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TO IMPROVE OPERATIONS OF FEDERAL INTERMEDIATE CREDIT BANKS

HEARING BEFORE THE SUBCOMMITTEE ON CONSERVATION AND CREDIT OF THE COMMITTEE ON AGRICULTURE HOUSE OF REPRESENTATIVES EIGHTY-NINTH CONGRESS

FIRST SESSION

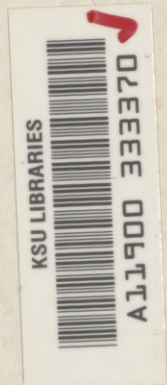
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TO IMPROVE OPERATIONS OF FEDERAL INTERMEDIATE CREDIT BANKS

WEDNESDAY, FEBRUARY 17, 1965

HOUSE OF REPRESENTATIVES,
SUBCOMMITTEE ON CONSERVATION AND CREDIT
OF THE COMMITTEE ON AGRICULTURE,
Washington, D.C.

The subcommittee met, pursuant to notice, at 11 a.m., in room 1310 Longworth House Office Building, Washington, D.C., Hon. W. R. Poage (chairman of the subcommittee) presiding.

Present: Representatives Poage, Gathings, Greigg, Callan, Harvey of Indiana, Teague, and Dole.

Also present: Martha Hannah, staff; Hyde H. Murray, assistant clerk; and Robert C. Bruce, assistant counsel.

Mr. POAGE (presiding). The committee will now pass to H.R. 4152, to increase the authority of intermediate credit banks to market debentures to the public and require a retirement of additional Government capital.

(The bill, H.R. 4152 introduced by Mr. Cooley, follows:)

[H. R. 4152, 89th Cong., 1st sess.]

A BILL To amend the Federal Farm Loan Act and the Farm Credit Act of 1933 to provide means for expediting the retirement of Government capital in the Federal intermediate credit banks, including an increase in the debt permitted such banks in relation to their capital and provision for the production credit associations to acquire additional capital stock therein, to provide for allocating certain earnings of such banks and associations to their users, and for other purposes

Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled, That the Federal Farm Loan Act, as amended, is hereby amended—

(a) by inserting immediately before the semicolon at the end of paragraph (1) of section 202(a) thereof (12 U.S.C. 1031(1)) the following: "or without collateral to the extent authorized under rules and regulations prescribed by the Farm Credit Administration";

(b) by striking out "Provided" and all that follows it in section 203(a) thereof (12 U.S.C. 1041) and substituting therefor the following: "Provided, That the aggregate amount of the outstanding debentures and similar obligations issued by the Federal intermediate credit banks shall not exceed fifteen times the surplus and paid-in capital of all such banks.";

(c) in section 205(a) thereof (12 U.S.C. 1061(a))—

(i) by substituting "one-eighth" for "one-sixth" in the ninth sentence of paragraph (1); and

(ii) by inserting the following as two separate paragraphs between the eleventh and twelfth sentences of paragraph (2):

"Each Federal intermediate credit bank, with the approval of the Farm Credit Administration, may determine the amount of additional class B stock in the bank to be subscribed for by the production credit associations in the farm credit district served by the bank in order to provide capital to meet the credit needs of the bank. The amount so determined shall be allotted among the production credit associations in the district upon such basis that, as nearly as may be practicable, the sum of the class B stock already owned and the additional amount to be subscribed for by each association will be

in the same proportion to the total amount of class B stock already owned and to be subscribed for by all of the associations in the district that the average indebtedness (loans and discounts) of each association to the bank during the immediately preceding three fiscal years is of the average of such indebtedness of all production credit associations to the bank during such three-year period. Each production credit association shall subscribe for class B stock in the bank in the amount so allotted to it. Such subscriptions shall be subject to call and payment therefor shall be made at such times and in such amounts as may be determined by the bank.

"Whenever the relative amounts of class B stock in a Federal intermediate credit bank owned by the production credit associations differ substantially from the proportion indicated in the preceding paragraph, and additional subscriptions to class B stock through which such proportion could be re-established are not contemplated, the Federal intermediate credit bank, with the approval of the Farm Credit Administration, may direct either separately or in combination such transfers, retirements, and reissuance of outstanding class B stock among the associations as will reestablish the aforesaid proportion as nearly as may be practicable. Outstanding class B stock which is transferred or retired for this purpose shall be the oldest stock held by the association and the bank shall pay the association therefor at the fair book value thereof not exceeding par and collect therefor from any production credit association to which such stock is transferred or reissued."; and

(d) in section 206 thereof (12 U.S.C. 1072)—

(i) by striking out "equal to 25 per centum of the outstanding capital stock and participation certificates of the bank" from clause (3) of the first sentence of subsection (a);

(ii) by striking out the second sentence of subsection (a) and inserting in lieu thereof as a separate paragraph the following:

"Amounts applied to reserve account as provided in (3) above, either heretofore or hereafter, shall be allocated on the same patronage basis and have the same tax treatment as is provided in subsection (b) of this section for patronage refunds. Such allocations of reserve account shall be subject to a first lien as additional collateral for any indebtedness of the holders thereof to the bank and in any case where such indebtedness is in default may be retired and canceled for application on such indebtedness, and, in case of liquidation or dissolution of a holder thereof, such reserve account allocations may be retired, all as is provided for capital stock and participation certificates in section 205 of this Act. At the end of any fiscal year that the reserve account of any bank exceeds 25 per centum of its outstanding capital stock and participation certificates, such excess may be distributed, oldest allocations first, in class B stock and participation certificates issued as of the date of the allocations and, whenever the bank has no class A stock outstanding, also in money."; and

(iii) by inserting immediately before the last sentence of subsection (c) the following new sentence: "Any of the reserve established pursuant to subsection (a) of this section shall be paid to the production credit associations and other financing institutions to which such reserve is allocated on the books of the bank.".

SEC. 2. The Farm Credit Act of 1933, as amended, is amended—

(a) by adding the following at the end of subsection (b) of section 22 thereof (12 U.S.C. 1131f(b)): "When so specified in the approval by the Federal intermediate credit bank, such dividends may be paid even though the amount in the surplus account provided for in subsection (a) is less than the minimum prescribed by the bank. If the bylaws of a production credit association so provide, (1) any remaining net earnings at the end of a fiscal year may be distributed on a patronage basis in class A stock of the association and, when the United States does not hold class A stock in the association, also in money, and (2) any part of the earnings for the fiscal year in excess of operating expenses held in the surplus account may be allocated to borrowers on a patronage basis. With the approval of the Federal intermediate credit bank, amounts so allocated may be distributed, oldest allocations first, in class A stock of the association issued as of the date of the allocation and, when the United States does not hold class A stock in the association, also in money. As used in the second preceding sentence 'on a patronage basis' means in the proportion that the amount of interest earned on the loans of each borrower bears to the total interest earned on the loans of all borrowers during the fiscal year."; and

(b) by adding the following as a separate paragraph at the end of section 23 thereof (12 U.S.C. 1131g):

"As a further means of providing capital, a production credit association may, upon such terms and conditions as may be provided in its bylaws, require borrowers to invest in an equity reserve in the association. Amounts so invested by each borrower shall be subject to a lien for the indebtedness of the borrower to the association, application on such indebtedness in event of default by the borrower, charges for losses of the association which are in excess of other loss reserves and surplus, and any portion of the amounts so invested which have not been so used and no longer are required for the purposes of the association may be returned to the borrower by revolving or retirement, all as may be provided in said bylaws."

Mr. POAGE. This is not a measure that has been passed upon as such before, but is a measure the general subject matter of which has been before this committee for a long time.

It seeks to implement what the committee has been trying to do for a long time—trying to move more and more of this Government capital into the hands of the farmers, and we have with us or I have listed here Mr. Stone as the first witness.

Mr. Stone is the Chairman of the Federal Farm Credit Board.

We have Mr. Tootell, Governor of the Farm Credit Administration. I presume Mr. Stone will make the first presentation.

STATEMENT OF J. PITTMAN STONE, CHAIRMAN, FEDERAL FARM CREDIT BOARD

Mr. STONE. Mr. Chairman and gentlemen of the committee, the Farm Credit Administration is recommending enactment of H.R. 4152, to amend certain provisions of the Federal Farm Loan Act and the Farm Credit Act of 1933 with respect to the Federal intermediate credit banks and the production credit associations.

The associations make loans to farmers and ranchers and the loans then are rediscounted with or used as collateral for a loan from a Federal intermediate credit bank. The credit banks in turn obtain funds by selling their collateral trust debentures to the investing public.

For a full explanation of the bill we will rely on our chief executive officer, Gov. R. B. Tootell, who is present and ready to testify right after I finish. However, as Chairman of the Federal Farm Credit Board, which has the general supervision of the Farm Credit Administration, I appreciate the opportunity to make a preliminary statement at this hearing on the bill.

If you are interested in anything personal about me, I am serving on the Federal Farm Credit Board from the Fifth or New Orleans Farm Credit District, consisting of the States of Alabama, Mississippi, and Louisiana. My home is in Mississippi where I am farming about 2,000 acres and also practice law.

When the Federal Farm Credit Board was established a little over 11 years ago, the Farm Credit Act of 1933 directed that the Board make recommendations to carry into effect the declared policy of Congress to encourage and facilitate increased borrower participation in the management, control, and ultimate ownership of the permanent system of agricultural credit made available through institutions operating under the supervision of the Farm Credit Administration.

This was to include means of increasing borrower participation in ownership of the farm credit system to the end that the investment of

the United States in the Federal intermediate credit banks and production credit associations, to which the present bill relates, as well as the banks for cooperatives, may be retired. It is also a specified and continuing function and duty of the Federal Farm Credit Board to make recommendations to Congress for amendments to the laws relative to Federal agricultural credit.

The production credit associations were first authorized in 1933. The capital stock in each association not purchased by the organizers or initial borrowers was all held on behalf of the United States. Government capital in the production credit associations reached a peak of \$90.1 million in 1934.

In accordance with the original design, the Government capital in each association was gradually retired as the borrowers acquired more and more capital stock. The first association to retire all of its Government capital did so at the end of 1944 and today there are only 2 out of 482 associations with Government capital, the total of which is \$40,000.

From their beginning in 1923 the 12 Federal intermediate credit banks were entirely capitalized by the United States and originally there was no provision for private capital to supplant Government capital. However, this was changed when Congress enacted the Farm Credit Act of 1956 following recommendations made by the Federal Farm Credit Board.

Within 2 years after the 1956 legislation became effective, that is, January 1, 1957, the production credit associations had to purchase capital stock in the Federal intermediate credit banks in an aggregate amount equal to 15 percent of the capital stock in the banks then owned by the United States and a corresponding amount of the capital stock owned by the United States, or slightly more than \$13.1 million, was retired. Further, seven of the banks have used earnings to retire about \$454,200 more of the capital stock held by the United States.

