attachments; it must also provide (or be accompanied by a document that provides):

* * * * *

PART 1655—LOAN PROGRAM

■ 8. The authority citation for part 1655 is revised to read as follows:

Authority: 5 U.S.C. 8433(g), 8439(a)(3) and 8474.

■ 9. Revise section 1655.2 to read as follows:

§ 1655.2 Eligibility for loans.

A participant can apply for a TSP general purpose or residential loan if:

(a) More than 60 calendar days have elapsed since the participant has repaid in full a TSP loan of the same type.

(b) The participant is in pay status;

(c) The participant is eligible to contribute to the TSP (or would be eligible to contribute but for the suspension of the participant's contributions because he or she obtained a financial hardship in-service withdrawal or because he or she stopped contributing to the TSP and is not yet eligible to resume contributing);

(d) The participant has at least $1,000 in employee contributions and attributable earnings in his or her account; and

(e) The participant has not had a TSP loan declared a taxable distribution within the last 12 months for any reason other than a separation from Government service.

■ 10. Amend section 1655.4 by revising the second sentence to read as follows:

§ 1655.4 Number of loans.

* * * One of the two outstanding loans may be a residential loan and the other one may be a general purpose loan. * * *

■ 11. Revise paragraph (b) of section 1655.11 to read as follows:

§ 1655.11 Loan acceptance.

* * * * *

(b) The participant has the maximum number of loans outstanding under § 1655.4;

* * * * *

■ 12. Add a new section 1655.21 to read as follows:

§ 1655.21 Loan fee.

The TSP will charge a participant a $50.00 loan fee when it disburses the loan and will deduct the fee from the proceeds of the loan.

PART 1690—THRIFT SAVINGS PLAN

■ 13. The authority citation for Part 1690 continues to read as follows:

Authority: 5 U.S.C. 8474.

■ 14. Revise section 1690.12 to read as follows:

§ 1690.12 Power of attorney.

(a) A participant or beneficiary can appoint an agent to conduct business with the TSP on his or her behalf by using a power of attorney (POA). The agent is called an attorney-in-fact. The TSP must approve a POA before the agent can conduct business with the TSP; however, the TSP will accept a document that was signed by the agent before the TSP approved the POA. The TSP will approve a POA if it meets the following conditions:

(1) The POA must give the agent either general or specific powers, as explained in paragraphs (b) and (c) of this section;

(2) A notary public or other official authorized by law to administer oaths or affirmations must authenticate, attest, acknowledge, or certify the participant's or beneficiary's signature on the POA; and

(3) The POA must be submitted to the TSP recordkeeper for approval.

(b) *General power of attorney.* A general POA gives an agent unlimited authority to conduct business with the TSP, including the authority to sign any TSP-related document. By way of example, a POA grants such authority by authorizing the agent to act on behalf of the participant or beneficiary with respect to ''all matters,'' ''personal property,'' ''Federal Government retirement benefits,'' or ''business transactions.''

(c) *Specific power of attorney.* A specific power of attorney gives an agent the authority to conduct specific TSP transactions. A specific POA must expressly describe the authority it grants. By way of example, a specific POA may authorize an agent to ''obtain information about my TSP account'' or ''borrow or withdraw funds from my TSP account.''

■ 15. Revise section 1690.13 to read as follows:

§ 1690.13 Guardianship and conservatorship orders.

(a) A court order can authorize an agent to conduct business with the TSP on behalf of an incapacitated participant or beneficiary. The agent is called a guardian or conservator and the incapacitated person is called a ward. The TSP must approve a court order before an agent can conduct business with the TSP; however, the TSP will accept a document that was signed by the agent before the TSP approved the court order. The TSP will approve a court order appointing an agent if the following conditions are met:

(1) A court of competent jurisdiction (as defined at 5 CFR 1690.1) must have issued the court order;

(2) The court order must give the agent either general or specific powers, as explained in paragraphs (b) and (c) of this section;

(3) The agent must satisfy the TSP that he or she meets any precondition specified in the court order, such as a bonding requirement;

(4) The court order must be submitted to the TSP record keeper for approval.

(b) *General grant of authority.* A general grant of authority gives a guardian or conservator unlimited authority to conduct business with the TSP, including the authority to sign any TSP-related document. By way of example, an order gives a general grant authority by appointing a ''guardian of the ward's estate,'' by permitting a guardian to ''conduct business transactions'' for the ward, or by authorizing a guardian to care for the ward's ''personal property'' or ''Federal Government retirement benefits.''

(c) *Specific grant of authority.* A specific grant of authority gives a guardian or conservator authority to conduct specific TSP transactions. Such an order must expressly describe the authority it grants. By way of example, an order may authorize an agent to ''obtain information about the ward's TSP account'' or ''borrow or withdraw funds from the ward's TSP account.''

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FARM CREDIT ADMINISTRATION

12 CFR Parts 614 and 615

RIN 3052–AB96

Loan Policies and Operations; Funding and Fiscal Affairs, Loan Policies and Operations, and Funding Operations; OFI Lending

AGENCY: Farm Credit Administration.

ACTION: Final rule.

SUMMARY: The Farm Credit Administration (FCA, agency, or we) adopts a final rule that amends regulations governing other financing institutions (OFIs). The purpose of the final rule is to make it easier for OFIs to obtain funding for short- and intermediate-term loans to farmers, ranchers, aquatic producers, farm-related businesses, and rural homeowners through Farm Credit System (FCS, Farm Credit, or System) banks. The FCA believes that these

changes will make credit to agriculture and other eligible borrowers in rural America more affordable. The final rule removes unnecessary provisions in the existing OFI regulations that: Impede the flow of credit; or do not enhance safe and sound operations. The FCA also adopts conforming amendments to its capital regulations.

DATES: *Effective Date:* This regulation will be effective 30 days after publication in the **Federal Register** during which time either or both Houses of Congress are in session. We will publish a notice of the effective date in the **Federal Register**.

FOR FURTHER INFORMATION CONTACT:

Dennis K. Carpenter, Senior Policy Analyst, Office of Policy and Analysis, Farm Credit Administration, McLean, VA 22102–5090, (703) 883–4498, TTY (703) 883–4434; or

Richard A. Katz, Senior Attorney, Office of General Counsel, Farm Credit Administration, McLean, VA 22102–5090, (703) 883–4020, TTY (703) 883–2020.

SUPPLEMENTARY INFORMATION:

I. Background

This rulemaking began on April 20, 2000, with an advance notice of proposed rulemaking (ANPRM) that asked all interested parties specific questions about the funding and discount relationship between Farm Credit banks and OFIs.[1] FCA staff subsequently conducted telephone and field interviews with interested parties. On August 3, 2001, we held a public meeting in Des Moines, Iowa, where interested parties offered suggestions on how we could facilitate greater cooperation between System and non-System lenders in providing credit to agriculture and rural America. The public meeting addressed both the OFI program and other arrangements where the FCS and non-System lenders could help each other in extending credit to farmers, ranchers, and other eligible borrowers in rural America.

Many of the comments and suggestions that we received from the ANPRM, interviews, and at the public meeting were incorporated into the proposed rule to revise both our OFI and the investment in farmers' notes (Farmers' Notes) regulations.[2] Basically, the proposed OFI rule would allow OFIs to establish a funding and discount relationship with any one Farm Credit Bank (FCB) or agricultural credit bank (ACB) (collectively Farm Credit banks). The proposed rule also would strengthen the equitable treatment provisions in the existing regulations by requiring a Farm Credit bank, at the request of an OFI or OFI applicant; to: (1) Disclose how it prices funds for OFIs; and (2) justify any discrepancy in the cost of funding between OFIs and associations. Another feature of the proposed rule is that it would allow Farm Credit banks to disclose the identity of OFIs with their consent. The preamble to the proposed OFI rule clarified the FCA's position on borrower rights, and it offered suggestions for improving relationships between OFIs and the System, and the role of the FCA Ombudsman. The FCA also proposed changes to the Farmers' Notes regulation and conforming amendments to its capital regulations regarding risk weighting for OFIs and Farmers' Notes.

The FCA received 111 comment letters on the proposed rule. A total of 8 comment letters came from the System; 1 from the Farm Credit Council (FCC), 5 from Farm Credit banks, and 2 from associations. Other commenters were an agricultural credit cooperative OFI, a Community Development Financial Institution (CDFI), the Credit Union National Association (CUNA), which is a trade association for credit unions, and two individuals. Finally, 98 letters came from commercial bankers, including the Independent Community Bankers of America (ICBA) and its state-affiliated associations.

The vast majority of the commenters generally supported the proposed OFI rule, but both System and non-System commenters offered suggestions and raised concerns about particular issues. Commercial banks and their affiliated trade associations opposed the proposed Farmers' Notes rule. These commenters asked the FCA to hold a public meeting, seek additional public comment, and solicit congressional input before adopting a final Farmers' Notes rule. Several FCS and non-System commenters asked the FCA to revise or clarify certain provisions in the proposed capital risk-weighting regulations that applied to OFIs.

