



**National Rural Utilities
Cooperative Finance Corporation**

Created and Owned by America's Electric Cooperative Network

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Via Electronic Mail to reg-comm@fca.gov

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**Re: Proposed Rule: "Federal Agricultural Mortgage Corporation General Provisions; Federal Agricultural Mortgage Corporation Governance; Federal Agricultural Mortgage Corporation Risk Management; Federal Agricultural Mortgage Corporation Disclosure and Reporting; Farmer Mac Corporate Governance and Standards of Conduct"
12 CFR Parts 650, 651, 653 and 655, March 26, 2015**

Introduction

The National Rural Utilities Cooperative Finance Corporation ("CFC"), a nonprofit member-owned cooperative, appreciates the opportunity to respond to the request for comment on the proposed rule (the "Proposed Rule") published by the Farm Credit Administration ("FCA") regarding FCA's consideration of regulations relating to the Federal Agricultural Mortgage Corporation's ("Farmer Mac") corporate governance. FCA has requested comments to the Proposed Rule and CFC is submitting comments in the following three areas: 1) requiring directors to have an affiliation with a stockholder, 2) allowing directors with affiliations to a stockholder to provide non-private, non-privileged information to such stockholder and 3) requiring agents to be subject to potentially burdensome disclosures and compliance.

Background on CFC

CFC is a member-owned cooperative association incorporated under the laws of the District of Columbia in April 1969. CFC's principal purpose is to provide its members with financing to supplement the loan programs of the Rural Utilities Service ("RUS") of the United States Department of Agriculture. CFC makes loans to its rural electric members so they can acquire, construct and operate electric distribution, generation, transmission and related facilities. CFC also provides its members with credit enhancements in the form of letters of credit and guarantees of debt obligations. As a cooperative, CFC is owned by and exclusively serves its membership, which consists solely of not-for-profit entities or subsidiaries or affiliates of not-for-profit entities. CFC funds its activities primarily through a combination of publicly and privately held debt securities and member investments.

CFC is a public reporting company with securities registered on the New York Stock Exchange ("NYSE") so it is subject to the rules and regulations of both the Securities and Exchange Commission ("SEC") and NYSE. By way of background, CFC is also the owner of a portion of Farmer Mac's Class A Common Stock; 5.875% Non-Cumulative Preferred Stock, Series A; and 6.875% Non-Cumulative Preferred Stock, Series B.

Farmer Mac's Important Role in Rural Electric Lending

Rural electric utilities are acutely reliant on capital to meet the demands of replacing aging infrastructure, deploying system automation technologies and boosting energy efficiency efforts. Affordable financing is critical for rural electric cooperatives to invest in new, and upgrade existing, transmission and distribution projects nationwide. These projects, in turn, enable them to provide safe, reliable and affordable electric service and ultimately benefit rural consumers in the form of lower electric bills.

Under its charter, Farmer Mac is permitted to purchase, and guarantee securities backed by, rural electric loans made by lenders organized as cooperatives to borrowers who have received or are eligible to receive loans under the Rural Electrification Act of 1936 ("REA"). The REA is administered by the RUS. Farmer Mac's activities are intended to provide lenders with an efficient and competitive secondary market that enhances these lenders' ability to offer competitively-priced financing to rural borrowers. This secondary market is designed to increase the availability of long-term credit at stable interest rates to America's rural communities and to provide rural borrowers with the benefits of capital markets pricing and product innovation. The secondary market provided by Farmer Mac functions as a bridge between the capital markets and the agricultural and rural credit markets by attracting new capital for financing rural borrowers.

Farmer Mac has a significant role in financing loans to rural electric cooperatives. As of March 31, 2015, the aggregate outstanding principal balance of rural utilities loans held by Farmer Mac was approximately \$1.0 billion. Additionally, Farmer Mac and CFC have entered into a revolving note purchase agreement, as amended, which allows CFC to borrow, repay and reborrow up to \$4.5 billion through January 11, 2020. As of February 28, 2015, CFC had approximately \$1.9 billion outstanding to Farmer Mac under the revolving note purchase agreement. The proceeds from the revolving note purchase agreement can be used by CFC to make additional loans to its rural utility members.

Public Company Regulation

Before addressing our comments to the Proposed Rule, we wish to note that as a public reporting company with securities registered on the NYSE, Farmer Mac's corporate governance must comply with the rules and regulations of the SEC, NYSE and the Sarbanes Oxley Act of 2002, as amended (collectively, the "Securities Regulations"). The Securities Regulations require Farmer Mac to meet extensive corporate governance standards and regularly disclose material information to maintain a transparent relationship between Farmer Mac and its stockholders. In addition, the Securities Regulations have been revised over time and are expected to continue to evolve to address changes in the financial services industry and changes in best practices. Therefore, FCA should exercise caution in proposing corporate governance changes for Farmer Mac as these may, and in some cases the Proposed Rules do, conflict with existing Securities Regulation or no longer meet corporate governance best practices as these continue to evolve.