Following the 1956 legislation, the production credit associations have also increased their holdings of capital stock in the banks because the annual patronage refunds by each Federal intermediate credit bank are paid to the associations of its district in the form of capital stock. However, there has been no net reduction in the amount of capital stock in the banks held by the United States. This is because during the same period, out of the revolving fund in the Treasury available for that purpose, it has been necessary for the Governor of the Farm Credit Administration to purchase \$46,750,000 of additional capital stock in six of the banks to keep their debt-to-capital ratio within the statutory limit of 10 to 1. As the volume of loans and discounts made by a bank increases, its own borrowings increase proportionately and when the debt-to-capital ratio of a bank approaches the 10-to-1 maximum, it means that the capital of the bank must be increased if the bank is to continue making more loans and discounts. On the whole, therefore, the amount of Government capital put into the banks since 1956 is over three times the amount that has been retired.

It was to do something about this that a study was conducted within the Farm Credit Administration and the bill now before you represents the recommendations growing out of that study. Its primary purpose is to check the flow of additional Government capital into the Federal intermediate credit banks and to expedite the re-

turn of the Government capital now in the banks while, at the same time, permitting the banks to continue the service expected of them.

In order that such a change in trend may begin as soon as possible, it is our hope that the bill may be enacted early in the present session of Congress. This proposed legislation has been considered by and is acceptable to the 12 district farm credit boards that serve as the board of directors of the Federal intermediate credit bank in their respective farm credit districts. A subsequent witness is expected to endorse the legislation on behalf of the National Advisory Committee of Production Credit Associations, of which he is chairman.

As I mentioned in the beginning, Governor Tootell is standing by to undertake a more detailed explanation of our proposal and two of my fellow members on the Federal Farm Credit Board are also present and may testify later.

Thank you, Mr. Chairman, for this opportunity.

Mr. POAGE. Thank you very much, Mr. Stone.

I just noticed that early in your statement you pointed out that you farmed 1,400 acres of land and also practiced law. I just wondered if you meant by that that nobody could farm 1,400 acres of land without practicing law or some other remunerative business to support the farm.

Mr. STONE. I think Lawyer Stone is a very good asset to Farmer Stone.

Mr. POAGE. I found a long time ago it was awfully hard as a lawyer to keep up the farm. In fact, you had to practice a whole lot of law to keep the farm going.

Mr. STONE. That is what I say.

Thank you very much.

Mr. POAGE. Are there any questions of Mr. Stone?

If not, we are very much obliged to you.

Mr. STONE. Thank you. It is a pleasure to be with you.

Mr. POAGE. Governor Tootell. Governor Tootell has been before this committee many, many times. He is the Governor of the Farm Credit Administration, and if you would like to introduce any of your coworkers, you may.

STATEMENT OF R. B. TOOTELL, GOVERNOR, FARM CREDIT ADMINISTRATION; ACCOMPANIED BY F. VERNON WRIGHT, DEPUTY GOVERNOR AND DIRECTOR, SHORT-TERM CREDIT SERVICE; AND PAUL O. RITTER, GENERAL COUNSEL

Mr. TOOTELL. Thank you.

Mr. Chairman, I have with me this morning Mr. F. Vernon Wright, who is Deputy Governor and Director of Short-Term Credit Service and Mr. Paul Ritter, who is our General Counsel in the Farm Credit Administration.

H.R. 4152 would amend certain sections of the Federal Farm Loan Act and the Farm Credit Act of 1933 that relate to the Federal intermediate credit banks and production credit associations. As Governor of the Farm Credit Administration, the independent agency in the executive branch of the Government that has the supervision of those banks and associations, I appreciate being a witness in explanation and support of the bill.

The basic purpose is to enable the Federal intermediate credit banks and the production credit associations to continue the service expected of them while at the same time reducing or eliminating the need for more Government capital in the credit banks and expediting the return of Government capital they now have.

As reflected in its title, the bill includes an increase in the debt permitted the credit banks in relation to their capital and would create an alternate source of capital by providing for the production credit associations to acquire additional capital stock in the credit banks.

In addition to these two major provisions, there are several others also designed to contribute to the purpose of the bill. Among them are provisions for allocating certain retained earnings of such banks and associations to their users.

Before getting into more detail about the bill, though, it may be helpful to present certain background information about the Federal intermediate credit banks and the production credit associations and the need for the proposed legislation.

The 12 Federal intermediate credit banks were established in 1923 to provide agriculture with a permanent, stable, and dependable source of short- and intermediate-term credit. They were organized and operate under title II of the Federal Farm Loan Act as added by the Agricultural Credits Act of 1923 and since amended.

There is 1 bank to serve each of 12 farm credit districts into which the 50 States and Puerto Rico now are divided. These banks discount for, or purchase from, production credit associations and other financing institutions, with their endorsement, notes representing loans made by them to farmers and ranchers. Also, they make loans and advances to such associations and other financing institutions secured by collateral approved by the Governor of the Farm Credit Administration. In addition, the credit banks supervise, assist, and provide services to the production credit associations.

Approximately 95 percent of the discounting and lending by the Federal intermediate credit banks is for the production credit associations, although there also are about 100 other financing institutions presently being served by the banks. For the most part, these other financing institutions are State chartered, privately capitalized credit corporations and livestock loan companies; some are commercial banks.

On the other hand, the production credit associations are chartered by the Farm Credit Administration and operate under the provisions of the Farm Credit Act of 1933, as amended, for the benefit of their member borrowers. There are 482 such associations with from 26 to 77 in each farm credit district. Each association has a prescribed territory, usually ranging from one or more counties up to as much as one State or more, within which it makes loans to farmers and ranchers. Loan maturities usually are not more than a year but loans may be made for terms up to 7 years.

The credit banks finance their operations primarily through the issuance and sale to the investing public of consolidated collateral trust debentures and by direct borrowings from commercial banks. The notes of farmers and ranchers received from production credit associations and other financing institutions are used as collateral for the debentures.

Under existing law, the outstanding debentures and similar obligations of a Federal intermediate credit bank may not exceed 10 times its surplus and paid-in capital. As a consequence, when the ratio of debt to surplus and paid-in capital of a credit bank is close to 10 to 1, and loans and discounts are increasing rapidly, the bank can continue to operate within that ratio only if its surplus and paid-in capital is increased. One way of doing this is to provide additional capital from the revolving fund in the Treasury that is available for the purchase of class A (Government) capital stock in such amount as the Governor of the Farm Credit Administration determines is needed to meet the credit needs of the bank.

The Federal intermediate credit banks were wholly owned by the United States from 1923 through 1956. Amendments made by the Farm Credit Act of 1956, however, provide for the gradual acquisition of capital stock of the credit banks by production credit associations, with a view to the eventual retirement of all Government capital.

Beginning in 1957, the capital stock of the banks was divided into class A stock to be issued to and held only by the Governor of the Farm Credit Administration on behalf of the United States, and class B stock to be issued only to production credit associations. Since then, too, the credit banks have been changed toward a cooperative basis of operation. After restoring any impairments of capital stock, participation certificates, and surplus account, their net earnings each year that are not required to be applied to reserve account or paid to the United States as a franchise tax are distributed as patronage refunds in the form of class B stock to production credit associations and in the form of participation certificates to other financing institutions.

As a first step toward retirement of Government capital the 1956 amendments required the production credit associations to purchase class B stock of the banks in an aggregate amount equal to 15 percent of the total amount of Government capital in the 12 banks on January 1, 1957. This was done and a corresponding amount or \$13.1 million of Government capital was retired.

In addition, the 1956 amendments require each credit bank annually to determine the amount of its class A stock that shall be retired. Whenever the total of the capital stock, participation certificates, surplus, and reserves (net worth) of the bank is more than one-sixth of the highest month-end balance of debentures and other obligations issued by or for the bank, outstanding during the immediately preceding 5 years, the minimum amount of class A stock to be retired is the total amount of class B stock and participation certificates issued for that year.

Under the annual retirement provisions, seven of the banks have retired a total of \$454,000 of class A (Government) stock out of earnings since January 1, 1957. During the same period, though, out of the revolving fund available for that purpose, the Governor of the Farm Credit Administration has had to purchase \$46,750,000 of additional class A (Government) stock in six of the banks to keep the ratio of debt to surplus and paid-in capital within the statutory limit of 10 to 1.

Thus, the amount of Government capital that had to be put into six of the banks is more than three times the amount of Government

capital retired from all of the banks since the 1956 amendments became effective.

Although the 12 banks added \$67.1 million to net worth out of earnings during the 7½-year period from January 1, 1957, through June 30, 1964, the growth in loan volume that made it necessary for some of the banks to obtain additional Government capital out of the revolving fund available for that purpose, in order to stay within the statutory 10-to-1 ratio of debt to surplus and paid-in capital, has resulted in the banks now having nearly \$33.2 million more Government capital than on January 1, 1957.

It is apparent, therefore, that the 1956 amendments have not been adequate to fully accomplish the shift from Government to private ownership within a reasonable period of time.

The amount of Government capital in the production credit associations is negligible, but, inasmuch as the associations actually make the loans to the farmers and ranchers and are being looked to as a source of capital for the Federal intermediate credit banks, it is important to have their financial structure in mind.

Production credit associations were first authorized in 1933. As each association was organized, all of the capital stock not purchased by the organizers or initial borrowers was held on behalf of the United States. In accordance with the original design the Government capital in each association was gradually retired as the borrowers acquired more and more capital stock. From a peak of \$90.1 million in 1934, there now are only 2 out of the 482 associations with Government capital the total of which is \$40,000.

Upon obtaining a loan from a production credit association, the borrower is required to purchase class B stock in the association in the amount of \$5 per \$100 of loan. Such stock is not canceled or retired when the loan is paid, but 2 years after the holder ceases to be a borrower his class B stock is required to be exchanged for class A stock. Class B stock may be transferred only to another farmer borrower or an individual eligible to become a borrower. Class A stock may be purchased and held by the Governor of the Farm Credit Administration and by investors. There also is provision for class C stock which may be purchased and held by the Governor of the Farm Credit Administration and by investors, but there is no such class C stock outstanding at the present time.

In the future the farmers and ranchers that are borrowers from and members of the production credit associations, in addition to providing the net worth of their associations, will also be expected to provide additional capital required by the Federal intermediate credit banks, including that necessary to retire the Government capital in the banks.

In saying this we have not overlooked the other financing institutions that do business with the credit banks but in most districts they provide only a relatively small part of the net worth of the bank. Because of the relationship of the production credit associations to the Federal intermediate credit bank in their respective districts, some of the amendments in the bill necessarily relate to the associations. Their nature and bearing on the operations of the associations will be indicated as we now take up the provisions of the bill section by section.

ANALYSIS OF BILL

Unsecured loans from Federal intermediate credit banks to production credit associations (sec. 1(a) amending sec. 202(a) of the Federal Farm Loan Act, 12 U.S.C. 1031(1)).

In addition to discounting for, or purchasing from a production credit association, the farmers' and ranchers' notes representing loans made by the association, a Federal intermediate credit bank may also—

make loans and advances to any such association secured by such collateral as may be approved by the Governor of the Farm Credit Administration.

To this would be added authority to make loans and advances to production credit associations—

without collateral to the extent authorized under rules and regulations prescribed by the Farm Credit Administration.

This will provide greater flexibility in utilizing the resources of an association. It will permit giving recognition to the value of assets such as accrued interest receivable, cash on hand, investment in office quarters and, at times, acquired property.

Debt to surplus and paid-in capital ratio for Federal intermediate credit banks (sec. 1(b) amending sec. 203(a) of the Federal Farm Loan Act, 12 U.S.C. 1041).

