

9874
Ag 8/1
C 86/11

IMPROVE CAPITALIZATION OF FEDERAL INTERMEDIATE CREDIT BANKS AND PRODUCTION CREDIT ASSOCIATIONS

Y4
.Ag 8/1
C 86/11

GOVERNMENT
Storage

HEARING BEFORE THE COMMITTEE ON AGRICULTURE HOUSE OF REPRESENTATIVES NINETIETH CONGRESS

SECOND SESSION

ON

H.R. 16674

APRIL 29, 1968

Serial UU

Printed for the use of the Committee on Agriculture

KSU LIBRARIES



TOHEEE 00PTTV



AY
A.A.
1/8
11/28/11

HEARING

REPORT

COMMITTEE ON AGRICULTURE

W. R. POAGE, Texas, *Chairman*

E. C. GATHINGS, Arkansas,
Vice Chairman
JOHN L. McMILLAN, South Carolina
THOMAS G. ABERNETHY, Mississippi
WATKINS M. ABBITT, Virginia
PAUL C. JONES, Missouri
FRANK A. STUBBLEFIELD, Kentucky
GRAHAM PURCELL, Texas
MASTON O'NEAL, Georgia
THOMAS S. FOLEY, Washington
JOSEPH Y. RESNICK, New York
ELIGIO DE LA GARZA, Texas
JOSEPH P. VIGORITO, Pennsylvania
WALTER B. JONES, North Carolina
JOHN G. DOW, New York
BILL NICHOLS, Alabama
G. V. MONTGOMERY, Mississippi
FRANK J. BRASCO, New York
JOHN R. RARICK, Louisiana

PAGE BELCHER, Oklahoma,
Ranking Minority Member
CHARLES M. TEAGUE, California
CATHERINE MAY, Washington
ROBERT DOLE, Kansas
GEORGE V. HANSEN, Idaho
WILLIAM C. WAMPLER, Virginia
GEORGE A. GOODLING, Pennsylvania
CLARENCE E. MILLER, Ohio
J. HERBERT BURKE, Florida
ROBERT B. MATHIAS, California
WILEY MAYNE, Iowa
JOHN M. ZWACH, Minnesota
THOMAS S. KLEPPE, North Dakota
ROBERT PRICE, Texas
JOHN T. MYERS, Indiana

RESIDENT COMMISSIONER

SANTIAGO POLANCO-ABREU, Puerto Rico

CHRISTINE S. GALLAGHER, *Clerk*
WILLIAM C. BLACK, *General Counsel*
HYDE H. MURRAY, *Assistant Counsel*
L. T. EASLEY, *Staff Consultant*

CONTENTS

H.R. 16674, a bill to amend the Federal Farm Loan Act and the Farm Credit Act of 1933, as amended, to improve the capitalization of Federal intermediate credit banks and production credit associations, and for other purposes-----	Page 1
Statement of:	
Bement, Benjamin F., Jr., Dowagiac, Mich-----	35
Bice, Lorin T., Chairman, Federal Farm Credit Board-----	2
Boddy, H. M., Chairman, National Advisory Committee of Production Credit Associations-----	9
Curtiss, Homer, Stockton, Ill-----	27
Enns, Paul I., chairman, Berkeley District Farm Credit Board-----	22
FunderBurk, C. B., representing the Third Farm Credit District-----	29
Hague, Lyle L., Cherokee, Okla-----	38
Haynes, Kit H., assistant legislative director, American Farm Bureau Federation-----	46
Hendry, James, Lost Cabin, Wyo-----	37
Hoffpauir, George E., Morse, La-----	33
Lage, E. Riddell, chairman, Farm Credit Board of Spokane-----	40
Nay Paul, Jane Lew, W. Va-----	25
Nelson, J. Richards, Madison, Conn-----	28
Newsom, Herschel D., master, National Grange-----	43
Schroeder, Guido, West Bend, Wis-----	36
Studebaker, Samuel S., Tipp City, Ohio-----	32
Thompson, Charles C., chairman, board of directors, Farm Credit Banks of Houston-----	18
Tootell, Hon. R. B., Governor, Farm Credit Administration-----	5
Correspondence submitted to the committee:	
McNeill, Charles R., director, Washington Office, American Bankers Association, letter of April 29, 1968-----	48
Norton, E. M., secretary, National Milk Producers Federation, letter of April 29, 1968-----	47
O'Connell, Richard T., secretary, National Council of Farmer Cooperatives, letter of April 29, 1968-----	42

IMPROVE THE CAPITALIZATION OF FEDERAL INTER-MEDIATE CREDIT BANKS AND PRODUCTION CREDIT ASSOCIATIONS

MONDAY, APRIL 29, 1968

HOUSE OF REPRESENTATIVES,
COMMITTEE ON AGRICULTURE,
Washington, D.C.

The committee met, pursuant to notice, at 10 a.m., in room 1301, Longworth House Office Building, Hon. W. R. Poage (chairman) presiding.

Present: Representatives Poage, Gathings, McMillan, O'Neal, de la Garza, Montgomery, Belcher, Teague, Mrs. May, Goodling, Miller, Mathias, Mayne, Zwach, Kleppe, Price, and Myers.

Also present: Christine S. Gallagher, clerk; William C. Black, general counsel; Hyde H. Murray, assistant counsel; L. T. Easley, staff consultant, and Fowler C. West, assistant staff consultant.

The CHAIRMAN. The committee will please come to order.

We are met this morning to consider certain amendments to the Federal Farm Loan Act and the Farm Credit Act of 1933, as amended, to improve the capitalization of Federal intermediate credit banks and production credit associations, and for other purposes.

(H.R. 16674 by Mr. Poage follows:)

[H.R. 16674, 90th Cong., second sess.]

A BILL To amend the Federal Farm Loan Act and the Farm Credit Act of 1933, as amended, to improve the capitalization of Federal intermediate credit banks and production credit associations, 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 substituting “twenty” for “twelve” in section 203(a) thereof (12 U.S.C. 1041);

(b) by changing the heading over section 205 thereof (12 U.S.C. 1061) to read “CAPITAL STOCK AND PARTICIPATION CERTIFICATES” instead of “CAPITAL STOCK” and by adding the following new subsection (c) at the end of section 205 thereof (12 U.S.C. 1061):

“(c) PARTICIPATION CERTIFICATES IN ADDITION TO THOSE ISSUED IN PAYMENT OF PATRONAGE REFUNDS.—In addition to the participation certificates issued in payment of patronage refunds, each Federal intermediate credit bank may issue further amounts of such participation certificates, with the same rights, privileges, and conditions, for purchase by institutions other than production credit associations that are entitled to receive participation certificates from the bank in payment of patronage refunds.”; and

(c) by inserting the following new paragraph between the present second and third paragraphs of subsection (a) of section 206 thereof (12 U.S.C. 1072(a)):

“If and when the relative amounts of class B stock in a Federal intermediate credit bank owned by the production credit associations are adjusted to re-establish the proportion of such class B stock owned by each association, as

provided in the second or third paragraphs of section 205(a)(2) of this Act (12 U.S.C. 1061(a)(2)), amounts in the reserve account that are allocated to production credit associations may be adjusted in the same manner, as far as practicable, to reestablish the holdings of the production credit associations in the allocated legal reserve accounts into substantially the same proportion as are their holdings of class B stock."

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

(a) by inserting "or otherwise, except as may be authorized under rules and regulations prescribed or approved by the Farm Credit Administration," immediately after the word "loan" in the last sentence of the first paragraph of section 23 thereof (12 U.S.C. 1131g); and

(b) by adding the following at the end of section 24 thereof (12 U.S.C. 1131h): "Subject to rules and regulations prescribed by the Farm Credit Administration, a production credit association may issue its capital notes for sale to borrowers and others, but the principal amount of such capital notes outstanding at any one time, together with other liabilities of the association, may not exceed ten times the paid-in and unimpaired capital and surplus of such association."

The CHAIRMAN. We have with us Mr. Bice, Chairman, Federal Farm Credit Board, and Governor Tootell, Governor, Farm Credit Administration; accompanied by Mr. F. Vernon Wright, Deputy Governor, and Director, Short-Term Credit Service; and Paul O. Ritter, General Counsel, Farm Credit Administration.

I understand that they will wish to appear at the table together. Is that the way they wish to do it? If so, we will be glad for them to do so.

We will be glad to hear you now, Mr. Bice. We will be glad to have you start this discussion.

STATEMENT OF LORIN T. BICE, CHAIRMAN, FEDERAL FARM CREDIT BOARD

Mr. BICE. Mr. Chairman and gentlemen of the committee, my name is Lorin T. Bice and I am appearing here today as chairman of the Federal Farm Credit Board in support of H.R. 16674 which is recommended by the Farm Credit Administration for enactment by Congress. The general purpose of the bill is to improve the capitalization of the Federal intermediate credit banks and production credit associations and also otherwise enhance their capacity to continue to meet the increasing credit needs of farmers and ranchers while at the same time retiring the remaining Government capital from the banks within a reasonable period.

The Farm Credit Administration is the agency of the Federal Government which has the supervision of the Federal intermediate credit banks and production credit associations whose capitalization and ability to serve their function would be improved by the bill. Also subject to supervision by the Farm Credit Administration are the Federal land banks and Federal land bank associations, and the banks for co-operatives, but the present bill does not concern them.

Originally established in 1933, the Farm Credit Administration itself, as reconstituted in 1953, now consists of the Federal Farm Credit Board, a chief executive officer, who is known as Governor of the Farm Credit Administration, and other necessary personnel. Under its Governor, R. B. Tootell, the official of the Farm Credit Administration most directly concerned with the Federal intermediate credit banks and production credit associations is the Deputy Governor and director of Short-Term Credit Service, F. Vernon Wright.

The Federal Farm Credit Board, established in 1953, has 13 members, one appointed by the President with Senate consent from each of the 12 farm credit districts, and a 13th member appointed by the Secretary of Agriculture. The Board meets six or more times a year to determine major policy for the Farm Credit Administration. A continuing function and duty of the Federal Farm Credit Board is to make recommendations to Congress for amendments to the laws relative to agricultural credit administered by the Farm Credit Administration.

Before undertaking to present some background information about the Federal intermediate credit banks and production credit associations, which may be helpful in your consideration of the bill now being recommended, I would like to offer some personal information about myself.

My own farming is producing and marketing citrus. My son is associated with me in operating family citrus groves in Florida. For many years I have been a member of the Florida Citrus Production Credit Association and the Federal Land Bank Association of Lakeland, and have had considerable experience on the boards of these local associations. I was a member of the Farm Credit Board of Columbia in the third farm credit district, which includes North and South Carolina, Georgia, and Florida, from 1956 until 1963 when I was appointed to the Federal Farm Credit Board for a 6-year term ending in 1969. For my last year on the Federal Board I am serving as Chairman.

The Federal intermediate credit banks, one in each of the 12 farm credit districts into which the 50 States and Puerto Rico are divided, were established in 1923. 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. Their primary function is to discount for, or purchase from, production credit associations and other financing institutions, with their indorsement, notes representing loans made by them to farmers and ranchers; and to make loans and advances to such associations and other financing institutions to enable them to make or carry loans for any agricultural purpose. Loans made to farmers or ranchers may be used as collateral for loans and advances from the credit banks. There now are about 118 other financing institutions being served by the Federal intermediate credit banks but approximately 95 percent of the discounting and lending by such banks is for production credit associations.

The Federal intermediate credit banks obtain funds for such discounting and lending by selling their consolidated debentures in the public securities market. These debentures, for which loans made to farmers or ranchers are pledged as collateral, are the joint and several obligations of the 12 credit banks and are not obligations of the United States. During the fiscal year ending June 30, 1967, \$4.2 billion of such debentures were issued and the total amount outstanding at the end of the year was \$3.3 billion.

Throughout the country there are 459 production credit associations, with the number in the 12 farm credit districts varying from 22 to 65. The associations are chartered by the Farm Credit Administration and operate under the provisions of the Farm Credit Act of 1933, as amended. Each association has a prescribed territory, within which

it makes loans to farmers and ranchers. Loan maturities usually are not more than one year but loans may be made for terms up to seven years. During fiscal 1967, the volume of this lending, with loan funds furnished by the Federal intermediate credit bank in each of the 12 districts totaled \$5.1 billion. Out of a total membership of 548,279 at the end of that year, there were 322,700 borrowing members of the associations with \$3.7 billion of loans outstanding.

From their beginning in 1923, all of the capital stock of the 12 Federal intermediate credit banks was owned by the United States and it was not until 1956 that provision was made for the Government capital to be supplanted by private capital. During 1957 and 1958, as required by the Farm Credit Act of 1956, the production credit associations purchased 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 \$454,000 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. In 1965, there was further legislation which authorized each Federal intermediate credit bank, with the approval of the Farm Credit Administration, to require the production credit associations in its district to purchase additional capital stock in the bank in order to meet its credit needs. A number of the banks are now preparing to do this. 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 \$51,950,000 of additional capital stock in eight of the banks in order to meet their credit needs. On the whole, therefore, the amount of Government capital put into the banks since 1956 is almost four times the amount that has been retired. Since the legal debt-to-capital ratio of the banks was increased to a maximum of 12 to 1 in 1965, though, there has been no change in the Government capital in the banks and the amount has remained at \$125,789,120.

Since 1953 it has been the declared policy of Congress that the Government capital in the Federal intermediate credit banks eventually should be supplanted by capital provided by borrowers from the banks. The amendments enacted in 1956 and 1965 were intended to facilitate this. However, experience has shown, as Governor Tootell will explain later, that we will need the further amendments now being recommended if the banks are to return their Government capital within a reasonable period and at the same time continue to serve the increasing needs for agricultural credit.

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. To indicate their support, a director from each

of the districts is present and available to testify if time permits. A subsequent witness is also expected to endorse the legislation on behalf of the National Advisory Committee of Production Credit Associations, of which he is chairman.

And now I would like to defer to Governor Tootell who is standing by to undertake a more detailed explanation of our proposals.

The CHAIRMAN. Thank you, Mr. Bice.

We will be glad to now have the presentation by Governor Tootell.

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. Mr. Chairman and gentlemen of the committee.

Against the background just provided by the chairman of the Federal Farm Credit Board, I would like to describe in detail the amendments to our existing laws which would be made by H.R. 16674, and the reasons why we are recommending them. There are five amendments, three of which will be discussed as Federal intermediate credit bank amendments and two as production credit association amendments. I will take them up in the order in which they appear in the bill.

FEDERAL INTERMEDIATE CREDIT BANK AMENDMENTS

Section 1(a). As has already been mentioned, the 12 Federal intermediate credit banks sell their consolidated collateral trust debentures in the public securities market in order to obtain funds with which to finance production credit associations and other institutions in making loans to farmers and ranchers. Under existing law (12 U.S.C. 1041 (supp. II, 1967)), there is a limitation "That the aggregate amount of the outstanding debentures and similar obligations issued by the Federal intermediate credit banks shall not exceed 12 times the surplus and paid-in capital of all such banks." The proposed amendment is to substitute "twenty" for "twelve" in this limitation so that the permissible debt-to-capital ratio would be 20 to 1 instead of 12 to 1. This would permit up to \$20,000 of debentures, secured by a like amount of collateral, to be issued for each \$1,000 of surplus and paid-in capital of the banks. Differently stated, as of June 30, 1967, the 20-to-1 ratio would have permitted \$6.2 billion of debentures and similar obligations to be outstanding instead of \$3.7 billion under the present 12 to 1 ratio. The present limitation (12 to 1) is unnecessarily conservative and too restrictive if the credit banks are to continue to meet the increasing demands for agricultural financing without calling on the Government for more capital and while returning within a reasonable time the Government capital they now have.

When the debt-to-capital ratio of the credit banks is close to 12 to 1, and loans and discounts are increasing rapidly, the banks can continue to operate within that ratio only if additional capital is paid in. The ratio as of June 30, 1967, was 11.35 to 1, but this was reduced to 10.78 to 1, after earnings for the year were distributed. Based on the latest available estimates, the ratio will closely approach the present 12 to 1 legal maximum in May or June 1968.

It is estimated that total loans and discounts outstanding at June 30, 1968, in the 12 Federal intermediate credit banks will be \$4,050 million. Ten years ago the amount at the same month-end was \$1,547 million. The estimated increase this June 30, over June 30, 1959, is 230 percent. Growth in outstandings over the previous year with 1968 estimated, was 14.1 percent in 1966, 15.6 percent in 1967, and 14.3 percent in 1968.

We see no evidence of any leveling off in the volume of loans and discounts of the credit banks. Some projections estimate the nonreal estate debt of farmers and ranchers in 1980 at \$40 billion. The share of this market to be handled by the Federal intermediate credit banks we estimate at from 20 to 25 percent.

At June 30, 1959, the total net worth of the 12 Federal intermediate credit banks was \$173,413,000. At June 30, 1968, it is estimated this amount will be \$334,893,000, or an increase of about 117 percent. Thus, over the 10-year period, growth in net worth percentagewise has been about half the rate of the increase in loans and discounts outstanding.

