Rural Development and the 2007 Farm Bill

Center for Rural Affairs
Policy White Paper

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VALUES. WORTH. ACTION.

Background

The Rural Development Title of the 2007 Farm Bill should be based upon and should focus on two themes: entrepreneurial development in rural areas and strategies to build assets and wealth for rural people and in rural communities. Both strategies address the persistent, deep-rooted poverty present in many rural parts of the nation and the growing economic disparity between rural and urban areas of the nation. And both strategies address the issues of how to repopulate rural areas and the how to ensure the long-term future of rural America.

There is a developing broad agreement among researchers, policy advocates and others that the traditional economic development models of industrial and business recruitment simply do not meet the needs of rural communities. Entrepreneurship has been lifted up as an economic development model that will better serve rural people and rural places. For example, the Federal Reserve Bank of Kansas City states that, "Rural policymakers, who once followed traditional strategies of recruiting manufacturers that export low-value products, have realized that entrepreneurs can generate new economic value for their communities. Entrepreneurs add jobs, raise incomes, create wealth, improve the quality of life of citizens and help rural communities operate in the global economy[1]." Federal rural policy must begin to recognize the importance of entrepreneurship as a rural development strategy and provide the resources necessary for rural people and rural communities to leverage the spirit, creativity and opportunities entrepreneurship creates.

Asset- and wealth-building strategies are equally important. Greater income alone cannot lead to economic well-being for individuals and families; asset- and wealth-building through home ownership, business ownership or enhanced education lead to important long-term psychological and social effects that cannot be achieved by simply increasing income. While income is an important factor, income can be achieved nearly anywhere in varying degrees. Assets like businesses and houses bond one to a place and help to build sustainable communities. A commitment to rural asset- and wealth-building strategies can lead to stronger individuals, families and communities.

Agriculturally-based entrepreneurship and innovation must also continue to play a vital role in rural development policy. Agriculturally-based entrepreneurship can contribute to the creation of jobs and businesses in rural communities and to the alleviation of poverty in the same communities. Programs that promote a new generation of farmers and ranchers and which provide incentives for entry into agriculture also benefit the development of rural communities and their institutions. Beginning farmer and rancher programs also provide opportunities for the advancement of agriculturally-based enterprises among a new generation of rural entrepreneurs.

Small Business and Entrepreneurial Development

Most new jobs in very rural areas come from non-farm proprietorships – people creating their own job by starting a small business. Small-scale entrepreneurship is the one development strategy that consistently works for most rural communities.

It can also bring back the young. Surveys of high school students in Nebraska, for example, find that up to 80 percent would like to own their own farm or business. That has the potential to draw them back to rural America. Low wage jobs will not.

Currently, most financial support for rural entrepreneurs comes from the Small Business Administration (SBA), with some smaller funding from USDA programs such as RBEG, RCDI and others. However, SBA

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[1] Federal Reserve Bank of Kansas City, Center for the Study of Rural America. 2002. "Are High-Growth Entrepreneurs Building the

funds are fully subscribed, with Nebraska the only state where services to rural entrepreneurs are available statewide.

Many rural communities have self-employment and small business ownership rates many times greater than urban areas. Small businesses are also the job creators in much of rural America. In the Great Plains region, for example, nearly 70 percent of job growth in the 1990s came from non-farm proprietorships.[2] To allow for continued creation and expansion of rural businesses and employment opportunities, resources to rural small business development must be enhanced.

The 2007 Farm Bill should create a Rural Entrepreneurs and Microenterprise Program that would allow rural entrepreneurs to acquire the skills, obtain capital, and build networks necessary to establish new small businesses in rural areas and receive continuing technical assistance as the individuals begin operating the small business. Microenterprise would be defined in the program as a business that employs five or fewer individuals, requires $35,000 or less in start-up capital, and does not have access to the commercial banking sector.

Grants would be provided to qualified organizations to provide training, technical assistance, or credit to qualifying rural entrepreneurs. In addition, grants would be made available to qualified organizations for training, operating support and capacity building services to assist them in developing training and services for rural microenterprise programs, or to assist them in developing the best practices in delivering training, technical assistance and micro credit to rural entrepreneurs.

A similar a program was included in the Senate version of the 2002 Farm Bill (Section 638 of Section. 1731). The Rural Entrepreneurs and Microenterprise Program should be included in the 2007 Farm Bill with $50 million in mandatory funding.

In general, rural communities have not been well-served by traditional economic development strategies. These strategies have lead to rural depopulation, the exporting of local wealth, and a growing economic disparity between rural and urban areas. Most importantly, these strategies have lead to a mentality of dependence on state and federal government programs to provide for the future of rural people and rural places.

