July 19, 2021

Mr. Kevin J. Kramp
Director, Office of Regulatory Policy
Farm Credit Administration
1501 Farm Credit Drive
McLean, VA 22102-5090

Re: Proposed Rule – 12 CFR Part 614 – RIN 3052-AC94; *Collateral Evaluation Requirements*; 86 Federal Register 27308-27323

Dear Mr. Kramp:

AgGeorgia Farm Credit appreciates the opportunity to comment on the Farm Credit Administration's ("FCA") Proposed Rule regarding Collateral Evaluation Requirements that was published in the May 20, 2021 *Federal Register* (the "Proposed Rule").

In order to better analyze the Proposed Rule and prepare a System comment, the Farm Credit Council ("FCC") assembled a workgroup of several Farm Credit System institutions, who met over a period of months to review and discuss the Prepublication Copy of the Proposed Rule, the Proposed Rule, existing regulations, relevant FCA-published materials (including FCA's *Collateral Evaluation Requirements* published in 1992), and materials and authorities relevant to other lending institutions. Members of the workgroup included persons who have significant expertise in underwriting, risk management, legal, and evaluation and appraisal services, and insight was sought from persons outside of the workgroup, as well.

AgGeorgia Farm Credit supports the stated objections and comments in the Farm Credit Council letter to FCA dated July 16, 2021. Based on the review performed and the comments made, AgGeorgia respectfully requests that the Proposed Rule be withdrawn. Rather than recite the entirety of the FCC letter to the agency, we elected to issue a general statement of support of the FCC letter, while specifically highlighting concerns related to a few areas of the proposed rule that were noteworthy to our association.

In general, a number of challenges are presented by the Proposed Rule. Such challenges not only fail to satisfy the goals and objectives identified by FCA but also present compliance issues for Farm Credit System institutions ("System institution(s)") and their appraisers and chattel evaluators, impose costs and burdens on System customers and borrowers, and invite unnecessary confusion and inconsistency within FCA regulations and with related authorities.

1. Preamble – Stated Goals and Approach to the Proposed Rule.

According to the Preamble, the objectives of the Proposed Rule are to: (i) improve the organization and readability of FCA appraisal and evaluation regulations; (ii) clarify expectations for internal controls in appraisal and evaluation practices; (iii) expand authorities on using various sources of appraisers and evaluators as well as specifically authorizing use of automated valuation tools; and (iv) update existing terminology and make other grammatical changes. AgGeorgia Farm Credit agrees that the stated goals are goals worth achieving with regard to collateral evaluation requirements and other laws; however, AgGeorgia believes that the Proposed Rule invites more challenges than it purports to resolve and believes that the existing regulations along with USPAP and other applicable authority provide better guidance for the System with regard to evaluation and appraisal requirements.

2. Proposed 12 CFR § 614.4245 General.

a. Required Appraisals or Evaluations.

The Proposed Rule in 12 CFR § 614.4245(a) provides that: "System lenders must obtain appraisals or evaluations of all collateral used to secure an extension of credit (including leasing activities) or the purchased interest in credit extended by another lender. System lenders must maintain appraisals or evaluations reflecting current market conditions. At a minimum, every item of collateral must be appraised or evaluated both at the time a lien is obtained and when the System lender expects to liquidate its lienhold interest." Proposed Rule 12 CFR § 614.4245.

In certain instances, collateral is taken for control purposes and not for providing needed collateral value. Such decisions are often credit-based decisions, which provide not only risk mitigation to the System institution but may also have a cost benefit to the customer in the form of potentially more competitive pricing.

Requiring all collateral taken as security to be valued does not take into consideration any *de minimis* values, which are especially important when valuing chattel under blanket lien purposes. If all collateral is required to be valued as contemplated under the Proposed Rule, then the accuracy, cost, and convenience associated with such appraisals or evaluations and the appraisal process would be sacrificed. Such costs and inconveniences would not be offset by improved accuracy or reduction in risk; but, instead, would be made at the expense of the System institution and the customer (*e.g.*, the time it would take to value such collateral and complete the required report(s) and the burden it would impose on the customer).

There is a cost associated with each appraisal or evaluation. As the nature of certain types of collateral evolve or as they are added, modified, substituted, replaced, or sold, a cost would be imposed on the System institution and/or the customer, which adds to the overall cost of lending and creates a disincentive to utilizing Farm Credit. This is especially true if a System institution were required to obtain an appraisal or valuation when it releases a lien, which is often when the account is paid down, if not paid in full. Safety and soundness are not furthered in such instances, at least not in proportion to the burdens and costs imposed.

Current practice, by comparison, allows for exclusions based on value to ensure an effort and risk return and to allow for appraisals and evaluations to be made consistent with both the size and risk inherent in the transaction. Requiring an evaluation in every instance would drive up the cost of borrowing, including the cost to young, beginning, and small borrowers, leasing and loan transactions, and loan syndications, loan participations, and other secondary market purchases, where a lot of work has been done to diversify System institution portfolios for safety and soundness and to allow System institutions to be relevant players in these areas.