We are enacting a final rule on OFIs, which includes conforming amendments to the capital regulations concerning the risk weighting of System bank loans to OFIs. We are not adopting a final Farmers' Notes rule at this time because we are continuing to consider the best regulatory approach to this program.

II. Final OFI Rule

As explained earlier, the purpose of this rule is to make it easier for OFIs to obtain funding from Farm Credit banks for their short- and intermediate-term loans to agricultural and aquatic producers, farm-related business, and rural homeowners. Improving OFI access to the funding and discount services of Farm Credit banks could make affordable credit more available to farmers, ranchers, and other eligible borrowers. Farm Credit banks fulfill their missions as a Government-sponsored enterprise by enhancing the liquidity of OFIs, thereby lowering the cost of funding agriculture.

The FCA now addresses concerns and suggestions that the commenters raised about various issues of the proposed OFI rule.

A. Assured Access (§ 615.4540(b)(1))

Section 1.7(b)(4)(B)(i) of the Farm Credit Act of 1971, as amended (Act) requires FCA regulations to assure that the funding and discount services of Farm Credit banks are available on a reasonable basis to any OFI that is significantly involved in lending for agricultural and aquatic purposes. Currently, § 614.4540(b)(1) states that Farm Credit banks must ''fund, discount, or provide other similar financial assistance to any creditworthy OFI that * * * maintains at least 15 percent of its loan volume at a seasonal peak in loans and leases to farmers, ranchers, aquatic producers and harvesters.'' Section 1.7(b) of the Act and § 614.4540 of the regulations allow OFIs that do not meet this 15-percent threshold to fund and discount their short- and intermediate-term loans at Farm Credit banks, but they are not assured access if credit becomes scarce.

During earlier phases of this rulemaking, some commercial banks and System lenders expressed the opinion that the 15-percent threshold was too onerous, and they asked the FCA to reduce or eliminate it. Some of these commenters mistakenly believed that § 614.4540(b)(1) automatically excluded non-System lenders from the OFI program if agricultural or aquatic loans did not compromise at least 15 percent of their loan portfolios. Although the current regulation assures access to creditworthy OFIs that maintain at least 15 percent of their loan volume at a seasonal peak in agricultural loans, some commenters erroneously thought that it only provided assured access to those OFIs that always maintain at least 15 percent of their loan portfolio in farm loans. The preamble to the proposed rule dispelled both of these misconceptions.[3]

The FCA did not propose to change the 15-percent threshold as the factor that determines whether an OFI is

[1] *See* 65 FR 21151 (April 20, 2000).

[2] *See* 68 FR 47502 (August 11, 2003).

[3] *See* 68 FR 47502, 47505 (August 11, 2003).

assured access to funding from a Farm Credit bank. The preamble to the proposed rule explained that the standard that the FCA uses to determine whether a non-System lender is substantially involved in agricultural lending is more permissive than the 25-percent benchmark that the Federal Deposit Insurance Corporation established for nonmember banks that it insures, and is comparable to the measure used by the Board of Governors of the Federal Reserve System.[4] The FCA invited comments on alternatives that reasonably demonstrate that an OFI is significantly involved in agricultural lending because the agency is open to ideas that would make this program more attractive to OFIs.

The FCA received two comment letters about assured access. Both letters came from FCS institutions that support the 15-percent threshold as the appropriate standard for determining whether an OFI is significantly involved in agricultural lending.

The final rule retains the 15-percent threshold in existing § 614.4540(b)(1). The 15-percent threshold strikes a fair balance between the needs of small rural lenders and larger institutions. Agricultural loans usually comprise a larger percentage of the loan assets of small rural lenders. However, larger institutions may extend more overall credit, in dollar terms, to farmers, although agricultural loans are a much smaller percentage of their loan portfolios.

B. Place of Discount (§ 614.4550)

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

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

The ANPRM, interviews, and public meeting revealed widespread dissatisfaction with the place of discount rule in § 614.4550. Except for one Farm Credit bank, all System and non-System commenters favored repealing all restrictions on place of discount so OFIs could choose their System funding bank. The one Farm Credit bank that opposed repealing § 615.4550 was concerned that FCS associations would be placed at a competitive disadvantage.

In response to these comments, the FCA proposed to revise § 615.4550 so OFIs could fund or discount loans with any FCS bank. The FCA reasoned that this approach would free Farm Credit banks from potential pressure by associations not to lend to their competitors. Another factor that supports the proposed rule is that when Farm Credit banks compete for OFI credit, the OFI may be able to obtain a more favorable funding cost, which it can then pass on to farmers and ranchers.[5]

The proposed rule would require a Farm Credit bank to notify another System bank in writing within 5 business days of receiving an application from an OFI that maintains its headquarters or has more than 50 percent of its loan volume in the territory of the other Farm Credit bank. The purpose of this notice requirement is to give the bank in whose territory the OFI is located ample opportunity to contact the applicant and offer it funding and discount services. The proposed rule would not allow any OFI to borrow from two or more Farm Credit banks at the same time. The preamble to the proposed rule justified this ban on safety and soundness grounds.

The FCA received 100 comments about place of discount. Of this total, 92 came from commercial banks or their trade associations, 6 from System banks and associations, and 1 each from CUNA and the agricultural credit cooperative OFI. All commercial bank commenters and CUNA supported the FCA's position on place of discount. None of these commenters sought any revision to proposed § 614.4550. System commenters agreed that an OFI should be allowed to fund or discount short-or intermediate-term loans with the Farm Credit bank of its choice.

However, System commenters opposed the 5-day notice requirement in the proposed rule. These commenters claim that the notice requirement grants too much flexibility to OFIs while imposing unnecessary burdens on System banks. One commenter thought that the OFI should bear the burden of notifying the local Farm Credit bank that it is taking its business elsewhere. Two System commenters stated that the mere receipt of a credit application from an OFI located outside its chartered territory does not mean that the Farm Credit bank will approve funding. Since the FCS bank is unlikely to make a credit decision within 5 days, these commenters stated that it should be under no obligation to notify the Farm Credit bank that serves the territory where the OFI is located.

System commenters and the agricultural credit cooperative OFI opposed the ban on two or more Farm Credit banks simultaneously funding the same OFI. Many of these commenters stated that our safety and soundness rationale was unpersuasive. These commenters note that many OFIs already have multiple sources of funding, and that multilender financing of commercial borrowers is commonplace today in credit markets. All of these commenters suggest that intercreditor agreements among different Farm Credit banks will adequately resolve the FCA's safety and soundness concerns about disputes over collateral if the OFI fails.

The FCA adopts final § 614.4550, which enables creditworthy OFIs to seek and establish a funding and discount relationship with the Farm Credit bank of their choice. Allowing OFIs to choose their System funding bank frees them from the problems associated with obtaining credit from banks that are owned and controlled by their competitors. This approach may lower the funding costs and improve the liquidity of OFIs which could, in turn, reduce the cost of credit to farmers, ranchers, and other eligible rural residents.

In response to System commenters, the FCA does not view the 5-day notice requirement as a burden on Farm Credit banks. This notice requirement ensures that Farm Credit banks communicate with each other in providing funding and liquidity to OFIs. Additionally, this regulatory requirement enables each Farm Credit bank to consider offering funding and discount services to OFIs in its chartered territory. The 5-day notice requirement has no relationship to the credit approval process at a Farm Credit bank that receives an application from an OFI outside its territory. Written notice is required within 5 days, regardless of whether the Farm Credit bank has considered or acted upon an application received from such OFIs.

[4] Ibid.

[5] Ibid.

Simply providing written notice to another Farm Credit bank within 5 days is neither costly nor difficult to any System bank that receives applications from OFIs outside its chartered territory.

The FCA retains the ban on two or more Farm Credit banks simultaneously funding the same OFI. Although System arguments against this ban have some merit, policy concerns justify the FCA's decision to retain it. In retail credit markets, financing by multiple lenders of the same borrower and intercreditor agreements are commonplace. However, discount banks established by Congress to fulfill a public policy mission generally do not engage in such practices. For example, two Federal Reserve Banks or two Federal Home Loan Banks do not simultaneously fund the same member bank. Generally, each FCS association receives all of its funding from one Farm Credit bank. In addition, an association cannot seek credit from another System bank unless its funding bank consents. Therefore, the ban on two or more Farm Credit banks simultaneously funding the same OFI is consistent with the FCA's policy of requiring FCS banks to treat their OFIs and System associations equitably.