We would also like to note that Farmer Mac has developed a sophisticated corporate governance framework that exceeds the requirements of both Securities Regulations and best practices. Farmer Mac continues to review its corporate governance and has implemented many additions to improve risk management and improve accountability to stockholders. Given Farmer Mac's requirements under the Securities Regulations and history of strong corporate governance, we believe

Farmer Mac will continue to assess and evolve its corporate governance without need for the additional regulations set forth in the Proposed Rule.

Requiring Directors to be Affiliated with Stockholders

Farmer Mac, like many public companies, has different classes of stock with certain classes able to elect directors. Directors elected by a certain class of stockholders are typically selected because they have particular experience or skills that provide them a perspective that is either similar to the stockholders of that class or makes them likely to view issues similar to those stockholders. However, Section 651.30(c) of the Proposed Rule requires that “elected director candidates must have a recognized affiliation or relationship with their respective class of voting stockholders.” The Supplementary Information accompanying the Proposed Rule indicates that the FCA considers a “recognized affiliation” as an “official” affiliation between the director and one of Farmer Mac’s stockholders. As stated above, each class of stockholders will elect directors that they believe share a common perspective with the investors. Requiring directors to have an official affiliation with a stockholder is therefore unnecessary.

Additionally, if a director has an official affiliation with a stockholder, the director is more likely to represent the interests of that stockholder above the class of stockholders. CFC currently holds approximately 8% of Farmer Mac’s Class A Common Stock. Holders of Class A Common Stock are entitled to elect 5 directors. CFC prefers to elect directors with experience that makes them likely to share CFC’s perspective but that do not have an official affiliation with any particular stockholder due to concerns over their loyalty to that stockholder. Requiring director affiliations may cause an unnecessary conflict between the director and Farmer Mac and it may make it difficult for the class of stockholders to agree on a director as other stockholders, like CFC, likely prefer a director with a common perspective with the class of stockholders but no official affiliation with a particular stockholder. While we appreciate FCA’s concerns that directors be accountable to the stockholders, the Proposed Rule will likely result in desirable candidates being excluded from the board, and increasing director accountability to only one stockholder but decreasing accountability to the class of stockholders.

Disclosure of Non-Private, Non-Privileged Information

In the Supplementary Information accompanying the Proposed Rule, FCA correctly states that “common law corporate principles affirm the fiduciary duty of directors to act in the best interest of Farmer Mac and all of its stockholders.” However, Section 651.40(d) of the Proposed Rule goes on to say that, “no director of the Corporation may be prohibited by confidentiality agreements or Corporation policies and procedures from publicly or privately commenting orally or in writing on non-private or non-privileged corporate business and related matters.” This section is problematic for a number of reasons as it is contrary to Securities Regulations and common law fiduciary duties, ambiguous, may harm full and frank discussion among board members, and is contrary to corporate governance best practices.

The presence of directors with affiliations to a particular stockholder in a board room raises two confidentiality concerns. First, such directors may have an incentive to provide sensitive or confidential information to their stockholder affiliate. The Proposed Rule allows “non-private or non-privileged” information to be disclosed to affiliate stockholders. Neither term has a fully developed meaning under case law and is likely to be interpreted broadly by a director seeking to disclose

information to the affiliated stockholder. Using ambiguous standards like “non-private and non-privileged” may result in over-disclosure of sensitive or confidential information due to a director’s ties to an affiliate stockholder. The incentive to disclose is further exacerbated by Farmer Mac’s difficulty in discovering when and what type of information directors are disclosing to stockholder affiliates.

Second, any information a representative director provides to a stockholder relating to board room discussions are likely to harm the trust and openness vital to a fully functioning board of directors. In the course of fulfilling their fiduciary duties to Farmer Mac, directors are entrusted with a significant amount of information that is non-public, in addition to information relating to how the board operates and the views and perspectives of each director. Such information could be potentially disruptive or embarrassing to the director if disclosed or could simply undermine the director’s expectation of confidentiality. If directors are aware that information is being relayed to affiliate stockholders, directors may censor their thoughts, not provide as much context when discussing issues, or simply refuse to speak for fear of having the conversation relayed to an unaffiliated stockholder. FCA states that the intention of the Proposed Rule is to “allow directors to converse with stockholders as a means of gathering information, gaining insights into stockholder wishes, and demonstrating accountability.” However, in allowing disclosure to stockholders, the Proposed Rule is undermining full and frank board discussion which may impair the effectiveness of the board and cause significant corporate governance risk. This is neither in the interest of Farmer Mac nor the stockholders of Farmer Mac.

