Agriculture and Agri-Food Canada
Agriculture et Agroalimentaire Canada

Canada

Report to Parliament

Review of the Canadian Agricultural Loans Act





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1. INTRODUCTION

The Minister of Agriculture and Agri-Food, in consultation with the Minister of Finance, is required to review, every five years, the provisions and administration of the *Canadian Agricultural Loans Act*, as stated in section 22.1 of the Act. This report to Parliament is in accordance with the requirements of the Act and covers the five-year period from 2009 to 2014.

This report provides a short background to the program (the *Canadian Agricultural Loans Act* program), briefly describing its origins and its role within the context of a broader set of government programs. The report then provides a description of how the program works and a list of its key legislative and regulatory program parameters. This is followed by a description of program activity over the last five years and a summary of the findings of the work done to formally review the program.

As part of the formal review, Justice Canada undertook a comprehensive examination of the Act and its associated regulations and found no need to make any amendments from a legal perspective. A formal program evaluation was also conducted in 2013 along with meetings and surveys of financial institutions. Together these form the basis of the discussion in this report on the program's relevance, the impact on stakeholders, its contribution to the Department mandate and priorities, as well as the costs incurred by the federal government.

2. BACKGROUND

The origin of the Act can be traced back to the *Farm Improvement Loans Act*, enacted in 1944. The *Farm Improvement Loans Act* was introduced to encourage the provision of medium- and short-term credit to farmers to improve and develop farms and enhance living conditions. The *Farm Improvement Loans Act* was replaced by the *Farm Improvement and Marketing Cooperatives Loans Act* in 1987. It broadened coverage to include the provision of credit for processing, distributing and marketing of the products of farming by co-operative associations. The focus became medium- and long-term credit.

The *Canadian Agricultural Loans Act* (the Act) replaced the *Farm Improvement and Marketing Cooperatives Loans Act* in June 2009. Specifically, the Act increased loan limits, expanded eligibility and increased the percentage value of the assets that could be financed for beginning farmers. These changes were in response to recommendations Agriculture and Agri-Food Canada received from national consultations undertaken in 2006 with producers and financial institutions on modernizations required for the *Farm Improvement and Marketing Cooperatives Loans Act*.

The Act is one of several federal acts and associated programming directed specifically at enhancing farm competitiveness in Canada. The Act, along with federal government initiatives, such as the *Agricultural Marketing Programs Act* and the *Farm Credit Canada Act*, helps to ensure that farmers have reasonable access to financing. Collectively, these initiatives help producers to better manage business risk associated with operating their farms and to make investment decisions. Specifically, the Act helps to improve the access of farmers and agricultural co-operatives to medium- and long-term financing for the acquisition and improvement of assets, such as machinery, buildings and land.

The Act provides financing options to farmers and agricultural co-operatives in a similar manner as Industry Canada's *Canada Small Business Financing Act* provides options for non-agricultural businesses. Both the Act and the *Canada Small Business Financing Act* provide government loan guarantees allowing lenders to offer loans to their clients with preferred interest rates, lower down payments and, in some cases, longer amortization periods when compared to more conventional bank loans.

3. THE PROGRAM

The Act and its associated regulations are referred to as the program.

Over the years, this program has provided necessary financing that many agricultural businesses may not have been able to access otherwise. Under the provisions of this program, a lender (e.g., bank, credit union or other designated organization) may offer a loan to an eligible farmer or agricultural co-operative. In exchange, the Minister of Agriculture and Agri-Food guarantees payment of 95 per cent of a net loss (including interest) sustained by the lender on a registered loan under the Act.[a]

The program includes the following parameters:

Loans are limited to a maximum of

- $500,000 for the purchase of land and the construction or improvement of buildings;
- $350,000 for all other eligible loan purposes (such as implements, machinery and livestock) and for consolidation/refinancing;
- The maximum aggregate loan limit for any one farm operation is $500,000; and
- The maximum aggregate loan limit for agricultural co-operatives is $3 million, with the Minister's approval.

