

BEGINNING FARMER LOAN PROGRAM

Loans By Lending Institutions

and Contract Sales

or Direct Loans by Investors Other than Lending Institutions

KDFA

KANSAS

DEVELOPMENT FINANCE

AUTHORITY

PROGRAM SUMMARY

TABLE OF CONTENTS

Section

- I PROGRAM POWERS AND ELIGIBLE ACTIVITIES
 - 1. Agricultural Land
 - 2. Agricultural Improvements
 - 3. Depreciable Agricultural Property
- II PROGRAM MAXIMUMS AND MINIMUMS
- III NATURE OF INVESTMENT RISK; LIMITED OBLIGATION BONDS
- IV APPLICANT ELIGIBILITY
 - 1. Age Limits
 - 2. First-Time Farmer
 - 3. Training and Experience
 - 4. Use of Project
- V INELIGIBLE PROGRAM ACTIVITIES
 - 1. Refinance Existing Debt
 - 2. Finance Working Capital
 - 3. Finance the Acquisition of Property
- VI APPLICATION AND PROCEDURES - DIRECT LOANS
 - 1. Application Forms
 - 2. Application Period
 - 3. Interim Financing
 - 4. Loans to Beginning Farmers and Security Arrangements
 - 5. Terms of Loan

6. Repayment of Loans
7. Assignment or Sale of Bonds
8. Fees
9. Use of Financial and Security Documents
10. Bond Purchasers
11. Procedures Following Bond Issuance
12. Timing Requirements for Spending Bond Proceeds
13. Assumption of Loans - Substitution of Collateral and Transfer of Property
14. Public Hearing and Governor's Approval of Bond Issuance
15. State Volume Cap Limitations
16. Modified Accelerated Cost Recovery System Limitations
17. Maximum Loan Maturity

VII APPLICATION AND PROCEDURES - SALES CONTRACTS

1. Application Form
2. Application Period
3. Sales Contracts and Security Arrangements
4. Terms of the Sales Contract
5. Payments Under the Sales Contract
6. Assignment or Sale of Bonds
7. Fees
8. Use of Financial and Security Documents
9. Bond Purchasers
10. Loan and Sales Contract
11. Assumption of Sales Contract - Substitution of Collateral and Transfer of Property
12. Public Hearing and Governor's Approval of Bond Issuance
13. Modified Accelerated Cost Recovery System Limitations

14. Maximum Terms of Sales Contract

VIII FEDERAL TAX EXEMPTION OF AUTHORITY BONDS

1. General Tax Exemption of Bonds

2. Federal Alternative Minimum Tax

3. Deduction for Interest Incurred to Carry Tax-Exempt Bonds

IX RIGHT TO AUDIT

X DEFINITIONS

- Agricultural Improvements

- Agricultural Land

- Beginning Farmer

- Bond Purchaser

- Depreciable Agricultural Property

- Farm

- Farming

- First-Time Farmer

- Indirect Ownership

- Related Person

- Substantial Farmland

CONCLUDING NOTE

PROGRAM SUMMARY

Loans by Lending Institutions

and Contract Sales

or Direct Loans by Investors Other than Lending Institutions

Contact Person(s):

Bonnie Hawkins

(785) 357-4445 telephone

Administrative Assistant

(785) 357-4478 facsimile

bhawkins@kdfa.org Email

THE PROGRAM SUMMARY IN BRIEF

The K DFA Beginning Farmer Loan Program ("Program"), is a tax-exempt bond program authorized pursuant to Section 147 of the Internal Revenue Code, and pursuant to K.S.A. 74-8901 et seq., designed to assist Beginning Farmers in the state of Kansas to acquire agricultural property at lower interest rates. The Program enables lending institutions, individuals, partnerships, corporations, and other entities (herein referred to as the "Bond Purchaser") to receive tax-exempt interest with respect to a direct loan or contract sale made to Beginning Farmers.

The Bond Purchaser, after arranging the loan or sales contract, will obtain from the Kansas Development Finance Authority (the "Authority") a state and federally tax-exempt Bond in the amount of the loan or the unpaid balance on the sales contract. In the case of a loan, the amount paid by the Bond Purchaser for the Bond will be lent to the Beginning Farmer by the Authority, and that loan and its collateral will be assigned to the Bond Purchaser as security for the Bond. In the case of a contract sale, the contract will be entered into by the Authority and the Bond Purchaser will receive the Bond to evidence the Authority's obligations under the contract. The Authority's right, title and interest in the contract will then be assigned to the Beginning Farmer who will assume the payment obligations of the Authority under the contract.

