ICBA
Independent Community Bankers of America®

Focus on Farm Policy

White Paper
March 2018

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Introduction

The 115th Congress is faced with the important task of writing a new farm bill in 2018 to replace the current bill (The Agricultural Act of 2014; PL-113-79), which expires Sept. 30. The current five-year farm bill was estimated by the Congressional Budget Office to have a 10-year budgetary cost of $956 billion from 2014 to 2023. Rather than saving $16.6 billion as initially projected, the current farm bill is on target to contribute more than $100 billion to deficit reduction.

The farm bill plays an important role in stabilizing our nation's farmers and ranchers, assisting many rural communities, and meeting the nutritional needs of millions of lower-income Americans. Thousands of community banks and their agricultural and rural customers are also significantly affected by farm bill policies. This white paper outlines important policies and solutions to ensure the new farm bill allows community banks to continue meeting the needs of farmers, ranchers and others in rural America.

THE ROLE OF COMMUNITY BANKS IN FARM AND RURAL ECONOMY

There are nearly 5,700 community banks in the United States, with most located in small, rural, and remote communities. While community banks represent 17 percent of all U.S. bank assets, they provide roughly half of all agricultural credit from the banking sector and more than 60 percent of small-business loans. Further, community banks under $10 billion in assets provide nearly 75 percent of all banking industry ag loans.[1] Those under $1 billion in assets extend about 52 percent of non-real estate loans and 57 percent of real estate credit to the farm sector.

Peer Group	Percent of Ag Loans	Percent of Total Farmland Loans	Percent of Ag and Farmland Loans
Less than $1B	52%	57%	54%
Less than $10B	73%	79%	76%
Less than $50B	83%	89%	86%
Total	$80.8B	$100.9B	$181.8B

1 12-31-2016 Call Report Data

Five Key Farm Bill Principles

1. Provide ample funding in the farm bill to help producers weather a potential farm credit crisis.
2. Change any programs needed to benefit producers, small businesses and community banks.
3. Direct agencies to reduce regulatory burdens and require regulations be based on specific statutes.
4. Require federal agencies to implement programs fairly for all stakeholders.
5. Ensure direct government loans complement—not undercut—private-sector lenders.

Commodity programs, crop insurance, USDA farm loan and rural development programs are all essential tools needed to help community banks maintain a prosperous farm economy. The 2014 farm bill was written in an era of much higher commodity prices and higher levels of net farm income, which peaked at $126 billion as the bill was being written.

However, USDA's February 2018 farm income forecasts project net farm income to decrease 6.7 percent from 2017 to $59.5 billion, the lowest level since 2006. Adjusted for inflation, net farm income is forecast to drop to the lowest level since 2002. Meanwhile, production expenses are forecast to rise due to higher fuel, labor and interest rate costs. According to recent testimony from Secretary of Agriculture Sonny Perdue, "about one-in-three poultry farms, one-in-four wheat farms, and one-in-five cotton farms are highly or very-highly leveraged."[2]

Estimated **50%** in Farm Income since 2013!
LARGEST DROP since Great Depression

69% of U.S. Farms in the **RED ZONE** of Financial Risk – Operating PROFIT MARGINS **of less than 10%**
- House Ag Committee, Farm Bill Facts Series

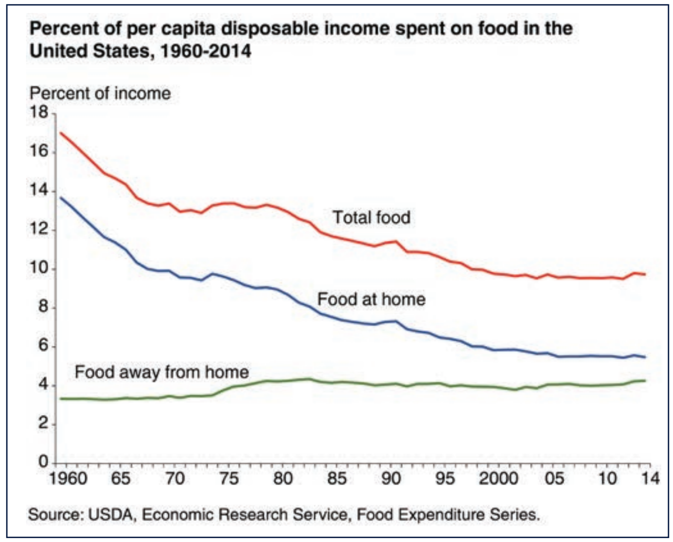
Agriculture & Food Industries Create Over **43** MILLION JOBS
More than 25% of ALL American Jobs
- House Ag Committee, Farm Bill Facts Series

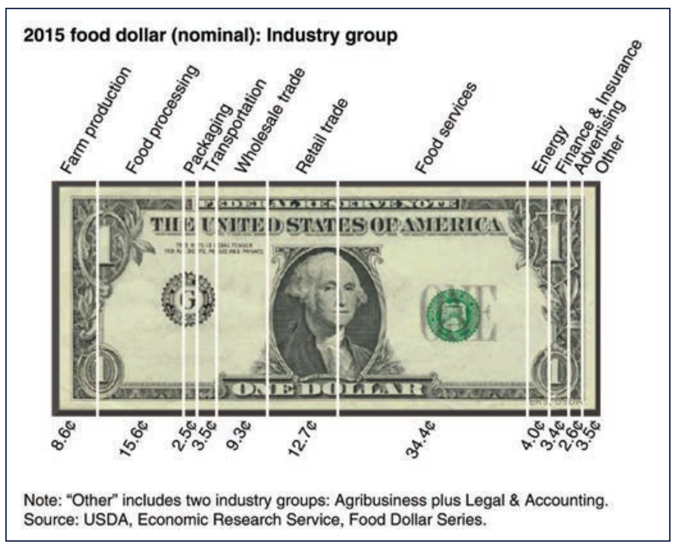
2 Testimony of Secretary Sonny Perdue, U.S. Department of Agriculture, United States House Committee on Agriculture, "The State of the Rural Economy," February 6, 2018, pg 2.

These troubling trends highlight the critical need to pass a new farm bill that maintains support for commodity prices as well as robust titles for farm and rural lending. For farmers and lenders, a five-year farm bill helps stabilize the farm and rural economy by providing a degree of longer-term economic certainty for business-planning purposes.

