



THE FARM CREDIT COUNCIL

April 25, 2016

Ms. Laurie A. Rea
Director, Office of Secondary Market Oversight
Farm Credit Administration
1501 Farm Credit Drive
McLean, Virginia 22102-5090

RE: Proposed Rule– RIN 3052-AC86 / Federal Agricultural Mortgage Corporation/
Federal Register 81, No. 35 (February 23, 2016) 8860

The Farm Credit Council (Council), on behalf of its membership, appreciates the opportunity to comment on the Farm Credit Administration's (FCA) Proposed Rule regarding Federal Agricultural Mortgage Corporation (Farmer Mac) investment eligibility requirements that was published in the February 23, 2016 Federal Register. The comments that follow were developed after soliciting input from all our members (the "System"). These comments are also submitted in accord with the Policy Resolutions adopted by our members.

Some institutions of the System, including System stockholders in Farmer Mac may be submitting their own comments, and we urge the FCA to consider their views as well as those expressed herein.

GENERAL COMMENTS

The background section of the proposed rule identifies Farmer Mac as an institution of the FCS, regulated by FCA through its Office of Secondary Market Oversight, with a mandate to create a secondary market for specific types of loans.

As a threshold matter, we note, as has FCA in previous rulemakings, that Farmer Mac "has a public policy purpose embedded in its corporate mission." We strongly support the FCA's view that Farmer Mac, as a government sponsored enterprise (GSE) with this public policy, is not like state-chartered, stockholder owned companies, who seek to maximize returns to investing stockholders.

The Farm Credit Act (the "Act") did not mandate creation of an investor class of stockholders, which is the model under which Farmer Mac now operates. This model has been widely criticized as a contributing factor in the failure of two other GSEs, Fannie Mae and Freddie Mac, and the financial crisis of 2007-2008.

As we commented previously in regard to Farmer Mac governance regulations, the potential for conflict between the entity's public policy mission and investor goals for

stock appreciation are inherent. We believe that Farmer Mac's ownership model, coupled with its practice of compensating directors and employees with stock and stock options exacerbates that potential conflict. As has been noted with other GSEs, the risks associated with seeking short term gains, and foregoing opportunities to retain earnings and to build capital have caused significant problems. Whatever merits may exist for an investor class of stockholders seeking return on investment, FCA should implement robust capitalization and liquidity regulatory requirements that are no less stringent than requirements applicable to Farm Credit System institutions. In our view, FCA has consistently implemented lower safety and soundness regulatory standards for Farmer Mac and implemented a regulatory environment that favors program activities over long-term financial safety and soundness. This current rulemaking is yet another example of FCA's permissive regulatory approach given it allows Farmer MAC to meet liquidity requirements using program related assets, specifically qualifying securities backed by Farmer Mac program loans guaranteed by the United States Department of Agriculture. Allowing Farmer Mac to count its own program securities in regulatory liquidity reserves requirements is inconsistent with regulatory standards applicable to other regulated financial institution, including Farm Credit banks. We can find no policy or business rationale for this inconsistency. The purpose for the liquidity reserve is to hold marketable assets beyond program assets as a financial cushion in the event Farmer Mac is unable to issue debt securities directly. In our view this leniency is exacerbated by Farmer Mac's reliance on regulatory capitalization requirements based on an internal economic model that fails to meet the current industry standards and the Basel Committee recommendations. FCA should hold Farmer Mac to at least as stringent liquidity and capitalization standards as are applicable to Farm Credit System institutions.

Specific Comments

The following are the specific comments on the proposed Farmer MAC Investment Eligibility proposed rule:

1. Concentration Risk [New § 652.10(c)] –We commend the FCA for addressing the level of single obligor credit risk that Farm MAC may have in non-program investments. As one might recall, investment risk concentration s were a critical factor in the near collapse of Farmer Mac in 2008, which resulted in the Farm Credit banks and others assisting to recapitalize it. The recapitalization meant Farmer Mac did not trigger statutory enforcement requirements because of deficient capital levels after recognition of non-program investments losses. In light of this past experience, concentration risk and capital levels are inherently linked, with high capital required when concentration risks are greater. Our concern is the proposed concentration limit appears appropriate for well capitalized financial institutions that meet or will meet Basel III capital requirements. This is not the case for Farmer Mac. Therefore, FCA should consider more restrictive concentration limits for Farmer Mac. Moreover, Farmer Mac capitalization is based on a regulatory required internal economic capital model that is not consistent with Basel III capital requirements. Allowing Farmer Mac to leverage its

already thin capital base in concentrated assets does not appear consistent with long-term financial dependability and resiliency. FCA should consider lowering the proposed concentration limit to 5 percent.