The amount of collateral trust debentures which the Federal intermediate credit banks now may have outstanding is subject to the statutory limitation:

That the aggregate amount of the outstanding debentures and similar obligations issued individually by any Federal intermediate credit bank, together with the amount of outstanding consolidated debentures or other similar obligations issued for its benefit and account, shall not exceed 10 times the surplus and paid-in capital of such bank.

The bill would change the foregoing limitation from a 10-to-1 to a 15-to-1 ratio and apply it to the 12 Federal intermediate credit banks collectively instead of individually. The amended limitation would be:

That the aggregate amount of the outstanding debentures and similar obligations issued by the Federal intermediate credit banks shall not exceed 15 times the surplus and paid-in capital of all such banks.

To the extent practicable, the presently intended policy is that the debt to surplus and paid-in capital ratio of each bank should not be permitted to exceed 12 to 1 except for temporary periods such as seasonal peaks in outstanding borrowings.

Mandatory retirement of Government capital by Federal intermediate credit banks (sec. 1(c)(i) amending sec. 205(a)(1) of the Federal Farm Loan Act, 12 U.S.C. 1061(a)(1)).

Annually at the end of its fiscal year, it is for each Federal intermediate credit bank to determine the amount of its class A (Government) stock that shall be retired. The only further requirement in this respect is that:

Whenever the total of the capital stock, participation certificates, surplus, and reserves of the bank is more than one-sixth of the highest month-end balance of debentures and other obligations issued by or for the bank, outstanding during the immediately preceding 5 years, the minimum amount of class A stock to be retired shall be the total amount of class B stock and participation certificates issued for that year.

The bill would substitute "one-eighth" for "one-sixth" in the quoted sentence. This is deemed warranted because of the increase in the debt to surplus and paid-in capital ratio being proposed under the preceding amendment. The class B stock and participation certificates referred to in the quoted sentence includes not only those issued to the production credit associations and other financing institutions as patronage refunds but also any additional class B stock purchased by production credit associations as may be required under the next amendment.

Additional purchases by production credit associations of class B stock in Federal intermediate credit banks (sec. 1(c)(ii) amending sec. 205(a)(2) of the Federal Farm Loan Act, 12 U.S.C. 1061(a)(2)).

Under the amendments made by the Farm Credit Act of 1956, the production credit associations were required to purchase class B stock in the Federal intermediate credit banks in an amount equal to 15 percent of the class A (Government) stock outstanding on January 1, 1957, and a corresponding amount of such class A (Government) stock was retired. Subsequently, when increased business made more capital necessary in order for a bank to stay within the statutory 10-to-1 debt to surplus and paid-in capital ratio, the Governor of the Farm Credit Administration, out of the revolving fund in the Treasury available for that purpose, purchased additional class A stock on behalf of the United States.

Under the bill, a Federal intermediate credit bank, in order to provide capital to meet its credit needs, may require the production credit associations of its district to subscribe for or otherwise acquire additional class B stock in the bank where necessary and feasible. The relative amount of class B stock in the bank to be held by each association would be in the general proportion that its indebtedness to the bank is to the total of all association indebtedness to the bank. All demands under the new legislation that the associations acquire additional class B stock in a bank would be subject to approval by the Farm Credit Administration and would be with due regard for the circumstances of the associations.

The revolving fund in the Treasury mentioned above would continue available for further subscriptions to class A (Government) stock of the banks if needed.

Allocation to users of Federal intermediate credit banks of net earnings applied to reserve account (sec. 1(d) amending sec. 206 of the Federal Farm Loan Act, 12 U.S.C. 1072).

Since January 1, 1957, each Federal intermediate credit bank, at the end of its fiscal year, after restoring any impairment of capital stock, participation certificates and surplus account, is required to apply 25 percent of its net earnings then remaining to create and maintain a reserve account equal to 25 percent of the outstanding capital stock and participation certificates of the bank.

And—

If at the end of any fiscal year the sum of the surplus and the reserve account of any bank is less than its outstanding capital stock and participation certificates, the bank shall continue to apply such 25 per centum of its net earnings to the reserve account until the sum of the surplus and the reserve account is equal to its outstanding capital stock and participation certificates.

The net earnings finally remaining after paying a franchise tax to the United States, while there is Government capital in a bank,

must be distributed as patronage refunds, in class B stock to production credit associations and participation certificates to other financing institutions. There is now no provision for allocating or distributing the earnings applied to reserve account.

Under the bill, the 25 percent of net earnings remaining after restoring impairments would always be applied to the reserve account each year. All amounts so applied, whether heretofore or hereafter, would be allocated to the production credit associations and other financing institutions on a patronage basis.

These allocations would have the same general treatment for tax and other purposes as is provided for patronage refunds. If a holder of such allocations is in default on indebtedness to the bank, it would be within the discretion of a bank to cancel and retire such allocations for application on the indebtedness. There would be a similar discretion to retire allocations when a holder is liquidated or dissolved. When the total of such allocations exceeds 25 percent of the outstanding capital stock and participation certificates of a bank, such excess may be distributed, oldest allocations first, in class B stock and participation certificates issued as of the date of the allocations and, whenever the bank has no class A stock outstanding also in money. In brief, that is what paragraphs (i), (ii), and (iii) of subsection (d) of section 1 would provide.

Option of production credit association to pay patronage refunds and allocate to borrowers net earnings retained in surplus account (sec. 2(a) amending sec. 22(b) of the Farm Credit Act of 1933 12 U.S.C. 1131f(b)).

Presently 342 production credit associations have bylaws, adopted with the approval of the Farm Credit Administration, under which certain net earnings may be paid to the borrowers as patronage refunds. These are the net earnings remaining each year after applying earnings as specifically directed or authorized by statute or the bylaws. The pertinent statutory provisions are that earnings in excess of operating expense must be applied, first, to restore any capital impairment and, second, to maintain a surplus account, the minimum amount of which is prescribed by the Federal intermediate credit bank.

Dividends on capital stock not to exceed 7 percent a year may be paid when approved by the Federal intermediate credit bank and consistent with policies established by the Farm Credit Administration.

The first sentence added by section 2(a) of the bill would provide that, when so specified in the credit bank approval, such dividends may be paid even though the amount in the surplus account is less than the prescribed minimum.

In addition to recognizing that the finally remaining net earnings may be paid as patronage refunds, the rest of the addition made by section 2(a) of the bill specifically would authorized an association to adopt a bylaw providing for allocation to the borrowers on a patronage basis of any part of the net earnings required to be applied to surplus account or otherwise retained therein.

For tax and other purposes this would permit any net earnings hereafter applied to or retained in the surplus account to be accorded the same treatment as now is given the patronage refunds paid by associations. Inasmuch as all bylaws of the production credit associations are subject to approval of the Federal intermediate credit

bank and the Farm Credit Administration, the policy presently intended to be followed is that bylaws should not be approved which would permit an association to allocate to its borrowers any allocations received by the association from the Federal intermediate credit bank with respect to net earnings included in the reserve account of the bank prior to July 1, 1965.

Option of production credit association to require borrowers to invest in equity reserve in the association as a means of providing capital (sec. 2(b) amending sec. 23 of the Farm Credit Act of 1933, 12 U.S.C. 1131g).

In addition to the capital stock in the production credit association which a borrower is required to own, section 2(b) of the bill would authorize an association, if its bylaws so provide, to require borrowers to invest in an equity reserve in the association upon such terms and conditions as may be provided in its bylaws. Such an equity reserve would be part of the surplus of the association in applying the 10-to-1 debt to paid-in and unimpaired capital and surplus ratio under which the production credit associations must operate. The equity reserve would serve that purpose and without the expense of dividends as would be expected if the same amounts were invested in class A capital stock of the association.

That concludes the section-by-section analysis of the bill and also my initial statement in explanation and support of H.R. 4152. Our submission of this proposed legislation includes a Budget Bureau letter with some comments that we think are not related to either the specific provisions or the general objectives and purposes of the present bill. But if any of them are to be considered in detail here I would like an opportunity later in the hearing to say more about them.

Mr. POAGE. Let me ask you, Governor, right here on that last page, is not that an error, about the middle, where you say "in applying the 10-to-1 debt to paid-in and unimpaired capital and surplus ratio," that it should be 15-to-1 ratio?

Mr. TOOTELL. Mr. Chairman, I did not hear your question.

Mr. POAGE. I say on your last page you read the sentence:

Such an equity reserve would be part of the surplus of the association in applying the 10-to-1 debt to paid-in and unimpaired capital and surplus ratio under which the production credit associations must operate—

That is really a 15-to-1 ratio.

Mr. TOOTELL. No, sir. This refers to the debt-to-capital ratio of a production credit association. The 15 to 1 which we propose has to do with the Federal intermediate credit banks.

Mr. POAGE. You are not changing it for the production credit associations?

Mr. TOOTELL. Not for the production credit associations which are the primary lenders.

Mr. POAGE. You are leaving that 10 to 1, and making 15 to 1 only on intermediate credit banks.

Mr. TOOTELL. Yes, sir.

Mr. POAGE. I did not get that clear.

Now, there was one other item here about which I wanted to raise a little question. I notice that you, on page 8, suggested there that there be, you add, authority to make loans to production credit associations without collateral to the extent authorized under the rules and regulations prescribed by the Farm Credit Administration.

On its face that always arouses a question. Then somewhere there did not you say a little further down that it was the intention that you would not go beyond a 12-to-1 ratio? That would seem to indicate that you felt that we should not go too far on this matter of expanding credit. I know they are not exactly the same thing, but I am particularly interested in finding out if you authorize it to 15 to 1 and you try to hold it to 12, and then you make loans without any collateral, how do you reconcile making those loans without collateral?

Mr. TOOTELL. Mr. Chairman, I would like to have Mr. Vernon Wright who himself for some 15 years was the manager of a production credit association, and for approximately almost 4 years now has been our Director of Short-Term Credit Service, to answer that one on the matter of loans without collateral.

Mr. POAGE. Yes, Mr. Wright.

Mr. WRIGHT. Congressman, the production credit associations today own Government bonds. These bonds are pledged with the intermediate credit banks for direct loans. This is over and above the discounting of loans.

It does not take into account office buildings, accrued interest, in some instances acquired property, and there are certain other assets owned by the production credit associations.

As a result of this, the PCA's have no way to utilize all of their assets in their operations. We have approximately \$22 million invested in production credit association office buildings alone.

This unsecured loan request we think is sound because it would enable the credit banks to lend on the total assets of the associations.

Mr. POAGE. Well, then, what you are saying is really you do not want to make unsecured loans, but you want to be able to use these assets that are a part of the security; is not that what you are saying?

Mr. WRIGHT. No, sir. We would intend, Mr. Chairman, to make unsecured loans.

Mr. POAGE. I know. You would not actually take a lien on the office building, but you would take that into consideration in making it.

Mr. WRIGHT. We would, sir, consider the assets owned by the associations; that is right.

Mr. POAGE. I suppose that gets pretty close to commercial banking when you go to loan something just on a man's signature, does it not? It either gets to commercial banking or it gets to FHA banking, one of the two.