The Farm Bill Benefits All Americans.

For all Americans, the farm bill is a key driver of the national economy. It fuels not only 20 percent of America's economic output, but also $140 billion in agricultural exports in 2017, the third highest on record, which generated a $20 billion trade surplus in farm goods. Farm exports provide more than 1 million American jobs, generating 20 percent of farm income.





And American agriculture provides tremendous benefits to the quality of life and well-being of all American citizens, with the share of disposable personal income spent on food declining dramatically in recent decades to about ten percent. Further, farmers receive less than one dime per every dollar spent on food. American producers, supported by a strong farm bill, provide consumers an abundance of low-priced food, which allow consumers to spend their income on other products.

Bottom Line: A new farm bill that includes robust price supports for ag commodities is essential for maintaining the economic health of our nation's farmers and ranchers and the lenders who extend them credit.

Rural America Needs a Robust Crop Insurance Program

Community banks view crop insurance as a vital protection enabling banks to lend to farmers and ranchers with the assurance that producers will be able to repay their loans in the event of a major weather disaster. Bank regulators view crop insurance as necessary to protect bank capital and would frown upon lenders making loans unprotected by crop insurance.

Today, crop insurance is available for approximately 130 crops and to farmers of all sizes in all 50 states. In 2016, farmers took out more than 1 million crop insurance policies to protect 278 million acres of farmland, $101 billion of crops, and $533 million of livestock value. Without crop insurance or with a diminished crop insurance program, **the ability of many farmers and ranchers to obtain loans would be curtailed**, particularly among the growing number of financially vulnerable farmers facing current low prices.

Some proposals to cut funding contend that "means testing" using limits on adjusted gross income and premium assistance caps will keep large, wealthy farmers from receiving assistance that is unnecessary. However, reducing participation from any group of farmers will increase the premiums for all remaining farmers because lower participation levels will diminish the financial strength of the risk pool.

By statute, crop insurance must be actuarially sound, with premium rates sufficient to cover anticipated losses plus a reasonable reserve. The more participants and more acres in the program, the more the risk is spread to all participants, keeping premiums low for all farmers. Mid-size to large farmers pay a much greater amount of premiums into the risk pool than small farmers due to farming larger acreages. Without their participation, the costs of providing crop insurance to remaining participants will increase markedly.

Proposals to limit the amount of premium support to, for example, $40,000 has been suggested by crop insurance critics to impact a small number of farms, but would put at risk **a very large portion of the nation's crop production**. The Harvest Price Option (HPO), also a target for cuts, allows farmers to cover the replacement value of their crop after the deductible

> President Donald Trump, AFBF 99th Annual Convention, January 2018:
>
> *I'm looking forward to working with Congress to pass the farm bill on time, so that it delivers for all of you, and I support a bill that includes crop insurance.*

has kicked in. HPO tools enable growers to insure a crop at its harvest price, rather than its price at planting, to utilize forward contracting opportunities.

Midsize family farms, large family farms and nonfamily farms represent only 10.3 percent of all farms in the United States. However, they represent 51.7 percent of the acres operated and more than 75 percent of the value of agricultural production. By affecting such a large number of acres, such changes can have significant negative impact on the cost of premiums for all farmers.

Significant cuts to crop insurance are unnecessary because the program operates efficiently. According to the USDA's Risk Management Agency, the crop insurance program has had **a loss ratio of less than one** over the past 5-, 10-, 15-, and 20-year periods, meaning that less than a dollar of indemnity was paid out for every dollar of premium paid into crop insurance.

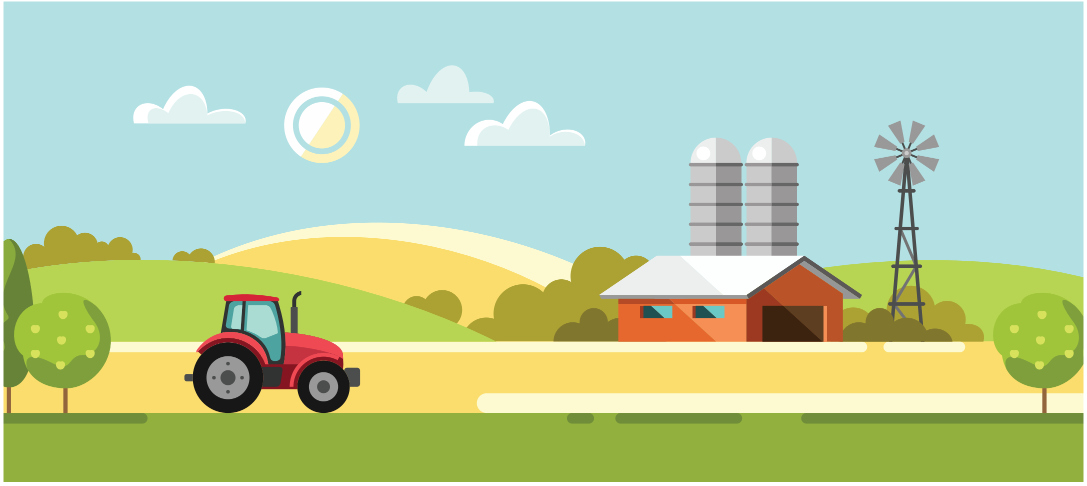
USDA Risk Management Data:

Period	Average Loss Ratio
5-Year (2012-2016)	0.91
10-Year (2007-2016)	0.80
15-Year (2002-2016)	0.83
20-Year (1997-2016)	0.85

Crop insurance is already cost efficient. Producers and crop insurance companies both share a portion of the risk, thus minimizing expenditures by taxpayers. Farmers receive an annual bill for crop insurance and pay approximately $4 billion in premiums. Farmers—who do not receive any payment from crop insurance unless there is a crop disaster—must lose approximately 25 percent of their crop value (the average deductible) before receiving crop insurance indemnity payments.

Over the past decade, farmers have paid $40 billion in premiums, including a significant amount from mid-size and larger farmers, but 80 percent of policies never pay an indemnity payment in a given year. **Why would Congress *not* want larger farmers paying into the risk pool, thus making crop insurance stronger for all participants?**

Other proposals suggest slicing administrative and operating (A&O) expenses or underwriting gains paid to insurance companies. Keep in mind the government heavily regulates crop insurance. Federal regulation ensures producers cannot be refused insurance and prohibits insurance companies



from raising premiums or imposing special standards or requirements on individual producers. **Premium rates are set not by insurance companies, but by the government**, which shares in underwriting gains or losses. Cuts to the private sector have already been significant, with more than $12 billion in reductions between 2005 and 2014.

