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July 19, 2010

Mr. Gary K. Van Meter  
Deputy Director, Office of Regulatory Policy,  
Farm Credit Administration, 1501 Farm  
Credit Drive, McLean, VA 22102-5090

**Re: RIN 3052-AC62 – FCA Proposed Rule, “Loan Purchases from FDIC”;  
Federal Register, 27660, Vol. 75, No. 95, Tuesday, May 18, 2010, Pgs 27660 -  
27662**

Dear FCA Reviewers:

We are sending this letter on behalf of the Independent Community Bankers of America (ICBA) and our 5,000 community bank members<sup>1</sup> in response to the Federal Register notice cited above requesting public comments on FCA’s proposed rule to allow Farm Credit System institutions (FCSIs) to purchase loans or loan pools from the FDIC. We appreciate the opportunity to offer our views.

**Background** – The Farm Credit Administration is proposing to amend its rules on loan policies and operations. The amended rule would permit FCSIs with direct lending authority to purchase loans or pools of loans from the Federal Deposit Insurance Corporation (FDIC) when a bank failure has occurred. FCA states that these purchases would be loans to farmers, ranchers, producers or harvesters of aquatic products and cooperatives that meet eligibility and scope of financing requirements, although adherence to scope and eligibility standards cannot be assured. FCA states the proposals would allow the System to provide liquidity and a stable source of funding and credit for borrowers in rural areas affected by the failure of their lending institution.

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<sup>1</sup> The Independent Community Bankers of America represents nearly 5,000 community banks of all sizes and charter types in the United States and is dedicated exclusively to representing the interests of the community banking industry and the communities and customers we serve. ICBA members represent more than 20,000 locations nationwide and employ nearly 300,000 Americans. ICBA members hold \$1 trillion in assets, \$800 billion in deposits, and \$700 billion in loans to consumers, small businesses and the agricultural community.

**Request for an Extension of Time** – The banking industry has been absorbed for the past several months, including the span of time encompassed by this proposal, in dealing with the nearly 2,500 page financial regulatory reform act (HR 4173). As a result, the banking sector has not had adequate time to review the impact of the proposed rule upon commercial banks, particularly community banks. ICBA believes that because this proposal could have significant ramifications, more time is necessary to discuss the proposal with community banks now that HR 4173 has been passed by the House and Senate.

ICBA would also like to conduct a survey of community bank opinions, particularly in rural areas, regarding this proposal. We would like to share the results of this survey with the FCA to help inform FCA’s decision making on the proposed rule. Therefore, ICBA requests a 60 day extension of the public comment period to allow for an adequate review of this proposal and its potential impact upon the community banking sector. We note that the FCA has extended the comment period on several recent occasions when requests were received via the public comment procedure.

**General Comments** – ICBA has several concerns regarding this proposal as briefly outlined below.

**Safety and Soundness / Illegal Territory Issues** – The proposed regulation appears to raise numerous safety and soundness issues which have not been reflected or discussed within the proposed rule. A major concern would be the FCA proposal to allow FCSIs to reach outside of their chartered geographical territories to purchase loan portfolios of failed banks. These out-of-legal-territory FCSIs would be buying loans of customers with whom they are not familiar.

Agricultural loans in particular can vary substantially in terms of risks not only by regional geographical areas but even within the same counties. Out-of-legal-territory FCSIs will be making decisions, perhaps within a very short timeframe, to buy loans in markets with which they are not familiar, which pose significant risks and which may have been contributing factors to the failed bank’s demise. Therefore, purchasing these types of loans could cause significant losses for FCSIs.

Alternatively, FCSIs may try to purchase loan portfolios to obtain some good credits while foreclosing on higher risk borrowers. Although FCA claims FCSIs will need to comply with borrower rights requirements, these requirements do not preclude FCS lenders from eventually dumping distressed borrowers.

Allowing FCSIs to reach beyond their legal territories to buy loans or pools of loans appears completely unwarranted. Congress has held hearings on the so-called “Customer Choice” proposal in the past expressing much opposition. To now incorporate the “Customer Choice” proposal, even in a slightly more limited form, as part of another proposal, is inappropriate. Allowing out-of-legal territory FCSIs to invade territories of other FCSIs was strongly opposed by many FCSIs in the past. This procedure violates basic tenets necessary for a cooperatively-owned finance system.

