October 23, 2014

Mr. Barry F. Murdock
Deputy Director
Office of Regulatory Policy
Farm Credit Administration
1501 Farm Credit Drive
McLean, VA 22102-5090

RE: RIN 3052-AC84 – Funding and Fiscal Affairs, Loan Policies and Operations, and Funding Operations, Investment Eligibility – Federal Register Number 79 Fed. Reg. 43301 (July 25, 2014).

Dear Deputy Director Murdock:

The proposed rule issued by the Farm Credit Administration (FCA) seeks to significantly expand investments held by Farm Credit Banks (FCBs) and Farm Credit Associations (Associations) under the guise of a required review of regulations under section 939A of the Dodd-Frank Wall Street Reform and Consumer Protection Act (Dodd-Frank Act). Section 939A merely requires agencies to review regulations that utilize credit ratings and substitute other appropriate standards for review. This proposed rule goes far beyond that required review and rewrites investment eligibility for Farm Credit System (FCS) institutions. This proposed rule spins the requirements of section 939A on its head. This provision was designed to remove risk from financial institutions by doing away with credit ratings that understated risk. Instead of simply meeting that goal, the proposed rule goes further and is authorizing FCS institutions to take on more risk.

This broad based investment expansion being conducted without express authorization from Congress is exactly the type of action that creates significant risk for all FCS institutions and American taxpayers could ultimately be on the hook for failures in the investment portfolios of FCS institutions if the proposed rule is adopted. The undersigned 53 state bankers associations representing thousands of large, mid-size and community banks, respectfully but strongly objects to the portions of the rulemaking where the FCA seeks to substantially expand the number and scope of eligible investments held by Farm Credit Banks (FCBs) and Farm Credit Associations (Associations).

The proposed rule is similar to the pilot program that the FCA had approved in 2005 which authorized FCS institutions to make investments in a broad category of investments including loans to entities that would otherwise be ineligible to receive loans from FCS institutions. While the FCA ultimately ended the pilot program after many years, the proposed rule seeks to codify the goals of the pilot program, namely authorizing an expansion of eligible investments for FCBs and Associations. This broad expansion of the eligible investments held by both FCBs and Associations raise serious concerns about what types of investments these institutions will hold and the level of risk these investments will interject into the FCS. Accordingly, we offer the following comments on the proposed regulation.

Expansion of Farm Credit Bank Investments

Section 615.5140 governs eligible investments for FCBs and currently provides a clear chart outlining various eligible investments FCBs may hold.[1] The proposed rule would eliminate the chart of eligible investments and replace it with a series of investment eligibility criteria. While the list of eligibility criteria serves a similar purpose to the chart in the current regulation, the eligibility criteria also includes a provision that authorizes FCBs to hold investments that "do not satisfy the requirements" of the new regulation.[2] Additionally, the proposed rule would provide the FCA blanket authority on a "case-by-case basis" to determine that a particular investment poses "inappropriate risk" and if determined so, the FCA will "notify the FCB as to the proper treatment of the investment."[3]

The expansion of the eligible investments authorized to be held by FCBs raises concerns about the amount and types of eligible investments the FCBs will hold and the potential risk this creates for the FCS. Income derived from these investments will continue to benefit from favorable tax treatment raising policy questions. However, the most concerning portion of the proposed rule is the ability of FCBs to invest in ineligible investments subject only to the closed door review of the FCA. Given the case-by-case nature of FCA ineligible investment reviews, it is unclear what types and volumes of ineligible investments will be authorized. The FCA seems to be acting in a manner that will provide the public with less transparency about FCS investments.

The discussion about ineligible investments is troubling. Why would FCA contemplate allowing any FCB or Association to make ineligible investments in violation of the proposed rule's restrictions? Accordingly, absent clear evidence of a need for the proposed rule, the FCA should withdraw the proposed rule and leave section 615.5140 as currently drafted in the Code of Federal Regulations.

Expansion of Farm Credit Association Investments

The proposed rule would modify section 615.5142 to greatly expand the ability of Associations to make investments to "manage risk".[4] Currently, section 615.5142 only allows an Association to hold eligible investments listed in section 615.5140 (eligible investments for FCBs) for the purposes of "reducing interest rate risk and managing surplus short-term funds."[5] To support this expansion, the proposed rule states that Associations "may need to hold investments for purposes other than managing surplus short-term funds and reducing interest rate risk".[6] We request that the FCA develop a list of what types of scenarios would fall under this exemption. If Associations are not managing surplus short-term funds and/or reducing interest rate risk, it raises the question, what are they doing with these investments? Unfortunately, the proposed

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[1] *See* 12 C.F.R. § 615.5140 (2014).
[2] Organization; Funding and Fiscal Affairs, Loan Policies and Operations, and Funding Operations; Investment Eligibility, 79 Fed. Reg. 43301, 43316 (proposed July 25, 2014).
[3] *Id.*
[4] *Id.*
[5] 12 C.F.R. § 615.5140 (2014).
[6] Organization; Funding and Fiscal Affairs, Loan Policies and Operations, and Funding Operations; Investment Eligibility, *supra* note 2, at 43302.

rule and the preambles explanatory background fail to provide any details as to why Associations require greater investment flexibility.

This failure to provide any details about the need for expanded investment authority makes it difficult to comment on the details of the proposed rule. Without a better public understanding of why the FCA believes Farm Credit Associations need expanded flexibility to increase their investment portfolios, it is almost impossible to make informed comments as to whether the proposed rule's expansion of investments and the purported "limits" on types and amount of investment are sufficiently limited to meet the Association's needs.