Down payments

- Loans issued to existing farmers and co-operatives can be up to 80 per cent of the purchase price or appraised value of the eligible asset.
- Loans issued to beginning farmers (those farming less than six years and reporting farm income for tax purposes) can be up to 90 per cent of the purchase price or appraised value of the eligible asset.

Maximum interest rate

- Maximum interest rate to be paid on a floating rate is the lender's prime rate plus one per cent.
- Maximum interest rate to be paid on a fixed-term rate is the lender's residential mortgage rate for a comparable term plus one per cent.

Repayment periods

- For farms, the maximum loan period for land is 15 years, and for agricultural co-operatives the maximum for land and building construction or improvement is 20 years.
- The maximum loan period for all other purposes is 10 years.

Fees

- A registration fee of 0.85 per cent of the amount of the loan must be submitted to the “Receiver General for Canada” when the loan is registered.
- The lender may also charge administration fees as prescribed in the Act.
- Both of these fees may be incorporated into the loan amount, provided the total does not exceed loan maximums.

4. PROGRAM USE AND ACTIVITY

When the program was first introduced in 2009, it was estimated that $217 million annually, or $1 billion over five years, would be guaranteed under the provisions of the program. This was based on the following assumptions:

- Improved eligibility criteria would result in 346 loans per year to beginning farmers, for a total of $127 million annually.
- Broader eligibility rules for co-operatives would increase the total value of loans to agricultural co-operatives to $40 million annually.
- Higher loan limits would increase existing farmers’ uptake by a total of $50 million per year.

From 2006 to 2009, the *Farm Improvement and Marketing Cooperatives Loans Act* program averaged approximately 1,800 loan guarantees annually. Initially (2009-2012), loan guarantees increased to 2,500 annually under the *Canadian Agricultural Loans Act* program .[b] More recently (2012-2014), the annual number of guarantees has dipped back into the 1,800 range.

Since the program’s implementation in 2009, interest rates have been low and commodity prices have been relatively high. This has reduced the cost of borrowing and made it easier for farmers to obtain loans from financial institutions without the program’s guarantee. According to a formal program evaluation conducted by Agriculture and Agri-Food

Canada's Office of Audit and Evaluation in 2013, uptake within the program has been lower than what was initially expected as a result of these economic conditions.[c]

For the review period from 2009 to 2014, a total of 10,149 loans were registered, with a value of $586 million (approximately $58,000 per loan). Of these, 1,076 loans were registered to beginning farmers, totaling $100.7 million (approximately $94,000 per loan).

In the review period, 265 loans (or 2.6 per cent of loans registered) were for amounts greater than $250,000, the former *Farm Improvement and Marketing Cooperatives Loans Act* program cap. Only five new loans were issued to co-operatives in the initial five years of the *Canadian Agricultural Loans Act* program. Three loans were recorded as intergenerational transfers. (Table 1)

TABLE 1: Amount and Number of Loans Registered by Fiscal Year

Fiscal Year	Total Number of Loans Registered	Total Value of Loans Registered ($ millions)	Loans Issued to Beginning Farmers	Value of Loans Registered to Beginning Farmers ($ millions)	Loans Issued Over $250,000	Number of Co-op Loans	Number of Inter-generational Loans
2009 - 10*	1,889	97	140	10.3	27	1	0
2010 - 11	2,381	137	242	23.0	60	0	0
2011- 12	2,311	132	232	19.6	62	1	2
2012 - 13	1,822	107	245	24.0	58	2	0
2013 - 14	1,746	113	217	23.8	58	1	1
Total	**10,149**	**586**	**1,076**	**100.7**	**265**	**5**	**3**

* As of the Act's enactment on June 18, 2009.
Source: Program data.