The net worth of the credit banks is made up of Government-owned capital stock, \$125,789,120, and net worth generated from earnings and stock purchases, estimated to be \$209,104,000 at June 30, 1968. Additions to net worth from earnings after payment of franchise taxes for the 10 years ending June 30, 1968, is estimated at \$129,143,000. While these earnings are substantial they have not been commensurate with growth in business. Consequently, it is estimated that the debt-to-capital ratio of the credit bank system would be 11.9 to 1 prior to the close of business on June 30, 1968.

If more capital must be put into the credit banks in order to permit increased lending under the present 12 to 1 limitation, there now are two general sources for such additional capital.

First, out of a revolving fund available for that purpose in the Treasury of the United States, the Governor of the Farm Credit Administration may subscribe to capital stock of the banks in such amount as he determines is needed to meet the credit needs of a bank or banks (U.S.C. 1061(a)(1)).

Second, each Federal intermediate credit bank, with the approval of the Farm Credit Administration, may also require the production credit associations in its district to purchase capital stock of the bank in order to provide capital to meet the credit needs of the bank (12 U.S.C. 1061(a)(2) (supp. II, 1967)). It would be contrary to the programs now being developed by the banks for the return of their Government capital within a reasonable time, if more Government capital were put into the banks in order to meet increasing credit needs under the 12 to 1 debt-to-capital limitation. As part of their Government capital retirement programs, the banks do expect to call on the production credit associations to purchase additional capital stock of the banks. However, it is not deemed feasible for the associations to do this in an amount that would both permit the return of Government capital and support increasing credit needs under the 12 to 1 debt-to-capital limitation now applicable. This is why it is proposed that the debt-to-capital limitation be changed to 20 to 1.

Such a change is necessary if the Federal intermediate credit banks are to continue to meet the increasing credit needs they are intended to serve, while at the same time returning Government capital, and looking to the associations, within their capacity, to provide additional

capital instead of calling for more Government capital. It is not only deemed necessary but is also deemed amply justified by the financial strength of the credit banks, supporting which, as hereafter explained, there is also the financial strength of the associations.

Before a Federal intermediate credit bank could suffer any loss on its financing of the production credit associations in its district, which represents about 95 percent of its financing, it would be necessary that one or more of the associations become insolvent. However, this is well guarded against because the liabilities of each association, including its liability to the credit bank, may not exceed 10 times the paid-in and unimpaired capital and surplus of the association (12 U.S.C. 1032). Overall the associations are currently operating within about a 7-to-1 debt-to-capital limitation. Their losses in the 33 years of their existence since 1933 have amounted to only eight-hundredths of 1 percent of the total cash advanced to farmers and ranchers. This has not resulted in any loss to the credit banks, which have sustained no losses on any of their loans or discounts made since 1933, when the associations came into being. Taking into account losses suffered from their organization in 1923, the net losses of the credit banks in 44 years of operation have amounted to approximately \$1 for each \$9,000 of credit extended.

Today the likelihood of losses by the credit banks on their loans and discounts for the associations is even further reduced. As a protection for their capital and surplus, the associations have accumulated reserves for losses totaling \$99.9 million, or 2.7 percent of total loans outstanding on December 31, 1967. Further, the associations in the different districts, within the past few years, have adopted either loss-sharing agreements, participation loan agreements, or guarantee plans, or combinations of these, in connection with their loans. While these agreements for the different districts are in varying terms, the general effect is that certain losses by one association would be made up by contributions from the other associations. In this manner, the collective financial strength of the associations in a district serves to insulate the credit bank from losses on its loans or discounts for the associations. The debentures issued by the Federal intermediate credit banks, therefore, are not only supported by a like amount of farmers' notes and the financial strength of the banks themselves, but also, to a considerable extent, by the financial strength of the associations. With due recognition of this, there is considered to be ample justification for the proposed amendment so far as concerns the financial stability of the Federal intermediate credit banks and the debentures issued by them.

While the major proposal in the bill is to increase the permissible debt-to-capital ratio of the Federal intermediate credit banks from 12-to-1 to 20-to-1, there also are amendments which would enlarge the amount of capital for the credit banks obtainable from other sources than the Government; that is, from production credit associations and other institutions that are financed by the credit banks.

Section 1(b). The capital of the Federal intermediate credit banks, against which their debt-to-capital ratio must be applied, includes not only the capital stock of the banks, which is held by the United States and production credit associations, but also participation certificates, which are held by financing institutions other than production credit associations that use the services of the credit banks. Under existing

law (12 U.S.C. 1072(b)), these participation certificates are issued by the banks to such other financing institutions only in payment of patronage refunds that are distributed annually by each bank; and there is no provision for issuing additional amounts of participation certificates. In the case of production credit associations, patronage refunds are paid in capital stock and such associations have in the past been required and may again be required to purchase additional capital stock in the bank. The present amendment would authorize a Federal intermediate credit bank to issue participation certificates, in addition to those issued in payment of patronage refunds, for purchase by financing institutions that are entitled to receive participation certificates in payment of patronage refunds.

Section 1(c). At the end of its fiscal year, each Federal intermediate credit bank is required to apply its net earnings as specified in the law (12 U.S.C. 1072(a) (supp. II, 1967)). Some of such net earnings are retained in a reserve account where they are allocated on a patronage basis to the production credit associations and other financing institutions that borrow from or rediscount with the bank. The remainder of such net earnings, which are not applied otherwise, are distributed as patronage refunds to production credit associations in the form of class B stock and to other financing institutions in the form of participation certificates. Over the years a production credit association thus acquires interests in a Federal intermediate credit bank; that is, allocations of surplus account and class B stock which are in proportion to the business done by the association with the bank during each year. The thought has been that the interests in a Federal intermediate credit bank owned by a production credit association occasionally should be brought into proportion with its current use of the bank.

Under a 1965 amendment (12 U.S.C. 1061(a) (supp. II, 1967)), the relative amounts of class B stock in a Federal intermediate credit bank owned by production credit associations may be adjusted to reestablish the amount of such class B stock owned by each association in proportion to the average indebtedness (loans and discounts) of each association to the bank during the immediately preceding 3 fiscal years. If and when this is done, the present amendment would authorize amounts in the reserve account that are allocated to production credit associations to be reestablished in substantially the same proportion as the holdings of class B stock.

PRODUCTION CREDIT ASSOCIATION AMENDMENTS

Section 2(a). Each borrower from a production credit association is required to own, at the time the loan is made, class B stock of the association in an amount equal to \$5 per \$100 or fraction thereof of the amount of the loan (12 U.S.C. 1131g). Class B stock entitles a holder to vote (one vote per holder) and may be purchased only by farmer borrowers from the association and individuals eligible to become borrowers; and within 2 years after a holder of class B stock has ceased to be a borrower from the association, such class B stock must be exchanged for nonvoting class A stock of the association which may be purchased and held by investors (12 U.S.C. 1131e). The present amendment concerns a provision in the law (12 U.S.C. 1131g) that the class B stock of a production credit association owned by a borrower from

the association "shall not be canceled or retired upon payment of the loan." Immediately after the quoted words would now be added "or otherwise, except as may be authorized under rules and regulations prescribed or approved by the Farm Credit Administration." This would make it possible to authorize retirement of the stock upon payment of the loan, as may sometimes be in the best interest of both the borrower and the association. The amendment would also permit retirement of the stock for application of the proceeds in partial or final payment of the loan and in other circumstances as authorized under the rules and regulations.

Section 2(b). Production credit associations are specifically authorized to borrow from, and rediscount paper with Federal intermediate credit banks. Except with the approval of the Governor of the Farm Credit Administration (12 U.S.C. 1131h, second sentence), such associations may not borrow from or rediscount paper with any other bank or agency. It has not been considered within their authority to borrow from investors generally as by the sale of capital notes. The proposed amendment would specifically authorize a production credit association to issue its capital notes for sale to borrowers and others. This new authority would be subject to rules and regulations prescribed by the Farm Credit Administration, and the capital notes outstanding at any one time, together with other liabilities of the association, may not exceed 10 times the capital and surplus of the association.

This concludes my prepared explanation of the bill and we hope that the committee may see fit to act favorably on it.

The CHAIRMAN. Thank you, Governor Tootell.

Do you want us to proceed with Mr. Boddy before we proceed to ask anybody questions?

Mr. TOOTELL. Just as you wish, Mr. Chairman.

The CHAIRMAN. I think it would be better to get all the background statements in here before we go into questioning.

We will now hear from Mr. Boddy, chairman of National Advisory Committee of Production Credit Associations.

We will be glad to hear from you now, Mr. Boddy.

STATEMENT OF H. M. BODDY, CHAIRMAN, NATIONAL ADVISORY COMMITTEE OF PRODUCTION CREDIT ASSOCIATIONS

Mr. BODDY. Mr. Chairman and members of the committee. I represent the National Advisory Committee of Production Credit Associations which is composed of the committeemen from each of the 12 districts and they represent, in turn, the 370,000 production credit association members.

These members are chosen in each district. They operate very closely together. They are members of their own production credit associations and also are committeemen.

At our annual meeting the 1st of April here, the primary interest of our members, 370,000 production credit association members, was this matter of capitalization and particularly the matter of the ratio requirements. The people from every area brought with them a mandate from their own associations to go into this matter, and at the suggestion of one of the districts we passed a resolution which was adopted which says, basically, three things:

That the present 12-to-1 ratio is overly conservative and restrictive;
 That the proposed 20-to-1 ratio will be adequate in view of past and projected loan losses by production credit associations;

That conservative loan loss projections are reasonable in view of the sound financial position, successful management, and mutual loss sharing plans that have been adopted.

We feel that the Federal intermediate credit bank system varies from other lending institutions in many ways:

In the first place, we are doubly capitalized by the members investment in the stock of both the production credit associations and the Federal intermediate credit banks. So, you have double-duty dollars; you have a doubling of the capitalization by the members in these associations. A reduction in Federal intermediate credit bank capital ratio will lessen the demands for additional capital at a time of large expense and small profit by agriculture.

Second, the investing public is insulated from any kind of loss by three layers of reserves, surplus, and capital; first, the capital of the bank, then by the capital of the association, and then by the farmer members of that association.

The loans are made on the land and the livestock, the cattle of the members. These notes in turn are placed or pledged with the association which, in turn, pledges their surplus which has been contributed by the same members, and a reserve has been built up. It is placed in the credit banks which in turn place it in their reserves.

The Federal Intermediate Credit Banks capital surplus and reserves must disappear before any investor loses a dime. For the Federal intermediate credit bank capital to disappear the same amount of reserve surplus and capital in the Production Credit Association must disappear. This would mean the loss of all equity in land and chattels of the individual members. Thousands of farmers and cattlemen must go broke, hundreds of Production Credit Associations must go broke and some Federal Intermediate Credit Bank must lose all it has before any investor is in jeopardy.

If an association goes broke, no one is affected, no one loses; no deposits are involved, no third parties are involved, and if an association goes broke, which would be a first, the only thing that would be involved would be the capital of the farmer members that they have already put in.

On June 30, the Houston Federal Intermediate Credit Bank will repay to the Treasury all the Government capital invested in it. Within 5 years, all the Government capital in all other Federal intermediate credit banks is scheduled for repayment.

With no Government capital at risk, no depositors or third party funds at stake, with investors protected by this pyramid of reserves, and with proven management and credit know-how it would seem that farm credit is justified in requesting this ratio change.

So, with these differences between our system and ordinary banking systems, the members of the National Advisory Committee would like to urge your consideration of this legislation.

(Following is a resolution passed by the National Advisory Committee of Production Credit Associations:)

Resolution of the National Advisory Committee of Production Credit Associations urging the passing of Federal legislation to change the Federal Intermediate Credit Bank maximum loans and net worth ratio from 12 to 1 to 20 to 1.

Whereas the present limitation of 12 to 1 is unnecessarily conservative and too restrictive if the credit banks are to continue to meet the increasing needs for agricultural financing without calling on the government for more capital while returning within a reasonable time the government capital they now have, and

Whereas the major reason for having a ratio requirement is a protection against loss for investors and stockholders, based on loss experience and the probability of future losses, the 20 to 1 ratio is adequate, and

Whereas the Production Credit Associations, the primary lenders in our System, are required to maintain sound financial structures and sizeable provisions for bad debt losses; and,

Whereas most Production Credit Associations have joined in a program for sharing of losses thereby spreading the risk of their lending business, and

Whereas it has been determined that because of the strong financial position of Production Credit Associations and their sound lending policies over the years, the changing of the ratio would not have an effect upon the debenture market, and

Whereas to ask farmer-members to invest additional money to capitalize Production Credit Associations and the Federal Intermediate Credit Bank, when it is not necessary, will put an additional financial burden on them: Now, therefore, be it

Resolved, by the National Advisory Committee of the Production Credit Associations, That Federal legislation be passed changing the present Federal Intermediate Credit Bank maximum loan to net worth ratio of 12 to 1 to 20 to 1.

The CHAIRMAN. Thank you, Mr. Boddy.

I think we might now ask questions of our panel and then call upon the representatives from the Farm Credit districts.

Do you think that is a proper way to proceed, or would you rather hear from the others at this time?

Mr. TOOTELL. I think there is merit to directing questions to those of us who are here at the present time and then proceed to the district people.

The CHAIRMAN. I was interested in Mr. Bice's statement.

On page 4, you have a statement about a membership of 548,279 at the end of 1967, and, of that number, there were 322,700 borrowing members of the associations. Now, how did you get that difference between the two groups, those that were and those that were not borrowers? They would have to be a borrower of the association to be a member, would they not?

Mr. BICE. That comes about in two ways, I would think.

A lot of these 548,000-odd that I have mentioned repay their loans before the end of the year so that the number is reduced. They are members at one time but not necessarily so at the end of the year, and then they would be in and out a year or two, just as their needs might require. So long as they retain their class B stock they are members. They are not voting members when they own class A stock, but they are members. So they come in and out. I think that is the answer to this discrepancy in the figures.

The CHAIRMAN. Does a man cease to be a member when he converts his class B stock into class A stock? He ceases to be a voting member. How does he cease to be a member?

Mr. BICE. Well, eventually, that stock can be offered for sale and picked up by another member. Under the proposed act it would be provided that his B stock may be retired as a part of his last payment on his loan. So then, of course, he would cease to be a member when the last payment was made.

The CHAIRMAN. Of course, when he comes to pay off the land bank loan, you can use that last 5 percent to pay the loan?

Mr. BICE. That is correct.

The CHAIRMAN. And you will require that procedure to be followed here?

Mr. BICE. That would be permissible under the amendment we are asking for; yes, sir.

The CHAIRMAN. Governor Tootell, on page 2 of your statement, you state:

When the debt-to-capital ratio of the credit banks is close to 12 to 1 and loans and discounts are increasing rapidly, the banks can continue to operate within that ratio only if additional capital is paid in.

And you state that as of June 30, 1967, the ratio was 11.35 to 1, but that this was reduced to 10.78 to 1 after earnings for the year were distributed, and that based on the latest estimates available, the ratio will closely approach the present 12-to-1 legal maximum in May or June 1968. I think you have actually answered the question that I had in my mind when you read that.

You pointed out that the Production Credit Associations were being called upon to provide more capital, that that is the way that you intended to continue to operate. Of course, the 12-to-1 would occur, so far as operation is concerned, but you would prevent that by additional purchasing of the stock by the Production Credit Associations, and you do not consider that that is a permanent solution and it will not bring in enough money to keep us in an operating position over a period of years, and that that is why we have to change the ratio for the intermediate credit banks.

Mr. TOOTELL. This is exactly right, Mr. Chairman; this is purely a temporary assistance to purchase the class B stock, in order to meet the increasing requirements of farmers that the Production Credit Associations are being called upon to meet. After the PCA's provide this additional capital to the credit banks, it simply means that the farmers would be called upon for completely unjustified capital contributions to the two credit institutions.

The CHAIRMAN. Which has the effect of raising the interest rate to the farmers.

Mr. TOOTELL. It would have the same effect; yes.

Another way is to increase the interest rate and to have these additional net earnings or net worth that will add to the capital, but this is a very, very expensive way from the farmers' standpoint.

The CHAIRMAN. I feel that it is, too, and I feel that we should arrive at a system that would enable us to extend the lending power of the intermediate credit banks to the extent that we get his money from the Production Credit Associations. It would seem to me that the effect of it is to postpone the time when the Production Credit Associations would pay off all of their capital. I believe there are only two—

Mr. TOOTELL. There are three in the United States.

The CHAIRMAN (continuing). That have not done that now, but they ought to get their Government capital all paid out and they ought to establish adequate reserves, it seems to me, at the local level, which has the same effect on the securities of the lending institutions when you add this additional capital at the local level, except that it does not meet the legal requirements of the ratio of the intermediate credit banks, and to me, it seems to be more desirable, or it would be desirable if we increased the reserves at the local level rather than putting their reserves in intermediate credit banks.

