

Via Electronic Submission

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Office of Regulatory Policy,
Farm Credit Administration
1501 Farm Credit Drive
McLean, VA 22102-5090

November 9, 2020

RE: Proposed Rule: Regulatory Capital Rules - Tier 1/Tier 2 Framework (Proposal)¹

Ladies and Gentlemen:

The American Bankers Association (ABA)² appreciates this opportunity to provide our views on several aspects of the Proposal, which would revise the regulatory capital framework applicable to institutions of the Farm Credit System (FCS). ABA is concerned that certain aspects of the Proposal would increase risks to the safety and soundness of FCS institutions and their ability to absorb losses, potentially destabilizing financial markets. In addition, certain aspects of the proposal depart from the regulatory capital framework of the Federal banking agencies,³ which would create or exacerbate competitive inequities in agricultural lending. Specifically, ABA believes the Proposal:

- Suggests that patronage refunds and other cash distributions could be paid without FCA approval, without regard to increases in an institution's overall size and other aspects of its risk profile compared to the prior year; and
- Would permit retirement of certain CET1 capital⁴ without FCA approval, without regard to emerging risks or other conditions that warrant the exercise of supervisory oversight.

¹ See 85 *Fed. Reg.* 55786 (September 10, 2020), available at <https://www.govinfo.gov/content/pkg/FR-2020-09-10/pdf/2020-16052.pdf>.

² The American Bankers Association is the voice of the nation's \$21.1 trillion banking industry, which is composed of small, regional and large banks that together employ more than 2 million people, safeguard nearly \$17 trillion in deposits and extend nearly \$11 trillion in loans.

³ As used in this letter, "Federal banking agencies" means the Office of the Comptroller of the Currency, the Board of Governors of the Federal Reserve System, and the Federal Deposit Insurance Corporation.

⁴ Defined at 12 CFR §628.20(b)

Discussion

1. Cash payouts should be allowed only after considering all regulatory measures of an institution's risk, not just the amount of its capital in the prior year.

The Proposal includes a liberalization of the “Safe Harbor Deemed Prior Approval” exception to the requirement for FCA approval of cash distributions, including patronage refunds. Under the Proposal, such payments would be permitted if the dollar amount of CET1 capital at the quarter-end after the declaration date equals or exceeds the dollar amount of CET1 capital on the same quarter-end in the previous calendar year.⁵ Under this formulation, as indeed is true under the existing regulatory capital regime, cash distributions are permitted based on the dollar amount of CET1 as of an earlier date, notwithstanding that an FCS institution in the meantime may have expanded its risk assets relative to the prior year's CET1 capital. Thus an institution's potential risk may have increased considerably when its loss-absorbing capacity (after the permitted cash distribution) has not. Permitting cash payouts based only on maintaining the dollar amount of CET1 capital in a prior year takes insufficient account of these potential risk increases.

ABA notes that under the current FCS regulatory capital framework, the “deemed prior approval” of cash distributions is conditioned on the institution's compliance with “all regulatory capital requirements and supervisory or [sic] enforcement actions.”⁶ In addition, the “deemed prior approval” is currently subject to capital distribution restrictions specified in 12 CFR §628.11,⁷ which establishes “capital conservation buffers” that limit payouts of retained earnings. The Proposal does not refer to these limitations, but any final regulation should make clear that these limitations remain in effect, and that an FCS institution cannot distribute cash that would breach its conservation buffer, regardless whether it would still have CET1 capital equaling the level in the relevant quarter of the previous year.

2. Retirement of an institution's stock without specific FCA approval should be strictly limited to protect the safety and soundness of FCS institutions.

The Proposal would permit (and current FCA regulations do permit) FCS institutions to retire stock, including stock counted as CET1 capital, without FCA approval if the institution meets holding periods for the stock and other regulatory requirements.⁸ The Proposal notes that it will clarify those requirements to state expressly that an institution may redeem statutory borrower stock only if, after such redemption, the institution continues to comply with all minimum regulatory capital requirements.⁹ ABA acknowledges and appreciates FCA's clarification, but notes that the Proposal would still leave FCS institutions subject to very lax requirements

⁵ Proposal at 55788.

⁶ Proposal at 55787.

⁷ See 12 CFR §628.20(f)(5).

⁸ See 12 CFR §628.20(b)(1)(xiv)(B).

⁹ Proposal at 55794.

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concerning stock redemptions compared to those applicable to commercial banks, who must maintain the ability to compete with FCS institutions to serve their customers and communities. National banks, for example, may redeem or repurchase capital stock without prior approval of the Office of the Comptroller of the Currency only in very limited circumstances.¹⁰ These restrictions, which apply notwithstanding a national bank's compliance with the Federal banking agencies' regulatory capital frameworks, are designed both to protect the safety and soundness of the issuing institution and to prevent abuses in transactions with stockholders. These considerations apply with equal force to FCS institutions, and similar supervisory requirements and oversight should apply to their stock retirement.

Thank you for the opportunity to express our views on these important issues. Should you have any questions, please do not hesitate to contact the undersigned at hbenton@aba.com.

Very truly yours,

A handwritten signature in black ink, appearing to read "Hu A. Benton". The signature is fluid and cursive, with the first name "Hu" and last name "Benton" clearly legible.

Hu A. Benton
Vice President, Banking Policy

¹⁰ See 12 USC §59; 12 CFR §7.2020.