Collateral is just one of the five factors of credit considered in making loan decisions. With regard to the other four factors, the regulatory framework allows for risk-based standards and guidelines to be established. The Proposed Rule places the collateral consideration into a separate category, requiring increased attention above the other four factors. This is further challenged when considering collateral is not the primary repayment source of the loan and is a secondary source of repayment.

For at least these reasons, this provision represents an incredible and unnecessary cost and burden on the System without any precedent cited for same.

b. Age of Appraisal or Evaluation Reports.

The Proposed Rule in 12 CFR § 614.4245(c) provides that: "It is the responsibility of the System lender to monitor market conditions and trends, loan risk, and collateral conditions to appropriately determine the frequency for performing new or updated collateral appraisals or evaluations in keeping with regulatory requirements. When making credit decisions or approving new or additional funds, the System lender may use existing collateral appraisals or evaluations reports only if the appraisals or evaluations reflect current market conditions at the time of use." Proposed Rule 12 CFR § 614.4245(c).

The Proposed Rule appears to recognize, in some respects, that the System institution should have procedures for determining when and whether appraisals and evaluations may be required to be made with regard to certain credits; however, the balance of this provision of the Proposed Rule limits such discretion or the ability to rely on existing appraisals or evaluations by adding in the "only if" requirement at the end. Such limitation swallows the rest of the Proposed Rule whole.

In many (if not most) instances, it may only be important to determine that the current value is no less than when the transaction was originally put on the books. Given the acceptable risk at time of origination, considering loan paydowns occurring, it may be unusual for agricultural property values in a current market condition to significantly deteriorate ahead of the paydown, depending upon the terms and conditions of the loan. And, with many agribusiness and more complex loans, the terms and conditions of the loan are adjusted to reflect the risk in the loan, including any special use collateral (where loan-to-value requirements or debt coverage ratios may be imposed), collateral subject to fluctuations in price, number, or type (where margin requirements might be required), pricing or payment terms that may adjust (*e.g.*, variable rates, payment frequency, annual renewals, balloon feature), and events of default classifications. In short, the existing regulations allow for System institutions to determine the frequency of

appraisals or collateral evaluations in many respects, and System institutions may account for risk through any number of appropriate ways, including loan terms and conditions and the ability to inspect, appraise, or value the collateral when needed or otherwise appropriate, with appropriate guidance supporting same based on the type of collateral, the amount at issue, and USPAP-compliance, among other things.

3. Proposed 12 CFR § 614.4250 Policies, Standards, and Internal Controls for Valuing Collateral.

The Proposed Rule in 12 CFR § 614.4250 provides for new and additional requirements concerning policies, standards, and internal controls regarding valuations of collateral. Such requirements impose burdens on the System institution that are not seen or imposed under other regulations concerning other lending institutions.

In the Proposed Rule, FCA has made one request for comment on the potential conflict between proposed 12 CFR § 614.4250(c) and existing 12 CFR § 618.8430 with regard to internal controls. The Proposed Rule is prescriptive with a directive of "how" management should establish internal controls over the collateral function. By comparison, 12 CFR § 618.8430 requires internal controls over the function; however, it allows a System institution to determine how to establish and maintain an effective internal control environment. The Proposed Rule requires specific internal control mechanisms that may or may not fit the size and complexity of each System institution's business model. This provision, therefore, would outstrip the purpose and existing guidance of 12 CFR § 618.8430 and would threaten to upset how System institutions develop, maintain, and test their internal control environment, creating an anomaly for appraisals and collateral evaluations alone.

4. Proposed 12 CFR § 614.4265 Valuing Real Property.

The Proposed Rule in 12 CFR § 614.4265 relates to valuing real property collateral. The proposed changes contained in this provision of the Proposed Rule exceed the regulatory requirements imposed on any other regulated lending institution without any explanation or benefit associated with such limitations. Each and every additional burden being prescribed reflects an additional cost or loss for the System institution, making it more difficult to provide agricultural financing at a relatively low cost to eligible borrowers and others who are served by the Farm Credit mission.

For example, the Proposed Rule proposes to continue the current *de minimis* levels of $250,000.00 established in the 1990's with regard to consumer loans, while other banking regulations have moved the *de minimis* amount to $400,000.00 for consumer loans and $500,000.00 for commercial real estate loans. Maintaining a reduced *de minimis* level of $250,000.00 on consumer loans as compared to other lending institutions places System institutions at a comparative disadvantage from a cost and convenience perspective, especially given the burdens and costs associated with other regulatory changes being proposed. At the very least, the $250,000.00 threshold for real estate transactions that require an appraisal should be

increased to $400,000.00 for residential real estate transactions and $500,000.00 for commercial real estate transactions to be in line with the thresholds established by other regulated lending institutions for the same or similar loans. FCC believes that this change would provide a meaningful burden relief from existing appraisal requirements without posing a threat to the safety and soundness of System institutions.

