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Handbook Mailing HM-09-4

[6705-01-P]

FARM CREDIT ADMINISTRATION

12 CFR Parts 619, 620, and 621

RIN 3052-AC35

Definitions; Disclosure to Shareholders; Accounting and Reporting Requirements; Disclosure and Accounting Requirements

AGENCY: Farm Credit Administration.

ACTION: Final rule.

SUMMARY: The Farm Credit Administration (FCA, we, or our) issues this final rule amending FCA's regulations related to disclosure and reporting practices of Farm Credit System (System) institutions. This rule updates references to accounting terminology, streamlines requirements for filing quarterly reports and the content of the annual report to shareholders, and updates the requirements for maintaining an allowance for loan losses. The amendments ensure that FCA regulations are consistent with System structural changes and are updated to include changes to accounting and reporting standards.

EFFECTIVE DATE: This regulation will be effective 30 days after publication in the Federal Register during which 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:

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SUPPLEMENTARY INFORMATION:

I. Objectives

The objectives of this final rule are to:

- Clarify FCA regulations related to disclosure and reporting practices of System institutions; and

- Ensure that FCA regulations are consistent with System structural changes and updated to include changes to accounting and reporting standards.

II. Background

The Farm Credit Amendments Act of 1985 (1985 Amendments)¹ added provisions to the Farm Credit Act of 1971, as amended (Act),² requiring FCA to regulate the disclosure and reporting practices of System institutions. In keeping with this provision, we published a proposed regulation in the Federal Register (73 FR 70921) on November 24, 2008, to amend parts 619, 620, and 621 affecting references to accounting terminology, requirements for the content of the annual report to shareholders, requirements for filing quarterly reports to shareholders, and requirements for maintaining an allowance for loan losses. We also proposed certain other clarifications and technical changes to our reporting and disclosure regulations. The proposed rule was published with a 60-day comment period, which closed on January 23, 2009.

III. Comments and Our Response

We received three comment letters on the proposed rule. Of the comment letters received, one was from the Federal Farm Credit Banks Funding Corporation (Funding Corporation) on behalf of the Farm Credit System's Accounting Standards Workgroup, one was from the Farm Credit Council (FCC) acting for its membership, and one was from a System association. In general, the commenters supported the proposed rule, but suggested additional changes to our rules. The commenters stated the suggested changes would allow for additional flexibility in meeting disclosure requirements. We discuss the comments to our proposed rule and provide our responses below. Those provisions of the proposed rule that did not receive comments are finalized as proposed.

A. Generally Accepted Auditing Standards [§§ 619.9270(e) and 621.2(d)]

We received no comments on our proposal to replace the language in § 621.2(d) referring to Auditing Standards Board of the American Institute of Certified Public Accountants (AICPA) with a reference to generally accepted auditing standards. We also received no comments on our proposed conforming change in § 619.9270(e) to replace the reference to AICPA with a reference to the authoritative body governing overall audit quality. We final these changes as proposed.

B. Signatures on Financial Reports [§ 620.3(b)(3)]

We received no comments on our proposal to remove the reference to reports of condition and performance from the signature requirements of § 620.3(b)(3). We finalize the change as proposed.

C. Contents of the Annual Report to Shareholders; Incorporation by Reference [§ 620.5(a) through (e)]

We received three comments supporting our proposal to allow the information required by § 620.5(a) through (e) to be incorporated by reference to the Management's Discussion and Analysis (MD&A) section. The commenters also suggested that we allow incorporation by reference in other areas of the report, not just the MD&A.

