank of Spo-*

Sept. 26, 1989)(1989 U.S. Dist. LEXIS 11642) (no implied cause of action relying on *Renick*); Ochs v. Federal Land Bank of Wichita, NO. 87-4113-R (D. Kan. July 12, 1989) (1989 U.S. Dist. LEXIS 9079) (no implied cause of action); Wilson v. Federal Land Bank of Wichita, No. 88-4058-R (D. Kan. Jan. 30, 1989) (1989 U.S. Dist. LEXIS 1558) (no implied cause of action); In re Reilly, 105 Bankr. 59 (Bankr. D. Mont. 1989) (no implied cause of action); Neth v. Federal Land Bank of Jackson, 717 F. Supp. 1478 (S.D. Ala. 1988) (no implied cause of action); Martinson v. Federal Land Bank of St. Paul, 725 F. Supp. 469 (D.N.D. 1988), *appeal dismissed*, No. 88-5202 (8th Cir. May 5, 1989) (finding an implied cause of action); Leckband v. Naylor, 715 F. Supp. 1451 (D. Minn. 1988), *appeal dismissed*, No. 88-5301 (8th Cir. May 5, 1989) (finding an implied cause of action); *In re* Jarrett Ranches, Inc., 107 Bankr. 963 (Bankr. D.S.D. 1989) (finding an implied cause of action). *See also* Payne v. Federal Land Bank of Columbia, 711 F. Supp. 851 (W.D. N.C. 1989) (implicitly finding an implied cause of action); *In re* Hilton Land & Cattle Co., 101 Bankr. 604 (D. Neb. 1989) (implicitly finding an implied cause of action); Meredith v. Federal Land Bank of St. Louis, 690 F. Supp. 786 (E.D. Ark. 1988) (implicitly finding an implied cause of action). *Aff'd*, 873 F.2d 1447 (8th Cir. 1989).

For a brief period, the Eighth Circuit recognized an implied cause of action. Zajac v. Federal Land Bank of St. Paul, 887 F.2d 844 (8th Cir. 1989), *vacated on grant of reh'g en banc*, Dec. 7, 1989 (1989 U.S. App. LEXIS 18809) (finding an implied cause of action). Before that decision was vacated, it was followed by at least one district court in the Eighth Circuit. Hill v. Farm Credit Bank of St. Louis, 726 F. Supp. 1201 (E.D. Mo. 1989).

At least two courts have recently considered whether there is an implied cause of action to remedy violations of regulations promulgated under the Farm Credit Act, as amended. Winkel v. Production Credit Ass'n of East Central Wisconsin, 451 N.W.2d 440 (Wis. Ct. App. 1989) (finding no implied cause of action and apparently considering the 1987 Act); Williams v. Federal Land Bank of Jackson, 729 F. Supp. 1389 (D.D.C. 1990) (same).

231. 725 F. Supp. 469 (D.N.D. 1988), *appeal dismissed*, No. 88-5202 (8th Cir. May 5, 1989).

232. 878 F.2d 1172 (9th Cir. 1989), *cert. denied*, 110 S. Ct. 867 (1990).

233. 715 F. Supp. 1451 (D. Minn. 1988), *appeal dismissed*, No. 88-5301 MN (8th Cir. May 5, 1989). *Accord In re* Jarrett Ranches, Inc., 107 Bankr. 963, 965 (Bankr. D.S.D. 1989) (relying on Leckband and Martinson, and noting that "the Eighth Circuit has yet to provide guidance on . . . [the] issue"). Subsequently, the Eighth Circuit held against an implied cause of action. Zajac v. Federal Land Bank of St. Paul, No. 88-5353ND (8th Cir. July 31, 1990) (1990 U.S. App. LEXIS 12932).

234. No. A3-88-115 (D.N.D. July 19, 1988) (1989 U.S. Dist. LEXIS 16698), *aff'd*, No. 88-5353ND (8th Cir. July 31, 1990) (1990 U.S. App. LEXIS 12932).

235. No. 88-4058-R (D. Kan. Jan. 30, 1989) (1989 U.S. Dist. LEXIS 1558). *Accord* Renick Bros., Inc. v. Federal Land Bank Ass'n of Dodge City, 721 F. Supp. 1198 (D. Kan. 1989); Stoppel v. Farm Credit Bank of Wichita, No. 89-1221-C (D. Kan. Sept. 26, 1989) (1989 U.S. Dist. LEXIS 11642); Ochs v. Federal Land Bank of Wichita, No. 87-4113-R (D. Kan. July 12, 1989) (1989 U.S. Dist. LEXIS 9079).

236. 717 F. Supp. 1478 (S.D. Ala. 1988).

kane,[237] *Griffin v. Federal Land Bank of Wichita*,[238] and *Zajac v. Federal Land Bank of St. Paul*,[239] the Ninth, Tenth, and Eighth Circuits each rejected the claim that the 1987 Act created an implied private cause of action.

The differences between the courts can best be illustrated by a comparison of the majority and dissenting opinions in *Zajac*. Each opinion addressed each element of the *Cort* test, and each made reference to the prior decision of the Ninth Circuit in *Harper*.

As noted earlier,[240] the first inquiry under *Cort* is whether the plaintiff is "one of the class for whose *especial* benefit the statute was enacted."[241] In *Zajac*, the plaintiffs were seeking to secure through injunctive relief an independent appraisal of the collateral securing their FLB loan at the credit review committee stage of the loan restructuring process, a right granted by the 1987 Act[242] which they alleged had been improperly denied them.[243] The Zajacs argued that the provisions of the 1987 Act at issue were enacted for their benefit as System borrowers.[244]

The majority in *Zajac* declined to decide whether the Zajacs were within the class for whose benefit the Act was enacted on the grounds that the "Zajacs cannot make the other showings required by *Cort*."[245] However, the majority noted that, in the earlier *Harper* decision, the Ninth Circuit had found that the primary purpose of the 1987 Act was to respond to the financial crisis facing the System. Specifically, although the Ninth Circuit conceded that one of the purposes of the loan restructuring provisions of the 1987 Act was to benefit borrowers seeking loan restructuring, the court chose to "look at the overall purpose of the 1987 Act . . . and

237. 878 F.2d 1172 (9th Cir. 1989), *cert. denied*, 110 S. Ct. 867 (1990).

238. 902 F.2d 22 (10th Cir. 1990).

239. Zajac v. Federal Land Bank of St. Paul, No. 88-5353 ND (8th Cir. July 31, 1990)(enbanc)(1990 U.S. App. LEXIS 12932).

240. See *infra* notes 198-199 and the accompanying text.

241. Cort v. Ash, 422 U.S. 66, 78 (1978).

242. 12 U.S.C.A. § 2220(d) (West 1989). The right to an independent appraisal where a loan restructuring application denial is under review by a credit review committee is specifically afforded to borrowers by the Technical Corrections Act of 1988, Pub. L. No. 100-399, sec. 103, 102 Stat. 989, 990 (1988)(codified at 12 U.S.C.A. § 2202(d)(1), (2), (3) (West 1989). *See infra* notes 407-09 and the accompanying text.

243. *Zajac*, slip op. at 7 (Heaney, J., dissenting). At the time that the Zajacs brought their action for injunctive relief before the federal district court, a foreclosure action brought by the FLB was pending against them. In a concurring opinion joined by Judge McMillian, Judge Arnold concluded that the Zajac's request for injunctive relief was barred by the Anti-Injunction Act, 28 U.S.C. § 2283. *Id.* at 4-5.

244. *Id.*, slip op. at 2.

245. *Id.* The loan restructuring provisions are found in Title I of the 1987 Act entitled "Assistance to Farm Credit System Borrowers." Agricultural Credit Act of 1987, Pub. L. No. 100-233, 101 Stat. 1568, 1572 (1988).

conclude that the major impetus for the legislature was the financial crisis of the Farm Credit System."[246] In doing so, the Ninth Circuit in *Harper* implicitly rejected the claim that the loan restructuring provisions of the 1987 Act were enacted for the special benefit of borrowers.[247]

The dissent in *Zajac* addressed the first test of *Cort* and concluded that it had been satisfied. It found that borrowers were a "protected class under the Act because its language and structure established broad rights for borrowers and mandatory duties for lenders."[248]

With respect to the second and most significant aspect of the *Cort* test, legislative intent, the majority in *Zajac* focused on the rejection of an amendment to the House bill[249] that formed the basis of the 1987 Act that would have expressly granted borrowers a right of action to enforce the Act. Although the dissent in *Zajac* relied heavily on other aspects of the legislative history of the legislation, it also referenced the rejection of the amendment. However, the two opinions put a different gloss on that rejection.

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246. *Harper*, 878 F.2d at 1176 (citing Midlantic Nat'l Bank v. New Jersey Dept. of Envt'l Protection, 474 U.S. 494, 501 (1986).

247. The distinction that the Ninth Circuit implicitly made between the financial interests of the Farm Credit System and those of its borrowers reflects a misunderstanding of the loan restructuring provisions of the 1987 Act. As is discussed later in this article, the 1987 Act requires a System lender to restructure a loan only when the restructured loan would result in a greater financial return to the institution than would be achieved through a foreclosure. In other words, loan restructuring under the Act is intended to force System institutions to act in their best financial interests by requiring them to consider alternatives to foreclosure. Accordingly, the distinction implicitly made by the Ninth Circuit is artificial and at odds with the goals of the Act. *See infra* notes 365-411 and the accompanying text. *See also Zajac*, slip op. at 21 (Heaney, J., dissenting) ("Granting borrowers a private right for injunctive relief requires lenders to weigh the costs of restructuring against the costs of foreclosure before resorting to the latter. Injunctive relief strenghtens, rather than weakens, the Farm Credit System by requiring lenders to make a decision based on a thorough review of all factors and procedures deemed important by Congress"); H. Rep. 100-295 (I), 100th Cong., 1st Sess. 62, *reprinted in* 1987 U.S. CODE CONG. & ADMIN. NEWS 2723, 2733 ("Complaints about the rights of System borrowers being abused at both the association and district levels have been like a constant drumbeat in the offices of some Members of Congress for several years. The package of borrower rights adopted in H.R. 3030 reflect a common sense approach which should have been standard operating procedures in a cooperative, borrower-owned lending system."). *But see* Walker v. Federal Land Bank of St. Louis, 726 F. Supp. 211, 217 (C.D. Ill. 1989). In reflecting on why Congress may have decided not to include an express cause of action in the 1987 Act, the court surmised that, "Congress may well have decided that a private right of action under the 1987 Act would generate too many meritless lawsuits filed simply to postpone the inevitable, and that these lawsuits, in addition to those with merit, would pose too heavy a financial burden upon the already strapped Farm Credit System." *Id.*

248. *Zajac*, slip op. at 33 n. 15 (Heaney, J., dissenting) ("The detail and precision with which Congress set forth borrowers' rights under . . . [the restructuring section of the 1987 Act] are powerful indicators [of] Congress' intent to confer specific enforceable rights on borrowers." *Id.* at 13).

249. H.R. 3030, 100th Cong., 1st Sess. (1987).

The dissent in *Zajac*, relying on colloquies[250] on the House

250. In introducing legislation that would have expressly created a cause of action, Representative Watkins of Oklahoma stated:

> My amendment would allow the borrower the right to sue. I really believe in my heart that the right to sue is implied within the bill itself, but I think it is our responsibility and our obligation to make sure that there is no question that the borrower has that right. If a person has a loan and has worked with the Farm Credit System and has suffered some legal wrong or been aggrieved or adversely affected by certain violations of the Farm Credit System, they should have a right to be able to sue.
>
> Every one of us in this Chamber today has heard of dictatorial actions, and we have heard of rigid abuses from individuals against the farmer and against the landowner, and they really have had no recourse to try to remedy their problems. I think my amendment assures them that they have that right if they can prove the wrong.

131 CONG. REC. H7692 (daily ed. Sept. 21, 1987).

Further discussion of the amendment brought about the following exchanges with Representatives Glickman and De La Garza:

> Mr. GLICKMAN: Mr. Chairman, I thank you gentleman for yielding to me.
>
> What factually right now is the state of the law as it relates to a borrower's right to sue? He is allowed to sue under State law, but not Federal law?
>
> It would be useful to know what right a borrower would have to enforce a decision by the Farm Credit System right now in court.
>
> Mr. WATKINS: I think, if the gentleman from Kansas might recall, some States do allow it, and some States do not.
>
> What we are saying is, so there will not be any mistake under this particular Federal legislation, that it be established that they do have the right to be able to sue if they feel like they have been legally wronged or adversely affected by some actions from the Farm Credit System.
>
> Mr. DE LA GARZA: Mr. Chairman, I thank the gentleman for yielding to me.
>
> I have no problem with the gentleman's intention in allowing borrowers to sue, although I think basically they have that right now.

131 CONG. REC. H7693 (daily ed. Sept. 21, 1987).

The Senate also debated the right of individuals to sue System institutions. Senator Burdick of North Dakota offered an amendment which gave any person, not just borrowers, the right to sue:

> This amendment is made necessary only because the House, in their Farm Credit bill, included a right to sue provision that actually restricts the right to sue.
>
> Currently, any person has the right to sue these two entities. However, the House provision arguably limits this right to borrowers of the System. This restricts rights of persons who are not yet borrowers, or who are former borrowers, to sue.
>
> My amendment simply clears up these problems and restores the rights to all persons, whether borrowers or not.
>
> My amendment also gives persons the right to sue in Federal Court. This does not create additional litigation, as some will argue, but only gives the option of suing in Federal court.

131 CONG. REC. S16995 (daily ed. Dec. 2, 1987).

Following Senator Burdick's statement, the following exchange occurred:

> Mr. BOREN: Mr. President, I have listened with interest as my good friend and colleague from North Dakota has explained the purpose of his amendment. I have certainly a high degree of sympathy with the principles that he has set forth.
>
> It has been our hope since we have carefully crafted this legislation in the committee that we not reopen this matter at this time. However, I am told that the house has unduly restricted the right of the borrower to bring suit and that this is the proposal that is in the House bill. It would be my thought, and I have also discussed this with Senator LEAHY, and Senator LUGAR will speak for himself, that we would oppose that House provision in the conference committee.

floor addressing proposals for an express cause of action that reflected, among other things, the misapprehension that a cause of action already existed, concluded that Congress contemplated that the borrowers' rights provisions of the Act would be enforceable without an express provision to that effect.[251] On the other hand, the majority in *Zajac* declined to give any weight to the remarks of individual members of Congress.[252] Instead, the majority based its conclusions on legislative intent solely on the conference committee report. That report noted that the committee had deleted the private right of action provision.[253]

In drawing its conclusions concerning legislative intent from the conference committee report, the majority in *Zajac* expressly adopted the analysis followed by the Ninth Circuit in *Harper*. Accordingly, the majority in *Zajac* reasoned that the conference committee report " 'represents the final statement of the terms agreed to by both houses' "[254] and that " '[n]ext to the statute itself it [the report] is the most persuasive evidence on congressional intent'."[255]

The *Harper* court had noted that an implied cause of action to enforce Farm Credit legislation had been consistently denied by courts as of the time of the debate on the 1987 Act. It then invoked the "normal rule of statutory construction . . . that if Congress intends for legislation to change the interpretation of a judi-

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That would have much the same effect as the adoption of the Burdick amendment would have without our attempting to write the actual language of the amendment here on the floor at this time.

I wonder if the Senator might consider withholding the actual offering of this amendment with the understanding that the Senate conferees would oppose the House amendment in the conference.

Mr. BURDICK: The proposal of the Senator is very acceptable.

Mr. BORDEN: I thank my colleague, and I believe the Senator from Indiana also has the same view.

Mr. LUGAR: Mr. President, I would confirm the understanding that the distinguished Senator from this amendment. We will in fact oppose the House amendment in conference. We understand the problem, and we would appreciate the Senator's not pursuing this amendment on this occasion with that assurance.

131 CONG. REC. S16995 (daily ed. Dec. 2, 1987).

The Senate was concerned that the House amendment would limit the existing right of individuals to sue System institutions and opposed the House amendment in Conference Committee. The House amendment was thus deleted. H.R. REP. NO. 100-490, 100th Cong., 1st Sess. 178, *reprinted in* 1988 U.S. CODE CONG. & ADMIN. NEWS 2723, 2973. *See also Zajac*, slip op. at 21-24 (Heaney, J., dissenting) (discussing the foregoing and other remarks made on the floor).

251. *Zajac*, slip op. at 22 n. 5 (Heaney, J., dissenting).

252. *Id.*, slip op. at 2-3.

253. *Id.*

254. *Id.* (citing *Harper*, 878 F.2d at 1176).

255. *Id.*

cially created concept, it makes that intent specific."[256] Applying that rule, the Ninth Circuit found that the deletion from the final version of the 1987 Act of a provision for an express cause of action reflected a Congressional intention that a cause of action also should not be implied.[257] The *Zajac* majority concurred.[258]

The *Zajac* majority and dissent were also at odds in their application of the third aspect of the *Cort* test; whether an implied cause of action would be consistent with the legislation's purpose.[259] The majority agreed with the Ninth Circuit's conclusion in *Harper* that the enforcement powers granted to the Farm Credit Administration revealed a legislative intention to exclude any other remedy.[260] The Ninth Circuit reached this conclusion even after acknowledging that those remedies might be inappropriate or ineffective because

> . . . there is no procedure for filing charges or for compelling FCA to commence an investigation. . . . [The] FCA's enforcement apparatus is inadequate to enforce the borrower's rights. . . . [The] FCA's authority to issue temporary cease and desist orders is limited to violations likely to cause insolvency and that FCA's issuance of permanent cease and desist orders is extremely time consuming. . . . [And] [t]here is no provision in the statute guaranteeing any remedy for the individual borrower."[261]

However, the dissent in *Zajac* vigorously took issue with the assertion that an implied cause of action would not be consistent with the scheme of the 1987 Act. The dissent seized on the inade-

256. *Harper*, 878 F.2d at 1176 (citing Midlantic Nat'l Bank v. New Jersey Dept. of Envt'l Protection, 474 U.S. 494, 501 (1986)).

257. *Id.*

258. *Zajac*, slip op. at 3-4. The dissent in *Zajac* argued that the *Harper* court's approach, specifically, its heavy reliance on the conference committee report, "relegates the language and structure of the statute to insignificant status under its *Cort v. Ash* analysis." *Id.* at 14 (citation omitted). The dissent maintained that "[a]s long as the implied cause of action doctrine exists, the dominant focus must be the language and structure of the Act in question." *Id.* at 15 (citing Thompson v. Thompson, 484 U.S. 174, 520 (1988)).

259. *Cort*, 422 U.S. at 66.

260. *Zajac*, slip op. at 3 (citing *Harper*, 878 F.2d at 1176).

261. *Harper*, 878 F.2d at 1176. *But see* Leckband v. Naylor, 715 F. Supp. 1451, 1455 (D. Minn. 1988) (finding an implied cause of action for reasons including that "[t]he cease and desist powers granted FCA by 12 U.S.C. § 2262 are inappropriate, both in scope and timimg, to effectively protect . . . [the right of first refusal granted to borrowers under the 1987 Act]"), *appeal dismissed* No. 88-5301 MN (8th Cir. May 5, 1989); *In re* Jarrett Ranches, Inc., 107 Bankr. 963, 967-68 (Bankr. D.S.D. 1989) (discussing the inadequacy of the FCA's powers as a means of protecting the right of first refusal granted to borrowers under the 1987 Act and finding an implied cause of action based, in part, on those inadequacies). *See also* Massey & Schneider, *supra* note 6, at 613-14 (discussing the inadequacy of the FCA as a protector of the borrowers rights provisions of the 1987 Act).

quacies of the FCA's powers noted in *Harper* as evidencing "[t]he plain fact . . . that the FCA is in no position to effectively enforce the borrowers rights provisions of the 1987 Act."[262] Moreover, it noted that the record before it did not support the view that the FCA has "either the ability or the willingness to enforce the borrowers' rights provisions."[263]

Finally, in addressing the fourth element of the *Cort* test,[264] the *Zajac* majority held that protecting rights created by federal law such as the right at issue would be "inappropriate" "because foreclosure is an area 'traditionally controlled by state law'."[265] That holding is consistent with *Harper*. There, the Ninth Circuit held that because the loan restructuring provisions of the 1987 Act were tied to the commencement of state law-governed foreclosure proceedings, the cause of action sought to be implied was one traditionally relegated to state law.[266]

On the other hand, the dissent in *Zajac* concluded that the protection of the federally created rights was appropriate, particularly when the right being protected, such as the right to an independent appraisal, was procedural. For that reason, the dissent would have limited the cause of action to injunctive relief tailored to secure lender compliance with the procedures prescribed by one or more of the specific borrowers' rights provisions. The dissent expressly disavowed any desire to imply a cause of action in favor of borrowers to secure judicial review of the merits of lender decisions, such as the decision to foreclose rather than to restructure.[267]

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262. *Zajac*, slip op. at 29 (Heaney, J., dissenting).

263. *Id.* at 30 (Heaney, J., dissenting). *But see* Walker v. Federal Land Bank of St. Louis, 726 F. Supp. 211, 216 (C.D. Ill. 1989) (in finding no implied private right of action, the court stated, "[b]ut clearly the *Zajac* court missed the point. . . . That the Farm Credit Administration has been lax in complying with Congressional intent is of no moment. . . ."). One of the borrowers' rights provisions relating to loan restructuring provides that "[t]he Farm Credit Administration may issue a directive requiring compliance with any provision of this section [Restructuring distressed loans] to any qualified lender that fails to comply with such provision." 12 U.S.C.A. § 2202a(i) (West Supp. 1989). Although that broad grant of authority would appear not to encompass the enforcement of borrowers' rights in areas other than loan restructuring, it does afford the basis for a more zealous oversight of the protection of borrowers in the process of seeking loan restructuring than the FCA has chosen to exercise. *See generally* Massey & Schneider, *supra* note 6, at 613-14 (discussing the "passivity" of the FCA in enforcing the borrowers' rights provisions of the 1987 Act).

264. *Cort*, 422 U.S. at 78.

265. *Zajac*, slip op. at 4 (citing *Harper*, 878 F.2d at 24).

266. *Harper*, 878 F.2d at 1177.

267. *Zajac*, slip op. at 33 n. 15 (Heaney, J., dissenting). Specifically, the dissent stated that it "would not be appropriate for a federal court to intrude into credit decisions of a System lender if the lender complies with the statutorily mandated procedures." *Id.*, slip op. at 33. Such an approach, had it been adopted by the majority, would have been consistent with earlier analogous decisions of the Eighth Circuit concerning the scope of review of the denial of Farmers Home Administration (FmHA) loan applications. Tuepker

The three courts of appeals that have ruled against an implied cause of action encompass within their respective circuits large areas of the major agricultural regions of this country. Accordingly, their respective decisions have a significant impact on large numbers of System borrowers. Moreover, their decisions will most certainly influence other circuits that may confront the issue. It appears that if borrowers are to be given the right to enforce the borrowers' rights provisions of the Farm Credit Act, as amended, the grant will have to be expressly made by Congress.

15. *RICO*

The federal RICO statute[268] appears to offer a basis for federal jurisdiction over PCAs and FLBs. However, there are no reported successful RICO actions against a PCA or FLB.[269] At least one federal district court, in an action brought *pro se*, has held, without elaboration, that because Farm Credit System institutions are federal instrumentalities, they are immune from liability under RICO.[270]

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v. Farmers Home Admin., 708 F.2d 1329, 1332 (8th Cir. 1983) (declining to review the denial of an FmHA loan in the absence of a claim "alleging a substantial departure from important procedural rights, a misconstruction of governing legislation, or some like error, going to the heart of the administrative determination"); Woodsmall v. Lyng, 816 F.2d 1241, 1245 (8th Cir. 1987) (declining to review the denial of an FmHA loan because the applicant was not creditworthy on the grounds that the federal courts "are not equipped to undertake such a task, for in these matters we have neither the training nor the experience of an FmHA loan officer").

268. 18 U.S.C.A. §§ 1961-68 (West 1984 & Supp. 1990). The federal RICO statute (racketeer influenced and corrupt organizations) claims are usually brought under § 1962(c) which provides that:

> It shall be unlawful for any person employed by or associated with any enterprise engaged in, or the activities of which affect, interstate or foreign commerce, to conduct or participate, directly or indirectly, in the conduct of such enterprise's affairs through a pattern of racketeering activity or collection of unlawful debt.