The Proposed Rule also requires an evaluation of all collateral taken out of an abundance of caution. This provision of the Proposed Rule appears to generally ignore FCA's current definition of "abundance of caution," whereby "abundance of caution" collateral is recognized as being that which was not needed for the support of the credit decision (revenue or collateral) or needed for regulatory or other compliance. The Proposed Rule can impact the customer and the various System institution's overall risk profile in, among other things: (i) increasing unsecured lending, which will increase the cost to the borrower by means of increased interest rates due to higher risks associated with credit; (ii) requiring evaluations on collateral that is being taken for control purposes only, which will increase the costs associated with the loans in terms of higher appraisal fees and render a less favorable customer experience; (iii) increasing the related costs substantially, making it cost-prohibitive to serve certain aspects of the market, which impacts the mission while providing nominal, if any, enhanced risk mitigation to the System institution or the System as a whole; (iv) diminishing competition by not adjusting *de minimis* levels to align with other regulatory agencies; and (v) limiting proactive portfolio risk management of obtaining blanket chattel liens, especially for smaller lending relationships (specifically YBS), as System institutions are relational and cash flow lenders, not transactional and net worth lenders.

Additionally, some of the prescriptions being proposed ignore the flexibility of existing regulations or guidance that would allow a System institution the ability to value chattel assets at the "lesser of cost or market" as a value conclusion. While fair market value is applicable in most cases, its exclusive requirement in the valuation of chattel assets is inconsistent with the industry and the broader regulated lending marketing. Similarly, the proposed changes would no longer allow a System institution to have the ability to assign classifications of collateral and adjust internal loan-to-value or margin requirements through its own policies and procedures, which allow for a better reflection of risk and market change and allow for a more appropriate examination of the System institution on a microeconomic level.

Further, some of the requirements, terms, and definitions do not provide additional guidance that are helpful in this area. For example, "material" changes to the property are equal to a new appraisal or evaluation; "adverse market conditions" should be considered in the Proposed Rule as opposed to obvious or material changes if a System institution is satisfied with the value in an existing appraisal; "determining value" is unnecessary and is already addressed within USPAP, and requiring this level of development for evaluations impairs many of the efficiencies inherent within alternative valuation solutions to an appraisal; and "additional report content requirements" is overly burdensome and unnecessary as it is addressed within USPAP, and these requirements, in particular, will cause significant delays and will far exceed the appraisal or evaluation requirements of other regulated lending institutions.

With regard to appraisals that are subject to USPAP, System institutions and appraisers alike should be able to rely on USPAP for current appraisal practices as it evolves and is vetted

through a lengthy public exposure process (*e.g.*, traditionally, every two years). Seemingly similar appraisal practice language codified in FCA's regulations today may starkly contrast with future USPAP requirements, placing appraisers in conflict with laws or standards that regulate their licensure and professional requirements. And, the Proposed Rule also requires a greater level of analysis to support a reported value conclusion, failing to realize that, in some instances, the value of what's described is inherent to the land, as improved, which are reported as one value, such as a ranch property.

In short, with the changes proposed in this provision of the Proposed Rule, the System institution is faced with choosing compliance at a cost, with a burden that makes lending more costly and more inefficient and makes the System institution less competitive, on the one hand, or choosing to make more unsecured loans to avoid the enormous burdens associated with new requirements and unnecessary prescriptions that supplant existing internal guidance that recognizes risks and reward – a balance favoring loan control versus value control, on the other hand. In the context of appraisals and collateral evaluations, the System would be better served by continuing to operate under existing FCA guidance or match-pair with regulations and guidance (*e.g.*, USPAP) applicable to other lending institutions with whom the System competes (or who guarantees System loans) to better ensure consistency, flexibility, and safety and soundness, without placing the System at a competitive disadvantage.

Conclusion

In conclusion, AgGeorgia Farm Credit appreciates the opportunity to comment on the Proposed Rule and to present some of its concerns to FCA for its consideration. For at least the reasons stated herein and in the entirety of the FCC letter, AgGeorgia respectfully requests that FCA withdraw the Proposed Rule so FCA and Farm Credit institutions can engage in a thoughtful and thorough discussion on current collateral evaluation practices and tools and find an alternative that better aligns with the stated aims and objective of the Proposed Rule and protects Farm Credit's ability to serve its customers and fulfill its mission.

We trust that our comments, as well as those comments submitted by FCC and other System institutions, will assist FCA in its consideration of the Proposed Rule. If you have any questions, then please do not hesitate to contact me.

Sincerely,

James R. (Rob) Crain
President & Chief Executive Officer