Multiple Factors to Drive Increase in Family Farmer Bankruptcy Filings

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Signing the Family Farmer Relief (FFR) Act of 2019 was like opening a pressure release valve. American farmers have suffered increasing financial stress this year from numerous sources, so a change in the law making Chapter 12 available to more farmers is likely to push the number of bankruptcy filings higher.

LEGAL CHANGES

The FFR has already taken effect, more than doubling the debt limit used to determine whether a family farmer is eligible to seek relief under Chapter 12. Now a family farmer may have aggregate debts of up to $10,000,000 and still take advantage of the Bankruptcy Code's provisions designed to make it easier for family farmers to reorganize their finances. Chapter 12 was enacted in 1986 and was criticized for having a debt limit so low that it excluded a significant percentage of American farmers whose business operations are larger and more highly leveraged than those of prior generations. The definition of "family farmer" now reads:

"...individual or individual and spouse engaged in a farming operation whose aggregate debts do not exceed $10,000,000 and not less than 50 percent of whose aggregate noncontingent, liquidated debts (excluding a debt for the principal residence of such individual or such individual and spouse unless such debt arises out of a farming operation), on the date the case is filed, arise out of a farming operation owned or operated by such individual or such individual and spouse, and such individual or such individual and spouse receive from such farming operation more than 50 percent of such

individual's or such individual and spouse's gross income..."

This change comes on the heels of another farmer-friendly change in the Family Farmer Bankruptcy Clarification Act of 2017. Before the 2017 change, any capital gains tax owed by a Chapter 12 debtor for sale of property used in farming operations was entitled to payment priority ahead of general unsecured creditors and could not be discharged. For many farmers with substantial capital gains tax liability, the law effectively made it impossible to get a Chapter 12 plan confirmed. The legislative fix made it possible for a family farmer to pay capital gains tax claims on a pro rata basis with other unsecured creditors over the life of the Chapter 12 plan and discharge any balance remaining at the successful conclusion on the plan.

WEATHER CONDITIONS

Prevalent drought conditions are contributing to the strain on American farmers. For instance, according to the U.S. Drought Monitor released by the U.S. Department of Agriculture on October 10, 2019:

→ Four states are experiencing drought affecting at least 25% of their corn crop production (Indiana 25%; Ohio 26%; Texas 31% and Kentucky 66%)

→ Five states are experiencing drought affecting over 20% of their soybean crop production (Indiana 27%; Ohio 24%; Kentucky 66%; Louisiana 46%; North Carolina 23%)

→ Seven states are experiencing drought affecting over 40% of their cattle inventory (Texas 43%; Kentucky 63%; Tennessee 47%; Virginia 72% Alabama 56%; Arizona 89%; Georgia 99%)

In other areas of the country, record flooding has eliminated the prospect of a profitable year for farmers and ranchers. Those facing poor crop yields and considerable cash flow problems may find the lure of relief offered by Chapter 12 too strong to refuse.

TRADE WAR

Even with the U.S. Department of Agriculture's market facilitation program, nearly all sectors of U.S. agriculture are being affected by retaliatory trade tariffs. According to news sources, U.S. farmers faced losing their fourth largest export market after China cancelled all purchases of U.S. agricultural products in reaction to the threat of tariffs on Chinese imports. Fortunately, on October 7, 2019, President Trump signed a U.S.-Japan Trade Agreement that will lower tariffs next year and help U.S. farmers and ranchers compete on a more level playing field in Japan, but the positive effects of this deal may come too late to stave off bankruptcy for some. For those who choose to file Chapter 12, looming uncertainty about foreign markets will complicate the already difficult task of forecasting income and expenses for the years their bankruptcy plan will be in effect.

TAKEAWAY

Creditors and vendors who work with farmers are already watching their accounts closely for signs of distress. Modifying terms to provide more time for repayment isn't always prudent, and the law does not support efforts to block a bankruptcy filing or impose penalties solely because of a filing. You can, however, consider adding collateral or guarantees to support repayment, and if you find yourself the recipient of a notice of Chapter 12 filing, retain experienced counsel who will help you protect and enforce your rights.

Lisa Sumner, a Member based in Nexsen Pruet's Raleigh office, is a commercial litigator focusing her practice in the areas of bankruptcy & creditors' rights. She is experienced in representing creditors in a variety of cases, including claims of lender liability, fraudulent transfers and breach of fiduciary duty, as well as in the filing of involuntary bankruptcy petitions.