Reducing A&O reimbursements or underwriting gains and losses beyond what has been already negotiated in the Standard Reinsurance Agreement could lead to a further exit of crop insurance companies from the industry, thereby diminishing access to this important coverage, particularly to producers in remote regions of the country.

Crop insurance policies can be complex to understand, and producers often need personal interaction with insurance agents to make the wisest and most cost-efficient policy choices. Companies must also manage the claims-adjustment process after losses occur. Crop insurance payments are also timely, unlike ad hoc disaster payments, which can come years after a disaster occurs and cover only a limited number of hard-hit commodities.

Bottom Line: Crop insurance provides certainty and expedited payments to farmers when widespread production losses occur, which ad hoc disaster assistance can never provide. Entire communities benefit when producers receive indemnity payments as Main Street businesses remain viable. Community banks retain farm customers and receive repayment on loans, satisfying regulators while ensuring banks can take the risks of extending credit for years to come. Congress should maintain current funding for crop insurance—it is an essential risk-management tool that enables producers to continue receiving loans.

Enhancing USDA Loan Programs

The USDA Farm Service Agency's (FSA) Farm Loan Programs assist producers and lenders through a combination of direct and guaranteed loan programs. The guaranteed farm loan programs allow community banks and other commercial lenders to provide credit to borrowers who would otherwise not qualify for credit in exchange for a USDA guarantee of up to 90 percent of the loan principal (95 percent for beginning farmers). But a 90 percent guarantee still leaves community bank lenders with a 10 percent risk of loss. Banks must carefully underwrite these loans to prevent losses because producers only qualify if they cannot obtain credit from commercial lenders. Default rates are negligible, though bank regulators often insist banks have guarantees on loans with potential cash flow problems.

Farm families across the country accessed nearly $6 billion in new credit in 2017, either directly or guaranteed through commercial lenders.[3] Updated fiscal 2018 numbers show a combined loan volume of $7.729 billion, reaching the highest levels in history for guaranteed loans. Since 2009, the USDA provided more than 200,000 loans totaling more than $27 billion. Direct and guaranteed loans supported approximately 42,000 producers in 2017. This amount of credit support to the farm community makes this unheralded program one of the most important in the farm bill arsenal.

USDA FY 2019 Budget Summary:

Item	2017 PL	BA	2018 PL	BA	2019 PL	BA
Discretionary:						
Farm Operating Loans:						
Guaranteed Unsubsidized	$1,960	$21	$1,877	$21	$1,600	$17
Direct	1,530	65	1,602	65	1,500	59
Total, Operating Loans	3,490	86	3,479	86	3,100	76
Farm Ownership Loans:						
Guaranteed Unsubsidized	2,750	-	2,750	-	2,750	-
Direct	1,500	-	1,500	-	1,500	-
Total, Ownership Loans	4,250	-	4,250	-	4,250	-

Since 2012, the guaranteed ownership (real estate) loan program has operated at no cost to the government and now provides $2.75 billion in longer term real estate loans. The guaranteed operating program has provided approximately $1.9 billion in short-term operating loans at a nominal cost of just $21 million, or about 1 percent of total loan volume. The amount of these loans are capped by Congress.

3 USDA press release, Jan 19, 2018: USDA Announces a Near-Record Year for Farm Loans, https://www.fsa.usda.gov/news-room/news-releases/2018/nr_2018_0119_rel_0006

Bank regulators challenge banks that work with producers that project negative cash flows, even if they have strong equity positions. The USDA's guaranteed loan programs can have a tremendously positive impact because regulators will only count the 10 percent of unguaranteed principal against a bank's capital if farmers miss payments, resulting in a loan's classification. The USDA credit programs, by lessening regulator concerns and allowing banks to provide continued credit in times of extreme financial distress, can therefore play a significant role in helping American agriculture withstand a major farm credit crisis.

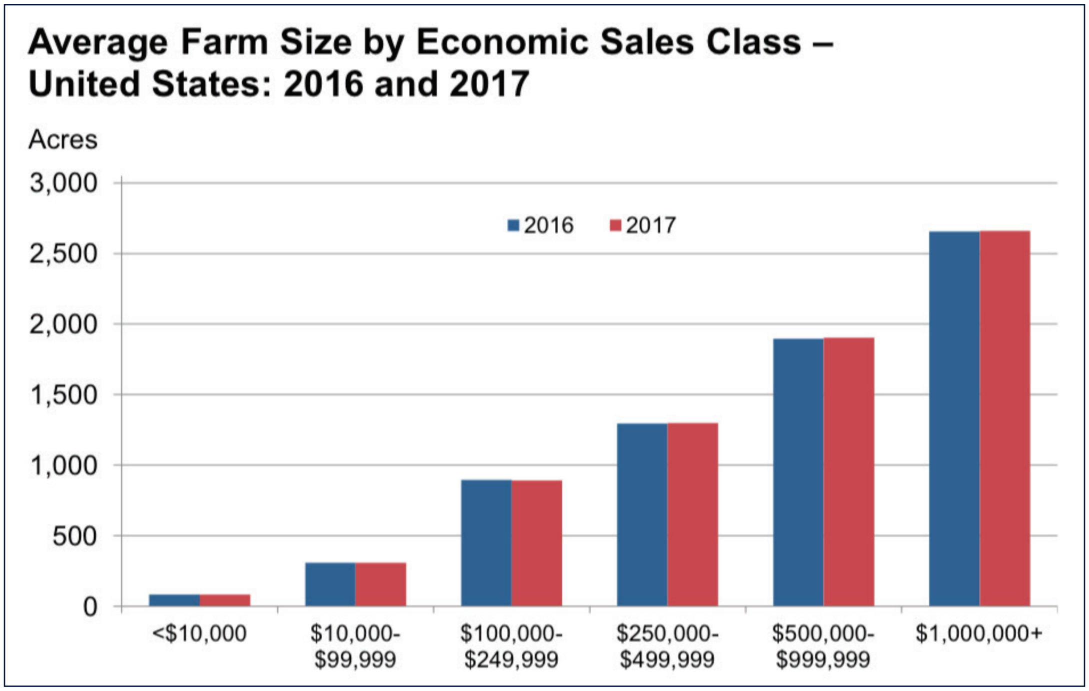
Increase the Amount of Guaranteed Loans: Congress should increase the guaranteed farm ownership program volume, which can be done at no cost because the program is self-financing. A small amount of additional funds would also greatly leverage the guaranteed operating program's loan volume.

