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Sent via Electronic Mail
Mr. Kevin J. Kramp
Director, Office of Regulatory Policy
Farm Credit Administration
reg-comm@fca.gov

**Re: Proposed Rule, Collateral Evaluation Requirements, 86 FR 27308-27323
Comment to Proposed Rule**

Dear Mr. Kramp:

Farm Credit Illinois ("FCI") appreciates the opportunity to provide comment regarding the Proposed Rule on Collateral Evaluation Requirements (the "Proposed Rule"). FCI submits this comment letter for two purposes. First, FCI joins in the comment letter provided by the Farm Credit Council ("FCC") and incorporates it in every respect into this comment letter. Second, FCI would like to expound upon how some of the concerns with the Proposed Rule outlined in FCC's comment letter could specifically impact FCI. With the foregoing in mind, for the reasons stated in FCC's comment letter, and the considerations discussed below, FCI joins in the request that the Farm Credit Administration ("FCA") withdraw the Proposed Rule.

From FCI's perspective, two themes continually cause concern when reviewing the Proposed Rule. First, the Proposed Rule appears to be trying to fix a problem (i.e. insufficient collateral valuations[1]) that does not materially exist. Second, the remedial provisions of the Proposed Rule harm FCI's member-owners by (i) increasing operational, and thereby loan, cost necessary for compliance, (ii) increasing portfolio risk (owned by the member-owners) by incentivizing decreased collateral, eliminating blanket liens, and inviting errors in the perfection of security interests, (iii) making the loan experience unpleasant; and (iv) making competitors' comparative ease of origination and servicing superior. These harms are exacerbated by the lack of benefit that FCI's member-owners will receive from the Proposed Rule given that FCI does not regularly suffer material losses via its retail loan portfolio, let alone losses caused by insufficient collateral valuations. This letter seeks to further explain how these two themes will negatively affect FCI member-owners based on the Proposed Rule's (1) rigid collateral valuation requirements; (2)

1 Because the Proposed Rule identifies appraisals as applying strictly to real estate and evaluations as applying strictly to non-real estate (a distinction with which FCI agrees), this letter will refer to appraisals and evaluations as valuations.

regulation of Automated Valuation Models ("AVMs"); (3) internal control specificity; and (4) creation of a seemingly benign asset class, the "business chattel."

1. The Proposed Rule's rigid collateral valuation requirements will harm FCI's member-owners.

Currently, FCI is able to make collateral determinations based on a holistic review of the loan application with due consideration of each of the five C's of credit (character, capacity, condition, capital, and collateral). Using this method, FCI employs multiple methods of valuing collateral that ensure properly collateralized obligations and proportionate cost of valuations relative to the benefit received from the collateral. The foregoing maximizes the value to FCI's member-owners by ensuring the provision of safe and sound credit at the minimum cost to the member-owner.

Under the Proposed Rule, FCI will be required to follow strict requirements to value every piece of collateral used to secure an extension of credit. See Proposed Rule, § 614.4245(a); 614.4245(b); 614.4260 and 614.4265. On any particular loan, the Proposed Rule would require valuation for each piece of collateral. This is particularly burdensome when taking a blanket lien on equipment. On today's modern farm, large items of equipment such as tractors, combines, planters, sprayers, and tillage equipment constitute the majority of the collateral value. The Proposed Rule as written, would require values to be assigned to older, smaller, and even obsolete equipment kept on the farm by our members even though those items do not add materially to the overall value of the collateral securing the loan.. While in a vacuum, the above-referenced Proposed Rule provisions adequately allow for an accurate valuation of collateral, FCI fears that the Proposed Rule's requirement of the foregoing valuation practices for every piece of collateral securing a Farm Credit loan will result in the needless sacrifice of sound credit practices in the name of obtaining collateral valuations that comply with the Proposed Rule.

Under the Proposed Rule, FCI fears that its current, holistic review described above that has resulted in sound and secure credit administration will be overrun by an emphasis on exemplary collateral valuation. The Proposed Rule could result in an increased emphasis on unsecured loans and a practice of taking the minimum collateral required to support secured loans.[2] The collateral that is taken will be harder to secure without the benefit of blanket liens or use of asset class descriptions, inviting the possibility of lost securitization due to inadequate descriptions in security documents. The foregoing suggests that the Proposed Rule will result in increased loan origination costs, decreased credit securitization, a more negative customer experience, and capitalization by competitors. Given the strong credit quality of FCI's retail portfolio, it sees no benefit that is in any way proportionate to the burdens that the Proposed Rule will place on FCI's member-owners.

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[2] As the FCC comment letter notes, the requirements for accepting other lender appraisals (see Proposed Rule 614.4245(d)) will likely only contribute to this strain on collateralization. See FCC's comment letter, p. 13.