There is, however, a developing alternative based on the Home Town Competitiveness program, the Community Vitality Center in Iowa and the Energizing Entrepreneurs program that encourages communities to take immediate action in four strategic areas:

1. Mobilizing local leaders – For rural communities to compete in the 21st century, they must tap into everyone's potential knowledge, talent and aspirations. Rural communities must recruit and nurture leadership among all segments of the population – including women, minorities, and young people. The entire community must be brought into decision-making roles, with continuing leadership training programs provided that allows today's leadership to reflect the challenges of a constantly changing global environment.

2. Capturing local wealth – Rural residents do not always recognize the existence of local wealth because it is often held through land ownership. Because of the aging farm population, much of that wealth is also in danger of permanently leaving the community in the next few decades. The Nebraska Community Foundation, for example, has estimated that $94 billion worth of wealth is at stake in rural Nebraska in the next 20-30 years. The power and the will to use these assets will no longer be tied the community unless active strategies are implemented now. Active community foundations and other vehicles of local philanthropy will allow rural communities to capitalize their hopes, dreams and needs employing their own assets.

[2] Bailey and Preston. 2003. *Swept Away: Chronic Hardship and Fresh Promise on the Rural Great Plains.* Center for Rural Affairs. Lyons Nebraska.

3. Energizing entrepreneurship – Too many rural communities continue to invest resources in economic development for job creation and business development that exports, rather than builds, local wealth. A more sustainable strategy for many rural communities is to create new wealth and jobs through developing local entrepreneurs, broader product lines and larger markets; develop planned business succession; and use local assets to support entrepreneurial development.

4. Attracting young people – The lack of opportunity and encouragement to "come back" drives many young people away from their rural hometowns. Rural communities, however, can set realistic goals for youth attraction, that when combined with the other strategies, can stabilize population and enhance the local economy.[3]

Targeting youth and young families for attraction, creating career opportunities through business transfer strategies and entrepreneurship and nurturing a sense of ownership and involvement in the community can lead to a community that is more attractive to young people and young families.

The 2007 Farm Bill should create a $75 million Community Entrepreneurial Development Program based on four pillars of rural economic and community development: entrepreneurship, capital, youth and leadership. This program would offer grants to collaborating communities to establish regional initiatives for entrepreneurial development, including small business education and technical assistance, leadership development, youth attraction and retention, community-based philanthropy and intergenerational business transfer planning.

Facilitating the growth and success of entrepreneurship in rural communities is an essential component of effective economic development initiatives at the local, state, and regional levels. The creation of sustainable small businesses in rural communities, including both agriculturally-based and other businesses, is the best alternative to fill a void left by the loss of manufacturing jobs and an historic reliance on economic activity based on natural resource extraction.

Grassroots groups, local economic development councils, Community Action Agencies, regional Small Business Development Centers, colleges and universities, state and local governments and several USDA programs currently provide leadership, technical assistance, and training to rural entrepreneurs. There is, however, a lack of comprehensive support or policy aimed at fostering rural entrepreneurship. Ensuring collaboration and cooperation among these individual local, regional, state, and federal initiatives is essential to increasing the number of rural entrepreneurial start-ups while simultaneously reducing the failure rates of small businesses. In addition, research focused on best practices in rural communities that can be shared with rural entrepreneurship practitioners is necessary for a sustainable economic development model.

The 2007 Farm Bill should create a $20 million Rural Entrepreneurship Research and Education Program overseen by the USDA's Cooperative State Research, Education, and Extension Service, and jointly administered by and through the four existing Regional Rural Development Centers with oversight by regional administrative councils. The Rural Entrepreneurship Research and Education Program would be a regional competitive organizations for projects to foster rural entrepreneurship, including, but not limited to, education and training; technical assistance; research; and partnership and network building.

The Rural Entrepreneurship Research and Education Program will provide much-needed resources and services to rural areas with the stated goal of creating jobs, spurring community innovation in all sectors of the rural economy, and increasing the start-up rate and reducing the failure rate of small

[3] This theory of youth attraction was developed by the Nebraska Community Foundation, and is an integral part of the Home Town Competitiveness model. See www.nebcommfound.org

businesses. The program will complement the individual-focused support provided by existing business development programs by creating partnerships with grassroots organizations, non-profits, educational institutions, and government agencies engaged in educating and training potential entrepreneurs in rural communities. With a goal of creating entrepreneurial networks, providing technical training, and conducting very applied research, the program will also provide a complement to the Rural Entrepreneurs and Microenterprise Program, which targets individuals who have already opened a small business, or are poised to do so.