18 U.S.C.A. § 1962(c) (West 1984 & Supp. 1990).

269. *See* Federal Land Bank of Omaha v. Gibbs, 809 F.2d 493, 496 (8th Cir. 1987) (stating that plaintiff's RICO claim fails to state a claim upon which relief can be given); Brekke v. Volcker, 652 F. Supp. 651, 655 (D. Mont. 1987) (holding plaintiff's RICO claim inadequate); Creech v. Federal Land Bank of Wichita, 647 F. Supp. 1097, 1100-11 (D. Colo. 1986) (stating that plaintiff's RICO claim failed to state underlying facts with enough specificity); Schroder v. Volcker, 646 F. Supp. 132, 135 (D. Colo. 1986) (holding that plaintiff failed to state a claim), *aff'd*, 864 F.2d 97 (10th Cir. 1988); Jacobson v. Western Montana Production Credit Ass'n, 643 F. Supp. 391, 395-96 (D. Mont. 1986) (stating that RICO action failed due to lapsed statute of limitations); Criswell v. Production Credit Ass'n, 660 F. Supp. 14, 16 (S.D. Ohio 1985) (stating that RICO claim failed to distinguish between enterprise and culpable person).

270. Wiley v. Federal Land Bank of Louisville, 657 F. Supp. 964, 967 (S.D. Ind. 1987) (also holding that the National Bank Act, 12 U.S.C. §§ 85, 86, does not apply to System institutions).

16. *Other Theories*

The following are other theories or claims which have been unsuccessfully asserted against System institutions:

a. Purchase of Stock
A Mississippi court has held that FLBA and PCA required purchases of stock are valid requirement in order to obtain financing, and those purchases do not create an " 'unlawful debt' " for " 'seeming nonexistent capital stock'."[271]

b. Renouncing Citizenship
The appellate court of Colorado rejected a farmer's attempt to stop foreclosure by renouncing his United States citizenship.[272]

c. Land Patent
At least two courts have held that arguing that possession of an original land patent precludes foreclosure constituted a frivolous claim under Rule 11 of the Federal Rules of Civil Procedure warranting sanctions.[273]

B. STATE COURT JURISDICTION

The amenability of Farm Credit System institutions to suits in state court on common law causes of action is beyond dispute.[274]

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271. Gregory v. Federal Land Bank of Jackson, 515 So. 2d 1200, 1204 (Miss. 1987).

272. Federal Land Bank of Wichita v. Deatherage, 739 P.2d 905, 906 (Colo. Ct. App. 1987) (holding that no basis in law exists to support plaintiff's claim).

273. Federal Land Bank of Spokane v. Redwine, 755 P.2d 822, 825 (Wash. Ct. App. 1988) (stating that use of the land patent was an obvious attempt to improve title by personal fiat); Britt v. Federal Land Bank Ass'n of St. Louis, 505 N.E.2d 387 (Ill. Ct. App. 1987) (holding that filing of alleged "land patent" by former mortgagors after judgment of foreclosure did not vest mortgagors with superior title), *appeal denied*, 515 N.E.2d 102 (Ill. 1987).

274. *E.g.*, Bowling v. Block, 602 F. Supp. 667, 670 (S.D. Ohio 1985), *aff'd*, 785 F.2d 556 (6th Cir.), *cert. denied*, 479 U.S. 829 (1986); Boyster v. Roden, 628 F.2d 1121, 1125 (8th Cir. 1980); Johansen v. Production Credit Ass'n of Marshall-Ivanhoe, 378 N.W.2d 59, 62 (Minn. Ct. App. 1985). In recent years, many of the state court actions against System lenders premised on common law causes of action have been lender liability claims. The literature on lender liability is becoming voluminous. For a sampling, see Flick & Replansky, *Liability of Banks to the Borrowers: Pitfalls and Protections*, 1986 BANKING L.J. 220; Bahls, *Termination of Credit for the Farm or Ranch: Theories of Lender Liability*, 48 MONT. L. REV. 213 (1987); Kelley, *Some Observation on Lender Liability and Representing the Farmer/Borrower*, AGRIC. L. UPDATE, Dec. 1986, at 4; Kelley, *supra* note 4; Special Project, *Lender Liability: A Survey of Common Law Theories*, 42 VAND. L. REV. 855 (1989); Lawrence & Wilson, *Good Faith in Calling Demand Notes and in Refusing to Extend Additional Financing*, 63 IND. L.J. 825 (1988); Ebke & Griffin, *Good Faith and Fair Dealing in Commercial Lending Transactions: From Covenant to Duty and Beyond*, 49 OHIO ST. L.J. 1397 (1989); Kunkel, *The Fox Takes Over the Chicken House: Creditor Interference with Farm Management*, 60 N.D.L. REV. 435 (1984); Tyler, *Emerging Theories of Lender Liability in Texas*, 24 HOUSTON L. REV. 411 (1987); Note, *The Fiduciary Controversy:*

However, courts have been vigilant in frustrating attempts to convert violations of the Farm Credit Act or the regulations promulgated under into state law causes of action. For example, it has been held that the Farm Credit Act and the regulations promulgated under it neither create enforceable duties upon which to base a negligence claim[275] nor does their violation support a claim based on the tort of bad faith.[276] Similarly, alleged violations of the Act have been held not to support a claim based on the breach of the contractual duties of good faith and fair dealing.[277] In essence, the rejection of such claims has been based on the absence of an expressed or implied cause of action under the Farm Credit Act and the reasoning that " 'the law does not permit by indirection what cannot be accomplished directly'."[278]

V. MISCELLANEOUS MATTERS

A. PUNITIVE DAMAGES

The prevailing view is that punitive damages are not awarda-

Injection of Fiduciary Principles into the Bank-Depositor and Bank Borrower Relationships, 20 LOY. L.A.L. REV. 795 (1987); Hagedorn, *The Impact of Fiduciary Principles on the Bank-Customer Relationship in Washington*, 16 WILLAMETTE L. REV. 803 (1980); Ellis & Gray, *Lender Liability for Negligently Processing Loan Applications*, 92 DICK. L. REV. 363 (1988); Fischel, *The Economics of Lender Liability*, 99 YALE L.J. 131 (1989); Nickles, *The Objectification of Debtor-Creditor Relations*, 74 MINN. L. REV. 371 (1989); Weissman, *Lender Liability: The Obligation to Act in Good Faith and Deal Fairly*, 8 COM. DAMAGES REP. 239 (1986); Douglas-Hamilton, *Creditor Liabilities Resulting from Improper Interference with the Management of a Financially Troubled Debtor*, 31 BUS. LAW. 343 (1975); Comment, *Lenders' Liability — The Shift from Contract to Tort Doctrine Deters Banks from Enforcing Unjustified and Detrimental Contract Provisions*, 21 J. MARSHALL L. REV. 369 (1988); Note, *Trust and Confidence and the Fiduciary Duty of Banks in Iowa*, 35 DRAKE L. REV. 611 (1985-86); Annotation, *Existence of Fiduciary Relationship Between Bank and Depositor or Customer So As To Impose Special Duty of Disclosure upon Bank*, 70 A.L.R. 3D 1344 (1976); Annotation, *Measure and Elements of Damages for Breach of Contract to Lend Money*, 4 A.L.R. 4TH 682 (1981); Annotation, *Recoverability of Compensatory Damages for Mental Anguish of Emotional Distress for Breach of Contract to Lend Money*, 52 A.L.R. 4TH 371 (1987); Annotation, *Bank's Liability for Breach of Implied Contract of Good Faith and Fair Dealing*, 55 A.L.R. 4TH 1026 (1987).

Lender liability litigation on behalf of borrowers against System institutions can be frustrating. For examples, see Zwemer v. Production Credit Ass'n of the Midlands, 792 P.2d 245 (Wyo. 1990); Nelson v. Production Credit Ass'n of the Midlands, 729 F. Supp. 677 (D. Neb. 1989); *In re* Louden, 106 Bankr. 109 (Bankr. E.D. Ky. 1989) (adversary proceeding against FLB); Lawrence v. Farm Credit System Capital Corp., 761 P.2d 640 (Wyo. 1988). *But see, e.g.*, Federal Land Bank Ass'n of Tyler v. Sloane, No. 12-88-00231-CV (Texas Ct. App. May 31, 1990) (1990 Tex. App. LEXIS 1345) (partially successful lender liability action against FLBA).

275. Yankton Production Credit Ass'n v. Jensen, 416 N.W.2d 860, 864 (S.D. 1987). *See also infra* note 299 and the accompanying text (discussing the related, but distinct, issue of negligence claims based on lender violations of their internal loan policies).

276. Production Credit Ass'n of Fargo v. Ista, 451 N.W.2d 118, 121-25 (N.D. 1990).

277. Mendel v. Production Credit Ass'n of the Midlands, 656 F. Supp. 1212, 1217 (D.S.D. 1987), *aff'd*, 862 F.2d 180, 183-84 (8th Cir. 1988).

278. Production Credit Ass'n of Fargo v. Ista, 451 N.W.2d 118, 124-25 (N.D. 1990) (citation omitted). For a discussion of the implied cause of action issue under the Farm Credit Act, as amended, see *infra* notes 184-267 and the accompanying text.

ble against a Farm Credit System institution. Generally, a federal instrumentality enjoys immunity from suit unless it waives that immunity. Congress has waived immunity from suit for Farm Credit System institutions by giving them the authority "to sue and be sued."[279]

Nevertheless, a federal instrumentality "retains its immunity from punitive damages unless Congress *explicitly* authorizes liability for such damages."[280] Several courts have held that the "sue and be sued" clause for PCAs does not waive immunity from punitive damages.[281] However, a federal district court recently denied a motion to dismiss a claim for punitive damages against an FLB on the grounds that the FLB's tort liability was the same as a private lender.[282]

By analogizing the Farm Credit System to the law governing federal and other public officers and employees, Farm Credit System directors, officers, or employees may not enjoy immunity from punitive damage awards for unlawful acts or conduct outside the scope of their authority when they are sued in their individual capacities.[283] Attorneys representing borrowers should be aware that the bylaws of many FLBA's and PCA's forbid indemnification of directors, officers, and employees for liabilities arising out of the person's gross negligence or willful misconduct in the performance of official duties.[284] Therefore, a suit against an individual based on gross negligence or willful misconduct is not, in effect, a suit against the institution. However, at least two courts have held that Farm Credit System employees are not subject to punitive damages for acts undertaken in their employment.[285]

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279. 12 U.S.C.A. § 2013(4) (FCBs), 2073(4) (PCAs), 2093(4) (FLBAs) (West 1989). *See In re* Sparkman, 703 F.2d 1097, 1101 (9th Cir. 1983) (citing Federal Housing Admin. v. Burr, 309 U.S. 242 (1940)).

280. *In re* Sparkman, 703 F.2d at 1101 (emphasis in original).

281. *Id. See also* Smith v. Russellville Production Credit Ass'n, 777 F.2d 1544, 1549-50 (11th Cir. 1985). *In re* Sparkman, 703 F.2d at 1101; Rohweder v. Aberdeen Production Credit Ass'n, 765 F.2d 109, 113 (8th Cir. 1985). *Accord* Smith v. Russellville Production Credit Ass'n, 777 F.2d at 1549-50. *See generally PCAs and Other Chameleons*, 3 AGRIC. L. UPDATE 1 (March 1986) (discussing the scope of the "sue and be sued" provision).

282. Jackson v. Farm Credit Admin. of America, No. CV-F-88-636 REC, slip op. at 30-31 (E.D. Cal. May 9, 1989) (citing Sterrett v. Milk River Production Credit Ass'n, 647 F. Supp. 299, 303 (D. Mont. 1986)).

283. *E.g.*, Davis v. Passman, 442 U.S. 228 (1979) (stating that congressmen may be sued for sexual discrimination); Hobson v. Wilson, 737 F.2d 1 (D.C. Cir. 1984), *cert. denied*, 470 U.S. 1084 (1985) (FBI agent held subject to punitive damages under 42 U.S.C.A. § 1985(3)).

284. The bylaws of System institutions are available to member-borrowers on request. 12 U.S.C.A. § 2200 (West 1989).

285. Reilly v. Production Credit Ass'n of the Midlands, No. 11243 (Osceloe Co., Iowa, Dist. Ct. Sept. 4, 1986) (holding that punitive damages were not awardable against a PCA employee sued in his capacity as an employee); Wilson v. Federal Land Bank of Wichita, No. 88-4058R (D. Kansas Jan. 30, 1989) (1989 U.S. Dist. LEXIS 1558) (FLB agents and

B. DISCOVERY

Rather than operating as a shield from discovery, the Farm Credit System regulations have been held "to disclose an intent to provide information in a court proceeding. . . ."[286] In that case, Agrivest Partnership v. Central Iowa Production Credit Association,[287] a PCA declined to produce certain board minutes as requested by the plaintiff.[288] The PCA asserted a privilege based on 12 C.F.R. §§ 618.8300 and 618.8320 (1985) which imposed both specific and general confidentiality requirements.[289]

In resolving the issue under an evidentiary rule similar to Rule 501 of the Federal Rules of Evidence, the Iowa Supreme Court noted that "privileges should not be called into play merely because an agency, acting on only general authority, issues regulations declaring certain information privileged."[290] From that point, the court reviewed other Farm Credit System regulations relating to the dissemination of information.[291] It found that 12 C.F.R. § 618.8330 (1985), which authorized employee testimony of production of documents "to the extent as under the conditions directed by the court," as counseling "greater liberality" than that shown by the PCA in the action before it.[292] Moreover, the court held that the regulations invoked by the PCA were not intended to apply to discovery requests, and that the PCA had no statutory or regulatory privilege.[293] The court also declined to find a common law governmental privilege.[294]

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attorneys not liable for punitive damages for actions taken in the course of the agency relationship).

286. AgriVest Partnership v. Central Iowa Production Credit Ass'n, 373 N.W.2d 479, 485 (Iowa 1985).

287. *Id.*

288. *Id.* at 481.

289. *Id.*

290. *Id.* at 483 (citations omitted). *See also* Matter of Nelson, 131 F.R.D. 161, 163 (D. Neb. 1989) (FCA regulations "cannot supplant the authority of the judicial branch to control discovery proceedings" (citations omitted)). However, courts have held that "[i]n order to secure information within the scope of regulations such as 12 C.F.R. § 602.289 [relating to responses to demands for FCA documents served on non-FCA employees and entities], a litigant must comply with agency regulations regarding discovery requests." Interstate Production Credit Ass'n v. Fireman's Fund Ins. Co., 128 F.R.D. 273, 276 (D. Ore. 1989) (citation omitted).

291. *AgriVest*, 272 N.W.2d at 483.

292. *Id.* at 485.

293. *Id. See also* Matter of Nelson, 131 F.R.D. 161, 162-65 (D. Neb. 1989) (discussing the deliberative process privilege as applied to the minutes of FICB board of director and other FICB meetings and finding that the privilege did apply).

294. *AgriVest*, 373 N.W.2d at 485-86. In Minnesota, borrowers were successful in obtaining orders directing a PCA to turn over Farm Credit Administration examination reports by relying on *AgriVest*. *See* Rieks v. Production Credit Ass'n of River Falls, No. 95566 (Dakota Co., Minn., Dist. Ct. December 11, 1986, & August 14, 1987) (orders compelling production of documents). *But see* Interstate Production Credit Ass'n v. Firemans Fund Ins. Co., 128 F.R.D. 273, 276 (D. Ore. 1989) ("The federal courts have

C. NO AGENCY RELATIONSHIP BETWEEN FLBS AND FLBAS

Generally, there is no agency relationship implied by law between a FLB and a FLBA within the FLB's district, for the two are distinct and separate entities. Although FLBAs accept applications to the district FLB for loans, the United States Supreme Court has held that an association could not be deemed the agent of the FLB in disbursing the proceeds of a loan.[295] Nevertheless, the Farm Credit Banks (FLBs and FICBs prior to the Agricultural Credit Act of 1987) have the authority to supervise the associations within their respective districts and to "delegate to Federal land bank associations such functions as the bank determines appropriate."[296] Thus, an agency in fact may exist.

D. INCORPORATION OF FARM CREDIT SYSTEM REGULATIONS IN CONTRACT DOCUMENTS

Members of some PCAs will have signed a "Membership Agreement" in connection with their loan application. Paragraph 10 of one such agreement provides as follows:

> 10. One Agreement/Interpretation: The Agreement includes and incorporates all amendments and supplements hereto, and all notes, security instruments, documents, and other writings submitted by Debtor to PCA in connection with this Agreement. Neither debtor nor the PCA shall be bound by the agreement or undertaking, nor shall this Agreement be amended or supplemented except as expressed in writing and signed by the party against whom

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consistently ruled that a court may not order an institution such as IPCA [a PCA] to produce information in violation of regulations such as 12 C.F.R. § 602.289 [relating to demands for FCA documents served on non-FCA employees or entities]" (citations omitted)).

295. Federal Land Bank of Columbia v. Gaines, 290 U.S. 247, 254 (1933). *See also* Federal Deposit Ins. Corp. v. Langley, 792 F.2d 541, 548-49 (5th Cir. 1986) (FLB not bound by the misrepresentations and omissions of the president of an FLBA), *aff'd*, 484 U.S. 86 (1987); Federal Land Bank of New Orleans v. Jones, 456 So. 2d 1, 5-10 (Ala. 1984) (detailed discussion of the relationship between an FLB and FLBA, concluding that "[i]n the present case, the controlling statutes clearly provide for the creation of two autonomous entities, and the courts interpreting those statutes have recognized that statutorily there is no agency relationship between the Bank and the Association" (citing Gantt v. Gunter, 225 Ala. 679, 145 So. 146 (1932)); Hinds v. Federal Land Bank of New Orleans, 235 Ala. 360, 179 So. 194 (1938)); Sterrett v. Milk River Production Credit Ass'n, 764 P.2d 467, 68-70 (Mont. 1988) (holding that FICB's supervisory duties over PCA did not establish agency relationship to impose on the FICB liability for alleged misrepresentations of PCA employee).

296. 12 U.S.C.A. § 2013(13), (18) (West 1989).

> enforcement is sought. The invalidity or unenforceability of any term or provision of this Agreement shall not affect the validity or enforceability of the remaining terms and provisions hereof.
>
> This Agreement and the transactions between the Debtor and PCA shall be governed by the Farm Credit Act of 1971 as amended, the Regulations adopted thereunder, the PCA bylaws and, where not inconsistent, applicable state law.[297]

This agreement provision appears to contemplate that all existing and future provisions of the Farm Credit Act of 1971 and the regulations promulgated under it are incorporated into the terms of the contractual relationship between borrower-members and the PCA. If so, then any failure by the PCA to abide by the Act or the regulations would be a breach of contract. This appeared to be one way for the borrower to avoid the obstacles inherent in attempting to assert claims based on violations of the Act or regulations under an implied cause of action theory. However, such an attempt was rebuffed in *Production Credit Association of Worthington v. Van Iperen*.[298]

E. NEGLIGENT FAILURE TO FOLLOW LOAN POLICIES

An assertion that is notable for its persistent appearance despite repeated rebuffs by the courts is the claim that the loan policies of System lenders create enforceable standards of care in favor of borrowers. The Eighth Circuit, the Minnesota Court of Appeals, and the Wisconsin Court of Appeals have rejected the argument that a PCA's internal policies set a standard of conduct that creates a cause of action based on common-law negligence if the policies are not followed.[299]

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297. PRODUCTION CREDIT ASSOCIATION OF NORTHEAST ARKANSAS MEMBERSHIP AGREEMENT (1986).

298. 396 N.W.2d 35, 38 (Minn. Ct. App. 1986). On the subject of the incorporation of regulations into contract documents, see Smithson v. United States, 847 F.2d 791 (Fed. Cir. 1988) (declining to broadly incorporate the Farmers Home Administration (FmHA) regulations into agreements between FmHA borrowers and the FmHA), *cert. denied*, 488 U.S. 1004 (1989).

299. Overvaag v. Production Credit Ass'n of the Midlands, No. 87-5332 (8th Cir. Mar. 7, 1988) (*See* 845 F.2d 1028 (D.S.D. 1988) (Table of Decisions Without Published Opinions)); Ebenhoh v. Production Credit Ass'n of Southeast Minnesota, 426 N.W.2d 490, 493 (Minn. Ct. App. 1988); Bevier v. Production Credit Ass'n of Southeast Minnesota, 429 N.W.2d 287, 289 (Minn. Ct. App. 1988); Winkel v. Production Credit Ass'n of East Central Wisconsin, 451 N.W.2d 440, 442-43 (Wis. Ct. App. 1989). *See also supra* notes 275-78 and the accompanying text (discussing related, but distinct claims); Williams v. Federal Land Bank of Jackson, 729 F. Supp. 1387, 1390 (D.D.C. 1990) (construing the provisions of the FLB's Credit and Operations Manual as not supporting borrower's claim). The argument

VI. THE FARM CREDIT SYSTEM'S FIDUCIARY DUTY TO ITS MEMBER-BORROWERS

In several reported actions, Farm Credit System borrowers have advanced claims premised on the assertion that the FLBA or the PCA of which they were a member owed them a fiduciary duty. The alleged sources of that duty have varied. For example, in *Boyster v. Roden*,[300] the plaintiff-borrowers sought to sustain federal question jurisdiction on the assertion that the White River PCA in Newport, Arkansas, owed them a fiduciary duty as a matter of federal common law.[301] The borrowers in *Boyster* alleged that the fiduciary duty was breached when the PCA disclosed confidential information about the borrowers to a third-party.[302] In support of their claim, the borrowers argued that the various Farm Credit Administration regulations specifying the standards of conduct for System officers and employees coupled with the "pervasive involvement of the federal government" in the creation and operation of PCAs established that the federal interest was of such a nature as "to require that the fiduciary responsibilities of production credit association officers and directors be governed by a body of federal common law rather than state law."[303]

In rejecting the borrowers' claim, the Eighth Circuit held as follows:

> We are not persuaded that the substantial federal interest in successful operation of the Farm Credit System will be impaired by application of state law to appellants' claims. Even if the fiduciary law varies somewhat from state to state, no burden to the System is perceived; each production credit association is a separate entity with a local situs, and its business transactions are with farmers and ranchers in its locale.[304]

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advanced by the borrowers in each of these cases overlooked the fundamental premise that tort duties are created by the law, not a lender's internal policies. For a properly developed negligence claim, see Jacques v. First National Bank of Maryland, 307 Md. 527, 515 A.2d 756 (Md. Ct. App. 1986). *But see* Nelson v. Production Credit Ass'n of the Midlands, 729 F. Supp. 677, 686-88 (D. Neb. 1989) (applying Nebraska law and noting that even if the Nebraska Supreme Court were to adopt the *Jacques* reasoning, it would not apply in the case before it).

300. 628 F.2d 1121 (8th Cir. 1980).

301. *Id.* at 1122.

302. *Id.* at 1123.

303. *Id.* at 1123-24.

304. *Id.* at 1125. *See also* Federal Land Bank of Jackson in Receivership v. Federal Intermediate Credit Bank, 727 F. Supp. 1055, 1059-60 (S.D. Miss. 1989) (relying on *Boyster* and Birbeck v. Southern New England Production Credit Ass'n, 606 F. Supp. 1030, 1041 (D. Conn. 1985), for the proposition that "[f]ederal law has not preempted the regulation and supervision of the Farm Credit System."); *In re* Louden, 106 Bankr. 109, 113 (Bankr.

However, the court indicated that the regulations imposing certain standards of conduct on System employees, could "probably be used by appellants as evidence in a trial of their claim under state law."[305]

Boyster was followed in *Hartman v. Farmers Production Credit Association of Scottsburg*.[306] In *Hartman*, the borrowers had asserted various claims against the PCA including a claim based on an assertion of an implied right of action under the Farm Credit Act of 1971.[307] In rejecting the borrower's argument that the purpose of the Farm Credit Act would be frustrated if a private cause of action was not implied, the court concluded that the borrower's state law remedies, including a claim for breach of fiduciary duty, would adequately protect the borrower's rights.[308]

In *Umbaugh Pole Building Co., Inc. v. Scott*,[309] the borrowers sought to establish that a PCA owed them a fiduciary duty, apparently as a result of the course of dealing between the borrowers and the PCA arising from a series of loans during a two year period.[310] Although the trial court found that a fiduciary relationship existed, the Supreme Court of Ohio reversed that finding.[311]

In reaching its decision, the court in *Umbaugh* noted that, ordinarily, the relationship between a debtor and creditor is not a fiduciary relationship.[312] Nevertheless, the court pointed out that a fiduciary relationship may be created out of an informal relationship, but "only when both parties understand that a special trust or confidence has been reposed."[313] When the court examined the

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W.D. Ky. 1989)(stating that any fiduciary relationship between a FLB and a borrower is governed by state law (citing Creech v. Federal Land Bank of Wichita, 647 F. Supp. 1097, 1101 (D. Colo. 1986)).