In light of the potential harm director disclosure of any company information may have, current best practice is to establish a confidentiality policy or confidentiality agreements that clearly delineate what information may not be disclosed by a director. This allows companies to be proactive in preventing disclosure of sensitive or confidential information and to address any disclosures that occur that are deemed harmful to the company or board discussions. Unfortunately, Section 651.40(d) of the Proposed Rule would prohibit confidentiality agreements or policies from addressing this potential harm. Section 651.22(b)(1)(iv) goes even further to create an exception for imputed interest of any entity for purposes of determining conflicts if the entity is “directly connected to the representational affiliations required by the Act for elected directors.” This section effectively allows directors employed or otherwise affiliated with a stockholder to engage in board deliberation and to vote on matters on which they have a conflict of interest. This is the anti-thesis of corporate governance best practices and contrary to applicable law. CFC therefore believes that Section 651.40(d) and Section 651.22(b)(1)(iv) of the Proposed Rule should be deleted to allow Farmer Mac to address disclosure by directors in accordance with best practices in corporate governance.

FCA should also consider that some shareholders of Farmer Mac may be in competitive lines of business. If FCA were to enact Section 651.30(c) of the Proposed Rule, shareholders that do not have an official affiliation with a stockholder could be significantly disadvantaged. In the event shareholders are in competitive lines of business, a shareholder with an official affiliation with a director may obtain information that provides an unfair competitive advantage over a shareholder without an official relationship with a director. If board membership is used as a means of obtaining confidential information, this could lead to hostility between shareholders and the departure of non-affiliated stockholders. Such actions could reduce board diversity, confuse director fiduciary duties, and potentially lead to director liability under the Securities Regulations.

Agent Disclosures and Compliance

The Proposed Rule includes a series of disclosure requirements, prohibitions, and penalties on agents, including requiring them to comply with a conflict of interest policy (to be developed under the Proposed Rules). Agents are defined as “any person (other than a director, officer or employee of the Corporation) who represents the Corporation in contacts with third parties or who provides professional services such as legal, accounting, or appraisal services to the Corporation.” This definition of “agents” is so broad that it would require almost any person who does business with Farmer Mac to comply with the Proposed Rule. Such a requirement is administratively burdensome and unnecessary.

Corporate governance best practices require directors, officers and employees to comply with a written conflict of interest policy since there is an important concern that individuals acting in these capacities could encounter a conflict that could cause them to make decisions in conflict with the company’s best interest. The harm could be severe since these individuals may be placed in positions in the company to make major decisions and the fact that their title within the company carries implied authority with third parties. The same concern does not apply to agents. Agents are separate legal entities whose rights are limited by contractual agreement. Additionally, these agreements provide for reporting and other monitoring which is not required of directors, officers and employees. Due to the presence of these agreements and the fact that they are entities separate from the company, there is little or no benefit a company would obtain from requiring agents to comply with a conflict of interest policy. However, the burdens of such requirement will be great since most companies doing business with Farmer Mac will be considered “agents” under the Proposed Rule and need to evidence compliance. We therefore believe FCA should rely on Farmer Mac’s current practice of monitoring compliance with contractual agreements to ensure any person engaging in business with Farmer Mac is acting in Farmer Mac’s interest.

Conclusion

While CFC appreciates the FCA’s requirement that directors owe their fiduciary duties to Farmer Mac and not any particular stockholder, we are concerned that requiring directors to have affiliations with stockholders may preclude stockholders from being able to elect their ideal candidates. Most stockholders prefer that a director share the same perspective as the stockholders as a class and not have affiliations with any one particular stockholder. Additionally, allowing directors to disclose information to an affiliated stockholder is likely to result in director and stockholder distrust, disputes, and an erosion of the effectiveness of the board as the keystone of Farmer Mac’s corporate governance. It also hamstring Farmer Mac from effectively developing policies to address director conflicts in accordance with corporate governance best practices. Therefore, FCA should exercise caution in proposing corporate governance changes for Farmer Mac that conflict with corporate governance best practices and existing Securities Regulation, including the rules and regulations of the SEC.

We also believe that the Proposed Rules should exclude agents for complying with the same disclosure and compliance obligations as Farmer Mac’s directors, officers and employees. Such a revision will prevent Farmer Mac and third parties engaging in business with Farmer Mac from burdensome compliance with little benefit.

We appreciate your consideration of the above matters and welcome the opportunity to further discuss our views. Please do not hesitate to contact Brad Captain by phone at (703) 467-1646 or by email at brad.captain@nrucfc.coop should you wish to discuss any of our comments or need additional information.