The agricultural credit cooperative OFI expressed concern about how the ban on two FCS banks simultaneously funding the same OFI would affect its business. The commenter stated that its parent is an agricultural cooperative that borrows from the ACB under title III of the Act, while it is an OFI that borrows from a Farm Credit bank and sells participations in loans to FCS associations. The FCA clarifies that nothing in the proposed or final regulation prevents: (1) OFIs from participating in loans with System associations; or (2) any parent or affiliate which is an agricultural cooperative from borrowing from the ACB under title III of the Act.

C. Borrower Rights (§ 614.4560(d))

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

During all phases of this rulemaking, System and commercial bank commenters have repeatedly advised the FCA that borrower rights are an impediment to the success of the OFI program. However, many commenters acknowledged that the Act requires OFIs to comply with borrower rights requirements. The FCA cannot repeal § 614.4560(d) because it implements statutory borrower rights requirements.

The FCA proposed a technical correction to § 614.4560(d) that would remove the reference to section 4.36 of the Act from the regulation because the plain language of the statute grants the right of first refusal only to borrowers of FCS institutions that operate under titles I or II of the Act, not OFIs. One System commenter agreed with the technical correction to § 614.4560(d), while all other commenters expressed no opinion about this matter. The final rule removes the reference to section 4.36 of the Act from § 614.4560(d) so that the regulation conforms to the statute.

The FCA recently moved all borrower rights regulations to part 617.[6] For this reason, the FCA revises all of the cross-references in final § 614.4560(d) to the borrower rights regulations to reflect this change.

Currently, § 614.4560(d) states that borrower rights apply to ''all loans that an OFI *funds* or discounts through a Farm Credit Bank or agricultural credit bank * * *'' (Emphasis added). Earlier, a Farm Credit bank pointed out that section 4.14A(a)(6)(B) of the Act requires an OFI to comply with borrower rights, ''but only with respect to loans discounted or pledged under section 1.7(b)(1).'' As a result, this System bank asserted that the language in § 614.4560(d) exceeds the scope of section 4.14A(a)(6) of the Act. Specifically, the Farm Credit bank interpreted section 4.14A(a)(6) of the Act to mean that borrower rights apply to OFI loans only during the time that they are actually pledged to the funding bank as collateral. Under this interpretation, most borrower rights would not apply to OFI loans because many of these rights apply before or after the time that these loans are actually pledged to the System funding bank. Examples of borrower rights that would not apply to OFI loans under this interpretation are: (1) Most EIR disclosures; (2) the right to appeal certain adverse credit decisions to an OFI's credit review committee; and (3) the right to restructure a distressed loan that the OFI has removed from collateral at its System funding bank. Under the bank's suggested interpretation of the statute, section 4.13A of the Act would be the only borrower rights provision of the Act that would always apply to OFI borrowers. This provision enables System and OFI borrowers to obtain copies of: (1) All loan documents they sign or deliver; (2) loan appraisals on their assets that the lender uses in making credit decisions; and (3) the lender's articles of incorporation and bylaws.

The proposed rule retained the provision in § 614.4560(d), which states that borrower rights apply to all loans that an OFI funds or discounts through a Farm Credit bank. The preamble to the proposed rule thoroughly examined and analyzed the text, structure, and legislative history of the borrower rights provisions of the Act, and it explained in detail why borrower rights apply to all loans that OFIs fund through a Farm Credit bank. The discussion in the preamble to the proposed rule revealed that Congress intended to grant OFI borrowers whose loans are funded by a Farm Credit bank all of these rights and protections, even at times when their loans are not actually pledged as collateral to the System funding bank.

Except for one association, which expressed no opinion on this matter, all other System commenters opposed the FCA's interpretation of the borrower rights provision of the Act. These commenters stated that this approach conflicts with the FCA's stated goal of making the OFI program more attractive to potential and existing OFIs. Some commenters stated that the FCA's position was impractical because neither the agency nor the funding bank can enforce compliance with borrower rights after an OFI has removed a distressed loan from collateral.

None of these commenters offered new information or provided any legal analysis that would cause the FCA to change its interpretation of section 4.14A(a)(6) of the Act. Accordingly, the FCA reaffirms its interpretation of section 4.14A(a)(6) that it presented in the preamble to the proposed rule. Under section 4.14A(a)(6) of the Act, borrower rights apply to all loans that an OFI funds or discounts through a Farm Credit bank. The borrower continues to be entitled to borrower rights after the OFI removes the loan from collateral. Only a statutory amendment could resolve the concerns raised by the commenters.

The ICBA and its member banks stated that depository institutions should not have to comply with borrower rights because they must

[6] *See* 69 FR 10901 (March 9, 2004).

comply with the Community Reinvestment Act (CRA). These commenters asked the FCA to treat compliance with the CRA as a substitute to compliance with borrower rights requirements.

The FCA responds that the Act explicitly requires OFIs to comply with borrower rights on all loans that they fund or discount through a Farm Credit bank, regardless of whether they are also subject to the CRA. The purposes, objectives, and compliance mechanism of the CRA are separate, distinct, and independent from the borrower rights requirements of the Act. The CRA does not provide farmers, ranchers, and aquatic producers and harvesters the rights and protections on agricultural loans that the Act confers on them. Neither the Act nor the CRA authorizes depository institutions to substitute CRA requirements for compliance with borrower rights. For this reason, the FCA has no authority to grant this request.

One Farm Credit bank asked the FCA to clarify that borrower rights do not apply to loans that an OFI pledges as supplemental collateral. Under § 614.4570(c), Farm Credit banks may require an OFI to pledge supplemental collateral or provide other credit enhancements that support the lending relationship. Farm Credit banks take supplemental collateral from their OFIs out of an abundance of caution. However, Farm Credit banks do not fund or discount supplemental collateral pledged by their OFIs. For this reason, borrower rights would not apply to agricultural loans that OFIs pledge to their System funding bank as supplemental collateral.

D. Equitable Treatment (§ 614.4590)

An FCA regulation, § 614.4590, requires Farm Credit banks to treat OFIs and FCS associations equitably. More specifically, § 614.4590(a) requires that Farm Credit banks apply comparable and objective loan underwriting standards and pricing requirements to both OFIs and FCS associations. Under § 614.4590(b), the total charges that a System bank assesses its OFIs must be comparable to the total charges it imposes on its affiliated associations. Section 614.4590(b) additionally requires that any variation between the overall funding costs that OFIs and FCS associations are charged by the same funding bank must result from differences in credit risk and administrative costs to the FCB or ACB.

Many respondents to the ANPRM and speakers at the public meeting told the FCA that Farm Credit banks continue to favor FCS associations over OFIs. According to these commenters, this perception of unfair treatment deters many agricultural lenders from becoming OFIs, while existing OFIs feel that FCS associations always receive preferential treatment from System funding banks.

Commercial bank commenters suggested that our regulations could rectify this problem by mandating equal, rather than equitable, treatment of OFIs and FCS associations. Because these commenters stated that this disparity of treatment was especially evident in the price of funding that Farm Credit banks charge their associations and OFIs, they asked the FCA to amend § 614.4590 so it requires Farm Credit banks to disclose to OFIs exactly how they price their loans to both OFIs and FCS associations. These commenters also stated that the FCA should require Farm Credit banks to identify the specific components that make up their cost of funds to OFIs and the amount of these components in terms of basis points. Another suggestion was that § 614.4590 should be revised so it expressly prohibits Farm Credit banks from charging OFIs fees that are not charged to FCS associations. Some commercial banks commented that the regulation should require Farm Credit banks to pay dividends or patronage to OFIs.

In response to these comments, the FCA proposed adding two new provisions to § 614.4590. Proposed § 614.4590(c) would require each FCB or ACB to provide any OFI or OFI applicant, upon request, a copy of its policies, procedures, loan underwriting standards, and pricing guidelines for OFIs. This provision would also require that the pricing guidelines must identify the specific components that make up the cost of funds for OFIs and the amount of these components in basis points. Proposed § 614.4590(d) would require each FCB or ACB to explain in writing the reasons for any variation in the overall funding costs it charges OFIs and FCS associations if such information is requested by an OFI or OFI applicant. This provision would require a Farm Credit bank to compare the costs that it charges OFIs and FCS associations as groups or, if possible, variations between groups of OFIs and FCS associations that are of a similar size. However, proposed § 614.4590(d) would expressly prohibit System funding banks from disclosing financial or confidential information about individual FCS associations.