305. *Id.* at 1125 n.5. *See also* Creech v. Federal Land Bank of Wichita, 647 F. Supp. 1097, 1101 (D. Colo. 1986) (noting that "The regulations governing operation of Farm Credit Associations impose high standards of honesty, integrity and professionalism on officers, employers and agents of the Farm Credit System" (citations omitted)).

306. 628 F. Supp. 218 (S.D. Ind. 1983).

307. *Id.* at 219.

308. *Id.* at 222. *Accord* Creech v. Federal Land Bank of Wichita, 647 F. Supp. 1097, 1101 (D. Colo. 1986); Spring Water Dairy, Inc. v. Federal Intermediate Bank of St. Paul, 625 F. Supp. 713, 720 (D. Minn. 1986); Apple v. Miami Production Credit Ass'n, 614 F. Supp. 119, 122 (S.D. Ohio 1985), *aff'd*, 804 F.2d 917 (6th Cir. 1986); Birbeck v. Southern New England Production Credit Ass'n, 606 F. Supp. 1030, 1034-44 (D. Conn. 1985); Bowling v. Block, 602 F. Supp. 667, 672, n.3 (S.D. Ohio 1985), *aff'd*, 785 F.2d 556 (6th Cir.), *cert. denied*, 479 U.S. 829 (1986).

309. 58 Ohio St. 2d 282, 390 N.E.2d 320 (1979).

310. Umbaugh Pole Building Co., Inc. v. Scott, 390 N.E.2d 320, 322 (1986).

311. *Id.* at 320.

312. *Id.* at 323.

313. *Id.* For a discussion of the generally applicable elements of an "informal" fiduciary relationship between a borrower and a lender, see *infra* note 336.

dealings between the borrowers and the PCA, it concluded as follows:

> There was no property or interest of the Scotts entrusted to the association. The only basis for the findings of the fiduciary relationship was the association's giving of advice and counseling to the Scotts relevant to their loans and business activities. But here the offering and giving of advice was insufficient to create a fiduciary relationship. While the advice was given in a congenial atmosphere and in a sincere effort to help the Scotts prosper, nevertheless, the advice was given by an institutional lender in a commercial context in which the parties dealt at arms length, each protecting his own interest.
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> * * * * *
>
> There was no promise for a continuing line of credit, and while a limited amount of advice and counseling was given, this did not vitiate the business relationship because neither party had, nor could have had, a reasonable expectation that the creditor would act solely or primarily on behalf of the debtor. Also, the rendering of advice by the creditor to the debtors does not transform the business relationship into a fiduciary relationship. The borrowers could not reasonably believe that the association was acting in a fiduciary capacity.[314]

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314. *Umbaugh*, 390 N.E.2d at 323 (citations omitted). In *Stone v. Davis*, 66 Ohio St.2d 74, 419 N.E.2d 1094, *cert. denied*, 454 U.S. 1081 (1981), the Ohio Supreme Court made a distinction between loan negotiations and "loan processing" in characterizing the relationship between the lender and borrowers. *Stone*, 419 N.E.2d at 1098. At issue was a mortgage lender's failure to advise and assist the borrowers in procuring mortgage insurance. *Id.* at 1095. In essence, the court found that the relationship between the parties changed after the loan agreement was completed and the loan transaction entered the processing or servicing stage. In the court's words:

> [t]he facts surrounding and the setting in which a bank gives advice to a loan customer on the subject of mortgage insurance warrant a conclusion that, in this aspect of the mortgage loan process, the bank acts as its customer's fiduciary and is under a duty to fairly disclose to the customer the mechanics of procuring such insurance.
>
> We observe that, while a bank and its customer may be said to, stand at arm's length in negotiating the terms and conditions of a mortgage loan, it is unrealistic to believe that this equality of position carries over into the area of loan processing, which customarily includes advising the customer as to the benefits of procuring mortgage insurance on the property which secures the bank's loan.

Id. at 1098.

See also Walters v. First National Bank of Newark, 69 Ohio St.2d 577, 433 N.E.2d 608, 610 (1982) ("The fiduciary nature . . . of the bank-customer relationship is predicated upon the bank's superior conversance with the area of loan processing. . . ."). The reasoning of the Ohio Supreme Court in *Stone v. Davis* is beneficial to borrowers in that most breaches

In *Jacobson v. Western Montana Production Credit Association*,[315] a PCA was held to a fiduciary standard in its dealings with a borrower.[316] However, in *Jacobson*, unlike the allegations based solely on a lender-borrower relationship as in *Umbaugh*,[317] the borrower alleged that the fiduciary relationship existed as a result of the PCA's involvement with a commodities broker in advising the borrower to participate in a futures trading venture.[318] Under those circumstances, the court in *Jacobson* found that the "obligation of the PCA was that of a fiduciary and the law would imply a duty to use reasonable care in giving of advice."[319]

In *Production Credit Association of Lancaster v. Croft*,[320] the borrowers attempted to establish that the PCA owed them a fiduciary duty, and that the PCA was negligent in making loans to the borrowers which the PCA knew the borrowers could not repay.[321] The trial court granted the PCA summary judgment and the borrowers appealed.[322] On appeal, the Crofts argued that the PCA owed them a fiduciary duty that was implied in law because the loan agreements gave the PCA control of the repayment requirements, and that there was a great disparity in knowledge and experience between the PCA and the Crofts.[323] The court held that the loan agreement did not create a fiduciary relationship because the provisions in the agreement that appeared to give the PCA control were necessary to protect PCA's interest in the collateral.[324] The court also held that the advice was offered by the PCA to the Crofts did not create a fiduciary relationship because the advice was not outside of what a lender would normally offer in protecting its interest.[325]

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of the lender's duties of honesty, disclosure, good faith, and fair dealing occur in the loan servicing stage.

315. 643 F. Supp. 391 (D. Mont. 1986).

316. Jacobson v. Western Montana Production Credit Ass'n, 643 F. Supp. 391, 392 (1979).

317. 390 N.E.2d. 320 (1979).

318. *Jacobson*, 643 F. Supp. at 395.

319. *Id.* at 395.

320. 423 N.W.2d 544 (Wis. Ct. App. 1988), *rev. denied*, 428 N.W.2d 554 (Wisc. 1988).

321. Production Credit Ass'n of Lancaster v. Croft, 423 N.W.2d 544, 548 (Wis. 1988).

322. *Id.*

323. *Id.* at 545-46.

324. *Id.* at 546-47.

325. *Id.* at 546-49. In reaching its decision, the court relied heavily on Bahls, *Termination of Credit for the Farm or Ranch: Theories of Lender Liability*, 48 MONT. L. REV. 213, 232 (1987) ("So long as the farmer makes his or her own business decisions and the advice given by the lender is nothing more than optional advice or is reasonably related to protection of the lender's interest in its collateral, lenders should not be treated as having a fiduciary responsibility to the borrower"). *See also* Production Credit Ass'n of West Central Wisconsin v. Vodak, 441 N.W.2d 338, 344, 346 (Wis. Ct. App. 1989) (stating that *Croft* did not hold that "a lending institution may not, under any circumstances, be liable to a customer for negligence in advising the customer on financial decisions" and also stating

A review of the foregoing cases reveals at least the following three points pertaining to a PCA's, FLBA's, or Farm Credit Bank's fiduciary obligations, if any:

1. there is no federal common law fiduciary duty of PCAs, FLBAs, or Farm Credit Banks, and any fiduciary obligation will arise solely under state law;
2. when a PCA, FLBA, or Farm Credit Bank is characterized simply as a lender in a lender-borrower relationship, "extraordinary circumstances" must be present before a fiduciary relationship will arise; and
3. if a PCA, FLBA, or Farm Credit Bank acts as a financial advisor or a broker, or in some other capacity where the law will ordinarily impose a fiduciary relationship, the institution will be treated no differently than any other entity so acting.[326]

Both Congress and the Farm Credit Administration have acknowledged that a fiduciary duty may be imposed upon Farm Credit System officers and directors to their respective institutions and shareholders under state law. For example, section 2264(a) of the Farm Credit Act provides that an institution's officers and directors may be removed from office by the Farm Credit Administration for a "breach of fiduciary duty as such director or officer."[327] Similarly, the Farm Credit Administration Board, in justifying certain regulations requiring financial disclosures by System officers and directors, has asserted that "such disclosure is needed to provide shareholders with sufficient information to hold directors and officers accountable for the performance of their fiduciary duties. . . ."[328]

It is unlikely that any Farm Credit System institution would contend that its officers and directors do not owe a fiduciary duty

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that "*Croft* simply held that a fiduciary relationship did not arise under the facts of that case," not that there could never be a fiduciary relationship between a PCA and one of its borrowers), *rev. denied*, 443 N.W.2d 311 (Wisc. 1989); Nelson v. Production Credit Ass'n of the Midlands, 729 F. Supp. 677, 685 (D. Neb. 1989) (declining, with little explanation, to find a fiduciary relationship between a borrower and a PCA, but indicating that it was not persuaded to find a fiduciary relationship by the assertion that the PCA had a "special concern" towards its member-borrowers).

326. Farm Credit Banks, FLBAs, and PCAs are authorized to provide technical assistance and financial related services to borrowers. 12 U.S.C.A. §§ 2020, 2093(15), 2076 (West 1989)). *See also* Federal Land Bank of St. Paul v. Asbridge, 414 N.W.2d 596, 600-01 (N.D. 1987) (holding that the borrowers had not established a fiduciary relationship between them and the FLB on which to premise the claim that the FLB had a "fiduciary responsibility . . . to provide it member borrowers with all necessary information so that borrowers may make timely payments").

327. 12 U.S.C.A. § 2264(a) (West 1989).

328. 51 Fed. Reg. 42,084-085 (1986) (prefatory comment).

to the institution. Of course, because the System is a cooperative entirely owned by its member-borrowers, the borrowers are the "institution." Moreover, because PCAs and FLBAs are cooperatives, they are subject to a body of law that applies only to cooperative associations or cooperative corporations.[329]

Cooperatives owe unique duties to their members. As expressed in a widely recognized treatise on agricultural cooperatives, "the relationship between the members and the [cooperative] association is much more intimate and personal than between other corporations and their stockholders."[330]

This "more intimate and personal" relationship between a cooperative's members and the cooperative institution arises from the basic aim of a cooperative "to create 'a union of men, not a union of capital, as does the ordinary commercial corporation'."[331] Thus,

> ". . .it is particularly important to remember that the [cooperative] association is an organization of individuals rather than a mere abstract and impersonal entity. The personal character of the ownership in a cooperative is one of the main distinctions between the cooperative and the ordinary corporation."[332]

The unique relationship between a cooperative and its members has led some courts to impose, as a matter of law, fiduciary obligations on officers of marketing cooperatives in their dealings

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329. *See, e.g.*, Knox National Farm Loan Ass'n v. Phillips, 300 U.S. 194, 198 (1937) ("A national farm loan association [predecessor to FLBAs] is a cooperative enterprise."). It is extremely important not to confuse corporate law principles with cooperative law principles. Although many cooperatives are incorporated, their actions and conduct are subject to a body of law that is in many respects unique to cooperatives. Thus, a claim such as was made in Production Credit Ass'n of Fargo v. Ista, 451 N.W.2d 118, 120-21 (N.D. 1990), that, as a matter of corporate law, there is a fiduciary relationship between a PCA and its borrowers, is misplaced. In that case, the court correctly held that corporate law does not create fiduciary duties running from a PCA to its members. *Id.* at 121. However, the court was never presented with the question, nor did it address, whether cooperative law imposed fiduciary duties on the cooperatively organized PCA in favor of its individual members. For a discussion of the cooperative law duties of a cooperative toward its members, see *infra* notes 334-38 and the accompanying text.

330. FARMER COOPERATIVE SERVICE, USDA, LEGAL PHASES OF FARMERS COOPERATIVES 10-11 (1976) [hereinafter LEGAL PHASES].

331. E. NOURSE, THE LEGAL STATUS OF AGRICULTURAL CO-OPERATION 268 (1927).

332. I. PACKEL, THE LAW OF THE ORGANIZATION AND OPERATION OF COOPERATIVES 17 (4th ed. 1970). *See generally* Note, *Legal Aspects of Cooperative Organizational Structure*, 27 IND. L.J. 377, 378 (1952) (noting that a member of a cooperative occupies two roles: "He is both a proprietor and one of the vendors with whom the cooperative transacts business"); Staatz, *Recent Developments in the Theory of Agricultural Cooperation*, 2 J. AGRIC. COOPERATION 74, 79-80, 88-89 (1987) (discussing the theoretical aspects of the cooperative as a "coalition").

with cooperative members.[333]

To some extent, the imposition, as a matter of law, of fiduciary duties on marketing cooperatives may be motivated by the fact of the entrustment of the member's crop with the cooperative for marketing purposes. If that is the case, then a different basis will need to be found for imposing a fiduciary duty on non-marketing cooperatives such as financial or lending cooperatives as are the institutions of the Farm Credit System.

An argument can be made that there is, as a matter of law, a fiduciary obligation on the part of a cooperative towards its members. In large part, that obligation flows from the following seven criteria or hallmarks of a cooperative:

1. [t]he basic purpose of cooperatives is to render economic benefits to members;
2. [c]ooperatives are organized around the mutual interest of members;
3. [r]isks, costs, and benefits are shared 'equitable' among members;
4. [c]ooperatives are non-profit enterprises in the sense that they are organized for the economic benefit of members as users of the cooperatives' services and not to make profits for the cooperatives as legal entities for their members as investors;
5. [c]ooperatives are democratically controlled;
6. [m]embers of cooperatives have an obligation to patronize their cooperatives; and
7. [c]ooperatives do business primarily with members.[334]

For example, because cooperatives are nonprofit organizations in the sense that they operate at cost, it has been held that "the cooperative stands in the relationship of a trustee to the members."[335] Thus, the nature of cooperatives, coupled with

333. *E.g.*, Rhodes v. Little Falls Dairy Co., Inc., 230 App. Div. 571, 245 N.Y.S. 432, 434-35 (1930), *aff'd*, 256 N.Y. 559, 177 N.E. 140 (1931). *See also* Snyder v. Colwell Cooperative Grain Exchange, 231 Iowa 1210, 3 N.W.2d 507 (1942) (ruling that a cooperative has a duty to each member to fully disclose all material facts regarding the cooperative and that member's dealings with the cooperative). In a marketing cooperative, the members frequently deliver their products to the cooperative for marketing. A fiduciary relationship usually arises when one entrusts property with another with the understanding that the latter will use the money for the benefit of the former on in a manner consistent with the former's desires. *See* RESTATEMENT (SECOND) OF TRUSTS 2 (1959).

334. LEGAL PHASES, *supra* note 329, at 4.

335. White, *The Farmer and His Cooperative*, 7 KANSAS L. REV. 334, 335 (1959) (citing San Joaquin Valley Poultry Producers v. Comm'r, 136 F.2d 382 (9th Cir. 1943)). The "service at cost" principle dictates that there be no exploitation by the cooperative of its

increasing judicial recognition that lending institutions should be held to a higher standard than the law of the marketplace,[336]

members. Ultimately, the members of a cooperative bear the risk for the success or failure of the cooperative. Accordingly, the cooperative must do what it can for its members, not what it must. Bakken, *Principals and their Role in the Statutes Relating to Cooperatives*, 1954 WIS. L. REV. 550, 559 (offering an informative discussion of basic cooperative principles and noting that "in cooperative business there shall be no elements of exploitation"). A pervasive theme in the academic writings on the law of fiduciaries is the role of fiduciary law as a shield against the potential abuse of power by the dominant party or parties in a relationship. *See* Frankel, *Fiduciary Law* 71 CALIF. L. REV. 795 (1983); Shepard, *Towards a Unified Concept of Fiduciary Relationships*, 97 L.Q. REV. 51 (1981).

336. *See, e.g.*, Barrett v. Bank of America, 183 Cal. App. 3d 1362, 1328, 229 Cal. Rptr. 16, 20 (1986) (holding that relationship between a bank and its borrower to be "at least quasi-fiduciary"); Lash v. Cheshire County Savings Bank, 474 A.2d 980, 982 (N.H. 1984) (upholding a jury finding of a commercial bank's breach of fiduciary duty). *See also* Djowharzadeh v. City Nat'l Bank & Trust Co., 646 P.2d 616, 619 (Okla. Ct. App. 1982) ("The precarious position of the borrower and the relatively superior position of the bank mandates there be a counterbalancing special duty imposed on the part of the bank."); Stewart v. Phoenix Nat'l Bank, 64 P.2d 101, 106 (Ariz. 1937) (noting that the changing role of banks from mere safeguarders of deposits to advice-givers justifies the imposition of higher standards of care on a bank that assumes the role of an advice-giver). *But see* Price v. Wells Fargo bank, 213 Cal. App. 3d 465, 261 Cal. Reptr. 735 (Cal. App. 1st Dist. 1989) (containing a highly critical discussion of injecting fiduciary concepts into the lender-borrower relationship), *rev. denied* (Cal. Dec. 7, 1989). *See generally* Harrell, *The Bank-Customer Relationship: Evolution of a Modern Form*, XI OKLA. CITY U.L. REV. 641 (1986) (discussing the changing nature of bank-borrower relationships and the standards of care applicable to those relationships); Oglivie, *Banks, Advice-Giving And Fiduciary Obligation*, 17 OTTAWA L. REV. 263 (1985) (same); Hagedorn, *Fiduciary Aspects of the Bank-Customer Relationship*, 34 MO. B.J. 406 (1978) (same).

In most jurisdictions, borrowers seeking to establish that an informally created fiduciary relationship exists between a lender and a borrower must satisfy at least two, and often three, requirements. First, it must be shown that the borrower had reposed trust and confidence in the lender. Second, as a result of that reposal of trust, the lender must have attained a position of influence and superiority over the borrower. *E.g.*, First Bank of Wakeeny v. Modern, 681 P.2d 11, 13 (Kan. 1984) (*per curiam*). In many jurisdictions a third requirement is implicitly or explicitly imposed. That requirement is that the trust and confidence reposed by the borrower "must actually be accepted by the second party [the bank]." Dewitt County Public Bldg. Comm. v. County of Dewitt, 469 N.E.2d 689, 770 (Ill. Ct. App. 4th Dist. 1984). *Accord* Umbaugh Pole Bldg Co. v. Scott, 58 Ohio St.2d 282, 390 N.E.2d 320, 323 (1979) ("A fiduciary relationship may be created out of an informal relationship, but this is done only when both parties understand that a special trust or confidence has been reposed") (citations omitted).

An argument has been advanced that the relationship between an agricultural lender and a farmer-borrower is sufficiently unique to warrant imposing a higher duty of care on the lender. When the lending relationship involves farm operating loans, this relationship is typically characterized by six attributes that distinguish it from many other lender-borrower relationships:

> First, the relationship is often a longstanding one. Once a farmer has a lender for operating capital, that relationship tends to continue.
>
> Second, the relationship is an exclusive one. The farmer depends exclusively on one lender for his operating money. That exclusivity benefits the lender by avoiding split repayment and split collateral problems.
>
> Third, the lender is intimately familiar with the operational and financial affairs of the farmer's enterprise. This familiarity is derived from the annual planning for loan disbursements and from the financial advice also given by the lender.
>
> Fourth, the lender, through its advice to the farmer and its realization that it has a financial interest in the farmer's success, may assume some control over the farmer's operation. This control is frequently manifested in the joint planning by the farmer and the lender for loan amounts and disbursements.
>
> Fifth, even if the lender does not exercise actual control, the lender has extraordinary latent control over the farmer. The source of this latent control is

strongly suggest that the cooperative institutions of the Farm Credit System might be held to a high standard of care in their dealings with their members in a properly presented case.

Of current concern to many System borrowers is the standard of care that a cooperative owes to its members when the cooperative seeks to expel a member from the cooperative. When a member is in default on a loan from a PCA, Farm Credit Bank, or FLBA, the member's stock in the PCA or FLBA is subject to liquidation.[337] Liquidation of the stock effectively expels the member from the cooperative.

Courts have consistently held that a cooperative seeking to expel a member must act fairly and in good faith. In essence, courts have resolved cooperative expulsion issues on the basic principle that "[a] private organization, especially if it has some public stature or purpose, may not expel or discipline a member and adversely affect substantial property, contract, or other economic rights unless such action results from proceedings conducted in an atmosphere of good faith and fair play."[338] These judicially imposed standards of good faith and fair play for cooper-

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> usually twofold. First, the lender has substantial latent control by virtue of its security interest in most, if not all, of the farmer's machinery, equipment, land, annual production, and other personal property. Second, latent control may often exist because the loan is evidenced by a demand note. Because a demand note is due at any time that the lender desires it to be due, the lender can force a farmer to refinance or liquidate at will.
>
> Sixth, as a result of their longstanding and relatively close working relationship with their lenders, most farmers develop expectations regarding their lenders. Specifically, where the relationship between a farmer and lender has been a good for one for several years, farmers reasonably expect that their lender will continue to deal with them honestly, fairly, and in good faith.

Kelley, *supra* note 4, at 19-20.

However, although this argument may afford a basis for showing that in the typical farm lender — farmer borrower relationship the borrower had reposed his confidence in the lender, and, as a result, the lender assumed a position of superiority and influence over the borrower, satisfying those elements of the three-part test for an informally created fiduciary relationship are usually not the borrower's biggest obstacle. Rather, the biggest obstacle has been showing that the lender tacitly or otherwise agreed to be held to the higher standard. Indeed, in one case where a borrower had attempted to show through the bank's advertisements that the bank had solicited the trust and confidence of the public, the bank disavowed any such intention. *In re* Werth, 37 Bankr. 979, 989 (Bankr. D. Colo. 1984) (the court characterized the bank's disavowal as "somewhat bizzare and extraordinary," but it also found that there was no fiduciary relationship established), *aff'd*, 54 Bankr. 619 (D.C. Co. 1985). *See also* Atlantic National Bank of Florida v. Vest, 480 So.2d 1328, 1333 (Fla. Ct. App. 2d Dist. 1985) (noting that where a breach of fiduciary duty between a bank and its customer has been found, it is generally possible to identify a benefit flowing to the bank as a result of the breach), *rev. denied*, 491 So.2d 281 (Fla. 1986), 508 So.2d 16 (Fla. 1987).

337. 12 U.S.C.A. §§ 2094(k), 2097 (West 1989).

338. Copeland, *Expulsion of Members by Agricultural Cooperatives*, J. AGRIC. COOPERATION 76, 82 (1986). *See also Developments in the Law — Judicial Control of Actions of Private Associations*, 76 HARV. L. REV. 983, 1006-36 (1963) (discussing the substantive and procedural limitations on actions by private associations against their members).

atives expelling member-borrowers from Farm Credit System institutions may afford the basis for enforcing or challenging the institution's consideration of the borrower for loan restructuring under section 2202(a) of the Farm Credit Act.[339]

VII. FARM CREDIT SYSTEM BORROWER RIGHTS

As a result of the Farm Credit Amendments Act of 1985 and the Agricultural Credit Act of 1987, borrowers from System institutions have statutory rights in the following areas:

1. protection of stock;
2. disclosure of interest rates and related information;
3. access to certain documents and information;
4. written notice on loan applications and review of loan application denials;
5. protection from foreclosure when loan obligations are current;
6. written notice of loan restructuring policies and review of loan restructuring denials;
7. prohibition against waiver of mediation rights;
8. rights of first refusal on land acquired by an institution from a borrower as a result of foreclosure or certain voluntary conveyances;
9. review of System lender decisions establishing the interest rate applied to a loan;
10. application of funds in uninsured accounts to borrower's outstanding loans;
11. use of FmHA guaranteed loans or other state or federal loan programs in restructuring.[340]

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339. 12 U.S.C.A. § 2202(a) (West 1989). *See also* Federal Land Bank of St. Paul v. Overboe, 404 N.W.2d 445, 448-50 (N.D. 1987) (applying equitable principles to protect FLB borrowers in judicial foreclosure proceedings); Benson Cooperative Creamery Ass'n v. First District Ass'n, 151 N.W.2d 422, 427 (Minn. 1967) (holding that a cooperative member who is wrongfully expelled from a cooperative may recover for any damages resulting from that wrongful expulsion). For a more detailed discussion of this issue, see Hoekstra, *The Cooperative Fiduciary Duty Owed by the Farm Credit System Cooperatives to their Member/Borrowers* (1989) (first place winner in the 1989 American Agricultural Law Association Writing Competition) (available from the National Center for Agricultural Law Research and Information, Leflar Law Center, University of Arkansas, Fayetteville, AR 72701) (scheduled for publication in the *J. of Agric. L. and Tax'n*, Spring 1991).

