The North Dakota Rural Credit System

By GILBERT W. COOKE*

CONFRONTED in the last two decades with agrarian discontent over alleged insufficient private credit institutions, three northwestern states—Minnesota, South Dakota, and North Dakota—established state-financed rural credit systems to furnish long-time loans on rural real estate. This article analyzes the behavior of one of these three experiments.[1] It is significant today as an example of what may happen to a portion of the expanded program of the Farm Credit Administration.

I. Political and Legislative Background

Although proposed as early as 1891 and recommended by Governor John Burke in his farewell address to the Legislature in 1913, the North Dakota rural credit program did not receive effective support until sponsored by the Non-partisan League in 1915.[2] As one of its major planks,[3] the League took the initiative in 1919 in obtaining constitutional amendments and enabling legislation for creation of a rural credit system.

Removal of the constitutional limitation on state loans was accomplished by an initiated amendment in 1918 providing that "the state may issue or guarantee the payment of bonds, providing that all bonds in excess of two million dollars shall be secured by first mortgages upon real estate in amounts not to exceed one-half of its value . . . "[4]

The legislative program for executing the provisions of this amendment resulted in an Industrial Commission composed of the governor, attorney-general, and commissioner of agriculture and labor; a Bank of North Dakota; and an issue of North Dakota bonds—real estate series. The Industrial Commission was empowered to manage, operate, control, and govern all state institutions except those of a charitable, penal, or educational character. Using such powers, it supervised the issuance of bonds and managed the Bank of North Dakota.[5]

The Bank of North Dakota is a state-owned and -operated bank intended primarily as a depository for public funds, a clearing-house for state banks, a central bank for reserves, and a lending agency for state institutions, private banks, and governmental subdivisions. In connection with the rural credit system, the Bank had a double function: (1) it was authorized to make loans to resident farmers on real estate secured by first mortgages not to exceed ½ the value of the security, and the total of those loans must exceed neither 30% of the bank's capital nor, in addition, 20% of its deposits;[6] (2) it could assign farm mortgages in blocks of $100,000 to the state treasurer, and receive in exchange state bonds which could be negotiated, sold, and delivered by the Bank of North Dakota, acting as agent of the Industrial Commission.[7]

The Bank of North Dakota received its first public deposits on July 28, 1919 and closed the first farm loan in August, 1919. During the next two years, loans

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[1] Terrance Leonhardy and Wilford Miller aided the writer in compiling statistics and constructing charts.

[2] See Cooke, G. W., "North Dakota State Mill and Elevator," 46 *Journal of Political Economy* 23–51 (February, 1938).

[3] Gaston, H. E., *Non-partisan League* (New York: Harcourt, 1920), p. 60.

[4] Constitution of North Dakota (1918), art. 31, §182.

[5] Laws of North Dakota, 1919, c. 151.

[6] *Ibid.*, c. 147, §15.

[7] *Ibid.*, c. 154, §§2, 4, 6. The first series was limited to $10,000,000.

were made and carried as general assets of the Bank. Because all capital of the Bank had been invested in two million dollars of bank bonds intended to be sold subsequently to secure liquid funds, none of this capital could be used for farm loans; these loans, therefore, were limited in amount to 20% of the public deposits. When the Bank was established, all public funds were ordered to be deposited therein; an initiated act of November 2, 1920 required only state funds to be there deposited, thus permitting withdrawal of local government funds from the Bank. Initial deposits had been about 12 million dollars; tax payments increased this to 29 million dollars, but current governmental expenses reduced the total to 15 million. With passage of the November amendment, however, the deposits fell during 1921 to around 6 million dollars. Maximum farm loans by the Bank proper totaled $2,910,000 on November 15, 1920.[8]

As already mentioned, the legislation of 1919 permitted the Bank to assign farm mortgages to the state treasurer in exchange for state bonds to the extent of ten million dollars. The operation of this law was delayed by the inability of the Bank, acting for the Industrial Commission, to sell the bonds in the public markets until after a decision of the United States Supreme Court had approved the constitutionality of the issue on June 1, 1920.[9] After this decision, the sale of bonds was further handicapped by a series of political maneuvers intended to destroy the entire industrial program. At the primary election Governor Lynn Frazier won a close decision from William Langer, then representing the conservative element, and in the fall election in 1920 Frazier defeated J. F. T. O'Connor by some 5,000 votes. League candidates William Lemke and John Hagan, attorney general and commissioner of agriculture and labor, respectively, also defeated their opponents by close votes. During 1921 a bitter opposition tried to win support for seven initiated proposals to destroy the program and to recall the Commission. On October 28, 1921 the people voted contrariwise: they defeated the proposed laws which would have killed the program but they also recalled the three leaders who had framed and executed the program for two years. Frazier, Lemke, and Hagan lost to R. A. Nestos, S. Johnson, and Joseph Kitchen.[10] This new Industrial Commission, which took office on November 23, 1921, reported in its next annual report that only $1,971,800 of real estate bonds had been sold by December 31, 1921.[11] These sales, however, had reduced the loans held as general assets from the $2,910,000 mentioned above to $820,000 on November 15, 1921.[12] Subsequent reports of the Commission credit the Bank with having closed during 1919, 1920 and 1921 some 755 loans totaling $2,760,331. This ends the first phase of the state rural credit system.