Raise Guaranteed Loan Limits: Guaranteed farm ownership and operating loans have a loan limit of $1.399 million. These loan levels should be raised to at least $2.5 million due to the higher capital needs of today's family farm operations. Land prices have risen sharply in recent years, as have input costs. The current $1.399 million loan size severely limits the ability of many family farmers and ranchers to participate in the USDA farm loan programs.

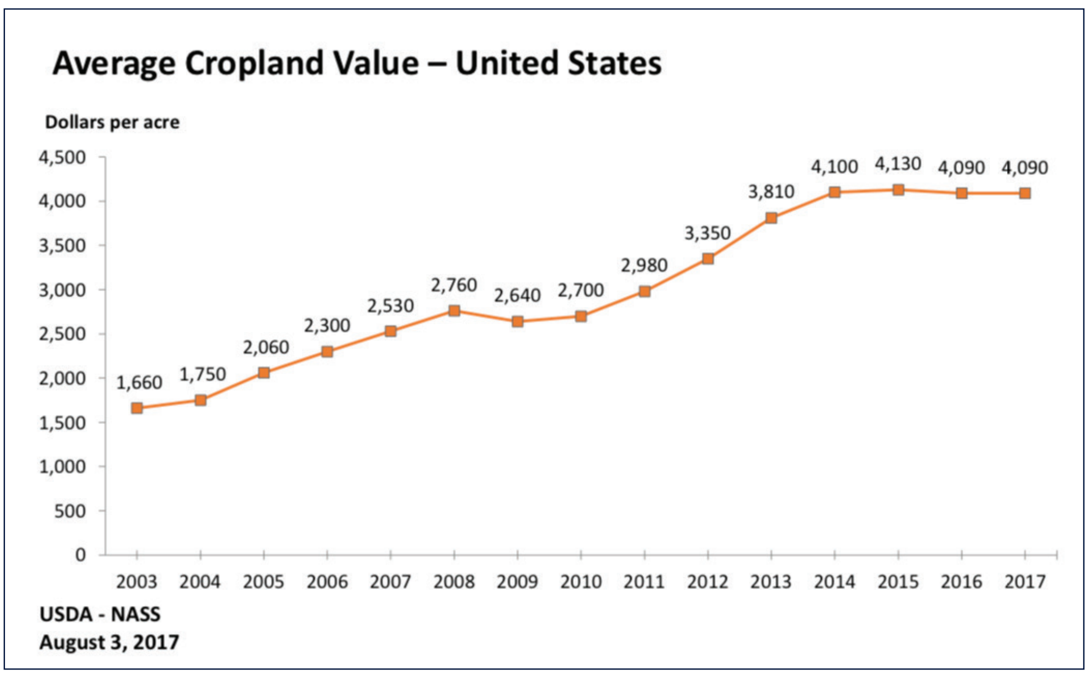
A relevant question is whether raising the loan cap for guaranteed loan programs would take away program funds from smaller family farmers. For the guaranteed farm ownership program, this would not be the case because this program is self-funding and Congress would simply need to ensure the level of allowable loans is high enough to accommodate demand. In addition, the guaranteed operating program can be adjusted to ensure currently eligible family farmers receive loan funds even with larger loan sizes to ensure small farms are unaffected.

For example, the law requires FSA to reserve or target loan funds for six months for exclusive use by beginning farmers (guaranteed loans, 40 percent; direct operating loans, 50 percent; direct ownership, 75 percent). However, the demand for guaranteed loans from beginning farmers never meets established targets and the money is reallocated by USDA to other eligible applicants after the six-month period. Additional appropriations could allow larger loan sizes once larger loan limits are authorized while meeting the demand from current borrowers.

A second pertinent question is do the loan sizes truly meet the needs of modern-day family farms? With very tight margins in agriculture, a profitable farm will often need to be of an average size or larger to be viable.



The "midpoint acreage" size of U.S. farms reached over 1,100 acres by 2007,[4] according to USDA. The average farm size per farm with sales of $250,000 to $499,000 is 1296 acres.[5] With an average value of cropland in 2016 of $4090, the cost to purchase a typical farm with this level of annual farm sales and acreage would be $5.2 million, far above the loan cap of $1.399 million. Likewise, a farm with sales of $500,000 to $999,000 averages 1897 acres. This size of farm would cost over $7.75 million to purchase.



4 "Midpoint acreage" defined—half of all cropland acres are on farms with more cropland than the midpoint, and half are on farms with less. Farm Size and the Organization of U.S. Crop Farming, Economic Research Report Number 152, August 2013, pg 8.

5 USDA, Farms and Land in Farms, 2016 Summary, February 2017, Pg 4. 2012 Census of Agriculture Highlights, Family Farms, ACH12-26/March 2015, pg 2, table 2

While 88 percent of all farms are considered small farms and operate 48 percent of all farmland, this category of farms accounts for only 5 percent of net farm income with only those between $150,000 - $350,000 having positive net farm income.[6]

Raising the loan limit would not provide larger loans to most community banks' farm customers. Rather, higher loan limits would help those farmers who may exceed the loan limit and allow community banks to serve family farmers and ranchers whose credit needs *occasionally* exceed the arbitrary USDA loan limit. Raising loan limits would also keep some borrowers on the farm during this difficult time of financial stress.

Direct Loan Programs: The direct loan programs are also a valuable financing tool for many farmers and ranchers, especially younger ones buying land. Because these programs are financed by the government instead of private-sector lenders, these programs need to ensure direct loans complement—not detract from—bank financing.

Additionally, because these programs have a "credit-elsewhere" test, which requires borrowers to affirm that they cannot access the loan on reasonable terms from a commercial lender, this test requirement should be tight enough to ensure producers don't shop for credit denials, such as from money-center banks that do not make farm loans. Further, many borrowers apparently do not pursue direct loans due to the amount of paperwork they have to fill out (more below).