BASIC QUALIFICATIONS:

- May not have previously owned any substantial amount of farmland.
- Program may be used to purchase agricultural land, agricultural improvements, and depreciable agricultural property (new and used).
- The loan maximums under existing federal law are:

- --\$543,800 base cap, indexed annually for inflation for agricultural land, agricultural improvements and depreciable agricultural property
 - Of which no more than \$62,500 may be for used property.
- There is no minimum loan amount for the Program.
 - Beginning Farmer may not cash rent or custom hire a majority of the fieldwork or livestock management to be completed.
 - The Beginning Farmer must be an individual. Loans to corporations, partnerships, LLC's, etc. are not eligible under the Federal Tax Code.

The Bond Purchaser will make a credit evaluation of the Beginning Farmer, may require any collateral deemed necessary and, with the Beginning Farmer, must arrange the terms of the loan or contract. The Bond will be a limited obligation of the Authority, and will be solely secured by the loan or contract and collateral provided by the Beginning Farmer. The Bond Purchaser will be responsible for the creation and perfection of any security interest which the Bond Purchaser deems necessary for the loan or contract.

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

If a sales contract is to be used, the Beginning Farmer must submit an Application with the contract seller as the Bond Purchaser. The Authority shall not be liable for the failure of a Bond Purchaser to perform under the sales contract.

GENERAL

The Kansas Development Finance Authority (K DFA) was created by the 1987 Kansas Legislature to finance capital improvements and improve access to long-term capital financing for state agencies, political subdivisions, public and private non-profit organizations and businesses. K DFA is authorized, subject to certain restrictions, to issue revenue bonds and various other debt instruments for the purpose of financing agricultural business enterprises.

K DFA is governed by a five-member Board of Directors, consisting of **five public members** appointed by the Governor subject to confirmation by the State Senate. The Governor also appoints the K DFA President who serves at the pleasure of the Governor and who is an ex-officio, non-voting member of the Board. Not less than three members of the Board must be representative of the general public, and not more than three members may be members of the same political party. K DFA employs a permanent full-time staff to work with borrowers and finance teams to structure finance transactions and to oversee post-issuance compliance responsibilities. **DEFINITIONS** - The definitions used in the Program are important to Bond Purchasers and Beginning Farmers contemplating using the Program. Please refer to Sections I and X for the definition of the terms used in this Program Summary.

SECTION I

PROGRAM POWERS AND ELIGIBLE ACTIVITIES

The Authority may issue its bonds to assist Beginning Farmers in financing the acquisition of the following:

1. **Agricultural Land** -- The Authority can finance the purchase of land suitable for use in farming.
2. **Agricultural Improvements** -- The Authority can finance the construction or purchase of improvements located on Agricultural Land (which are suitable for use in farming). Examples: Confinement systems for swine, cattle, or poultry; barns and other out-buildings; grain storage facilities; silos; improvements to land such as drainage tile and other soil conservation improvements which could include, but not be limited to, terraces, farm ponds, erosion control structures, waterways, etc. Agricultural Improvements may be new or used and may include additions to or renovation of existing buildings or other structures.

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

3. **Depreciable Agricultural Property** -- The Authority can finance the purchase of personal property suitable for use in farming for which an income tax deduction for depreciation is allowed in computing federal income taxes. Examples: Livestock used for breeding or dairy purposes, farm machinery, trucks, etc. Feeder cattle (including steers), feeder pigs, or feeder lambs do not qualify as depreciable property. Bond proceeds may be used to finance new or used Depreciable Agricultural Property. "Used" livestock are female animals that have been used for breeding purposes. Open or bred heifers, gilts, or lambs would not be considered as "used" property under this definition (this class of animals would be considered "new" property). Male animals that have not yet been used for breeding purposes would be considered as "new" property.
4. **Purchases from Close Relatives** – Purchase of land, improvements or equipment from parents, grandparents, and siblings is allowed so long as the purchase price paid by the Beginning Farmer is fair market value, the Bond Purchaser certifies that the purchase price paid was fair market value, an appraisal is supplied showing the fair market value and the close relative certifies to the Authority that the close relative will not have a financial interest in the Project after the closing. In addition, financing may not be by the use of a sales contract – a loan from a third-party lender must be used.

SECTION II

PROGRAM MAXIMUMS AND MINIMUMS

Federal law sets maximum amounts that may be financed under the Program. The maximums are:

1. No more than a lifetime base aggregate amount per borrower of \$543,800 as indexed for inflation, for Agricultural Land, Agricultural Improvements and Depreciable Agricultural Property.
2. Of the possible \$543,800, no more than \$62,500 can be for "used" property.

