Modernizing Agricultural and Manufacturing Bonds Act (MAMBA)

The **Modernizing Agricultural and Manufacturing Bonds Act (MAMBA)** is a common-sense, bipartisan, targeted reform package that will modernize two categories of qualified small issue private activity bonds: Small Issue Manufacturing Bonds (more commonly known as **Industrial Development Bonds** (**IDBs**)), and First-Time Farmer Bonds (also called **Agricultural Bonds**, or simply **Aggie** Bonds). These types of bonds are key economic development tools used by state and local agencies to finance the small- to mid-sized manufacturing and agricultural sectors.

Unfortunately, IDBs and Aggie Bonds have not been modernized in over 30 years, causing stagnation and decline in these respective industries. Over the past decade, IDB and Aggie Bond issuances have substantially declined due in major part to the outdated rules and regulations that govern the use of these bonds. The six reforms contained within MAMBA will update the Internal Revenue Code (IRC)'s private activity bond rules for IDBs and Aggie Bonds. The six reforms are as follows:

1. Expand the definition of "manufacturing facility"
2. Eliminate restrictions on "directly related and ancillary facilities"
3. Increase the maximum IDB size limitation from $10 million to $30 million
4. Increase the limitation on small issue bond proceeds for first-time farmers
5. Repeal the separate dollar limitation on the use of small issue bond proceeds for depreciable property
6. Modify the definition of "substantial farmland"

Reform 1 – Expand the definition of "manufacturing facility"

Current federal law defines a "manufacturing facility" as one that produces tangible property. However, manufacturing processes, production, and technology have changed significantly since this definition was established. Today's manufacturers encompass more modern, high-tech, and intangible manufacturing practices such as bio-technology, energy generation, food processing, software, design and formula development, and intellectual property. CDFA proposes expanding the definition of manufacturing, which would enable small issue manufacturing bonds to support manufacturers that produce software, patents, copyrights, formulas, processes, designs, patterns, know-how, format, and similar intellectual property. The expanded definition would align the growing high-tech manufacturing sector with the tools necessary to finance industry growth and expansion, making an immediate impact nationally on job creation and manufacturing investment.

Reform 2 – Eliminate restrictions on "directly related and ancillary facilities"

The current usage of small issue manufacturing bonds is limited to the financing of facilities that house the production of tangible property, and that are directly related and ancillary to a manufacturing facility. A directly related and ancillary facility is defined as being located on the same

site as the manufacturing facility, and not more than 25 percent of the net proceeds of a bond issuance can be used to provide such facilities. Facilities such as offices, locker rooms, and cafeterias are deemed "directly related and ancillary facilities" and thus are limited to a 25% use of net bond proceeds requirement. While a sound idea in theory, in practice the restriction on financing directly related and ancillary facilities has hindered the use of the tool for small-to-mid-sized manufacturers. Eliminating financing restrictions on directly related and ancillary facilities, and allowing manufacturing bonds to finance all facilities that are functionally related and subordinate to a manufacturing facility, will significantly improve the usability of the tool.

Reform 3 – Increase the maximum IDB size limitation from $10 million to $30 million

The decision to increase the maximum bond size limitation from $10 million to $30 million is based on several issuer and industry surveys conducted by the Council of Development Finance Agencies. Issuers in every U.S. state have informed CDFA that most projects demand a total issuance amount of between $15 and $30 million. The $10 million limit on bond issuance is forcing many issuers to forgo the financing of worthwhile projects, hurting local economies. Additionally, in today's terms the $10M bond size limit that was established in 1979 has less than a third of the financing power that it had when the limit was set in 1979. Increasing the maximum bond size limit to $30 million would remedy the problem of reduced financing power.

Reform 4 – Increase the limitation on small issue bond proceeds for first-time farmers

The IRC provides that no more than 25 percent of bond proceeds may be spent on land acquisitions, and that no portion of bond proceeds may be used for the acquisition of land for farming purposes. However, the IRC provides an exception to this rule for land acquisitions by first-time farmers. The IRC states that the maximum issuance amount that can be used for farming purposes is $450,000. The $450,000 amount was set in 2007 and indexed to inflation. The proposed increase to $552,500 would bring the total issuance amount stated in the IRC in line with the current issuance limitation.

Reform 5 – Repeal the separate dollar limitation on the use of small issue bond proceeds for depreciable property

First-time farmers that gain access to small issue bond proceeds can currently only use $62,500 of those proceeds for used depreciable property and $250,000 for existing buildings, farm improvements, and/or new depreciable agricultural property. Given the numerous restrictions that already apply to the usage of small issue bonds by first-time farmers, the separate dollar limitation is overly restrictive and has turned-off many would be farmers to the agriculture industry. By eliminating the separate dollar limitation, first-time farmers would have the freedom to use the entire $552,500 issuance for farming equipment, breeding livestock, and other capital assets essential to farming operations.

Reform 6 – Modify the definition of "substantial farmland"

The 2014 Farm Bill changed the ownership limitation of a qualified beginning farmer to someone whose land ownership does not exceed 30 percent of the *average* acreage in a given county. Previously, the ownership limitation was defined as land ownership not exceeding 30 percent of the

median county acreage. For reasons explained in the following paragraph, the change from median to average is beneficial to beginning farmers. However, the IRC still defines first-time farmers (equivalent to beginning farmers) as individuals owning less than 30 percent of the *median* county acreage. Most loans to first-time farmers combine the proceeds of a small issue bond issuance with a loan from the USDA Farm Services Agency (FSA), yet the 2014 Farm Bill changed how the FSA defines beginning farmers. The differing definitions impedes the ability of lenders to combine small issue bonds with FSA loans, limiting the availability of affordable capital for first-time farmers. By bringing the IRC land ownership definition in line with the FSA definition, small issue bonds can once again become a usable financing tool for first-time farmers.