The FCA declined requests to amend § 614.4590 so it would require equal, instead of equitable, treatment of FCS associations and OFIs. The preamble to the proposed rule listed five fundamental differences that distinguish FCS associations from OFIs. The FCA reasoned that these fundamental differences preclude § 614.4590 from mandating equal treatment for associations and OFIs. The preamble to the proposed rule also explained that these fundamental differences mean that OFIs expose Farm Credit banks to different credit risks and administrative costs than direct lender associations. As a result, some disparity in cost of funds that an FCB or ACB charges FCS associations and OFIs may be justified. The proposed rule did not require Farm Credit banks to pay dividends or patronage to their OFIs because the FCA found it inappropriate to impose, by regulation, business practices on FCS institutions in the absence of a compelling safety and soundness reason.[7]

In response to the proposed rule, the FCA received comment letters on equitable treatment from the FCC, a Farm Credit bank, an agricultural credit cooperative OFI, the ICBA and several of its commercial bank members. The two System commenters believe that the new disclosure requirements in proposed § 614.4590 impose costs and burdens on FCS banks that outweigh the benefits to OFIs. The Farm Credit bank stated that the revisions to § 614.4590 ''are heavily slanted in favor of the OFIs.'' Both System commenters expressed concern that § 614.4590 would require Farm Credit banks to disclose ''proprietary pricing procedures'' and information to OFIs, which could now establish a funding or discount relationship with any System bank under § 614.4550. Although commercial bank commenters support the new disclosure requirements in § 614.4590, they continue to state that this regulation should require equal, rather than equitable, treatment of associations and OFIs.

The commercial bank commenters urged the FCA to enact a final rule that requires the equal funding costs for FCS associations and OFIs because in their view, System institutions ''have easy access to all the credit they need'' while OFIs must rely on several funding sources, each which is limited. Commercial banks and the agricultural credit cooperative OFI asked the FCA to require FCS banks to: (1) Earmark the capital contribution of each OFI, and (2) pay patronage and dividends to OFIs whenever FCS associations receive such payments.

After considering these comments, the FCA has decided to enact proposed § 614.4590 as a final rule without

[7] *See* 68 FR 47502, 47505 (August 11, 2003).

revision. The final rule appropriately balances the interests of Farm Credit banks, OFIs, and System associations.

In response to System concerns, the FCA believes that OFI program will become more transparent because final § 614.4590(c) and (d) now require Farm Credit banks to disclose pricing information to their OFIs. Transparency enables both OFIs and FCA examiners to objectively determine whether a Farm Credit bank is treating its associations and OFIs equitably. Allowing OFIs to choose their System funding bank while simultaneously requiring Farm Credit banks to disclose pricing information to OFIs achieves the FCA's objective of making this program more attractive to existing and potential OFIs. Disclosing pricing information helps OFIs make informed decisions in selecting their System funding bank. As a result, the OFI can pass these pricing advantages along to farmers, ranchers, and other eligible borrowers. Funding and discounting loans for OFIs is part of the public policy mission of System banks, which are cooperative institutions that are jointly and severally liable for FCS debt. Accordingly, the FCA is not persuaded by the commenters' arguments that the regulation gives OFIs access to ''proprietary'' pricing information at several different Farm Credit banks.

Commercial bank commenters offered no new information or analysis that would persuade the FCA to amend this regulation so it requires equal, rather than equitable, treatment of OFIs and FCS associations. In fact, the most recent comments from commercial banks reinforce the notion that OFIs are fundamentally different than FCS associations. Thus, OFIs pose different credit risks to System banks than associations which, in turn, could justify the differential in the cost of funding charged to the two groups of lenders.

The FCA declines the request that the final rule require FCS banks to: (1) Allocate the capital contribution of each OFI; and (2) pay patronage and dividends to OFIs when FCS associations receive similar payments. System banks distribute patronage and dividends to their shareholders in accordance with their bylaws. FCA regulations do not prescribe business practices at System institutions in the absence of compelling safety and soundness reasons. However, each System bank must factor in capital contributions as well as patronage and dividend payments when it prices credit for an OFI. The new regulatory disclosure requirements make it easier for the OFIs and other interested parties to determine whether Farm Credit banks are pricing OFI credit equitably.

E. Ombudsman

Many commercial banks and their trade associations asked us in their response to the ANPRM and during the public meeting to appoint an Ombudsman to assist OFI applicants and existing OFIs in establishing and maintaining good relations with System funding banks. On February 25, 2003, the FCA Board established the Office of the Ombudsman. The public announcement, which informed the public of the creation of this office stated, ''The Office of the Ombudsman will be an effective, neutral and confidential resource and liaison for the public.'' One of many duties of the Ombudsman is to address the concerns of OFIs and facilitate better relationships between them and the FCS. The FCA repeated this information in the preamble to the proposed rule.[8]

The FCC and a System bank stated in their comment letters that the sole task of the Ombudsman is to serve as an advocate for OFIs. Since System banks pay for the Office of the Ombudsman through assessments that the FCA levies on them, these commenters suggest that it would be appropriate for these banks to pass the cost along to their OFIs. One commenter stated that the FCA has no express statutory authority to establish the Ombudsman position.

The FCA repeats what it said in the public announcement and the preamble to the proposed regulation. The FCA emphasizes that the Office of the Ombudsman is an effective, neutral and confidential resource and liaison for the public. Addressing the concerns of OFIs is only one of the Ombudsman's duties.

Several provisions of title V of the Act grant the FCA power to establish the Office of the Ombudsman. Section 5.9 of the Act enables our Board to ''provide for the performance of all the powers and duties vested in the Farm Credit Administration.'' Section 5.11(b) of the Act empowers the Chairman of the FCA to ''appoint such personnel as may be necessary to carry out the functions of the Farm Credit Administration.'' This section of the Act also states, ''The appointment by the Chairman of the heads of major administrative divisions under the Board shall be subject to the approval of the Board.'' The FCA Board voted to establish this office in order to address concerns by members of the public about how the agency or the System is carrying out their responsibilities under the Act.

The FCA would oppose any attempt by System banks to encumber their OFIs with the entire cost of the Office of the Ombudsman. Such attempts would violate the requirement in § 614.4590 that Farm Credit banks treat their associations and OFIs equitably.

F. Disclosure of OFI Identities (§ 614.4595)

The ANPRM asked the public whether FCA regulations should allow Farm Credit banks to disclose the identities of the OFIs that they fund. Current FCA regulations prohibit FCS institutions from releasing information about their retail borrowers and stockholders to the public.[9] However, the FCA never interpreted these regulations as prohibiting the release of names of FCS associations that borrow from Farm Credit banks.[10] The preambles to both the ANPRM and the proposed rule explained why the FCA believes that the reasons for protecting the identity of retail borrowers do not apply to financial institutions that fund and discount loans with a Farm Credit bank.[11] As both preambles explained, retail borrowers often are individual consumers, and keeping their identities confidential shields them from unwanted marketing solicitations or publicity involving their personal financial business whereas OFIs could benefit from the disclosure of their identity because it could make prospective retail borrowers aware of other credit options.

In response to ANPRM comments and testimony in the public meeting, the FCA proposed a new regulation, § 614.4595 which would allow Farm Credit banks to disclose to the public the names, addresses, telephone numbers, and Internet Web site addresses of those OFIs that consent in writing. The proposed regulation also would require each Farm Credit bank to adopt policies and procedures for: (1) Obtaining and maintaining the consent of its OFIs; and (2) disclosing this information to the public. Financial statements of Farm Credit banks should not disclose the identity of an OFI unless it consents. The FCA believes that this regulatory approach empowers each OFI to make the decision whether disclosure of its name, address, telephone number, and Internet Web site address to the public is in its best interest.

[8] Ibid.

[9] 12 CFR part 618, subpart G.

[10] In fact, information about the identities of FCS associations is widely available because it is contained in financial statements that Farm Credit banks release to the public.

[11] *See* 65 21151, 21154 (April 20, 2000); 68 FR 47502, 47508 (August 11, 2003).

The FCA received comments about this issue from the FCC, two Farm Credit banks, the ICBA, and CUNA. The FCC and a System bank see no need for this regulation because they believe that the regulations in subpart G of part 618, which govern the release of information about System borrowers and shareholders, already permits Farm Credit banks to disclose the identity of an OFI that consents. If the FCA adopts a final disclosure regulation for OFIs, two System banks suggest preamble clarifications and minor edits to the text of § 614.4595. The CUNA supports proposed § 614.4595 because it believes that disclosure of a credit union's identity will help inform farmers, ranchers, and other eligible borrowers about their other credit options and the benefits of credit union membership. The ICBA suggests the FCA switch from an ''opt-in'' to an ''opt-out'' approach in the final rule. Under an ''opt-out'' approach, each Farm Credit bank would automatically disclose an OFI's identity to the public unless the OFI instructed it, in writing, not to do so. The ICBA contends that an ''opt-out'' approach is consistent with the trend in the law governing disclosure of customer information by financial institutions.

The FCA adopts § 614.4595 as a final rule after slightly changing the text of the regulation in response to a comment from a System bank. The FCA disagrees with the two System commenters that this regulation is unnecessary because the regulations in subpart G of part 618 already govern releases of information about System borrowers and shareholders. As the preambles to the ANPRM and proposed rule explain, the regulations in subpart G of part 618 apply only to releasing information about retail borrowers. For this reason, a new regulation is needed to clarify the authority of System banks to disclose information about OFIs.