II. Administration and Allocation of Loans

Under a voters' mandate to carry on the industrial program, the new Industrial Commission set up the Farm Loan Department as a separate division of the Bank of North Dakota to handle farm loans. On the Commission's recommendation the voters approved an initiated statute, June 28, 1922, increasing the issuable bonds to 20 million dollars; the Legislature in 1923 cancelled part of the foregoing issue but allowed 25 mil-

[8] Bank of North Dakota, *Bulletin*, November 15, 1920.

[9] *Green v. Frazier*, 253 U.S. 233 (1920).

[10] *Manual for the State of North Dakota*, 1932, Bismarck, N.D., p. 129.

[11] Industrial Commission, *Annual Report*, 1921, p. 18.

[12] Bank of North Dakota, *Bulletin*, November 15, 1921.

lion more. Subsequently, the 1929 and 1931 Legislatures expanded the 1923 amount to 35 million. From these acts a total of $42,750,000 of loans were authorized for rural credit purposes.[13] In 1923 also, collection of interest and principal on the loans was transferred from the state treasurer to the Bank of North Dakota—a collection division being established for that purpose. Under this new arrangement the Bank of North Dakota had, and still has, two distinct departments: the Banking Department handling public deposits; the Farm Loan Department which has a closing division examining applications and assigning farm mortgages to the state treasurer and a collection division receiving the income from farmers to remit to the state treasurer who holds title to the mortgages and pays interest on the bonds. Under this arrangement the Farm Loan Department does not take any responsibility for any loss in principal or interest on the loans or for paying interest or principal on the bonds.[14] It is sort of an in-between agency with powers but no responsibility.

The details of the rural credit system may now be summarized: (1) the Industrial Commission prescribes the forms for application and appraisal of loans; (2) the Farm Loan Department receives the application, directs an appraisal, and closes loans which are approved by the appraiser, the head of the closing section, and a finance committee of the Bank;[15] (3) closed loans are assigned to the state treasurer in batches of $100,000; (4) upon receipt of the mortgages, the state treasurer issues bonds to the Bank which sells them on the open market to obtain funds for the farmer; (5) two contracts are made: one between the farmer and the state treasurer, the other between the state treasurer and the creditor of the bonds; (6) the rate of interest charged the farmer is a function of the rate on the bonds; (7) amortization charges are collected by the collection division of the Farm Loan Department and turned over to the state treasurer; (8) interest on the bonds is paid by the state treasurer out of a Bond Payment Fund.[16]

The legislation concerning the plan of amortization states:

"Every such mortgage shall contain an agreement providing for the repayment of the loan on an amortization plan by means of a fixed number of annual installments sufficient to cover, first, a charge on the loan, at a rate not exceeding the interest rate on the last series of real estate bonds issued, if any, by the State of North Dakota; second, a charge for administration and surplus, at a rate not exceeding one per cent per annum on the unpaid principal, said two rates combined constituting the interest rate on the mortgage; and third, such amounts to be applied on the principal as will extinguish the debt in not less than ten nor more than thirty years; . . . "[17]

In the operation of the amortization law, 16 series of loans were closed, labeled alphabetically from A to P. The percentage of interest and principal for the initial installment together with the period of amortization for these series are as follows:[18]

Series	Percentage of Initial Installment			Amortization Period
	Interest	Principal	Total	
A..........	6 %	1 %	7 %	30 years
B, C, D, E...	6½	1½	8	26 years
D, E*.......	6	1½	7½	28 years
Remainder..	6	1½	7½	28 years

* D and E series were of two types.

[13] Laws of North Dakota, 1923, p. 548; *Ibid.*, c. 292; *Ibid.*, 1929, c. 182; *Ibid.*, 1931, c. 102.

[14] The Banking Department, however, held the bonds as assets and earned about 35% of its gross income therefrom.

[15] Only 1% of the loans were changed by this committee.