340. Proposed regulations implementing the rights created by the Agricultural Credit Act of 1987 were published on May 12, 1988, at 53 Fed. Reg. 16,934-947 (1988). The final regulations appear at 53 Fed. Reg. 35,427-458 (1988). The final regulations are codified at 12 C.F.R. Pt. 614, subpts. L & N (1990). Descriptive summaries of the borrowers' rights provisions of the Agricultural Credit Act of 1987 can be found in N. HAMILTON, BORROWERS' RIGHTS AND THE AGRICULTURAL CREDIT ACT OF 1987: A GUIDE FOR FARMERS HOME ADMINISTRATION AND FARM CREDIT SYSTEM BORROWERS AND THE ATTORNEYS (1988) (available from the Agricultural Law Center, Drake University School of

A. PROTECTION OF BORROWER STOCK

"Eligible borrower stock" in a system institution must be retired at par value.[341] "Eligible borrower stock" is defined as stock that:

(a) is outstanding on January 6, 1988;
(b) is required to be purchased, and is purchased, as a condition of obtaining a loan made after January 6, 1988, but prior to the earlier of —
  (i) in the case of each bank and association, the date of approval, by the stockholders of such bank or association, of the capitalization requirements of the institution in accordance with section 4.9B; or
  (ii) the date that is nine months after January 6, 1988;
(c) was, after January 1, 1983, but before January 6, 1988, frozen by an institution that was placed in liquidation; or
(d) was retired at less than par value by an institution that was placed in liquidation after January 1, 1983, but before January 6, 1988.[342]

B. DISCLOSURE OF INTEREST RATES AND RELATED INFORMATION

The stock purchase requirement for System loans increases the equivalent annual rate by one-half to two percentage points depending on the level of the stock requirement, the interest rate, whether "automatic or end-of-period cancellation" is used, and other factors.[343] Prior to the 1985 Act, that increased cost was not always disclosed to borrowers. Enacted in 1985 and amended by the 1987 Act, Section 2199(a) of the Farm Credit Act requires that System lenders provide borrowers with the following information:

Law, Des Moines, Iowa 50311), and Farmers' Legal Action Group, Inc., *Special Report on the Agricultural Credit Act of 1987*, FARMERS' LEGAL ACTION REP. (1988) (available from the Farmers' Legal Action Group, Inc., 1301 Minnesota Building, 46 East Fourth Street, St. Paul, Minnesota 55101). *See also* Massey & Schneider, *supra* note 6, at 589-613 (describing the borrowers' rights regulations and discussing some of the problems encountered by borrowers under the regulations).

341. 12 U.S.C.A. § 2162(a) (West 1989).

342. 12 U.S.C.A. § 2162(d)(2) (West 1989).

343. LaDue, *Influence of the Farm Credit System Stock Requirement on Actual Interest Rates*, 43 AGRIC. FIN. REV. 50, 51-52 (1983). *See also* Jones & Barry, *Impacts of Production Credit Association Capitalization Policies on Borrowers' Costs*, 46 AGRIC. FIN. REV. 15 (1988) (discussing the affect of PCA capitalization on borrower interest rates).

. . . meaningful and timely disclosure not later than the time of the loan closing of:

(1) the current rate of interest on the loan;
(2) in the case of an adjustable or variable rate loan, the amount and frequency by which the interest rate can be increased during the term of the loan or, if there are no such limitations, a statement to that effect, and the factors (including, but not limited to, the cost of funds, operating expenses, and provision for loan losses) that will be taken into account by the lending institution on the effective rate of interest;
(3) the effect, as shown by a representative example or examples, of the required purchase of stock or participation certificates in the institution on the effective rate of interest;
(4) any change in the interest rate applicable to the borrowers loan;
(5) except with respect to stock guaranteed under section 2162 of this title [protection of borrower stock], a statement indicating that stock that is purchased is at risk; and
(6) a statement indicating the various types of loan options available to borrowers, with an explanation of the terms and borrowers' rights that apply to each type of loan.[344]

System lenders that offer more than one rate of interest to borrowers, often referred to as interest rate "tiers," must, at the request of a borrower holding a loan, provide the following information:

(1) provide a review of the loan to determine if the proper interest rate has been established;
(2) explain to the borrower in writing the basis for the interest rate charged; and
(3) explain to the borrower in writing how the credit status of the borrower may be improved to receive a lower interest rate on the loan.[345]

344. 12 U.S.C.A. § 2199(a) (West 1989).
345. 12 U.S.C.A. § 2199(b) (West 1989). *See also* 12 C.F.R. §§ 614.4365-614.4368 & 614.4440-614.4444(1990) (regulations governing disclosure of loan information).

C. ACCESS TO CERTAIN DOCUMENTS AND INFORMATION

The 1985 Act added section 2200 to the Farm Credit Act to provide as follows:

> In accordance with regulations of the Farm Credit Administration, System institutions shall provide their borrowers, at the time of execution of loans, copies of all documents signed or delivered by the borrower and at any time, on request, a copy of the institution's articles of incorporation or charter and bylaws.[346]

That provision and other borrowers' rights provisions and regulations prompted the only farmer on the Farm Credit Administration Board to comment, "I think it's a shame when the FCA has to issue regulations to ensure the rights of stockholders and loan applicants."[347] That statement is most telling when it is noted that an act of Congress was required to give borrowers access to loan documents that they had signed. Therefore, many observers of Farm Credit System behavior were not surprised when Congress chose to act again in 1987 to expand section 2200 to give borrowers the right to receive "copies of each appraisal of the borrower's assets made or used by the qualified lender."[348]

D. WRITTEN NOTICE ON LOAN APPLICATIONS AND REVIEW OF LOAN APPLICATION DENIALS

Section 2201 of the Act provides as follows:

> Each qualified lender to which a person has applied for a loan shall provide the person with prompt written notice of —
> (1) the action on the application;
> (2) if the loan applied for is reduced or denied, the reasons for such action; and
> (3) the applicant's right to review under section 2202 of this title.[349]

If an application for a loan is denied, the applicant may request a review of that denial before the institution's credit

346. 12 U.S.C.A. § 2200 (West Supp. 1986). *See also* 12 C.F.R. § 618.8325 (1990) (disclosure of loan documents).

347. Webster, *Lenders of Interest* (interview with James R. Billington) AGRIFINANCE 12 (Dec. 1966).

348. 12 U.S.C.A. § 2200 (West 1989). *See also* 12 C.F.R. § 618.8325(b) (1990) (requiring the furnishing, on request, of copies of appraisals).

349. 12 U.S.C.A. § 2201(a) (West 1989). *See also* 12 C.F.R. § 614.4441 (1990) (notice of action on loan applications).

review committee.[350] The institution must be the lender with the "ultimate decision making authority on the loan."[351] The request must be made in writing within 30 days "after receiving a notice denying or reducing the amount of the loan application."[352]

The institution's credit review committee is usually composed of three individuals. It must include a farmer board member.[353] The delegation of duties is limited:

> The duties of the members of the review committees may not be delegated to any other person, except that the credit review committee duties of the board member may be performed from time to time by an alternate designated by the board who shall also be a board member.[354]

A loan officer who was involved in the initial decision on a loan may not serve on the credit review committee reviewing that loan.[355] However, that loan officer may "participate" in the review to answer questions but may not "serve" on the committee by being present or voting in the final deliberations.[356] The borrower has a right to appear before the credit review committee and may be accompanied by an attorney or other representative.[357]

Unsuccessful applicants for a loan or loan restructuring who appeal to the credit review committee may include in their request for review a request for an independent appraisal of any interest in property securing the loan other than the stock held by the borrower in the institution.[358] The procedure for obtaining the independent appraisal is as follows:

> Within 30 days after a request for an appraisal under paragraph (1), the credit review committee shall present

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350. 12 U.S.C.A. § 2202 (West 1989).
351. 12 C.F.R. § 614.4442 (1990).
352. 12 U.S.C.A. § 2202(b)(1) (West 1989).
353. 12 U.S.C.A. § 2202(a)(1) (West 1989).
354. 12 C.F.R. § 614.4442 (1990).
355. 12 U.S.C.A. § 2202(a)(2) (West 1989).
356. *See* 53 Fed. Reg. 35,427, 35,436 (1988).
357. 12 U.S.C.A. § 2202(c) (West 1989). *See also* 12 C.F.R. § 614.4443(a) (1990) (personal appearance in the review process).
358. 12 U.S.C.A. § 2202(d)(1) (West 1989); Agricultural Credit Technical Corrections Act of 1988, Pub. L. No. 100-399, 103, 102 Stat. 989, 990. *See also* 12 C.F.R. § 614.4443(c) (1990) (independent appraisals). The right to an independent appraisal in the review of a loan restructuring denial was at issue in Zajac v. Federal Land Bank of St. Paul, No. 88-5353ND (8th Cir. July 31, 1990) (*en banc*) (1990 U.S. App. LEXIS 12932) (holding that there is no implied cause of action under the 1987 Act). For a discussion of the *Zajac* decision, see *supra* notes 242-67 and the accompanying text.

the borrower with a list of three appraisers approved by the appropriate qualified lender from which the borrower shall select an appraiser to conduct the appraisal the cost of which shall be borne by the borrower and shall consider the results of such appraisal in any final determination with respect to the loan.[359]

A copy of the appraisal must be provided to the borrower.[360] "Promptly" after a review by a credit review committee, the committee must notify the applicant in writing of its decision and the reasons for that decision.[361]

E. PROTECTION FROM FORECLOSURE WHEN LOAN OBLIGATIONS ARE CURRENT

The Agricultural Credit Act of 1987 added a new provision that prohibits System institutions from foreclosing on any loan "because of the failure of the borrower thereof to post additional collateral, if the borrower has made all accrued payments of principal, interest, and penalties with respect to the loan."[362]

In addition, as a result of the 1987 Act, sections 2202d(b) and (c) now provide as follows:

> (b) Prohibition against required principal reduction
>
> A qualified lender may not require any borrower to reduce the outstanding principal balance of any loan made to the borrower by any amount that exceeds the regularly scheduled principal installment payment (when due and payable), unless —
>
> (1) the borrower sells or otherwise disposes of part or all of the collateral; or
>
> (2) the parties agree otherwise in a written agreement entered into by the parties.
>
> (c) Nonenforcement
>
> After a borrower has made all accrued payments of principal, interest, and penalties with respect to a loan made by a qualified lender, the lender shall not enforce acceleration of the borrower's repayment

359. 12 U.S.C.A. § 2202(d)(2) (West 1989). *See also* 12 C.F.R. § 614.4443(c) (1990) (independent appraisals in the review process).

360. 12 U.S.C.A. § 2202(d)(3) (West 1989). *See also* 12 C.F.R. § 614.4443(c) (1990) (independent appraisals in the review process).

361. 12 U.S.C.A. § 2202(e) (West 1989). *See also* 12 C.F.R. § 614.4443(d) (1990) (review process decisions).

362. 12 U.S.C.A. § 2202d(a) (West 1989). *See also* 12 C.F.R. § 614.4443(a) (1990) (protection of borrowers who meet all loan obligations).

schedule due to the borrower having not timely made one or more principal or interest payments.[363]

The 1987 Act also affords borrowers certain rights with respect to the placing of a loan in nonaccrual status. Specifically, section 2202d(d) provides as follows:

> (d) Placing loans in nonaccrual status
>
> (1) Notification
>
> If a qualified lender places any loan in nonaccrual status, the lender shall document such change of status and promptly notify the borrower thereof in writing of such action and the reasons therefore.
>
> (2) Review of Denial
>
> If the borrower was not delinquent in any principal or interest payment under the loan at the time of such action and the borrower's request to have the loan placed back into accrual status is denied, the borrower may obtain a review of such denial before the appropriate credit review committee under section 2202 of this title.
>
> (3) Application
>
> This subsection shall only apply if a loan being placed in nonaccrual status results in an adverse action being taken against the borrower.[364]

F. WRITTEN NOTICE OF LOAN RESTRUCTURING POLICIES AND REVIEW OF LOAN RESTRUCTURING DENIALS

The Agricultural Credit Act of 1987 imposed new "mandatory" restructuring requirements on System lenders. The requirements are mandatory in the sense that an institution desiring to foreclose on a distressed loan must, except in limited circumstances,[365] notify the borrower of the right to apply for

363. 2202d(b), (c) (West 1989). *See also* 12 C.F.R. § 614.4514(c) (1990) (nonenforcement of acceleration).

364. 12 U.S.C.A. § 2202d(d) (West 1989). *See also* 12 C.F.R. § 614.4514(d) (1990) (nonaccrual status resulting in adverse action against the borrower; the regulation emphasizes that the placing of the loan in nonaccrual status must have resulted in adverse action being taken against the borrower).

365. When the lender has reasonable grounds to believe that "loan collateral will be destroyed, dissipated, consumed, concealed, or permanently removed from the state in which the collateral is located," the lender may take "appropriate" action to protect the

restructuring not later than 45 days before commencing foreclosure proceedings, and, after consideration of such an application, the institution must restructure the loan if the "cost" of the proposed restructuring plan is equal to or less than the "cost" of foreclosure.[366]

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collateral, including foreclosure. 12 U.S.C.A. § 2202a(j) (West 1989). Assumably, the notice of the right to apply for loan restructuring would be given after the collateral has been protected. See notes 475-79 *infra* and the accompanying text in Appendix A for an additional discussion of this issue.

It is axiomatic that only "borrowers" have the right to seek restructuring. *See* 12 C.F.R. §§ 614.4516, 614.4518 (1990) (implicitly defining a "borrower" as a "primary obligor." A mortgagor of a borrower is not a "borrower" for purposes of loan restructuring. Federal Land Bank of St. Louis v. McGinnis, 711 F. Supp. 952, 957-58 (E.D. Ark. 1989).

366. 12 U.S.C.A. § 2202a (West 1989). *See also* 12 C.F.R. §§ 614.4512 & 614.4514-4522 (1990) (consisting of Part K, subpart N).

A borrower who files a bankruptcy petition is eligible for a loan restructuring under the 1987 Act. *See In re* James Desmond Woods, Jr., No. 88-BK-01659-M11 (W.D. La. March 16, 1989)(interim order in adversary proceeding) (1987 Act remedies and remedies under Bankruptcy Code are not mutually exclusive). Thus, it has been held that an FLB's compliance with the 1987 Act is "a condition precedent to the commencement of a proceeding in bankruptcy that constitutes a foreclosure proceeding as defined by the Act." In the Matter of Dilsaver, 86 Bankr. 1010, 1015 (Bankr. D. Neb. 1988), *aff'd sub nom., In re* Hilton Land & Cattle Co., 101 Bankr. 604, 606 (D. Neb. 1989) (holding that an FLB "must comply with the [1987] Act by providing the appropriate restructuring process requested by the debtors prior to commencing a foreclosure proceeding to sequester rents and profits"); Hill v. Farm Credit Bank of St. Louis, 726 F. Supp. 1201, 1205 (E.D. Mo. 1989) ("[U]pon review of the legislative history of the 1987 Act, the Court is persuaded that Congress did not intend to exclude debtors in bankruptcy from the protections of the Act"); *In re* Kramer, 107 Bankr. 668, 669-70 (Bankr. D. Neb. 1989)(1989 Bankr. LEXIS 2076) (following *Dilsaver* as affirmed *sub nom. In re* Hilton Land and Cattle Co.).

However, by the weight of authority, the 1987 Act does not alter or displace any provision of the Bankruptcy Code. *See In re* Kraus, No. BK 86-2677, slip op. at 2 (Bankr. D. Neb. May 20, 1988) (memorandum order denying, *inter alia*, debtor's motion to dismiss) (holding that "the enactment of the Agricultural Credit Act [of 1987] should not be construed to alter the rights, interests and relationships of the parties under a [Chapter 11] plan confirmed before the effective date of the statute"); *In re* Pennington, No. 87-01485-BKC-DTW (Bankr. N.D. Miss. March 22, 1988) (1987 Act does not affect the valuation of secured property in bankruptcy pursuant to 11 U.S.C.A. § 506(a)); *In re* Bellman Farms, Inc., 86 Bankr. 1016 (S.D. Iowa 1988) (1987 Act does not affect the valuation of secured property in bankruptcy pursuant to 11 U.S.C.A. § 506(a)); *In re* Kvamme, 91 Bankr. 77, 78 (Bankr. D.N.D. 1988) (1987 Act does not "overrule, repeal, or render inoperative any portion of the Bankruptcy Code including [11 U.S.C.] section 1111(b)"); *In re* Felton, 95 Bankr. 629 (Bankr. N.D. Iowa 1988); *contra In re* Burton, No. 87-01099-K52, slip op. at 1 (Bankr. E.D. Wash. Aug. 12, 1988) (order fixing value of secured claim) (ordering that "the allowed secured claim of FCB [Farm Credit Bank of Spokane] under 11 U.S.C.A. § 1225(a)(5)(B)-(ii) shall be equal to the fair value of the real property collateral reduced by the cost of foreclosure as defined in the 1987 Act").

The issue of whether a debtor in a Chapter 12 bankruptcy proceeding may surrender or compel the retirement of his or her stock in an FLBA or PCA has resulted in inconsistent holdings by the courts addressing the issue. All of the reported decisions have permitted either full or partial surrender of stock, although the first of those decisions to be reported was reversed and the most recently decided case is on appeal to the Sixth Circuit. *In re* Massengill, 73 Bankr. 1008 (Bankr. E.D. N.C. 1987), *rev'd in part*, 100 Bankr. 276 (E.D. N.C. 1988); *In re* Indreland, 77 Bankr. 268 (Bankr. D. Mont. 1987); *In re* Chaney, 87 Bankr. 131 (Bankr. D. Mont. 1988); Matter of Arthur, 86 Bankr. 98 (Bankr. W.D. Mich. 1988); *In re* Ivy, 86 Bankr. 623 (Bankr. W.D. Mo. 1988); *In re* Neff, 89 Bankr. 672 (Bankr. S.D. Ohio 1988), *modified in part on reconsideration*, 96 Bankr. 800 (Bankr. S.D. Ohio 1989); *In re* Miller, 98 Bankr. 311 (Bankr. N.D. Ohio 1989), *order amended*, 106 Bankr. 136 (Bankr. N.D. Ohio 1989); *In re* Shannon, 100 Bankr. 913 (S.D. Ohio 1989), *appeal filed*, No. 89-3585 (6th Cir. June 19, 1989). *See also In re* Greseth, 78 Bankr. 936 (D. Minn. 1987) (affirming the

As a threshold matter, "restructuring" is broadly defined as follows:

> The terms "restructure" and "restructuring" include rescheduling, reamortization, renewal, deferral of principal or interest, monetary concessions, and the taking of any other action to modify the terms of, or forbear on, a loan in any way that will make it probable that the operations of the borrower will become financially viable.[367]

A borrower seeking to have a loan restructured must apply in writing on forms provided by the institution and, where appropriate, must support the proposed restructuring plan with "sufficient financial information and repayment projections."[368]

The general criteria for evaluating a restructuring proposal are as follows:

> When a qualified lender receives an application for restructuring from a borrower, the qualified lender shall determine whether or not to restructure the loan, taking into consideration —
> (a) whether the cost to the lender of restructuring the loan is equal to or less than the cost of foreclosure;
> (b) whether the borrower is applying all income over and above necessary and reasonable living and operating expenses to the payment of primary obligations;
> (c) whether the borrower has the financial capacity and the management skills to protect the collateral from diversion, dissipation, or deterioration;
> (d) whether the borrower is capable of working out existing financial difficulties, reestablishing a viable

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bankruptcy court's approval of a partial surrender of stock). *But cf. In re* Stedman, 72 Bankr. 49 (Bankr. D. N.D. 1987) (declining to deduct the value of the debtors' FLBA stock from the debtors' indebtedness to the FLB in determining the debtors' eligibility for Chapter 12). In addition, in affirming an unreported bankruptcy court decision, a district court has approved a Chapter 12 plan allowing the debtors to surrender their stock. *In re* Cansler, 99 Bankr. 758 (W.D. Ky. 1989).

367. 12 U.S.C.A. § 2202a(7) (West 1989). *See also* 12 C.F.R. § 614.4512(h) (1990) (defining "restructure" and "restructuring"). See 12 U.S.C.A. § 2202b (West 1989) and *supra* note 366 for the effect of restructuring on the borrower's stock in the institution.

368. 12 U.S.C.A. § 2202(a)(1) (West 1988). *See also* 12 C.F.R. § 614.4512(a) (1990) (defining "application for restructuring"); Federal Land Bank of Omaha v. Christensen, No. 22641 (Buena Vista Co. Dist. Ct., Iowa, July 6, 1988) (order granting FLB's motion for summary judgment on the grounds that an application for restructuring unaccompanied by a plan was fatally defective); Federal Land Bank of St. Louis v. McGinnis, 711 F. Supp. 952, 957 (E.D. Ark. 1989) ("FLB has authority to establish a deadline for submitting an application.").

operation, and repaying the loan on a rescheduled basis; and

(e) in the case of a distressed loan that is not delinquent, whether restructuring consistent with sound lending practices may be taken to reasonably ensure that the loan will not become a loan that it is necessary to place in nonaccrual status.[369]

Of those five criteria, the initial two warrant explanation and discussion.

A comparison of the "cost of foreclosure" with the "cost of restructuring" is at the core of the evaluation process. Indeed, because section 2202a(e)(1) provides that: [i]f a qualified lender determined that the potential cost to a qualified lender of restructuring the loan in accordance with a proposed restructuring plan is less than or equal to the potential cost of foreclosure, the qualified lender shall restructure the loan in accordance with the plan,[370] the comparison may be determinative.

"Cost of foreclosure" is specifically defined as follows:

The term "cost of foreclosure" includes—

(a) the difference between the outstanding balance due on a loan made by a qualified lender and the liquidation value of the loan, taking into consideration the borrower's repayment capacity and the liquidation value of the collateral used to secure the loan;

(b) the estimated cost of maintaining a loan as a nonperforming asset;

(c) the estimated cost of administrative and legal actions necessary to foreclose a loan and dispose of property acquired as the result of the foreclosure, including attorneys' fees and court costs;

(d) the estimated cost of changes in the value of collateral used to secure a loan during the period beginning on the date of the initiation of an action to foreclose or liquidate the loan and ending on the date of the disposition of the collateral; and

(e) all other costs incurred as the result of the foreclosure or liquidation of a loan.[371]

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369. 12 U.S.C.A. § 2202a(d)(1) (West 1989).

370. 12 U.S.C.A. § 2202a(e)(1) (West 1989).

371. 12 U.S.C.A. § 2202a(a)(2) (West 1989). *See also* 12 C.F.R. § 614.4512(c) (1990) (defining "cost of foreclosure").

"Cost of restructuring," or the computation of it, takes into account "all relevant factors" including the following:

(a) the present value of interest income and principal forgone by the lender in carrying out the restructuring plan;
(b) reasonable and necessary administrative expenses involved in working with the borrower to finalize and implement the restructuring plan;
(c) whether the borrower has presented a preliminary restructuring plan and cash-flow analysis taking into account income from all sources to be applied to the debt and all assets to be pledged, showing a reasonable probability that orderly debt retirement will occur as a result of the proposed restructuring; and
(d) whether the borrower has furnished or is willing to furnish complete and current financial statements in a form acceptable to the institution.[372]

Because the "cost of restructuring" considers "the present value of interest income and principal forgone by the lender in carrying out the restructuring plan," the conceptual approach to restructuring under the 1987 Act has generated confusion and questions as to whether Congress intended that the System apply traditional approaches to restructuring.