3. There is no minimum loan amount for the Program.

SECTION III

NATURE OF INVESTMENT RISK; LIMITED OBLIGATION BONDS

THE BOND PURCHASER MUST MAKE A CREDIT EVALUATION OF THE LOAN OR SALES CONTRACT, THE BEGINNING FARMER'S ABILITY TO REPAY PRINCIPAL AND INTEREST, AND THE SUFFICIENCY OF THE SECURITY FOR THE LOAN OR SALES CONTRACT. THE AUTHORITY WILL NOT MAKE AN INDEPENDENT EVALUATION OF THE BEGINNING FARMER'S ABILITY TO REPAY THE LOAN OR PAY THE CONTRACT. IN SETTING THE TERMS OF THE LOAN OR SALES CONTRACT, THE BEGINNING FARMER AND BOND PURCHASER ARE STRONGLY ENCOURAGED TO CONSULT THEIR LEGAL COUNSEL AND TAX CONSULTANTS.

The Bond Purchaser will be required to execute a letter with respect to the Bond Purchaser's understanding of the Authority's limited obligation on the Bond and the credit risks inherent in purchasing such a Bond.

The principal and interest on the Bond are limited obligations, payable solely out of the revenue derived from the debt obligation or sales contract, collateral, or other security furnished by or on behalf of the Beginning Farmer. A guarantor, letter of credit or alternative credit enhancement on the debt is permissible. A guarantor may be a Related Person. Generally, the Federal Government or any of its agencies cannot guarantee the debt. If a guarantee by an agency of the Federal Government is *being* considered, please contact the Authority. **The Bond, which is issued by the Authority and purchased by the Bond Purchaser, is a non-recourse obligation. The principal and interest on the Bond shall be a limited obligation only of the Authority, and in no event shall the bonds constitute an indebtedness of the State of Kansas or an indebtedness for which the faith and credit or taxing powers of the State of Kansas are pledged.** It should also be noted that any recording, filing or other fees or charges associated with the loan or sales contract will be paid by the Beginning Farmer or Bond Purchaser and not the Authority.

NOTE: In purchases of irrigated land, the Beginning Farmer has the responsibility to notify, in writing, the Division of Water Resources, Kansas State Department of Agriculture, and any applicable Groundwater Management District, of the transfer of land ownership.

SECTION IV

APPLICANT ELIGIBILITY

The basic eligibility requirements for the program are as follows:

1. **Age Limits** -- A Beginning Farmer must be at least age 18 unless he or she has a co-signer who is 18 years or older. There is no upper age limit.
2. **First-Time Farmer** -- All Beginning Farmers must be First-Time Farmers regardless of the purpose of the loan.

3. **Training and Experience** -- The Beginning Farmer must have documented, to the satisfaction of the Bond Purchaser and the Authority, sufficient education, training or experience in the type of farming operation for which the Bond is requested.
4. **Use of Project** -- The Agricultural Land, Agricultural Improvements, and Depreciable Agricultural Property shall only be used for farming by the individual, the individual's spouse, the individual's minor children, or any of them.

SECTION V

INELIGIBLE PROGRAM ACTIVITIES

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

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

In addition, the Beginning Farmer shall not make any expenditures with respect to the acquisition or construction of any part of the Project prior to the date which is 60 days prior to the date on which the Authority approves the Program Application. To do so runs a risk that the IRS would deem the bond transaction a refinancing. **Tax-exempt bond proceeds may not be used for the purpose of refinancing.**

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

SECTION VI

APPLICATION AND PROCEDURES - DIRECT LOANS

(NOTE: Section VI applies to transactions involving a direct loan made by the Bond Purchaser to the Beginning Farmer. If the Beginning Farmer is purchasing the project on a sales contract from the Bond Purchaser, Section VI should be disregarded and Section VII should be followed.)

A Beginning Farmer and Bond Purchaser must prepare and submit a joint application to the Authority. The following should be noted:

1. **Application Forms** -- Application forms are available from the Authority. The Application should be completed by the Beginning Farmer and the Bond Purchaser and submitted directly to the Authority. Applicants are encouraged to contact the Authority staff if they have questions in completing the Application.

A letter must be submitted with the application to explain the Beginning Farmer's background with respect to his or her education and experience in the type of farming operation for which a loan is sought. The letter should also outline the Beginning Farmer's access to machinery, if the loan is for land; or his or her access to land, if the loan is for Agricultural Improvements or Depreciable Agricultural Property. The letter should also state where the Beginning Farmer will obtain operating capital and interim financing if necessary.

2. **Application Period** -- A completed Application will be reviewed and considered by the Authority within five business days of its receipt.

3. **Interim Financing** -- As noted in Section V, a Beginning Farmer must not make any expenditure with respect to the acquisition or construction of any part of the Project to be financed with the proceeds of the Bond prior to the date which is 60 days prior to the date the Authority approves the Application; if this were to occur, the bond transaction could be deemed a refinancing. However, once the Application has been approved, the Project may move forward with either construction or possession and, if necessary, the Bond Purchaser or another lender may interim finance the loan prior to bond issuance. The interim financing will be paid with the proceeds of the Bond when issued.

