

ranchers, aquatic producers and harvesters.” Section 1.7(b) of the Act and § 614.4540 of the regulations allow OFIs that do not meet this 15-percent threshold to fund and discount their short- and intermediate-term loans at Farm Credit banks, but they are not assured access if credit becomes scarce.

Several commercial bank and System commenters believe that this 15-percent threshold is too onerous, and they asked the FCA to reduce or eliminate it. These commenters erroneously claim that the requirement that agricultural loans always comprise 15 percent of an OFI’s loan portfolio discourages potential OFIs and deters existing OFIs from depending on Farm Credit banks as their primary source of agricultural funding. The FCA seeks to dispel the misconception that § 614.4540(b)(1) requires OFIs to always maintain at least 15 percent of their loan portfolio in farm loans in order to maintain assured access. Instead, this regulation requires such OFIs to maintain at least 15 percent of their volume at a seasonal peak in farm loans and leases.

At this time, the FCA does not propose to change the 15-percent threshold as the factor that determines whether an OFI is significantly involved in agricultural lending, and thus assured access to funding from a System bank. In reaching this decision, the FCA examined how two of the other Federal bank regulatory agencies determine if a bank engages in substantial agricultural lending. The FCA’s research revealed that the Federal Deposit Insurance Corporation (FDIC) classifies banks as agricultural banks if at least 25 percent of their loans are to farmers or ranchers. The Board of Governors of the Federal Reserve System (Federal Reserve Board) classifies a bank as agricultural if its ratio of farm loans to total loans exceeds the unweighted average of the average of all banks on a given date. Based on this formula, the Federal Reserve Board most recently classified banks as agricultural banks if farm loans comprise at least 14.97 percent of their loan portfolios. Thus, the standard that the FCA uses to determine if a non-System lender is substantially involved in agricultural lending is significantly more permissive than the FDIC’s benchmark and comparable to the measure used by the Federal Reserve Board.

The current regulatory threshold also seems to strike a fair balance between the needs of small rural lenders and larger institutions. Agricultural loans usually comprise a larger percentage of the loan assets of small rural lenders. However, larger institutions may extend more overall credit, in dollar terms, to farmers, although agricultural loans are

a much smaller percentage of their loan portfolios. Additionally, § 614.4540(b)(1) continues to forbid Farm Credit banks from including the loan volume of an OFI’s parent, affiliates, or subsidiaries in determining compliance with this 15-percent threshold. In practice, most lenders establish a separate OFI affiliate to access System bank funding and, therefore, the 15-percent threshold should not be onerous to OFIs. As noted earlier, failure to meet the 15-percent threshold does not prohibit FCS bank funding to creditworthy OFIs unless credit is scarce.

Because the FCA wants to make the OFI program more attractive to eligible agricultural lenders, we invite your comments on alternatives that reasonably demonstrate that an OFI is significantly involved in agricultural lending, as section 1.7(b)(4)(B)(i) of the Act requires.

2. Place of Discount

Non-System lenders and many Farm Credit banks have long considered place of discount restrictions as a major reason why the OFI program has not been widely used by commercial banks and other agricultural lenders. Historically, OFIs borrowed from the Farm Credit bank that serves the territory where such OFIs maintain their headquarters or makes the most of their loans. As a result, OFIs have maintained a funding or discount relationship with a System bank that is owned and controlled by their competitors.

In 1998, the FCA sought to remedy this problem by adopting § 614.4550, which established new place-of-discount rules for OFIs. Under this regulation, every OFI must apply first to the Farm Credit bank that serves the territory where the OFI operates. If the bank denies funding, or otherwise fails to approve a completed application within 60 days, the OFI may apply to any other FCB or the ACB. Additionally, the regulation allows a Farm Credit bank to consent to another System bank funding or discounting loans for an OFI.

We received 28 comments about place of discount in response to the ANRPM, and another five comments about this issue during the interviews and public meeting. Specifically, we received comments on this issue from 12 commercial banks and seven commercial bank trade associations. Additionally, six Farm Credit banks and one FCS association commented on this issue. All commercial bank and bank trade association commenters, five Farm Credit banks, and the one FCS association favored repealing regulatory restrictions on place of discount so OFIs

could choose their System funding bank. One Farm Credit bank opposed repealing § 614.4550, so FCS associations would not be placed at a competitive disadvantage.

In response to these comments, the FCA proposes allowing OFIs to apply for funding and discount services from any FCS bank. However, the proposed rule will require a Farm Credit bank to notify another System bank in writing within five (5) business days of receiving an application from an OFI that maintains its headquarters or has more than 50 percent of its loan volume in the territory of the other Farm Credit bank. This notice will give the bank in whose territory the OFI is located ample opportunity to contact the applicants and offer them funding and discount services. Under the proposed rule, no OFI may borrow from two or more Farm Credit banks at the same time. Farm Credit banks extend wholesale credit to OFIs, and they hold the OFIs’ retail loans and other collateral as security. Allowing two or more Farm Credit banks to simultaneously fund the same OFI could pose safety and soundness risks to the funding banks if the OFI experienced financial stress and disputes arose over collateral pledged.

Our new regulatory approach would resolve the difficulties that often arise when OFIs must borrow from a Farm Credit bank that is owned and controlled by their competitors. When Farm Credit banks compete for OFI credit, the OFI can lower its funding costs, which it can then pass on to its agricultural borrowers. Additionally, this approach frees Farm Credit banks from potential association pressure not to lend to their competitors. If a Farm Credit bank is concerned about another System bank funding OFIs in its territory, written notice gives it ample opportunity to seek the relationship with the OFI.

3. Borrower Rights

Section 4.14A(a)(6)(B) of the Act expressly requires OFIs to adhere to borrower rights, “but only with respect to loans discounted or pledged under section 1.7(b)(1).” The borrower rights that apply to loans that OFIs discount or pledge with a Farm Credit bank are: (1) Effective Interest Rate (EIR) disclosures; (2) notice of adverse credit decision; (3) the right to appeal adverse credit decisions to the lender’s credit review committee; (4) receiving copies of certain documents; and (5) the right to restructure distressed loans. Existing § 614.4560(d) implements section 4.14A(a)(6)(B) of the Act by requiring OFIs to comply with borrower rights on