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STATEMENT ON

PROPOSED AMENDMENTS
TO THE
UNITED STATES BANKRUPTCY CODE

PRESENTED TO

COMMITTEE ON THE JUDICIARY
SUBCOMMITTEE ON ADMINISTRATIVE PRACTICE AND PROCEDURE
AND
SUBCOMMITTEE ON COURTS
UNITED STATES SENATE

BY

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Room SD-226, Dirksen Senate Office Building
November 12, 1985
10:00 a.m.

Mr. Chairman and members of the Subcommittees, the FDIC appreciates the opportunity to appear before you to discuss the proposed changes in the bankruptcy statute. I am Steven A. Seelig, Associate Director of the FDIC's Division of Liquidation. Accompanying me this morning is Thomas A. Rose, Assistant General Counsel for Bankruptcy in our Legal Division.

The FDIC is acutely aware of the problems facing this nation's farmers from two different but related perspectives. In our capacity as insurer of the deposits in the nation's commercial banks and as federal regulator for state non-member banks, we are concerned that the banking system remain sound and profitable. We are also directly involved in the problems of the nation's farmers in our capacity as receiver of failed banks. As receiver, the FDIC "steps into the shoes" of the failed bank and becomes a creditor of a farmer or other borrower of the failed bank. In this capacity we have had first hand experience dealing with the problems being confronted by farmers and other businesses involved in agriculture. While these problems are complex and varied, the legislation being considered by the Committee represents a piecemeal attempt at relieving farmers' financial problems.

The liberalization of the Bankruptcy Code for the benefit of family farmers clearly will have a detrimental effect on creditors while not granting the debtors the assistance they need. It must be recognized that the agricultural financial system in this country has many players. Aside from those organizations affiliated with the farm credit system, commercial banks, numerous small businesses, equipment dealers and manufacturers, as well as others, provide credit to farmers. Any increase in the number of farm bankruptcies generated by the proposed changes will adversely affect these creditors. While larger financial institutions may be able to withstand these changes, the potential implication for a feed store, hardware dealer, and other small businessman who typically provides trade credit to farmers may be significant. The resulting financial problems faced by other merchants will further exacerbate the problems confronted by banks serving agricultural communities.

As of the end of June, there were 3,909 agricultural banks in this country. These are banks with 25% or more of their loan portfolio invested in agriculture. Of these banks, 406 are on the FDIC's problem bank list, representing 37% of the total number of problem banks in this country. To put this into a different perspective, of the 98 banks that have failed as of November 1, 1985, fifty percent were agricultural banks. The FDIC is clearly concerned with the viability and condition of these banks. The proposed changes to the Bankruptcy Code will impact these banks, making it more difficult for them to achieve collections on their credits and further cloud the value of underlying collateral.

The singling out of "family farmers" for special treatment within the bankruptcy statute because of their current financial stress appears to give one business group preferential treatment over others. When one combines this preferential treatment with the increased risk to creditors, we are concerned that the group the legislation is designed to help will, in fact, be harmed. The proposed changes in the Bankruptcy Code, rather than benefiting farmers as a group, will have the perverse effect of discouraging lending to agriculture and encouraging the allocation of credit to competing sectors. The largest well capitalized farmers, those that are most creditworthy, will continue to get credit, but the more marginal farmer may find that credit is more difficult to obtain.

Under the existing Bankruptcy Code both creditors and debtors benefit from the procedures in Chapter 13 that allow for more simplified handling of small business reorganizations, as well as the even-handed approach the Code takes toward the interests of all parties. As the culmination of years of experience with prior bankruptcy law and its impact on debtors and creditors, the present Bankruptcy Code is on the whole efficient and fair and operates with a view towards a cohesive approach to distressed debtors' financial problems. Where the financial problems are more complex, the current law and the practices that surround it promote dialogue between debtors and creditors to seek a resolution to a mutual problem. In our view, the proposed changes tear at the delicately woven fabric of the Code.

While having general concern with the overall implications of the proposed legislation, the FDIC also has specific concerns with selected sections.

The creation of a new debtor whose eligibility is tied to the source of the debt, rather than income, may be so overly broad as to result in benefiting "gentlemen", hobby and tax-shelter farmers more than the true farm family.

The proposed increase from an aggregate of $450,000 to $1 million or $1 1/2 million in the debt allowed a Chapter 13 debtor ignores the design of Chapter 13 as a streamlined version of reorganization capable of handling the simple debt structure of regular income earners. Such cases are only feasible by virtue of the typically less complex nature of the debtor's affairs. This carefully formulated structure will be destroyed by allowing larger filings by businesses with complicated debt and income stream.

The proposed extensions of time for repaying Chapter 13 debts and commencing those payments not only delay the recovery of all creditors but also hurt family farmers in the long run. It is likely that the potential for these lengthy delays will result in farmers having greater difficulty locating short-term credit. Clearly trade creditors and other short-term lenders will face significantly increased risks if forced to wait an additional five years for recovery. To the extent that farming impacts a debtor's ability to schedule payments, the Code presently contains sufficient flexibility to deal with this problem.

Finally, given the Code's allowance for liberal extensions of time to file a Chapter 11 plan, the proposed extension to 240 days for farmers is unnecessary. Bankers and other farm lenders, as active members of agricultural communities, are knowledgeable about their debtors and the current difficulties they face. The current provision encourages constructive interaction between debtors and their creditors towards reaching a solution. This interaction should be further encouraged not discouraged.

In conclusion, the FDIC believes that many of the remedies envisioned by the proposed Family Farm Credit Rehabilitation Act are already available in the present Bankruptcy Code. Moreover, this legislation is likely to have an adverse effect on lenders and borrowers alike. Financially distressed agricultural banks and other creditors will be further harmed and private credit may become less available to family farmers.