While we received support for the proposed change to § 620.5, we have determined it is unnecessary to change our existing rules and withdraw the proposed change. We originally proposed a change to allow incorporation in the MD&A the annual report items contained in paragraphs (a) through

(e) of § 620.5. We, in part, made this proposal because of the existing introductory language of § 620.5 stating that the annual report “must contain the following items in substantially the same order.” However, existing § 620.2(d) provides that information in any part of the annual report may be incorporated by reference in answer to any other item of the report. In consideration of this language and the introductory language of § 620.5, we believe institutions are already authorized under the provisions of § 620.2(d) to incorporate the information of any required section of the annual report in another section, if the institution desires to do so. However, to ensure compliance the introductory language of § 620.5, institutions applying the provisions of § 620.2(d) will need to maintain the annual report section headings, as identified in § 620.5, and state under the heading where the “answer” may be found, i.e. the location where the reader may find the information.

D. Description of Business; Significant Developments [§ 620.5(a)(4)]

We received no comments on the proposal to require the disclosure of significant developments that had or could have material impact on patronage and dividends. We finalize the change as proposed.

However, we received three comments suggesting that the current requirement to report significant developments for the last 5 years be limited to the last 3 years. The commenters explained that such a change would be consistent with the requirement in § 620.5(m) to furnish financial statements and related footnotes for the last 3 years. The commenters also explained that the continuation of the 5-year disclosure requirement would provide no additional relevant information to the reader. While we consider the suggested change to our rule worth additional consideration, we did not propose this change. We cannot, in this final rulemaking, make the change without providing additional notice and comment because it does not constitute a logical outgrowth of the proposed rulemaking. We will, however, consider this issue in a future rulemaking.

E. Description of Business; the Institution’s Interdependent Relationship with its Funding Bank [§ 620.5(a)(10)]

We proposed removing language that may be interpreted as limiting disclosures of certain interdependent relationships, including removal of paragraph (a)(10)(v). We also proposed new language for paragraph (a)(10) that captures a broader relationship between associations and their funding banks, including the elements of paragraph (a)(10)(v). We received no comments on our proposal and final these changes as proposed.

F. Description of Liabilities; Description of Statutory Responsibility for Repayment of Obligations Issued by the Farm Credit System Financial Assistance Corporation [§ 620.5(e)(4)]

We received no comments on our proposal to remove a remaining reference in § 620.5(e)(4) to the Farm Credit System Financial Assistance Corporation (FAC), which is no longer a chartered entity. We final this change as proposed.

G. Selected Financial Data; Associations that are not Direct Lender Associations [§ 620.5(f)(2)]

We received no comments on our proposal to remove § 620.5(f)(2) addressing associations that are not direct lender associations. All System associations are now direct lenders. We final this change as proposed.

H. Description of Funding Sources [§ 620.5(g)(3)(i)(A)]

We received no comments on our proposed clarification that § 620.5(g)(3)(i)(A) applies to all debt obligations held by each System institution, not just the consolidated System-wide debt and bond obligations. We final this change as proposed.

I. Listing of Directors and Senior Officers and their Terms of Office [§ 620.5(h)(1)]

We received no comments on the proposal to require disclosure of the date each senior officer commenced employment in his/her current position. We are finalizing this change as proposed.

We did receive three comments on this section suggesting changes not otherwise proposed. The commenters suggested requiring disclosure of prior positions held, if in the current position less than 5 years, explaining that it would provide useful information. The commenters contend that without this information the experience of the senior officer would be understated. We believe the commenters' concerns are sufficiently addressed by the requirements in § 620.5(h)(2). However, if institutions wish to disclose more information than that required by regulation, such additional disclosures may be made, provided that the disclosures comply with § 620.3(a).

J. Director Compensation [§ 620.5(i)(1)]

We received no comments on our proposal to clarify that the disclosures required by § 620.5(i)(1) apply to all directors who served in that capacity during the fiscal year, including those who resigned from the board or whose terms expired during the fiscal year. We final this change as proposed.

K. Fees Paid to the Qualified Public Accountant Engaged to Conduct the Financial Statement Audit [§ 620.5(l)(2)]

We received no comments on our proposal clarifying that disclosure of fees paid to the qualified public accountant applies only to the the qualified public accountant engaged to conduct the audit of the institution's financial statement. We finalize this change as proposed.