2. The Proposed Rule's treatment of AVMs will exacerbate the issues created by the Proposed Rule's rigid valuation requirements.

FCI does not currently utilize AVMs, but it is exploring the introduction of an AVM to its valuation scheme. The Proposed Rule would frustrate FCI's investigation into how AVMs could improve its business, because it lacks sufficient clarity regarding who can use an AVM and how an AVM can be used. The concerns regarding the Proposed Rule's lack of clarity regarding the acceptable uses of AVMs are exacerbated by the fact that AVMs could be implemented to alleviate some of the stress caused by the Proposed Rule's rigid valuation requirements if clear direction were provided that allowed for AVM valuations.

FCI's initial interpretation of the Proposed Rule is that it limits the use of AVMs to only AVMs that assist appraisers and evaluators in their collateral valuations, and not AVMs that can independently provide valuations. It also arguably precludes FCI from utilizing certain AVMs that are accepted as safe, reliable, and industry-standard. If FCI's interpretation is correct, such a regulation will only further the strain placed on FCI's currently sound credit practices in the name of exemplary collateral valuations regardless of need. If not, the lack of clarity found in the current Proposed Rule is itself a burden with which system institutions will have to contend if the Proposed Rule is implemented as drafted. In any event, at a minimum, the unclarity surrounding AVMs in the Proposed Rule should be clarified so that system institutions can have a clear picture of the tools available to them as they navigate the collateral valuation requirements expected of them.

3. The internal controls mandated by the Proposed Rule will further exacerbate the strain on credit quality caused by the collateral valuation requirement of the Proposed Rule.

FCI already employs internal controls that protect the integrity of its collateral valuations and the process whereby such valuations occur. FCI's internal controls already facilitate most of the Proposed Rule's dictates with respect to internal controls.

However, the Proposed Rule's requirement that internal controls require the verification that collateral condition is as listed on the valuation report again seeks to fix a non-existent problem to FCI's member-owners' detriment. Like the valuation requirements discussed earlier, requiring the blanket verification of collateral condition will increase cost, discourage full collateralization, frustrate member experience, and put FCI at a competitive disadvantage. In most cases, it will have these negative affects without improving credit quality or decreasing FCI's portfolio risk. In cases where monitoring collateral condition may improve credit quality or decrease risk, it will not result in material, tangible benefit as FCI's retail portfolio does not experience material losses due to poor collateralization.[3]

[3] FCI also reiterates the point made by the FCC comment letter regarding the fact that the nature of property commonly used as collateral in agricultural lending makes the collateral condition verification provision particularly problematic for system institutions. See FCC Comment Letter, p. 5-6.

4. The Proposed Rule's introduction of the new, "business chattel" asset class with no apparent purpose will increase FCI's portfolio risk with no apparent benefit.

FCI is concerned by the Proposed Rule's introduction of a new asset class not found in any securitization laws of which FCI is aware and for which FCI cannot find a purpose in the Proposed Rule. Other than identifying certain collateral as "business chattel," the Proposed Rule seems to treat "business chattel" identically to "personal property," the asset class for which the Proposed Rule's defined business chattel would belong in all other contexts. Given that the Proposed Rule appears to treat business chattel exactly the same as personal property, its inclusion into the Proposed Rule, at worst, invites the inadvertent non-securitization of collateral by trying to describe collateral as business chattel in UCC filings and, at best, invites uncertainty around collateral evaluation in direct derogation of one of the stated purposes of the Proposed Rule.

Without a well-defined, stated purpose for the business chattel classification, the seemingly superfluous addition of the foreign asset class could lead to non-regulatory expectations for the asset class that the Proposed Rule defines separately from, but treats exactly the same as, personal property. Even if this fear is not an immediate impact of the added asset class, the Proposed Rule gives no functional purpose to the new asset class, resulting in it doing nothing more than inviting confusion. The burdens of the formation of this novel asset class appear to far outweigh any benefit that could arguably be presented by its origination.

5. Conclusion.

FCI understands the desire to modernize FCA's Collateral Evaluation regulations and agrees with the stated objective of the Proposed Rule. However, any such modernization should not sacrifice member-owner experience, profitability, portfolio risk, and cost, in the name of rigid valuation practices that do not address system wide valuation problems or add any other material benefit to the system's member-owners. For the reasons stated in FCC's comment letter, and above, FCI believes that the Proposed Rule does sacrifice member-owner experience, profitability, portfolio risk, and cost without a material benefit. As such, FCI respectfully requests that FCA withdraw the Proposed Rule and offers to assist in any way requested to modernize the Collateral Evaluation regulations in a way that provides maximum benefit to all stakeholders.

Sincerely,

Steve Carson

Stephen W. Carson
Executive Vice President, Chief Risk Officer
Farm Credit Illinois