Alongside the obvious need for technical alignment between the FSA and IRC definitions, the rapid growth of hobby farms (small farms operated for pleasure rather than for primary income) over the last decade strengthens the argument for changing the IRC definition of substantial farmland. The rapid growth of hobby farms has skewed the median size of substantial farmland downward, making it harder for first-time farmers to access small issue bonds. Changing the definition of substantial farmland to 30 percent of the *average* size instead of median would correct this problem. The enormous size of certain industrial farms (ranging from several hundred to several thousand acres) will generally skew the definition of substantial farmland upward, so long as the average size is used instead of median size.

MAMBA's Impact on Rural Development

Over the past several decades the average age of principal farm operators in the U.S. has steadily increased, with more than 31 percent of principal operators identifying as 65 or older in a 2012 study.[1] While an aging farm workforce is partly attributable to the decline of the foreign-born farm laborer population, as well as the drop off in family farm succession planning (where family members raised in farming do not build a career in farming), a primary driver behind the aging workforce is the inability of new farmers to access land and capital. The USDA reports that farmland values have been increasing since 2000, with farm real estate values in the Corn Belt more than twice the national per-acre average in 2018.[2] For many aspiring young farmers, the cost of purchasing the land and equipment necessary is prohibitively high, forcing them to look elsewhere for jobs and careers. Declining interest and participation in farming hurts the rural economy, and eliminates job opportunities for rural citizens that depend on the availability of labor-intensive jobs for income. By improving the usability of small issue bonds for first-time farmers, Congress can take a meaningful step forward in supporting the rural economy by improving an established financing tool that offers low-cost, flexible capital.

[1] Economic Research Service, United States Department of Agriculture. "Beginning Farmers and Age Distribution of Farmers." Last modified April 26, 2019. https://www.ers.usda.gov/topics/farm-economy/beginning-disadvantaged-farmers/beginning-farmers-and-age-distribution-of-farmers/

[2] Economic Research Service, United States Department of Agriculture. "Farmland Value." Last modified September 6, 2018. https://www.ers.usda.gov/topics/farm-economy/land-use-land-value-tenure/farmland-value/

Manufacturing is of nearly equal value to the rural economy as farming/agricultural production, with manufacturing jobs offering higher earnings than both agriculture and mining. According to the USDA, manufacturing jobs totaled 2.5 million in 2015 whereas farm jobs totaled 1.4 million. By extension, manufacturing earnings make up 21 percent of rural private nonfarm earnings.[3] Unfortunately, despite the importance of the manufacturing sector to the rural economy, the industry has been in near constant decline since 2000. Competition from overseas, the advance of manufacturing technology, and the rural-to-urban population shift have each contributed to the decline of the rural manufacturing sector. In an effort to counteract the decline, Congress should pass the Modernizing Agricultural and Manufacturing Bonds Act, which contains specific reforms to manufacturing bonds that would aid the rural economy. Research suggests that financing manufacturing plant development in rural areas is an essential step in sustaining the manufacturing sector, and the reforms outlined in MAMBA would dramatically improve the ability of bond issuers to support plant/facility development.

MAMBA's Connection to Opportunity Zones

Although the basic incentive to invest in an Opportunity Zone is the same across all U.S. cities, states, regions, and territories, some Opportunity Zones have a clear strategic advantage in attracting Opportunity Fund investments over others. For example, Opportunity Zones located in urban areas that are already experiencing economic growth will have an advantage in attracting equity investments from Opportunity Funds over Opportunity Zones located in more depressed areas. As the most valuable piece of the Opportunity Zones incentive is the permanent exclusion on Opportunity Fund gains over 10 years from taxes, smart investors will look to make their investments in areas that will generate the largest gains. More often than not, the largest gains will be found in the Zones that are already experiencing economic growth and that have the best long-term economic indicators. While competition between OZs is an unavoidable – and often desirable – consequence of market-driven incentives, additional economic development tools will be needed to maintain some competitive balance between the more relatively prosperous OZs and their most highly-distressed counterparts.

The Modernizing Agricultural and Manufacturing Bonds Act can help alleviate the competitive imbalance between Opportunity Zones by strengthening an already widely used economic development tool – Small Issue Bonds – for supporting small manufacturers and first-time farmers. Smaller communities that lack investment-ready projects will need to do more work to position themselves for Opportunity Fund investments. By improving the usability of Small Issue Bonds, communities around the country can get projects off the ground in struggling Opportunity Zones and create more viable investment opportunities for fund managers. Agricultural bonds for first-time farmers can be used to support the purchase of land in rural Opportunity Zones, which could then be used in the development of industrial agriculture production centers. Similarly,

[3] Sarah A. Low, Economic Research Service, United States Department of Agriculture. *Rural Manufacturing Survival and Its Role in the Rural Economy*. October, 2017. https://www.ers.usda.gov/amber-waves/2017/october/rural-manufacturing-survival-and-its-role-in-the-rural-economy/

manufacturing bonds can be used to purchase vacant or abandoned buildings in Opportunity Zones, which then can be converted into facilities or warehouses for the production of tangible and/or intangible goods. In either scenario, modernized Small Issue Bonds could be used to create investment opportunities for Opportunity Funds where none previously existed.