Mr. TOOTELL. Mr. Chairman, I would like to add this: Production credit associations not infrequently make unsecured loans.

Mr. POAGE. I did not know that. I will have to look into that.

Mr. TOOTELL. If your financial statement is good enough, you see, I am sure that they would make you one.

But the other point that I would make in connection with this is that the production credit associations are not permitted by law to borrow anywhere except from a Federal intermediate credit bank.

Mr. POAGE. Yes.

Mr. TOOTELL. And that has a bearing on this point.

Mr. WRIGHT. Mr. Chairman, also all of the assets of an association really are pledged to the credit bank by virtue of the rediscount agreement that each association has with the respective credit bank.

So this, in a sense, I think, would make it justifiable to make unsecured loans to all PCA's.

Mr. POAGE. You do that in one paragraph and then the next paragraph—I will not say paragraphs—but at the same time you greatly increase the ratio of loans to assets. Now, all of this is loosening up considerably your credit.

I think I recognize full well that we are going to have to always keep increasing the amount of money that these people can borrow because the demands are just larger and larger. That is the reason we have not paid off this intermediate credit bank stock. The banks, these production credit associations, have been called upon to make more loans to their borrowers, they have had to make more and more loans to serve their borrowers, and, therefore, they get up to a 10-to-1 ratio, and you have to go out and put more Government stock into them, more Government capital into their capital structure, if they are going to keep making loans. That, as I see it, is the basic reason for the law of 1956 not having retired more of this capital than it has, and I think that is going to continue; do you not?

Mr. TOOTELL. We expect our demand for credit to continue, Mr. Chairman.

However, PCA volume, I think we pointed out here, has increased about $2\frac{1}{2}$ times just since this act went into effect January 1, 1957. Our conservative estimate is that our PCA volume will double in the next 10 years.

I would point this out with regard to this ratio thing. The original legislation that created the 12 intermediate credit banks provided for this 10-to-1 debt-to-capital ratio. They were established presumably to loan to livestock loan companies and agricultural credit corporations that would be set up, and this was the case.

Most of those were weakly capitalized. They did not have experienced management, and this was considered by Congress to be about as wide a ratio as should be permitted, and we think wisely so.

But I would point out that since 1934 practically all of the business, 90 to 95 percent of the business, of the Federal intermediate credit banks has been with production credit associations; and before a Federal intermediate credit bank can lose a dollar, a production credit association has to go completely broke. No Federal intermediate credit bank has lost a dollar on any loan made to a production credit association, or, in fact, on any loan made since 1934. In the meantime, the production credit associations have built up a very strong net worth, and what we really are confronted with here is in a sense a double capitalization of the institutions in our system that are financing farmers.

There is, first, this capitalization of the credit bank, the discounting bank, and then the capitalization of the primary lender, the production credit association. We do not propose to reduce the capital structure, you see, of the production credit associations. We propose to retain this at 10 to 1.

But we feel that our experience indicates that now with the very substantial capital structure in the production credit associations as a backstop against any loss to the credit banks that we would be safe in widening this ratio to a 15-to-1 systemwise.

Mr. POAGE. I do not mean it is necessary to argue with that. But in Washington we have already liberalized our commercial

banking institutions by act of this Congress; at least the Federal Reserve, we have liberalized that. That is one of several things the Congress has done.

There has been a lot of liberalizing of credit, and I think that is really the basis of what we want to consider here: Are we willing to liberalize credit still further.

Personally, I think we must provide the additional source of credit, and I think we have got to keep real clear, though, that we do not want farm credit to become another FHA.

Mr. TOOTELL. Yes.

Mr. POAGE. I have great respect for the FHA, and I think it serves a very worthy purpose. But I do not want you to serve that purpose. I think that there is a difference in the field in which you should operate.

Mr. TOOTELL. Mr. Chairman, I am very glad that you have drawn this distinction. We certainly appreciate your understanding of this distinct difference, and I would say that we do not propose to lower the standards in our lending to farmers and ranchers.

Mr. POAGE. Well, it is almost inevitable that when you have plenty of credit you are going to be a little easier in making your loans than when you do not have.

I have observed that the ordinary bank, when it has a whole lot on deposit is going to be a little easier to borrow money from than in time when deposits are scarce.

Mr. TOOTELL. Mr. Chairman, we are under just the opposite situation. When this banker has his deposits built up and he is paying interest on them he is under pressure to get those loaned. All of our money is hired in the market, and we only hire it as the demand for it has manifested itself through the production credit association and OFI loans, so we have no shortage of money. We are able to get every dollar that is needed. There is no ceiling authorization on us.

The thing that determines the amount of money which we loan is simply the number of sound loans that are submitted by farmers and ranchers, and we go to the market and hire the funds that are needed to cover them, and for the benefit of the new members of the committee, I will point out, without a Government guarantee on them.

Mr. POAGE. Mr. Callan.

Mr. CALLAN. One thing that I would be interested in knowing about: In our area the PCA and the Federal land bank are the two agencies that sponsor the Nebraska football games.

Mr. TOOTELL. Sponsor which?

Mr. CALLAN. They are advertising on the radio that broadcasts the Nebraska football games. In other words, they are out soliciting loans and they sponsor the whole program throughout the year.

In other words, are they soliciting loans to promote their business?

Mr. TOOTELL. Yes, sir; they are soliciting business.

You see, the Federal land banks have been completely member-owned since 1947. The production credit associations are 99⁹⁹/₁₀₀ percent farmer-owned, and they do solicit business, and they do that for these reasons: One, an increase in the volume of business that an association has permits it to extend credit at a lesser rate to its members than would be the case if it had a small volume.

We have a few associations in the United States that do have a small volume of business, and because they have to pay the market cost of money, plus the cost of maintaining an office, and doing business, their interest charged to their members is relatively high.

The objective of the production credit and the land bank is to make loans to their farmer members at the lowest cost consistent with sound business principles.

Mr. POAGE. Yes.

Mr. HARVEY. Governor, on page 13 up near the top of your statement you refer to a ceiling on dividends. I assume now this is referring to production credit.

Mr. TOOTELL. Yes, sir.

Mr. HARVEY. And you are saying that they may pay dividends to their borrowers. Is this now on their class B stock?

Mr. TOOTELL. On class B stock or on class A stock.

Mr. HARVEY. Not to exceed 7 percent. Now, I am intrigued to know just what goes here. In the first place, do very many of your PCA's after they have met all of their other reserve requirements and so forth, get to the place where this becomes a factor?

Mr. TOOTELL. Well, Mr. Harvey, this depends upon how good a year they have had. If the interest rate in the market, the cost of money in the market, is going down, it will mean that the PCA probably has good earnings for that year, and will pay a reasonable dividend.

If, as happened this last year, the cost of money is going up, they pass on this additional cost to the farmer as sparingly as possible. They compress their net earnings. And last year, Mr. Wright, only a relatively small percentage of the PCA's paid dividends, I believe.

Mr. WRIGHT. Well, 412 out of the 482 PCA's paid dividends on class A stock in 1964 and 11 associations paid dividends on class B stock in 1964.

Mr. HARVEY. How much was the dividend, how much was the total of the dividends paid on class A stock?

Mr. WRIGHT. Well, let me see, the total amount in dividends was \$2,758,724, and most of this, of course, Congressman Harvey, would have been class A stock dividends, because only 11 associations paid dividends on B stock.

Mr. HARVEY. When they pay this dividend on class A stock, the Government holds, the intermediate credit bank holds, that stock; is that not right?

Mr. WRIGHT. No, sir, Mr. Harvey. The farmer borrowers.

Mr. HARVEY. The farmer borrower who continues to hold and carry that stock becomes class A instead of class B when he ceases to become an active borrower, and he holds the stock, so it is actually just the same as if you would hold stock in any other enterprise so far as that is concerned.

Mr. TOOTELL. Well, it is difficult to keep the credit bank operation and the PCA operation clear and distinct, but this is the PCA operation referred to here.

I think we need to keep in mind that the class A stock in a production credit association is investment stock over and above the legal requirement.

Now, the B stock requirement is a legal requirement equivalent to 5 percent of the maximum amount of the loan.

Many borrowers, many farmer members, in associations that have been expanding rapidly have been prevailed upon to invest additional sums in class A stock in order to help capitalize the association and, therefore, when dividends are paid they are paid first on A stock which is to those people who invested beyond the legal requirement.

Now, in a year in which PCA's make good earnings, why, a fairly high percentage of them will pay some dividends, 2, or 3, or up to 4 percent on B stock, and would you not say that generally dividends are not paid in excess of about 4 percent?

Mr. WRIGHT. Generally this is true.

Mr. HARVEY. Is that just sort of a policy that you have persuaded them to follow or is it a limit because they do not make more than that?

Mr. TOOTELL. Well, I would say that it is both. There is not much point in their pursuing a policy that would result in earnings which would permit them to pay 7 percent. They try to operate in a way that permits them to make just reasonable earnings out of which ordinarily 3½- or 4-percent dividends on B stock would be the limit.

Mr. HARVEY. That was my understanding. When I saw this 7-percent figure there it intrigued me because if you were supervising these PCA's adequately, and advising them with regard to the procedures, as I am sure you do, well, I just do not think that 7-percent figure is a very important one, really.

Mr. TOOTELL. It is not. It is simply a statutory limit or ceiling, and we do not have to invoke that.

Mr. HARVEY. It would be like giving your boy a Volkswagen and telling him not to drive over 120 miles an hour. That is all, Mr. Chairman.

Mr. POAGE. Any further questions?

Mr. Teague.

Mr. TEAGUE. Yes, Mr. Chairman, I have one brief question. It does not have to do with this specific bill, but it does have, I believe, to do with—it does involve—the Governor's general area of responsibility.

It may not have come to your attention that California fruit and produce growers are having a very difficult time because of their inability to harvest their crops. I would hope it is temporary, but I am not sure it is. It will be temporary if they can develop a domestic supply or if the Government changes its policy to allow foreign supplemental labor to come in. But at the moment I am told that farmers are having an increasingly difficult time in getting credit from commercial banks. It may be too early for you to have reached any judgment on this. But have you yet noticed any increase in your applications for credit in California from produce and tree farmers, tree fruit farmers?

Mr. TOOTELL. Mr. Congressman, I was in California just the day before yesterday. I flew back overnight in order to be here for the hearing, and I met with the Berkeley Farm Credit Board and talked with the officers in the intermediate credit bank. They are very concerned, of course, about this labor shortage, but they said that to date that it had not influenced their credit operations or their requests for credit.

Mr. TEAGUE. Which probably—pardon me, Governor, it is probably a little early.

Mr. TOOTELL. Yes, I think that is right.

Mr. TEAGUE. There is citrus all year but lettuce and tomatoes are also grown in the more northerly California counties. In several weeks or more there will be the harvest peak, which I predict will be a disaster situation.

Mr. TOOTELL. Later on this morning Mr. Glen Harris, a member of our Federal Farm Credit Board from California, is going to testify, and he might have something to add on that point.

Mr. TEAGUE. Thank you, Mr. Chairman.

Mr. POAGE. Mr. Dole.

Mr. DOLE. Just as a matter of information, in the last decade, for example, your volume of loans, of course, has increased. I am wondering if the number of borrowers has gone down and you now make bigger loans to fewer farmers?