Rural Asset- and Wealth-Building

Asset- and wealth-building strategies allow rural people to undertake activities that have both individual and community benefits. Individuals and families build an asset base that lifts the veil of poverty and dependence on low-wage work. Communities become stronger and more viable as opportunities and ownership are expanded to a wider group of people. The issues of depopulation, poverty and low-wage employment facing many rural communities are largely a function of a lack of opportunity in those communities. In order to create a future for those communities and their residents, a commitment must be made to enhance opportunity through the building of assets and wealth.

As a result of economic and demographic challenges facing many rural communities (lackluster local economies highlighted by low-wage employment without health and retirement benefits, high levels of poverty, and a general lack of economic opportunity resulting in spiral of depopulation), many rural families have difficulty accumulating enough resources to invest in the future. The wealth held by rural families tends to be concentrated in illiquid assets such as personal residences, farms and ranches, or other forms of real estate. Rural households and residents are less likely to hold liquid assets and have higher rates of "asset poverty" (enough assets to support them for three months) than do urban households and residents.

Rural households and individuals also possess housing that is older and in poorer condition than urban and suburban housing. Rural households and individuals, on average, also possess less education than urban households and individuals, thus limiting earning potential and economic opportunities. Taken together, rural families and individuals are less able to manage income disruptions (due to health issues or a loss of job) and are less able to invest in the future of their families and their communities. As a result, rural families are more susceptible to a continuing lifestyle of low-wage work and asset poverty and remaining on the lower rungs of the economic ladder.

Providing incentives for rural households and individuals to undertake asset- and wealth-building strategies will allow for activities that have both individual and community benefits. Individuals and families build an asset base that lifts the veil of poverty and dependence on low-wage work. Communities become stronger and more viable as opportunities and ownership are expanded to a wider group of people. The issues of depopulation, poverty and low-wage employment facing many rural communities are largely a function of a lack of opportunity in those communities. In order to create a future for those communities and their residents a commitment must be made to enhancing opportunity through the building of assets and wealth.

The New Homestead Act of 2005 (S. 675) contains an Individual Development Account-like program for people in qualifying counties (those rural counties experiencing 10 percent or more out-migration in the past 20 years) entitled "Individual Homestead Accounts." Individual Homestead Accounts (IHA) – like Individual Development Accounts – are savings accounts (matched, generally, with public funds) that allow tax-free withdrawals for certain purposes; IHA allowable purposes are costs incurred in developing a small business expenses related to obtaining higher education, first-time home purchases in qualifying counties, unreimbursed medical expenses, and qualified retirement account rollovers. Any individual who is a bona fide resident of a qualifying county is allowed to create an IHA. The IHA provision is generally identical to Individual

Development Account programs that have been employed successfully in urban areas. Individual Homestead Accounts would allow individuals and families of distressed rural areas to begin building assets and would allow communities to institute strategies to address issues of depopulation and a lack of economic opportunity.

Based on 2000 Census data, over 3.3 million households in qualifying counties would have household income that would qualify them for matching IHA funds. This represents about 16 percent of all non-metropolitan households in the United States, but about 81 percent of households in New Homestead Act counties. The IHA provisions, as with other provisions in the New Homestead Act, would apply to 698 counties in 38 states. Our research shows that IHAs could create over 150,000 businesses and over 260,000 jobs in New Homestead Act counties.[4]

Rural America is at a federal funding disadvantage. The Consolidated Funds Report for 2003 (the most recent data available) shows a $6.5 billion annual federal funding deficit to rural areas compared to urban areas, with a per capita deficit of over $100 for each rural person in the nation. Even more lopsided is the rural disadvantage in community development funding. Each year since 1994, the federal government funded two to five times as much per capita to urban community than to rural community development. The federal government provided only one-third as much for rural areas since 1994, an annual $16.5 billion funding disadvantage. Much of the rural funding disadvantage is in programs promoting and assisting asset- and wealth-building activities. Providing for Individual Homestead Accounts will relieve a measure of the rural funding disadvantage in asset- and wealth-building activities.

The 2007 Farm Bill should include the Individual Homestead Account provision of the New Homestead Act (Section 104 of S. 675, 2005). Individual Homestead Accounts (IHA) should be used for the specific purposes of developing a small business, expenses related to obtaining higher education, first-time home purchases in qualifying counties, unreimbursed medical expenses, and qualified retirement account rollovers. Any individual who is a bona fide resident of a qualifying, high out-migration county is allowed to create an IHA. The IHA program should be capped at $250 million annually.

Agricultural Entrepreneurship and Innovation

Many farmers and ranchers are pursuing new consumer driven markets for agricultural products, thus creating enhanced economic opportunities in rural communities. By providing resources to farmers and ranchers to supply those markets, issues of agricultural profitability, economic decline and poverty alleviation in rural communities can be addressed. The 2007 Farm Bill can address these issues and promote agricultural entrepreneurship and innovation by reauthorizing and reforming the Value-Added Producer Grant program and by providing other means to promote and reward agricultural innovation.

