LONE STAR
AG CREDIT

Date: January 29, 2015

Mr. Barry Mardock
Deputy Director, Office of Regulatory Policy
Farm Credit Administration
1501 Farm Credit Drive
McLean, Virginia 22102-5090

Dear Mr. Mardock:

Thank you for the opportunity for Lone Star Ag Credit's Board to comment on Farm Credit Administration's (FCA or Agency) proposed capital rule. The Agency's efforts to modernize Farm Credit System (FCS) capital requirements should result in a framework that is consistent with Basel III standards applied to other financial institutions. We believe that adopting Basel III standards for the FCS will enhance investor understanding of the FCS's financial strength and increase marketability of third-party capital and debt securities, especially in periods of stress, thereby enabling the FCS to fulfill its mission.

We appreciate the Agency's efforts to carefully consider and accommodate the FCS's cooperative structure in developing the proposed capital framework. While FCA has done an admirable job in drafting the proposed capital rule, we are concerned that it does not strike the appropriate balance between supporting and protecting the cooperative structure on which Congress based the FCS and aligning with the Basel III concepts written for joint stock companies. Unfortunately, some parts of the Agency's proposal have the potential to undermine our cooperative structure. As a result, we ask that FCA pursue revising the proposed rule after reviewing comments from other System entities and our comments below so that the final capital rule is both workable and supportive of the FCS's congressionally mandated cooperative structure:

1. Eliminate the requirement that FCS institutions obtain shareholder votes on the capitalization bylaw changes required by the proposed rule. This requirement puts the institution and its member-customers in an awkward situation if member-customers do not approve the bylaw changes. I appreciate FCA's desire to ensure that the capital plan features of each FCS institution are effectively communicated to their member-owners. However, rather than direct capitalization bylaw changes, the FCA should rely on board policies, directives, loan documentation or capital plans for such communication. Structurally, a board directive or similar document could accomplish the same outcome as a capitalization bylaw vote.

2. Reduce the proposed revolvement period for Common Equity Tier 1 (CET1) and permit the normal revolving features of loan-based cooperative equity plans. There is no basis in Basel III for the proposed 10-year revolvement cycle of an individual

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share, and it is fundamentally inconsistent with cooperative principles. It is also unnecessary given the other proposed capital controls. For cooperative capital, the length of time a share is outstanding is irrelevant to permanence. Rather, permanence is determined by member-customers' clear understanding that their shares are at-risk and committed to the long-term financial stability of their cooperative.

3. Eliminate the concept of 10-year revolvement cycles for association investments in their funding bank to qualify for CET1. Within the closed FCS cooperative structure, requiring a revolvement cycle for association-held bank equities is unnecessary, inefficient, ineffective, and without any discernable benefit. Each affiliated association's capital investment is understood and legally structured as a permanent capital contribution to the bank that is fully at risk and available to absorb losses. The law requires affiliated associations to capitalize and obtain funding from a Farm Credit Bank, which means they need to maintain a permanent investment in the bank. The ability to adjust this investment is critical for ensuring associations share proportionately and appropriately in bank capitalization and risk of loss. It is unnecessary to require each association's individual bank shares to be outstanding for 10-years to qualify as CET1. This requirement means that the bank will be unable to function as a cooperative or equalize capital investments. It is critical FCA understand that the permanence of the bank capital is entirely unaffected by how capital is equalized among affiliated associations. I ask that FCA provide flexibility for banks to equalize capital investment among affiliated associations without compromising CET1 treatment.

4. Revise the proposed "safe harbor" provision that authorizes limited distributions, including stock retirements, without FCA prior approval. In addition, the "haircut deduction" for early distributions should be eliminated from the proposed regulations and handled through examination.

5. Eliminate or refine the unallocated retained earnings (URE) sub-limit embedded within the proposed Tier 1 leverage requirement. The proposed sub-limit implies URE is of higher quality than CET1.

6. Reduce the proposed Tier 1 leverage requirement to 4% to be consistent with Basel III standards implemented by regulators across the globe. The proposed 5% standard appears to deviate from Basel III and could raise questions about the FCS's

risk profile compared to other lending institutions. Such questions could harm the FCS and its mission achievement. I ask FCA to establish a 4%Tier 1 leverage ratio consistent with the Basel III guidance.

7. Maintain the 50% and 20% risk-weight treatment of rural electric cooperative assets consistent with the current regulatory treatment. In our opinion, there has not been an observable change in the overall risk profile of the electric cooperative industry that would support any changes. The proposed rule could also adversely affect the FCS's capital capacity to serve this industry and place it at a competitive disadvantage compared to other lenders who finance this industry.

Please consider the comments above in order to make the proposed capital rule workable and effective from a safety and soundness perspective and consistent with the implementation of Basel III by other regulators. These comments are meant to ensure that the FCS can function consistent with cooperative principles for the benefit of its member-customers as Congress clearly intended.

We feel it is our responsibility as a Board to protect the System's cooperative structure. This cooperative structure sets us apart from other financial institutions and it has given us the ability to fulfill our mission for nearly 100 years.

Lone Star's Board appreciates the opportunity to comment on this proposed rule and FCA's willingness to consider our feedback.

Sincerely,

Tom Johnson
Lone Star - Board Chairman