The annual total value of loans made in Saskatchewan ranged from $106 million in 2010-2011 to $82 million in 2013-2014 (77 per cent and 72 per cent of total loans, respectively). Most other provinces had a relatively constant annual total loan value, year over year, or had a slight decline. The one exception was Manitoba, where the annual total loan value has doubled over the past four years. (Table 2)

TABLE 2: Amount and Number of Program Loans by Province

Prov.	2009-2010* #	2009-2010* Value ($ 000s)	2010-2011 #	2010-2011 Value ($ 000s)	2011-2012 #	2011-2012 Value ($ 000s)	2012-2013 #	2012-2013 Value ($ 000s)	2013-2014 #	2013-2014 Value ($ 000s)
NL	0	0	2	307	3	547	3	718	0	0
PE	14	1,036	20	1,074	20	862	20	1,074	12	1,139
NS	1	23	4	581	5	820	5	1,300	8	1,733
NB	6	838	10	1,115	10	998	11	728	10	734
QC	16	1,390	16	2,300	11	1,269	2	239	2	144
ON	59	5,495	87	9,454	58	7,086	30	4,280	21	4,047
MB	122	7,277	114	8,192	100	6,079	87	5,573	200	15,969
SK	1,575	74,261	2,006	105,861	2,005	106,402	1,597	85,078	1,436	81,528
AB	87	5,812	111	7,337	83	6,305	53	7,177	40	5,534
BC	9	904	11	1,052	16	1,119	14	792	17	2,344
Total	**1,889**	**97,036**	**2,381**	**137,273**	**2,311**	**131,487**	**1,822**	**106,958**	**1,746**	**113,172**

Fiscal Year

* As of the Act's enactment on June 18, 2009.
Source: Program data.

Over 8,200 loans were registered under the program by credit unions. The majority of these were registered in Saskatchewan. (Table 3)

TABLE 3: Number and Total Amount of Guaranteed Loans by Type of Lending Institution (June 18, 2009 to March 31, 2014)

Institution	Number of Loans	Per cent of Loans (%)	Average Amount ($)	Total Amount ($)
Chartered Banks	1,925	19.0	70,351	135,425,106
Credit Unions	8,217	81.0	54,683	449,330,644
Other	7	0.0	167,279	1,170,950
Total	**10,149**	**100.0**	**57,738**	**585,926,700**

Source: Program data.

Sixty-five per cent of loans were issued for the purchase of agricultural implements over the evaluation period. As might be expected, average loan values for all other categories were smaller than for land. (Table 4)

TABLE 4: Number and Total Amount of Guaranteed Loans by Primary Purpose (June 18, 2009 to March 31, 2014)

Primary Purpose	Number of Loans	Per cent of Loans (%)	Average Amount ($)	Total Amount ($)
Implements	6,646	65.5	49,549	329,304,174
Livestock	1,029	10.1	38,150	39,256,750
Equipment	984	9.7	55,160	54,277,122
Land	876	8.6	141,369	123,838,998
Building	357	3.5	59,178	21,126,638
Consolidation/Refinancing	140	1.4	92,561	12,958,571
Improvement or Development	60	0.6	49,718	2,983,069
Major Repair/Overhaul	38	0.4	24,641	936,367
Intergenerational Loans	<10*	0.0	-	461,715
Other	<20*	0.2	-	783,189
Total	**10,149**	**100**	**57,738**	**585,926,700**

Source: Program data.
* Data suppressed to ensure confidentiality.

5. THE REVIEW

As described in the background, there were a number of components to the formal review process for the Act, including a comprehensive examination of the Act and its associated regulations by Justice Canada, a program evaluation and engagement with lenders through meetings and surveys.

Program evaluation: An evaluation of the performance, relevancy and efficiency of the program was undertaken by the Office of Audit and Evaluation, using both internal and external resources. This evaluation, published in February 2014 on Agriculture and Agri-Food Canada's website, included a review of program data by a third party, a scan of similar provincial programs, and a survey of farmers who received program loans, of lenders under the program and of federal government officials. The evaluation concluded that the program is a low-risk, low-cost way to support the agricultural sector, allowing farmers to increase their investments in their operations and improve the overall value of their farm operations. Involvement of lenders in qualifying loans and collecting on defaulted loans lowers program risk, resulting in fewer defaults and fewer claims for loss. The evaluation recommended that Agriculture and Agri-Food Canada should work to increase awareness of the program among lenders and producers. The resulting report, entitled *Evaluation of the Canadian Agricultural Loans Act Program*, is referenced in this report as "the Evaluation".[d]

Lender engagement meetings: In 2013-2014, Agriculture and Agri-Food Canada held four engagement meetings with lenders and the Canadian Co-operatives Association to gather information on the operation and delivery of the program. Specifically, lenders were asked to comment on the program parameters and factors affecting program delivery. Comments from these meetings are referenced in this review as “Lender Engagement Meetings”.