The FCA declines the ICBA's request to revise § 615.5495 so that the final regulation requires System banks to disclose an OFI's identity unless the OFI ''opts-out.'' The FCA believes that the ''opt-in'' approach in the proposed rule is easier for System banks to administer than the ''opt-out'' approach favored by the commenter. Requiring an OFI to affirmatively consent, in writing, to the disclosure of its identity avoids the misunderstandings and miscommunications that are more likely to occur if disclosure happens automatically unless or until the OFI takes action to stop it. Also, the FCA's ''opt-in'' approach gives OFIs more control and flexibility over the decision to allow System funding banks to publicly disclose their identity than the ICBA's ''opt-out'' approach. Under the approach in § 615.4595, the OFI decides whether to allow its System funding bank to disclose its identity to the public, and then it communicates its decision to the bank, which honors its decision. In contrast, disclosure occurs under the ''opt-out'' approach unless the OFI takes action to stop it by a certain deadline.

Under final § 614.4595, a Farm Credit Bank or agricultural credit bank may disclose to members of the public the name, address, telephone number, and Internet Web site address of any affiliated OFI only if such OFI, through a duly authorized officer, consents in writing. Each Farm Credit Bank and agricultural credit bank must adopt policies and procedures for requesting, obtaining, and maintaining the consent of its OFIs and for disclosing this information to the public.

The FCA inserted the word ''requesting'' into the final regulation § 614.4595 in response to a comment from a Farm Credit bank. The commenter suggested that the FCA change the word ''obtaining'' in the proposed regulation to ''requesting.'' According to the commenter, a System bank should not be accountable for ''obtaining'' consent from an OFI. The commenter believes that ''requesting'' the OFI's consent is the most the System funding bank can do. After considering this comment, the FCA amended the regulation so it requires System banks to adopt policies and procedures for ''requesting, obtaining, and maintaining'' the consent of its OFIs. This revision enhances the clarity and accuracy of the final regulation. A Farm Credit bank must request and obtain the OFI's written consent before it can publicly disclose the OFI's identity.

One Farm Credit bank asked the FCA for assurances that § 614.4595 does not restrict the System bank's right to file financing statements or other routine public filings that protect its security interest under applicable law. The FCA affirms that the final rule does not hinder the right or ability of any System bank to perfect its security lien in collateral pledged by its OFIs. This approach is similar to other Federal laws that protect the privacy of consumers who buy goods and services on credit. Although these laws restrict the release of confidential information by the creditor, they do not prevent the creditor from filing public documents that enable it to collect the debt in event of default.

G. Associations Acting as Farm Credit Bank Agents

Both System and non-System commenters suggested in their responses to the ANPRM and during testimony at the public meeting that FCS associations could serve as an effective conduit for funding OFIs. These commenters pointed out that associations often have established relationships with local OFIs and other commercial lenders. In many cases, FCS associations and existing and potential OFIs already have entered into joint financing arrangements for common borrowers.

The FCA stated in the preamble to the proposed rule that the Act allows only Farm Credit banks that operate under title I of the Act, not FCS associations, to establish funding and discount relationships with OFIs. However, the preamble to the proposed rule pointed out that section 1.5(18) of the Act allows a Farm Credit bank to delegate to associations such functions as the bank deems appropriate while section 2.2(19) allows a direct lender association to perform functions delegated to it by its funding bank. Thus, sections 1.5(18) and 2.2(19) of the Act enable FCS associations to act as point-of-contact or servicing agents for the Farm Credit bank in its lending relationship with its OFIs.[12]

Allowing FCS associations to act as intermediaries between Farm Credit banks and OFIs may make this program more successful and reduce tensions between the System and OFIs. In particular, designating associations as intermediaries and servicing agents for Farm Credit banks on their OFI loans may help diminish the competitive rivalries that have historically troubled the relationship between OFIs and associations. Farmers and ranchers benefit when FCS associations and OFIs work together. Agreements between the parties can establish these arrangements and, therefore, no new regulation is necessary.

The FCA received 2 comment letters about this issue from a Farm Credit bank and association. The Farm Credit bank commenter concurred that existing statutory authorities are sufficient to support associations acting as agents of Farm Credit banks in their relationship with OFIs and, therefore, no regulation is necessary. The association fully supported allowing associations to act as intermediaries for the Farm Credit banks in establishing and servicing OFI relationships.

[12] *See* 68 FR 47502, 47508 (August 11, 2003).

The FCA reaffirms that FCS associations have no authority under the Act to lend directly to OFIs, but they can act as intermediaries or servicing agents on loans from a Farm Credit bank to OFIs.

H. OFI Lending Limits

In 1998, the FCA repealed former § 614.4565, which imposed a lending limit on the amount of credit that any OFI could extend to a single credit risk with FCS funds. At the time, we acknowledged that certain OFIs would remain subject to lending limits that their primary regulator imposes under applicable Federal or state law. The preamble to the final rule stated that we expect each Farm Credit bank to prudently manage risk exposures to concentrations in OFI loan portfolios through underwriting standards and its general financing agreement (GFA) with each OFI.[13]

After the FCA repealed former § 614.4565, some Farm Credit banks considered imposing a lending limit on both FCS associations and OFIs that is lower than the lending limit that: (1) § 614.4353 establishes for System direct lender associations; and (2) Federal or state laws place on depository institutions. During earlier phases of this rulemaking, two non-System commenters asked us to enact a new regulation that would forbid Farm Credit banks from imposing a lending limit on OFIs that is lower than the limit established by applicable Federal or state law. The FCA declined this request because it is inconsistent with safety and soundness. The preamble to the proposed rule stated that each Farm Credit bank may establish, by underwriting standards and the GFA, limits on its exposure to concentrations in the loan portfolios of both FCS associations and OFIs that are more stringent than lending limits imposed by statute or regulation, as long as it does not favor FCS associations over OFIs.[14]

The FCA received comments on this issue from a Farm Credit bank, the ICBA, and 95 commercial banks. The Farm Credit bank supported the FCA's position. The ICBA agreed with the FCA that lending limits imposed by FCS banks on OFIs should be on the same basis as for FCS associations. The ICBA asserted that System banks should not impose ''unduly restrictive'' lending limits on OFIs, and they should be commensurate with limits set by the OFI's parent or primary regulator. Several commercial banks continued to urge the FCA to enact a regulation that prevents Farm Credit banks from imposing a lending limit that is more stringent than the limit established by Federal or state law.

The FCA reaffirms its earlier position that each Farm Credit bank may establish, by underwriting standards and GFAs, limits on its exposure to concentrations in the loan portfolios of FCS associations and OFIs that are more stringent than lending limits imposed by statute or regulation. However, System banks would not be treating OFIs equitably if they establish lending limits that favor FCS associations over OFIs. Additionally, any decision by a Farm Credit bank to establish a lending limit that is more stringent than the limit imposed on an OFI by applicable Federal or state law, or its corporate parent must have a safety and soundness justification. Commercial bank commenters have provided no new information or analysis that would persuade the FCA to prohibit Farm Credit banks, by regulation, from imposing a lending limit on OFIs that is more stringent than the limit established by law or the corporate parents of such OFIs. The FCA declines this request.

I. Eligible Collateral Pledged To Support an OFI's Discounting Arrangements With a Farm Credit Bank (§ 614.4570)

Currently, § 614.4570 requires a secured lending relationship between each Farm Credit bank and every OFI. Under § 614.4570(b)(2), each FCB or ACB must perfect its security interest in any and all obligations and the proceeds thereunder that the OFI pledges as collateral, in accordance with applicable state law. Additionally, § 614.4570(c) allows each FCB and ACB to require its OFIs to pledge supplemental collateral to support the lending relationship.

A comment letter from a System bank acknowledged that the Act prohibits Farm Credit banks from: (1) Advancing funds for long-term real estate mortgages to OFIs; and (2) accepting mortgages as primary collateral from OFIs. The commenter opined that the statutory ban on System banks funding and discounting agricultural mortgages for OFIs is a major impediment to expansion of this program. The commenter then asked the FCA to develop regulatory interpretations that would enable System banks to overcome this obstacle.

As acknowledged by the commenter, the Act does not authorize long-term funding for OFIs. FCA regulations, policies, or interpretations must comply with the Act. Therefore, an amendment to the Act is necessary to authorize Farm Credit banks to fund or discount agricultural mortgage loans that OFIs make to their customers.