Mr. TOOTELL. I think this is a very good point in favor of this. Actually, as pointed out in the testimony, there is no effort at all or intention to change either the legal ratio of the Production Credit Associations which has been a 10-to-1 ratio, from the beginning in 1934, nor to change the factual operating ratio which is about 7 to 7½ to 1. The Production Credit Associations as primary lenders will continue to make loans in that fashion and will continue to be kept in a very sound financial position.

The CHAIRMAN. But, as you know, for some years I have been one of those who have been reluctant to let this ratio of loans to capital get too high in any of these institutions, because I felt that solvency was the most important thing that we should have and that we could not perform any of the rest of the functions of the banks unless we had absolute assurance of the solvency of the institutions.

And I think, as I recall it, back 10 or 12 years ago when we revised this, that I thought that the 12-to-1 ratio was probably as high as we could go, but I do recognize that we have had a great expansion in the institutions in the meantime and that the need for capital reserves is not nearly as great as it was, in my judgment, 10 years ago—certainly 40 years ago. I think that with the passage of time these institutions have become very much stronger than they were; that the local support, meaning the Production Credit Associations are so much stronger than they were 10, 20 years ago, it seems to me that it would justify making the change that is being proposed here.

Mr. TOOTELL. I would like to draw another comparison. You mentioned the other institutions in our Farm Credit system, the Federal land banks, that they from the beginning in 1916 have had a 20-to-1 ratio and that the Federal land banks are primary lenders while the credit banks are secondary lenders and have the financial strength of the PCA's ahead of them in case of any loss. I think this is further evidence.

The CHAIRMAN. Are there any other questions?

Mr. TEAGUE of California. I have to leave in a moment.

Through the years I have been on this committee, I have come to have a very high regard for Governor Tootell and his judgment, and therefore, I expect to support these amendments unless some very unforeseen thing happens. I am sorry that I do have to leave.

The CHAIRMAN. Thank you, Mr. Teague.

Mr. Gathings?

Mr. GATHINGS. On page 5 of your statement, Governor Tootell, that "Their losses in the 33 years of their existence since 1933 have amounted to only .08 of 1 percent," and then a little farther down on your statement you say that "the net losses of the credit banks in 44 years of operation have amounted to approximately \$1 for each \$9,000 of credit extended."

I am greatly impressed with the reserve situation mentioned at the bottom of page 5. You state that the reserves for losses total \$99.9 million or 2.7 percent of total loans outstanding on December 31, 1967.

That seems to me to be a very great record. I commend you for it.

Mr. TOOTELL. Thank you, Mr. Gathings.

May I add, with regard to this reserve bad-debt losses, that is being built up to 3.5 percent, generally. There are some associations that have actually exceeded that at the present time.

Mr. GATHINGS. That 2.7 would move up, then?

Mr. TOOTELL. Yes. A few years from now, maybe just 2 or 3 years from now, that will probably be 3.5 percent for the system as a whole.

Mr. GATHINGS. Thank you. That is all, Mr. Chairman.

The CHAIRMAN. Are there any further questions?

Mr. McMillan?

Mr. McMILLAN. Mr. Chairman, I would like to thank the governor for the fine work the banks have done in my State of South Carolina. They have been a great help and a lifesaver to the farmers.

And I appreciate your statement.

Mr. TOOTELL. Thank you.

The CHAIRMAN. Mr. Goodling?

Mr. GOODLING. I am not as familiar with this as I would like to be. What is your present loan rate to farmers?

Mr. TOOTELL. Do you mean of the Production Credit Associations?

Mr. GOODLING. Yes.

Mr. TOOTELL. This varies, sir, by associations, depending, in large part upon the size of the association and its operating efficiency. The typical loan rate today is 7 percent, with the next most common loan rate being 6 percent. This is the answer. Of course, the reason that is that high is because the PCA's have to hire their money and they hire it from the credit banks which, in turn, hire it from the money markets, and you know where the money markets are and have been these last few years.

Mr. GOODLING. That answers my next questions with reference to how you compete with commercial banks with a loan rate of 7.5 percent. In my home State, commercial banks are limited to 6 percent.

Mr. TOOTELL. Of course, over a long period of years, the typical loan rate of the PCA's has been 6 percent or less. And just to keep the record straight, I would have to admit that the PCA's do compete to a limited extent with commercial banks, but I would hasten to point out that the PCA's are specialized lenders. They are permitted by law to loan only to farmers and ranchers. They are not permitted to make any other types of loans. They are required to do that, and they cannot accept deposits. And so that the competition is limited. In most parts of the country, let me say that the local bankers in the agricultural lending business welcome the additional funds that the PCA's bring into the rural areas and also are glad to have the deposits which the PCA's maintain with the commercial banks locally.

Mr. GOODLING. What is your criteria for making loans to farmers and ranchers?

Mr. TOOTELL. Well, in the first place, he must be an agricultural producer, and he must have the ability to repay. It is never the intention to make a rancher or a farmer a loan unless an analysis of his situation leads the loan committee of the PCA to believe that the loan will do him some good and that means that he will be able to repay the loan and we hope will have considerably more benefit than just getting enough additional money.

Mr. GOODLING. Do you pay Federal income tax on your earnings?

Mr. TOOTELL. The PCA which are the primary lenders do so; they do so.

Mr. GOODLING. Thank you. That is all, Mr. Chairman.

The CHAIRMAN. Are there any further questions?

Mr. Mayne?

Mr. MAYNE. I would like to commend Governor Tootell and Chairman Bice and all of the other gentlemen here on the very splendid work that the farm credit system has been doing in the Omaha District which is personally known to me. I would like to ask you, Governor Tootell, this question: On page 5, you say that moving the debt-to-capital limitation from 12 to 1 to 20 to 1 is justified by the financial strength of the credit banks and the associations, and that one of the safeguards of assuring this is, as you point out, that the liability of each PCA, including its liability to the credit banks, may not exceed 10 times the paid-in and unimpaired capital and surplus of the association.

Now, this seems like a strong argument to me, if you intend to adhere to this 10 to 1 ratio.

I would like to ask if there are any plans to ask the Congress for a liberalization of the 10 to 1 ratio?

Mr. TOOTELL. I will answer unequivocally no.

Mr. MAYNE. Well, I am glad to hear that. So that we will understand that we will not be getting into a situation where if we do have the 20-to-1 debt-to-capital limitation it will then be argued that the 10-to-1 limitation is unrealistic or unfair when compared with the 20-to-1 ratio. That will not be the situation?

Mr. TOOTELL. I have just checked. I do not foresee any situation of that kind at all. As a matter of fact, most associations are required by the credit banks to keep that ratio down to around 7 or 7½ to 1.

Mr. MAYNE. Well, with that additional assurance, I will reiterate that I think that you have a very strong argument.

Thank you.

That is all, Mr. Chairman.

The CHAIRMAN. Thank you.

Mr. Zwach?

Mr. ZWACH. I would like to commend especially the group I am familiar with, the St. Paul district, over the many years, for their work, the Federal land banks, the production credit associations and the Bank for Cooperatives, and the others. They have been a very important part of our agriculture.

I would like to ask you now if the farm debt is increasing more rapidly than the farm asset?

Mr. TOOTELL. No, Mr. Zwach; it is not. The farm debt has been increasing at a very rapid rate. Since 1950, particularly in the last few years, it has been increasing at the rate of about \$4 billion a year, but actually farm assets have been increasing at a faster rate. This increase in farm asset value is something that can be debated by some, because a high percentage of that is the increase in the land price. And the present land price is there. And further the increase in the other prices which I think are going to be determined is dependent upon the income situation of the farmers over the years.

We know about outside income. We know that a fairly high percentage of farmers nowadays have some sources of outside income, and if it were not for that income I do not believe that the present would be such as it is.

Mr. ZWACH. In other words, your feeling is that without increasing their income, we would be approaching what would be a questionable area in the farmers ability to repay at the present high interest rates?

Mr. TOOTELL. I think that is a distinct possibility.

The actual equity ratio of the farmers is good. This debt-asset ratio has been going up from about 12 percent to some 17 percent at the present time, maybe 18 percent. This makes the equity of the farmers in the current value of their farm assets about 82 percent.

Mr. ZWACH. My impression sort of was that your operations have been pretty conservative on farm loans. I am thinking specially of the Federal land banks and perhaps the PCA's. I do not think you have been over extended. The fact is that I think that other agencies have had to come in to sort of supplement.

Mr. TOOTELL. Well, the Farmers Home Administration, for instance, was created to do a low-equity and higher risk financing job than the farm credit system. Whether that is due to undue conservatism, I do not know, on the part of the cooperative farm credit system. It is a matter of opinion.

Mr. ZWACH. I am basically conservative. But when I look at the credit needs and see the denial of this need in specific cases, I come to this conclusion, but I have to commend you and I think that your request here for this change in the ratio is very reasonable. Thank you.

That is all, Mr. Chairman.

The CHAIRMAN. Mr. Kleppe?

Mr. KLEPPE. Governor Tootell, some 26 years ago I was running a little commercial bank somewhat in competition with the PCA's and at that time, and to my knowledge since, they performed a service in the community that by and large could not be met by the commercial banks.

You indicated, in answer to one of the earlier questions, that to some degree the PCA did compete with commercial banks. In our part of the country I think that we, generally, agree and accept the fact that they fully meet this need just below where the commercial banks can go. Is this not generally true?

Mr. TOOTELL. The term "just below" puzzles me. If you mean by this serving a clientele that the bankers would not be willing to serve, I would say "No."

Mr. KLEPPE. This is what I mean generally.

Mr. TOOTELL. No. I would say, "No." I would say that, generally, because the PCA's have to rely upon the market itself; that by and large their loan policy would not be greatly different than that of good country bankers.

Mr. KLEPPE. Just a little bit is all I am talking about. [Laughter.]

Mr. TOOTELL. I will concede "a little bit."

Mr. KLEPPE. I remember loans that I could not handle that were just barely out of the category of what I could handle which were good loans for the PCA and they did fill that need, and, as a general rule, it seemed to me, and does seem to me that this is still true up in our part of the country anyway, that this serves a real purpose and has a real meaning.

Did you not say that three of the banks have the Government capital paid out?

Mr. TOOTELL. Three of the PCA's out of 459 PCA's—there are only three that have any Government capital. The 12 intermediate credit banks, none of them have retired all of their Government capital.

Mr. KLEPPE. In effect, these PCA's are private, independent operators, competing in the market selling debentures, and they are paying the going-money rate, whatever it is?

Mr. TOOTELL. That is right.

Mr. KLEPPE. And the interest rates that are being charged are, generally, competitive within that area, are they not?

Mr. TOOTELL. Yes; they are.

Mr. KLEPPE. My question is pretty academic, I realize.

In the history of this operation, ever since it was set up, has there ever been a default on debentures?

Mr. TOOTELL. There never has been, no; and this goes back to 1916 when the Federal Land Bank was started.

Mr. KLEPPE. There has never been a request from your organization, or any part of it, to the Government to come in and pick up the slack where there was a default of any kind?

Mr. TOOTELL. No.

Mr. KLEPPE. It seems to me that your request here in these amendments is very much in order, because this item of credit in farm operations and in ranching operations is so very vital because we have people today who could become good operators if they had the capital, and here is the way, it seems to me, that we can provide some more. And I commend all of you at the table for your presentations and being a part of a Government program that has really worked.

I think this is very commendable.

I thank you.

That is all, Mr. Chairman.

The CHAIRMAN. Are there any further questions?

Mr. Mathias?

Mr. MATHIAS. Is there a limit on the authorized loans?

Mr. TOOTELL. Actually not on the total dollar value. If a production credit association proposes to make a loan, or does make a loan, that exceeds 15 percent of the net worth of the association, it must get the permission of the intermediate credit bank, it must have prior approval of the intermediate credit bank. If the proposed loan exceeds 35 percent of the net worth of the association, then the additional approval of the Farm Credit Administration must be had. So, there are those two safeguards in there with respect to the size of the loans. But, you see, when the net worth of the PCA varies, as it does, very substantially, these loans also may vary very substantially.

Mr. MATHIAS. With regard to the amount that they can loan?

Are there any large loans?

Mr. TOOTELL. I should like to defer that question to Mr. Wright who is a deputy governor in charge of that.

Mr. WRIGHT. We have a few large loans that would run up into a few million dollars, but precious few. Most of our loans would be below \$10,000. I have a table here on that which I will be glad to refer to.

Mr. MATHIAS. What is your average?

Mr. WRIGHT. \$11,587 on the outstanding basis. So, even though we have a few large loans, primarily in the ranching sector, they are few in number.

Mr. MATHIAS. That is all. Thank you.

The CHAIRMAN. Thank you.

Are there any further questions?

If not, we will now call on Mr. Charlie Thompson of the Houston District.

STATEMENT OF CHARLES C. THOMPSON, CHAIRMAN, BOARD OF DIRECTORS, FARM CREDIT BANKS OF HOUSTON, AND PRESIDENT, CITY NATIONAL BANK OF COLORADO CITY, TEX.

Mr. THOMPSON. Mr. Chairman and gentlemen of the committee. I have only a very brief statement to supplement what these gentlemen have already said.

I am taking advantage of you before you do of me, in telling you that I am chairman of the board of directors of the Farm Credit Banks of Houston which as you know, also acts as the board of directors of the Federal Intermediate Credit Bank of Houston, and also I am president of the City National Bank of Colorado City, Tex. I have been president of the bank for 30 years. I make that explanation in the beginning.

Generally speaking, this bill represents an effort to solve some of the capital problems of our intermediate credit banks and production credit associations. One or two of the sections are technical in nature and I am sure will be explained in detail by other witnesses. I shall address myself only to the three provisions which appear to me to be fundamental. These are:

(1) Increase the debt-to-capital ratio of the intermediate credit banks from 12 to 1 to 20 to 1;

(2) Authorize sale by the intermediate credit banks of participation certificates to agricultural credit corporations, and

(3) Authorize production credit associations to issue capital notes to members and others.

Now, as to the increase in ratio from 12 to 1 to 20 to 1.

I would like to direct your attention to two basic ideas which I will state and then discuss briefly.

First: If we continue with the 12-to-1 ratio, farmers and ranchers of America will be required to invest added millions in their intermediate credit banks. They should be spared this requirement if it can be done soundly—and I emphasize the word "soundly."

As you know, the philosophy of our farm credit system long has been that eventually, the capital needs of our banks and associations are to be met by investments of American farmers and ranchers in our banks and associations.

These farmers and ranchers are willing—yes, even anxious—to supply this capital; they have proved this in the case of our land banks and production credit associations; they are proving it in the case of our banks for cooperatives and our intermediate credit banks.

At the same time, however, we must recognize that while these farm and ranch people want to supply the capital that is needed for these banks and associations, they must not be required to put in more than is required for sound and safe operations. In these times, they cannot afford this. They need the money in their own operations.

Now, gentlemen, it will be obvious to you from other testimony offered here that with continuation of this 12-to-1 ratio, the intermediate credit banks cannot generate from earnings sufficient capital

to take care of the expansions in credit which all of us know are coming. They simply cannot afford to charge sufficient interest to do this, and farmers and ranchers cannot afford to pay such charges.

In light of this we come right up against it: If the ratio is not increased, this added capital will have to come from some source. Since our policy is to repay Government capital and not receive more, the only source remaining is the farmer and rancher who uses our facilities. We are talking about many millions of dollars. If we keep this ratio 12 to 1, farmers and ranchers must dig up these huge sums; if we increase it as requested, they will keep this money in their own business.

Believe me, gentlemen, they need it.

Second: In my opinion, you can increase this ratio without risk either to the intermediate credit banks, the production credit associations, or the investing public.

Bear in mind that this 12-to-1 ratio is only two points higher than the 10-to-1 ratio created in the original intermediate credit bank legislation in 1923. This 10-to-1 ratio remained in effect for 42 years, during which time the banks increased their net worth from nominal amounts originally subscribed by the Government, to a total of \$292,707,918 at the end of 1965, the year we increased the ratio 12 to 1. At the end of 1967, this net worth figure was \$327,814,852.

And in addition to this, since 1934, we have added to the overall strength of our system the net worth and reserves of production credit associations, which at the end of 1967 came to \$591,064,409.

Now, while these figures are impressive in themselves, even more important is the recognized fact that the intermediate credit banks were and are firmly established as institutions of unquestioned soundness and stability; they are so considered everywhere, and their history bears this out. First, we have the financial stability; and, secondly, we have historical stability, as witness the astounding statement made elsewhere in these hearings that their losses on loans in the 44 years of their history have been approximately \$1 for each \$9,000 loan, and no losses since 1933.

In light of the foregoing, it is my opinion and that if the farm credit people in the Houston District, that the system has proved itself ready for this 20-to-1 ratio and fully capable of handling it. This being true, I hope the Congress will give it to us and allow us to keep these millions of extra capital where they are most needed.