6 2012 Census of Agriculture Highlights, Family Farms, ACH12-26/March 2015, pg 2, table 2.

Additional Enhancements to USDA Programs

Direct the USDA to enhance user-friendliness and report regularly to Congress:

1. The USDA should continually explore ways to reduce paperwork requirements, which often prevent farmers from using its programs.
2. Lenders serving borrowers across state lines indicate county office requirements are often different. Loan application and approval processes should be as uniform as possible.
3. Lenders should have flexibility to have at least some loans approved in a county office of their choice, such as a neighboring county, to prevent backlogs of loan applications and approvals. USDA staff levels are shrinking, and producers often need credit decisions quickly.

These goals are consistent with the USDA's recent efforts to modernize operations and service delivery, reduce burdens on stakeholders, serve customers, ensure responsible use of the department's resources, and centralize administrative and information technology operations.[7] These concepts should also be applied to county-level offices.

Removing Burdensome NEPA Prohibition on Refinancing Loans: The USDA's final rule regarding the National Environmental Protection Act (NEPA) included a provision to prohibit refinancing 12-24 months after ground disturbance. Producers complain of not being able to access guaranteed loans and considerable delays. Additionally, requiring several layers of governmental and agency approvals for environmental clearances is time-consuming, costly and unnecessary.

> Secretary of Agriculture Sonny Perdue, Feb. 6, 2018, House of Agriculture Committee Testimony
>
> *The primary goal of federal farm programs is to provide an effective financial safety net for farmers and ranchers to sustain viable production of food, fiber, and fuel in the face of changing market and production conditions without distorting markets.*

7 Secretary of Agriculture Sonny Perdue, Feb. 6, 2018, House of Agriculture Committee Testimony, discussing FPAC, pg 4

USDA Secretary Sonny Perdue has said regulatory reform is a cornerstone of USDA's strategy for creating consistent, efficient service to customers, reducing burdens and improving efficiency.[8]"

Bottom Line: NEPA regulations on refinancing guaranteed operating loans should be included in the USDA's list of regulations to terminate. The farm bill should ensure small farmers are exempt or receive waivers from refinancing restrictions and multiple agency approvals should be reduced to a single sign-off in the case of larger farmers.

Farmer Mac's Technical Changes

Farmer Mac was created to serve as a secondary market for agricultural real estate and rural housing loans made by community banks and other rural lenders, thus freeing up funds to make additional loans.

Farmer Mac has proposed three ICBA-supported technical changes to its charter. One deals with the eligibility of farms organized as family trusts, consistent with changes made in the 2014 farm bill, which recognized family trusts as eligible for guaranteed farm operating loans. A second change deals with Farmer Mac's ability to purchase the guaranteed portion of USDA guaranteed loans not under the ConAct of 1972. This change is consistent with the 2014 farm bill's reorganization of USDA programs. The third item removes an arbitrary loan limit pertaining to farms or ranches under 1,000 acres.

Bottom Line: In addition to benefitting rural borrowers, **Farmer Mac's proposed charter enhancements would benefit all lenders**, including community banks, large banks and the Farm Credit System.

8 Ibid. Pg. 6.

Rural Development Programs Can Help Main Street & Rural America Adapt, Thrive, and Grow

Through its broad variety of rural development programs, the USDA helps community banks extend credit to America's rural communities and Main Street businesses to bring prosperity and economic vitality to rural America.

The farm bill authorizes a variety of important rural development programs that assist rural communities and small businesses that populate Main Street.

ICBA and other organizations have urged Congress to adequately fund rural development programs, many of which are already well established. However, ICBA is concerned that recent administration budget proposals would eliminate funding for several important programs and shift funding from guaranteed loan making to direct loans. While funding issues will need to be addressed by the appropriations committees, the authorizing committees and the new farm bill should ensure that ensure the USDA's priorities are appropriately focused.

For instance, the USDA has proposed in recent years to drastically reduce or eliminate funding for the Business and Industry (B&I) Guaranteed Loan Program. Under this program, community banks and other private lenders have provided approximately $900 million in guaranteed loans in each of the past two fiscal years at a cost of $35 million per year. However, the budget again proposes to eliminate funding for this valuable public-private partnership.

The idea that the government should crowd out the private sector from extending credit in rural communities when they are willing to do so with a guarantee is misguided. The government, due to its low cost of borrowing at rates equivalent to the U.S. Treasury's cost of borrowing, could crowd out any private-sector lender if it chose to do so. The government can also fund loans for periods of 40 years because it is borrowing from itself, a huge advantage over community bank lenders.

> ICBA and Campaign for a Renewed Rural Development letter, Jan. 9, 2018
>
> *As Congress begins drafting the new farm bill, we ask for your continued support for rural communities through a robust Rural Development Title that promotes economic growth.*

Such crowding out of the private sector from areas in which it is willing to participate tends to jeopardize the economic diversity of our rural areas. Likewise, the USDA's proposal to provide $3.5 billion in program-level funding for the Community Facilities direct loan program but eliminate the meager amount on the guaranteed loan side is similarly misguided. The USDA's proposed budget would also eliminate guaranteed loans for the Waste and Waste Disposal program and the Electric Program categories.[9]

The USDA has also unfairly administered the Rural Business Investment Corporation (RBIC) program, requiring applicants to demonstrate that one or more Farm Credit System (FCS) institutions will invest in the RBIC with at least 10 percent of the capital.[10] This requirement, which was neither part of the statute nor the intent of Congress, illustrates why regulations should be based on statute and fairly implemented for all shareholders.

Bottom Line: The USDA's rural development programs represent an important arsenal of tools. Congress should conduct hearings to question the USDA's shift to direct loans from guaranteed.

ICBA Recommendations:

- Congress and the new farm bill should direct the USDA to emphasize guaranteed loan programs.
- The Community Facilities program should ensure a portion of all direct loans involve guaranteed lending if private lenders are willing.
- The requirement for every RBIC to have 10 percent investment by FCS, but not other lenders such as community banks, is unfair and should be eliminated.