Traditionally, most lenders and borrowers have used the recovery value of the assets securing the note together with any other unencumbered, nonexempt assets as the benchmark for assessing the propriety of restructuring. If the borrower could "cash flow" a restructured note that had a present value equal to or greater than the value of the recoverable assets, then the lender could justify restructuring on the grounds that the restructured note would pay the same sum than the lender would realize through foreclosure or in a Chapter 12 bankruptcy proceeding.[373]

372. 12 U.S.C.A. § 2202a(e)(2) (West 1989). *See also* 12 C.F.R. § 614.4517(a) (1990) (consideration of application).

373. 11 U.S.C.A. §§ 1201-31 (West Supp. 1990) (codifying Bankruptcy Judges, United States Trustees, and Family Farmer Bankruptcy Act of 1986, Pub. L. No. 99-554, 251-57, 100 Stat. 3088, 3104-16 (1986)). For general discussions of Chapter 12, see Aiken, *Chapter 12 Family Farmer Bankruptcy*, 66 NEB. L. REV. 632 (1987); Armstrong, *The Family Farmer Bankruptcy Act of 1986: An Analysis for Farm Lenders*, 104 BANKING L.J. 189 (1987); Hahn, *Chapter 12 — The Long Road Back*, 66 NEB. L. REV. 726 (1987); Matson, *Understanding the New Family Farmer Bankruptcy Act*, 21 U. RICH. L. REV. 521 (1987); Wilson, *Chapter 12: Family Farm Reorganization*, 8 J. AGRIC. TAX'N & L. 299 (1987); Note, *Bankruptcy Chapter 12: How Many Family Farms Can It Salvage?*, 55 UMKC L. REV. 639 (1987); Note, *An Analysis of the Family Farmer Bankruptcy Act of 1986*, 15 HOFSTRA L. REV. 353 (1987).

Although each of the Farm Credit districts are operating under the same statute and essentially the same restructuring policies,[374] at least three different approaches to computing the appropriateness of restructuring appear to be in use. One approach, apparently employed only by the Seventh Farm Credit District based in St. Paul, Minnesota, is discussed in detail below.[375] Described charitably, the Seventh Farm Credit District's approach is nonsensical. As can be seen by examining the worksheets and their accompanying instructions set forth below, the Seventh Farm Credit District determines the cost of restructuring essentially by subtracting the present value of the proposed restructured note from the present value of the outstanding principal and interest on the original note computed at an interest rate, currently 12.5 percent, that is higher than the discount rate, currently 9 percent.[376] In effect, the computational formula used by the Seventh Farm Credit District allows the sum of money owed on the original rate that will never be paid, under any circumstances, to be the reference point for comparing all other cost. Under traditional, common sense approaches to restructuring, the reference point is the recovery value of the collateral together with any other recoverable assets, not a sum of money that the borrower is unable to repay.

No other district appears to be following the Seventh Farm Credit District's approach. Most appear to be using a liquidation analysis.[377] A liquidation analysis first determines the recovery value of any collateral and/or other recoverable assets.[378] Next, it determines the present value of the proposed restructured note.[379] Finally, it compares the recovery value of the assets with

374. Each system lender was required by the 1987 Act to develop a restructuring policy. 12 U.S.C.A. § 2202a(g) (West 1989). By and large, each of the policies parroted the language of the 1987 Act's loan restructuring provisions. (Copies of the policies are available from Mr. Kelley.) *See* Massey & Schneider, *supra* note 6, at 593 (the authors of this article reviewed the same policies reviewed by Mr. Massey and Ms. Schneider and came to the same conclusion).

375. *See infra* notes 389-94 and the accompanying text.

376. *Id.*

377. Although the meaning of a "liquidation analysis" varies with the context in which it is used, for bankruptcy purposes, liquidation analysis has been defined as follows: "... the debtor's equity (value of debtor's assets less the amount of any liens) in his non-exempt assets, when divided by all unsecured claims, must not exceed the percentage repayment to unsecured creditors proposed under the plan." Matson, *Understanding the New Family Farmer Bankruptcy Act*, 21 U. RICH. L. REV. 521, 531 (1987). A further definition is that a plan cannot be approved unless unsecured creditors receive as much under the plan as they would have in a chapter 7 bankruptcy. *Id.*

378. *Id.*

379. *Id.*

the present value of the proposed restructured note.[380] To the extent that other districts incorporate into their analysis the present value of interest income and principal forgiven by the lender in carrying out the restructure plan, those districts compute that figure under both the cost of foreclosure and the cost of restructuring so that the sum is "cancelled out."[381] In that way, the restructuring decision is not based on the sum of money that the borrower is unable to repay and that will never be recovered by the institution. However, at least one court has ruled that the 1987 Act "does not mandate the restructuring of the debt at the liquidation value of the collateral."[382]

At least one of the districts, the Fifth Farm Credit District based in Jackson, Mississippi, appears to be using what might be described as an "institutional cash flow analysis" approach to restructuring.[383] The analysis has many of the same features of a liquidation analysis, but it also incorporates the institution's "cost of funds" in the computations.[384]

Currently, borrowers seeking to apply for restructuring are encountering at least two practical difficulties. First, the computational process contemplated by the restructuring provisions of the 1987 Act are not discernible from anything less than a laborious, time-consuming reading of the statute. The restructuring policies issued to date pursuant to section 2202a(g) and provided to bor-

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380. *Id.*

381. *See* Wilson, *supra* note 373, at 302.

382. *In re Bellman Farms, Inc.*, 86 Bankr. 1016, 1022 (Bankr. D.S.D. 1988).

383. *See* FIFTH FARM CREDIT SYSTEM 1987, INTERNAL RESTRUCTURING MANUAL (1988) (available from Mr. Kelley).

384. Although the authors of this article have examined restructuring "worksheets" given to borrowers by System institutions in a number of districts, the authors only have copies of the internal restructuring manuals for the St. Paul and Jackson districts. Because North Dakota is in the Seventh Farm Credit District based in St. Paul, that district's restructuring formula is the focus of this article. Readers who represent borrowers in other districts may find common issues in the discussion that follows, but they should be aware that St. Paul may be the only district employing the formula discussed.

Readers are also advised that the restructuring formulas employed by System lenders may be modified from time to time. There is reason to believe that the restructuring requirements of the 1987 Act caused some confusion and disagreement among System lenders as to the specific methods by which the cost of restructuring and the cost of foreclosure were to be computed. As a consequence, the development of restructuring formulas has been influenced by differing interpretations of the law and differing institutional traditions, philosophies, and biases as well as an element of "trial and error."

It has been the experience of one of the authors, Mr. Kelley, an experience reportedly shared by others, that occasionally a loan will be restructured with little or no regard to the stated formula. Such experiences should not be unexpected given the number of differences between institutions, loan officers, and borrowers. Nevertheless, despite the difficulties of doing so, borrowers would be well advised to attempt to obtain their respective lender's formula prior to submitting an application for loan restructuring. Those difficulties are discussed at *infra* note 390 and the accompanying text. *See also* Massey & Schneider, *supra* note 6, at 592.

rowers as a part of the restructuring application "packet" generally parrot the language of the statute.[385]

In other words, as a matter of course, borrowers are not being provided with a clear, simple explanation of the computational steps involved in computing and comparing the cost of foreclosure and the cost of restructuring.

The second difficulty is that borrowers, as a matter of course, are not being provided with the institution's anticipated costs of foreclosure. In addition, some of the cost projections used by some institutions are either not justified or are not justifiable.[386]

The Seventh Farm Credit District, has issued a manual to its employees explaining the computational steps and the cost figures to be used in restructuring.[387] The manual includes worksheets that are to be completed by the loan officer and presented to the borrower at the credit review committee should review be necessary and requested. The current practice of the Seventh Farm Credit District is not to provide those worksheets to the borrower prior to the credit review committee meeting.[388] Even then, some institutions will not provide the borrower with a photocopy of the worksheets.[389]

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385. The adoption of restructuring policies is required by 12 U.S.C.A. § 2202a(g) (West 1989).

386. SEVENTH FARM CREDIT SYSTEM 1987, RESTRUCTURING MANUAL (1988). Significant portions of the manual can be found at *Oversight On The Implementation Of The Agricultural Credit Act Of 1987: Hearings Before the Subcommittee on Agricultural Credit of the Senate Committee on Agriculture, Nutrition, And Forestry*, 100th Cong., 2nd Sess. 415-76 (1988) (statement of James T. Massey, Executive Director of the Farmers' Legal Action Group, Inc.).

387. A more detailed statement of the views of one of the authors on these difficulties can be found at *Review Of Implementation Of The Agricultural Credit Act of 1987, Public Law 100-233: Hearing Before the Subcommittee on Conservation, Credit, And Rural Development of the House Committee on Agriculture*, 100th Cong., 2nd Sess. 286-94 (1988) (statement of Christopher R. Kelley, Visiting Assistant Professor of Law, William Mitchell College of Law).

Although the System lenders are not subject to the Freedom of Information Act (FOIA), 5 U.S.C.A. § 552 (West 1977 & Supp. 1990), the Farm Credit Administration is subject to the Act. *See* 12 C.F.R. §§ 602.250-602.265 (1990). Pursuant to 12 U.S.C.A. § 2202a(g)(3) (West 1989), some System lenders submitted substantial portions of their loan restructuring manuals or worksheets to the FCA. Those materials are available from the FCA through an FOIA request. *See also* Massey & Schneider, *supra* note 6, at 593 (referencing loan restructuring documents obtained through FOIA). *See generally* COMMITTEE ON GOVERNMENT OPERATIONS, 101ST CONG., 1ST SESS., A CITIZEN'S GUIDE ON USING THE FREEDOM OF INFORMATION ACT AND THE PRIVACY ACT OF 1974 TO REQUEST GOVERNMENT RECORDS (Comm. Print 1989) (a guide to the use of FOIA).

388. This statement is based on one of the author's, Mr. Kelley's, experience with borrower litigation. He found the practice to result in a significant waste of time at the credit committee review hearing because time had to be spent reviewing the figures used and checking the accuracy of the calculations made.

389. This practice is particularly pointless in light of the fact that the committee will usually permit the copying of the figures and calculations by hand. It underscores why Congress heard enough complaints from borrowers to prompt it to enact a statute requiring System lenders to give borrowers copies of the loan documents that they had signed. 12

The text of two of the basic worksheets used by the Seventh Farm Credit District together with the text of the instructions provided by the District together with the text of the instructions provided by the District to its loan officers follows. The worksheets included here are used for analyzing a restructuring proposal contemplating level payments. A restructuring proposal contemplating a cash-out, partial deed-back, or debt set aside requires the use of different restructuring worksheets. However, most of the basic concepts and calculations remain the same regardless of the terms of the restructuring proposal.

Because the worksheets and instructions require the use of present value calculations, present value and annuity tables based on a nine percent discount rate follow the worksheets and instructions. The Seventh Farm Credit District has chosen nine percent as its discount factor, and the tables must be consulted to complete the worksheets. Following the tables is a brief discussion of several aspects of the worksheets and the instructions that require clarification or comment.

U.S.C.A. § 2200 (West 1989). *See also supra* note 347 and the accompanying text (quoting a member of the FCA Board as stating that "I think it's a shame when the FCA has to issue regulations to insure the rights of stockholders and loan applicants").

FORECLOSURE COSTS

WORKSHEET

MEMBER VIEW $_____

PRINCIPAL $_____

INTEREST $_____

			COSTS
1. INVESTMENT			$ _____
2. ADD: COSTS			
A) TAXES	$ _____		
B) DISPOSITION COSTS	$ _____		
C) LEGAL	$ _____		
D) INSURANCE AND REPAIR	$ _____		
$ _____			
3. TOTAL INVESTMENT			
$ _____			
4. LESS: RECOVERABLE ASSETS			
A) STOCK	$ _____		
B) AV OF PROPERTY X (.8780) NPV	$ _____		
C) OTHER RECOVERABLE ASSET (PV)	$ _____	$ _____	
5. FORECLOSURE			
$ _____			

COST OF FORECLOSURE PROCEDURE

1. INVESTMENT — This line shows our total investment to date, including all expenses advanced and accrued interest.
2. ADD: COSTS —
   a) TAXES — This represents all past due taxes (excluding those advanced and shown above in Line 1) and two years of estimated future taxes.
   b) DISPOSITION COSTS — This represents our anticipated sales costs. Based on projections and experience in acquired property sales, this is a flat 3% of appraised value. Calculation: AV X 3%.[390]
   c) LEGAL — Again, these are anticipated legal expenses which are not already included in Line 1. We expect 1-2% of AV for legal expenses; however, your legal expense levels must be based on individual service center experience.
   d) INSURANCE AND REPAIR — Enter estimated insurance and repair expenses during the foreclosure process.
3. TOTAL INVESTMENT — This represents our investment after adding the foreclosure costs FCS faces in a foreclosure action. Please note that the added costs are not calculated on a net present value basis. The timing of expenses is so varied, including many front-end expenses, such that a present value calculation would require an inordinate amount of time and would show only a slight impact on the costs presented.
4. LESS: RECOVERABLE ASSETS
   a) STOCK — Enter the current amount of stock held by the borrower. Remember that on a foreclosure in process stock may have been applied as a reduction in the investment amount (Line 1). If that is the case, Line 4a should be zero.

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390. The three percent figure may have been increased to five percent in mid-1988. Because it is the current policy of the Seventh Farm Credit District not to divulge the specific contents of current loan restructuring policy manuals, this figure cannot be confirmed. Telephone interview with William Collins, General Counsel for the Seventh Farm Credit District, Dec. 22, 1989. Moreover, as noted at *supra* note 384, loan restructuring policies for all of the System lenders are subject to change in various respects. Accordingly, the reader is advised to attempt to obtain the current manual or other written policy statement prior to relying on the information provided in this article regarding the contents of the Seventh Farm Credit District's loan restructuring manual. Failing that, the reader should use the portions of the manual discussed or reproduced in this article only as a general guide.

b) AV OF PROPERTY — This line represents the present value of the property we would recover in foreclosure. We recommend calculating an amount by multiplying the appraised value of the property by a .8780 discount factor (based on a 9% discount rate over one and a half years). However, if the loan officer has *strong* evidence that the property value will change (up or down), you may use the present value of the appreciated or depreciated property. Also, the length of foreclosure may vary if properly supported.

c) OTHER RECOVERABLE ASSETS — This line includes the present value of any other assets we could recover in the foreclosure process, including the value of any deficiency judgments. The asset should reflect present values.

5. COST OF FORECLOSURE — This line represents the cost of foreclosure for comparison with restructuring costs. It is calculated by subtracting the Total Recoverable Assets from Total Investment. Line 3 — (lines 4a + 4b)

COMMENTS — If foreclosure costs exceed restructure costs, explain here the appropriate credit factors which support foreclosure over restructure. This section must address factors supporting foreclosure such as:

a) borrower applying all available income to the payment of primary obligations

b) borrower's financial capacity and management skills to protect collateral

c) borrower's capacity to work out of existing financial difficulties

RESTRUCTURE COSTS — LEVEL PAYMENTS[391]

WORKSHEET

1. RESTRUCTURE TERMS
   - A) PRINCIPAL $ _____
   - B) CASH $ _____
   - C) STOCK _____
   - D) OTHER CONSIDERATIONS _____
   - E) TOTAL CONSIDERATIONS $ _____
   - F) INTEREST RATE/TERMS _____

COSTS

2. PRESENT VALUE ORIGINAL LOAN $ _____
3. ADD: PRESENT INTEREST FORGIVEN
   - A) PRESENT INTEREST $ _____
   - B) LESS: CASH PAYMENT _____
   - C) LESS: STOCK _____
   - D) LESS: OTHER CONSIDERATIONS _____ _____
4. LESS: PRESENT VALUE RESTRUCTURED LOAN $ _____
5. OTHER RESTRUCTURE COSTS
   - A) $ _____
   - B) _____

$_____

6. COMPROMISE/RESTRUCTURE COSTS

$_____

391. The Seventh Farm Credit District has changed the restructure costs worksheet that formerly accompanied the instructions that follow. The worksheet set forth is the newer one. Thus, Item 2 in the instructions that follow, "Present Interest Forgiven," is now found at Item 3 on the new worksheet. Item 4 is the instructions, "Present Value of Interest Concessions," is omitted from the newer worksheet. Item 3(a) in the instructions, "Present Value of Foregone Principal and Interest — Original Amount," is now shown at Item 2 on the newer worksheet. Item 3(b) of the instructions, "Less: Restructured Amount," is shown at Item 4 of the newer worksheet.

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RESTRUCTURE COSTS — LEVEL PAYMENTS
PROCEDURES/DEFINITIONS

1. RESTRUCTURE TERMS —
   a) PRINCIPAL — This line shows the principal balance of the loan after the restructure is completed and accounted for.
   b) CASH — Enter any cash payment received.
   c) STOCK — Enter the value of all stock reductions which are applied to the loan in the restructure.
   d) OTHER CONSIDERATIONS — This category includes any other monetary considerations received for the restructure, including up-front cash, set aside loans or net recovery value of collateral deeded to FCS. In complex restructures, loan officers have the option to add lines (d, e, f . . .) if necessary to clarify the restructure terms. Do not include the value of additional collateral as other considerations.
   e) TOTAL CONSIDERATION — This line is the sum of Lines 1a, 1b, 1c and 1d.
   f) INTEREST RATE/TERMS — This line briefly defines the interest rates charged on the restructured loan, including any concessionary rates (and their duration). It also should identify the term of the restructured loan. This format is for level payments.
2. PRESENT INTEREST FORGIVEN — The Agricultural Credit Act of 1987 provides Farm Credit institutions with the ability to consider foregone principal and interest as part of its Restructure Costs. This section identifies the cost associated with present interest forgiven.
   a) PRESENT INTEREST — Enter the present interest balance.
   b) LESS: CASH PAYMENT — Enter any cash payment (if any) intended to be a payment of interest. Show the net of Lines 2a and 2b under the "Cost" column.
   c) LESS: STOCK — Enter the value of any stock applied to the loan as part of the restructure.
   d) LESS: OTHER CONSIDERATIONS — Enter the value of other considerations identified on Line 1d. Enter the result of Lines 2a minus 2b minus 2c minus 2d in the right hand column.

3. PRESENT VALUE OF FOREGONE PRINCIPAL AND INTEREST — This section evaluates the present value of foregone principal and interest by comparing the present value of the original loan with the present value of the restructured loan. We use the present value of the original loan with the present value of the restructured loan. We use the present value of an annuity concept (annual payments over a defined period of time) to determine the present value of a flow of equal payments. The difference is foregone for the life of the loan.
   a) ORIGINAL AMOUNT — Enter the result of the original payment amount times the appropriate present value factor (PVF) to show the present value of the original loan.
   b) LESS: RESTRUCTURED AMOUNT — This line begins with a restructured payment amount which is calculated from the restructured principal amount and the general interest rate that would apply to the loan without any interest rate concessions. Enter the result of the restructured payment times the appropriate present value factor to show the present value of the restructured loan. Subtract this amount from the result in Line 3a and enter this difference in the right hand column.
4. PRESENT VALUE OF INTEREST CONCESSIONS — There are costs associated with interest concessions which can be calculated on a present value basis. These calculations are less exact, but provide a sound approximation of the cost of an interest rate concession. Use this only when offering a concessionary interest rate for part of the loan term.
   a) RESTRUCTURED PAYMENT AMOUNT — Enter the same payment amount as shown on Line 3b.
   b) LESS: CONCESSION PAYMENT AMOUNT — Enter the payment amount based on the concessionary interest rate and the term of the concessionary rate.
   c) FOREGONE ANNUAL PAYMENT AMOUNT — Enter the difference between Line 4a and 4b on this line.
   d) TIMES: PRESENT VALUE FACTOR — Multiply the result on Line 4c by appropriate present value factor based on the interest rate concession and the length of the concession. Show the results of this calculation under the "Cost" column. (We are using a present value of an annuity table — further directions will be provided in the final draft.)

5. OTHER RESTRUCTURE COSTS — Recognizing there may be additional out of pocket costs for the Farm Credit lender in restructuring a loan, this section allows for consideration of those costs. Most will likely be up-front costs and, therefore, no present value calculations are necessary. Show the total other restructure costs under the "Cost" column.
6. COMPROMISE/RESTRUCTURE COSTS — Add the costs for each section and show the total at Line 6 under the "Cost" column.

ORDINARY ANNUITY TABLE

(Present Value Factors)

DISCOUNT FACTORS: 9% annual rate

DIRECTIONS: To use this ordinary annuity table to determine appropriate present value factors, begin by identifying the number of years the periodic payments will be made. Moving down the year column to the appropriate year identifies the present value factors available for monthly, quarterly, semi-annual and annual payment options. Move across from the year column at the selected number of years to the payment option that fits the loan being present valued. The present value factor is the number under the appropriate payment option and across from the appropriate year. For example, the present value factor for a 20 year loan with annual payments is 9.129.

	PAYMENT OPTIONS			
YEAR	MONTHLY	QUARTERLY	SEMI-ANNUAL	ANNUAL
1	11.435	3.785	1.873	.917
2	21.889	7.247	3.588	1.759
3	31.447	10.415	5.158	2.531
4	40.185	13.313	6.596	3.240
5	48.173	15.964	7.913	3.890
6	55.477	18.389	9.119	4.486
7	62.154	20.608	10.223	5.033
8	68.258	22.638	11.234	5.535
9	73.839	24.495	12.160	5.995
10	78.942	26.194	13.008	6.418
11	83.606	27.748	13.784	6.805
12	87.606	29.170	14.495	7.161
13	91.770	30.470	15.147	7.487
14	95.335	31.660	15.743	7.786
15	98.593	32.749	16.289	8.061
16	101.573	33.745	16.789	8.313
17	104.297	34.656	17.247	8.544
18	106.787	35.490	17.666	8.756
19	109.064	36.353	18.050	8.950
20	111.145	36.950	18.402	9.129
21	113.048	37.588	18.724	9.292
22	114.788	38.172	19.018	9.442
23	116.378	38.706	19.288	9.580
24	117.832	39.195	19.536	9.707
25	119.162	39.642	19.762	9.823
26	120.377	40.051	19.969	9.929
27	121.488	40.425	20.159	10.027
28	122.504	40.767	20.333	10.116
29	123.433	41.080	20.492	10.198

PRESENT VALUE TABLES

DISCOUNT FACTOR: 9% annual rate

DIRECTIONS: Use this table to determine the present value of a single payment at a future point in time. Determine the present value factor by moving down the Year column to the year in which you will receive the single payment. Then move across to the Present Value Factor column and identify the appropriate present value factor. For example, the present value factor for a single payment in year 20 is .178. These factors assume annual compounding of the discount factor.

YEAR	PRESENT VALUE FACTOR
1	.917
2	.842
3	.772
4	.708
5	.650
6	.596
7	.547
8	.502
9	.460
10	.422
11	.388
12	.356
13	.326
14	.299
15	.275
16	.252
17	.231
18	.212
19	.194
20	.178
21	.164
22	.150
23	.138
24	.126
25	.116
26	.106
27	.098
28	.090
29	.075
30	.069

The preceding worksheets and instructions are largely self-explanatory. However, they are imprecise at points and possibly inaccurate with respect to certain foreclosure costs. Therefore, several comments are in order.[392]

FORECLOSURE COSTS:

Item 2(b) *Disposition Costs*: The use of 3% of the appraised value of the collateral for the disposition cost of that collateral appears to be extraordinarily conservative. The instructions offer no justification for that figure. Bearing in mind that arbitrary and capricious behavior by the institution may be the basis for a defense to a foreclosure action,[393] the institution should be put to the task of justifying all of its foreclosure cost figures.

Item 2(c) *Legal Costs*: Note that the instructions require that those costs be based on actual service center experience. As with disposition costs, legal costs must be justified. If the institutions assume incorrectly that the foreclosure will be uncontested and not followed by a bankruptcy reorganization proceeding, the institution should be requested to adjust its legal costs accordingly.

Item 2(d) *Insurance and Repair*: Generally, the insurance cost for bare land will be 0. For buildings, it will be $9.00 per $1,000 of insurable value. Repair needs and costs should be brought to the attention of the institution. Some institutions are using 1-12% of appraised value for their cost.