4. **Loans to Beginning Farmers and Security Arrangements** -- The Program involves the Bond Purchaser, Beginning Farmer, and the Authority. If the Bond Purchaser is making a loan to the Beginning Farmer, the financing is accomplished as follows: In simultaneous transactions the Bond Purchaser purchases the Bond from the Authority; the Authority makes the loan to the Beginning Farmer from the proceeds of the Bond sale; and the Authority assigns the promissory note it receives from the Beginning Farmer to the Bond Purchaser as security for the Bond.

- 1) Bond purchased by Bond Purchaser from the Authority;
- 2) Bond proceeds lent by Authority to Beginning Farmer;
- 3) Beginning Farmer gives promissory note to Authority;
- 4) Promissory note assigned to Bond Purchaser as security for the Bond;
- 5) Beginning Farmer makes loan payments to Bond Purchaser.

5. **Terms of Loan** -- The Beginning Farmer and Bond Purchaser must agree on terms of the loan: interest rate (fixed or variable), length of loan, prepayment or call options, service fees and repayment schedule.

6. **Repayment of Loans** -- Under the Authority's bond documents, the Beginning Farmer's payment obligations are subject to mandatory prepayment in the event the interest income on the Bond becomes includable in gross income for purposes of federal income taxation, in the event that the loan agreement entered into by the Beginning Farmer becomes void or enforceable, and to the extent any bond proceeds remain following completion of the acquisition or construction of the Project. In addition, the documents provide for optional prepayment from insurance or condemnation proceeds (at

the discretion of the Bond Purchaser) in the event of damage, destruction or condemnation of all or any part of the Project.

The documents also provide for prepayment at the option of the Beginning Farmer, the terms and conditions of which are to be agreed upon between the Beginning Farmer and the Bond Purchaser.

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

7. **Assignment or Sale of Bonds** -- The Authority does not place any restrictions on a Bond Purchaser's ability to participate out, assign or sell a bond issued under the Program. Generally, Bond Purchasers participating in the Program purchase the Bond for their own investment and do not anticipate assigning the Bond to another investor. It should be noted there are laws that prevent certain sales and participations or at least seriously restrict them. For example, the Kansas Securities Act may impose certain restrictions or requirements if the Bonds are sold to investors other than financial institutions. In addition, there are adverse tax consequences if the Bond is assigned, participated out or sold to a "Related Person" of the Beginning Farmer. Therefore, a Bond Purchaser should consult with legal counsel to determine if any of these laws or regulations will be violated before selling, assigning, or participating out a bond.

The bond documents allow a Bond Purchaser to assign a loan in whole or in part to any person. The Authority must be notified in writing prior to assignment of the loan.

8. **Fees** -- The Beginning Farmer or Bond Purchaser must pay to the Authority a non-refundable \$100 application fee (submitted with the Application). A bond closing fee equal to 1 1/2 % of the amount of the Bond, but not less than \$500, must be paid by the Beginning Farmer or Bond Purchaser at closing. The bond closing fee and other closing costs, up to 2% of the Bond amount, may be financed with bond proceeds.

The Authority's bond counsel will review each Bond for legality and tax exemption. Bond Counsel will submit a bill at closing and the Beginning Farmer will be required to pay the Bond Counsel directly as a portion of the bond closing fee.

9. **Use of Financial and Security Documents** -- The Bond Purchaser should use forms of financial statements and security documents which the Bond Purchaser believes are necessary and appropriate under the particular loan circumstances. These items should be referenced in the bond documents and their provisions incorporated therein. Any additional requirements not specifically provided for in the bond documents, such as insurance coverage and amounts, should also be added.

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

TO A PARTICULAR PROJECT AND IS NOT RESPONSIBLE FOR THE FILING OR RECORDING OF ANY SECURITY DOCUMENTS.

10. **Bond Purchasers** -- Any lending institution, individual, corporation, government or governmental subdivision or agency, business trust, estate, trust, partnership or association, or any other legal entity, may be a Bond Purchaser for contract sales and direct loans.

11. **Procedures Following Bond Issuance** -- Following disbursement of the bond proceeds, the Bond Purchaser and Beginning Farmer must certify to the Authority that all of the proceeds were used by a qualified Beginning Farmer for a qualified purpose.

12. **Timing Requirements for Spending Bond Proceeds** -- Federal tax law restrictions generally do not permit the investment of bond proceeds in securities, which bear a higher interest rate than the Bond.