Lender survey: In 2014, Agriculture and Agri-Food Canada polled participating lenders to ascertain: a) how the 2009 program changes have been received; b) why they issue loans using the program; c) what benefits the program offers; and d) how the new Online Loan Registration System is working. The lender survey is referenced as “Lender Survey”.

6. THE REVIEW FINDINGS

6.1. Legal review

As part of the formal review, Justice Canada thoroughly examined the Act and its associated regulations. They found that there is no need to amend either the Act or the regulations from a legal perspective.

6.2. Relevancy of the Program

Access to external financing is critical for farmers to both start up and grow. Farmers can face many challenges that stem from their shortage of financial resources. Farming enterprises continue to play a major role in the Canadian rural economy. Government support to encourage investment in agriculture and to enhance farm performance is especially important for a sustainable and competitive sector. More generally, farms with greater access to financing are more likely to increase their production and are more sustainable than those with limited access.

The *Canadian Agricultural Loans Act* program is one of several federal programs directed specifically at enhancing farm competitiveness in Canada by ensuring that farmers have access to loans with competitive terms. The program, using loan guarantees, like its counterpart for non-agricultural enterprises, the Canada Small Business Financing program, can leverage a great number of privately funded loans for a small government administrative cost.

The program reduces the risk that financial institutions face when lending to agricultural producers, thereby increasing their capacity and willingness to lend to the sector. This is particularly important when market conditions are poor and the lender’s portfolio is highly exposed to the sector. During periods of poor markets and tighter credit availability, lenders tend to reduce their exposure to the sector, particularly if their portfolio already has a significant number of agricultural loans. With a guarantee in place, lenders can make the loans and offer more favorable terms reflecting their lower risk. The fact that credit unions represent 78 per cent of loans demonstrates the importance of the guarantee to the smaller, less capitalized lenders that operate in rural communities where agriculture represents a significant portion of their business.

Through loan guarantees, the program continues to help farmers and agricultural co-operatives to better manage business risk associated with making investments in their operations by reducing the required down payment, lowering interest rates on capital loans and amortizing these loans over a longer loan term.

Financial credit offerings to the agricultural sector are not consistent across Canada. This can create gaps in financial products/solutions for the agricultural sector. The program is particularly important for Saskatchewan, where provincial legislation prevents financial institutions from seizing property that would affect the borrower's livelihood. This reduces the amount of security available to lenders, making it difficult for Saskatchewan producers and co-operatives to obtain loans. The guarantee offered by the program provides additional security to lenders, ensuring they continue to offer loans into the sector in the province. The program is also excluded from restrictions in the provincial legislation, thus allowing property to be used as security for program loans. (Evaluation)

The program both complements and supplements private and provincial credit by helping to ensure farmers have equal access to the same competitive loan terms across the country. The program also complements lending under the *Farm Credit Canada Act*. While Farm Credit Canada is the only national financial institution focused solely on agriculture, the program plays an important role in ensuring banks and credit unions have the flexibility to provide alternative credit solutions to producers.

As a result of interest rates being low and commodity prices being high, program activity has been below expected levels. Nevertheless, the program remains relevant by acting as a backstop in circumstances and periods when credit gets tighter. Even though credit has been favourable over the five-year review period, the program has provided an important option to beginning/startup farmers by financing investments in their operations.