[16] Laws of North Dakota, 1919, c's. 147, 154; *Ibid.*, 1923, c. 292.

[17] *Ibid.*, 1919, c. 147, §17.

[18] Letter from A. T. Bellingmier, Bank of North Dakota, April 24, 1936.

The period of closing loans extended from August, 1919 to October, 1933. A total of 16,486 loans amounting to $40,549,972.95 were made; four loans were assumed by the Banking Department and consequently this study is concerned with 16,482 loans totaling $40,505,450.11. Table I presents the number of closed loans, the amount, average loan, and average loan per acre.

TABLE I. STATE OF NORTH DAKOTA FARM LOANS CLOSED BY THE FARM LOAN DEPARTMENT*

Year	Number	Amount	Average Loan	Average Loan per Acre
1921†	755	$2,760,331	$3,656	$14.07
1922	1,077	3,470,691	3,272	12.66
1923	1,984	5,950,500	2,998	11.31
1924	2,213	6,382,600	2,884	11.14
1925	1,804	4,772,100	2,645	9.82
1926	1,330	3,169,150	2,382	9.42
1927	1,202	2,569,700	2,137	8.52
1928	808	1,767,000	2,186	8.44
1929	780	1,616,700	2,072	7.98
1930	1,257	2,546,800	2,026	7.74
1931	2,291	4,074,300	1,777	6.96
1932	928	1,384,400	1,491	6.05
1933	57	85,700	1,507	5.95

* Industrial Commission, *Annual Reports*, 1922–33.
† Includes also 1919 and 1920; figures not given separately.

The basis for territorial allocation of the loans is stated in the *Annual Report* of the Industrial Commission for 1922:[19]

"The allotment of available funds to the respective counties of the first $9,000,000 authorized for making farm loans was on the basis of .0095 per cent of the 1921 assessed valuation of the land in each county. The counties were classified in four groups: those in the western part of the state in District Number One were allotted 200 percent of the base; those in District Number Two, 150 percent of the base; those in District Number Three, the base; and those in District Number Four, the Red River Valley, one half the base percent of the assessed valuation.

"In the second $10,000,000 made available by initiated law, the allotment was the same except that the counties of Burke, Divide, Mountrail, Renville, Ward, and Williams of the Second District were included in the First District allotment base."

The effect of this allotment scheme is pictured on Chart I which shows the ratio by counties of total State of North Dakota farm loans closed at the end of 1934 to assessed farm land values for the same year. Examination of this chart shows that counties in the eastern part of the State have less than 4% of State loans to assessed valuation; centrally located counties carry between 4 and 7.9% of loans to assessed valuation; western counties average 10%; and a group of counties located about the Missouri River (in District One) hold over 12% of loans to assessed valuation. It must be emphasized that this chart includes only loans made by the State of North Dakota; private loans or Federal Government loans are not included (except so far as State loans were later refinanced by the Federal Government). To this extent Chart I does not show the *total* burden of farm loans by counties. The significance of this allocation scheme will be evident in connection with the problem of delinquency.

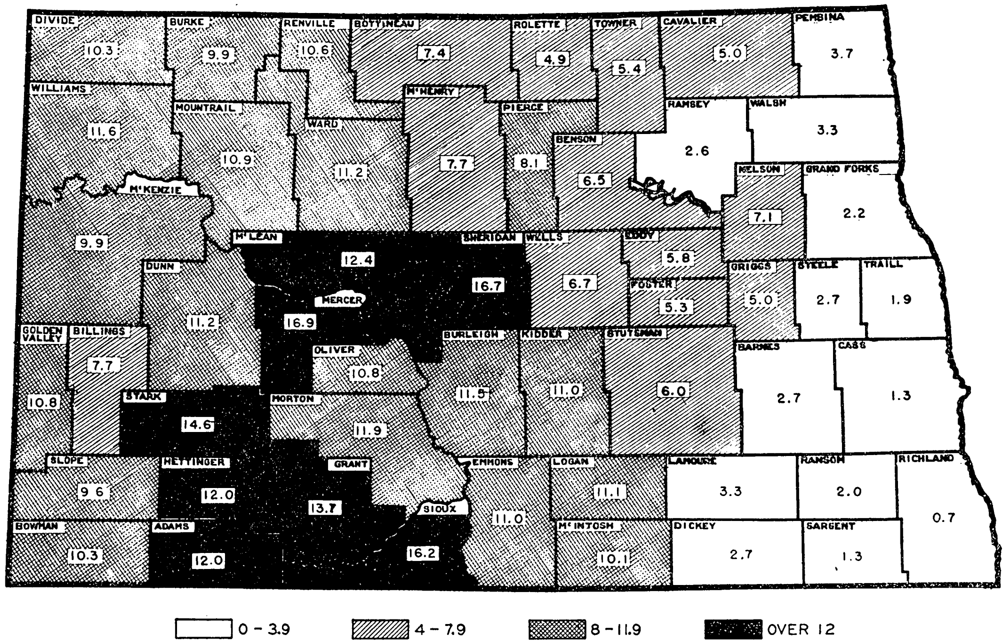
Revenues to operate the closing division of the Farm Loan Department were obtained from a $5.00 fee for each application and an appraisal charge proportionate to the expense incurred. The chief outlay, aside from personnel, was for interest to the Banking Department on money borrowed to meet annual losses. From August, 1919 through 1921 no separate account was kept of the closing division; between January 1, 1922 and January 2, 1934 a deficit of $225,686.68 was incurred. At the latter date the closing division was discontinued and the deficit charged to the collection division of the Farm Loan Department.[20]