J. Improving the Relationship Between Farm Credit Banks and OFIs

In response to the ANPRM and during the public meeting, several System and non-System commenters offered various suggestions for improving the relationship between Farm Credit banks and prospective and existing OFIs. The commenters' suggestions are confidence-building measures that could attract more OFIs to establish funding and discount relationships with Farm Credit banks. These suggestions could help improve relations between existing OFIs and their funding banks and encourage prospective OFIs to establish funding and discount relationships with Farm Credit banks.

The FCA conveyed these ideas to Farm Credit banks by publishing the suggestions in the preamble to the proposed rule. These suggestions would require Farm Credit banks to take the initiative and reach out to existing and prospective OFIs. More specifically, the FCA encouraged Farm Credit banks to consider developing internal programs and initiatives that:

1. Establish outreach programs for contacting prospective OFIs and providing them with information about the banks' services;
2. Routinely publish updated information about their products and services for OFIs, and their underwriting standards, funding terms and conditions, and pricing guidelines for OFI loans;
3. Allow OFI representatives to observe meetings of the banks' board of directors;
4. Promote better communication through roundtable discussions, focus groups, and public discussions that bring OFIs, associations, and other interested parties together to discuss issues of mutual interest;
5. Work with OFIs to identify and remove administrative barriers that hinder OFI access;
6. Allow FCS associations to act as intermediaries and servicing agents on extensions of credit from the funding bank to OFIs, as discussed earlier; and
7. Identify best practices for OFIs.

The FCA published these suggestions in the preamble to the proposed rule because we are strongly committed to the success of the OFI program. The FCA reasoned that by adopting the internal programs and initiatives described above, Farm Credit banks can attract more OFIs which, in turn, will provide eligible farmers, ranchers, aquatic producers and harvesters, farm-related businesses, and rural

[13] *See* 63 FR 36541, 36545 (July 7, 1998).

[14] *See* 68 FR 47502, 47508 (August 11, 2003).

homeowners with more plentiful and affordable credit, as Congress intended. Another passage in the preamble to the proposed rule advised the public that the FCA may provide additional guidance to Farm Credit banks about improving the OFI program through bookletters, informational memoranda, and the Office of the Ombudsman. The preamble to the proposed rule informed the public that new regulations may not be required to implement these suggestions for improving the OFI program.[15]

The FCA received several comments about this guidance from both FCS and non-System commenters. Letters from commercial banks strongly supported the recommendations and urged the FCA to encourage Farm Credit banks to undertake all of these initiatives so: (1) Their relationships with OFIs would improve; and (2) this program would become more attractive to non-System agricultural lenders. In contrast, System commenters stated that the FCA was interfering in the internal business affairs of System banks without any safety or soundness justification. These commenters found it unusual for the preamble to encourage certain practices at System banks while acknowledging that new regulations are unnecessary.

Four System commenters objected to the suggestion that Farm Credit banks invite OFI observers to their board meetings. According to these commenters, matters discussed at bank board meetings are confidential and only board members and officers attend such meetings. One System commenter objected to the suggestion that Farm Credit banks identify best management practices for OFIs. From this commenter's perspective, OFIs are independent financial institutions that are responsible for their own operation, and Farm Credit banks should not attempt to impose their own views about best management practices on their OFIs. This commenter expressed concern that System banks could be exposed to lender liability claims if they prescribed best management practices to their OFIs.

As stated earlier, the FCA is committed to the success of the OFI program. Providing funding and liquidity to OFIs is an essential and integral part of the public policy mission of System banks to ensure that farmers and ranchers always have access to sound, adequate, and constructive credit. The FCA offered these seven suggestions in the hope that they would encourage System banks to: (1) Reach out to potential OFI applicants and existing OFIs; and (2) take the initiative in building confidence between OFIs and the System. All of these suggestions concentrated on ideas for improving communications between the System and non-System agricultural lenders that are, or may become OFIs.

From time to time, the FCA and other regulators offer guidance to institutions that they regulate. The suggestions are not mandatory, but are guidelines, which pertain to business practices instead of safety and soundness or compliance with laws and regulations. System banks may consider other approaches that foster strong and healthy relationships with OFIs in addition to, or instead of, the ideas that the FCA has suggested. If System banks invite OFI observers to their board meetings, they should consider appropriate measures that protect the confidentiality of information. The FCA emphasizes the importance of System banks reaching out to OFIs.

K. CDFIs

A CDFI urged the FCA to amend the OFI regulations so they facilitate System bank lending to CDFIs that primarily serve young, beginning, small, and low resource farmers and ranchers. The commenter made no specific regulatory recommendations to the FCA with regard to CDFIs being designated as OFIs. The commenter did suggest a regulatory change to treat CDFIs as the equivalent of Organization for Economic Cooperation and Development (OECD) banks[16] for risk-weighting purposes. We address this comment later under section III. *Capital Risk Weighting* of this preamble.

CDFIs are private sector financial intermediaries that offer financial services to economically distressed communities. These institutions provide economically distressed communities with credit, capital, and financial services that often are unavailable from other financial institutions. The Community Development Financial Institutions Fund (CDFI Fund), which is a wholly owned Government corporation within the United States Department of the Treasury (Treasury), certifies and oversees CDFIs.

CDFIs attract capital for their operations from both private and public sources of funding. The CDFI Fund provides financial and technical assistance in the form of grants, loans, equity investments, and deposits to competitively selected CDFIs. The private sector also provides equity investments and credit to CDFIs. Some CDFIs are depository institutions and, therefore, they obtain some funds for their operations from deposits as well as credit lines with other lenders. CDFIs work in partnership with other financial institutions to channel credit and investment into economically distressed communities.

There are six basic types of CDFIs. Specific language in section 1.7(b)(1)(B) of the Act determines whether an entity is eligible to borrow from a Farm Credit bank as an OFI and would authorize certain types of CDFIs as OFIs. Under section 1.7(b)(1)(B) of the Act and § 614.4540 of FCA regulations, two types of CDFIs, community development banks and community development credit unions, could become OFIs that fund, discount, or obtain other similar financial assistance from a Farm Credit bank in order to extend short- and intermediate-term credit to eligible borrowers for authorized purposes pursuant to sections 1.10(b) and 2.4(a) and (b) of the Act. Since the mission of CDFIs is to serve economically distressed segments of the population, those CDFIs that become OFIs may use funding, discount services, and other financial assistance from a Farm Credit bank to serve young, beginning, small, and low resource farmers and ranchers. In addition, the FCA encourages Farm Credit banks to work with eligible CDFIs that make loans or extend other similar financial assistance to agriculture and are interested in establishing an OFI relationship. Because of eligibility restrictions in the Act for OFI funding, no other amendments to the regulations are allowable.

Section 4.19(a) of the Act mandates that Farm Credit banks and associations have programs for furnishing sound and constructive credit and related services to young, beginning, and small (YBS) farmers and ranchers. According to the statute, the YBS program of each FCS direct lender association must comply with policies prescribed by the board of their funding banks. Section 4.19(a) of the Act also states, ''Such programs shall assure that such credit and services are available in coordination with other units of the Farm Credit System serving the territory *and with other governmental and private sources of credit.*'' (Emphasis added.)

A CDFI that seeks funding, discount services, and other financial assistance

[15] Ibid.

[16] *OECD* means the group of countries that are full members of the Organization for Economic Cooperation and Development, regardless of entry date, as well as countries that have concluded special lending arrangements with the International Monetary Fund's General Arrangement to Borrow, excluding any country that has rescheduled its external sovereign debt within the previous 5 years. For purposes of United States banking operations, all federally regulated depository institutions are considered the equivalent of OECD banks.

from a Farm Credit bank should consult with the bank about how they can work together to provide credit to YBS and low resource farmers and ranchers. When feasible, the Farm Credit bank should encourage CDFIs and local FCS associations to coordinate their efforts to serve YBS and low resource farmers and ranchers.

III. Capital Risk Weighting

A. Background

As discussed in the preamble to the proposed rule, we have interpreted our capital adequacy regulations as requiring Farm Credit banks to risk weight loans to OFIs at 100 percent. In contrast, existing § 615.5210(f)(2)(ii)(I) allows Farm Credit banks to risk weight loans to System associations at 20 percent. This means Farm Credit banks currently hold more capital (at a minimum) for loans to OFIs than loans to System associations, which in many cases have similar structures and financial conditions as OFIs. The preamble to the ANPRM explained, in detail, the risk-reducing features of FCS associations that justified a 20-percent risk weighting.[17]

The FCA acknowledged in the preambles to the ANPRM and the proposed rule that many OFIs, particularly commercial banks or their affiliates, might pose no greater risk to their FCS funding bank than System associations. However, unregulated non-bank OFIs could expose the FCS bank to greater risk than FCS associations and regulated OFIs.

The risk-weighting categories in FCA's capital regulations are patterned after the risk-weighting categories in the 1988 Basel Accord, which apply to all depository institutions regulated by the other Federal bank regulatory agencies. As a result, many, but not all, OFIs have the same risk-reducing features as FCS associations.