6.3. Farm and co-operative impact

Participating farmers (84 per cent) reported that financing terms under the program allowed them to increase their investments and improve the overall value of farm operations, and more than 90 per cent said it was an important option. (Evaluation)

Many farmers are in favour of the relatively small 10 per cent down payment requirement for beginning farmers. Conventional loans usually have at least a 25 per cent down payment and beginning farmers typically do not have as much equity as do established farmers. (Lender Survey)

The ten-year amortization period for assets such as equipment is also appreciated by farmers, giving them access to financing beyond the conventional amortization term for similar assets. (Lender Survey)

Only a small number of loans were recorded as intergenerational loans over the five-year period under review. Program administrators pointed out that this likely understates the actual number of intergenerational transfers that, in part, have been facilitated by the program. Some of the loans recorded by lenders as beginning farmer loans also could be classified as intergenerational loans.

A significant number of loans guaranteed under the program are below the maximum loan limit. The program tends to be used for smaller purchases. Nevertheless, some farmers have expressed concern about current loan limits being too low for major purchases, such as land and large equipment. Increases to loan and land amortization limits could expand the number of farms participating in the program. (Evaluation, Lender Survey)

It is believed that one reason for a low uptake by co-operatives may be due to difficulties in establishing appropriate equity security, thus limiting access to financing. Some program administrators have indicated that certain types of agricultural businesses may be moving away from co-operatives and toward the formation of corporations for this reason.

6.4. Lender impact

The program provides financial institutions with a risk management tool for lending to farming operations, as the loan guarantee mitigates lenders' exposure to losses resulting from loan defaults.

Some lenders, most notably credit unions, perceive the program as helping them to be competitive with Farm Credit Canada. Some lenders feel that the program helps "even the playing field. (Evaluation, Lender Engagement Meetings)

Some lenders and producers have expressed concern about the perceived burden of registering loans under the program and of any resulting claims. However, other lenders have appreciated the ease of use and cost savings of the new Online Loan Registration System, which was implemented in February 2013. (Lender Engagement Meetings)

The external registration system works well for lenders registering loans online, (whether or not they use the Bill Payment System for electronic payments) and is simplifying program delivery. (Lender Survey)

Lenders also have expressed concern about current loan limits to farmers for major purchases being too low. (Evaluation, Lender Survey)

6.5. Government costs of the program

Since the inception of the *Farm Improvement and Marketing Cooperatives Loans Act* in 1987, and subsequently the *Canadian Agricultural Loans Act* in 2009, loan default costs to the federal government have been less than one per cent of the dollar value of loans issued. (Evaluation) The average annual net cost of the program for the past five years (2009-2014) has been $562,014.[e] (Table 5)

TABLE 5: Program Revenue and Expenditures

	2009-10* ($)	2010-11 ($)	2011-12 ($)	2012-13 ($)	2013-14 ($)	Total ($)
Expenditures						
Vote 1 - Program Administrative Costs	303,680	2,510,814	1,410,159	715,520	573,140	5,513,313
Statutory Grants & Contributions - Default Costs	1,681,536	316,603	164,679	251,843	20,883	2,435,544
Total Expenditures	**1,985,216**	**2,827,417**	**1,574,838**	**967,363**	**594,023**	**7,948,857**
Revenue						
Registration Fees	823,837	1,204,905	1,113,212	901,592	946,374	4,989,920
Default Recoveries	84,241	84,132	23,637	47,736	33,712	273,458
Total Revenue	**908,078**	**1,289,037**	**1,136,849**	**949,328**	**980,086**	**5,263,378**
Total Net Cost	**1,077,141**	**1,538,380**	**437,989**	**18,035**	**(386,063)**	**2,685,479**

Source: Program data.

- Default costs and recoveries include loans guaranteed under the *Farm Improvement and Marketing Cooperatives Loans Act* and the *Canadian Agricultural Loans Act*.

*2009-2010 fiscal year expenditures were adjusted to represent the portion of the year where the program operated (9.4 months, or 78.6 per cent of the annual amount).

- The Main Estimates allocation for Statutory Grants and Contribution guarantee payments for the program in 2014 was $13.1 million.

The program is being delivered as planned and has met all of its service standards over the evaluation period of 2009 to 2014. Overall, the program's operating costs are comparable to, or less than, those of other federal loan programs with similar delivery mechanisms and objectives. (Evaluation)

Part of the program delivery efficiencies stem from the February 2013 implementation of an online loan registration process. This process was developed at the same time as the

Canada Small Business Financing program. The process reduces the administrative costs of issuing loans and managing claims for both the government and lenders.