The **Value-Added Producer Grant** program (VAPG) was authorized by the 2002 Farm Bill. The VAPG program should be reauthorized and funded at least at the $40 million annual level with mandatory funding status as contained in the 2002 Farm Bill. In addition, the VAPG program should contain a priority use for proposals that are most likely to increase the profitability and viability of small- and medium-sized farms and ranches and a 10-15 percent set aside of program funding for projects concerning beginning farmers and ranchers.

The next farm bill should include a **Family Farm Innovation Fund** to provide seed capital for innovative initiatives to strengthen family farming and ranching opportunities. For example, an agricultural bank in

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[4]Bailey and Preston. 2005. *Building Wealth in Rural Communities: the New Homestead Act and Individual Homestead Accounts. Center for Rural Affairs: Lyons NE.*

eastern Iowa is sponsoring a series of forums on machinery cooperatives as a means of enabling small and mid-size farms to lower machinery costs to competitive levels. But it takes legal work and research to launch such initiatives. USDA innovation funds could support such initiatives by providing the Secretary of Agriculture authority to use up to $2.5 million annually to support such initiatives from funds authorized and appropriated for USDA direct lending programs.

The 2007 Farm Bill should also reauthorize and reform the **Rural Business Enterprise Grant** (RBEG) program. It should be made clear that RBEG can be used for agriculturally-related business development. A recent report by the Center for Rural Affairs found that many states specifically tell prospective grantees that RBEG cannot be used for agriculturally-related enterprises and business development, while other states fund many such projects.[5] Statutory language for RBEG should be reformed to clarify that use of program funds, and that agriculturally-related projects funded by RBEG should maintain the viability of and increase the profitability of small- and mid-size farms and ranches.

Beginning Farmers and Ranchers

The future of agriculture depends on the ability of new family farmers and ranchers to enter agriculture. Providing opportunities for beginning farmers and ranchers is also important for rural communities – the viability of rural businesses, schools, and other community institutions are all dependent in part on the existence of new agriculturalists on the land. The **Beginning Farmer and Rancher Development Program** can play an important role in addressing critical issues facing new farmers and ranchers. Extension of other 2002 Farm Bill programs and modifications in tax law can also provide opportunities for beginning farmers and ranchers.

The Beginning Farmer and Rancher Development Program (BFRDP) was authorized in Section 7405 of the 2002 Farm Bill. This program was primarily targeted to collaborative local, state, and regionally-based networks and partnerships to support training, mentoring, linking, education and planning activities to assist beginning farmers and ranchers. The BFRDP would have been the first ever USDA program other than farm credit/debt financing programs targeted specifically to beginning farmers and ranchers. However, the program was only extended discretionary funding status under the 2002 Farm Bill and never appropriated funds to be implemented. The BFRDP should be reauthorized with $15 million in mandatory funding for the 2007 Farm Bill.

Escalating land values across the nation have priced most beginning farmers and ranchers out of the market for land, the most valuable commodity in any agricultural operation. The 2002 Farm Bill established the **Beginning Farmer Land Contract** pilot program to allow USDA to provide loan guarantees to sellers who self-finance the sale of land to beginning farmers and ranchers. The 2007 Farm Bill should permanently and

nationally implement this provision. Current tax law should also be modified to provide incentives to sellers of land to beginning farmers and ranchers. The prohibition on USDA loan guarantees being used in conjunction with state beginning farmer "aggie" bonds should be removed. Combined with federal **"first time farmer bonds**," which make interest income tax exempt if earned on loans or contract land sales (seller financed) to beginning farmers and ranchers, this would provide a powerful incentive to lend and sell land to beginners and would mitigate the risk to lenders land sellers.

[5] *The Impact and Benefits of USDA Research and Grant Programs to Enhance Mid-size Farm Profitability and Rural Community Success.* 2005. Center for Rural Affairs: Lyons, NE.

California FarmLink has established an Individual Development Account (IDA) program specifically targeted to beginning farmers; the 2007 Farm Bill should institute a similar program for beginning farmers and ranchers nationally. The **Beginning Farmer and Rancher IDA** would be a special matched savings account designed to assist those of modest means to establish a pattern of savings and to promote a new generation of farmers and ranchers; the account proceeds may be used toward capital expenditures for a farm or ranch operation (e.g., expenses associated with purchases of land, equipment or livestock).

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Established in 1973, the Center for Rural Affairs is a private, non-profit organization working to strengthen rural communities through action oriented programs addressing social, economic, and environmental issues.

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