Under the current rules, the period of time during which bond proceeds may be invested in an unrestricted yield has been effectively shortened to eighteen months. The "Gross Proceeds" of a tax-exempt Bond must be spent on the project being financed in accordance with the following schedule: (i) 15% within 6 months, (ii) 60% within 12 months, and (iii) 100% within 18 months. If the proceeds are not spent in accordance with such schedule, the parties to the bond issue will be subject to some very onerous federal reporting requirements and will be required to pay any profits earned on bond proceeds to the federal government.

It should be noted the "Gross Proceeds" of a Bond include more than the original principal proceeds. Also included are any amounts earned on the investment of bond proceeds: funds, securities or other obligations (such as a certificate of deposit), which are pledged as security for the payment of the Bond.

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

13. **Assumption of Loans - Substitution of Collateral and Transfer of Property** -- Loans may not be assumed without the prior approval of the Authority, and then only if the purchaser of the property will qualify as a First-Time Farmer. Equipment and other depreciable property may be exchanged or traded in on similar property, and other property such as breeding livestock may be added or substituted as collateral at the discretion of the Bond Purchaser without the prior approval of the Authority. The benefits of the Authority Bond must remain with a qualified First-Time Farmer, and no person to whom property is traded or otherwise transferred may obtain the benefits of the Bond.

14. **Public Hearing and Governor's Approval of Bond Issuance** -- In compliance with state law, the Authority must notify the city or county in which the Project is located, no less than 30 days before the closing, that it intends to provide the financing. The local government may stop the financing by adopting a resolution or ordinance disapproving the Project within 15 days of the giving of the notice by the Authority. Federal law requires the Authority to hold a public hearing on the issuance of the Bond before the closing, public notice of which will be published at least 14 days in advance in a regional newspaper of general circulation in the city or county in which the Project is located. State law requires the Authority to publish notification of the issuance of bonds 14 days prior to any bond hearing in the official county newspaper where such bonds will be used

and in the *Kansas Register*. The Authority will hold hearings and approve all financing documents at their monthly board meeting. Once the Board has approved the documents, a bond closing can be scheduled.

Generally, these public hearings will be conducted by the Authority in conjunction with its monthly meeting. However, on some occasions authorized Authority staff may conduct the hearings. A hearing need not be held prior to an Application being approved, but it must be held before the bond documents are approved.

The Governor of Kansas, after receiving a report on the results of the public hearing, may then approve or disapprove the Bond. In addition to the hearing process described above, an allocation of the State's Volume Cap must be received from the Kansas Department of Commerce and Housing before the Bond may proceed to closing.

15. **State Volume Cap Limitations** -- The federal tax law establishes a limit on the total principal amount of tax-exempt Private Activity Bonds, which may be issued within any state during a calendar year (the "Volume Cap"). All Authority bonds issued for this program are subject to the limitation. The Kansas Legislature has established a procedure to allocate the Volume Cap among bond issuers. The procedure for the allocation is set forth in the Kansas Private Activity Bond Allocation Act. The Authority will process the necessary paperwork to receive an allocation from the state Volume Cap. If an allocation from the Volume Cap is not available for a particular Bond, the Bond Purchaser and the Beginning Farmer will be so advised.

16. **Modified Accelerated Cost Recovery System Limitations -- Bond Purchasers and Beginning Farmers should be aware that federal law limits the application of the Modified Accelerated Cost Recovery System (MACRS) with respect to facilities financed with the Authority's bonds.** If an item is financed with the proceeds of a Bond, the Beginning Farmer must use an alternate MACRS method where deductions are computed by applying the straight line method, the applicable averaging convention, and the applicable longer recovery period for such item (12 years for personal property with no class life, 40 years for real property, and the class life for all other property).

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

17. **Maximum Loan Maturity** -- Federal law provides that the weighted average maturity of an Authority bond can be no more than 120% of the average reasonably expected economic life of the project being financed with proceeds of the Bond (except land).

SECTION VII

APPLICATION AND PROCEDURES - SALES CONTRACTS

(NOTE: Section VII applies to transactions involving a sales contract from the Bond Purchaser (the seller) to the Beginning Farmer (the buyer). This section should be disregarded if the Bond Purchaser is making a direct loan to the Beginning Farmer and Section VI should be followed.)

A Beginning Farmer and Bond Purchaser must prepare and submit an Application jointly to the Authority. The following should be noted:

1. **Application Forms** -- Application forms are available from the Authority. The Application should be completed by the Beginning Farmer and the Bond Purchaser and submitted to the Authority. Applicants are encouraged to contact the Authority staff if they have questions in completing the Application.

A letter must be submitted with the application to explain the Beginning Farmer's background with respect to his or her education and experience in the type of farming operation for which a Bond is sought. The letter should also outline the Beginning Farmer's access to machinery, if the sales contract is for [agricultural land](#); or his or her access to land, if the sales contract is for Agricultural Improvements and Depreciable Agricultural Property. The letter should also state where the Beginning Farmer will obtain operating capital and interim financing if necessary.