[19] Industrial Commission, *Annual Report*, 1922, p. 19.

[20] Industrial Commission, *Annual Report*, 1934, p. 20.

CHART I

RATIO OF TOTAL NORTH DAKOTA FARM LOANS CLOSED AT END OF 1934 TO ASSESSED FARM LAND VALUES, 1934



III. Collection and Delinquency of Loans

From a lender's point of view the success of any farm credit program is measured by the regularity of the amortization charges to cover interest and sinking fund. The following analysis of the delinquency of North Dakota State loans to farmers is to be considered only a rough approximation, inasmuch as (1) the amortization schedule did not follow any strict mathematical system; (2) foreclosures reduced the amount of the open loans and made impossible an accurate study of individual series default; (3) accrued interest on delinquent issues that were still open loans was not given by series regularly. Hence, the accompanying tables present only the general trend.

Under the amortization plan all loans provided for an initial interest charge of 6 or 6½% plus a principal payment of either 1 or 1½%; subsequent payments lowered the proportion for interest and increased the amount for principal. Two conditions should exist with such a plan: (1) the principal payments should increase annually, and (2) the interest payment should cover fixed charges on the bond issue supplying the capital.

Table II represents the condition of the loans at two different periods. The year 1929 is selected because it is a pre-depression year; 1934, because the influence of two severe drought years (1934 and 1936) is not present. Without repeating here the figures of this table, one may point out that exceptionally large foreclosures occurred and were ultimately represented in land owned; that by 1934 only 25% of the remaining open loans were not delinquent in installments; and that the percentage of land owned even in 1929 is significantly high. The table shows also that the older

TABLE II. CONDITION OF NORTH DAKOTA RURAL CREDIT LOANS AT TWO PERIODS:*
September 30, 1929 and October 31, 1934
(Percentage of dollar amounts)

Series and Year†	Amount (000 Omitted)†	Open Loans		Good Standing in 1934§	Being Foreclosed, 1929	Land Owned¶		Refinanced, 1934
		1929	1934			1929	1934	
A-1921	$2,500	42.9%	26.5%	10.4%	7.8%	34.9%	46.4%	13.1%
B-1922	3,000	64.3	29.4	8.5	2.3	14.8	30.0	18.3
C-1922	2,000	70.6	35.3	7.9	1.5	12.7	23.2	22.9
D-1923	3,750	74.5	40.2	8.3	1.4	8.9	22.2	20.2
E-1923	4,109	75.6	38.4	10.1	1.2	8.6	21.4	21.2
F-1924	3,000	82.5	40.9	7.9	—	4.7	18.5	23.1
G-1925	6,000	87.7	44.1	9.5	—	3.3	18.4	24.2
H-1926	4,000	92.2	47.9	10.8	—	2.4	14.3	27.5
I-1929	3,000	84.4	54.0	11.7	—	—	10.0	33.0
J-1929	1,000	—	55.3	11.4	—	—	6.7	33.7
K-1930	2,000	—	68.4	14.6	—	—	1.1	28.6
L-1930	2,000	—	61.4	14.6	—	—	2.7	33.9
M-1931	500	—	73.6	15.1	—	—	—	25.0
N-1931	1,000	—	66.3	13.8	—	—	—	31.4
O-1931	1,000	—	74.3	39.2	—	—	—	22.7
P-1931	714	—	72.0	23.9	—	—	—	26.6
S.A.‡	931.6	—	50.3	9.5	—	—	—	27.8
Total	40,505	79.9	46.0	12.2	1.6	8.3	17.3	24.3

* Board of Auditors, *Report on Bank of North Dakota*, 1929, p. 164; *Ibid.*, 1934, p. 230.
† Year of series and dollar amount of issue relate to bond issues; the exact date and amount of loan series were not available.
‡ S.A. stands for special assessments held by the Banking Department for which no bonds were issued; paid to Bank by state treasurer in 1933.
§ "Good standing" is the label for loans not delinquent.
¶ "Land owned" is the label for face value of loans already foreclosed.

series yielded a much larger percentage of land owned.