The FCA proposed amendments to § 615.5210 that would permit Farm Credit banks to risk weight their loans to OFIs that are Federal- or state-regulated depository institutions, or their affiliates, at 20 percent. Under this proposal, Farm Credit banks would continue to risk weight loans to OFIs that are unregulated, or exhibit a higher risk profile at either 50 or 100 percent, depending on certain factors.

The proposed rule would establish a 20-percent risk weighting for OFIs that are either: (1) An equivalent to an OECD bank (Federal- or state-regulated depository institution); (2) subsidiaries of OECD equivalent banks or bank holding companies and carry full guarantees from such parent entities; or (3) an institution that carries one of the three highest ratings from a nationally recognized statistical rating organization (NRSRO).[18] OFIs are required by regulations to pledge full recourse on all loans they fund or discount with a Farm Credit bank.

Proposed § 615.5210 would establish a 50-percent risk weighting for OFIs that: (1) Are not OECD banks but otherwise meet similar capital and operational standards; and (2) carry an investment grade or higher NRSRO rating. The FCA proposed to retain a 100-percent risk weighting for all loans to OFIs that do not qualify for the 20-percent or 50-percent risk-weight categories.

B. Comments Received

We received 98 comments on capital risk weighting in response to our proposed rule. The comments came from 3 Farm Credit banks, a CDFI, an OFI that is affiliated with a group of farmer cooperatives, the CUNA, the ICBA, and 91 commercial banks. The majority of the commenters supported differentiating the risk weighting of loans to OFIs based on the structure and risk-mitigating characteristics of the OFIs.

The 3 Farm Credit banks generally supported the proposed capital risk-weighting rule for OFIs. However, these commenters sought clarification of two issues, and they requested two technical changes to the regulation. The CUNA supported the rule as proposed, while the ICBA and 47 bankers supported equal risk weighting for FCS associations and OFIs that are depository institutions or their affiliates. Forty-four (44) commercial bank commenters supported equal risk-weighting treatment for all OFIs and the FCS associations. The CDFI stated that the final rule should require Farm Credit banks to risk weight all CDFIs at 20 percent. The CDFI also stated that all CDFIs should be treated as equivalent to OECD banks because of the CDFIs ''good standing'' status with Treasury. The agricultural credit cooperative OFI expressed concern that the new regulation will increase the cost of funds to OFIs that are risk weighted at 100 percent.

A Farm Credit bank asked the FCA to clarify whether the three highest NRSRO investment ratings (for institutions that are risk weighted at 20 percent) include subset designations (*e.g.*, AAA+, AA+, or A+). The FCA responds that the regulation refers to the generic rating categories, not plus or minus signs that show relative standing within each rating category. Under this regulation, for example, a rating of ''AA−'' would be within the second highest investment-grade ratings by an NRSRO.

Two Farm Credit banks asked the FCA whether the full recourse requirement for OFIs extended to their parents. According to these commenters, requiring both the parent and the OFI subsidiary to pledge full recourse on the OFI's loan (so the funding bank could risk weight it at 20 percent) could become a significant impediment to the growth of the OFI program. One of these commenters expressed concern that requiring the parent to pledge full recourse to the System funding bank clashes with its capital reasons for establishing an OFI subsidiary. The FCA replies that the rule requires full recourse from the OFI. Generally, the full recourse requirement would not extend to an OFI's parent, but the System funding bank could require it to provide such a guarantee as a condition for approving the OFI for credit.

A Farm Credit bank suggested that the final rule allow OFIs that are not OECD banks or their affiliates to qualify for a 20-percent risk weighting if they receive an investment grade or higher rating from a NRSRO. Under the proposed rule, such OFIs do not qualify for a 20-percent risk weighting unless a NRSRO rates them in one of the three highest investment rating categories. However, OFIs that are not OECD banks or their affiliates could qualify for a 50-percent risk weighting under the proposed rule if they receive an investment-grade rating by a NRSRO and they meet the other requirements of this regulation.

The FCA rejects the commenter's recommendation because it eliminates the distinction in the regulation between OFIs that are risk weighted at 20 percent and those that are risk weighted at 50 percent. NRSRO ratings provide Farm Credit banks with a credible, objective, and independent standard for determining risk exposure from an OFI. Each risk-weighting category in our regulation is based on the System's potential exposures to risk, as well as risk mitigation factors. A lower investment rating from a NRSRO means that an OFI (that is not an OECD bank or its affiliate) exposes its System

[17] *See* 65 FR 21151 (April 20, 2000).

[18] ''Nationally recognized statistical rating organization'' means an entity recognized by the Division of Market Regulation of the Securities and Exchange Commission (or any successor Division) (Commission) as a nationally recognized statistical rating organization for various purposes, including the Commission's uniform net capital requirements for brokers and dealers.

funding bank to greater risks which, in turn, justifies a 50-percent, not a 20-percent, risk weighting. The FCA's approach is consistent with the approach taken by the other federal bank regulatory agencies and pending revisions to the Basel Accord. For this reason, the final rule will require each Farm Credit bank to risk weight OFIs that are not OECD banks or their affiliates at 20 percent only if they achieve and maintain one of the three highest investment-grade ratings from a NRSRO.

A Farm Credit bank asked the FCA to amend a provision in the proposed rule so that an OFI can qualify for a 50-percent risk weighting if its loan is guaranteed by a parent that receives an investment grade or higher rating from a NRSRO. The rule already allows an OFI to qualify for a 20-percent risk weighting if its parent: (1) Guarantees the loan; and (2) has one of the three highest NRSRO investment-grade ratings. The commenter sought this change so that the final rule applies consistent standards for risk weighting OFIs at either 20 or 50 percent. The FCA agrees with the commenter and, accordingly, the final rule includes this change.

As discussed earlier, the agricultural credit cooperative OFI expressed concern that this regulation will increase the cost of funds to OFIs that are risk weighted at 100 percent. The FCA believes that this concern has no merit. All OFIs are currently risk weighted at 100 percent. Lowering the risk weighting of some OFIs based on lower risk profiles should not result in increased costs to other OFIs. Although the regulation differentiates between OFIs on the basis of risk to the funding bank, the FCA does not expect that FCS banks should raise the cost of funding that they charge to OFIs that do not fall within the 20- or 50-percent risk-weighting categories.

In response to the ICBA and other commercial bank commenters, the FCA confirms that the final rule treats FCS associations and OECD banks the same for risk-weighting purposes. As discussed earlier, the CDFI inquired about the risk weighting of CDFIs that become OFIs. The FCA replies that CDFIs as a group are not considered the equivalent of OECD banks despite their ''good standing'' status with Treasury. The certification criteria imposed on CDFIs by Treasury are mission-based rather than safety- and soundness-based and, therefore, do not address risk identification and control criteria as required of the OECD banks by the federal bank regulatory agencies. Accordingly, it would be inconsistent with the agency's safety- and soundness-based regulations to automatically equate CDFIs as equivalent to the risk weighting for OECD banks. However, CDFIs that are community banks and credit unions would probably qualify as OECD banks and, therefore, a Farm Credit bank could risk weight discounted CDFI loans at 20 percent.

Forty-four (44) commercial bank commenters took the position that the risk weighting for all OFIs and FCS associations should be the same. As explained earlier, not all OFIs pose the same risks to their funding banks. Some OFIs are not OECD banks or their affiliates. In other cases, nonbank OFIs do not meet the capital, risk identification and control, and operational standards that apply to OECD banks, or they do not carry an investment-grade rating from a NRSRO. For these reasons, not all OFIs should be risk weighted at 20 percent.

C. Final Rule

The final rule establishes a 20-percent risk weighting for OFIs that are either: (1) An equivalent to an OECD bank (Federal-or state-regulated depository institution); (2) subsidiaries of OECD equivalent banks or bank holding companies and carry full guarantees from such parent entities; or (3) an institution that carries one of the three highest investment-grade ratings from a NRSRO.

Under final § 615.5210, a 50-percent risk weighting applies to OFIs that: (1) Are not OECD banks but otherwise meet similar capital, risk identification and control, and operational standards; and (2) carry an investment-grade or higher NRSRO rating, or the claim is guaranteed by a parent company with such a rating.

The final rule establishes a 100-percent risk weighting for all OFI loans that do not qualify for the 20-percent or 50-percent risk-weight categories. OFIs that are well-capitalized and well-managed expose the System to less risk. Therefore, FCS institutions need less capital to support loans to these OFIs. This approach is consistent with the direction from the pending Basel Accord revisions, which are currently under consideration.