2. **Application Period** -- There is no formal or defined application period because the Program is ongoing. A completed Application will be reviewed and considered by the Authority within five business days of its receipt.
3. **Sales Contracts and Security Arrangements** -- The Program involves the Bond Purchaser, Beginning Farmer, and the Authority. After an Application has been submitted and approved, the Bond Purchaser and the Authority will enter into a sales contract and the Bond Purchaser will receive a Bond to evidence the Authority's obligations under the contract. The Authority's right, title, and interest in the contract will then be assigned to the Beginning Farmer, who will assume the payments and other obligations of the Authority under the contract.
4. **Terms of the Sales Contract** -- The Beginning Farmer and Bond Purchaser will negotiate the terms of the sales contract. They must agree on terms such as purchase price, interest rate (fixed or adjustable), payment schedule, down payment, prepayment rights and obligations, security, insurance coverage, payment of taxes, defaults and remedies on default.

It must be clearly stated in the sales contract as to the portion of the payments constituting principal and the portion constituting interest.

In addition to other terms the Beginning Farmer and Bond Purchaser may include in the sales contract, **THE FOLLOWING TERMS MUST BE INCLUDED:**

- (1) This contract will be assigned by the Contract Buyer (the Authority) to (the Beginning Farmer(s)) and may not be reassigned by Beginning Farmer(s) without the written consent of Seller(s) and the Authority, which consent, if given, shall not operate as a waiver of the requirement of written consent on any subsequent assignment. Any attempt by Beginning Farmer(s) to reassign this contract without written consent shall entitle Seller(s) to declare all amounts due hereunder immediately due and payable.
- (2) To evidence its payment obligations under this contract, the Authority will issue its tax-exempt Bond (the "Bond") in an amount equal to the unpaid balance of the purchase price contained herein and bearing interest at the rate of per annum (the "Tax Exempt Rate") with payment terms identical to those contained herein. Beginning Farmer(s) have expressly warranted to Seller(s) that the interest payments received pursuant to the terms contained herein will come to the Seller(s) in the form that will make it not includable in gross income for federal income tax purposes. Seller(s) are relying on the representations made by the Beginning Farmer(s) in this regard and in the event the interest payments are determined to be includable in gross income for federal income tax purposes, then all interest payments will be computed on the basis of interest at the rate of per annum (the "Taxable Rate") and Beginning Farmer(s) shall be responsible to make payment to the Seller(s) for the difference between interest paid at the Tax Exempt Rate and the amount calculated on the basis of interest at the Taxable Rate. This provision shall not apply in the event a Related Person (as defined by the Internal Revenue Code) to the Beginning Farmer (s) holds the Bond.

NOTE: The above provision may be modified if an adjustable interest rate is used.

(3) The Seller(s) acknowledges that this contract will be assigned by the Authority by separate instrument, the Guarantee, Assignment and Assumption Agreement (the "Guarantee") to the Beginning Farmer(s) who will assume the rights, duties, obligations and liabilities of the Authority hereunder and guarantee the payment of principal and interest on the Bond. Seller(s) approves such assignment and assumption and acknowledges that the principal of, premium, if any, and interest on the Bond, the installment payments under this contract and other amounts due and owing to the Seller(s) as holder of the Bond and seller under this contract are special limited obligations of the Authority and, in no event, shall the Bond or this contract constitute an indebtedness of the State of Kansas or indebtedness for which the faith and credit or taxing powers of the State of Kansas are pledged.

5. **Payments Under the Sales Contract** -- The Beginning Farmer's payment obligations and rights and obligations to prepay principal and interest under the sales contract shall be determined by the Beginning Farmer and Bond Purchaser and included in the sales contract.

6. **Assignment or Sale of Bonds** -- The Authority does not place any restrictions on a Bond Purchaser's ability to participate out, assign or sell a bond issued under the Program. Generally, the Bond Purchaser participating in the Program purchases the Bond for the Bond Purchaser's own investment and does not anticipate assigning the Bond to another investor. It should be noted there are laws that prevent certain sales and participations, or at least seriously restrict them. For example, the Kansas Securities Act may impose certain restrictions or requirements if the Bonds are sold to investors other than financial institutions. In addition, there are adverse tax consequences if the Bond is assigned, participated out, or sold to a "Related Person" of the Beginning Farmer. Therefore, a Bond Purchaser should consult with legal counsel to determine if any of these laws or regulations will be violated before selling, assigning or participating out a Bond.

The bond documents allow a Bond Purchaser to assign a loan in whole or in part to any person. The Authority must be notified in writing prior to assignment of the loan.