L. Preparing and Publishing the Quarterly Report [§ 620.10(a)]

We received no comments on our proposals to require institutions to electronically file the quarterly report with the FCA and publish the report on the institution's Web site. We also received no comments on our proposal to replace "Farm Credit bank and direct lender association" with "institution" in § 620.10. We final these changes as proposed.

M. Interim Financial Statements and Pro Forma Presentations Subsequent to Consummation of a Business Combination [§ 620.11(b)(4) and (b)(5)], and Reporting Accounting Changes and Error Corrections [§ 620.11(b)(6) and (b)(7)]

We received no comments on our proposal to remove § 620.11(b)(4) through (7) due to recent changes in accounting standards. We final these changes as proposed.

N. Independent Public Accountant [§§ 620.11(e) and 620.21(f)]

We received no comments on our proposal to replace the references to "independent public accountant" with "qualified public accountant or external auditor" in §§ 620.11(e) and 620.21(f). We final these changes as proposed.

O. Accounting for the Allowance for Loan Losses and Chargeoffs [§ 621.5(a)]

We received no comments on our proposal to revise § 621.5(a) by clarifying that a System institution's allowance for loan losses should be determined in accordance with GAAP. We final this change as proposed.

P. Reports of Condition and Performance; Applicability and General Instructions; Filing of Reports [§ 621.12(c)]

We received no comments on our proposal to require institutions to file their Call Reports electronically in accordance with the instructions prescribed by the FCA. We final this change as proposed.

Q. Technical Corrections [§ 620.5]

We received no comments on our proposal to replace the word “financing” with the word “financial”. We final this change as proposed.

IV. Regulatory Flexibility Act

Pursuant to section 605(b) of the Regulatory Flexibility Act (5 U.S.C. 601 *et seq.*), 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 Farm Credit 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.

¹Pub. L. 99-205, 99 Stat. 1678, Dec. 23, 1985.

²Pub. L. 92-181, 85 Stat. 583, Dec. 10, 1971.

List of Subjects in 12 CFR Parts 619, 620 and 621

Accounting, Agriculture, Banks, banking, Reporting and recordkeeping requirements, Rural areas.

For reasons stated in the preamble, parts 619, 620, and 621 of chapter VI, title 12 of the Code of Federal Regulations are amended as follows:

PART 619--DEFINITIONS

1. The authority citation for part 619 is revised to read as follows:

Authority: Secs. 1.4, 1.7, 2.1, 2.4, 2.11, 3.2, 3.21, 4.9, 5.9, 5.17, 5.18, 5.19, 7.0, 7.1, 7.6, 7.8, and 7.12 of the Farm Credit Act (12 U.S.C. 2012, 2015, 2072, 2075, 2092, 2123, 2142, 2160, 2243, 2252, 2253, 2254, 2279a, 2279a-1, 2279b, 2279c-1, 2279f).

2. Section 619.9270 is amended by revising the second sentence of paragraph (e) to read as follows:

§ 619.9270 Qualified Public Accountant or External Auditor.

* * * * *

(e) * * * For the purposes of this definition, the term “independent” has the same meaning as under the rules and interpretations of the authoritative body governing overall audit performance. * * *

PART 620--DISCLOSURE TO SHAREHOLDERS

3. The authority citation for part 620 is revised to read as follows:

Authority: Secs. 4.19, 5.9, 5.17, 5.19, 8.11 of the Farm Credit Act (12 U.S.C. 2207, 2243, 2252, 2254, 2279aa-11); sec. 424 of Pub. L. 100-233, 101 Stat. 1568, 1656.

Subpart A--General

4. Section 620.3 is amended by revising paragraph (b)(3) as follows:

§ 620.3 Accuracy of reports and assessment of internal control over financial reporting.

* * * * *

(b) * * *

(3) A board member formally designated by action of the board to certify reports on behalf of individual board members.