Mr. TOOTELL. No, Mr. Dole, we are rather proud of the fact that in spite of a very substantial decrease in number of farms, and I suppose that would be at least a million and a quarter in the last decade, that our number of borrowers has increased.

One of my assistants may be able to look up the increase in number, but it has been fairly substantial. Our production credit associations, I would say, had approximately 25 percent more borrowers in 1964 than they had in 1954.

Our Federal land banks had something like 20 percent more borrowers. Our banks for cooperatives had something like 35 percent more borrowers. So it is a combination of number of borrowers and also the size of the loan. The size of loan certainly has been going up markedly.

Mr. DOLE. Do you have any figure on it, Mr. Wright?

Mr. WRIGHT. Yes, sir; I do. Since 1957 the number of PCA members are up 55,507 or 11.5 percent since January 1, 1957.

We have a total membership now of 537,751.

Mr. DOLE. What percent of your loans are loans during that same period?

Mr. WRIGHT. I would say roughly the same. This past year the number of loans made were up a little less than that, but roughly the same, I would say.

Mr. DOLE. If this ratio is changed from 10 to 1 to 15 to 1, how much are we talking about making available in dollars on an estimate? Do you have any estimate on that?

Mr. TOOTELL. Well, the Federal intermediate credit banks in calendar year 1964 loaned \$4.7 billion mostly to production credit associations.

As I indicated earlier, we believe that over the next 10 years that this volume will double.

The effect of our proposed change in ratio would simply be to make it possible to meet this increasing volume without having to go to the Treasury for more revolving fund money.

Mr. DOLE. Thank you.

Mr. POAGE. Are there any further questions?

If not, we are very much obliged to you, Governor.

Mr. TOOTELL. Thank you, Mr. Chairman.

Mr. POAGE. I believe next is Mr. Banks, if he would care to make a statement. We will be glad to hear from him.

This is Mr. King L. Banks, chairman of the National Advisory Committee of Production Credit Associations.

STATEMENT OF KING L. BANKS, CHAIRMAN, NATIONAL ADVISORY COMMITTEE OF PRODUCTION CREDIT ASSOCIATIONS

Mr. BANKS. Thank you, Mr. Chairman and gentlemen of the committee, my name is King L. Banks and I live in Delta, Colo. It is on the western slope of the Rockies.

I am chairman of the Ninth District Production Credit Advisory Committee. The ninth district is composed of Kansas, Oklahoma, New Mexico, and Colorado. I represent the ninth district on the National Advisory Committee of Production Credit Associations and at present am chairman of that body. I am making this statement in that capacity.

As background, I was born and reared on a farm and have been a farmer all my life. Like Mr. Stone I am a farmer by proxy at present. I still own the farm, of course.

I graduated from two agricultural colleges, the last one being the University of Missouri.

I helped organize the Montrose Production Credit Association in 1933, went on the board and loan committee in February 1937, and have served as a director ever since, becoming president in 1952. I have served on the national committee for 10 years and have been chairman the past 8 years. I am also a member of the Federal Land Bank Association of Montrose.

The production credit associations in each of 11 farm credit districts have formed an advisory committee, consisting of association directors, that consults with the board of directors and officers of the Federal intermediate credit bank of the district. Each district advisory committee has named a representative to the National Advisory Committee of Production Credit Associations. The national advisory committee meets once a year in Washington to consider questions submitted by the district advisory committees. Recommendations emanating from that meeting are then discussed with the Federal Farm Credit Board.

Our last meeting was here in Washington in April of 1964, at which time the committee endorsed the proposed legislation which has since been introduced as H.R. 4152.

Of the 482 production credit associations there are today only 2 associations with Government capital, the total of which is \$40,000. This is a reduction from a peak of \$90.1 million in 1934.

Those of us who have worked with the production credit associations since they were first organized in 1933 and 1934 are proud of this record. We look forward to the enactment of this bill, to the end that the capital structure of the system may be employed more effectively in meeting the credit needs of farmers and stockmen; and that production credit associations may make more rapid progress in acquiring capital stock in the Federal intermediate credit banks, in order that retirement of Government-owned stock in the banks may be expedited.

The proposed legislation has been thoroughly discussed with all associations in the country. There was very little objection in these discussions and they were on minor matters. As it now stands this proposed legislation has the unanimous support of all production credit associations.

I might say that this report I am making is in my own words, and you may want to overlook some of my expressions in it.

In section 1(a) at present PCA's are restricted in their loaning capacities to a 10-to-1 ratio of their capital and surplus. A large number of associations have built and own their own home as well as branch offices, in some cases.

I might say in my own association we have three branch offices. In addition, some have a small amount of acquired property obtained in the process of liquidation of loans. The value of this real property is not counted in this ratio. This has tied up a large amount of capital and yet is excellent collateral. Section 1 (a) simply authorizes the Federal intermediate credit bank to recognize the value of real property and other assets in making loans to the associations.

Here I might depart from this just a little bit. In Governor Tootell's testimony, as far as the question on unsecured loans, gentlemen, everything we have got is in the intermediate credit bank. We are buying the intermediate credit bank, and if we, as far as being unsecured is concerned, if we cannot pay our loan they are going to take the real property and the home offices and everything else we have got.

Now, section 1(b), the present law restricts FICB's to a loaning ratio of 10 to 1. I doubt if anyone in this room visualized what would take place in Farm Credit when it was organized some 32 years ago. Nor do I think very many foresaw 10 years ago what has taken place since. Requirements for credit in farming have increased enormously. Whether this movement of small farmers off the land is good or bad is debatable but there can be no debate on the statement that larger farm units for those who remain are an absolute necessity. Only those small farmers with off-the-farm jobs are able to buck the tide. This means more land, more livestock, and larger and more expensive machinery. So the need for additional credit is fully justified.

Due to reasons mentioned and the loaning ratio of 10 to 1 the FIBCS's have been bumping the ceiling. To keep their doors open and to keep this avenue of farm credit available many have had to ask for additional Government capital from the revolving fund. This revolving fund as you know was set up with this in mind and is a source of additional capital for the FICB's so that they can continue to discount the paper of the PCA's and OFI's. The Farm Credit Act of 1956 called for the PCA's to purchase the credit banks and by a prescribed formula to orderly retire Government capital in the system. This act also placed the FICB's on a cooperative basis so that net earnings could be returned to PCA's and OFI's on a patronage basis. The purpose of this section to raise the FICB ratio up to 15 to 1 is mainly to obviate the credit banks having to call on the revolving fund for additional capital in these rapidly changing farm credit times. We feel that this is fully justified for the reason that the PCA's will eventually retire all Government capital and own the system outright.

Section 1(c)(i): It is felt that this change is desirable due to the change in debt to capital ratio proposed in the preceding section. Our managers and accounting departments recommend this and our committee has agreed to it.

Section 1(c)(ii): This was the only part of the proposed legislation about which there was any question when it was presented to all associations last year. It was very thoroughly discussed in all dis-

tricts and it was agreed that it would be for the good of the system if due regard for the circumstances of the associations concerned were taken into consideration. To show our good faith we agreed we would go along with this change.

Section 1(d): As mentioned before each FICB was set up on a cooperative basis in the 1956 act and any earnings, after certain provisions in the law were complied with, were to be paid in B stock on a patronage basis to each PCA and participation certificates to OFI's. Among these regulations was one concerning certain additions to reserves. However, there was no provision for allocating these reserves to the associations and the OFI's. The three paragraphs under subsection (d) will provide for correcting this situation.

Section 2(a): This will allow an association, with proper changes in its bylaws, to follow the same procedure with its members as the FICB proposes to do with associations. At present the surplus of associations as well as the credit banks has never been allocated to those responsible for its accumulation. This means that only on dissolution could these funds be distributed. We have no intention of dissolving so we should provide means for starting allocation of these reserves. However, a cutoff date is necessary and this is set for July 1, 1965.

If you will pardon me I would like to make a personal reference to our own association in Colorado. We recently looked at a sample of our loans which we have done periodically since 1955. We came up with some startling figures. Our B stock members, who are active farmers, have remained about the same in number although we made some 608 new loans during this period. During this same period we lost 563, very few of whom have gone to other financing agencies. Some have moved away, some deceased and others just decided to sell out and quit while they still had a little left.

With only a few more members on last January 1 than we had in 1955, our dollar volume of loans has increased almost three times, from \$3.5 million to \$9.8 million.

Our average size loan has increased 2½ times. Over half of our members have outside income. This certainly emphasizes the necessity for passage of H.R. 4152 because we are sure this trend will continue at least for the foreseeable future and we want to be in a position to serve the credit needs of our members.

I thank you gentlemen for the opportunity of appearing before you.

Mr. POAGE. Thank you very much, Mr. Banks. I do not want to cut anybody off, but we just want to hear the rest of the witnesses.

If there are no questions of Mr. Banks, we are much obliged to you.

We will hear from Mr. Glen R. Harris, a member of the Federal Farm Credit Board.

STATEMENT OF GLEN R. HARRIS, MEMBER, FEDERAL FARM CREDIT BOARD

Mr. HARRIS. Mr. Chairman and gentlemen of the committee, my name is Glen R. Harris and I am just finishing up a 6-year term on the Federal Farm Credit Board as the member from the 11th or Berkeley Farm Credit District, which includes the States of Hawaii, California, Nevada, Utah, and Arizona.

I have farmed since 1924 and that is also my present occupation.

I am now a borrower from and a member of the Chico Production Credit Association in California and in the past I have been both a director and president of the association.

From 1953 to 1959 I was a member and chairman of the National Advisory Committee of Production Credit Associations, the position Mr. Banks now holds.

I have always been interested in the relationship between the production credit associations, which makes the short- and intermediate-term loans to farmers and ranchers, and the Federal intermediate credit bank which finances the associations in its district, and I might add particularly interested in providing means by which the farmers and ranchers may finally own the complete system.

When the Farm Credit Act of 1956 changed the operation of a Federal intermediate credit bank toward a cooperative basis and provided for the production credit associations to acquire capital stock in the Federal intermediate credit bank of the district in substitution for capital stock held by the United States, the associations were called upon to undertake certain responsibilities which they were glad to do.

During 1957 and 1958 they purchased capital stock in the Federal intermediate credit banks equal to 15 percent of the capital stock then owned by the United States. This amounted to some \$13.1 million and a corresponding amount of Government capital was retired.

Under the present bill, H.R. 4152, the production credit associations may be called upon to purchase additional capital stock in the Federal intermediate credit banks. I am sure that they will again be willing to meet their responsibilities in this respect. However, it would be tantamount to a breach of faith if, changes should now be made in the basis set forth in the 1956 act under which the associations made their initial purchase and embarked on a program for acquiring the remaining capital stock in the Federal intermediate credit banks.

I mention this and would like to develop it a little further in view of some statements made in the letter by which the Bureau of the Budget cleared the present recommendations of the Farm Credit Administration for submission to Congress. It is our thought that none of the ideas contained therein should be given effect to hold up or alter the provisions proposed in H.R. 4152.

As we see it, allocation on a patronage basis of the amounts retained in the reserve account of a Federal intermediate credit bank will place its operation on a more cooperative basis and will have the further effect of adding to the net worth of the production credit associations.