7. **Fees** -- The Beginning Farmer or Bond Purchaser must pay to the Authority a non-refundable \$100 application fee (submitted with the Application). A bond closing fee equal to **1 1/2%** of the amount of the Bond, but not less than \$500, must be paid to the Authority by the Beginning Farmer or Bond Purchaser at closing. The bond closing fee and other closing costs, up to 2% of the Bond amount, may be included in the purchase price reflected in the sales contract.

The Authority's bond counsel will review each Bond for legality and tax exemption. Bond Counsel will submit a bill at closing and the Beginning Farmer will be required to pay the bond counsel directly as a portion of the bond closing fee.

8. **Use of Financial and Security Documents** -- The Bond Purchaser should use forms of financial statements and security documents that the Bond Purchaser feels are necessary and appropriate under the particular sales contract circumstances.

BOND PURCHASERS PLEASE NOTE: IT IS THE BOND PURCHASER'S RESPONSIBILITY TO INSURE THAT ANY SECURITY AGREEMENTS, GUARANTEES OR OTHER SECURITY DOCUMENTS, WHICH THE BOND PURCHASER REQUIRES IN A TRANSACTION, HAVE BEEN COMPLETED AND SIGNED, AND THAT ANY FINANCING STATEMENTS HAVE BEEN FILED, DOCUMENTS RECORDED, TRANSFER OR OTHER TAXES PAID, OR ANY OTHER NECESSARY STEPS TAKEN TO PROTECT THE BOND PURCHASER'S INTERESTS. THE AUTHORITY MAKES NO WARRANTIES OR REPRESENTATIONS WITH RESPECT TO THE EFFECTIVENESS, VALIDITY OR PRIORITY OF ANY LIENS OR SECURITY INTERESTS WHICH A BOND

PURCHASER HAS WITH RESPECT TO A PARTICULAR PROJECT AND IS NOT RESPONSIBLE FOR THE FILING OR RECORDING OF ANY SECURITY DOCUMENTS.

The Authority also advises that any security documents or guarantees required to be delivered in connection with the sales contract clearly state that they are given as additional security for the indebtedness under the sales contract and to further secure the agreements, covenants and obligations of the Beginning Farmer contained in the sales contract. The security documents and any guarantees should run directly between the Beginning Farmer and the Bond Purchaser.

9. **Bond Purchasers** -- Any lending institution, individual, corporation, government or governmental subdivision or agency, business trust, estate, trust, partnership or association, or any other legal entity may be a Bond Purchaser for contract sales and direct loans.

10. **Loan and Sales Contract** -- In the event the Bond Purchaser will make a loan to the Beginning Farmer (e.g., for Depreciable Agricultural Property) as well as enter into a sales contract with the Beginning Farmer, both of which are to be financed with an Authority bond, it will be necessary for the transaction to comply with the requirements of Section VI and Section VII of this Program Summary.

11. **Assumption of Sales Contract - Substitution of Collateral and Transfer of Property** - The sales contract may not be assumed without the prior approval of the Authority, and then only if the purchaser of the property will qualify as a First-Time Farmer. Equipment and other depreciable property may be exchanged or traded in on similar property, and other property such as breeding livestock may be added or substituted as collateral at the discretion of the Bond Purchaser without the prior approval of the Authority. The benefits of the sales contract must remain with a qualified First-Time Farmer, and no person to whom property is traded or otherwise transferred may obtain the benefits of the Bond.

12. **Public Hearing and Governor's Approval of Bond Issuance** -- In compliance with state law, the Authority must notify the city or county in which the Project is located, no less than 30 days before the closing, that it intends to provide the financing. The local government may stop the financing by adopting a resolution or ordinance disapproving the Project within 15 days of the giving of the notice by the Authority. Federal law requires the Authority to hold a public hearing on the issuance of the Bond before the closing, public notice of which will be published at least 14 days in advance in a newspaper of general circulation in the city or county in which the Project is located. State law requires the Authority to publish notification of the issuance of bonds 14 days prior to any bond hearing in the official county newspaper where such bonds will be used and in the *Kansas Register*. The Authority will hold hearings and approve all financing documents at their monthly board meeting. Once the Board has approved the documents, a bond closing can be scheduled.

13. **Modified Accelerated Cost Recovery System Limitations** -- **Bond Purchasers and Beginning Farmers should be aware that federal law limits the application of the Modified Accelerated Cost Recovery System (MACRS) with respect to facilities financed with the Authority's bonds.** Beginning Farmers should contact their tax consultant regarding the specific effect this change in the MACRS will have on their operations and Project. For a discussion of the MACRS limitations, see paragraph 16 in Section VI of this Program Summary.

14. **Maximum Terms of Sales Contract** -- Federal law provides that the weighted average maturity of an Authority bond can be no more than 120% of the average reasonably expected economic life of the Project being financed with the proceeds of the Bond. (There is no maximum for land.)