SALE OF PARTICIPATION CERTIFICATES

The second item of importance, is the authorization to the intermediate credit banks to issue—in effect to sell—participation certificates to agricultural credit corporations.

We call these corporations OFI's (other financing institutions, as distinguished from production credit associations).

As the law now stands, the only way an OFI may acquire participation certificates from a bank is through the patronage refund process, or, in other words, from the bank's annual earnings.

A bank may issue stock to a production credit association; it even may assess the associations and require them to buy this stock. It has no authority to do this for OFI's, and, in fact, under existing law it cannot even sell a single certificate for cash.

As the banks continue to expand, this OFI business in some districts will take on added importance. In my district (Texas), they are doing about 15 percent of the total business with the bank. They always have been an important segment of our overall financing.

If they are to use the banks' facilities in a substantial way, then, in my opinion, the banks should have opportunity to ask them to furnish the capital necessary to carry this use. Otherwise, they would be using capital put in by production credit associations and other OFI's. This is only equity in action.

For your information, I am advised that our bank people in Texas have discussed this matter in detail with all our OFI representatives; they are aware of the problem and feel that this is a proper amendment.

SALE OF CAPITAL NOTES

The third item is authorization of sale of capital notes by production credit associations.

You may know that heretofore our associations have raised needed capital by sale of what is known as "A" stock. In effect, this has been sort of a preferred stock.

Many associations have paid dividends on this stock. These dividends are taxable to the associations; taxable to the recipients.

Since they have considered it somewhat of an obligation to retire this stock on demand, many associations have felt that this is more in the nature of a loan by the member than a stock purchase.

This being so, they have said: "If it is a loan, let's call it a loan. Thus the interest on the note would be tax deductible."

I am a banker. I do not visualize a great use of this section outside the membership of production credit associations—certainly not one which would be considered as affecting banks or other institutions seeking savings from the public. I do see in it a device wherein an association in need of added capital may solve part of its problems by a benefit both to itself and to its membership and other folks in a rural community.

Thank you.

The CHAIRMAN. Thank you, Mr. Thompson.

Are there any questions of Mr. Thompson?

Let me say that Mr. Thompson has had a fairly long experience in operating these things as chairman of the board in the Houston district. He is as familiar with these operations as anybody and certainly, as the head of a country bank—if I may call it that—

MR. THOMPSON. That is correct, Mr. Chairman.

The CHAIRMAN. He has had a good bit of experience on the other side, where there has been some fear expressed that there might be some kind of competition, expressed by Mr. Goodling.

Mr. PRICE?

MR. PRICE. I would like to ask Mr. Thompson a question.

I have heard that the insurance companies are moving as rapidly as possible out of the farm and ranch loan business.

MR. THOMPSON. Out of farm and ranch loans?

MR. PRICE. Is this correct?

MR. THOMPSON. Not true in our district; they are still operating; but they are moving towards larger and larger loans. They are interested in big farms and big ranches.

Mr. PRICE. I had understood that because of the high-risk area in agriculture there have been a number of major companies that have been moving out of the farm and ranch loans into, oh, say, the big apartment-house complexes where they turn their money over faster. What I am trying to say is that this is creating a demand for more capital for these loans from the Federal loan banks and the like. If we could substantiate this showing, the need for more capital in these areas, it would be helpful.

Mr. THOMPSON. I certainly think it would be helpful for the Federal intermediate credit banks and the PCA's. The insurance companies are not interested in little loans, and not in the rate of interest that we charge, either. I will say that.

They do not make nearly as many loans as they did for a while, because, as I said, they have moved out of the small-loan area in our district in the State of Texas. They are still making a considerable number of loans, particularly in the ranching part of the country, in sections of the high plains, but not as many as have been made in the past. There are so many opportunities for income off of these loans of various kinds, stock, bonds, and everything else, that they can pick where they want to go, and that is the reason that the PCA's and Federal intermediate credit banks need to have this increase in interest rates so that they might meet that situation soundly.

Mr. PRICE. In my district alone, in the Panhandle, people are going to need a billion dollars in the next few years for cattle feeding and other normal agriculture credit, and our banks are going to be strained to furnish this money.

Mr. THOMPSON. And they could not lend it without the increase in the rates, because it would be impossible for the farmers to go in now and buy 8 or 10 percent additional stock certificates to make that ratio go up to 20 to 1. It is not feasible and it is unfair to the farmers. I think the record of the last, certainly, 33 years of the PCA's has indicated that they are making a success, they have built up reserves; and, now, in the last few years we have had the privilege of building reserves to guard against losses. How long has that been? Since 1961. All of these reserves for losses have been built since 1961, at which time the Internal Revenue Service said something to the effect that we could build it up to 3.5 percent.

Mr. PRICE. You do not get into any other areas of loaning other than to farmers and ranchers?

Mr. THOMPSON. No, this is a production credit association, and it is strictly for farm loan business—all types of agriculture. And the Federal intermediate credit bank is able to discount its paper with any institution if it is a farm piece of paper. A bank in Amarillo right now has some paper discounted there.

Mr. PRICE. Thank you.

That is all, Mr. Chairman.

The CHAIRMAN. Thank you, Mr. Price.

Are there any further questions of Mr. Thompson?

If not, we are always glad to have you with us, and we appreciate your statement.

Mr. THOMPSON. Thank you.

The CHAIRMAN. I will now call on Mr. Paul Enns of the Berkeley District.

Mr. Mathias?

Mr. MATHIAS. This is Mr. Enns. He is a constituent in the fine city of Bakersfield, Calif. He is a farmer. He has a ranch about 12 miles west of Bakersfield. He can tell us something about this subject that we are discussing this morning. It is my pleasure to introduce Mr. Paul I. Enns.

The CHAIRMAN. We are glad to have you, Mr. Enns. You may proceed.

STATEMENT OF PAUL I. ENNS, CHAIRMAN, BERKELEY DISTRICT FARM CREDIT BOARD

Mr. ENNS. Mr. Chairman and members of the committee, my name is Paul I. Enns and I am a member of the 11th, or Berkeley District Farm Credit Board, and presently am serving as its chairman. The Berkeley District serves California, Arizona, Nevada, Utah, and Hawaii. After being released from the service in 1945, I went into farming. I have used the facilities of the farm credit system since that first loan. I am a full-time farmer and I now operate and live on a 520-acre irrigated farm located about 15 miles west of Bakersfield, Calif., which is in the southern part of the San Joaquin Valley. My present operation consists of 140 acres of cotton, 146 acres of alfalfa, and 230 acres of grain. I have also been finishing about 3,000 head of cattle annually. This is the 23d year that I have been using farm credit system loans in my operations.

In 1951, the farmer-owners of the Bakersfield Production Credit Association elected me to be a director of their association and I am now serving as vice president of the board, and in my sixth 3-year term. In addition, the 28 production credit associations (PCA's) of the 11th Farm Credit District have elected me to represent them on the district board. I am now serving my fourth 3-year term.

Our district board has asked me to come here to support the legislative changes proposed in H.R. 16674. My recommendations and views are based on my experiences as a farmer-user of the system, the experience of serving on the local PCA board, and the district farm credit board.

I will now present my views on the proposed legislation affecting the Federal intermediate credit banks (FICB's).

Section 1(a), the proposal to change the debt to capital ratio from 12 to 1 to 20 to 1.

There are a great number of reasons that substantiate this change and I would like to begin with this analogy:

The FICB's were established in 1923 and we could say that this would be like taking the model T Ford, so popular and revolutionary at that time, and subjecting it to the competition of other vehicles on the freeways and parkways of today.

Since 1923 many changes have taken place in farm credit. Originally, loans were made only to other financing institutions (OFI's), and some cooperatives under completely different conditions such as:

1. Complete Government capitalization of the FICB's.
2. Under direction of Federal land bank boards.
3. No earned reserve or surplus accounts in the FICB's.
4. Limited experience of personnel employed to operate the banks.

It soon became evident that this method of farmer crop mortgage financing was not fulfilling the great need.

I will now identify some very important developments in the 1933-68 period that support the change in the debt-to-capital ratio as stated in section 1(a) of this proposed legislation.

1. Establishment of production credit associations (PCA's) in 1933 with supervision provided by the district production credit corporations under the general supervision of the Farm Credit Administration (FCA), provided the guidance and policies so necessary for progress and success.

2. PCA's elect two members to the district boards for improved representation.

3. PCA's maintain reasonable debt-to-capital ratios (10-to-1 legal limit). The 11th district PCA's, at the end of February 1968, had a debt-to-capital ratio ranging from a low of 3.8 to 1, to a high of 6.9 to 1. These ratios fluctuate from year to year and in various seasons of the year, depending on loan volume and other factors.

4. PCA's make the loan with the farmer and must "go broke" before the FICB becomes at all involved, with the exception of its general supervisory responsibilities delegated by the Farm Credit Administration.

5. In addition, "share the loss" or "participation loan" programs are being used as a first line of defense by the PCA's against possible losses to the FICB.

6. Establishment and funding of reserve for loss accounts in PCA's.

7. Loss history in PCA's remains small compared to dollars loaned, even though today there are many farm problems.

8. The losses suffered by the FICB's were in the period from 1923 to 1933 and are the only losses in their entire history.

9. Continuance of specialization in agricultural lending for the best possible service to farmers.

10. Farmer capital is continually increasing in the FICB's even though increased volume has not allowed repayment of Government capital.

11. Manpower development and training of personnel for improved and increased efficiency and resulting astuteness.

12. Better organization development to handle problems as they develop.

In recommending favorable consideration of the proposed legislation to change the debt-to-capital ratio of the FICB's to 20 to 1, I do so with the firm conviction that substantial savings will result to farmers and ranchers. I am positive that this proposal will not weaken the financial structure of these farm credit organizations, but, rather, will restore a proper balance in the utilization of the resources now available in the system.

Our relationship between one another is such that we understand what we are doing. They both have to tie together, and these are both very important.

I feel that this proposed legislation is very important. I do not feel that the credit bank is just to restore anything but a proper balance between the capital that we have available and debt and it will result in savings to the farmers.

I also support the other sections of this proposed legislation which are:

Section 1(b). This proposed section would permit OFI's to purchase additional participation certificates in FICB's when conditions prevail where OFI business adds to the stress on the debt to capital ratio of FICB's.

Section 1(c). Permits reallocation of FICB allocated reserve account proportionately with the use of the bank by the owners of the bank.

Following are sections affecting the production credit associations (PCA's) :

Section 2(a). This would allow the PCA to liquidate "B" stock. Situations now arise where a farmer ceases to use the services of the association and it is advisable to also sever all ownership relations.

Section 2(b). Circumstances now arise where PCA's may wish to obtain additional capital on specific terms. Associations could beneficially use this method, especially where private capital is available in their local area.

In conclusion, I am convinced that this legislation is desirable to keep the short-term lending services of the farm credit system up to date with the current and future needs of agriculture. In meeting our responsibility in providing credit service to American agriculture, it is vital that we employ the capital resources of our farm credit system to optimum advantage consistent with sound financial and fiscal principles.

Thank you very much.

The CHAIRMAN. Thank you.

I believe that to get an understanding of the way the testimony is going so far, I wish to suggest that the committee insert in full the written statements of any of the witnesses, together with the questions that will be asked, or we can insert the statement in the record that you are making along with any questions. If you take a written statement, in my opinion, and paraphrase that statement and then put the full statement into the record, it will encumber the record. Either one that the witness wants, if you will advise the clerk which you want inserted, we will put that in, and we will put in all of the questions and answers, but we will not duplicate the statements where they are written out and then paraphrase it as has been happening. There is nothing wrong with that, but I just want that to be known.

As I understand it, the next witnesses are Mr. Nay and Mr. Curtiss. Mr. Nay and Mr. Curtiss will conclude those that will testify orally and the remainder will insert their statements, it is my understanding. Is that correct?

Mr. TOOTELL. These men, before this session started, this morning agreed that these folks would have preferential treatment as to time. I think it depends upon the time that is available and the wishes of the committee. They all have statements. If the committee would like to have them, they would like to present them.

The CHAIRMAN. If I could quote something that is well known to all lawyers, "Never argue with the Court when he is ruling with you." I do not think there has been any serious objection thus far presented by the committee.

We will be glad to hear from Mr. Nay, who is the next witness.

I do not want anyone to feel that I am suggesting that the testimony will not be worthwhile, but, after all, there is no purpose in just ac-

cumulating testimony that is repetitious. I am afraid that you have done such a good job that you could leave the rest of your witnesses in the position of just saying that what they would have to say would be somewhat repetitious.

We will be glad to hear from you now, Mr. Nay.

STATEMENT OF PAUL NAY, JANE LEW, W. VA.

Mr. NAY. Mr. Chairman and gentlemen of the committee, I had already intended to insert my statement into the record, if permitted, because much of my testimony is repetitious. I am well aware of this. Consequently, you may use the filed statement, and I will be very brief in my remarks.

My name is Paul Nay, and I operate a farm at Jane Lew, W. Va., which is in the territory of the Clarksburg Production Credit Association. I am a member of that association and helped finance my farming operations by obtaining loans from it.

Also I am a member of the board of directors of the Federal Intermediate Credit Bank of Baltimore, and vice chairman of that board. We serve Pennsylvania, Maryland, Virginia, West Virginia, and Puerto Rico. These affiliations give me an opportunity to observe the operations, and the related problems, of the associations and the credit bank.

I am glad to have this opportunity to testify to the need for, and the desirability of, this legislation proposed by the Farm Credit Administration. Increasing farm production costs and the demand for larger quantities of food, with which I am well aware as a farmer, have resulted in requests for larger amounts of short- and intermediate-term credit to be provided by our production credit associations. The associations obtain their lending funds from the Federal intermediate credit banks. These banks are being called upon to discount an increasing volume of loans, which requires a corresponding increase in the bank's volume of debentures and other short-term borrowings, such borrowings are now limited by law to 12 times their capital and surplus. To meet the increasing demand for loans, the system needs additional capital and a more realistic ratio which will permit the capital of the credit banks to support a larger volume of loans.

A number of years ago, the PCA's throughout the Nation, with a few minor exceptions, completed the repayment of the Government capital which had been invested in them in the formative stages of their development. Partly as a result of purchase and partly by means of patronage distributions, the associations now own a substantial portion of the stock of the FICB's. Plans have been made for their systematic acquisition of the remaining stock, thereby permitting the Government capital now in the banks to be repaid. In the Baltimore district, with which I am most familiar, the PCA's have just purchased \$2 million of additional stock in the Federal Intermediate Credit Bank of Baltimore.

It would not be appropriate, nor in the best interest of our farm credit organizations in the long run, to endeavor to meet the FICB's capital needs by requesting additional Government capital; our aim continues to be in the opposite direction—complete farmer ownership of all of our farm credit organizations.

The legislation that has been requested is designed to help our short-term credit system (the Federal intermediate credit banks and production credit associations) help itself during this period of expansion. This would be accomplished in the following ways:

The proposed increase in the FICB's debt-to-capital ratio (from 12 to 1 to 20 to 1) would permit the capital to serve as a base for a substantially larger volume of loans. The proposed ratio is the same as that which, for many years, has applied to the Federal land banks by the Federal Farm Loan Act.

The change would be sound because the credit banks are not primary lenders but, instead, discount agricultural loans made by PCA's and other financing institutions. The notes are endorsed by such primary lenders. The production credit associations, which operate under the supervision of the Federal intermediate credit banks, have had a remarkable loss experience (less than one-tenth of 1 percent of the money they have loaned).

As a further precaution against losses resulting from catastrophe to one or more PCA's, a large percentage of the associations in each district participate in loss sharing plans. While the associations are restricted by law to debts equal to 10 times their paid-in and unimpaired capital and surplus, it is general practice for them to operate on a more conservative basis. The debt-to-capital ratio is about 7 to 1 in most of the associations in my district, and I understand that this is true generally in PCA's throughout the Nation. All of these factors minimize the risk of loss to the FICB's. Therefore, our district strongly urges liberalization of the banks' debt-to-capital ratio to 20 to 1, as proposed in this bill.

Financing institutions, other than PCA's, which discount agricultural loans with FICB's, receive participation certificates each year from distribution of the banks' earnings. We support the proposal that the law be changed to permit them to purchase participation certificates and thus also aid the credit banks in meeting their capital needs.

The other three provisions of the proposed legislation would not contribute directly to the solution of the capital problem; however, they are desirable and we urge they be enacted into law. One would allow the reserves which the credit banks have allocated to the PCA's in their respective districts over a period of years to be reallocated in order that they will be in proportion to the borrowings of the associations from the credit banks during the past 3 years. The capital stock owned by the associations in credit banks was similarly reallocated and it is equitable that both the stock and the reserves be owned by the individual PCA's in proportion to their borrowings.

Another recommended change would permit PCA's to sell capital notes to borrowers and others. This will make it possible to secure funds locally from persons who are not accustomed to buying FICB debentures or any other type of security.