2. Eligible Non-Program Investment [§ 652.20 (a)(4) and (5) – As discussed in the General Comment, the proposed rule does not specifically exclude Farmer Mac securities as eligible securities in the definition of applicable to GSE Asset Backed Securities (ABS) and Mortgage-Backed Securities (MBS). We ask that the FCA amend the proposed § 652.20 (4) and (5) to specifically exclude Farmer MAC securities from the GSE ABS and MBS securities as eligible non-program investments.
3. Table to §652.40(c) Repurchase Agreement – The proposed table permits Farmer Mac to count repurchase agreements made up with Level 1 assets in Level 1 of the liquidity reserve requirement. Importantly, FCA did not propose a similar treatment of repurchase agreements for Farm Credit System institutions. If the FCA feels that repurchase agreements secured by Level 1 assets should be included with overnight money market, then we ask FCA to modify the regulations for the other Farm Credit System institutions to be consistent on that point. Otherwise, FCA is again providing Farmer Mac with a more permissive regulatory framework than applicable to Farm Credit System institution with no discernable or stated policy basis for the different treatment. While these repurchase agreements with Level 1 assets appear to meet the liquidity standards, the operational and legal requirements to convert these pledge securities into cash in a timely manner should be considered prior to finalization of the inclusion of these assets in the liquidity regulations. Repurchase agreements would appear more appropriate to include at Level 3 if they are to be considered as a liquid asset.
4. Table to §652.40(c) GSE Debt – The Level 1 assets include GSE senior debt with maturities less than 60 days and specifically excludes Farm Credit System debt. The regulation should be expanded to specifically exclude all Farmer Mac program securities held on balance sheet. We also believe that it is essential that FCA be clear that Farm Credit System and Farmer Mac debt are not in any way linked. They are not. Farmer Mac's debentures have long been confused with the FCB's debt issuances which are rated, insured and have a developed secondary market. FCA should make it clear in the table the Farm Credit System debt is separate and apart from Farmer Mac debt. One way to clarify this matter is to not exclude Farm Credit System debt from Level 1 in this regulation, which would be a clear indicator of the fact that there is no connection between Farmer Mac debt and Farm Credit System debt. We make the same observation and comment with respect to the Level 3 assets which includes GSE debt with maturities greater than 60 days, excluding Farm Credit System debt. For the reasons already stated, FCA should also exclude all Farmer Mac program securities held on balance sheet.

5. Table to §652.40(c) Qualifying securities backed by program assets – For the reasons discussed in the General Comment, the FCA should reconsider the inclusion of Farmer Mac qualifying securities backed by certain program asset securities as Level 3 securities. Additionally, Farmer Mac has not developed a liquid secondary market for these types of qualifying securities, in fact they rarely trade and almost all of the current securities are held by Farmer Mac internally to generate income to pay dividends to its stockholders and incentives to management. We can see no policy or financial rationale that certain qualifying securities should be included in the liquidity reserve and we note that FCA has not provided Farm Credits System institution a similar treatment with respect to its various loan assets made under various lending authorities that are analogous conceptually with Farmer Mac’s program activities. FCA should eliminate this preferential inclusion of Farmer Mac’s program assets in the liquidity reserve. Including program assets in its liquidity requirement appears as a way to allow Farmer Mac to avoid holding lower yielding, but higher quality liquid investments that would strengthen its liquidity position but would lower Farmer Mac’s overall earnings performance. We also note that qualifying program securities are not included in the list of eligible non-program assets found in § 652.20. As a result, FCA should be consistent with its regulatory framework and not include such program securities in the liquidity reserve.

Conclusion

We appreciate the opportunity to comment on the Proposed Rule on Farmer Mac Investment Eligibility. We believe that with some minor adjustments as we highlighted in this letter, the rule would significantly strengthen and enhance the long-term financial strength of Farmer Mac. Our members are significant Class B voting shareholders in Farmer Mac, and care deeply that Farmer Mac operate in a safe and sound manner that fulfills its public policy mission, and that does not expose the System to undue risk.

Sincerely,



Charles P. Dana
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