Further, simply giving notice by an out-of-legal territory FCSI to an in-territory FCSI provides no significant protections for in-territory lenders. The out-of-legal territory lending aspects of this proposal are treated far too lightly and discussed far too minimally in the proposal.

**No Need for the Proposal** – FCA has not indicated any real need for the proposal. In fact, as the economy has improved, investors have grown confident that problem loans are at or near their peak. That confidence has been reflected in banking stocks, which have soared 111 percent from their low in March 2009, as measured by the KBW bank index. One article in the New York Times recently stated: “More buyers are showing up at F.D.I.C. auctions, and to avoid a bidding frenzy, some are doing deals with little or no government help.”<sup>2</sup> This suggests there is no lack of liquidity for the purchase of FDIC loans.

In addition, the FDIC lowered its estimate for bank failures in 2010, an important sign that the financial system is getting stronger. According to another article: “Confidence in the banking system has steadily increased in recent weeks as banks have reported first-quarter earnings that showed declining delinquency rates and charge offs: signs that the worst of the credit crisis has passed.”<sup>3</sup> Further, bidding on FDIC loans has become even more competitive as the article states: “In another sign of confidence, the FDIC said that the bidding process for bailed bank assets has become more competitive.”<sup>4</sup> The FDIC has also been able to reduce loss-sharing agreements that help protect bidders against loan losses.

FCA has not provided any substantive rationale for why, given that there are 8,000 community banks in the country, including thousands of community banks in rural areas, other community banks and other investors are not able to provide sufficient liquidity for loan purchases from the FDIC.

Further, it is unlikely that FCSIs will choose to work with community banks in making bids on loans of failed banks. Rather, FCSIs, not wanting greater competition from area community banks, will seek to link up with large investors and investor firms. The rule imposes no requirements for FCSIs to work cooperatively with a multitude (or any) community banks.

The ability of these FCSIs to leverage their advantages as a GSE will shut many community banks out of opportunities to purchase loans from the FDIC, even though community banks have paid extremely high assessments to the FDIC while FCS institutions have paid no assessments to the FDIC’s Deposit Insurance Fund (DIF). The DIF is used to resolve bank failures. This represents a gross unfairness against the community banking sector by a GSE.

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<sup>2</sup> New York Times, *Investors Ease Strains on FDIC*, May 19, 2010

<sup>3</sup> Financial Times, *FDIC Lowers Bank Failures Estimate*, April 29, 2010

<sup>4</sup> Ibid

There is no requirement for FCSIs to work through community banks to purchase FDIC loans of failed banks. There is no requirement for FCSIs to target geographical areas where there exists a lack of liquidity, the central reason FCA states for the proposal (if such areas can be shown to exist).

Further, FDIC loan pools are not solely made up of non-performing or distressed loans. They typically contain performing loans, meaning there would be bidders on these loan pools without FCSIs bidding.

**No Authorization for the Proposal** – There is no provision in the Farm Credit Act that authorizes FCSIs to purchase loans or loan pools from the FDIC. It is disingenuous for FCA to suggest that all powers not denied by Congress are therefore granted by Congress. Obviously, Congress cannot foresee all potential lending activities but rather has explicitly authorized specific lending activities for the FCS while allowing the FCA authorities to implement and regulate the specific lending activities authorized by Congress.

**Scope and Eligibility Issues** – The proposed rule would allow FCSIs to purchase illegal loans and pools of loans and suggests that although FCSIs would conduct due diligence to prevent purchase of illegal loans it may not be possible when purchased as part of loan pools. If FCA were truly serious about preventing illegal lending by FCSIs, they would have worked out this procedure prior to publishing a proposed rule. Also, we note the proposal does not require any timeline for divesting illegal loans, suggesting the illegal loans could remain on the FCSI's books for a lengthy period of time, which is completely inappropriate. FCSIs should not be allowed to purchase illegal loans – period. Regulators should not allow their regulated entities to engage in illegal activities under the guise that such illegal activities may be eventually discontinued.

According to the FDIC, “Typically, sales contain loans that have similar characteristics. The loans are refined into pools according to specific criteria. Pooling considerations may include loan size, quality, type, collateral and location.”<sup>5</sup> Thus, it is doubtful that FCSIs would need to bid on pools with illegal loans nor is there a satisfactory justification as to why FCSIs would not be precluded from bidding on pools with illegal loans.