The last recommended change would permit the Farm Credit Administration to issue regulations which would enlarge the basis upon which class B stock PCA's could be retired. This change would make the purchase of stock less objectionable to borrowers if it can be retired on payment of the loan under certain circumstances.

I sincerely believe that the changes recommended in this proposed legislation are needed and would be beneficial, and I certainly urge that the amendments be adopted.

Thank you.

The CHAIRMAN. Thank you, Mr. Nay. Are there any questions? If not, we will hear now from Mr. Homer Curtiss of Stockton, Ill.

STATEMENT OF HOMER CURTISS, ROUTE 1, STOCKTON, ILL.

Mr. CURTISS. Mr. Chairman and members of the committee. My name is Homer Curtiss. My home is Route 1, Stockton, Ill. I have been a farmer all of my life and now own and operate, with one of my sons, a 427-acre grain and dairy farm in northern Illinois.

I have been a director of the Farm Credit Board of St. Louis since 1953, and have had long service on the board of directors of the Blackhawk Production Credit Association of Freeport, Ill., as well as a number of other farm organizations.

As a farmer, I look on the farm credit system as an essential credit tool to help the farmer. Under today's conditions it is necessary for every farmer to have a dependable credit home. Most farm costs are going up fast while prices for farm products are going the other way. The purpose of this bill is to help our farm credit machinery operate more efficiently and at lower capital cost.

I strongly favor section 1(a), increasing the aggregate debt obligations issued by the bank from 12 to 20 times the capital and surplus of all such banks.

It is costing us too much to capitalize our system at both the production credit association and Federal intermediate credit bank level. By increasing the permitted discount ratio of the Federal intermediate credit bank to 20 to 1, we can cut down on some of the excess capital required in the system without risk to anyone, as the capital of the Federal intermediate banks and the production credit associations support the same loans, for the most part.

The Federal intermediate credit banks are banks of discount, not primary lenders. They are fully protected by the capital structure of the production credit associations and other discounting institutions, as well as the farmers' notes. Also the production credit associations and the other financing institutions are limited by law or regulation to 10 to 1 to capital ratio, or less.

Section 1(b) seems only fair as it will help put other financing institutions which use our system on a more equitable basis with production credit association in financing the discount agencies we both use, which are the Federal intermediate credit banks.

Section 1(c) is another way of seeing to it that the users of the system contribute fairly to the capitalization of the Federal intermediate credit bank. I strongly favor both 1(b) and 1(c) as a basis for strengthening capital of the bank and equalizing discounting institution responsibilities.

Section 2(a) has been needed by production credit association and the farmer for a long time. The Federal Land Banks have, and use this authority and the farmer appreciates it. This provision can be applied as needed on this point of retiring class B stock on payment of a loan. Farmers generally need their money and hate to wait for it after a loan is paid unless they plan to borrow back soon.

Section 2(b) will give farmers another method of getting capital for their credit system and also helping to capitalize it themselves on

a local basis as their finances permit. There has been a strong demand for this.

I thank you for this opportunity of presenting the viewpoint of a man whose income depends entirely on farming and who uses the farm credit system. Also, this represents the opinion of all the members of the Farm Credit Board of St. Louis which, in turn, is representative of the farmers of the great States of Arkansas, Missouri, and Illinois.

The CHAIRMAN. Thank you very much, Mr. Curtiss. There are a number of other members of the District Farm Credit Boards who are present. I think we have statements from all of them. Those that want to be heard, or have anything that they feel is unique that has not been presented, may make such presentations, but in all frankness I do not see any purpose in presenting the same testimony from a number of witnesses.

The chair will recognize each individual member, unless someone else especially wants to be heard, and we will ask each one of you if you favor this legislation, and you will have the opportunity to say that you do or do not. We have next as a witness Mr. J. Richards Nelson of Madison, Conn. Did you want to make a statement, Mr. Nelson?

STATEMENT OF J. RICHARDS NELSON, MADISON, CONN.

Mr. NELSON. Mr. Chairman and members of the committee.

I have filed a written statement.

The CHAIRMAN. Yes, you may file your written statement, and we will be glad to insert it in the record as a part of the record, and we will be glad to have you confirm now whether you favor this legislation?

Mr. NELSON. I do, sir. I favor it very strongly.

(The prepared statement submitted by Mr. Nelson reads in full as follows:)

STATEMENT OF J. RICHARDS NELSON, MADISON, CONN.

Mr. Chairman and Members of the Committee: I very much appreciate this opportunity to appear before you today. My name is J. Richards Nelson of Madison, Connecticut. My business is shellfish farming in Connecticut and New York. I belong to the Long Island Shellfish Farmers' Association of Long Island, New York. I am a past director of the former Providence, Rhode Island, Production Credit Association and a present borrower of the Southern New England Production Credit Association. I am presently Vice Chairman of the Farm Credit Board for the Springfield District which serves the farmers and their cooperatives in the six New England states, New York and New Jersey.

I sincerely believe that the Federal Intermediate Credit Bank of Springfield is a tremendous force for good for the agriculture of our area by serving as a source of lending funds to the Production Credit Associations and other financing institutions. Therefore, I favor whatever will continue or improve upon our ability to serve farmers. The proposed legislation will improve the opportunity for the Bank, the Associations and the other financing institutions to continue to provide effectively the money needs of farmers. This is the reason Congress put the Banks and the Associations in business, and I, for one, want to see that they have the necessary tools to continue that business. I would hate to see the day come when a farmer could not borrow from his Production Credit Association because inadequate loan funds were available.

I am pleased with the performance of the Federal Intermediate Credit Bank—Production Credit Association System. However, the demand for credit has grown sharply. This has created a strain on its capital structure and a concern for obtaining adequate loan funds. I feel that as a result of skilled people, strong reserves, excellent loss experience and the coming of age of our lending system,

we may safely increase the debt-to-capital limitation on the Banks from 12 to 1 to 20 to 1. It is this ratio which determines the amount of debentures which the Banks may sell to the investing public to obtain the funds for their lending and discounting operations. If I thought that this increase would cause a blowup in the system, I certainly would not be in favor of this change. As a spokesman both for the farmer lenders who make up the Farm Credit Board of Springfield and for the farmers who borrow from us, I only want changes which will strengthen, not weaken, Farm Credit. In my opinion, our legislative proposals will definitely strengthen Farm Credit's ability to serve farmers.

It is true that increased lending under the present 12 to 1 limitation could be accomplished by more capital being put into the Banks. Two primary ways exist to obtain this added capital—from the Government and from the Production Credit Associations. Increasing the investment of Government capital runs counter to the progress of the Banks toward retiring all of the Government capital they now have as soon as they may safely do so. If necessary and within their capabilities, the Springfield Bank in the future may have its Associations purchase more of its stock. However, the amount of stock which the Associations would have to buy to keep the Bank within the 12 to 1 ratio would place a major burden upon them and more seriously upon the individual farmers who own the Associations.

Part of the proposed Bill is to provide the Federal Intermediate Credit Banks with an additional source of capital. The financing institutions other than the Production Credit Associations which use the services of each Bank would be allowed to buy participation certificates of the Bank. This is toward consistency with the present law under which the Associations may acquire stock in the Bank beyond what they receive as patronage refunds.

The Farm Credit System has always prided itself on being a dependable source of credit in good times and bad. When it reaches the point that enough loan funds may not be available for the needs of farmers without placing undue pressure on capital, I must ask Congress for help—not for money but to remove a barrier to the most efficient use of farmer capital. I am afraid that without the passage of this legislation, a time may be at hand when a deserving farmer may not be able to obtain credit when he needs it most unless the Federal Intermediate Credit Banks' capital were increased in a manner inconsistent with the best interests of all. Toward this same objective of serving farmers is the proposal that a Production Credit Association be authorized to issue its capital notes for sale to borrowers and others. This would provide the Associations with an additional source of funds for lending and expenses and also would provide farmers with a means of investing surplus funds in their own credit business.

The present explosive demand for agricultural credit requires us to deal today with increasing the Banks' unnecessarily conservative debt-to-capital limitation and with the other related legislative proposals. Passage of this Bill will be Congress' way of saying that the Farm Credit System's performance thus far deserves the continuing confidence of Congress and adjustments as needed from time to time to permit maintaining a sound operation sensitive to the credit needs of a changing agriculture.

The CHAIRMAN. We next have Mr. C. B. FunderBurk of the Third Farm Credit District, Columbia, S.C.

STATEMENT OF C. B. FUNDERBURK, REPRESENTING THE THIRD FARM CREDIT DISTRICT

The CHAIRMAN. Do you favor this legislation?

Mr. FUNDERBURK. Mr. Chairman and members of the committee, I do; yes, I do.

The CHAIRMAN. We will make your statement a part of the record at this point.

Mr. FUNDERBURK. Thank you.

(The prepared statement submitted by Mr. FunderBurk reads in full as follows:)

STATEMENT OF C. B. FUNDERBURK, CHAIRMAN, BOARD OF DIRECTORS, THIRD FARM CREDIT DISTRICT, COLUMBIA, S.C.

Mr. Chairman and gentlemen of the Committee: My name is C. B. FunderBurk, of Atlanta, Georgia. I am Chairman of the Board of Directors of the Third Farm Credit District at Columbia, South Carolina. We serve the States of North and South Carolina, Georgia and Florida.

I should like also to tell you that for 33 years, from September 1933 to January 1966, I was Treasurer of Cotton Producers Association of Atlanta, Georgia, which is a farmer cooperative marketing and purchasing organization. In addition to that, I am the founder and still President of Cotton States Mutual Insurance Company and Cotton States Life and Health Insurance Company. All three of these organizations are farmer owned and controlled and serve the farmers in their efforts to make a living on their farms. I cite this merely to indicate that most of my business career has been devoted to aiding farmers.

My Board has designated me to appear before your committee today to ask your support of this pending legislation to amend the Farm Credit Act to permit the Federal Intermediate Credit Banks to increase their debt to capital ratio from the present ratio of 12 to 1 to a ratio of 20 to 1.

I am sure that you gentlemen understand the set-up of the Farm Credit System, but for the sake of clarity let's review it very briefly.

The nation is divided into 12 districts. Each district has a Federal Intermediate Credit Bank (abbreviated as FICB's or "credit banks"). These banks make no direct loans to farmers or ranchers. Instead, they accept discounted loans from Production Credit Associations (abbreviated PCA's) in their respective districts. These loans cover short term needs of farmers and ranchers.

Originally, the Federal Government provided the capitalization of the FICB's by buying their Class A Stock in the amount of \$125.7 million nationwide. The Third District, which I represent, has Class A Stock outstanding in the amount of \$15.5 million.

None of the FICB's have been able to retire the Class A Stock because through the years the demand for loans has been so great that they have been unable to generate enough capital from their earnings to do so. All of their earnings have, of necessity, been plowed back into loans to make available sufficient operating capital to the farmers.

Each district has a number of Production Credit Associations. Nationally, there are 459 such associations including 65 in our district. All of these were originally capitalized by the Government, but all of this capital has been retired by the PCA's. They were able to do this because they required farmer borrowers to purchase capital stock in their associations. This, plus the earnings on their own capital and patronage refund from FICB's, raised enough capital to pay out the Government. Therefore, the farmers own *all* of the capital stock of the PCA's in our district.

Now, let's examine the record of these operations. The Columbia FICB has loaned since its organization in 1923 \$5.6 billion while its losses in that period were \$1,623,000, or .00029%. All of this loss occurred in the period prior to 1933 when the PCA's were organized. No losses have occurred in the FICB since 1933.

The PCA's in our district have loaned \$3.3 billion since organization in 1933. Their losses have been \$2,328,000, or 7/100 of 1%.

We believe that our district is about on a par with all districts and we assert that this is a peerless record in the farm lending field and a great testimony to the management skills and practices which farmers have created in their Farm Credit structure.

Now, let's look at the future. The volume of credit extended to farmers in the Third District has increased 76.8 percent in the past five years. This, too, is about on a par with the national figures. Based upon projections from our agricultural colleges and farmers themselves, it appears that the volume of credit will perhaps double in the next ten years. There is considerable evidence that many lenders are pulling out of farm credit financing because they can use their capital more lucratively elsewhere. This increases the actual number of farmers who need financial help over and beyond the normal increase brought about by increasing cost of technological changes in farm equipment and the inflation that engulfs all of us.

While we have no desire to pre-empt the whole field of farm finance, we do have the duty and obligation under the law to help as many farmers as we can, provided they can meet the requirements. We are serving 90,000 in our district now and still they come—not only in numbers but each with increased demands. This is part of the struggle to keep this nation supplied with food and fibre.

Years of experience have proven that the FICB's cannot generate, internally, enough capital to meet the increasing demands for loans and repay the Government capital at the same time, even though we have at present a debt to capital ratio of 12 to 1. This repayment is required, and rightfully so, under the Farm Credit Act. We do not feel that we can possibly require the farmers to capitalize the FICB's when they have already capitalized their own PCA's in our district to the sum of \$72,621,000. This would be an impossible burden if the loan volume doubles in ten years as is anticipated.

We have made a serious study of this problem and have evolved a plan and a projection which we believe will retire the Government capital in five years in our district, but it is based on the assumption of your granting us the authority to maintain a debt to capital ratio of 20 to 1. This projection calls for repayment in annual equal payments which will be completed in 1973, at which time the debt peak will be \$664,300,000 with a capital base of \$36,857,000, which is a debt to capital ratio of 18.1 to 1.

When a higher debt to capital ratio is considered, there immediately arises the question, "Will not this weaken the credit structure of the banks in relation to the debenture buyers?" Our answer is "No, it will not, for these reasons:"

1. The soundness of a credit risk is based essentially on two factors:

(a) The individual farmers: Today they, in increasing numbers, are college trained, younger, and more technically proficient operators than were those of one or two generations past. They are also better financial managers.

(b) The amount of the loan in relation to the collateral: Our people have many years of training in weighing this factor and they are constantly re-schooled in their work. Our lifetime record of extremely low loss ratios in both our FICB's and PCA's attests the fact that we make only what we believe to be sound loans and we shall not change our rules in this respect.

2. The collateral which we hold doubtless has some cushion between its value and what we have loaned on it.

3. All of this collateral is pledged to the debenture buyers, in addition to the net worth of all the FICB's.

4. As a first line of defense behind the actual value of the collateral is the net worth of the PCA's. In our district this is further strengthened by a mutual assistance agreement among our 65 associations. The second line of defense is the net worth of our FICB.

5. Nationally, the PCA's and FICB's have accumulated and continue to accumulate reserves for losses which now aggregate many times the actual losses for our entire history.

6. Generally, balance sheets are judged, in part, by the ratio of its current assets to its current liabilities. A current ratio of 2 to 1 is considered an unusually good ratio. Not all corporations nor individuals can maintain it. At December 31, 1967, our FICB had a current ratio of 1.09 to 1. Our projections for 1973 indicate a current ratio of about the same as 1967. The reason for this low ratio in the FICB in comparison with the desirable ratio of 2 to 1 is that it borrows on a 9-month basis only, which places all its debt in current liabilities. However, our comparison of the 1967 and 1973 ratios prove that current portion of our balance sheet has not been weakened by the use of debt capital ratio of 20 to 1.

7. This matter of debt-capital ratio has been discussed many times with the security dealers through whom we sell the debentures. They have stated repeatedly that they see no danger in raising the ratio to 20 to 1, because of the financial strength of our system and our historical success in management.

8. The Federal Land Banks have, since their inception in 1917, had a debt to capital ratio of 20 to 1. This enabled them to pay out the Government capital in 30 years. They never were accused of having a weak capital structure nor did any debenture holder ever suffer a loss or even raise a question about their security. They have been 100 percent owned by the farmer-members since 1947 and are steadily increasing the capital and service to themselves and their neighbors.

Comparing the character of the Federal Land Bank with that of the FICB, the Land Bank is a primary lender (making loans directly to the borrower) whereas the FICB is a secondary lender and has the financial strength of the PCA's between it and a possible loss. To that extent, it would have greater strength than the Land Bank and thus offers greater security to the debenture buyer, which should overcome any possible suggestion of fearing the 20 to 1 ratio in the FICB.

The next question that arises is, "Will this debt to capital ratio of 20 to 1 jeopardize the Government capital?"

We believe that the same answers that we gave with respect to the debenture holders would apply here, except, of course, that Government capital is the final

protection to the debenture holder. We cannot imagine a situation so cataclysmic as to wash out this capital. Speaking personally for a moment, if I may, I think the Government investment in this capital stock is safer and far more likely to be repaid than some debts receivable from some of our "friends" abroad.

Gentlemen, let's consider some alternatives to passage of this proposed amendment. We could:

1. Curtail our loans to keep within the present 12 to 1 ratio. Considering our growth in the last five to ten years and the prospective demands of the next ten years, this approach would impose a terrific hardship on some fine people who will desperately need help.