Further, we see no way in which this would adversely affect the Government's interest.

When it enacted the Farm Credit Act of 1956, Congress specified how the franchise tax for a Federal intermediate credit bank should be computed for any year in which it had Government capital. At the same time, Congress also provided that while a Federal intermediate credit bank has Government capital the patronage refunds paid by it to a production credit association in capital stock and to other financing institutions in participation certificates should not be subject to Federal income tax thereon to the recipient. Since both of such provisions will no longer have any application to a bank after its Government capital is retired, and since a basic objective of the present bill is to expedite retirement of Government capital, we do not consider

that this is occasion for changing the decisions made by Congress in these two respects as recently as 1956. Neither do we feel that the present legislative proposals made by the Farm Credit Administration should afford occasion for the suggestion that all existing tax exemptions of the Federal intermediate credit banks should be eliminated upon retirement of Government stock.

I would like to hope, therefore, that you may see fit to act favorably on the proposals that have been made to you by the Farm Credit Administration.

Mr. POAGE. Thank you very much, Mr. Harris.

Any questions?

Mr. TEAGUE. I have no questions, but I would like to commend Mr. Harris, my fellow Californian, on his very precise statement.

Mr. POAGE. Thank you, Mr. Harris.

Mr. HARRIS. Thank you.

Mr. POAGE. Now we will hear from my fellow Texan friend, Mr. David Gault, who is a member of the Federal Farm Credit Board. I know he is a practicing farmer and makes his living at it, and, so far as I know, without any other profession.

Mr. Gault, we will be glad to hear from you.

STATEMENT OF DAVID G. GAULT, MEMBER, FEDERAL FARM CREDIT BOARD

Mr. GAULT. Mr. Chairman, it certainly is a pleasure to meet before you today.

My name is David G. Gault and I am the member of the Federal Farm Credit Board from the 10th or Houston Farm Credit District which consists of the State of Texas. Since 1945 I have been self-employed in general farming and dairying. My present operation is a 1,400-acre 200-milking cow dairy farm, plus replacement heifers and small beef herd. I have also been general manager of the Mid-Tex Milk Producers' Association since 1956. In the past I have been a director of the Austin Production Credit Association, of which I have been a member since 1936. I have also served on the National Advisory Committee of Production Credit Associations.

Others may mention it too but I do not believe it does any harm to say it more than once. The production credit associations now have over \$2.1 billion loans outstanding to over 290,000 farmers and ranchers. For 1964, there were over 360,000 loans made in the total amount of \$3.7 billion. The total of the member stockholders of these associations is 540,000. To finance the associations in making these loans the Federal intermediate credit banks now have outstanding with the investing public over \$2.1 billion of their consolidated collateral trust debentures. This reflects a very great service being rendered by the credit banks and associations.

I would like to express myself in favor of H.R. 4152 as recommended by the Farm Credit Administration. I am just finishing the first year of my 6-year term on the Federal Farm Credit Board and it was largely during this period that the Board decided upon the proposals included in H.R. 4152. Governor Tootell has explained in some detail why they are considered necessary. On that I would only repeat that the changes made by the Farm Credit Act of 1956 will need to be supplemented with some further amendments if the shift

from Government to private ownership of the Federal intermediate credit banks is to be accomplished within a reasonable period of time.

I think it is important that the provisions of the bill be considered in the light of the policy and purpose intended to be served by the Federal intermediate credit banks and the production credit associations as heretofore specified by Congress. In the Farm Credit Acts of 1953 and 1956 Congress declared as policy that borrower participation should be increased and for the Government capital in the Federal intermediate credit banks to be retired and replaced with capital stock held by the production credit associations. If we measure the present bill against this policy, as I think we should, some of the comments made in connection with the bill are hardly relevant.

Under such an approach it would seem inappropriate to suggest that there now should be any change in the decisions made by Congress in 1956 regarding the tax treatment of patronage refunds paid by a Federal intermediate credit bank and the formula for computing its franchise tax. Both of such provisions will be applicable only so long as there is Government capital in a particular bank.

It would seem to follow also that any suggestion to eliminate all existing tax exemptions of a Federal intermediate credit bank upon retirement of Government stock is not relevant to the provisions included in H.R. 4152 or to the policy and purpose intended to be served by them. While the function performed by the Federal intermediate credit banks is much better known today and likely to be taken for granted, that function is no less in the public interest than it always has been. The law under which the credit banks were established provided certain general tax exemptions for the banks that are in continuing terms. When the operation of the banks was changed toward a cooperative basis in 1956, with provision for retirement of Government capital and substitution of capital provided by the production credit associations, no change was made in the continuing tax exemptions of the credit banks. Since then the production credit associations have purchased capital stock in the banks and we now are looking to them to acquire more in order that the Government capital may be retired within a reasonable time. In the circumstances, we think that no change in the exemptions is indicated either by anything in the present bill or otherwise.

Mr. Chairman, I want to express my thanks for the opportunity to meet with this committee. I know time is running short and that concludes my statement.

Mr. POAGE. We are very much obliged to you, Mr. Gault.

Are there any questions?

If not, we thank you so much.

We will now hear from Mr. Harry Graham of the National Grange.

STATEMENT OF HARRY L. GRAHAM, LEGISLATIVE REPRESENTATIVE, NATIONAL GRANGE

Mr. GRAHAM. Mr. Chairman, I am only going to call attention to the first three pages of this now, and of the statement.

Mr. POAGE. Without objection, it will all be inserted in the record.

Mr. GRAHAM. I would like to also say that the last part of the statement that has been prepared has been an attempt to answer some of the objections that were raised by the Bureau of the Budget,

and having said that, I am going to leave it simply for your information.

Beginning in the middle of page 1, let me read for a little bit because I think I can do it faster that way.

Our concern about farm credit is increasing because of developments during the last few years, which indicate the increasing need and demand for long-term credit at reasonably low costs if the farm operators who have continued to expand their operation as a means of staying in business are to survive.

The phenomena of American agricultural production is based on a technological revolution which has been the direct result of substituting capital for labor. This trend is increasing in tempo. It is complicated by the fact that the prices for agricultural production have not kept pace with the costs of production and consequently the inputs into the agricultural plant have exceeded the outputs for a number of years.

Another way of saying this is to remind this committee that farm prices have reached a parity index of 100 percent only twice during the last 50 years and each of these times was when the country was either preparing for war or engaged in war. The parity index is holding at a steady 75 percent.

The obvious result of this expansion of the productive plant without adequate compensation has been that the farmers have been substituting credit for earnings. The capitalization both in land and in the assets of production or the non-real-estate loans have been increasing steadily.

I would point out to you that farm mortgage debt index has increased from 100 in 1950 to 249 in 1962. The non-real-estate debt index has increased from 100 to 235 during the same period. All debt has increased from 100 to 362 during this 12-year period; however, the production assets have increased only from 100 to 277. In other words, during this 12-year period the debt index increased by 262 points and the asset index increased by 177.

At present, most of the increase in assets is in real property despite the continued increase in non-real-estate debts. This is also despite the fact that increasing numbers of the so-called production or operating loans are being secured by mortgages on real estate.

At the same time the character of the loans has changed from the regular commercial loans for short-term indebtedness to production credit-type loans and to longer term, lower interest loans such as the Farmers Home Administration. This is partly the result of the availability of credit through our cooperative lending agencies or through our Federal institutions but it is also partly a result of the fact that the rural banks which supply the majority of the private capital for the short-term loans have loaned up to their legal limitation.

Might I take just a second to say in these reports from the Independent Bankers Association and the Federal Reserve Board indicate that they are loaning about 80 percent of their total deposits. Now, they cannot go any further under legal limits. The reports that we have had during the last week indicate that due to the change in the interest rate which the Federal Reserve bank made recently, trying to compensate for some of the outflow of gold or trying to control that, due to that change these rural banks are telling us now they are being forced to discount their loans somewhere between 95 and 100

percent, more of them toward the 95 percent than the 100 percent, which means that the operating capital that they have been using is being used up in this discounting of the loans.

Now, this kind of a situation is serious enough that the bankers are beginning to worry very much about it, and I think we have got to worry about it, too, and this is one reason why we are so enthusiastic about supporting this particular legislation, because we have a fear there is going to be an increased demand for this kind of legislation due to what is happening in our rural banks.

This was primarily what I wanted to call to your attention except for one other thing, and that is the next paragraph.

Revised estimates of the total amount of real estate farm debt and non-real-estate farm debt held by nonreporting creditors shows that the non-real-estate farm debt held by reporting institutions has increased from \$2,834 million in 1950 to \$9,465 million in 1964.

Of equal significance and more hazardous to the financial structure of American farms is the fact that the debt held by nonreporting creditors including merchants and dealers, consumers and sales finance companies, and various nonreporting lending institutions, individuals, and miscellaneous creditors, have increased from \$2,320 million in 1950 to \$6,720 million in 1964. It is also significant to note that this last figure compares with an earlier estimate \$4,500 million for debts held by nonreporting creditors.

In other words, our estimates on this have been too low until very recently. This confirms the suspicions that some of us had in the past.

Now, I think, with that statement I would conclude this except, that I want to state for the record, that we are concerned with any attempt to solve the problem of farm income on a permanent basis by simply extending credit; that once this is done, and we think this has to be done, we have still got to come to grips, and very rapidly and very thoughtfully, with this whole problem of farm income and what is involved in it, because only thus can we actually justify the increase in farm credit in the amounts that seem to be required in the future.

Mr. POAGE. Thank you very much, Mr. Graham.
(The prepared statement of Mr. Graham follows:)

STATEMENT OF THE NATIONAL GRANGE BY HARRY L. GRAHAM, LEGISLATIVE REPRESENTATIVE, WASHINGTON, D.C.

Mr. Chairman, members of the committee, my name is Harry L. Graham. I am the legislative representative for the National Grange.

We appreciate the opportunity to appear before this committee and its members who have long distinguished themselves by their interest in the farm problems and especially the problem of farm credit because the problems confronting American farmers at this point are serious and they need the immediate attention of this committee and the Members of the House of Representatives and the Senate.

The National Grange has had a long history of interest in farm credit and through the leadership of Mr. Albert Goss, former master of the National Grange, and the present national master, Herschel D. Newsom, it has rendered significant service to the field of agricultural credit.

Our concern, however, is increasing because of developments during the last few years which indicate the increasing need and demand for long-term credit at reasonably low costs if the farm operators who have continued to expand their operation as a means of staying in business are to survive.

The phenomena of American agricultural production is based on a technological revolution which has been the direct result of substituting capital for labor. This trend is increasing in tempo. It is complicated by the fact that the prices for agricultural production have not kept pace with the costs of production and consequently the inputs into the agricultural plant have exceeded the outputs for a number of years. Another way of saying this is to remind this committee that farm prices have reached a parity index of 100 percent only twice during the last 50 years and each of these times was when the country was either preparing for war or engaged in war. The parity index is holding at a steady 75 percent.

The obvious result of this expansion of the productive plant without adequate compensation has been that the farmers have been substituting credit for earnings. The capitalization both in land and in the assets of production or the non-real-estate loans have been increasing steadily. I would point out to you that farm mortgage debt index has increased from 100 in 1950 to 249 in 1962. The non-real-estate debt index has increased from 100 to 235 during the same period. All debt has increased from 100 to 362 during this 12-year period; however, the production assets have increased only from 100 to 277. In other words, during this 12-year period the debt index increased by 262 points and the asset index increased by 177.