Item 4(b) *Net Present Value of the Collateral*: The .8780 net present value factor reflects a 9% discount rate for 1-1/2 years. If a longer time before recovery is anticipated, such as where a contested foreclosure or reorganization proceeding is contemplated, a lower net present value factor should be used.

Item 4(c) *Other Recoverable Assets*: This figure should reflect net recovery value discounted from the date of anticipated recovery. In other words, there will be costs associated with the recovery of those assets, and the institution should take those costs into account.

COST OF RESTRUCTURING:

Item 2 *Present Interest Forgiven*: Make sure that this future has not been improperly included in the item 2 calculation above it. If the item 2 calculation runs from the date of the initial default, it necessarily will have included the accrued interest reflected in the item 3(a) figure. Thus, the institution will have

392. These comments are based on Mr. Kelley's experiences in representing borrowers seeking restructuring and on his conversations with other attorneys and borrowers.

393. See *infra* notes 444-73 and the accompanying text.

"double-dipped" and improperly increased the cost of restructuring amount.

Item 3 *Present Value of Foregone Principal and Interest*: Make sure that the original loan payment used in the item 2 calculation is not based on a default interest rate. Using a default interest rate is inappropriately punitive and will result in a higher cost of restructuring. The institution should assume that the foregone payments on the original note will be based on the interest rate applicable to the loan prior to default. Also, be sure that the calculation is based only on foregone payments. In other words, the present value factor used should correlate with the number of payments that will not be made, not the full term of the note from its inception. Otherwise, the borrower is not given credit for payments made prior to default.

Item 5 *Other Restructure Costs*: This figure will usually be $500.00.

In applying for restructuring, borrowers should be aware of the "least cost alternative" provisions of section 2202a(f).[394] That section provides as follows:

> If two or more restructuring alternatives are available to a qualified lender under this section with respect to a distressed loan, the lender shall restructure the loan in conformity with the alternative that results in the least cost to the lender.[395]

If a borrower's restructuring proposal does not contemplate paying to his primary creditors all of his income in excess of his reasonable living and operating expenses, section 2202a(f) appears to give the institution the option of proposing an alternative that captures that income.[396]

System institutions are required to provide written notice to a borrower that the borrower's loan "may be suitable for restructuring" when the institution determines that the loan is or has

394. 12 U.S.C.A. § 2202a(f) (West 1989).

395. *Id.*

396. *See* 12 U.S.C.A. § 2202a(d)(1)(B) (West 1989) (a consideration in determining whether a borrower is eligible for restructuring is "whether the borrower is applying all income over and above necessary and reasonable living and operating expenses to the payment of primary obligations"); 12 U.S.C.A. § 2202a(d)(2) (West 1989) ("This section shall not prevent a qualified lender from proposing a restructuring plan for an individual borrower in the absence of an application for restructuring from the borrower."). *See* Hill v. Farm Credit Banks of St. Louis, 726 F. Supp. 1201, 1206 (E.D. Mo. 1989) ("The 1987 Act specifically provides that a lender may propose a restructuring plan in the absence of an application from the borrower." (citing 12 U.S.C. § 2202a(d)(2)). *See also* 12 C.F.R. § 614.4516(c) (1990) ("A qualified lender may, in the absence of an application for restructuring from a borrower, propose a restructuring plan for an individual borrower.").

become a "distressed loan."[397] The notification must include a copy of the appropriate restructuring policy and "all materials necessary to enable the borrower to submit an application for restructuring the loan."[398] A distressed loan is defined as follows:

> The term "distressed loan" means a loan that the borrower does not have the financial capacity to pay according to its terms and that exhibits one or more of the following characteristics:
>
> (a) The borrower is demonstrating adverse financial and repayment trends.
>
> (b) The loan is delinquent or past due under the terms of the loan contract.
>
> (c) One or both of the factors listed in subparagraphs (a) and (b), together with inadequate collateralization, present a high probability of loss to the lender.[399]

Notice must also be given not later than 45 days before the commencement of foreclosure proceedings against the borrower.[400] In addition, section 2202(b)(3) provides as follows:

> No qualified lender may foreclose or continue any foreclosure proceeding with respect to any distressed loan before the lender has completed any pending consideration of the loan for restructuring under this section.[401]

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397. 12 U.S.C.A. § 2202a(b)(1) (West 1989). *See also* 12 C.F.R. § 614.4516(a) (1990) (restructuring procedures: notice); Erickson v. Federal Land Bank of Omaha, 101 Bankr. 124, 125-26 (D. Neb. 1989) (borrowers unsuccessfully argued that the FLB had failed to make a specific determination that their loan was distressed before advising them of the right to seek restructuring), *aff'd*, 894 F.2d 1342 (8th Cir. 1989); *In re* Wagner, 107 Bankr. 662, 663 (Bankr. D. Neb. 1989) ("The statute requires and the debtors have the right to know that the Farm Credit Bank has made a determination that the loan 'is or has become distressed' before any restructuring obligations fall upon debtors and before any foreclosure rights accrue to Farm Credit Bank."); *In re* Rudloff, 107 Bankr. 663, 665 (Bankr. D. Neb. 1989) (interpreting the Act to require the lender to determine that the loan is distressed prior to providing notice of restructuring rights).

398. 12 U.S.C.A. § 2202a(b)(1)(B) (West 1989). *See also* 12 C.F.R. § 614.4516(a)(2) (1990) (same requirement).

399. 12 U.S.C.A. § 2202a(3) (West 1989). *See also* 12 C.F.R. § 614.4512(d) (1990) (defining "distressed loan").

400. 12 U.S.C.A. § 2202a(b)(2) (West 1989). *See also* 12 C.F.R. § 614.4516(a)(2), 614.4519(a) (1990) (same requirement).

401. 12 U.S.C.A. § 2202a(b)(3) (West 1989). *See also* 12 C.F.R. § 614.4519(b) (1990) (same requirement). The issue of whether a "foreclosure proceeding" is continuing or has been completed is to be resolved under state law. *See* Harper v. Federal Land Bank of Spokane, 692 F. Supp. 1244, 1250 (D. Ore. 1988), *rev'd* 878 F.2d 1172 (9th Cir. 1989), *cert. denied*, 110 S. Ct. 867 (1990); Federal Land Bank of St. Louis v. Cupples, 889 F.2d 764, 767-68 (8th Cir. 1989); Griffin v. Federal Land Bank of Wichita, 708 F. Supp. 313 (D. Kan. 1989), *aff'd*, 902 F.2d 22 (10th Cir. 1990); Federal Land Bank of Omaha v. Engelken, No. C85-2062 (N.D. Iowa Aug. 25, 1988).

The term "foreclosure proceeding" is specifically defined in section 2202a(4) as follows:

> The term "foreclosure proceeding" means:
>
> (a) a foreclosure or similar legal proceeding to enforce a lien on property, whether real or personal, that secures a nonaccrual or distressed loan; or
>
> (b) the seizing of and realizing on nonreal property collateral, other than collateral subject to a statutory lien arising under subchapters I or II of this chapter to effect collection of a nonaccrual or distressed loan.[402]

Apparently, an action to collect on an unsecured note would not be a foreclosure proceeding within the meaning of section 2202a(4).

Section 2202a(c) requires institutions to give borrowers a "reasonable opportunity" for a meeting between the borrower and a loan officer or other representative.[403]

Specifically, that section provides as follows:

> On determination by a qualified lender that a loan made by the lender is or has become a distressed loan, the lender shall provide a reasonable opportunity for the borrower thereof to personally meet with a representative of the lender —
>
> (1) to review the status of the loan, the financial condition of the borrower, and the suitability of the loan for restructuring; and
>
> (2) with respect to a loan that is in nonaccrual status, to develop a plan for restructuring the loan if the loan is suitable for restructuring.[404]

If the restructuring proposal is denied, the borrower may request a review of the denial by a credit review committee. The request must be made in writing within seven days after receiving the notice of denial.[405]

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402. 12 U.S.C.A. § 2202a(4) (West 1989). *See also* 12 C.F.R. § 614.4512(e) (1990) (defining "foreclosure proceeding").

403. 12 U.S.C.A. § 2202a(c) (West 1989). *See also* 12 C.F.R. § 614.4516(b) (1990) (opportunity for meeting).

404. 12 U.S.C.A. § 2202a(4) (West 1989). *See also* 12 C.F.R. § 614.4516(b)(1) (1990) (same requirement).

405. 12 U.S.C.A. § 2202(b)(2) (West 1989). *See also* 12 C.F.R. § 614.4518(c) (1990) (same requirement).

At the credit review committee, the borrower may appear in person accompanied by counsel or any other representative.[406] Prior to the enactment of the Agricultural Credit Technical Corrections Act of 1988,[407] the borrower seeking review of a denial of restructuring did not have the right to an independent appraisal except when "additional collateral for a loan is demanded by the qualified lender when determining whether to restructure the loan."[408] However, under the 1988 Act, the borrower now has a right to request an independent appraisal.[409] The borrower must be notified in writing of the decision of the credit review committee and the reasons for that decision.[410]

The credit review committee's review ends the institution's review process. If the credit review committee affirms the initial denial of the restructuring, the institution may and usually will commence the appropriate legal proceedings to foreclose on the collateral and obtain judgment on the note.[411]

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406. 12 U.S.C.A. § 2202(c) (West 1989). *See also* 12 C.F.R. § 614.4443(a) (1990) (personal appearance).

407. Pub. L. No. 100-399, 102 Stat. 989 (1988).

408. 12 U.S.C.A. § 2202(d)(4) (West Supp. 1989).

409. Agricultural Technical Corrections Act of 1988, Pub. L. No. 100-399, 103, 102 Stat. 989, 990 (codified at 12 U.S.C.A. § 2202(d) (West 1989). *See also* 12 C.F.R. § 614.4443(c) (1990) (same requirement). However, neither the statute nor the regulations provide that the credit review committee must give any particular weight to the independent appraisal. The only requirement is that the committee must "consider" the results of the appraisal. In the absence of an implied cause of action permitting judicial review of that "consideration," System institutions have little, if any, fear of recourse if the appraisal is ignored. *See also* Payne v. Federal Land Bank of Columbia, 711 F. Supp. 851, 855 (W.D.N.C. 1989) ("It is common knowledge in land and lending circles that appraisers can be selected with a view toward valuation of a given property that is congenial to the employing party. . . . This is why many evaluation provisions in real estate contracts are drafted to permit each side to choose an appraiser, the two of whom in turn choose a third; the resulting three appraisals then being averaged").

410. 12 U.S.C.A. § 2202(e) (West 1989). *See also* 12 C.F.R. § 614.4443(d) (1990) (same requirement).

411. If the institution has been certified by the Assistance Board pursuant to 12 U.S.C.A. § 2278a-4 (West 1989), there is one more stage in the review process. Specifically, 12 U.S.C.A. § 2202c(a) (West 1989) provides as follows:

> Within 9 months after a qualified lender is certified under section 2278a-4 of this title, such lender shall review each loan that has not been previously restructured and that is in nonaccrual status on the date the lender is certified, and determine whether to restructure the loan.

Id. The review contemplated by section 2202c(a) is to be done by a special asset group established by each district. 12 U.S.C.A. §§ 2202, 2202c(b)(1) (West 1989). If the district special asset group determines that a loan should be restructured, "the group shall prescribe a restructuring plan for the loan that the qualified lender shall implement." 12 U.S.C.A. § 2202c(b)(2) (West 1989). If the group determines that a loan should not be restructured, it must submit a report to the National Special Asset Council described below explaining that decision. 12 U.S.C.A. § 2202c(d) (West 1989).

The statute is silent as to the borrower's right to participate in the review by the district special asset group. The regulations governing that review are also silent as to that issue. 12 C.F.R. § 614.4520 (1990).

Pursuant to 12 U.S.C.A. § 2202c(c)(1) (West 1989), the Assistance Board is to establish a National Special Asset Council to do the following:

G. RIGHT OF FIRST REFUSAL

The 1987 Act requires System institutions, except for the bank for cooperatives, holding agricultural real estate acquired through foreclosure or voluntarily conveyed by a borrower who, in the institution's determination, did not have the financial resources to avoid foreclosure to give the former owner the right of first refusal to repurchase or lease the property.[412] With respect to the right of first refusal to purchase the property, sections 2219a(b)(1) - (5) provide as follows:

> (1) Election to sell and notification
> Within 15 days after an institution of the System first elects to sell acquired real estate, or any portion of such real estate, the institution shall notify the previous owner by certified mail of the owner's right —
> (A) to purchase the property at the appraised fair market value of the property, as established by an accredited appraiser; or
> (B) to offer to purchase the property at a price less than the appraised value.
> (2) Eligibility to purchase
> To be eligible to purchase the property under paragraph (1), the previous owner must, within 30 days after receiving the notice required by such paragraph, submit an offer to purchase the property.[413]
> (3) Mandatory sale

> (A) monitor compliance with the restructuring requirements of this section by qualified lenders certified to issue preferred stock under section 2278b-7 of this title, and by special asset groups established under subsection (b) of this section; and
> (B) review a sample of determinations made by each special asset group that a loan will not be restructured.

Id. In addition, 12 U.S.C.A. § 2202c(c)(2) (West 1989) provides that the National Special Asset Council "shall review a sufficient number of determinations made by each special asset group to foreclose on any loan to assure the Council that such group is complying with this section." *Id.* For each determination reviewed, "the Council shall make an independent judgment on the merits of the decision to foreclose rather than restructure the loan." *Id.* In addition:

> If the National Asset Council determines that any special asset group is not in substantial compliance with this section, the Council shall notify the group of the determination, and may take such other action as the Council considers necessary to ensure that such group complies with this section.

12 U.S.C.A. § 2202c(c)(3) (West 1989). As with reference to the district special asset group, the statute and the regulations are silent regarding the borrower's right to participate in any review by the National Special Asset Council. 12 C.F.R. § 614.4520 (1990).

412. 12 U.S.C.A. § 2219a (West 1989). *See also* 12 C.F.R. § 614.4522(2) (1990) (defining "previous owner").

413. As originally enacted, the 1987 Act prescribed a fifteen day time period. The fifteen day period was changed to thirty days by the Agricultural Technical Corrections Act

An institution of the System receiving an offer from the previous owner to purchase the property at the appraised value shall, within 15 days after the receipt of such offer, accept such offer and sell the property to the previous owner.[414]

(4) Permissive sale

An institution of the System receiving an offer from the previous owner to purchase the property at a price less than the appraised value may accept such offer and sell the property to the previous owner. Notice shall be provided to the previous owner of the acceptance or rejection of such offer within 15 days after the receipt of such offer.

(5) Rejection of offer of previous owner

(A) Duties of institution

An institution of the System that rejects an offer from the previous owner to purchase the property at a price less than the appraised value may not sell the property to any other person —

(i) at a price equal to, or less than, that offered by the previous owner, or

(ii) on different terms and conditions than those that were extended to the previous owner, without first affording the previous owner an opportunity to purchase the property at such price or under such terms and conditions.

(B) Notice

Notice of the opportunity in subparagraph (A) shall be provided to the previous owner by certified mail, and the previous owner shall have 15 days in which to submit an offer to purchase the property at such price or under such terms and conditions.[415]

The provisions governing the right of first refusal to lease acquired

of 1988, Pub. L. No. 100-399, 104, 102 Stat. 989, 990 (codified at 12 U.S.C.A. § 2219a(b)(2) (West 1989). *See also* 12 C.F.R. § 614.4522(c)(3) (1990) (thirty days).

414. As originally enacted, the 1987 Act prescribed a thirty day time period. The thirty day period was changed to fifteen days by the Agricultural Technical Corrections Act of 1988, Pub. L. No. 100-399, 104, 102 Stat. 989, 990 (codified at 12 U.S.C.A. § 2219a(b)(3) (West 1989). *See also* 12 C.F.R. § 614.4522(c)(2) (1990) (fifteen days).

415. 12 U.S.C.A. § 2219a(b)(1)-(5) (West 1989).

property are similar.[416]

The right of first refusal as set forth in sections 2219(a)(b)(1)-(5) presents several potential difficulties for borrowers. First, neither the statute nor the regulations specifically define the event constituting the institution's "first elect[ion] to sell."[417] In states where corporations are prohibited from owning agricultural real estate, it might be argued that the "election to sell" occurs as soon as the land is acquired since the institution is not permitted to retain it. On the other hand, it might be argued that no election to sell occurs until an eligible purchaser actually has agreed to buy the parcel.

A more troublesome difficulty for borrowers is the absence of any express mechanism for challenging the appraisal of the property. In addition, neither the statute nor the regulations define the statute's term "accredited appraiser."[418] It can be expected that some Farm Credit Banks will use "in house" appraisers who may base their appraisals on sales of other inventory land that has been sold with inflationary inducements such as money-back guarantees and low interest rate financing that would not be offered to former owners under the right of first refusal.[419]

The former owner who cannot match the appraised price faces uncertainty as to whether he will receive another opportunity to elect to buy the land. The statute does permit the former owner to offer a sum less than the appraised value. However, if that offer is rejected, the institution must again offer the right of first refusal only if it subsequently desires to sell the land at "a price equal to, or less than, that offered by the previous owner" or "on different terms and conditions than those that were extended to the previous owner."[420] In areas where land values are increasing, it is unlikely that the institution will desire to sell the land at a price equal to, or less than, that offered by the previous owner. In addition, it is very likely that the terms and conditions will be dif-

416. 12 U.S.C.A. § 2219a(c)(1)-(6) (West 1989).

417. 12 C.F.R. § 614.4522 (1990).

418. *Id.* *See* 55 FED. REG. 24,861 (1990) (prefatory comments stating that the FCA intends to republish proposed regulations on appraisal standards "in the near future").

419. *See* 12 U.S.C.A. § 2219a(f) (West 1989) (". . . a system institution shall not be required to provide financing to the previous owner in connection with the sale of acquired real estate"). *See also* Payne v. Federal Land Bank of Columbia, 711 F. Supp. 851, 855 (1989) ("It is common knowledge in land and lending circles that appraisers can be selected with a view toward valuation of a given property that is congenial to the employing party"); *In re* Jarrett Ranches, Inc., 107 Bankr. 969, 973 (Bankr. D.S.D. 1989) (invalidating the FCB's appraisal of former borrowers' land in parcels rather than as a whole and setting an appraised value).

420. 12 U.S.C.A. § 2219a(b)(5) (West 1989). *See also* 12 C.F.R. § 614.4522(c)(3) (1990) (same requirement).

ferent. This occurs because the only "terms and conditions" that likely will have been initially offered to the former owner are the sale of the land at a lump sum cash price. On the other hand, a third-party prospective purchaser is likely to be offered many other "terms and conditions" such as a money-back guarantee, apportionment of real estate taxes, etc.[421] The uncertainty regarding a second chance to elect to buy the land arises because even if the "terms and conditions" differ, it is possible that the institution may neglect to inform the former owner not only of those differences but also, and more fundamentally, of the transaction itself, because the institution may choose to ignore or narrowly read the statute.

To date, some System institutions have attempted to avoid giving former owners the benefits of sections 2219a(b) (1) - (5) by choosing to sell the acquired property by auction without first giving the former owner the opportunity to buy it at its appraised value.[422] Institutions may sell acquired land by auction. In that regard, sections 2219a(d) (1) - (3) provide as follows:

> (d) Public Offerings
>
> (1) Notification of previous owner
>
> If an institution of the System elects to sell or lease acquired property or a portion thereof through a public auction, competitive bidding process, or other similar public offering, the institution shall notify the previous owner, by certified mail, of the availability of the property. Such notice shall contain the minimum amount, if any, required to qualify a bid as acceptable to the institution and any terms and conditions to which such sale or lease will be subject.
>
> (2) Priority
>
> If two or more qualified bids in the same amount are received by the institution under paragraph (1), such bids are the highest received, and one of the qualified bids is offered by the previous owner, the institution shall accept the offer by the previous owner.
>
> (3) Nondiscrimination
>
> No institution of the System may discriminate

421. Financing is not considered a "term or condition" of sale. 12 U.S.C.A. § 2219a(e) (West Supp. 1989). *See also* 12 C.F.R. § 614.4522(c)(4) (1990) (same).

422. *See infra* notes 424-25 and the accompanying text.

> against a previous owner in any public auction, competitive bidding process, or other similar public offering of property acquired by the institution from such person.[423]

However, at least two federal district courts have held that sales by auction must be preceded by giving the former owner the opportunity to buy the acquired land at its appraised value.[424] A third federal district court has held to the contrary.[425]

Finally, with respect to the right of first refusal, 2219a(h) provides that "[t]he rights provided in this section shall not diminish any such right of first refusal under the law of the State in which the property is located."[426] This provision appears to provide that state first refusal statutes will supplement the federal right.

H. PROHIBITION AGAINST WAIVER OF MEDIATION RIGHTS

The 1987 Act encourages the states to establish mediation programs. Further, the Farm Credit System is required to participate in mediation.[427] In addition, Congress had the foresight to realize that the right to mediation could be used as a chip in negotiations for a loan. In order to avoid that, the 1987 Act contains the following language:

> No System institution may make a loan secured by a mortgage or lien on agricultural property to a borrower on the condition that the borrower waive any right under the agricultural loan mediation program of any State.[428]

The Farm Credit Administration is required to promulgate rules

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423. 12 U.S.C.A. § 2219a(d)(1)-(3) (West 1989).

424. Leckband v. Naylor, 715 F. Supp. 1451, 1455 (D. Minn. 1988), *appeal dismissed*, Nos. 88-5301 MN & 89-5141 MN (8th Cir. May 5, 1989); Martinson v. Federal Land Bank of St. Paul, 725 F. Supp. 469 (D.N.D. 1988), *appeal dismissed*, No. 88-5252 ND (8th Cir. May 5, 1989). *See also In re* Jarrett Ranches, Inc., 107 Bankr. 969, 975-76 (Bankr. D.S.D. 1989) (invalidating the particular bidding process used by a FCB under the right of first refusal).

425. Payne v. Federal Land Bank of Columbia, 711 F. Supp. 851, 859-60 (W.D.N.C. 1989) (holding that auction sales need not be preceded by opportunity to buy land at appraisal value).

426. 12 U.S.C.A. § 2219a(h) (West 1989). *See generally* Houser, *A Comparative Study of the Former Owner's Right of First Refusal Upon a Lender's Resale of Foreclosed Agricultural Land: A New Form of State Mortgagor Relief Legislation*, 13 J. CORP. L. 895 (1988) (discussing statutory rights of first refusal).

427. Agricultural Credit Act of 1987, Pub. L. No. 100-233, 503, 101 Stat. 1663 (1988). Unlike other provisions of the 1987 Act relating to the Farm Credit System, this provision was codified in Title 7 of the United States Code, not Title 12, at 7 U.S.C.A. § 5103(b)(1) (West 1988). *See generally* Note, *Mediation in Debtor-Creditor Relationships*, 20 U. MICH. J. L. REF. 110 (1987) (discussing debtor-creditor mediation); Note, *The American Response to Farm Crises: Procedural Debtor Relief*, 1988 U. ILL. L. REV. 1037 (discussing various farm debtor relief measures).

428. 12 U.S.C.A. § 2202e (West 1989).

regarding System lender's participation in mediation.[429]

I. DIFFERENTIAL INTEREST RATES

Farm Credit System institutions in the past have used different interest rates on loans. This is commonly known as the "three-tier" method. The interest rate was based on a number of factors, including borrower qualifications. The 1987 Act allows the System institutions to continue this practice.[430] However, the borrower can now ask a System institution:

1) to provide a review of the loan to determine if the proper interest rate has been used;
2) give the borrower a written explanation of the basis for charging the interest rate used; and
3) give the borrower a written explanation of what the borrower must do to improve his credit status to receive a lower interest rate.[431]

J. UNINSURED ACCOUNTS

Some System institutions have used uninsured accounts in the past as part of their loan servicing procedures.[432] Borrowers would deposit funds in these accounts over a period of time in order to insure that they would meet their scheduled payments. The 1987 Act provided that if the institution becomes insolvent, all of the funds in uninsured accounts are to be applied to a borrower's debt.[433]

K. USE OF FMHA GUARANTEED LOANS, ETC.

The 1987 Act also expresses Congress' desire for the Farm Credit System to look outside the System in restructuring:

> It is the sense of Congress that the banks and associations (except for the banks for cooperatives) operating under the Farm Credit Act of 1971, should administer distressed loans to farmers with the objective of using the

429. The rules regarding System lenders' participation in mediation are found at 12 C.F.R. § 614.4521 (1990).

430. Agricultural Credit Act of 1987, Pub. L. No. 100-233, 109, 101 Stat. 1584 (1988) (codified at 12 U.S.C.A. § 2199(b) (West 1989).