The program is a low-risk, low-cost government program that supports the agricultural sector.

The program is a lender-driven program. Low awareness and hesitation in using the program on the part of lenders affects program uptake. Lenders are a primary source of program information for farmers and co-operatives and are the decision-makers on whether or not guaranteed loans are issued. (Evaluation, Lender Engagement Meetings)

6.6. Contribution to the departmental mandate and priorities

The program is aligned with federal government priorities in support of Canada's agricultural sector as it innovates and grows. Canada is supporting its agricultural sector by making financing available to existing and beginning farmers to establish, develop, maintain and grow their farms. As well, the program helps agricultural co-operatives to take advantage of market opportunities. Overall, the program supports the renewal of the agricultural sector and enables co-operatives to better seize competitive opportunities. The Government of Canada is contributing to its goal of fostering business investment and growth. (Evaluation)

The program supports Agriculture and Agri-Food Canada's first strategic outcome of its 2014-2015 Program Alignment Architecture, which is to foster "A competitive and market-oriented agriculture, agri-food and agri-based products sector that proactively manages risk." (Evaluation)

7. CONCLUSIONS

Following a comprehensive review of the Act and its associated regulations, Justice Canada found that there is no need to make any amendments to the legislation or the regulations from a legal perspective.

The program is efficiently managed and delivered and provides a low-risk, low-cost government program that supports the agricultural sector. The involvement of lenders in qualifying loans and in collecting loans in arrears results in low defaults.

The program is an integral part of the federal government's commitment to ensure that Canada has a sustainable, competitive and innovative agricultural sector. The program provides improved access to medium- and longer-term financing for farmers and agricultural co-operatives. The program complements and supplements private and provincial credit, ensuring farmers have equal access to the same competitive loan terms across the country. The program ensures banks and credit unions have the flexibility to offer credit solution options to producers, thereby increasing competition in the market.

It appears to be particularly beneficial to beginning farmers. Farmers reported that the financing terms under the program allow them to increase investments in their operations and improve the overall value of farm operations, which ultimately boosts productivity and the sustainability of their operations.

Although a number of lenders raised concerns with the program limits, the administrative data would suggest that the current limits are meeting the needs of the vast majority of producers. Program officials will continue to monitor the size of loans being registered as well as engage the industry and lenders in further conversations. As farming operations continue to expand and increase capitalization, there may be a future need to reconsider the loan limits.

Participation in the program over this review period was not as high as originally anticipated. Economic conditions in recent years have facilitated access to credit without the need for the program guarantee. However, a period of lower commodity prices and higher interest rates could lead to increased program usage.

Lenders play a crucial role in awareness, delivery and uptake of the program. It is important that they have a clear and accurate understanding of all aspects of the program. Improved program awareness of lenders will be key for expanding program uptake over the next review period.

ENDNOTES

[a] As specified in the Act, the program's exposure to risk from a single lender is mitigated through a diminishing rate of payment for claims.

[b] The 1,889 loans approved for 2009-2010 were approved over a nine month period. Hence, the annual loan approval rate for this period is 2,532 (4/3 x 1,889).

[c] When commodity prices are high (and incomes are high as a result), farmers have a greater capacity to repay their loans. As a consequence, lenders tend to offer preferred interest rates directly, without a government guarantee. If income declines, the ability of farmers to service their debt becomes less certain and lenders are more inclined to seek further assurances, including adding the security of the government guarantee. As well, when interest rates are low, lenders have little room to offer significantly lower preferred rates, even with government guarantees backing the loan. Thus, the combination of low interest rates and higher commodity prices is likely to have affected the program's loan registration level.

[d] Data for the Evaluation covered the 2009-2012 period. The data included in this review were updated and cover the 2009-2014 period.

[e] The average annual net cost of the program equals the total cost ($2,689,799) divided by the length of the program (4.786 years).