Notwithstanding the proposed rule's lack of necessary details to make a fully informed comment, there are a number of significant problems with the proposed changes to section 615.5142 that the FCA should address.

First, the proposed rule greatly expands the eligible investments Associations may purchase and hold. Currently, section 615.5142 limits Associations investments to the defined list of investments that are eligible for FCBs in section 615.5140. As the proposed rule also modifies and expands section 615.5140 to allow greater flexibility for FCBs, that change expands authority of the Associations. This expansion strikes the current list of defined eligible investments and replaces it with broader investment authority. By significantly expanding the eligible investments the proposed rule increases the ability of the Associations to engage in government sponsored arbitrage.

Second, the proposed rule incorporates a number of new requirements on FCBs in approving investments held by Associations. While the proposed rule contains the current requirement that all eligible investments be approved by FCBs, the new requirements placed upon the FCBs are no substitute for regulatory approval from the FCA. Instead, this requirement appears to be little more than a devolution of investment authority oversight from the FCA to FCBs that may be engaged in the exact same investment strategy as the Associations. As a result, the proposed rule would greatly increase the risk profile of Associations.

Third, the proposed rule would limit Association investments to 10% of total outstanding loans. The FCA has asked whether this limit is the proper number as a limit to the greatly expanded investments. The FCA is presenting the public with a weak and meaningless limit. Given the lack of detail provided in the proposed rule, including the lack of detail as to why the investment expansion is necessary and lacking a clearly defined list of eligible investments, it is impossible to determine if this number is too high or too low. However, one clear problem with the 10% limit is that it is tied to Association loans outstanding and not to capital held by the Association. There is no other similar or comparable limit within the financial regulatory community. On the face of it, tying the amount of investments to the loan portfolio of an Association is absurd, and a recipe for disaster.

As a result of this proposal, the portfolio of eligible investments could expand or contract based upon the size of an Association's loan portfolio. As loans expand, so does the ability of Association to increase investments under the proposed rule. This in turn could increase the risk profile of the Association. Conversely, if loans were to decline at an Association, the Association may be required to liquidate investments in order to stay within the 10% limitation. Given that it is unclear as to how liquid these new investments may be, this could increase risk to the

Association in the event loan declines occur requiring a rapid liquidation of eligible investments under the proposed rule. The 10% limit is a poorly designed policy, and should be re-proposed by the FCA.

Finally, the proposed rule authorizes the FCA to approve "other investments" above and beyond those approved by the FCB overseeing the Association's investments. This broad expansion of authority authorizes Associations to seek approval of investments by the FCA that are outside the limitations in the proposed rule. This is effectively a loophole that could authorize an investment in anything the FCA deems worthy. Depending on what the FCA approves, this significantly expands the footprint and scope of Association investments beyond the stated mission Congress created the FCS to address. Again, without a clearly defined need for investments outside of managing short-term funds and/or reducing interest rate risk, the entire basis for this regulatory expansion of investments held by FCBs and Associations is unnecessary.

To address these concerns, the FCA should withdraw the proposed rule until FCA provides a more detailed public statement as to why FCS institutions (both FCBs and Associations) need the expanded authority. Failing to do this, FCA should take these concerns regarding FCB and Association investments to Congress and provide Congress with a sound analysis as to why changes to the Farm Credit Act of 1971 are necessary. If FCS institutions are able to leverage their tax preferred, government sponsored enterprise status to make investments outside of the congressionally mandated mission of the FCS, it will inevitably lead to more risk to FCS institutions, more risk to taxpayers, and more uncertainty for FCS owners, who are farmers and ranchers.

Otherwise, the FCA is expanding FCB and Association authority to engage in government sponsored financial arbitrage absent a compelling reason. Accordingly, sections 615.5140 and 615.5142 should not be amended as proposed under the guise of addressing section 939A of the Dodd-Frank Act.

Thank you in advance for considering our views.

Respectfully,

Alabama Bankers Association
Alaska Bankers Association
Arizona Bankers Association
Arkansas Bankers Association
California Bankers Association
Colorado Bankers Association
Connecticut Bankers Association
Delaware Bankers Association
Florida Bankers Association
Georgia Bankers Association
Hawaii Bankers Association
Heartland Community Bankers Association
Idaho Bankers Association
Illinois Bankers Association
Illinois League of Financial Institutions
Indiana Bankers Association
Iowa Bankers Association
Kansas Bankers Association
Kentucky Bankers Association
Louisiana Bankers Association
Maine Bankers Association
Maryland Bankers Association
Massachusetts Bankers Association
Michigan Bankers Association
Minnesota Bankers Association
Mississippi Bankers Association
Missouri Bankers Association
Montana Bankers Association
Nebraska Bankers Association
Nevada Bankers Association

New Hampshire Bankers Association
New Jersey Bankers Association
New Mexico Bankers Association
New York Bankers Association
North Carolina Bankers Association
North Dakota Bankers Association
Ohio Bankers League
Oklahoma Bankers Association
Oregon Bankers Association
Pennsylvania Bankers Association
Puerto Rico Bankers Association
Rhode Island Bankers Association
South Carolina Bankers Association
South Dakota Bankers Association
Tennessee Bankers Association
Texas Bankers Association
Utah Bankers Association
Vermont Bankers Association
Virginia Bankers Association
Washington Bankers Association
West Virginia Bankers Association
Wisconsin Bankers Association
Wyoming Bankers Association