431. 12 U.S.C.A. § 2199(b) (West 1989). *See also* 12 C.F.R. § 614.4368 (1990) (same requirement).

432. 12 C.F.R. § 614.4510 (1988) (currently found at 12 C.F.R. § 614.4513(b) (1990)).

433. 12 U.S.C.A. § 2219b (West 1989). *See also* 12 C.F.R. § 614.4513(a) (1990) (same requirement).

> loan guarantee programs of the Farmers Home Administration and other loan restructuring measures, including participation in interest rate buy down programs that are Federally or State funded or other Federal or State sponsored financial assistance programs that offer relief to financially distressed farmers, as alternatives to foreclosure, considering the availability and appropriateness of such programs on a case-by-case basis.[434]

While this section has not been codified, it may prove helpful to the borrower who wishes to use the FmHA guaranteed loan program or other program in order to qualify for restructuring.

VIII. JUDICIAL REVIEW OF RESTRUCTURING DENIALS

At least one court has declined to review decisions adverse to the borrower under the former forbearance policies developed by System institutions. In Federal Land Bank of Wichita v. Read,[435] the borrower's request for forbearance under the FLB's forbearance policy adopted pursuant to pre-1985 Act forbearance regulation[436] had been denied.[437] The policy conditioned forbearance on the borrower meeting three conditions: the borrower must be cooperative; the borrower must make an honest effort to meet the conditions of the loan contract; and the borrower must be capable of working out the debt burden.[438] The FLB found that the borrower did not satisfy the third condition.[439] In declining to review the forbearance decision, the court expressed the belief that the "matter is best left to those in whom the land bank places that responsibility. . . . We find no statutory authority for court review of such a determination."[440]

For similar reasons, a federal district court recently declined

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434. Agricultural Credit Act of 1987, Pub. L. No. 100-233, 102, 101 Stat. 1579 (1988). For a description of the FmHA guaranteed loan program, see Scott & Roth, *Guaranteed Farmer Program Loans: Questions and Answers*, FARMERS' LEGAL ACTION GROUP REP. 1 (Winter 1989).

435. 703 P.2d 777 (Kan. 1985).

436. *See* 12 C.F.R. § 614.4510 (1985).

437. Federal Land Bank of Wichita v. Read, 703 P.2d 777 (Kan. 1985).

438. *Id.* at 780. *See* 12 C.F.R. § 614.4510(1) (1985).

439. Federal Land Bank of Wichita v. Read, 703 P.2d at 779.

440. *Id.* at 780. *See also* Woodsmall v. Lyng, 816 F.2d 1241, 1245 (8th Cir. 1987) (denial of Farmers Home Administration (FmHA) loan on the grounds that the applicant was not creditworthy was not reviewable because the federal courts "are not equipped to undertake such a task, for in these matters we have neither the training nor the experience of an FmHA loan officer"); Tuepker v. Farmers Home Admin., 708 F.2d 1329, 1332 (8th Cir. 1983) (declining to review a Farmers Home Administration loan denial in the absence of a claim "alleging a substantial departure from important procedural rights, a misconstruction of governing legislation, or some like error 'going to the heart of the administrative determination' ").

to review the "quality and good faith" of an FLB's decision not to restructure a borrower's loan under the 1987 Act.[441] The court expressed the view that "though courts will enforce consideration of loan restructuring under the Act, they probably will not scrutinize the details of loan decisions when FLB has considered applications for restructure and reviewed denial."[442]

However, despite the absence of express statutory authority for judicial review under the Farm Credit Act and the regulations and policies adopted pursuant to it, there are several potential theoretical bases for seeking judicial review. Listed in order of their current state of judicial development, the respective basis for each of those theories are as follows:

1. invocation of the maxim "he who seeks equity, must do equity" as an equitable affirmative defense to the institution's foreclosure proceeding;
2. failure to follow statutory directives asserted as an implied cause of action under the Farm Credit Act, as amended by the Agricultural Credit Act of 1987;[443] and
3. failure to adhere to state cooperative law requiring procedural and substantive fairness in the expulsion of members from cooperative institutions.

The latter two theories are discussed elsewhere in this article.[444] The following is a discussion of the first theory, the equitable defense.

In most, if not all jurisdictions, a proceeding to foreclose a mortgage is a proceeding in equity.[445] One of the fundamental

441. Troutman v. Federal Land Bank of Spokane, No. CV88-726-PA, Slip. op. at 4 (D. Ore. Sept. 15, 1988) (order denying preliminary injunction).

442. *Id.* at 3 (citing Miller v. Federal Land Bank of Spokane, 587 F.2d 415 (9th Cir. 1978), *cert. denied*, 441 U.S. 962 (1979)). *See also* Williams v. Federal Land Bank of Jackson, 729 F. Supp. 1387, 1390 (D.D.C. 1990) (". . . once a federal land bank has properly determined whether or not a particular borrower's offer of debt refinancing should be accepted, this Court will not second-guess that determination." (citing Perez v. Jefferson Standard Life Ins. Co., 781 F.2d 475, 479-80 (5th Cir. 1986); Federal Land Bank of Wichita v. Read, 237 Kan. 751, 703 P.2d 777, 780 (1985)).

443. This basis is unavailable in the Ninth, Tenth, and Eighth Circuits. *See* Harper v. Federal Land Bank of Spokane, 878 F.2d 1172, 1177 (9th Cir. 1989), *cert denied*, 110 S. Ct. 867 (1990); Griffin v. Federal Land Bank of Wichita, 902 F.2d 22, 24 (10th Cir. 1990); Zajac v. Federal Land Bank of St. Paul, No. 88-5353ND (8th Cir. July 31, 1990) (*en banc*) (1990 U.S. App. LEXIS 12932). Given the trend represented by these decisions, review through an implied cause of action is not likely to be available in any jurisdiction.

444. *See supra* notes 184-267 & 333-38, respectively, and the accompanying text.

445. *See, e.g.*, Federal Land Bank of St. Paul v. Bosch, 432 N.W.2d 855, 858 (N.D. 1988) ("An action to foreclose a mortgage is an equitable proceeding"); Continental Federal Savings and Loan Ass'n v. Fetter, 564 P.2d 1013, 1019 (Okla. 1977) ("Foreclosure of a real estate mortgage is an equitable action, and it is within the province of the court exercising

precepts of equitable relief is that it "cannot be demanded as a matter of right whenever specified facts are shown . . .," rather it "is granted in the discretion of the court."[446] Judicial discretion is ". . . to be exercised by applying established principle of equity to the situation presented by all of the facts in the case, and adapting the remedy to accomplish the most equitable result possible."[447]

The discretionary nature of equitable relief is "rooted in the historical concept of [a] court of equity as a vehicle for affirmatively enforcing the requirements of conscience and good faith."[448] As emphasized by the United States Supreme Court:

> A court of equity acts only when and as conscience commands, and if the conduct of the plaintiff be offensive to the dictates of natural justice, then, whatever may be the rights he possesses and whatever use he may make of them in a court of law, he will be held remediless in a court of equity.[449]

The discretion inherent in the granting or denial of equitable relief is guided by maxims or general principles.[450] One of those maxims is "he who seeks equity must do equity." As explained by Pomeroy, "this maxim expressed the governing principles that every action of a court of equity in determining rights and awarding remedies must be in accordance with conscience and good faith."[451] More specifically,

> The meaning is, that whatever be the nature of the controversy between two definite parties, and whatever be the nature of the remedy demanded, the court will not confer its equitable relief upon the party seeking its interposition and aid, unless he has acknowledged and conceded or will admit and provide for all the equitable rights, claims, and demands justly belonging to the adversary party, and growing out of or necessarily involved in

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its equitable power to see that the party seeking equity shall have dealt fairly before relief is given." (quoting Murphy v. Fox, 278 P.2d 820, 826 (Okla. 1955)).

446. H. MCCLINTOCK, PRINCIPLES OF EQUITY 49 (2nd ed. 1948).

447. *Id.*

448. Precision Instrument Mfg. Co. v. Automotive Maintenance Mach. Co., 324 U.S. 806, 814 (1945) (holding that dismissal of a patent infringement suit was justified by the "unclean hands" doctrine).

449. Deweese v. Reinhard, 165 U.S. 386, 390 (1897) (stating that land dispute relief was available at an action of law).

450. *See Precision Instrument*, 324 U.S. at 814 (1945) ("The guiding doctrine . . . that he who comes into equity must come with clean hands . . . is far more than a mere banality. It is a self-imposed ordinance that closes the doors of a court of equity to one tainted with inequitableness or bad faith relative to the matter in which he seeks relief . . .").

451. J. POMEROY, EQUITY JURISPRUDENCE 51 (5th ed. 1941).

the subject-matter of the controversy.[452]

The principle requires the plaintiff to do "equity."[453] In essence, a condition precedent to the equity court's granting of relief to the plaintiff is the awarding to the defendant any rights possessed by the defendant, including those that have their genesis in the principles of fair dealing.

The failure of the FLB to consider a borrower for forbearance was held to be a defense to a foreclosure action in the case of Federal Land Bank of St. Paul v. Overboe.[454] In *Overboe*, the borrower obtained a loan from the Federal Land Bank of St. Paul which was secured by a mortgage.[455] The borrower became late in his payments, and in June, 1983, he requested that his annual payment date be changed from July 1 to December 31 of each year to coincide with the cash flow of his farm.[456] The federal land bank advised the borrower that a change in payment dates would require a reamortization of his loan, and that, based on the borrower's financial information on file, it was unable to grant a reamortization.[457] The borrower subsequently provided new financial information but the federal land bank declined to change its position and initiated a foreclosure action.[458]

The borrower contested the foreclosure action on the grounds that the federal land bank had failed to follow its policies, regulations, and procedures adopted under the Farm Credit Act of 1971 relating to forbearance when it denied his request for reamortization.[459] The federal land bank responded by asserting that its failure to follow its policies and the regulations governing it could not be raised as a defense to foreclosure, and, in the alternative, that it had not violated its policies and the applicable regulations.[460]

The forbearance regulation at issue in *Overboe* was adopted prior to the enactment of the Farm Credit Amendments Act of 1985.[461] The regulation provided that the federal land bank was

452. *Id.*
453. *Id.*
454. 404 N.W.2d 445 (N.D. 1987).
455. Federal Land Bank v. Overboe, 404 N.W.2d 445, 446 (N.D. 1987).
456. *Id.*
457. *Id.*
458. *Id.*
459. *Id.* at 447.
460. *Id.*
461. 12 C.F.R. § 614.4510(d)(1) (1986). The *Overboe* equitable defense was applied to a claim arising under the 1985 Act in Federal Land Bank of St. Paul v. Bosch, 432 N.W.2d 855, 858-59 (N.D. 1988). *See also* Federal Land Bank of St. Paul v. Asbridge, 414 N.W.2d 596, 597 (N.D. 1987) (applying *Overboe*); Farm Credit Bank of St. Paul v. Huether, 454 N.W.2d 710, 715 (N.D. 1990) (applying *Overboe*).

to develop loan servicing policies that included a provision for "a means of forbearance for cases when the borrower is cooperative, making an honest effort to meet the conditions of the loan contract, and is capable of working out of the debt burden."[462] Pursuant to that regulation, the federal land bank had adopted a policy authorizing the extension of "appropriate assistance" to borrowers who met certain criteria.[463]

The federal land bank argued that its failure to follow the policy that it adopted pursuant to the forbearance regulation could not be asserted as a defense because of the holding of several courts that borrowers do not have a private cause of action for damages under the Farm Credit Act of 1971 or the regulations promulgated pursuant to that Act.[464]

Although the *Overboe* court acknowledged that the Farm Credit Act of 1971 and the forbearance regulation did not create a private cause of action, it rejected the federal land bank's argument that the absence of a private cause of action precluded a borrower's assertion of noncompliance with the Act or the regulation as a defense in a foreclosure action.[465] The *Overboe* court's analysis of the issue was grounded on the recognition that "an action to foreclose a mortgage is an equitable proceeding."[466] With this recognition forming the basis of the court's analysis, the court then examined other instances, specifically, cases involving noncompliance with Department of Housing and Urban Development regulations, where federal regulations which have been held not to imply a private cause of action may nevertheless provide a basis for an equitable defense to a foreclosure action.[467]

The *Overboe* court examined the notions of fair dealing applicable to the Farm Credit System, and noted that the Congressional goal under the Farm Credit Act was "fostering agricultural development."[468] With that Congressional objective in mind, the Supreme Court of North Dakota held as follows:

> Allowing FLB to foreclose its mortgages without regard to the administrative forbearance regulation would be inimical to the achievement of this goal. We therefore

462. *Overboe*, 404 N.W.2d at 447 (citing 12 C.F.R. § 614.4510(d)(1)).
463. *Id.* at 447 (citing "District Policy 2501" of the Federal Land Bank of St. Paul).
464. *Id.* at 447-48. *See, e.g.*, Farmers Production Credit Ass'n of Ashland v. Johnson, 24 Ohio St.3d 69, 493 N.E.2d 946 (1986), *cert. denied*, 479 U.S. 1032 (1987).
465. *Overboe*, 404 N.W.2d at 449.
466. *Id.* at 448 (citations omitted).
467. *Id.* at 449.
468. *Id.* (citing Federal Land Bank of St. Paul v. Lillehaugen, 404 N.W.2d 452 (N.D. 1987)).

> conclude that the failure of FLB to comply with administrative forbearance regulation and policies adopted pursuant to the regulation gives rise to a valid equitable defense to a foreclosure action under state law.[469]

Having held that a federal land bank's failure to abide by its forbearance policies and the regulations governing it was a permissible affirmative defense to a foreclosure action, the *Overboe* court also concluded that the administrative forbearance defense permits judicial consideration of both the procedural and substantive aspects of the System institution's action.[470] In this regard, the court stated that the initial inquiry is whether the institution "has established a general policy of forbearance and whether it applied that policy in arriving at its decision to seek foreclosure."[471]

The *Overboe* court explained that if the trial court finds that the borrower's qualifications were considered by the institution in accordance with its procedures, the court's review of the merits of that consideration is to be confined to whether the institution abused its discretion.[472] In other words, to prevail, the borrower must show that the institution acted in an "arbitrary, capricious, unreasonable or unconscionable manner."[473] Finally, the *Overboe* court indicated that appellate review of a trial court's determination of the substantive issue will be guided by the standard of whether the abuse of discretion standard of review "appears to have been misapprehended or grossly misapplied."[474]

Litigation by member-borrowers against System institutions will undoubtedly continue. The current interest in lender liability in the farm community suggests that some of that litigation will take the form of "generic" lender liability claims.[475] However, a number of issues concerning the borrowers' rights provisions of the Agricultural Credit Act of 1987 remain unresolved.

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469. *Id.*

470. *Id.* at 449-50.

471. *Id.* at 449.

472. *Id.* at 450.

473. *Id.*

474. *Id.* (citing Universal Camera Corp. v. National Labor Relations Board, 340 U.S. 474, 491 (1951)). In jurisdictions providing for nonjudicial foreclosure, borrowers seeking to invoke the equitable defense employed in *Overboe* will have to seek injunctive relief in order to obtain judicial intervention. For a recent discussion and collection of authorities regarding the enjoining of the nonjudicial foreclosure process, see Note, *Nonjudicial Foreclosure in Arkansas with the Statutory Foreclosure Act of 1987*, 41 ARK. L. REV. 373, 389-403 (1988).

475. *See* Welsh, *Are Banks to Blame?*, FARM J., June-July 1988, at 11.

IX. CONCLUSION

Two specific and fundamental issues relating to the new borrowers' rights provisions are in need of immediate attention. A third, more general, issue is not likely to arise until the secondary agricultural mortgage market is implemented.

The first issue arises from the failure of most, if not all, of the farm credit districts to adopt loan restructuring policies that require the institutions within the district to explain in simple, understandable terms the computational steps involved in the determination of the cost of foreclosure and the cost of restructuring. That information, which has been made available to loan officers, is not routinely provided to borrowers holding distressed loans.[476] Without that information, the borrower is faced with the extraordinarily difficult task of gleaning the computational steps and arriving at an understanding of the restructuring formula from language in current policies that merely restates the language of the statute. Because the statutory language is not so specific as to make the computational steps self-evident, the practical effect is that the borrower "shoots in the dark" when submitting a restructuring application. Moreover, without knowledge of the computational steps involved, the borrower is not in a position to identify and urge the correction of computational errors made at either the initial stage of the review of his application or at the credit review committee level. As a matter of fundamental fairness, both parties to the restructuring process should have the instructions before them.

The second issue arises from the failure of most institutions to disclose or justify their "costs of foreclosure." That information is readily accessible to the institutions, but it is completely inaccessible to members unless the institution chooses to make it available.[477] Although member-borrowers are required to make a full disclosure of their current and projected financial and operational conditions when they apply for restructuring, institutions have routinely chosen not to disclose their costs. Thus, a member-borrower without that information cannot submit a restructuring proposal that will properly address each cost and other factors that will be considered by the institution in evaluating that application.

If one accepts that premise that restructuring is intended to

476. *See supra* notes 386-91 and the accompanying text.

477. For a discussion of the availability of information regarding the costs of foreclosure, *see supra* notes 386-91 and the accompanying text.

produce "win-win" results, the failure of System institutions to make the process accessible to its members by providing them with adequate instructions and to disclose and justify their anticipated costs of foreclosure is inexcusable. Moreover, if System institutions are under either an equitable or legal duty to be fair, that failure may be actionable. As discussed elsewhere in this article, ample authority exists to impose enforceable duties of good faith and fairness on System institutions in the restructuring process.[478]

The final, and less immediate, issue arises from sections 2279 aa-9(a) and (b) of the Farm Credit Act, as amended in 1987.[479] Those provisions, concerning loans from System institutions that may be pooled in the secondary market for farm mortgages, a market that is being created pursuant to sections 2279aa—2279aa-14,[480] provide as follows:

> (a) Restructuring
>
> Notwithstanding any other provision of law, sections 2202, 2202a, 2202b, 2202c, and 2219b of this title shall not apply to any loan included in a pool of qualified loans backing securities or obligations for which the Corporation provides guarantee. The loan servicing standards established by the Corporation shall be patterned after similar standards adopted by other federally sponsored secondary market facilities.
>
> (b) Borrowers rights
>
> At the time of application for a loan, originators that are Farm Credit System institutions shall give written notice to each applicant of the terms and conditions of the loan, setting forth separately terms and conditions for pooled loans and loans that are not pooled. This notice shall include a statement, if applicable, that the loan may be pooled and that, if pooled, sections 2202, 2202a, 2202b, 2202c, and 2219b of this title shall not apply. This notice also shall inform the applicant that he or she has the right not to have the loan pooled. Within 3 days from the time of commitment, an applicant has the right to refuse to allow the loan to be pooled, thereby retaining rights under sections 2202, 2202a, 2202b, 2202c, and 2219b of

478. *See generally* Federal Land Bank of St. Paul v. Overboe, 404 N.W.2d 445 (N.D. 1987) (applying equitable principles); Copeland, *Expulsion of Members by Agricultural Cooperatives*, 1 J. AGRIC. COOPERATION 76 (1986) (discussing the law governing the expulsion of members from agricultural cooperatives).

479. 12 U.S.C.A. § 2279aa-9 (a), (b) (West 1989).

480. 12 U.S.C.A. §§ 2279aa—2279aa-14 (West 1989).

this title, if applicable.[481]

It remains to be seen whether System institutions will attempt to pool significant numbers of loans and thus avoid the administrative expenses created by the restructuring provisions and whether borrowers will be "encouraged" to waive their rights in order to allow the pooling of loans.[482] The primary goal of farm credit system loan restructuring is to gain lender acceptance of a restructuring proposal that the borrower can actually perform. However, such a proposal may be denied, and judicial review may be sought. To prepare for this, documentation of any procedural irregularities or other arbitrary and capricious lender behavior is essential. But borrowers and their counsel must be aware that judicial intervention in the restructuring program is likely to be limited or even nonexistent. Thus, a realistic restructuring of a farm credit loan that is acceptable to the Farm Credit lender must be the paramount aim of the borrowers and counsel.

481. 12 U.S.C.A. § 2279aa-9(a), (b) (West 1989).

482. An overriding issue for the future, one beyond the scope of this article, is the availability of credit and the Farm Credit System's role in providing that credit. For recent discussions of those issues, see Boehlje and Pederson, *Farm Finance: The New Issues*, CHOICES, Third Quarter, 1988, at 16; Thompson, *The Farm Credit System: Rebuilding After the Big Debt Crisis*, AGRIFINANCE, Sept. 1990, at 30; Maio, *Think About It! Duncan Worries About Farm Credit System's Future*, ABA Bankers Weekly, Sept. 18, 1990 at 8; Duncan, *Rural Credit Markets: More Changes Ahead*, CHOICES, Third Quarter 1988, at 20; *Lessons From a System That Didn't Go Under*, WASH. POST NAT. WEEKLY ED., June 26-July 2, 1989, at 18, col.1.

APPENDIX A

THOUGHTS, COMMENTS AND A ROUGH CHECKLIST ON FARM CREDIT SYSTEM LOAN RESTRUCTURING FROM THE BORROWER'S PERSPECTIVE

I. GOALS:

A. Primary: Lender acceptance of a restructuring proposal that the borrower can perform. Unrealistic borrower cash flows may gain lender acceptance, but inability to perform may preclude subsequent loan restructuring.

B. Secondary: Because judicial review of a restructuring denial ultimately may be sought, documentation of any procedural irregularities or other arbitrary and capricious behavior on the part of the lender should be a continuing consideration throughout the process.[483] However, borrowers and their counsel should be mindful that judicial intervention in the restructuring process is likely to be very limited and, in some circumstances and jurisdictions, nonexistent.[484]

II. ELIGIBILITY FOR RESTRUCTURING

A. Definition of distressed loan:

The term of "distressed loan" means a loan that the borrower does not have the financial capacity to pay according to its terms and that exhibits one or more of the following characteristics:

A. The borrower is demonstrating adverse financial and repayment trends.
B. The loan is delinquent or past due under the terms of the loan contract.

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483. *See* Federal Land Bank of St. Paul v. Overboe, 404 N.W.2d 445 (N.D. 1987).

484. *See, e.g.*, Harper v. Federal Land Bank of Spokane, 878 F.2d 1172, 1177 (9th Cir. 1989), *cert. denied*, 110 S. Ct. 867 (1990) (no implied cause of action to enforce borrowers' rights under the 1987 Act); Griffin v. Federal Land Bank of Wichita, 902 F.2d 22, 24 (10th Cir. 1990) (same); Zajac v. Federal Land Bank of St. Paul, No. 88-5353ND (8th Cir. July 31, 1990) (1990 U.S. App. LEXIS 12932) (same); Williams v. Federal Land Bank of Jackson, 729 F. Supp. 1387, 1390 (D.D.C. 1990). "[O]nce a federal land bank has properly determined whether or not a particular borrower's offer of debt refinancing should be accepted, this Court will not second-guess that determination. . . . *Williams*, 729 F. Supp. at 1390 (citations omitted); Troutman v. Federal Land Bank of Spokane, No. CV88-726-PA, slip op. at 4 (D. Or. Sept. 15, 1988) (order denying preliminary injunction) (declining to review the "quality and good faith" of FLB in denying restructuring); Kramer v. Federal Land Bank of St. Paul, No. Civ. 3-88-297 (D. Minn. Sept. 16, 1988) (order denying preliminary injunction) (finding, *inter alia*, that foreclosure does not present irreparable harm in view of state redemption and first refusal rights). *See also* Woodsmall v. Lyng, 816 F.2d 1241, 1245 (8th Cir. 1987) (denial of FMHA loan on the grounds that the applicant was not creditworthy was not reviewable because the federal courts "are bit equipped to undertake such a task, for in these matters we have neither the training nor the experience of a Farmers Home Administration loan officer"); Tuepker v. Farmers Home Admin., 708 F.2d 1329, 1332 (9th Cir. 1983) (declining to review an FmHA loan denial in the absence of a claim "alleging a substantial departure from important procedural rights, a misconstruction of governing legislation, or some like error going to the heart of the administrative determination").