At present, most of the increase in assets is in real property despite the continued increase in non-real-estate debts. This is also despite the fact that increasing numbers of the so-called production or operating loans are being secured by mortgages on real estate.

At the same time the character of the loans has changed from the regular commercial loans for short-term indebtedness to production credit type loans and to longer term, lower interest loans such as the Farmers Home Administration. This is partly the result of the availability of credit through our cooperative lending agencies or through our Federal institutions but it is also partly a result of the fact that the rural banks which supply the majority of the private capital for the short-term loans have loaned up to their legal limitation.

Reports from the Independent Bankers Association and the Federal Reserve Board indicate that the rural banks at the present time are loaning about 80 percent of their total deposits which is their legal limit. Indeed, a number of them are discounting their short-term farm paper for as low as 96 percent in order to get capital on which to operate.

Revised estimates of the total amount of real estate farm debt and non-real-estate farm debt held by nonreporting creditors shows that the non-real-estate farm debt held by reporting institutions has increased from \$2,834 million in 1950 to \$9,465 million in 1964. Of equal significance and more hazardous to the financial structure of American farms is the fact that the debt held by nonreporting creditors, including merchants and dealers, consumers and sales finance companies, and various nonreporting lending institutions, individuals, and miscellaneous creditors, have increased from \$2,320 million in 1950 to \$6,720 million in 1964. It is also significant to note that this last figure compares with an earlier estimate \$4,500 million for debts held by nonreporting creditors. In other words, these debts are \$2,220 million more than it was believed prior to a recent revision of the estimates.

Much of this latter group of nonreported debts is of a relatively short-term and high-interest character. The hazard is that many of these are demand debts or they are exceptionally expensive to service. We must anticipate that many of these must move from their present relationships into the more permanent type credit agencies. This movement will be rapidly accelerated if there is any further deterioration in the price of agricultural commodities. Therefore, we think that it is a matter of prudence and caution that legislative provision is being proposed to deal with the anticipated needs of our agricultural producers both in the cooperative lending institutions which they own and in the Farmers Home Administration which makes credit available where no other credit can be obtained. We congratulate both the distinguished chairman of this committee for having introduced H.R. 4152 to amend the Federal Farm Loan Act and Farm Credit Act of 1933 to provide means for expediting the retirement of Government capital in the Federal intermediate credit banks and to increase the amount of debts permitted such banks in relation to their capital.

We urge passage of this legislation.

We have noted with interest the communication addressed to the Honorable R. B. Tootell, Governor, the Farm Credit Administration, and directed to the attention of Mr. Paul O. Ritter and which was written by Mr. Phillip S. Hughes, Assistant Director for Legislative Reference of the Bureau of the Budget. This

letter was printed in the January 15, 1965, issue of the Congressional Record on page 522 of the Senate section. The last paragraph of this letter dealt with the specific criticisms of the bill from the Bureau of the Budget. This paragraph reads as follows:

"With respect to specific provisions of the bill, we regard the proposed section 1(d), relating to the allocation of the FICB earnings, as adversely affecting the Government's interest and unnecessary to the basic objective of the bill. Further, we believe that the basis for computing the franchise tax paid by the FICB's should be modified to make it more consistent with the credit program policy guidelines. We also believe that, in line with general tax policy, patronage refunds received by the PCA's from FICB's in which the Government owns stock should be made taxable. Finally, we believe that there should be provision for the elimination, upon retirement of Government stock, of existing tax exemptions afforded the FICB's."

In studying this bill it is our considered judgment that section 1(d) contributes to the overall purpose and objective of the bill and we do not recognize any way in which it should adversely affect the Government's interest. The other three suggestions serve other interests and are not related to the specific provisions of the bill or its overall purpose and objective. In the circumstances, it is not considered that such suggestions either singly or collectively should be permitted to delay H.R. 4152 or alter any of its provisions.

"With respect to specific provisions of the bill, we regard the proposed section 1(d), relating to the allocation of FICB earnings, as adversely affecting the Government's interest and unnecessary to the basic objective of the bill."

Section 1(d) would provide that the net earnings of a Federal intermediate credit bank applied to its reserve account each year shall be allocated on the same patronage basis and have the same tax treatment as is provided under existing law for patronage refunds. This means that such amounts would be allocated to production credit associations and other financing institutions in the proportion that they pay interest to the bank and, while the United States owns capital stock in a bank, that the recipients of such allocations shall not be subject to Federal income taxes thereon.

As to a Federal intermediate credit bank, such allocations will put the annual application of net earnings more completely on a cooperative basis. As to the production credit associations, such allocations will increase their net worth for several purposes, one of which would be to increase the permissible amount of their borrowings from the Federal intermediate credit bank, since such borrowings are limited to 10 times their capital and paid-in surplus. In these respects, therefore, section 1(d) seems appropriate to the basic objective of the bill.

We think it would be difficult to demonstrate, too, that allocation of Federal intermediate credit bank earnings retained in reserve account would adversely affect the Government's interest.

"Further, we believe that the basis for computing the franchise tax paid by the FICB's should be modified to make it more consistent with the credit program policy guidelines."

The reference presumably is to the report of the Committee on Federal Credit Programs to the President of the United States which was transmitted by the President to agencies with responsibilities for Federal credit programs on February 11, 1963. However, we have not located therein the specific "guidelines" to which it was intended that reference should be made. The intent may be that a Federal intermediate credit bank with Government capital should compute its franchise tax to yield a more equitable rate to the Treasury. The present standard for computing the franchise tax is found in step (4) of the section which directs how each Federal intermediate credit bank shall apply its net earnings at the end of the fiscal year (12 U.S.C. 1072(a)):

"(4) if said bank shall have outstanding capital stock held by the United States during the whole or any part of its fiscal year, it shall next pay to the United States as a franchise tax, a sum equal to 25 per centum of its earnings then remaining, not exceeding, however, a rate of return on such Government capital calculated at a rate equal to the computed average annual rate of interest on all public issues of public debt obligations of the United States issued during the fiscal year of the United States Treasury ending next before such tax is due, as certified to the Farm Credit Administration by the Secretary of the Treasury."

The foregoing formula was prescribed by Congress in 1956 and, as then intended, we think this provision should be permitted to run its course which is until the Government capital is retired from a bank. In any event we see no relationship

between increasing the franchise tax payable by a Federal intermediate credit bank which has Government capital and the provisions recommended by the Farm Credit Administration that are now included in H.R. 4152.

"We also believe that, in line with general tax policy, patronage refunds received by the PCA's from FICB's in which the Government owns stock should be made taxable."

Under amendments made by the Farm Credit Act of 1956, the operation of the Federal intermediate credit banks was changed toward a cooperative basis. The amended law specified how the net earnings of a Federal intermediate credit bank were to be applied at the end of each fiscal year. After meeting all other requirements, any remaining net earnings are required to be distributed as patronage refunds. Whenever the United States holds capital stock in a bank, the patronage refunds for that year must be paid in class B stock to production credit associations and in participation certificates to other financing institutions borrowing from or rediscounting with the bank during the fiscal year for which such refunds are declared. Congress then made the further specific provision, "The recipients of such patronage refunds shall not be subject to Federal income taxes thereon" (12 U.S.C. 1072).

One reason for the quoted provision is that for Federal income tax purposes there would always be the question of assigning any present market value to "paper" refunds of this type. In any event, Congress enacted this provision in 1956 with the intention that it should continue in effect until Government capital was retired from a Federal intermediate credit bank. To the extent that the present bill would make this same sentence applicable to allocations of earnings retained in the reserve account of a bank, we think it is not only appropriate but indicated that such account allocations should have the same tax treatment as patronage refunds that are paid in capital stock and participation certificates.

"Finally, we believe that there should be provision for the elimination upon retirement of Government stock, of existing tax exemptions afforded the FICB's."

The proposals now embodied in H.R. 4152 were made in furtherance of general policy declared in the Farm Credit Acts of 1953 and 1956 for the Federal intermediate credit banks and the production credit associations. Any suggestion that the existing tax exemptions of the Federal intermediate credit banks should be eliminated upon retirement of Government capital stock is not relevant to the provisions of H.R. 4152 or the objective or purpose it is intended to serve. We, therefore, think that H.R. 4152 should not be held up by any such suggestion which necessarily is to serve a different interest.

What we have been trying to say is that, although we recognize the reasons for the objections raised by the Bureau of the Budget, we do not believe that they are sufficiently important or sufficiently germane to require the attention of this committee to the point that the proposed legislation should be amended to care for these objections. In fact, we believe that much of the useful purpose of this legislation would be destroyed if this was done; therefore, we urge the committee to approve the legislation as it is written and submit it to the Congress which we sincerely hope will also approve the proposal.

I would note in conclusion that every prediction which is available to us indicates that the demand for credit by American farmers is going to continue and increase during the present year. And therefore, we believe that the suggestions which are made in these legislative proposals should be enacted into law with the greatest dispatch that is consistent with the proper hearing and discussion techniques so profitably employed by the Congress.

Meanwhile, necessity is laid upon us all to revise and improve our farm programs and farm income so that the shadow of increasing farm indebtedness can be made to disappear in the bright sunshine of adequate farm income.

Mr. GATHINGS. Mr. Graham, these figures are amazing to me, and I wondered, did your research people on your staff compile these?

Mr. GRAHAM. We took them from available—

Mr. GATHINGS. Where did they take them from?

Mr. GRAHAM. We took them from the material we got from the Farm Credit Branch of the Economic Research Service of the Department of Agriculture. These figures are available for anybody. We just dug them out.

Mr. GATHINGS. They are authentic?

Mr. GRAHAM. They are authentic. They are the figures I received yesterday. I presume they are still good today. Yes, they are authentic figures from the Department of Agriculture.

Mr. GATHINGS. Thank you.

Mr. POAGE. Thank you, Mr. Graham.

We will now hear from Mr. Reuben Johnson.

Mr. BRUCE. I think he stated earlier that he would put his statement in the record.

Mr. POAGE. Without objection, his statement will be included at this point in the record.

(The statement of Mr. Johnson follows:)

STATEMENT OF NATIONAL FARMERS UNION BY REUBEN L. JOHNSON, DIRECTOR
OF LEGISLATIVE SERVICES

Mr. Chairman and members of the subcommittee, I am Reuben L. Johnson, director of legislative services, National Farmers Union. I appear today here in behalf of Mr. James G. Patton, president, National Farmers Union, and the 700,000 members of National Farmers Union.

Farmers Union supports this bill under consideration by the subcommittee.

The following brief comments will further explain the views of our organization.

H.R. 4152

On behalf of our members who are able to qualify for loans through production credit associations and Federal intermediate credit banks, we support this bill. The bill has the strong endorsement of the Board of Directors of the Farmers Credit Administration. Further, we understand the bill is fully consistent with the policies established in the Farm Credit Acts of 1953 and 1956.

In expanding our comments, Mr. Chairman, we would like to refer to a letter from the Budget Bureau to the Governor of the Farm Credit Administration dated December 1, 1964.