9 USDA's FY 2019 Budget Summary, pgs 35-36.

10 Federal Register/Vol. 81, No. 223/Friday, Nov. 18, 2016/Notices, III Eligibility Information, pg 81725

Time to Reform & Refocus the Farm Credit System

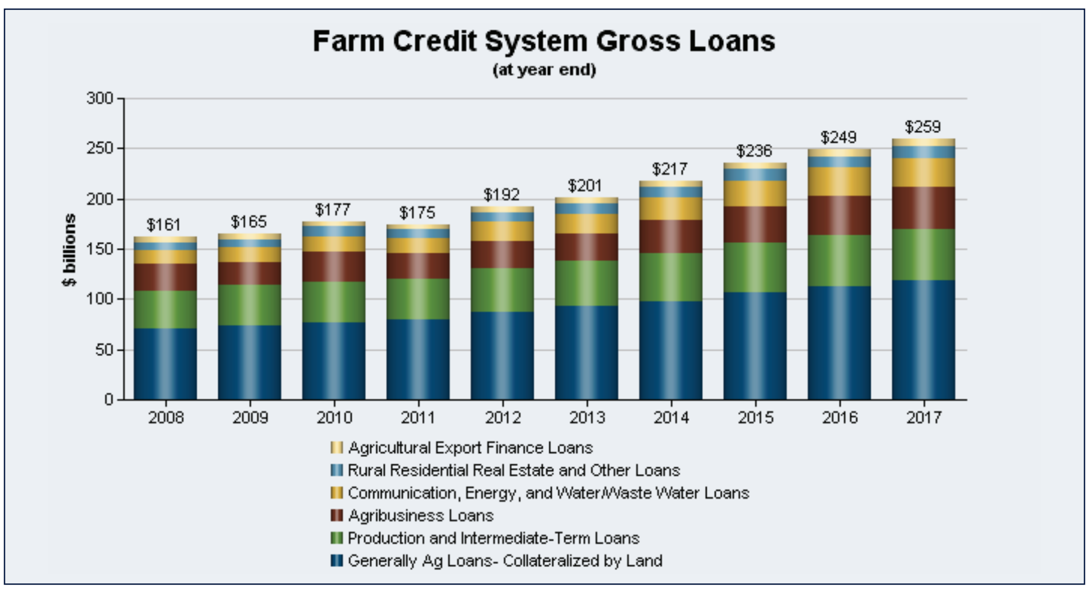
THE FARM CREDIT SYSTEM—A GOVERNMENT-SPONSORED ENTERPRISE THAT HAS GROWN SPECTACULARLY

The Farm Credit System is a government-sponsored enterprise (GSE) that Congress chartered to primarily serve *bona fide farmers and ranchers*. The FCS is the only GSE that competes directly against the private sector at the retail level.

FCS lenders are considered federal instrumentalities of the U.S. government. As a GSE, the FCS can raise funds at slightly above the Treasury's cost of borrowing, and FCS entities are essentially tax-exempt (see below). These lavish benefits allow FCS lenders to underprice loans offered by tax-paying community banks and thus siphon off their best customers.

FCS—INCREASING PROFITS, LOANS, AND ASSETS WHILE LOWERING TAX RATES AND REDUCING SERVICE TO FAMILY FARMERS

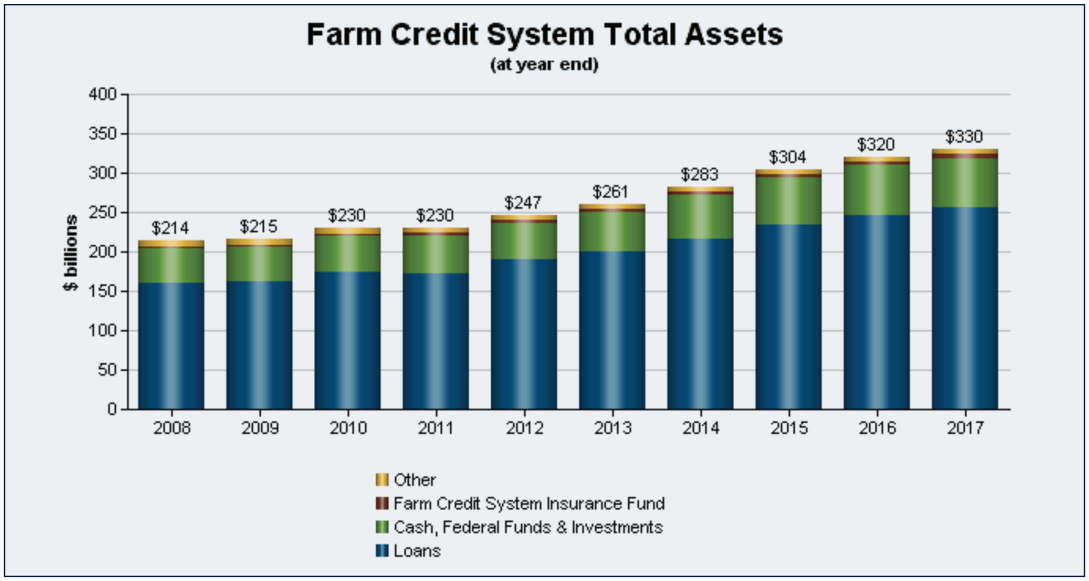
The FCS's **loan growth** has been significant in recent years, with gross loans rising over 81 percent from $143 billion in 2007 to $259 billion in 2017.



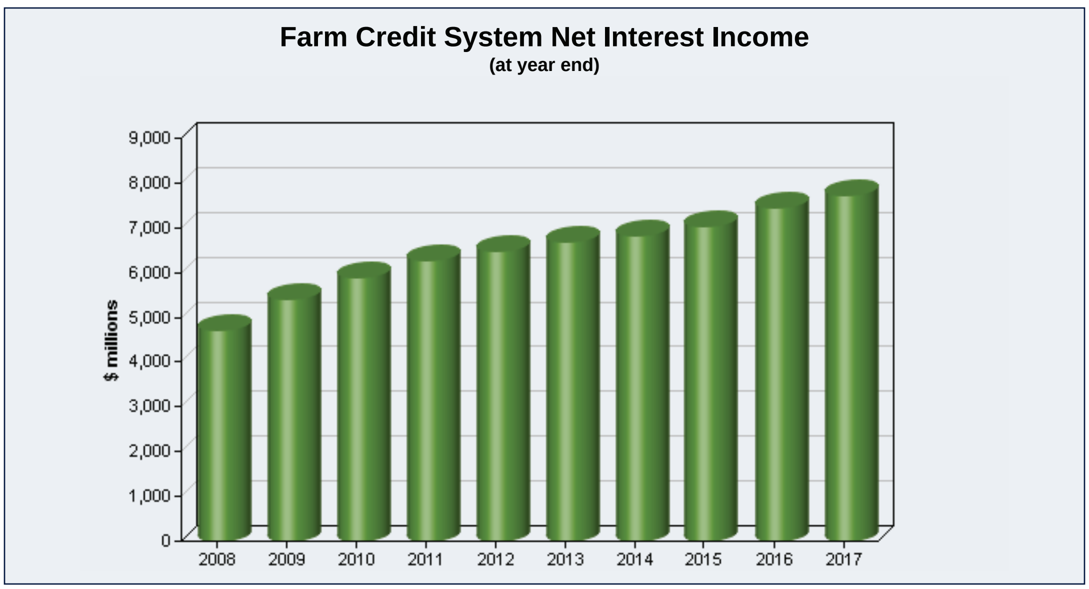
The system has become a behemoth, with **total assets** rising 72 percent since 2007 to $330 billion today.[11] If the FCS were considered a bank, it would be the seventh largest in the nation.[12]