C. One or both of the factors listed in subparagraph (A) and (B), together with inadequate collateralization, present a high probability of loss to the lender.[485]

The regulations provide that the lender has discretion in determining if the borrower has the financial capacity to repay the loan.[486]

B. What does a borrower do when he believes that his loan is a "distressed loan" eligible for consideration for restructuring, but the lender disagrees?

1. Creating a monetary default to "get the attention" of the lender is rarely, if ever, advisable. The lender may deem the default "voluntary" and continue to maintain that the loan is not distressed. Moreover, a "voluntary default" may result in the borrower being ineligible for the right of first refusal. "Previous owner," for purposes of the right of first refusal, is limited to prior record owners who "did not have the financial resources, as determined by the institution, to avoid foreclosure. . . ."[487]

2. A better alternative would be to prepare a cash flow that both illustrates that the borrower faces the prospect of being unable to pay the original loan according to the terms and also demonstrates that the borrower could repay a restructured note that would meet the criteria for mandatory loan restructuring. The lender may be more willing to consider a distressed loan if the borrower also presents to the lender an acceptable restructuring proposal with the request for a determination that the loan is distressed.

C. What does a borrower do if he has created a "voluntary default" and now desires to backtrack to avoid a foreclosure without the opportunity to be considered for restructuring? The best alternative may be to cure the default. Lenders may not enforce acceleration for monetary default "after a borrower has made all accrued payments of principal, interest, and penalties. . . ."[488]

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485. 12 U.S.C.A. § 2202a(a)(3) (West 1989).
486. 12 C.F.R. § 614.4522(a)(2) (1990).
487. 12 C.F.R. § 614.4522(a)(2) (1990).
488. 12 U.S.C.A. § 2202d(c)(West 1989); 12 C.F.R. § 614.4514(c) (1990). In most instances, when a loan is accelerated, the loan accrues interest based on the accelerated principal. An unresolved issue is whether the borrower desiring to "de-accelerate" the loan must pay the interest on the accelerated principal or only the interest that had accrued irrespective of the accelerated principal. The Act's legislative history is ambiguous. The House bill, H.R. 3030, provided that the interest was to be computed "without regard to

D. Is a borrower who has converted collateral eligible for restructuring?

1. Conversion of System lender's collateral is a federal criminal offense.[489]

2. Conversion may prevent the borrower from avoiding acceleration by paying all accrued principal, interest, and penalties.[490]

3. Conversion or the dissipation, destruction, or deterioration of the collateral may also excuse the lender from having to provide the 45 day notice of the availability of restructuring prior to commencing foreclosure proceedings.[491] However, even though the 45 day notice is excused, the loan theoretically is still eligible for restructuring if it is a distressed loan.[492] As a practical matter, a conversion will probably provide a sufficient basis to deny restructuring, and the prior replevin or foreclosure of the collateral will have substantially impaired the borrower's ability to "cash flow" a restructured loan. The availability of restructuring may have practical significance only if the borrower can somehow excuse the loss or deterioration of the collateral and can file for bankruptcy relief prior to the replevying or foreclosure seizure. Of course, in such a case, the failure to excuse the conversion may result in the debt not being discharged.[493]

E. If the lender began foreclosure proceedings but did not complete those proceedings (according to state law) prior to January 6, 1988, the effective date of the Agricultural Credit Act of 1987, the loan is still eligible for restructuring.[494]

F. So long as a reorganization plan has not been confirmed, a borrower in bankruptcy appears to be eligible for consideration for restructuring.[495]

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acceleration." The Senate amendment did not contain a comparable provisions, and the Conference report adopted the House provision, but deleted the language "without regard to acceleration." HOUSE CONF. REP. NO. 100-490, 100th Cong., 1st Sess. 175, *reprinted in* 1987 U.S. CODE CONG. & ADMIN. NEWS 2956, 2970.

489. 18 U.S.C.A. § 658 (West 1976).

490. 12 C.F.R. § 614.4514 (1990).

491. 12 U.S.C.A. § 2202a(j) (West 1989); 12 C.F.R. § 614.4519 (1990).

492. 12 U.S.C.A. § 2202a(b)(1) (West 1989).

493. 11 U.S.C.A. § 523(a)(4) (West 1979).

494. *See* 53 Fed. Reg. 35,427, 35,428 (1988). *See also* Griffin v. Federal Land Bank of Wichita, 708 F. Supp. 313, 317 (D. Kan. 1989), *aff'd*, 902 F.2d 22 (10th Cir. 1990); Federal Land Bank of Omaha v. Engleken, No. C85-2062 (N.D. Iowa Aug. 25, 1988); Federal Land Bank of St. Louis v. Cupples Bros., 889 F.2d 764 (8th Cir. 1989).

495. *E.g.*, In the Matter of Dilsaver, 86 Bankr. 1010 (Bankr. D. Neb. 1988); Stainback v.

III. APPLYING FOR RESTRUCTURING:

A. Notification by a lender to the borrower of eligibility for loan restructuring consideration:

1. When lender determines loan is distressed;[496] or

2. 45 days prior to the commencement of foreclosure proceedings.[497]

B. Suit on the note or debt instrument is probably not a foreclosure proceeding.[498]

C. Notification must include a copy of the district restructuring policy and all material necessary to enable the borrower to submit an application.[499]

D. What should the borrower do upon receipt of the notification?

1. Immediately assemble financial records and obtain expert assistance in developing and exploring cash flow potentials and possibilities. If necessary, explore farm reorganization alternatives. Good cash flow projections take time to prepare. The borrower's financial data, including cash flow alternatives, will be the most significant information under consideration in most cases.

2. Consider requesting additional information from the lender, including the following:

(a) the computational formula that the lender will use to determine and compare cost of foreclosure with the cost of restructuring;

(b) the known costs of foreclosure, i.e., attorney's fees, disposition costs, etc.; and

(c) the appraised value of the collateral.

3. If the request is not answered, send another request bearing in mind the secondary goal listed under the first heading, "Goals," above. Stress that restructuring is designed to produce a "win-win" result, requiring good faith and full disclosure by both lender and bor-

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Federal Land Bank of Jackson, No. GC 88-25-NB-O (N.D. Miss. Feb. 5, 1988) (order granting preliminary injunction); *In re* Kraus, No. BK 86-2677 (Bankr. D. Neb. May 20, 1988); *In re* James Desmond Woods, Jr., No. 88-BK-01659-M11 (W.D. La. March 16, 1989) (interim order in adversary proceeding).

496. 12 U.S.C.A. § 2202a(b)(1) (West 1989); 12 C.F.R. 614.4516 (1990).

497. 12 U.S.C.A. § 2202a(b)(2) (West 1989); 12 C.F.R. § 614.4518) (1990).

498. 12 U.S.C.A. § 2202a(4) (West 1989); 12 C.F.R. § 614.4512(e)(1), (2) (1990).

499. 12 U.S.C.A. § 2202a(b)(1) (West 1989); 12 C.F.R. § 614.4516(a) (1990).

rower.[500] Restructuring is not a poker game — it involves a major business decision by both parties, each having legally enforceable duties to the other. In that regard, not all of the lender's duties arise from the Farm Credit Act, state cooperative law may impose overlapping and additional duties of good faith and full disclosure.[501]

4. Remember that all expenses and income considered in the cost of foreclosure and cost of restructuring are present-valued. Knowledge of the lender's discount rate is essential. Borrowers must be aware that in most districts the proposed restructured note will be discounted to reflect its present value.

5. Borrowers should also consider applying for a lower interest rate during the 45 day period.[502] The required written response by the lender may identify problem areas with the loan that can be addressed in the restructuring proposal.

6. Consider meeting with the loan officer before submitting the restructuring proposal.[503] Document all requests for information, responses, and other discussions at such a meeting.

7. Consider using any available mediation proceedings to obtain information from the lender. A provision of the 1987 Act, 504 requires that FCS lenders:

> (a) "present and explore debt restructuring proposals advanced in the course of such mediation" and
>
> (b) "cooperate in good faith with requests for information or analysis of information made in the course of mediation. . . ."[504]

8. Remember to provide all the information requested by the lender in submitting the borrower's applications for restructuring. This may include balance sheets, income tax returns, projected cash flow, production records, etc.

9. The application must be accompanied by a propo-

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500. *See* 53 Fed. Reg. 35,427, 35,433 (1988) ("A reading of the statute and regulation, [sic] indicates that both parties must put forth a good faith effort and work together").

501. *See, e.g.*, Snyder v. Colwell Cooperative Grain Exchange, 231 Iowa 1210, 1213, 3 N.W.2d 507, 509 (1942) (officers of a corporative have a duty of full and fair disclosure to members).

502. *See* 12 U.S.C.A. § 2199(b) (West 1989); 12 C.F.R. § 614.4368 (1990).

503. 12 U.S.C.A. § 2202a(c) (West 1989); 12 C.F.R. § 614.4516(b) (1990).

504. 7 U.S.C.A. § 5103 (West 1988).

sal for the restructuring of the loan.[505]

10. Consider "packaging" the application and plan in "brochure" from or as an extended letter beginning with a discussion of the background of the borrower, the nature of the borrower's farming operation, and the reasons for the default. Then, discuss in detail the proposed plan and justify it with specific references to the projected cash flow. Also an analysis of the cost of foreclosure and the cost of restructuring, including the necessary computations. Do not assume that there will be considerable negotiations. Put the best plan the borrower can propose on the table. The lender has a right to the "[l]east cost alternative,"[506] and the borrower may not be well served by a proposal that does not reflect that the borrower "is applying all income over and above necessary and reasonable living and operating expenses to the payment of primary obligations."[507] Remember that the burden of justifying restructuring is ultimately borne by the borrower.

IV. CREDIT REVIEW COMMITTEE PROCEEDINGS:

A. The borrower must receive prompt written notice of denial and the reasons for the denial.[508]

B. Insist on lender disclosure of all "critical assumptions and relevant information" (whatever that means) prior to the credit review committee meeting.[509]

C. Remember that the review process is just that, a review; most credit review committees will not consider new proposals at the committee meeting.[510]

D. The loan officer who made the initial denial of the restructuring proposal may participate in the review meeting by providing information and answering questions, but he may not vote or participate in the committee's deliberations.[511]

E. Borrowers may obtain "independent" appraisals of

505. 12 C.F.R. § 614.4521(a), (b) (1990).

506. Federal Land Bank of Omaha v. Christensen, No. 22641 (Buena Vista Co. Dist. Ct., Iowa, July 6, 1988) (order granting plaintiff's motion for summary judgment on the grounds that an application for restructuring unaccompanied by a plan was fatally defective).

507. 12 U.S.C.A. § 2202a(f) (West 1989); 12 C.F.R. § 614.4517(b) (1990).

508. 12 U.S.C.A. § 2202a(d)(1)(B) (West 1989); 12 C.F.R. § 614.4517(a)(2) (1990).

509. 12 U.S.C.A. § 2201(b) (West 1989); 12 C.F.R. § 614.4518 (1990).

510. 53 Fed. Reg. 35,427, 35,444 (1988) (prefatory comments to the regulations).

511. 53 Fed. Reg. 35,427, 35,426 (1988) (prefatory comments to the regulations).

collateral.[512]

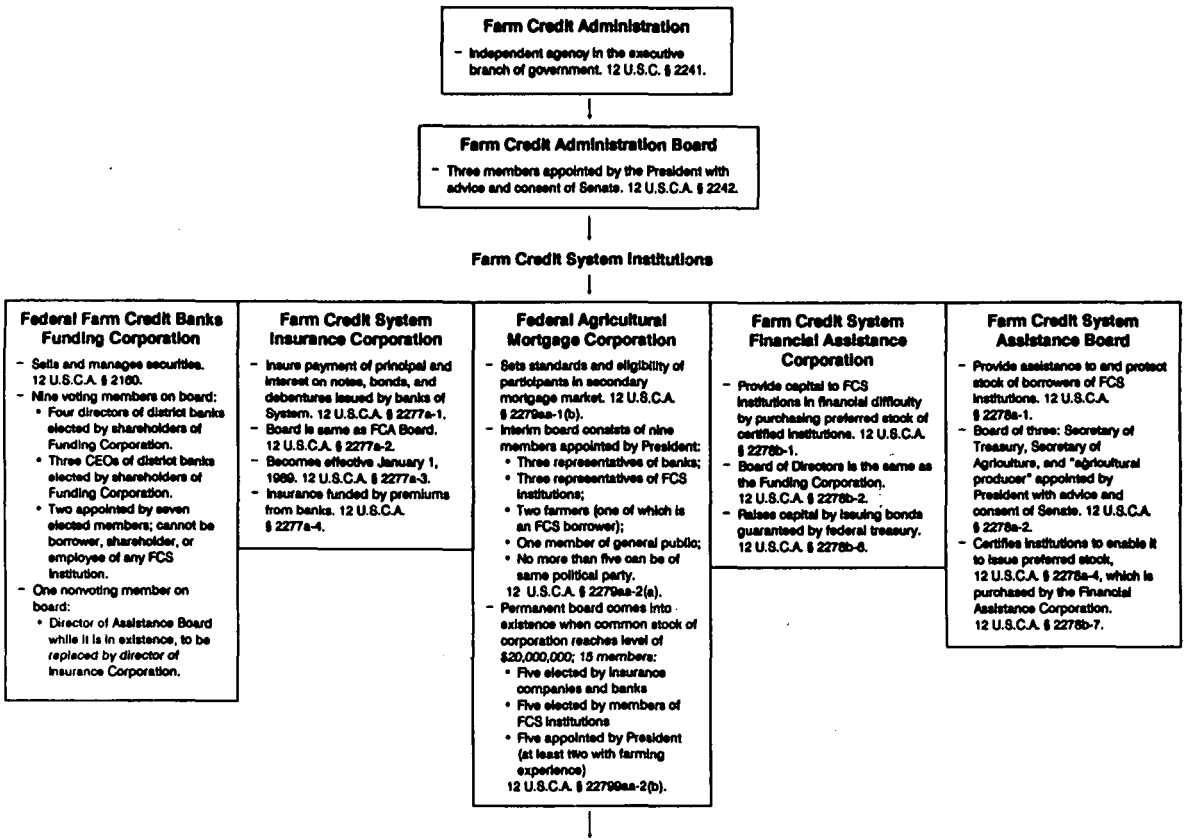
F. The board member serving on the committee must be a member of the board of the lender having ultimate authority over the loan.[513] Where the review is a consolidated one involving both an FLB loan and a PCA loan, a board member from each entity must be present, unless the district Farm Credit Bank has the ultimate authority over both loans.[514]

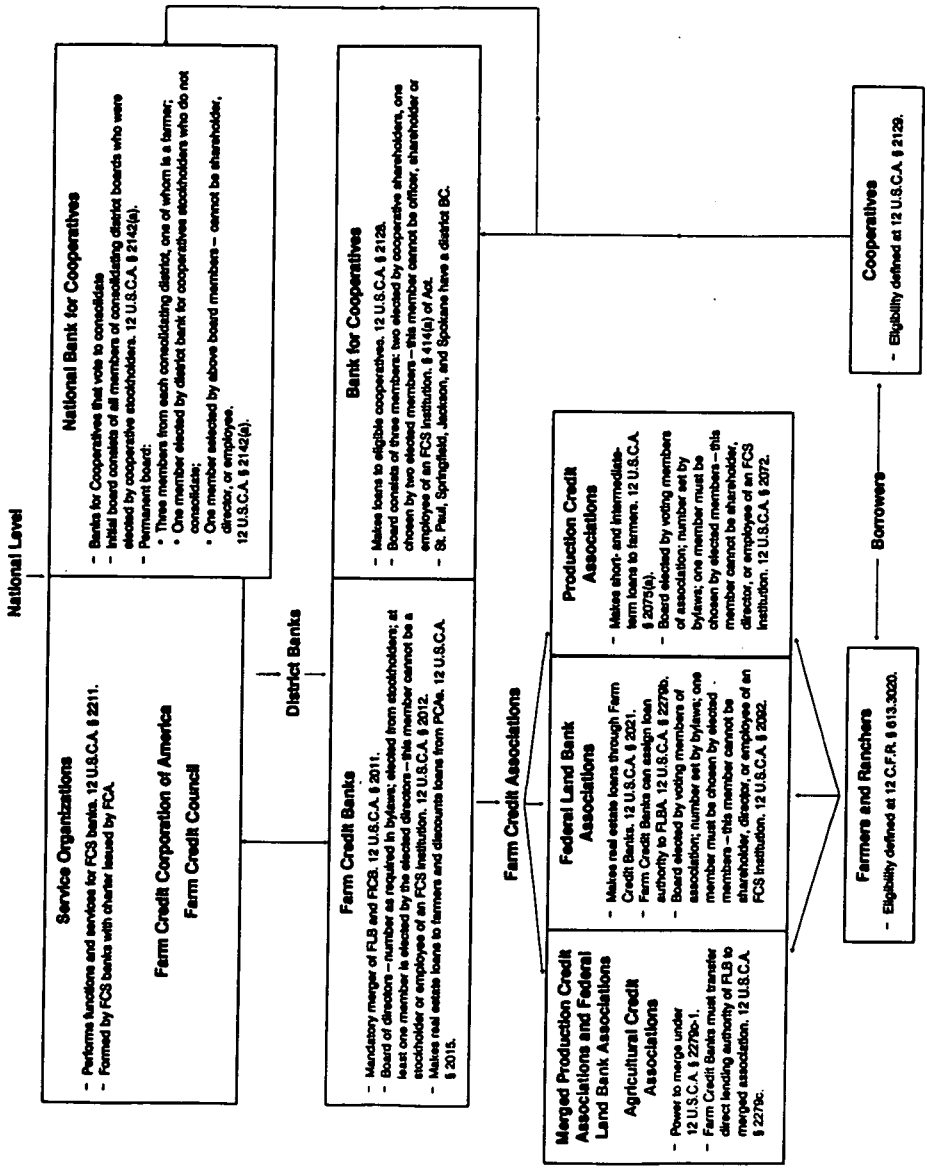
512. 53 Fed. Reg. 35,427, 35,436 (1988) (prefatory comments to the regulations). *See also* 12 U.S.C.A. § 2202(a)(2) (West 1989) ("In no case shall a loan officer involved in the initial decision on a loan serve on the credit review committee when the committee reviews such loan."); 12 C.F.R. § 614.4442 (1990) (same).

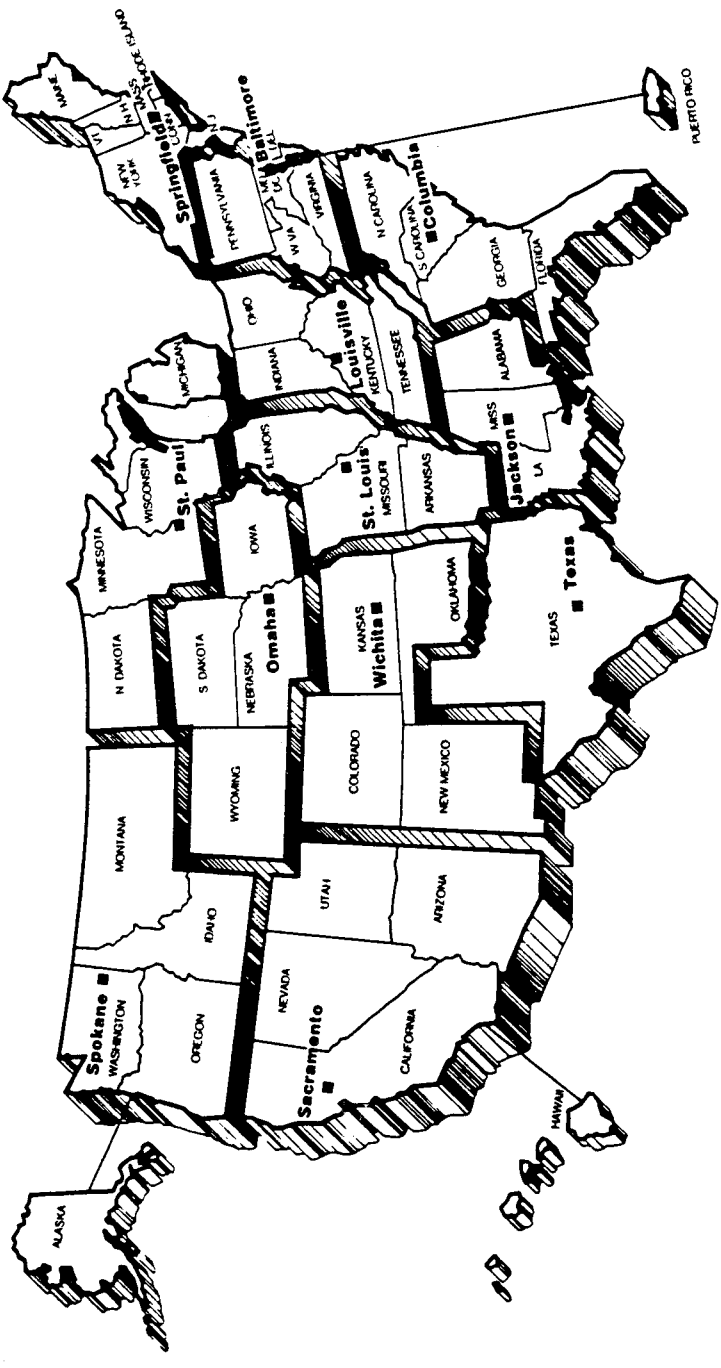
513. 12 U.S.C.A. § 2202(d) (West 1989); 12 C.F.R. § 614.4443(c) (1990).

514. 12 C.F.R. § 614.4442 (1990).

Structure of the Farm Credit System




National Level
Service Organizations
- Performs functions and services for FCS banks. 12 U.S.C.A. § 2211.
- Formed by FCS banks with charter issued by FCA.
Farm Credit Corporation of America
Farm Credit Council
National Bank for Cooperatives
- Banks for Cooperatives that vote to consolidate
- Initial board consists of all members of consolidating district boards who were elected by cooperative stockholders. 12 U.S.C.A. § 2142(a).
- Permanent board:
• Three members from each consolidating district, one of whom is a farmer;
• One member elected by district bank for cooperatives stockholders who do not consolidate;
• One member selected by above board members – cannot be shareholder, director, or employee.
12 U.S.C.A. § 2142(a).
District Banks
Farm Credit Banks
- Mandatory merger of FLB and FCB. 12 U.S.C.A. § 2011.
- Board of directors – number as required in bylaws; elected from stockholders; at least one member is elected by the elected directors – this member cannot be a stockholder or employee of an FCS institution. 12 U.S.C.A. § 2012.
- Makes real estate loans to farmers and discounts loans from PCAs. 12 U.S.C.A. § 2015.
Bank for Cooperatives
- Makes loans to eligible cooperatives. 12 U.S.C.A. § 2128.
- Board consists of three members: two elected by cooperative shareholders, one chosen by two elected members – this member cannot be officer, shareholder or employee of an FCS institution. § 414(a) of Act.
- St. Paul, Springfield, Jackson, and Spokane have a district BC.
Farm Credit Associations
Merged Production Credit Associations and Federal Land Bank Associations
Agricultural Credit Associations
- Power to merge under 12 U.S.C.A. § 2279b-1.
- Farm Credit Banks must transfer direct lending authority of FLB to merged association. 12 U.S.C.A. § 2279c.
Federal Land Bank Associations
- Makes real estate loans through Farm Credit Banks. 12 U.S.C.A. § 2021.
- Farm Credit Banks can assign loan authority to FLBA. 12 U.S.C.A. § 2279b.
- Board elected by voting members of association; number set by bylaws; one member must be chosen by elected members – this member cannot be shareholder, director, or employee of an FCS institution. 12 U.S.C.A. § 2092.
Production Credit Associations
- Makes short- and intermediate-term loans to farmers. 12 U.S.C.A. § 2075(a).
- Board elected by voting members of association; number set by bylaws; one member must be chosen by elected members – this member cannot be shareholder, director, or employee of an FCS institution. 12 U.S.C.A. § 2072.
Farmers and Ranchers
- Eligibility defined at 12 C.F.R. § 613.3020.
Borrowers
Cooperatives
- Eligibility defined at 12 U.S.C.A. § 2129.



Farm Credit System Districts