2. We could demand that farmers put some ten million dollars into the capital account. Where they would get it, we don't know. It could have the adverse effect of their increasing their borrowings so that they could get their capital contribution out of the loan proceeds.

3. We could increase our interest rates so as to build a larger surplus out of which to repay the Government capital. Here again we would impose another burden on people who are already heavily burdened.

The other provisions of the proposed legislation are sound and we believe the advantages are obvious; therefore, I shall not take your time in discussing them.

In conclusion, Gentlemen, let me say that the farmers of the country have proven their support of the cooperative Farm Credit System and their willingness to capitalize it on a sound basis, and the production credit associations in our four-state area, without exception, are in full support of this proposed legislation.

Thank you so much for hearing us.

The CHAIRMAN. The next is Mr. Samuel S. Studebaker of Tipp City, Ohio.

STATEMENT OF SAMUEL S. STUDEBAKER, TIPP CITY, OHIO

The CHAIRMAN. I take it that you favor this legislation?

Mr. STUDEBAKER. Mr. Chairman and members of the committee, I do.

There is just one point that I do not think has been emphasized on this matter of the rapid conversion of the stock in the PCA's, and that is in the matter of settling an estate. One loan is paid up by the estate and the stock is listed with the PCA and if the PCA is in a period of retraction of loans it has a large block of stock listed and it takes a long time to get the estate stock up on top so that it can be paid off. I think if we had the opportunity of applying these stocks as the last payment on the loan, we could make more rapid settlement of the estates.

The CHAIRMAN. Thank you.

Your entire statement will be made a part of the record at this point.

(The prepared statement submitted by Mr. Studebaker reads in full as follows:)

STATEMENT OF SAMUEL S. STUDEBAKER, TIPP CITY, OHIO

I am Samuel S. Studebaker, a dairy farmer from Tipp City, Ohio, a member and director of the Miami Valley Production Credit Association, and a member of the District Board of the Farm Credit Banks of Louisville, elected to that position by the production credit associations of the district.

We wish to express our support for certain amendments to the Federal Farm Loan Act and the Farm Credit Act of 1933, as amended, to improve the capitalization of Federal intermediate credit banks and production credit associations, and for other purposes, such amendments being incorporated in Senate Bill 3292 and House Bill 16674.

Legislation making it possible for the production credit associations to purchase and eventually own the twelve Federal intermediate credit banks was

passed in 1956, and was another important milestone in developing the Farm Credit System into its present constructive program through which the farmers and ranchers of this country are assured a dependable source of credit at reasonable cost and on terms to fit the special needs of agriculture.

When the 1956 legislation was passed, it was impossible to foresee the tremendous growth in demand for production credit by the farmers of the country. In the Louisville District which I represent, the amount of credit extended by the Federal Intermediate Credit Bank of Louisville increased from \$208,380,066 in 1956 to a total of \$718,198,192 in 1967, or an increase of 345 percent. Thus the program of farmer ownership of the bank, which was hailed in 1956 as being easily attainable, became increasingly difficult to attain because of the tremendous amount of capital which the farmers would have been forced to provide if the government capital were to be retired as planned.

As a result, even though the PCAs of the district (and thus their farmer members) increased their investment in the bank through ownership of class B stock and reserves by over \$15,000,000, it was still necessary to secure from the Revolving Fund a total of \$11,600,000 to maintain the capital needed under the 10-to-1 ratio that was in effect. (Amended to 12 to 1 in 1965.)

During the past few years it has become increasingly evident that if the Federal intermediate credit banks are to attain the status of full ownership, and thus return the government capital as contemplated in the 1956 legislation, then a more realistic position must be taken on the required capital-to-debt ratio of these banks. Thus, we strongly urge the proposed change to 20 to 1.

Another proposal in this legislation applies to OFIs (other financial institutions discounting with the Federal intermediate credit banks).

In order to provide for equitable treatment and equitable distribution of the overall task of capitalizing their Federal intermediate credit banks, this legislation provides that other financial institutions using the resources of the banks shall share in the capitalization requirements through making the same basic requirements apply to participation certificates as now apply to PCA-owned class B stock in the bank.

The original Farm Credit Act of 1933 providing for the establishment of the production credit associations contained certain restrictions on the cancellation or retirement of member-owned class B stock. These restrictions have been found, in practical application, to work a hardship on certain farmer members, and the request is being made for a liberalization of this provision through permitting the Farm Credit Administration to prescribe authorization for the cancellation and retirement of class B stock.

A further amendment which we strongly support is that making it permissive, under rules and regulations prescribed by the Farm Credit Administration, for PCAs to issue in limited amounts capital notes for sale to borrowers and others. This is considered most desirable in order for production credit associations to better serve the needs of their farmers, and to provide for greater flexibility in providing loanable funds.

We commend this committee for its understanding and leadership in farm credit legislation, and appreciate this opportunity to make a statement in support of the present amendments.

This proposed legislation has been given extensive study, not only as to the fiscal soundness of the proposal, but also as to its acceptability by the farmer owners of the production credit associations and other financial institutions that use the banks. We, in the Fourth Farm Credit District strongly support the proposed legislation, and urge that it be given favorable consideration.

The CHAIRMAN. Now, we have next Mr. George E. Hoffpauir, of Morse, La.

STATEMENT OF GEORGE E. HOFFPAUIR, MORSE, LA.

Mr. HOFFPAUIR. Mr. Chairman and members of the committee.

I favor the legislation, and I would like to submit my statement for the record.

The CHAIRMAN. Thank you, sir. It will be made a part of the record.

(The prepared statement submitted by Mr. Hoffpauir reads in full as follows:)

STATEMENT OF GEORGE E. HOFFPAUIR, MORSE, LA.

I am George E. Hoffpauir of Morse, Louisiana, where I am engaged in operation of a farm producing rice, soybeans and cattle. I am a member of the Board of Directors of the Fifth Farm Credit District comprising the states of Alabama, Louisiana and Mississippi. My purpose here is to attempt to point out the urgent necessity for favorable consideration of the bills now pending before you that affect the Federal Intermediate Credit Bank of New Orleans and the production credit associations of the New Orleans District.

AMENDMENT TO INCREASE THE PERMISSIBLE DEBT TO CAPITAL RATIO TO 20 TO 1
INSTEAD OF THE PRESENT 12 TO 1 RATIO

Sec. 1(a). The discounting of loans by the Federal Intermediate Credit Banks for production credit associations and other financing organizations have rapidly increased during the past two years. This increase in loans discounted in my district was due in part to plans of many producers to plant 95% of their cotton allotment as compared to 65% that was planted last year. In addition, the rice acreage allotment has been increased by 20% for the year 1968. The continual increase in costs of production of crops and livestock has also contributed to the increase in loans.

The loans discounted by the Federal Intermediate Credit Bank and loans made by production credit associations and other financing institutions are for productive purposes and are not made for speculative reasons or inflationary purposes.

The present law provides "That the aggregate amount of the outstanding debentures and similar obligations issued by the Federal Intermediate Credit Banks shall not exceed twelve times the surplus and paid-in capital of all such banks." This limitation (12 to 1) is unnecessarily conservative and too restrictive if the credit banks are to continue in the future to meet the increasing demands for agricultural financing without calling on the Government for more capital and also returning within a reasonable time the Government capital they now have. The production credit associations will be called upon to purchase additional capital stock of the banks as part of the program to return their Government capital within a reasonable time.

The proposed amendment substitutes 20 to 1 for the present 12 to 1 debt to capital ratio.

This amendment is deemed necessary and considered justified by the financial strength of the credit banks, and the associations. The Federal Intermediate Credit banks could not suffer any loss in connection with its financing unless the production credit association became insolvent. During the past 33 years, the losses experienced by associations have amounted to .08 of one percent of the total cash advanced to farmers and cattlemen. During this period the Federal Intermediate Credit Banks have sustained no losses on loans discounted for production credit associations. As an added protection to the capital and surplus of the production credit associations, reserves for bad debts have been accumulated in excess of 86 million dollars.

The associations at present have a debt-to-capital limitation of 10 times the paid-in and unimpaired capital and surplus. At the present time the associations are operating at about a 7 to 1 debt-to-capital ratio.

With proper recognition of the above factors, a change from the present 12 to 1 debt-to-capital ratio to 20 to 1 seems justified.

PARTICIPATION CERTIFICATES IN ADDITION TO THOSE ISSUED IN PAYMENT OF
PATRONAGE REFUNDS

Sec. 1(b) At present, participation certificates are issued in payment of patronage refunds to financing institutions other than production credit associations that use the services of the Federal Intermediate Credit Bank. Production credit associations are paid patronage refunds in capital stock of the bank, and such associations have, in the past, and will, in the future, be required to purchase additional capital stock in the bank. The proposed amendment will permit other financing institutions to purchase participation certificates in the bank and thereby share in the capitalization of the banks and the benefits therefrom, along with production credit associations. This amendment would provide the Credit banks with an additional source of capital.

REESTABLISH THE HOLDINGS OF THE PRODUCTION CREDIT ASSOCIATIONS IN THE ALLOCATED LEGAL RESERVE ACCOUNT OF THE BANK IN SUBSTANTIALLY THE SAME PROPORTION AS ARE THEIR HOLDINGS OF CLASS B STOCK

Sec. 1(c) At the present time the relative amounts of Class B stock owned in the Federal Intermediate Credit Bank by production credit associations may be adjusted to reestablish the amount of such Class B stock owned by each association in proportion to the average indebtedness of each association to the bank during the immediately preceding three years.

The present amendment would authorize the reestablishment of amounts in the reserve account that are allocated to production credit associations to be in substantially the same proportion as the holdings of Class B stock.

THIS AMENDMENT WOULD MAKE IT POSSIBLE TO AUTHORIZE RETIREMENT OF THE STOCK OWNED BY AN ASSOCIATION BORROWER UPON REPAYMENT OF THE LOAN

Sec. 2(a) Each borrower from the production credit association is required to own Class B stock at the time the loan is made in an amount equal to five dollars for one hundred dollars or fraction thereof of amount of loan. The present law states that Class B stock of a production credit association owned by a borrower from the association "shall not be cancelled or retired upon payment of the loan." The proposed amendment would place the authority in the Farm Credit Administration to prescribe rules and regulations under which stock could be retired upon payment of the loan in instances where such retirement is in the interest of the borrower and the association. This amendment is necessary and would add flexibility to the retirement of Class B stock owned by the production credit association borrowers.

ASSOCIATIONS' AUTHORITY TO BORROW FROM INVESTORS BY THE SALE OF CAPITAL NOTES

Sec. 2 (b) At the present time, production credit associations are authorized to borrow from and rediscount paper with the Federal Intermediate Credit Banks. The proposed amendment would authorize a production credit association to borrow from investors generally by the sale of its capital notes. The new authority, however, would be subject to rules and regulations prescribed by the Farm Credit Administration. Such capital notes are to be considered along with other liabilities of the association, and may not exceed ten times the capital and surplus of the association.

The CHAIRMAN. We next have Mr. Ben Bement, Jr., of Dowagiac, Mich.

STATEMENT OF BENJAMIN F. BEMENT, JR., DOWAGIAC, MICH.

Mr. BEMENT. Mr. Chairman and members of the committee, I have filed with you a written statement that I would like to have made a part of the record, and I strongly urge support of this proposed legislation.

Thank you.

The CHAIRMAN. Thank you.

Your statement will be made a part of the record at this point.

(The prepared statement submitted by Mr. Bement reads in full as follows:)

STATEMENT OF BENJAMIN F. BEMENT, JR., DOWAGIAC, MICH.

I am Ben Bement, Jr., a grain and livestock farmer from Dowagiac, Michigan, seventeen years a member-borrower of my Production Credit Association. Presently, I am a member of the Seventh District Farm Credit Board.

I appear here today representing approximately 69,000 farmers and ranchers from the States of North Dakota, Minnesota, Wisconsin and Michigan, who are stockholders in Production Credit Associations, in support of this proposed legislation which will allow a debt-to-capital ratio of 20 to 1 for the twelve Federal Intermediate Credit Banks.

The farmer needs this bill or else he will pay the burden of unnecessary capitalization. This legislation is justified by the present financial strength of the System. Those of us who may survive in agriculture are increasing in size, crop and livestock production. We are substituting capital for labor, and are making other necessary farm and equipment improvements. With all this, we face the need for larger sums of operating money under somewhat limited restrictions of its use, and even the possibility of an insufficient supply of capital.

In addition to the present high cost of borrowed money, I invest \$5.00 for each \$100.00 borrowed. This 5 percent B stock investment helps meet my association's legal capital reserve requirement of 10 to 1. Also, many Production Credit Association borrowers have further invested in A stock.

During times of rapid association growth, such as in the past few years, it is difficult to generate enough earnings to meet the capital reserve requirements. At this point, may we keep in mind Production Credit Associations are the primary lenders and are required to maintain a sizable reserve for losses. Production Credit Associations have joined together either in a loss-sharing program or participation loan agreements, or both. Since organization in the Seventh District, Production Credit Associations have had six one-hundredths of one percent losses, with the Federal Intermediate Credit Bank having no losses since 1933.

Without the proposed 20 to 1 ratio, the Federal Intermediate Credit Banks will have to assess larger amounts from the Production Credit Associations, and then, in turn, the Production Credit Associations will have to turn to the farmer-borrowers for funds further in excess of those I have already mentioned. I sincerely believe that the 69,000 farmers and ranchers in my district need any relief, support, and consideration possible within our power to provide, rather than ask farmer-members to invest additional money to capitalize Production Credit Associations and Federal Intermediate Credit Banks when not necessary and place additional financial burden on us.

I, therefore, strongly support and urge your favorable consideration on the passage of this legislation.

Thank you.

The CHAIRMAN. We have next Mr. Guido Schroeder, of West Bend, Wis.

STATEMENT OF GUIDO SCHROEDER, WEST BEND, WIS.

Mr. SCHROEDER. Mr. Chairman and gentlemen of the committee.

I would like to have my statement filed for incorporation in the record and at this time I would like to say that I have been connected with the Farm Credit Board for a good many years as a farmer, as proven by our records, and I hope that the committee will see fit to endorse this legislation.

The CHAIRMAN. Thank you.

Your statement will be made a part of the record at this point.

(The prepared statement submitted by Mr. Schroeder reads in full as follows:)

STATEMENT OF GUIDO SCHROEDER, WEST BEND, WIS.

My name is Guido Schroeder a dairy farmer from West Bend, Wisconsin, Route 1. I am President of the Juneau Production Credit Association serving 1364 farmers in six counties. Also I am a Director of the Seventh District Federal Intermediate Credit Bank of St. Paul by virtue of election by 68,880 Farmers and Ranchers who use the services of the Bank through their local Production Credit Associations as the primary lenders.

The Production Credit Associations are the primary lenders in our System and are required to maintain sound financial structures. Further, they are required to maintain a sizeable reserve for losses. In the Seventh District, as of December 31, 1967, this amounted to \$11,387,000. The Production Credit Associations of the Seventh District have joined in a program of sharing of losses, thereby spreading the risk of their lending businesses. The loss ratio in the District since organization represents a little under $\frac{1}{100}$ of one percent of the total cash advances of \$3,144,000,000.

A major reason for having a ratio requirement should be as a protection against loss for investors and stockholders and based on the loss experience and the probable future losses, the 20 to 1 ratio for Federal Intermediate Credit Banks is adequate.

Because of the facts already stated, plus my own knowledge of the lending policies of Production Credit Associations, I do not believe that a change in the Federal Intermediate Credit Banks debt to capital ratio would affect the debenture market. This is an important point as I would not support any change which could increase further the cost of money to the farmers and ranchers in my District.

As the change in ratio requirement would not adversely affect the ability of the System to absorb reasonable losses, nor would it affect the cost of money, I, therefore, support as strongly as possible the passage of this legislation rather than ask farmer-members to invest additional money to capitalize PCAs and FICBs when it is not necessary and would, in fact, put an additional financial burden on farmer-members.

There are two objectives which I have supported since the beginning of the PCA-FICB System:

1. To provide short and intermediate-term credit on a sound, dependable and constructive basis to qualified farmers and ranchers.

2. To build and maintain a strong independent financial structure which will insure a dependable source of money to meet the credit needs of responsible farmers and ranchers and also provide the necessary protection to our investors.

The passage of the proposed legislation complements these two important continuing objectives. On behalf of the nearly 69,000 members in my District I urge favorable consideration.

The CHAIRMAN. We next have Mr. James Hendry, Lost Cabin, Wyo.

STATEMENT OF JAMES HENDRY, LOST CABIN, WYO.

Mr. HENDRY. Mr. Chairman and members of the committee, I endorse this legislation, and I ask that my statement, which has been submitted be made a part of the record.

The CHAIRMAN. It will be made a part of the record, sir.

Thank you.

(The prepared statement of James Hendry reads in full as follows:)

STATEMENT OF JAMES D. HENDRY, LOST CABIN, WYO.