11 Federal Farm Credit Banks Funding Corp. website: https://www.farmcreditfunding.com/ffcb_live/financialInformation.html#

12 Federal Reserve Statistical Release, U.S. chartered commercial banks that have consolidated assets of $300 million or more, ranked by consolidated assets as of September 30, 2017, https://www.federalreserve.gov/releases/lbr/current/



Likewise, FCS **net interest income** has increased 83.4 percent from $4 billion in 2007 to $7.447 billion at year-end 2016. Additionally, its **net income** rose 80 percent to $4.848 billion.



While the FCS was dramatically increasing its loan volume, total assets and income, it has been able to orchestrate a sharp reduction in its **effective tax rate**. FCS institutions had a paltry 6.4 percent effective tax rate in 2011, but further reduced this amount to only 3.48 percent in 2016 and a trivial 0.7 percent in 2017, an enormous reduction of 89 percent! Further, FCS institutions pay no taxes (zero percent) on income from real estate loans and home loans.

This means the FCS does NOT support the tax base and revenue needed for federal, state and local governments that are starved for funds to pay for our military, infrastructure, struggling school systems and other infrastructure.

The table below sets forth the loans by dollar size:

Range ($ in thousands)	December 31, 2014 Amount Outstanding ($ in millions)	December 31, 2014 Number of Loans	December 31, 2013 Amount Outstanding ($ in millions)	December 31, 2013 Number of Loans
$1 - $250	$51,041	861,024	$49,666	849,100
$251 - $500	26,665	74,227	25,216	69,837
$501 - $1,000	24,349	34,445	23,127	32,267
$1,001 - $5,000	48,678	23,997	45,637	22,482
$5,001 - $25,000	30,886	3,610	28,438	3,442
$25,001 - $100,000	10,465	298	9,786	241
$100,001 - $250,000	12,493	81	9,479	64
Over $250,000	12,432	28	9,711	23
Total	$217,054	997,710	$201,060	977,456

Note: Loans greater than $100 million are aggregated by borrower.

The following table sets forth the loans by dollar size and number of borrowers:

Range ($ in thousands)	December 31, 2015 Amount Outstanding ($ in millions)	December 31, 2015 Number of Borrowers
$1 - $249	$32,643	402,724
$250 - $499	20,871	59,528
$500 - $999	23,956	34,298
$1,000 - $4,999	51,137	26,454
$5,000 - $24,999	35,954	3,654
$25,000 - $99,999	29,718	620
$100,000 - $249,999	21,188	135
$250,000 and over	20,423	49
Total	$235,890	527,462

FCS'S DECLINING FOCUS ON SMALL FARMERS

According to the Federal Farm Credit Banks Funding Corp., FCS loans to smaller farmers declined by 53 percent from 2014 to 2015. This precipitous crash in loans to small farmers in only one year's time raises numerous questions Congress should explore in public hearings.

For example, what caused the decline? Did the FCS refuse to extend credit to these farmers? Did FCS make a strategic decision to shift from lending to small farmers to "clean up their books" due to declining farm income?

The FCS appears to have reduced exposure to smaller, more highly leveraged farmers to increase profits and pay higher dividends to attract new, larger farm customers. For example, it more than doubled loans to producers borrowing $25 million or more and increased loans to those borrowing over $100 million over 95 percent!

FCS loans to small farmers made up 29 percent of system loan volume at year-end 2007, but only 13 percent by year-end 2016. This is a steep drop of more than 55 percent in only one decade. Two-thirds of all FCS farm loan volume now exceeds $1 million, almost 50 percent of loan volume exceeds $5 million, and roughly one-third of loan volume exceeds $25 million or more.

Unlike banks, which must comply with the Community Reinvestment Act, the FCS has only a loose reporting requirement on loans to young, beginning and small farmers (YBS). But even these FCS numbers are suspect because loans to a YBS farmer can count as at least three separate loans.

FCS'S BELOW-MARKET PRICING HARMS RURAL AMERICA

Banker surveys indicate the FCS is using its GSE status and tax advantages to siphon the best farm customers away from community banks. As one banker said of YBS producers, "FCS wants us to get these farmers started first, and then later FCS attempts to take them away once they become financially stronger."

Bankers describe the frustration of YBS farmers as FCS often charges higher interest rates to YBS prospective borrowers while simultaneously offering much lower rates to the FCS's best prospects. While the FCS may lend to some YBS farmers, particularly if parents co-sign the loan, YBS farmers are not their preference and appear the exception.

While **stiff competition exists among thousands of banks for farm loans**, they cannot match the below-market rates offered by the FCS to their best customers while remaining profitable and passing regulatory scrutiny. **By targeting large, more stable borrowers, FCS's actions elevate risks in community banks' ag loan portfolios**.

Another serious issue: the FCS urges newly acquired customers to move their deposit accounts to one of the large banks, thus **taking deposits out of local communities and hurting their economic base**. These lower deposit balances limits the ability of community banks to make local loans, further harming rural communities.

FCS activities weaken community banks across the board. The FCS primarily targets top borrowers, offers these top borrowers below-market rates, and is willing to fix those below-market rates at longer terms or time periods. By taking top borrowers from community banks, FCS weakens overall community bank portfolios, leaving younger and more highly leveraged borrowers with community banks. If community banks stretch to keep top borrowers, they must accept negligible returns and assume higher interest rate risks.