In an attempt to get at the true chronological picture of all the loans, the writer has constructed Table III to present the median condition of all series at the end of given years after issuance of the bonds. The main purpose of this table is to show that all series possess a tendency to approach an undesirable condition: at the end of five years approximately 10% of the loans were being foreclosed or in land owned (sheriff's deeds); at 10 years, over 30% was in

TABLE III. CONDITION OF NORTH DAKOTA RURAL CREDIT LOANS AT GIVEN PERIODS*
(Median of the series expressed in per cent)

At End of	Open Loans	In Foreclosure	Resold Land	Sheriff's Deed	Sale Pending	Total Unpaid
1 year	99.00%	.37%	—	—	.07%	99.00%
2 years	98.40	.65	—	.37%	—	98.80
3 years	92.61	2.56	.08%	.80	.28	97.05
4 years	87.72	1.82	.18	2.65	.48	91.55
5 years	81.19	3.20	.43	6.02	.46	84.47
6 years	74.05	2.80	1.11	7.02	.40	87.71
7 years	71.07	2.04	1.63	10.80	.59	85.58
8 years	67.29	2.65	2.57	13.17	.30	84.33
9 years	63.05	3.93	3.55	16.03	2.44	83.13
10 years	61.42	4.85	8.32	19.64	—	82.26

* Calculated by the writer from the original data in the Board of Auditors, *Annual Report on Bank of North Dakota*, 1926–1934. Each of the 16 series was changed from dollars amount to percentage under the above headings; these percentages were arranged in chronological order by years from date of issue; all percentages with the same time sequence were assembled and the median of these groupings obtained. These medians are in the table. Because of this median method "total unpaid" is not the sum of all items in each row.

that status. The evidence is plain that excessive foreclosing took place in each issue, the early as well as the late.

The decrease in regular amortization charges prevented accumulation of the expected sinking fund to redeem the bonds at maturity; on the other hand, the unexpected expansion of the Federal Government's program permitted the refinancing of about 50% of the North Dakota State loans and accumulated a premature sinking fund which had to be used at once or else earn only about 3% interest in regular financial markets. The condition of the real estate loans principal account on December 31, 1936, under these changed conditions, is as follows:[21]

Total loans closed.........	$40,505,450.11
Open loans $8,395,563.94	
Land owned 8,697,119.04	$17,092,682.98
Federal refinancing..........	18,581,690.57
Amortization principal paid...	4,831,076.56
Total as above............	$40,505,450.11

In summary, at that date 21% of the loans were still open, 21% in land owned, 46% were refinanced by the Federal Government, and 12% had been amortized as originally planned. In the federal refinancing, however, the State of North Dakota took a loss of $1,831,126.45 in principal and thus received credit in cash for only $16,750,564.12. From the total cash principal collections (amortization and federal) $15,451,450.11 of bonds and loans held by the Bank of North Dakota were redeemed, leaving a cash balance in the principal fund of $6,130,190.57.

On this same date, December 31, 1936, "interest accrued and interest discounted on farm loans and lands" totaled $6,106,776.69 and "accrued interest not collected" (on open loans) totaled $1,836,022.21.[22] The first item is the accrued interest on either loans foreclosed or the discounted interest on loans refinanced which discount amounted to $2,868,014.63; the second item is the accrued interest on the $8,395,563.94 of open loans.

As mentioned before, collection of loan interest and management of the land owned are performed by the collection division of the Farm Loan Department. To finance this agency an administration fee of ½ of 1% (see quotation at note 17) was added to all loans after the D series. The chief expense, other than personnel, was the interest on funds borrowed from the Banking Department to cover taxes, insurance, and miscellaneous advances on land owned; on December 31, 1933 this revolving fund, as it was called, reached a maximum of $900,000. Even with this interest expense the collection division almost broke even from its organization January 1, 1923 until December 31, 1932. At the latter date, it had a small deficit of $57,118.87. After that date the income, expense, and operating balance are as shown in Table IV.[23]

A few explanations are needed with this profit and loss account: (1) operating expenses increased because of costs for refinancing and management of land owned; (2) the refund from the Banking Department was an interest overcharge on money loaned for advances; (3) the exceptional income during 1934 and 1935 was from fees charged the Federal Government in refinancing the State loans; (4) interest charged off was due from the state treasurer; (5) the closing division deficit (mentioned before) was absorbed by the collection division; (6) the administration fee which constituted the

[21] Industrial Commission, *Annual Report on Bank of North Dakota*, 1936, pp. 21–39. Various tables in this report show a discrepancy of $3,000 in open loans. The writer has used his discretion above.