My name is James D. Hendry. I own and operate a cattle and sheep ranch near Lost Cabin in the central part of Wyoming. I appear before this committee in support of HR 16674, both as an individual and as a director of the Farm Credit Banks of Omaha, serving farmers and ranchers in Iowa, South Dakota, Nebraska, and Wyoming.

At the turn of the century my father migrated from Scotland because of a promise that in America he could own his own land. After years as a sheepherder and tenant rancher, he bought the nucleus of the ranch on which I was born and which I still operate. Had it not been for the Federal Intermediate Credit Bank and the production credit system, we would have lost this ranch some 30 years ago, because there was no private money available in my area at any cost. My father became a member of the Wyoming Production Credit Association shortly after it was organized in 1934, and he or I after him have been members ever since. I give you this background to show you my vital interest and concern in the continuance of this source of credit, and I assure you that I would recommend nothing that I did not firmly believe was for the best interests of the Farm Credit System and the farmers and ranchers.

Among other provisions, HR 16674 would increase the statutory debt-to-capital limitation in the 12 Federal Intermediate credit banks from the present 12 to 1 ratio to a 20 to 1 ratio. In order to conserve time I will confine my remarks to this phase of the bill. Not only do I believe this increase to be sound, but I also believe such action is essential in order to assure the farm and ranch operators in my district continued access to funds through the Federal Intermediate Credit Bank and production credit associations.

Last year \$700 million of such credit was extended to more than 20,000 operators in our four-state district. It is therefore, evident that this service is a very important factor in livestock and crop production.

The rising cost of farm machinery, the increased use of fertilizers and insecticides and, whether good or bad, the growing need for farm consolidations to absorb these mounting costs, have contributed to an increase in the demand for agricultural credit in recent years. This demand will undoubtedly continue to expand during coming years. The volume of loans and discounts outstanding in the Federal Intermediate Credit Bank of Omaha has climbed from \$60 million in 1956 to \$375 million at the present time. However, the capital structure of the Bank has not kept pace with this growth.

Although \$6 million additional government capital was invested in the Omaha Bank from 1961 to 1964, the debt-to-capital ratio has increased to 14.2 to 1 at the present time. Since the statutory limitation of 12 to 1 is applicable to the combined system of 12 banks, up to now the Omaha Bank has benefited from the lower ratio of other credit banks whose growth until recently has not been as rapid. The system ratio will probably reach the statutory limit within the next few months. When this happens, the Omaha Bank would have to restrict its lending or require the 40 production credit associations in our district to purchase possibly as much as \$7 million additional stock in the Bank. To supply this additional capital will put a considerable strain on the resources of the associations, and on the farmers and ranchers who own them. The Wyoming Production Credit Association, of which I am also a director, would be required to purchase \$630,000 of such stock.

The credit banks were established in 1923 with a limitation on borrowings of 10 times their net worth. This limitation was subsequently increased to the present 12 to 1. This is unrealistic in view of certain protective features which are now operative in the production credit system. All of the loans and discounts of the banks are backed with full recourse against the production credit associations and other financing institutions which make the loans to the farmers and ranchers. Before a bank could suffer any loss on such financing, it would be necessary that the endorsing institutions become insolvent. This possibility is minimized by the fact that all 40 production credit associations in our district (and this is also the case in other districts) have substantial reserves for losses and have entered into a mutual loss sharing agreement whereby all of them would share excessive losses incurred by an individual association. The banks have sustained losses of less than one-hundredth of one percent of the amount loaned since they were organized in 1923, and have had no losses on loans made by the PCAs since they came into being in 1934.

Therefore, we believe that the limitation presently imposed on the Federal intermediate credit bank system is unnecessarily conservative, and could soon restrict the lending funds available to agriculture.

The provisions of the subject bill are proposed in order that the Farm Credit System may meet the demands of modern agriculture, which is requiring constantly increasing amounts of credit.

I respectfully request that you extend favorable consideration to H.R. 16674.

The CHAIRMAN. We next have Mr. Lyle L. Hague, of Cherokee, Okla.

STATEMENT OF LYLE L. HAGUE, CHEROKEE, OKLA.

Mr. HAGUE. Mr. Chairman and members of the committee. I have filed a statement which I should like to have made a part of the record. I have no other comment than to say that we need this now.

Thank you.

The CHAIRMAN. Thank you.

We will make your statement a part of the record.

(The prepared statement submitted by Mr. Hague reads in full as follows:)

STATEMENT OF LYLE L. HAGUE, MEMBER, NINTH FARM CREDIT DISTRICT BOARD

My name is Lyle L. Hague of Cherokee, Oklahoma. I have spent my entire lifetime as a farmer and stockman in this community.

I was a charter member and have served on the board of directors of the Enid Production Credit Association of Enid, Oklahoma, since its organization in 1934. I am presently serving as president of that association.

For more than 12 years I have been a member of the Ninth Farm Credit District Board, having been elected to this position for five consecutive terms by the production credit associations of this district. I am presently Chairman of that board.

My other business experience includes approximately 12 years as an appointed member of the Federal Reserve Board of the Tenth Federal Reserve District.

Previous testimony before your Committee has outlined the changes in existing law which are proposed by this legislation and indicated the developments in the FICB-PCA System which have brought about the need for the changes proposed.

The increasing demands for capital which are pressing on all agricultural operators and the unfavorable net income position of farmers and ranchers makes it imperative that all organizations serving farmers operate as efficiently as possible. Among other things, the provisions of this bill will, by increasing the permitted liability-to-capital ratio of the Federal intermediate credit banks, utilize more efficiently the farmer invested capital in the FICB-PCA System.

The rapidly rising credit requirements of farmers, caused in part by low net income and operating losses, create the need for additional capital in the credit banks and the production credit associations. Under present policy, the burden of capitalizing growth in both of these organizations is upon the farmer-user. Unfortunately, for the reasons mentioned above, they must provide this capital largely by increasing their own capital debt.

The higher ratio cannot conceivably expose the institutions, the investors or to farmer owners of these organizations to undue risk. This is due both to the remaining capitalization in the banks required by the proposed ratio, the maximum ratios of the production credit associations, and their reserves for losses and risk-sharing arrangements.

One proposed change will permit other financing institutions to make direct contributions to the banks' capital structure. This will make it possible for all users of the banks to contribute to their capital in direct proportion to their use of the banks' facilities. Officials of other financing institutions using the Federal Intermediate Credit Bank of Wichita have indicated their willingness to make such contributions and agree that the proposed arrangement is equitable.

The proposed provision to permit reallocation of the banks' legal reserve accounts will provide and maintain full proportionate PCA ownership of the banks' capital components owned by them. The ability to restore proportionate ownership of class B stock in the banks by the associations exists in present law. This provision will bring about fairness and consistency.

The provision to make the circumstances under which class B stock in a production credit association may be retired and canceled subject to rules and regulations of the Farm Credit Administration, will facilitate the maintenance of the principle of proportionate ownership of capital stock in the associations by their borrowing members. The present provisions for the retirement of class B stock have, at times, forced members who might be unwilling or financially unable to retain such investment to do so. It is not believed that an association board of directors would approve retirement and cancellation of a member's stock except when the capital structure of the association, related to its needs, would be adequate after such retirement. It is further anticipated that the district boards and the Farm Credit Administration, both of whom would be establishing policy or making rules and regulations relating to such retirement, would do so in such manner that the financial position of each association would be fully safeguarded.

The provision to permit production credit associations to issue capital notes would provide for production credit associations an additional source of senior capital of a type now available to some other financial institutions. It would also permit the association to comply with requests frequently made by members and other local investors that an interest bearing investment in the local association be made available. While this is expected to provide only a limited amount of additional lending funds, it would strengthen the local support of the production credit association.

I believe this entire proposal should be enacted by the Congress at the earliest possible date. The increase in the permitted ratio of the credit banks is particularly urgent. Some of the credit banks have already found it necessary to

assess production credit associations for additional cash investment in their class B stock. This is an added burden upon farmers and ranchers. Prompt action might eliminate need for further assessments to support volume growth.

The record of the Farm Credit System, including the production credit associations and the Federal intermediate credit banks, indicates that they have attempted to continuously adapt their services to the changing needs of their agricultural producer owners. This has been necessary in order to keep the institutions abreast of the rapid changes in agriculture of which members of your committee are fully aware. The proposed legislation represents another step in the process of keeping the associations and the Federal intermediate credit banks strong, useful, and in a position to fulfill their responsibility for providing a sound and dependable source of short- and intermediate-term credit to the farmers and stockmen of this country.

The CHAIRMAN. We next have Mr. E. Riddell Lage, chairman, Farm Credit Board of Spokane.

STATEMENT OF E. RIDDELL LAGE, CHAIRMAN, FARM CREDIT BOARD OF SPOKANE

Mr. LAGE. Mr. Chairman and members of the committee, we heartily endorse this legislation. And we appreciate very much the opportunity to appear before you today. We thank you for your courtesy in helping us to clear this up so that we could come to this hearing and take part in the Senate hearing tomorrow.

The CHAIRMAN. Thank you very much.

Your statement will be made a part of the record.

(The prepared statement submitted by Mr. Lage reads in full as follows:)

STATEMENT OF E. RIDDELL LAGE, CHAIRMAN, FARM CREDIT BOARD OF SPOKANE

Mr. Chairman and gentlemen of the committee, my name is E. Riddell Lage. I am the principal stockholder in a family corporation known as Lage Orchards, Inc., which owns and operates an orchard and packing plant at Hood River, Oregon. I am a member and borrower of the Mid-Columbia Production Credit Association, The Dalles, Oregon and of the Federal Lank Bank of Spokane. I am a director and president of the Mid-Columbia Production Credit Association. I am chairman of the board of directors of the three Farm Credit Banks of Spokane. I have been elected to this board by the Production Credit Associations in my district.

The district I represent is the Twelfth Farm Credit District comprising the States of Alaska, Idaho, Montana, Oregon and Washington. I greatly appreciate this opportunity to appear before your Committee and express the views of myself, my fellow directors and constituents.

We consider passage of HR 16674 of paramount importance to the Federal Intermediate Credit Bank and Production Credit Association Systems and to the more than 21,000 Production Credit Association member-stockholders as well as potential new members in our district.

We heartily endorse and recommend passage of HR 16674 in its entirety, as being in the best interests of agriculture as a whole. In the interest of brevity, I will confine my remarks to the section of the bill pertaining to the debt-to-capital ratio which is of primary importance.

This section increases the maximum debt-to-capital ratio of the Federal intermediate credit banks from 12 to 1 to 20 to 1. In our opinion this increase is necessary and justified for the following reasons:

1. It will enable the banks to make more effective use of their present capital structures, a substantial portion of which has been derived from production credit associations and their members, under directives of the Congress as expressed in the Farm Credit Acts of 1953 and 1956.

2. This amendment will not jeopardize the sound financial condition of the banks.

3. It will enable the banks to generate the additional capital needed to support anticipated growth in credit requirements of PCA present and prospective members, at minimum cost to or investment by such members.

4. It will facilitate and expedite the present plans which have been developed by each Federal intermediate credit bank for orderly retirement of the Government's capital investment in the Banks.

At June 30, 1967, the close of the last fiscal year, the capital structure of the Federal Intermediate Credit Bank of Spokane was as follows:

Capital stock and participation certificates:	
Class A—U.S. Government-----	\$5, 645, 530. 00
Class B—Production Credit Associations-----	7, 077, 040. 00
Participation certificates—Other financing institutions-----	30, 360. 00
<hr/>	<hr/>
Total -----	12, 752, 930. 00
Surplus—Reserved -----	5, 889, 724. 77
Legal reserve (allocated to PCA's and other financing institutions) -----	2, 529, 761. 44
<hr/>	<hr/>
Total capital-----	21, 172, 416. 21
Debentures and notes payable, plus accrued interest-----	221, 745, 336. 48
Ratio of debt to capital-----	10.49 to 1

By the end of the current fiscal year, June 30, 1968, it is anticipated that the debt-to-capital ratio of the Spokane Bank will be crowding the present 12 to 1 legal limitation.

In the 44-year history of the Spokane Bank, it has sustained net credit losses of \$1,598,218.70 (all sustained prior to 1933), or only .03% on \$5.9 billion in credit extended from organization through June 30, 1967. This loss record demonstrates the stability of the Bank, and its ability to support a large debt structure in relationship to capital, with negligible risk to investors in its debt instruments.

Before the Bank could suffer any loss on its financing of the Production Credit Associations in its district, which represents over 95% of its financing, it would be necessary that one or more of the associations become insolvent. However, this is well guarded against by the following factors:

1. Liabilities of each association may not exceed 10 times the paid-in and unimpaired capital and surplus of the association. (12 U.S.C. 1032). Actually, the associations generally are currently operating within a 7 to 1 debt-to-capital ratio, at seasonal peaks.

2. The net losses of the PCAs in the Spokane District aggregated \$1.4 million, or only .04% of the \$3.6 billion cash advanced from organization to December 31, 1967.

3. The associations in the Spokane District have capital structures and reserves for losses aggregating \$50.8 million, to support loans outstanding averaging \$228 million, during calendar year 1967.

4. All associations in the Spokane District have entered into a mutual loss sharing agreement, under the terms of which excessive credit losses by one association will be made up by contributions from the other associations. Thus, the collective financial resources of the associations in the Spokane District serve to insulate the Bank from credit losses. To all intents and purposes this is complete protection from loss to the Bank except under conditions of total disaster.

The Bank and the associations are committed to the principle of generating, from retained net earnings or direct investment, the additional capital that will be needed (1) to support the steadily increasing credit requirements of present and prospective PCA members, and (2) to accomplish orderly retirement of the balance of Government capital in the Bank, in accordance with a plan approved by FCA. Irrespective of the method(s) by which this capital will be generated, it must come from the users of the system. They have accepted their responsibility to capitalize the associations and the Bank. Management, in turn, has the responsibility to use such capital with maximum effectiveness, consistent with the law and sound business practices.

Interest rates and other costs to farmers are currently at historic highs. Anything that can be done legitimately to reduce the cost and investment required to operate the system will be of significant benefit to these people and to the agricultural industry generally. The foregoing representations, in our opinion, support the proposition that a larger debt-to-capital relationship than that permitted under existing law will not jeopardize the sound financial condition of the banks nor the safety of their debt instruments, and will facilitate orderly growth and service to farmers and ranchers.

I am convinced that this bill will be for the ultimate good of agriculture. The other members of my board concur with me. Thank you.

The CHAIRMAN. I have before me a statement dated April 29, 1968 in the form of a letter from Mr. Richard T. O'Connell of the National Council of Farmer Cooperatives which he asks be inserted into the record, and, without objection, it will be inserted into the record at this point.

Incidentally, the statement indicates that he is in favor of the legislation.

(The letter dated April 29, 1968 follows:)

NATIONAL COUNCIL OF FARMER COOPERATIVES,
Washington, D.C., April 29, 1968.

HON. W. R. POAGE,
Chairman, Committee on Agriculture,
House of Representatives,
Washington, D.C.

DEAR CHAIRMAN POAGE: The National Council of Farmer Cooperatives urges the passage of H.R. 16674.

The amendments contained in H.R. 16674 will act to improve credit for farmers, reduce the dependency on the Federal Government for additional funds from the revolving fund, and avoid pressing farmer-owned Production Credit Associations for additional capital stock purchases in the Federal Intermediate Credit Banks.

The most significant portion of this measure is the increasing of the debt-to-capital ratio of the Federal Intermediate Credit Banks from 12 to 1 to 20 to 1. The Federal Intermediate Credit Banks are now approaching their legal debt-to-capital limitations while the need for farmer credit steadily increases. To enable the Federal Intermediate Credit Banks to expand credit to farmers, either they will be required to seek additional Government capital from the revolving fund or require additional capital stock purchases from the farmer-owned Production Credit Associations.

We do not believe either alternative is desirable or necessary.

It is not desirable because it delays the time when the banks of the Farm Credit Administration will retire Government capital. We do not believe it is necessary because the stability of the Production Credit Associations has not been impaired in previous changes in the debt-to-capital ratios. Further adequate funds have been set aside for bad debt losses and the historic bad debt losses through the Production Credit Associations-Federal Intermediate Credit Banks relationship have been miniscule.

One element frequently overlooked in discussing the growing credit needs of farmers is the availability of funds from other sources. This is best reflected in a recent statement by Mr. Darryl R. Francis, President, Federal Reserve Bank of St. Louis. He said, "Some banks are in low savings and high credit demand areas. Since loanable funds of banks are generally obtained locally, these banks may not be able to meet their farm credit requests at going rates."¹

We believe this statement accurately presents the growing dependence by farmers on a Production Credit System where funds do not have to be obtained locally. This growing dependence emphasizes the need for H.R. 16674.

We urge its adoption.

We respectfully request this letter be made part of the record.

Sincerely,

RICHARD T. O'CONNELL.

The CHAIRMAN. We have two further witnesses, Mr. Herschel D. Newsom, master, National Grange, and Mr. Kit H. Haynes, assistant legislative director of the American Farm Bureau Federation.