In fact, the FDIC encourages bidders to review loan files and has a specific procedure in place for bidders to do so. This procedure would prevent FCSIs from bidding on loan pools with illegal loans.

**Proposed Rationale is Faulty** – The FCA's stated rationale for this proposal is to “provide a source of credit and liquidity to borrowers whose operations are financed with agricultural or cooperative loans affected by commercial bank failures.” However, agricultural banks have outperformed their non-agricultural bank peers in recent years, including during the credit crisis. Only three agricultural banks failed during 2009 according to the FDIC.

<sup>5</sup> <http://www.fdic.gov/buying/loan/loan/index.html> Loan Sales FAQs, Number 2.

An article addressing this issue states: “Banks that lend to farmers appear to be emerging from the recession relatively unscathed, with the latest federal data showing that agriculture lending continued to outperform most other segments of the banking industry in the third quarter.”<sup>6</sup>

The article also notes that lenders are “very eager to get a good loan on the books with their company. There is an ability to repay the loans . . . the recession has been relatively pain free for farm lenders.”<sup>7</sup>

Industrywide, farm loans were up approximately 3 percent from the prior quarter as of Sept. 30, 2009, and 0.7% from the previous year. The significance of the increase in agricultural lending is that it occurred at a time when other lending segments, such as commercial real estate, had declined.

Therefore, the FCA’s proposal to assist agricultural borrowers by purchasing loan pools from the FDIC is faulty since the agricultural lending sector has been one of the strongest lending sectors with very few ag bank failures. Of the three banks that failed, bankers reported at the time of failure of one large ag lender that the loans were not sound loans when credit was initially extended and included large loans made in geographically distant areas far removed from the bank’s headquarters which had gone bad. It is not agricultural loans, but rather commercial real estate loans that pose the biggest risk to U.S. banks.<sup>8</sup> FCSIs are not allowed by law to extend loans for commercial real estate purposes. Given these facts, it would appear one major reason for the FCA proposal is to allow FCSIs to bid for illegal loans that are primarily non-agricultural in nature as a way to significantly expand FCSIs balance sheets.

We also note that the FCS did not seek to expand their lending to the ethanol and biofuels industry during the past two years, even though that was a primary justification for FCA’s new processing and marketing regulation. The FCA also encouraged *more restrictive lending* to the ethanol sector in 2007. This provides evidence that the FCSIs are also constrained by economic conditions in lending to troubled sectors and will not provide credit and liquidity more than community banks would when an industry sector is stressed, counter to one of the FCA’s assertions for this proposal.

Moreover, there were 141 new or de novo banks chartered banks in 2007 with a risk-based capital ratio of 16.5% and 72 de novo banks opened in 2008 with a 21.7% risk based capital ratio. These statistics do not include banks formed by existing bank holding companies. Many of these banks have a total risk-based capital ratio double the minimum 10% that regulators consider well capitalized. During that same timeframe, there has been continued consolidation of FCSIs to well below 100 overall institutions comprising the Farm Credit System. These statistics indicate that community banks continue to seek loans and bank assets even in troubled times and serve local markets and that there is no real need for FCSIs, whose local presence continues to recede, to purchase loans from the FDIC.

<sup>6</sup> American Banker, *What Recession? Farm Lending Holding Up Well*, Dec. 2<sup>nd</sup>, 2009

<sup>7</sup> Ibid

<sup>8</sup> American Banker, *Losses from CRE Loans Pegged As Banks’ Main Threat in 2010*, Jan. 7, 2010

## Conclusion

There are many unanswered questions due to the proposed rule. Many items are not addressed or are not addressed adequately by FCA. These issues include procedures for divestiture of illegal loans, incorporating a limited version of the controversial “Customer Choice” proposal into this proposal, parameters for determining stock membership programs, the 10 percent of capital level before requiring approval by the FCSI’s funding bank, no FCS fees paid to the DIF while bidding on loans made available by the resolution process funded by the DIF, no requirements to work with community banks and so on.

Just as importantly from our perspective is the need to discuss this issue more thoroughly with rural community banks that have paid considerable assessments into the FDIC’s Deposit Insurance Fund. Therefore, we request a 60 day extension of the public comment period and look forward to discussing this proposal further with the FCA.

Sincerely

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Mark Scanlan  
Vice President, Agriculture and Rural Policy, ICBA