[22] *Ibid.*, p. 21.

[23] *Ibid.*, 1933–1936.

TABLE IV. OPERATING DATA, COLLECTION DIVISION, FARM LOAN DEPARTMENT, 1933-1936

	1933	1934	1935	1936
Total income	$ 56,092.97	$541,130.29	$579,163.84	$116,383.73
Operating expense	167,488.62	292,909.33	265,836.19	240,056.59
Operating profit	—	248,220.96	313,327.65	—
Operating loss	111,395.65	—	—	123,672.86
Refund from Bank Dept	109,458.39	—	—	—
Interest charged off	—	64,429.82	—	—
Closing division deficit	—	225,686.68	—	—
Cumulative deficit	59,056.13	100,951.67	212,375.98*	88,703.12*

* Surplus.

chief early income had become negligible by 1936 and thus it appears that future statements will show an operating loss.

IV. Causes for Delinquency of the Rural Credit Loans

It seems desirable at this point to offer some explanation of the serious delinquency of the loans and the resultant foreclosure or refinancing by the Federal Government.

First will be mentioned the decline in the average state yield per bushel of wheat per acre harvested. Wheat constitutes about ½ the cash crop in North Dakota. Whereas the 10-year average yield for 1919-1928 was about 11.1 bushels per acre, the 5-year average for 1929-1934 was only 8.5 bushels.[24] At this writing, data are not at hand for 1934, 1935, and 1936, but the severe droughts of 1934 and 1936 and the rust of 1935 make it appear that the average for these years was still below the 1929-1934 average.

Second in the list of incidents is the serious decline in cash farm income as presented in Table V.

Low-acreage production or low farm prices, or a combination of both, perhaps, has waged havoc with a farm income in North Dakota which normally approximates 200 and 250 million dollars. Loans written on such an income cannot be otherwise than in default when the state income falls to ¼ of normal (or $60,000,000) unless reserve assets have been established to meet such contingencies.

[24] Department of Agricultural Economics, North Dakota Agricultural College, *Basic Data for Farm Planning*, Fargo, N.D. (Jan. 20, 1936.)

TABLE V. NORTH DAKOTA CASH FARM INCOME FROM CROPS AND LIVESTOCK*

(Thousands of dollars)

Year	Crops	Live-stock	AAA Benefits	Total
1924	$226,758	$53,142	—	$279,900
1925	181,723	68,923	—	250,646
1926	108,151	76,858	—	185,009
1927	183,253	62,466	—	245,719
1928	153,670	68,421	—	222,091
1929	121,746	71,250	—	192,996
1930	71,900	57,284	—	129,184
1931	18,089	42,202	—	60,291
1932	37,950	29,513	—	67,463
1933	42,918	32,409	—	75,327
1934	31,701	29,763	$37,693	99,157
1935	41,662	33,988	17,443	93,093
1936	30,607	51,311	12,379	94,297

* Letters from Ben Kienholz, Bureau of Agricultural Economics, Fargo, N.D.

But it is evident, third, that such stored assets did not exist. Deposits of state banks in North Dakota fell from $123,129,000 in 1919 to $49,451,000 in 1929 and to a low of $15,279,000 in 1933; deposits of national banks in North Dakota fell from $73,884,000 in 1919 to $42,008,000 in 1933. Losses of $108,000,000 in state bank deposits and $30,000,000 in national bank deposits are certain to lessen the capacity of the farmer to pay.