SECTION VIII

FEDERAL TAX EXEMPTION OF AUTHORITY BONDS

1. **General Tax Exemption of Bonds** -- Under federal tax law an Authority bond is classified as a Qualified Small Issue Bond. Therefore, if all the provisions of the state and federal law continue to be complied with by the Beginning Farmer and Bond Purchaser, the interest on an Authority bond will not be included in the Bond Purchaser's gross income for federal income tax purposes. In addition, interest on the Authority bond will be exempt in the State of Kansas from all state, county and municipal taxes, including income, inheritance and property taxes; except that such interest will be included in the calculation of "Net Income" for purposes of computing the Privilege Tax imposed by sections of K.S.A. 79-1107 and 79-1108.

2. **Federal Alternative Minimum Tax** -- Notwithstanding the preceding paragraph, interest on Authority bonds, which is otherwise tax-exempt, shall be directly includable in the calculation of a bondholder's "alternative minimum taxable income" under Section 57(a)(5) of the Internal Revenue Code of 1986. Pursuant to the American Recovery and Reinvestment Act of 2009, during 2009 and 2010, interest on private activity bonds, including Beginning Farmer bonds, is not taken into account in determining adjusted current earnings for the purpose of the computing the alternative minimum tax.

3. **Deduction for Interest Incurred to Carry Tax-Exempt Bonds** -- The Authority bonds are NOT "qualified tax-exempt obligations" within the meaning of Section 265(c)(3) of the Internal Revenue Code of 1986. Accordingly, financial institutions will not be allowed any deduction for that portion of the financial institutions interest expense which is allocated by law to the purchasing or carrying of the Authority's bond.

NOTE: The effects of the taxes and deductions discussed above will vary with each Bond Purchaser and, with a given Bond Purchaser, from year to year. Bond Purchasers should consult their tax consultants as to the specific effects of these provisions in their case.

SECTION IX

RIGHT TO AUDIT

The Authority shall have, at any time, the right to audit or monitor records of the Bond Purchaser and the Beginning Farmer relating to a bond to insure a qualified user used the bond proceeds for qualified purposes.

SECTION X

DEFINITIONS

"Agricultural Improvements" As defined in Section I, (2) of this Program Summary.

"Agricultural Land" As defined in Section I, (1) of this Program Summary.

"Beginning Farmer" An individual that engages in farming or ranching or wishes to engage in farming or ranching and qualifies as a first time farmer.

"Bond Purchaser" Any lending institution, individual, corporation, business trust, estate, trust, partnership or association, or any other legal entity, that is the purchaser of an Authority bond under the Program in connection with a contract sale or loan to a Beginning Farmer.

"Depreciable Agricultural Property" As defined in Section I, (3) of this Program Summary.

"Farm" A farming enterprise that is recognized in the community as a farm rather than a rural residence. The term "farm" includes stock, dairy, poultry, fruit, fur-bearing animal, and truck farms, plantations, ranches and all lands used for farming, orchards, ranges, fish farms, nurseries, greenhouses or other similar structures used primarily for the raising of agricultural or horticultural commodities.

"Farming" The cultivation, operation or management of a farm.

"First-Time Farmer" An individual who has never had any direct or indirect ownership interest in substantial farmland in the operation of which he or she has materially participated. Ownership interest or material participation by an individual's spouse or minor child will be attributed to the individual, as well.

However, the federal tax law also provides that an individual's prior ownership interest in farmland will be disregarded if:

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

"Indirect Ownership" If an individual holds a minimal interest in a family farm corporation, a limited partnership, a trust, or any other type of entity which in turn owns substantial farmland, and the individual materially participates in the operation of such farmland, then the individual will not qualify as a First-Time Farmer.

"Related Person" According to the IRS, includes grandfather, grandmother, father, mother, brother or sister (whether whole or half blood), child, grandchild, or spouse. It also includes certain corporations and partnerships.

"Substantial Farmland" is any parcel of land unless the parcel is smaller than 30 percent of the median size of a farm in the county where the parcel is located.

CONCLUDING NOTE: The Authority recognizes some of the provisions in this Program Summary may be confusing to the Beginning Farmer or Bond Purchaser. The Authority will provide whatever assistance it can in answering questions or completing documents. All information is available in other formats if necessary. Beginning Farmers and Bond Purchasers are encouraged to visit with the Authority staff early in the application process to make the entire transaction as simple as possible. The Authority's telephone number is (785) 357-4445.

After the Authority has approved the application, a set of documents (including a promissory note) will be sent for completion by the Beginning Farmer and Bond Purchaser. Following completion of these materials and upon receipt of those materials by the Authority, the bond documents will be prepared by the Authority staff for signatures of the Beginning Farmer and Bond Purchaser.