YOSEMITE FARM CREDIT

Helping Our Members Prosper!

800 W. Monte Vista Avenue
Turlock, CA 95382
P.O. Box 3278
Turlock, CA 95381
Office: 209-667-2366
Fax: 209-634-9612

www.yosemitefarmcredit.com

June 6, 2014

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

RE: Proposed Rule on Standards of Conduct – RIN 3052–AC44 / *Federal Register* 79 (February 20, 2014) 9649-9661

Dear Mr. Mardock:

Ethical business practices and a culture of honesty and fairness are critically important to Yosemite Farm Credit, ACA (YFC).

In fact, in the most recent Report of Examination (March 31, 2014), FCA applauds the YFC standards of conduct program noting that "The Association holds directors, employees and agents to high ethical standards of conduct". The report also points out that while several improvements can be made to strengthen existing internal controls, overall, the YFC Standards of Conduct program, director elections, and training programs at YFC "provided a sound basis for conducting an ethical organization".

Given our culture, we appreciate FCA's effort to clarify the existing standards of conduct regulation. However, in our opinion, many of the regulatory changes being proposed by FCA are unnecessarily burdensome and would be a real disincentive to serving on the board. The proposed changes also appear to be an overreaction to isolated problems involving the purchase of Farm Credit System acquired properties at other institutions. It is important to point out that research indicates there are no standards of conduct regulations or requirements applicable to federally insured depository institutions that are in any way comparable to many aspects of the existing or proposed FCA Standards of Conduct regulations.

Key Areas of Concern

There are many problematic issues and concerns about the proposed regulation, as set forth in detail in comment letters being submitted by CoBank and the Farm Credit Council. We support and endorse those letters.

In addition, we have the following areas of concern that we feel warrant special commentary.

1. Standards of Conduct Official Approval for Ordinary Course of Business Transactions with Borrowers-Proposed § 612.2136

The FCA Preamble to the proposed rule states as follows:

> "The proposed rule would add a new § 612.2136 on conflicts of interest. It would require immediate reporting of conflicts of interests and would supplement employee's and director's existing annual and periodic reporting requirements. Paragraph (b) would require recusal from any board action on, discussion of, or any other official action on or discussion of, those matters. For example, if a director or employee were to purchase farm equipment such as a combine harvester from a known borrower, the purchase should be reported and reviewed by the Standards of Conduct Official for conflicts.

Directors (and some employees and their spouses who also farm) routinely purchase feed, equipment, livestock and other goods and services from other farmers. In many cases, especially in smaller communities, some of the other parties to the transaction can be Farm Credit borrowers.

We feel strongly that a regulatory requirement to obtain prior approval from the Standards of Conduct Official is unnecessary and burdensome for ordinary course of business transactions involving purchases or sales of goods, services or other property. The proposed regulation also shifts the role of the Standards of Conduct Official from a corporate officer to an enforcement official.

The boards of directors at most System institutions no longer participate in the loan approval or loan collection process. These responsibilities have been delegated to management. This removes the potential for conflict of interest regarding ordinary course of business purchase and sale transactions between directors and borrowers. Regarding employees, many employees also are not involved in loan approval or the loan collection process.

The proposed regulation unreasonably interferes with the director's (or employee's) ability to run their farming business. YFC is a lender that operates with the highest integrity. It is not reasonable to require that YFC monitor director and employee daily activity taken in the ordinary course of business. Except for real estate purchase transactions (which can take weeks or months to close escrow), directors and employees will not have the time to obtain Standards of Conduct approval before entering into a purchase or sale transaction with a borrower, particularly those transactions involving the purchase of feed, equipment, livestock or other goods and services. Therefore, as written, the proposed regulation would be a serious disincentive for serving as a director (or employee) and has the potential to place the standards of conduct official in the middle of a number of ordinary course of business transactions on a daily basis.

Another concern is that directors and employees do not necessarily know whether the person with whom they are doing business is a Farm Credit borrower. Under the proposed regulation, a director or employee can be deemed to have violated the standards of conduct if an auditor takes the position that the director or employee "had reason to know" that the other party to the transaction was a borrower even though the director or employee had no actual knowledge that they were doing business with a borrower.

Therefore, we ask FCA to revise the proposed rule to provide as follows:

- No prior approval (or post-transaction approval) is needed from the Standards of Conduct Official for ordinary course of business transactions between borrowers and directors or employees involving the purchase or sale of goods, services or other real or personal property.
- With regard to the purchase or sale of goods, services or other personal property in the ordinary course of business, a director or employee will be required to report to the Standards of Conduct Official on a post-transaction basis if the director or employee had actual knowledge that the other party to the transaction was a borrower, but if and only if:
    a. In the case of a director, the institution's board had not previously delegated to management authority to approve and collect loans; or
    b. In the case of an employee, the employee's job duties include loan approval or loan collection.
- In our experience, real property transactions do not occur as frequently as do transactions involving the purchase or sale of goods, services or other personal property, making it less burdensome to require reporting of these transactions in all cases where a director or employee actually knows that the other party to the transaction is a borrower. Therefore, with regard to real property purchase transactions, we recommend that the regulation be revised to provide that a director or employee will be required to report a transaction involving the purchase or sale of real property with a borrower to the Standards of Conduct Official on a post-transaction basis provided the director or employee had actual knowledge that the other party to the transaction was a borrower.

We think these changes make the rule more reasonable and workable for all concerned.

2. Prohibited Conduct-- Proposed 612.2145 and 612.2155.

We do not necessarily disagree with these proposed regulations to the extent the regulations prohibit a director or employee from entering into a lending transaction (as opposed to a purchase or sale transaction) with a borrower, subject to Standards of Conduct Official approval or any of the exceptions described in the proposed regulations.

However, we do think that the proposed regulation needs the following modifications:

- The proposed rule currently requires that these determinations made by the Standards of Conduct Official be renewed annually. We think this requirement is unnecessary and burdensome. Once a determination is made by the Standards of Conduct Official, it should only be required to be renewed or modified if the circumstances change.
- Further, the preamble of the proposed rule makes clear that the Standards of Conduct Official cannot ratify prohibited conduct after the fact. This creates an untenable situation where disciplinary action would be immediately required despite the circumstances and intent. In order to strengthen the rule and encourage transparency, the Standards of Conduct Official must have the authority to ratify transactions which have occurred in the past if appropriate.

3. Requirement to Observe FCA "Guidance"—Proposed § 612.2135

The FCA Preamble to the proposed rule states:

> "The words "and guidance" are added to paragraph (b) to make clear that in addition to regulations, policy statements, instructions and procedures, directors and employees must observe "guidance" of the FCA."

The term "guidance" is vague, making compliance with the regulation virtually impossible.

Does "guidance" include statements made by FCA examiners during closeout discussions and or statements and recommendations set forth in FCA's examination close-out letters.

Therefore, we think the phrase "and policy statements, instructions, procedures, and guidance" needs to be stricken in its entirety from the regulation.

Thank you again for allowing us the opportunity to comment on this regulation and we hope that you will find these comments constructive and useful.

Sincerely,

Arnold Barcellos
Board Member