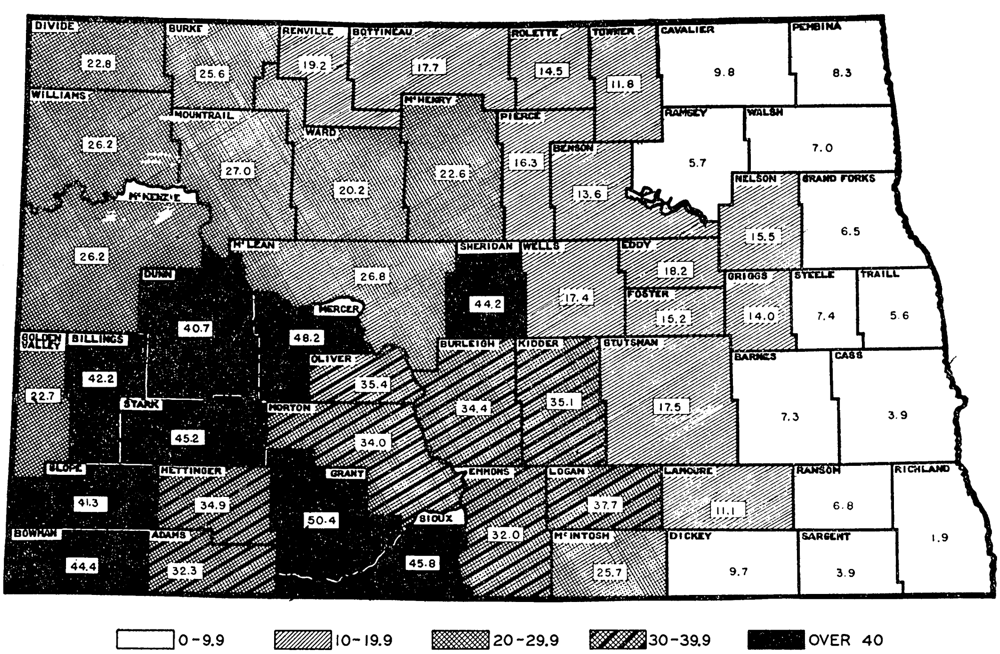
What may be considered the major reason for default on the loans (and possibly a contributing factor in the previously mentioned conditions) is the decline in rainfall. The average rainfall in the eastern half of the State is over 20 inches, in the western half about 16 inches. During the period from 1929 to 1934, however, the eastern average was only 16 inches and the western average fell to 10 and 12. (This is serious because a 10-inch rainfall is considered desert precipitation.)

The above comments are considered explanatory remarks of the general failure, particularly after 1929, to keep up the loan installments. To explain the delinquency before 1929 (as indicated in Table III) one must examine sectional influences. It will be recalled that in allocating the loans, preference was given to farmers in the western counties.[25] Chart I presented the results of that allotment. Chart II presents the ratio of total State of North Dakota farm loans to crop income in each county for three representative years, 1919, 1924, and 1929 averaged. As might be expected, the counties with the highest per cent of loans to assessed valuation (Chart I) also have the highest per cent of loans to income (Chart II). When one considers that the researches by the North Dakota Agricultural College indicate that droughts occurred in the western part of the State in 15 out of the last 45 years, it is difficult to dodge the evidence that farm loans were made in areas least able to carry them. A sectional analysis made by the Board of

[25] Excepting the A series, these loans were closed during a period when the Industrial Commission was controlled by the conservative political faction, called the Independent Voters Association. To that degree, the Non-partisan League forces cannot be blamed for the character of the loans.

CHART II

RATIO OF NORTH DAKOTA FARM LOANS TO CROP INCOME



Auditors (not presented here for lack of space) indicated that as of October, 1934 the borrowers living in the western counties had paid in the least principal, suffered the least foreclosures, and held the most open loans. This paradoxical situation indicates that the western areas were favored in collecting and foreclosing as well as in the original closing. It would appear that areas which suffer a crop loss one year out of three cannot support loans equal to 40 or 50% of the annual income.[26]

V. Condition of North Dakota Real Estate Bonds

The second section of the constitutional amendment authorizing bond issues for rural credit purposes contained the following:[27]

"Every law authorizing a bond issue shall provide for levying an annual tax, or make other provision, sufficient to pay the interest semi-annually, and the principal within thirty years from the passage of such law, and specially appropriate the proceeds of such tax, or of other provisions, to the payment of said principal and interest, and such appropriation shall not be repealed nor the tax or other provision discontinued until such debt, both principal and interest, shall have been paid . . . "

In conforming to these provisions, both the bond acts of 1919 and 1923 contain identical sections stating that the bonds shall mature in not less than 10 nor more than 30 years; that the state treasurer shall pay the interest and principal at maturity; that, if the Real Estate Bond Payment Fund be insufficient to pay the interest and principal, then the State Board of Equalization shall include in the annual levy such a tax as will meet the need. Both laws asserted that the "full faith and credit of the State of North Dakota is pledged for the payment thereof, both principal and interest . . . "[28]