> Upper Midwest YBS farmer:
>
> *I am a young beginning farmer and was offered a loan through my local FCS with a rate of 8.5 percent along with the requirement of additional real estate pledged by my parents and my dad's co-signature on the loan. My local community bank offered their base lending rate of 5.25 percent along with my dad's guarantee for a five-year period. It was clearly obvious to me FCS was only interested in taking advantage of me with a higher rate. My neighbor, who is a large farmer, recently closed a real estate loan with an interest rate of 3 percent. Is this really the purpose of a tax-subsidized entity?*

Taking the "Farm" out of the Farm Credit System

FCA'S "INVESTMENTS IN RURAL AMERICA" SCHEME

Not content to remain "on the farm," the FCS now seeks to leverage its significant GSE tax and funding advantages to siphon the best non-farm loans from community bank portfolios.

Defying Congress, the FCS has pursued its non-farm agenda with the help of a complicit regulator, the Farm Credit Administration (FCA). The FCA has approved FCS non-farm "investments" that would be illegal if made as loans under the Farm Credit Act. The FCA has refused to explain the difference between a bond and a loan.

These "investments" are designed to allow FCS lenders to lend to hospitals, commercial offices, manufacturers, apartment complexes and hotels, among other non-mission related activity. The FCA has issued guidance in the form of an "informational memorandum" (IM) to allow these same activities if approved by the FCA on a case-by-case basis. The FCA issued its IM even before proposing regulations on this same topic.[13] In discussing its investment proposal, the FCA said "no investment is ineligible if it has been approved by the FCA." This statement indicates FCA's belief that it can approve any lending purpose if loans are called "investments."

Congress did not authorize an "anything goes" approach for the FCA's approval of investments. The rationale for FCS investments is to allow FCS to hold high-quality, readily marketable investments to provide sufficient liquidity for ongoing operations; to manage interest rate risk; to manage surplus funds; for hedging and other similar purposes. ICBA strongly objects to the FCA allowing the FCS to finance businesses and broad community activities, which undermines the Farm Credit Act's limits on loan purposes and represents a dramatic expansion of the FCS with no basis in legislative history. Congress authorized the RBIC statute for FCS and other lenders' rural investments, which should be the focus of the FCS's investment activities.

FCS's Latest Expansion Effort: The FCS is now suggesting it is hindered from its illegal investment activities due to a reliance on FCA's case-by-case approval authority and that FCS lenders should be able to make their own illegal investment decisions. **ICBA strongly opposes any weakening of the case-by-case decision authority and believes FCA's investment program should not exceed the parameters of the Farm Credit Act's loan authorities**.

13 Proposed Rule, Investments Eligibility, 12 CFR Parts 611 and 615, RIN 3052-AC84, October 30, 2014

Bottom Line: The FCA is cleverly abusing its authority to regulate investments to manage the safety and soundness of the FCS and is instead developing an entirely new lending scheme that circumvents the Farm Credit Act and further displaces community banks from local lending markets.

FCS's "Similar Entities" Ruse

FCS institutions are authorized to lend to operations that are ineligible for FCS loans if they are "functionally similar" to eligible borrowers. The FCS has misused its "similar entity" authority to make loans to some of the world's largest corporations in the world's largest cities. Such financing has included loans to Verizon, Vodafone, U.S. Cellular, Constellation Brands, AT&T, Frontier and CyrusOne to name a few.

While these companies may have a presence in rural areas, these lending activities do not focus on rural America. The Verizon-Vodafone deal involved two large corporations headquartered in New York City and London. CoBank, the lead lender in this case, is supposed to be the "lending bank for cooperatives," not the lending bank for large corporations.

The FCS and FCA have tried to hide behind the argument that such loans help with diversity and risk management. Such arguments are ludicrous and effectively would mean that FCS entities should be allowed to make any non-farm loan anywhere, because it would lead to greater risk management. While the FCS may welcome such an outcome, the argument is irrational. The FCS was granted a GSE charter along with enormous tax advantages to ensure it focuses on serving agriculture.

Bottom Line: Congress should refocus the Farm Credit Act's "similar entities" authority so it does not include loans to gargantuan corporations in the world's largest cities. The focus should primarily benefit rural communities, not the FCS's profits and bottom line, as it does today.

Dealing with Other FCS Outrages

$10 Billion Line of Credit: The FCS should not be granted a $10 billion line of credit annually from the U.S. Treasury. This was done without any record of congressional involvement, contrary to the Brookings Institution's recommendation for the FCS to approach Congress and administration for legislative help.[14]

14 The Brookings Institution: Farm Credit System Liquidity and Access to a Lender of Last Resort, Report for the Farm Credit System Insurance Corporation, page 8, Kohn and McGarry; http://www.brookings.edu/~/media/research/files/papers/2012/11/06%20farm%20credit%20system%20liquidity%20kohn/06%20farm%20credit%20system%20liquidity%20kohn.pdf

Greater Transparency Needed: Contrary to banking regulators, the FCA promotes a lack of transparency by not, for example, publishing names of institutions and infractions when illegal activities occur. The FCA does not publish details of serious accounting or fraud issues.

No Below-Market Pricing of Loans: The Farm Credit Act should be clarified to ensure FCS lenders are prohibited from engaging in below-market pricing contrary to the FCA's interpretation of the Farm Credit Act.[15]

Reform and Refocus the FCS

- Oppose any FCS expansion including for greater infrastructure "investments." FCS's current authorities as outlined under the Farm Credit Act are sufficient for infrastructure investing.
- Limit the FCA's "Investment" authority to not exceed to the loan-making constraints of the Farm Credit Act.
- Reform the FCS's "similar entity" provision to ensure benefits accrue primarily to rural populations.
- Discontinue the FCS's $10 billion line of credit with the U.S. Treasury.
- Require the FCA to publish illegal actions by FCS lenders, including all unethical or substantial instances of institutional fraud and accounting irregularities.
- Prohibit the practice of below-market pricing by ensuring this prohibition in the Farm Credit Act applies to current interpretation of the law.

15 1971 Farm Credit Act as Amended, Sec. 101, Policy and Objectives: "Provided, that in no case is any borrower to be charged a rate of interest that is below competitive market rates for similar loans made by private lenders..."