In the last paragraph of the Budget Bureau letter, reference is made to the allocation of the earnings of Federal intermediate credit bank as adversely affecting the Government's interest and unnecessary to the basic objective of the bill. As we understand the matter, these earnings now applied to the reserve account of Federal intermediate credit banks are not allocated. It is difficult to see how allocations of such earnings would adversely affect the interest of the Government and we hope that Congress will make no change in the proposed method of allocation.

The last paragraph of the letter relates also to the computation of franchise tax paid by a Federal intermediate credit bank each year that Government capital is used. The present formula for the computation of this tax was specified when Congress enacted the Farm Credit Act of 1956. We see no need or justification for any change in the procedure spelled out in earlier legislation.

Also called for in the Budget Bureau letter is a change in the tax policy whereby patronage refunds received by production credit associations from the Federal intermediate credit banks in which the Government owns stock would be made taxable. The changes called for in the computation of the franchise tax and for the taxation of patronage refunds have no further effect or use when Government capital has been repaid. Therefore, we do not understand why the current legislative proposal which would encourage repayment of Government capital should be made the occasion for changing the direction given by Congress in 1956 to lending activities of these credit institutions.

The last change called for in the Budget Bureau letter is elimination upon retirement of Government stock of the tax exempt status of the Federal intermediate credit banks. We would further point out that we see no relationship of such change to the purpose of the proposed legislation and we urge the subcommittee not to alter the existing provision of the Farm Credit Act of 1956.

We appreciate very much the opportunity to appear before the subcommittee in behalf of these bills.

FARM CREDIT

TABLE A.—*Changes in farm debt*

Year	Farm mortgage debt	1950-62 non-real-estate debt ¹	All debt ¹	Production assets
1950.....	100	100	100	100
1962.....	249	222	362	277

¹ Excludes CCC loans.

TABLE B

[In millions of dollars]

Year	Non-real-estate debt (excluding CCC loans)			Earlier estimates of non-real-estate debt held by non-reporting creditors
	Total (revised)	Held by reporting institutions ¹	Held by non-reporting creditors (revised) ²	
1950.....	4,930	2,710	2,220	2,200
1958.....	8,814	4,994	3,820	3,500
1964.....	16,185	9,465	6,720	4,500

¹ All operating banks, production credit associations, Farmers Home Administration, and Federal intermediate credit banks.

² Merchants and dealers, consumer and sales finance companies, various other nonreporting lending institutions, individuals, and miscellaneous creditors.

Mr. POAGE. We have Mr. Lynn representing the American Farm Bureau of Federation. I believe he sent someone else.

Mr. NAY. Mr. Lynn stepped out.

Mr. POAGE. We will be glad to hear from you.

STATEMENT OF PAUL NAY, PRESIDENT, WEST VIRGINIA FARM BUREAU

Mr. NAY. Mr. Chairman, and gentlemen, I am Paul Nay, president of the West Virginia Farm Bureau. I am a dairy farmer from West Virginia. I have used farm credit system loans in my own farming operation for 25 years. I have been a member or a director of Clarksburg, W. Va., farm credit office at that office for close to 20 years.

Most of the statement that I have prepared has been covered thoroughly by Chairman Stone, Governor Tootell, and some of the others who have already appeared. So, Mr. Chairman, with your permission, I would like to file the statement.

Mr. POAGE. Without objection it will be included in the record.

Mr. NAY. And confine my remarks to the Farm Bureau's support of H.R. 4152.

The American Farm Bureau Federation represents 1,647,455 paid-up member families in 49 States and Puerto Rico. The membership includes farmers and ranchers from every part of the country who produce every kind of agricultural commodity, and who use the farm credit system.

Now, if you are following my statement, I would refer you to page 3.

Farm Bureau has supported the farm credit system. At our most recent annual meeting a policy dealing directly with the issue before this subcommittee was adopted as follows:

We recognize the value of the enactment during recent years of a series of laws, beginning with the Farm Credit Act of 1953, to provide for an independent bipartisan Farm Credit Board, retirement of Government capital, preservation of revolving funds, and decentralization of authority to increase ownership and control of farm credit institutions by farmers and ranchers. We support the continuation and development of these principles. We oppose efforts to establish Federal budgetary control over farm credit institutions or the surpluses existing therein.

Now, gentlemen, we recognize that all H.R. 4152 is designed to enable the Federal intermediate credit banks on the production credit associations to serve and expand needs of farmers and ranchers better—to serve the expanded needs of farmers and ranchers; to reduce or eliminate the need for additional Government capital and to retire the Federal capital now in the system at an increasing annual rate.

This is to be accomplished by increasing the debt-to-capital ratio permitted by the Federal intermediate credit banks from 10 to 1 to 15 to 1.

The effect of this amendment would be to allow the banks to have outstanding obligations for their benefit and account equal to 15 times their paid-in capital and surplus. The current limit is 10 to 1.

Also we recognize the bill provides for mandatory retirement of the Government capital now in the banks. It provides further for additional purchase of class B stock in the Federal intermediate credit banks by the production credit associations.

We believe the proposed amendments would strengthen the system by providing more adequate credit for modern-day farm needs and, at the same time, speed up the retirement of Government capital, thus hastening the day when the farm credit system will be wholly owned by farmers.

We, therefore, recommend favorable consideration of H.R. 4152. Thank you, gentlemen.

(The prepared statement of Mr. Nay follows:)

STATEMENT OF THE AMERICAN FARM BUREAU FEDERATION BY PAUL NAY,
PRESIDENT, WEST VIRGINIA FARM BUREAU

The American Farm Bureau Federation represents 1,647,455 paid-up member families in 49 States and Puerto Rico. The membership includes farmers and ranchers from every part of the country who produce every kind of agricultural commodity, and who use the farm credit system.

H.R. 4152 would amend the Federal Farm Loan Act and the Farm Credit Act of 1933 to provide means for expediting the retirement of Government capital in the Federal intermediate credit banks. It would authorize an increase in the debt permitted such banks in relation to their capital, and also provide for production credit associations to acquire additional capital stock in the banks.

There is a Federal intermediate credit bank in each of the 12 farm credit districts. These banks make funds available to production credit associations and other eligible financing institutions by discounting agricultural paper. Throughout the country there are some 483 production credit associations with the number varying from 26 to 77 in the 12 farm credit districts. These associations are chartered by the Farm Credit Administration and operate under the provisions of the Farm Credit Act of 1933, as amended.

From 1923 through 1956 the Federal intermediate credit banks were wholly owned by the United States. Beginning in 1957, under amendments made by the Farm Credit Act of 1956, the capital stock of the banks was divided into

class A stock, issued to and held only by the Governor of the Farm Credit Administration on behalf of the United States, and class B stock, issued only to production credit associations. At the same time the plan for FICB operations was changed to a cooperative basis. Under the 1956 act, as long as there is Government capital in a Federal intermediate credit bank, net earnings each year after restoring any impairments of capital stock, participation certificates, and surplus must be applied as follows:

(1) Twenty-five percent goes to a reserve account until it reaches a specified level.

(2) Up to 25 percent of what then remains, but not more than the Treasury cost of the Government capital in the bank, is next paid to the United States as a franchise tax.

(3) Dividends of not to exceed 5 percent may then be paid on outstanding class B stock and participation certificates.

(4) The remaining net earnings are distributed as patronage refunds by issuing class B stock to production credit associations and participation certificates to other financing institutions.

Under the 1956 amendments, it was expected that the capital stock of the Federal intermediate credit banks held by the United States gradually would be retired and that eventually all of the capital stock of such banks would be owned by production credit associations. However, under the existing law the banks have not been making the progress in retiring Government capital that was expected when the 1956 amendments were adopted.

Although the 12 banks added \$67.1 million to net worth out of earnings during the 7½-year period from January 1, 1957, through June 30, 1964, growth in loan volume made it necessary for some of the banks to obtain additional Government capital out of the revolving fund available for that purpose in order to stay within the statutory 10-to-1 debt-to-capital ratio. As a result the banks now have nearly \$33.2 million more Government capital than on January 1, 1957.

Farm Bureau has supported the farm credit system. At our most recent annual meeting a policy dealing directly with the issue before this subcommittee was adopted as follows:

"We recognize the value of the enactment during recent years of a series of laws, beginning with the Farm Credit Act of 1953, to provide for an independent bipartisan Farm Credit Board, retirement of Government capital, preservation of revolving funds, and decentralization of authority to increase ownership and control of farm credit institutions by farmers and ranchers. We support the continuation and development of these principles. We oppose efforts to establish Federal budgetary control over farm credit institutions or the surpluses existing therein."

H. R. 4152 is designed to enable the Federal intermediate credit banks and the production credit associations to serve the expanded needs of farmers and ranchers better, to reduce or eliminate the need for additional Government capital, and to retire the Federal capital now in the system at an increasing annual rate. This is to be accomplished by increasing the debt-to-capital ratio permitted the Federal intermediate credit banks from 10 to 1 to 15 to 1. The effect of this amendment would be to allow the banks to have outstanding obligations for their benefit and account equal to 15 times their paid-in capital and surplus. The current limit is 10 to 1.

The bill also provides for mandatory retirement of the Government capital now in the banks. It further provides for additional purchases of class B stock in the Federal intermediate credit banks by the production credit associations. We believe that the proposed amendments would strengthen the system by providing more adequate credit for modern-day farm needs and, at the same time, speed up the retirement of Government capital thus hastening the day when the farm credit system will be wholly owned by farmers.

We, therefore, recommend favorable consideration of H. R. 4152.

Mr. POAGE. Thank you very much, Mr. Nay. Any questions? If not, we are much obliged to you.

Now we have a request from Mr. Richard T. O'Connell for permission to file a statement, and without objection that request will be granted.

(The prepared statement of Mr. O'Connell referred to follows:)

NATIONAL COUNCIL OF FARMER COOPERATIVES,
Washington, D.C., February 17, 1965.

Hon. W. R. POAGE,
Chairman, Special Subcommittee on Conservation and Credit,
House of Representatives, Washington, D.C.

DEAR MR. POAGE: This letter is to indicate our support of H.R. 4152. We support the bill in its entirety for the following reasons:

(1) The change of the ratio of the lending limits from 10 times the surplus and paid-in capital of all the banks to 15 to 1 will expedite the retirement of Government capital; will reduce the input of money from the revolving fund, while continually providing expanding credit needs for farmers.

(2) Of significance is the fact that the production credit associations will be required to purchase additional capital stock in the Federal intermediate credit banks.

It has been the position of the National Council of Farmer Cooperatives to continually support progressive development of the farm credit system and we believe the amendment to the Farm Credit Act of 1933, as written in H.R. 4152, will continue to meet the goals of agriculture by providing a viable and useful farm credit system.

We urge the passage of this measure and its adoption into law. I would appreciate your making this a part of the record for H.R. 4152.

Thank you.

Sincerely,

RICHARD T. O'CONNELL, *Secretary.*

Mr. POAGE. Is there anyone else who would like to be heard on this bill? If not, that will conclude the hearings.

The committee will meet in executive session at 3 o'clock this afternoon.

(Whereupon, at 12:20 p.m., the subcommittee was adjourned, to reconvene subject to call of the Chair.)