Lowering the capital requirements for most OFI loans will lower the operating costs of the OFI program to Farm Credit banks. This, in turn, should lower the cost of funds to well-capitalized and well-managed OFIs. Lower funding costs should enable these OFIs to reduce interest rates charged to their borrowers. These results would advance the System's public policy mission to provide affordable credit on a consistent basis to agriculture and rural America. Greater flexibility for the risk weighting of OFI loans should provide the Farm Credit banks additional incentives to expand their lending to both existing and new OFIs.

IV. Regulatory Flexibility Act

Pursuant to section 605(b) of the Regulatory Flexibility Act (5 U.S.C. 601 *et seq.*), the FCA hereby certifies that the final rule will not have a significant economic impact on a substantial number of small entities. Each of the banks in the System, considered together with its affiliated associations, has assets and annual income in excess of the amounts that would qualify them as small entities. Therefore, System institutions are not ''small entities'' as defined in the Regulatory Flexibility Act.

List of Subjects

12 CFR Part 614

Agriculture, Banks, Banking, Foreign trade, Reporting and recordkeeping requirements, Rural areas.

12 CFR Part 615

Accounting, Agriculture, Banks, Banking, Government securities, Investments, Rural areas.

■ For the reasons stated in the preamble, parts 614 and 615, chapter VI, title 12 of the Code of Federal Regulations are amended as follows:

PART 614—LOAN POLICIES AND OPERATIONS

■ 1. The authority citation for part 614 continues to read as follows:

Authority: 42 U.S.C. 4012a, 4104a, 4104b, 4106, and 4128; secs. 1.3, 1.5, 1.6, 1.7, 1.9, 1.10, 1.11, 2.0, 2.2, 2.3, 2.4, 2.10, 2.12, 2.13, 2.15, 3.0, 3.1, 3.3, 3.7, 3.8, 3.10, 3.20, 3.28, 4.12, 4.12A, 4.13B, 4.14, 4.14A, 4.14C, 4.14D, 4.14E, 4.18, 4.18A, 4.19, 4.25, 4.26, 4.27, 4.28, 4.36, 4.37, 5.9, 5.10, 5.17, 7.0, 7.2, 7.6, 7.8, 7.12, 7.13, 8.0, 8.5 of the Farm Credit Act (12 U.S.C. 2011, 2013, 2014, 2015, 2017, 2018, 2019, 2071, 2073, 2074, 2075, 2091, 2093, 2094, 2097, 2121, 2122, 2124, 2128, 2129, 2131, 2141, 2149, 2183, 2184, 2201, 2202, 2202a, 2202c, 2202d, 2202e, 2206, 2206a, 2207, 2211, 2212, 2213, 2214, 2219a, 2219b, 2243, 2244, 2252, 2279a, 2279a–2, 2279b, 2279c–1, 2279f, 2279f–1, 2279aa, 2279aa–5); sec. 413 of Pub. L. 100–233, 101 Stat. 1568, 1639.

Subpart P—Farm Credit Bank and Agricultural Credit Bank Financing of Other Financing Institutions

■ 2. Revise § 614.4540(c) to read as follows:

§ 614.4540 Other financing institution access to Farm Credit Banks and agricultural credit banks for funding, discount, and other similar financial assistance.

* * * * *

(c) *Underwriting standards.* Each Farm Credit Bank and agricultural credit bank shall establish objective policies, procedures, pricing guidelines, and loan underwriting standards for determining the creditworthiness of each OFI applicant. A copy of such policies, procedures, guidelines, and standards shall be made available, upon request to each OFI and OFI applicant.

* * * * *

■ 3. Revise § 614.4550 to read as follows:

§ 614.4550 Place of discount.

A Farm Credit Bank or agricultural credit bank may provide funding, discounting, or other similar financial assistance to any OFI applicant. However, a Farm Credit Bank or agricultural credit bank cannot fund, discount, or extend other similar financial assistance to an OFI that maintains its headquarters, or has more than 50 percent of its outstanding loan volume to eligible borrowers who conduct agricultural or aquatic operations in the chartered territory of another Farm Credit bank unless it notifies such bank in writing within five (5) business days of receiving the OFI's application for financing. Two or more Farm Credit banks cannot simultaneously fund the same OFI.

■ 4. Revise § 614.4560(d) to read as follows:

§ 614.4560 Requirements for OFI funding relationships.

* * * * *

(d) The borrower rights requirements in part C of title IV of the Act, and the regulations in part 617 of this chapter shall apply to all loans that an OFI funds or discounts through a Farm Credit Bank or agricultural credit bank, unless such loans are subject to the Truth-in-Lending Act, 15 U.S.C. 1601 *et seq.*

* * * * *

■ 5. Amend § 614.4590 by adding new paragraphs (c) and (d) to read as follows:

§ 614.4590 Equitable treatment of OFIs and Farm Credit System associations.

* * * * *

(c) Upon request, each Farm Credit Bank or agricultural credit bank must provide each OFI and OFI applicant, that has or is seeking to establish a funding relationship with the Farm Credit Bank or agricultural credit bank, a copy of its policies, procedures, loan underwriting standards, and pricing guidelines for OFIs. The pricing guidelines must identify the specific components that make up the cost of funds for OFIs, and the amount of these components expressed in basis points.

(d) Upon request of any OFI or OFI applicant, that has or is seeking to establish a funding relationship with the Farm Credit Bank or agricultural credit bank, the bank must explain in writing the reasons for any variation in the overall funding costs it charges to OFIs and affiliated direct lender associations. The written explanation must compare the cost of funds that the Farm Credit Bank or agricultural credit bank charges the OFIs and affiliated direct lender associations. When possible, the written explanation shall compare the costs of funding that the bank charges several OFIs and Farm Credit associations that are similar in size. However, the Farm Credit Bank or agricultural credit bank must not disclose financial or confidential information about any individual Farm Credit association.

Subpart P—[Amended]

■ 6. Amend part 614, subpart P by adding a new § 614.4595 to read as follows:

§ 614.4595 Public disclosure about OFIs.

A Farm Credit Bank or agricultural credit bank may disclose to members of the public the name, address, telephone number, and Internet Web site address of any affiliated OFI only if such OFI, through a duly authorized officer, consents in writing. Each Farm Credit Bank and agricultural credit bank must adopt policies and procedures for requesting, obtaining, and maintaining the consent of its OFIs and for disclosing this information to the public.

PART 615—FUNDING AND FISCAL AFFAIRS, LOAN POLICIES AND OPERATIONS, AND FUNDING OPERATIONS

■ 7. The authority citation for part 615 continues to read as follows:

Authority: Secs. 1.5, 1.7, 1.10, 1.11, 1.12, 2.2, 2.3, 2.4, 2.5, 2.12, 3.1, 3.7, 3.11, 3.25, 4.3, 4.3A, 4.9, 4.14B, 4.25, 5.9, 5.17, 6.20, 6.26, 8.0, 8.3, 8.4, 8.6, 8.7, 8.8, 8.10, 8.12 of the Farm Credit Act (12 U.S.C. 2013, 2015, 2018, 2019, 2020, 2073, 2074, 2075, 2076, 2093, 2122, 2128, 2132, 2146, 2154, 2154a, 2160, 2202b, 2211, 2243, 2252, 2278b, 2278b–6, 2279aa, 2279aa–3, 2279aa–4, 2279aa–6, 2279aa–7, 2279aa–8, 2279aa–10, 2279aa–12); sec. 301(a) of Pub. L. 100–233, 101 Stat. 1568, 1608.

Subpart H—Capital Adequacy

■ 8. Amend § 615.5210 by adding new paragraphs (f)(2)(ii)(M); (f)(2)(iii)(C); and (f)(2)(iv)(E) to read as follows:

§ 615.5210 Computation of the permanent capital ratio.

* * * * *

(f) * * *

(2) * * *

(ii) * * *

* * * * *

(M) Claims on other financing institutions provided that:

(*1*) The other financing institution qualifies as an OECD bank or it is owned and controlled by an OECD bank that guarantees the claim, or

(*2*) The other financing institution has a rating in one of the highest three investment-grade rating categories from a NRSRO or the claim is guaranteed by a parent company with such a rating, and

(*3*) The other financing institution has endorsed all obligations it pledges to its funding Farm Credit bank with full recourse.

(iii) * * *

(C) Claims on other financing institutions that:

(*1*) Are not covered by the provisions of paragraph (f)(2)(ii)(M) of this section, but otherwise meet similar capital, risk identification and control, and operational standards, or

(*2*) Carry an investment-grade or higher NRSRO rating or the claim is guaranteed by a parent company with such a rating, and

(*3*) The other financing institution has endorsed all obligations it pledges to its funding Farm Credit bank with full recourse.

(iv) * * *

(E) Claims on other financing institutions that do not otherwise qualify for a lower risk-weight category under this section.

* * * * *

Dated: May 20, 2004.

Jeanette C. Brinkley,

Secretary, Farm Credit Administration Board.

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