As listed in Table II, the governor and the state treasurer issued 16 series of real estate bonds, lettered alphabetically from A to P, maturing in from 8 to 30 years and so spaced that approximately one million dollars worth matured each year between 1930 and 1960. From July 1, 1921 to January 1, 1931 a total of $39,573,000 bonds were issued. This bond total differs from the loan total by $931,600 which represents loans carried as assets of the Banking Department until redeemed by the state treasurer out of the Bond Payment Fund.[29]

In considering the condition of the real estate bond payment fund, a distinction must be drawn between the interest and the principal requirements. To meet the cash outlay necessary to offset the delinquent interest income of about 8 million dollars, additional revenue had to be raised as follows:[30]

Motor vehicle tax transfers	$2,941,718.62
Beer revenue transferred	1,015,000.00
General tax levy collected	4,033,274.70
Total additional revenue as of December 31, 1936	$7,989,993.32

Corresponding somewhat to a previous statement on loans, there is now presented a balance sheet on the real estate bonds:[31]

[26] The delinquency traced for the State of North Dakota loans is prevalent also in the federal loan program in North Dakota. As of December 31, 1936, 80% of the Land Bank loans in North Dakota were delinquent as compared with only 22.5% for the entire United States, and 83.1% of the Land Bank Commissioner loans in North Dakota were delinquent as compared with only 18.6% for the United States. In both instances, North Dakota had the highest delinquency of any state. (Cf. *Fourth Annual Report*, Farm Credit Administration, 1936, pp. 124, 159.)

[27] Constitution of North Dakota (1918), Art. 31, §182.

[28] Laws of North Dakota, 1919, c. 154; *Ibid.*, 1923, c. 232.

[29] Industrial Commission, *Annual Report*, 1936, p. 38.

[30] *Ibid.*, p. 21.

[31] *Ibid.*, pp. 21, 36.

Total bonds issued	$39,573,000.00
Redeemed by state through refinancing	14,519,000.00
Outstanding on December 31, 1936	$25,054,000.00
Secured by:	
Outstanding loans	$ 8,395,563.94
Real estate owned	8,697,119.04
Cash in fund	6,130,190.57
Total	$23,222,873.55
Deficit (refinancing)	1,831,126.45
Total as above	$25,054,000.00

Inasmuch as the bond maturities through January 1, 1945 total only $6,415,000 and the cash in the principal fund totals $6,130,190.57, there is no immediate concern over the maturity of the bonds. However, to meet the maturity of the remaining 19.4 million dollars there exists only 8.4 million dollars of open loans and 8.7 million dollars of land owned. (The former is now 75% delinquent and the latter is carried on the books at the value of the loan granted.) The total loss to the State in handling the principal amounts to $1,831,126.45 taken on refinancing with the Federal Government and $2,181,444.21 incurred as expenses in foreclosing the farms owned.[32]

A more serious matter is the interest requirements on the outstanding $25,054,000 of bonds. Only 8 of the original 40 million dollars of open loans remain to bring in amortization charges; yet 25 out of 39 million dollars of bonds must still be paid interest. Furthermore, instead of an expected income of about $500,000 annually on these remaining open loans, only $138,548.93 was received in 1936. The difference between this amount and the $1,339,725.64 due on the bonds must be obtained from state revenue, or interest on the principal fund (interest amounts to about $180,000 yearly). Thus it is evident that the state must raise over one million dollars annually to cover real estate bond interest, until such time as the loans discontinue their delinquency and the land owned is either sold or rented on as favorable a basis as if it were earning amortization charges.

On December 31, 1936 the past deficits on interest payments and the deficits on principal totaled as follows:[33]

Interest accrued and interest discounted	$6,106,776.69
Principal of loans and lands discounted	1,831,126.45
Non-ledger deficits in collection division	979,310.92
Sub-total, real estate bond payment fund	8,917,214.06
Surplus in collection division expense account	88,703.12
Total deficit, as of December 31, 1936	$8,828,490.94

Future deficits are likely to approximate the following:

Loss on discounting accrued interest on open loans	$ 1,000,000
Loss on disposal of land owned	1,000,000
Interest to be met by taxes for, say, 10 years	10,000,000
Total loss estimated by writer for the future	$12,000,000

In summary, therefore, one may conclude that the 40 million dollar rural credit program will cost the State of North Dakota about 20 million dollars when completely liquidated. Without considering in this brief article any theoretical aspects of the matter, one cannot help in closing but raise the issue as to whether this experience does not cast doubt upon the propriety of attempting to use credit facilities to equalize unequal economic income. The experiment surely ought to serve as a warning to the Federal Government and to provide a question for economists to discuss as to the best method of solving agricultural problems and of handling marginal producers.

[32] *Ibid.*, pp. 21, 30, 38.

[33] *Ibid.*, footnote 32.