Mr. Newsom, do you care to make any comments?

¹ "Maneuverability of Funds for Agriculture," p. 5. An Address by Darryl R. Francis, President, Federal Reserve Bank of St. Louis, Missouri, November 13, 1967, before the National Agricultural Credit Conference.

STATEMENT OF HERSCHEL D. NEWSOM, MASTER, NATIONAL GRANGE

Mr. NEWSOM. Mr. Chairman and members of the committee, in addition to filing the statement I would simply like to point out that, as you know, Mr. Chairman, and some of the other members of the committee, for many years I have had the satisfaction of serving on the joint farmer-credit committee representing the Grange and the National Council of Farmer Cooperatives and the Farm Bureau Federation.

So far as I know there is no objection to this proposal.

As a matter of fact, the urgency of moving in this direction, I think, Mr. Chairman, if I may say so, is necessary.

I should like to indicate by asking that, as a part of my testimony, the balance sheet of agriculture as of January 1, 1956 through January 1, 1967, and selected indebtedness ratio to total assets in agriculture be filed also, because you will see in this table that the ratio of agricultural indebtedness to the total assets is increasing rather rapidly. This does not refute the statement made by Governor Tootell, but it does indicate very clearly that the urgency is very great.

The CHAIRMAN. We will file those with the record.

Thank you very much, Mr. Newsom.

(The prepared statement submitted by Mr. Newsom and the balance sheet of agriculture, January 1, 1956 to January 1, 1967, are as follows:)

STATEMENT OF HERSCHEL D. NEWSOM, MASTER, NATIONAL GRANGE

Mr. Chairman and committee members, the Grange supports the proposed legislation to improve the capitalization of the Federal intermediate banks and of the production credit associations so that these agencies of the Farm Credit Administration may more adequately meet the rapidly increasing credit requirements of farmers and their service agencies.

Grange interest in the evolution of our cooperative farm credit structure is historic and needs no definition before this Committee. From the original conception of the National Farm Loan Act as it began to appear in Grange policy statements in 1908, the basic conception of temporary use of Government funds to develop a cooperative farm credit structure, up to this very moment, the Grange has continued to support such plans as those proposed by the twelve Federal intermediate banks to retire within a reasonable time their capital stock owned by the United States, so that all of the capital in each of these banks will then be owned by the production credit associations in its district.

Currently, we are much concerned that the Federal intermediate banks shall have the capacity to meet the increasing requirements for credit from the 459 production credit associations and the 118 other lending institutions that are financed by the Federal intermediate credit banks. This means, under current circumstances, that the credit banks must be in a position to obtain sufficient loan funds with which to meet these credit requirements.

As the members of this Committee know full well, these loan funds are obtained by the 12 Federal intermediate credit banks through the selling of consolidated debentures for which the loans made to farmers are offered as collateral, in the public securities market. With credit requirements increasing as they have been recently and are destined to continue to increase for some time to come, the amount of such debentures and similar obligations that may be outstanding at one time, limited as they presently are to twelve times the surplus and paid in capital of the Federal intermediate credit banks, needs re-examination.

It is on the basis of such re-examination that we now support proposals to make permissible debt-to-capital ratio, twenty to one, in lieu of the present twelve to one ratio. This would increase the amount of loan funds obtainable by the Federal intermediate credit banks without interfering with our basic

target of relying increasingly on our participation and the normal commercial money market for these credit requirements.

We, therefore, commend to you the acceptance of the explanation of the Farm Credit Board, the Governor and his co-workers of the Farm Credit Administration that a twenty to one debt-to-capital ratio for these intermediate credit banks is justified and necessary.

Working rather closely with the Governor and the members of the Board as we have done throughout the history of the Farm Credit Administration since it became operative in its present form as a result of the Farm Credit Act of '53, we are convinced that this legislation is important and the present twelve to one limitation should be lifted so that this cooperative farm credit system may continue to meet the increasing production credit needs of farmers that can qualify for such credit on a self-sustaining basis.

The members of this Committee know full well that most of the business of the Federal intermediate banks is with the production credit associations. I am advised that this percentage is currently about 95 percent. But these banks also finance other institutions that make loans to farmers. At present, the production credit associations acquire capital stock in the Federal intermediate credit bank serving their district, both as annual patronage refunds and by purchase. The interests in the bank acquired by such other financing institutions are known as participation certificates, and presently are issued only as annual patronage refunds. We see no objection to additional participation certificates being issued for purchase by the other financing institutions as would be provided in section 1(a) of the bill. This would be an additional source of capital for a credit bank.

Section 1(c) seems to be in furtherance of the general idea that the ownership interests in a Federal intermediate credit bank held by a production credit association should be reasonably related to the current patronage of the bank by the association, inasmuch as the volume of patronage may vary considerably over the years.

In 1965, as many of you will recall, provision was made for a Federal intermediate credit bank to adjust the amount of its capital stock held by each production credit association in proportion to its patronage during the intermediately preceding three fiscal years. However, in addition to the capital stock in the bank held by an association, each association is also allocated on a patronage basis each year, a certain portion of the earnings that are retained in the reserve account of the bank. In order that all ownership interests in the bank held by an association may be related to its patronage during the immediately preceding three fiscal years, adjustment should be made for the reserve account allocations held by an association as well as for the capital stock.

This would be authorized as to reserve account allocations by section 1 (c) of the bill. For each shift of such ownership interests there would be an offsetting transfer of money so that it would not cause any change in the net worth of an association.

The remaining two amendments concern the production credit associations. With Farm Credit Administration approval, section 2 (a) would authorize a production credit association to retire the class B stock which a borrower is required to own. Presumably retirement could be permitted upon payment of a loan or to apply the proceeds in partial or final payment of a loan and in other special circumstances. It seems to us that this is preferable to requiring that the borrower in every case continue to hold the stock, even though he does not expect to borrow from the association again.

We also see no objection to section 2 (b) which would permit a production credit association to obtain funds by selling its capital notes to borrowers and others. This is deemed sufficiently safeguarded because any notes issued, together with other liabilities of the association, may not exceed ten times the capital and surplus of the association and could only be issued under rules and regulations prescribed by the Farm Credit Administration.

The bill clearly seems to be an effort to improve the capacity of the Federal intermediate credit banks and the production credit associations to continue to provide the service expected of them in meeting the increasing credit needs of farmers. I, therefore, recommend that the Committee report the bill favorably and seek its early passage.

THE BALANCE SHEET OF AGRICULTURE, JAN. 1, 1956, TO JAN. 1, 1967, AND SELECTED INDEBTEDNESS RATIO

Item	1956	1957	1958	1959	1960	1961	1962	1963	1964	1965	1966	1967 ¹	1968 estimate
	Billion dollars												
Assets:													
Real estate	102.9	110.4	115.9	124.4	129.9	131.4	137.4	143.6	152.3	161.3	172.2	182.0	191.5
Other physical assets ²	48.7	49.5	51.6	58.9	55.3	54.5	56.7	58.2	58.6	57.4	62.9	66.3	67.7
Financial ³	18.0	18.0	18.3	19.2	18.3	18.0	18.3	18.9	19.1	19.8	20.6	21.1	22.0
Total	169.6	177.9	185.8	202.5	203.5	203.9	220.7	220.7	230.0	238.5	255.7	269.5	281.2
Liabilities:													
Real estate debt	9.0	9.8	10.4	11.1	12.1	12.8	13.9	15.2	16.8	18.9	21.2	23.3	25.0
Non-real-estate debt (including Commodity Credit Corporation loans)	9.8	9.6	10.0	12.6	12.8	13.4	14.8	16.6	18.1	18.6	20.4	22.4	24.9
Total	18.8	19.4	20.4	23.7	24.9	26.2	28.7	31.8	34.9	37.5	41.6	45.7	49.9
Proprietors' equities ⁴	150.8	158.5	165.4	178.8	178.6	177.7	183.7	188.9	195.1	201.0	214.1	223.8	231.8
Percent													
Ratio real estate debt-real estate assets	8.7	8.9	9.0	8.9	9.3	9.7	10.1	10.6	11.0	11.7	12.3	12.9	13.4
Ratio total debts-total assets	11.1	10.9	11.0	11.7	12.2	12.8	13.5	14.4	15.2	15.7	16.3	16.9	17.7

¹ To be published in 1967 Balance Sheet.² Livestock, machinery and motor vehicles, crops stored on and off farms, and household furnishings and equipment.³ Deposits and currency, U.S. Savings Bonds, and Investments in Cooperatives.⁴ Assets minus liabilities.

The CHAIRMAN. The next is Mr. Kit H. Haynes, assistant legislative director, the American Farm Bureau Federation.

We will be glad to hear from you now.

STATEMENT OF KIT H. HAYNES, ASSISTANT LEGISLATIVE DIRECTOR, AMERICAN FARM BUREAU FEDERATION

Mr. HAYNES. Mr. Chairman and members of the committee, our statement endorses the objective of the bill. I think that, in view of the time, it would be wiser to file the written statement. I am only a telephone call, 15 minutes away, if anyone has any questions.

The CHAIRMAN. Thank you, Mr. Haynes, and without objection your statement will be made a part of the record.

(The prepared statement of the American Farm Bureau Federation follows:)

STATEMENT OF KIT H. HAYNES, ASSISTANT LEGISLATIVE DIRECTOR, THE AMERICAN FARM BUREAU FEDERATION

We appreciate this opportunity to present views of the American Farm Bureau Federation on legislative proposals to amend the Federal Farm Loan Act and the Farm Credit Act of 1933 to improve the capitalization of the Intermediate Credit Banks and the Production Credit Associations.

The American Farm Bureau Federation is the nation's largest general farm organization, with a voluntary paid membership of more than 1,753,000 member families in some 2,770 County Farm Bureaus located in 49 states and Puerto Rico.

Adequate credit available under reasonable terms has been an important factor in development of the nation's agriculture. The steady advancement of agricultural technology in recent years and the degree to which efficient and profitable farming operations depend upon maximum utilization of that technology have cast skillful use of credit in an even more significant role in present-day farming operations. It is safe to say that most Farm Bureau families use or have used credit as a working tool in production and marketing of crops and livestock.

For this reason, Farm Bureau has long recognized that sound agricultural credit is essential to successful farming, that credit needs are continually changing and growing and that those needs must be met.

The proposed amendments to the agricultural credit legislation would change present law in five respects, all of which are aimed at increasing the capital available for lending by the 12 Federal Intermediate Credit Banks and, in turn, by the more than 450 Production Credit Associations.

Farm Bureau supports the objectives of these amendments, the major one of which would increase the debt-to-capital limitations on the Federal Intermediate Credit Banks from the current ratio of 12 to 1 to 20 to 1. Such an increase would enable the banks to sell additional debentures to the investing public in the nation's money markets and thereby increase the amount of funds available for agricultural financing without calling upon the government for more capital.

In view of the ever-expanding use of credit in agriculture and with due consideration of the banks' outstanding record with respect to losses, an increase in their permissive debt-to-capital ratio would seem both reasonable and safe. We recommend that the debt-to-capital ratio be raised to the extent required to enable the banks to meet expanding credit needs of PCA's and other agricultural financing institutions which they serve while, at the same time, maintaining the soundness which has characterized their operations for more than 30 years.

The 12 Federal Intermediate Credit Banks were established in 1923, and their losses since that time have amounted to approximately \$1 for each \$9,000 of credit extended, with no losses at all since 1933. This is an enviable record and reflects both the soundness of the credit program conducted by these banks and the skill of those who are responsible for management. The banks initially operated on an individual 10-to-1 debt-to-credit ratio. This was raised to 12-to-1 for the whole system about three years ago, without any increase in the amount of losses.

Primary function of the FIBC's is discounting or purchasing from Production Credit Associations or other agricultural financing institutions notes representing loans made by them to farmers and ranchers. The banks also make loans and ad-

vances to the PCA's and other financing institutions to enable them to make or carry loans for agricultural purposes. There now are about 118 other financing institutions being served by the banks, but approximately 95 percent of the banks' discounting and lending business is done with the PCA's.

Because of his membership, the individual farmer has a more direct tie with his local Production Credit Association than with other agencies of the Farm Credit Administration. The success of the PCA's is a good example of farmers working to help themselves. Set up to provide individual farmers and ranchers credit—generally for periods not to exceed one year—these associations operate in all of the 50 states and in Puerto Rico. The soundness of their operations is evidenced by the fact that of the 459 associations in the nation, all but a very few are now completely farmer-owned. During the 1967 fiscal year, these associations made loans totaling more than \$5 billion. At the end of the year, there were 322,700 borrowing members out of a total membership of 548,279, and outstanding loans amounted to \$3.7 billion.

The amendment increasing the debt-to-capital ratio of the intermediate credit banks would enable the PCA's to continue to meet the expanding credit needs of individual farmers and ranchers promptly and effectively.

Included in the bill before you, H.R. 16674, are four other amendments of a more technical nature and of relatively lesser importance. Each is aimed at strengthening the credit structure of the credit banks and the PCA's. In the interest of the Committee's time, we shall not attempt to discuss each of these individually.

We believe that the objective of these amendments is sound and is in the interest of American farmers and ranchers.

We thank you for the opportunity to present Farm Bureau's views on this matter.

(The following letters were also submitted to the committee:)

NATIONAL MILK PRODUCERS FEDERATION,
Washington, D.C., April 29, 1968.

HON. W. R. POAGE,
Chairman, House Agriculture Committee,
Longworth House Office Building,
Washington, D.C.

DEAR MR. POAGE: We shall greatly appreciate it if you will place in the record of the hearing on H.R. 16674 this letter supporting the bill.

The purpose of this bill is to improve the capital structure of the Federal intermediate credit banks and the production credit associations. We are in accord with the purposes of this legislation, and we believe that the excellent record established by these agricultural credit institutions justifies the proposed amendments.

One of the objectives of this legislation is to permit these lending institutions to meet the increased credit requirements of today's agriculture without increasing the amount of capital supplied by the U.S. Government or interfering with the steady progress being made toward the retirement of the Government capital in the Federal intermediate credit banks. Dairy farmers and dairy cooperatives make extensive use of the Farm Credit lending agencies. Dairy farming requires substantial capital, as does also the operation of dairy cooperative plants, and this need is steadily increasing.

We never cease to be impressed by the remarkable story of the Farm Credit Administration. By merely providing the use of Government capital for a relatively short period of time, Congress has been able to establish a system of agricultural credit which is of tremendous importance. The steady progress being made in the retirement of the Government capital and its replacement with farmers' funds is a tribute to the integrity of the American farmer and the able leadership which the Farm Credit Administration has provided.

We again express, as we have many times before, our appreciation for the legislation enacted several years ago to enable the banks for cooperatives to embark on an effective program to retire the Government capital used by those banks. Cooperatives have responded favorably to that legislation, and we have come a long way toward accomplishment of our goal which is the repayment in full of all of the Government capital.

The pending legislation further promotes this objective and we urge its prompt enactment.

Sincerely,

E. M. NORTON, *Secretary.*

THE AMERICAN BANKERS ASSOCIATION,
Washington, D.C., April 29, 1968.

Hon. W. R. POAGE,
Chairman, Committee on Agriculture, U.S. House of Representatives,
Longworth House Office Building, Washington, D.C.

DEAR CHAIRMAN POAGE: The American Bankers Association takes this opportunity to express its views concerning Section 2(b) of H.R. 16674, which would authorize a Production Credit Association to issue its capital notes for sale to borrowers and others. The A.B.A. is forced to oppose Section 2(b) as it would merely siphon funds from small country banks, some of whom are having trouble acquiring funds required to finance farm customers in the present tight money market. Giving PCA's authority to enter this new field will not create any additional funds. There is a sharp distinction between the Federal Intermediate Credit Banks entering the national capital market and PCA's competing for local funds.

It seems that before the Congress should make such a drastic change in the financial structure of the Federal farm credit agencies, the proposal should be reviewed in context with other efforts which are directed towards solving the problem of availability of funds for agriculture. The study of the discount window presently being made by the Board of Governors of the Federal Reserve System will throw new light on this problem. We feel that commercial banks and government agencies, such as the Board of Governors of the Federal Reserve System, the Federal Home Loan Bank Board, the Federal Deposit Insurance Corporation, and the Comptroller of the Currency, should have an opportunity to study this Section in detail and express their views.

Sincerely yours,

CHARLES R. MCNEILL

The CHAIRMAN. That completes the testimony.

We thank all the witnesses.

The committee will now go into executive session on the bill.

Mr. BICE. Mr. Chairman, may I make this further comment?

We wish, on the part of the Farm Credit, to thank you for your very attentive consideration, your understanding. It has been most helpful; you have been most gracious in your comments, and we indeed are most appreciative.

Thank you.

The CHAIRMAN. Thank you very much.

We are very glad to have had all of you here.

We will now go into executive session.

(Whereupon, at 11:45 a.m., the committee retired into executive session.)

○