* * * * *

Subpart B--Annual Report to Shareholders

5. Amend § 620.5 as follows:

a. Remove the word “financing” and add in its place the word “financial” each place it appears in paragraphs (e)(2), (f) heading and introductory text, (f)(1)(iii) heading, (g) heading and introductory text, (g)(1)(iv), (g)(2)(ii), (g)(2)(vi), (j)(3)(ii), and (m)(1);

- b. Revise paragraphs (a)(4), (a)(10) introductory text, (g)(3)(i)(A), (h)(1), (i)(1) introductory text, and the first sentence of paragraph (l)(2);
- c. Remove paragraphs (a)(10)(v), (e)(4) and (f)(2); d. Add the word “and” at the end of paragraph (a)(10)(iii);
- e. Remove “; and” and add a period at the end of paragraph (a)(10)(iv); and
- f. Redesignate existing paragraphs (f)(3) and (f)(4) as newly designated paragraphs (f)(2) and (f)(3).

§ 620.5 Contents of the annual report to shareholders.

* * * * *

(a) * * *

(4) Any significant developments within the last 5 years that had or could have a material impact on earnings, interest rates to borrowers, patronage, or dividends, including, but not limited to, changes in the reporting entity, changes in patronage policies and practices, and financial assistance provided by or to the institution through loss-sharing or capital preservation agreements or from any other source;

* * * * *

(10) For associations, in a separate section of the annual report, discuss the interdependent relationship between the association and its funding bank, including, but not limited to, the financial relationship, a service provider relationship, other material operational relationships, and other specific issues or areas that create a material interdependent relationship between the association and its funding bank. This separate section may incorporate by reference information from other sections of the annual report. At a minimum, the separate section must include the statement required by § 620.2(h)(2)(i) of this part and the following information required elsewhere in this section, if applicable:

* * * * *

(g) * * *

(3) * * *

(i) * * *

(A) Describe the average and yearend amounts, maturities, and interest rates on outstanding consolidated System-wide debt obligations, bond obligations, or any other obligations used to fund the institution's lending operations.

* * * * *

(h) * * *

(1) List the names of all directors and senior officers of the institution, indicating the position title and term of office of each director, and the position, title, and date each senior officer commenced employment in his or her current position.

* * * * *

(i) * * *

(1) *Director compensation.* Describe the arrangements under which directors of the institution are compensated for all services as a director (including total cash compensation and noncash compensation). Noncash compensation with an annual aggregate value of less than \$5,000 does not have to be reported. State the total cash and reportable noncash compensation paid to all directors as a group during the last fiscal year. For the purposes of this paragraph, disclosure of compensation paid to and days served by directors applies to any director who served in that capacity at any time during the reporting period. If applicable, describe any exceptional circumstances justifying the additional director compensation as authorized by § 611.400(c) of this chapter. For each director, state:

* * * * *

(1) * * *

(2) Disclose the total fees, by the category of services provided, paid during the reporting period to the qualified public accountant engaged to conduct the institution’s financial statement audit. * * *

* * * * *

Subpart C--Quarterly Report

6. Amend § 620.10 by revising paragraph (a) to read as follows:

§ 620.10 Preparing the quarterly report.

(a) Each institution of the Farm Credit System must:

(1) Prepare and send, to the Farm Credit Administration, an electronic copy of its quarterly report within 40 calendar days after the end of each fiscal quarter, except that no report need be prepared for the fiscal quarter that coincides with the end of the fiscal year of the institution; and

(2) Publish a copy of its quarterly report on its Web site when it electronically sends the report to the Farm Credit Administration.

* * * * *

§ 620.11 [Amended]

7. Amend § 620.11 as follows:

a. Remove paragraphs (b)(4) through (b)(7);

b. Redesignate existing paragraph (b)(8) as newly designated paragraph (b)(4); and

c. Remove the words “independent public accountant,” “an independent public accountant,” and “the independent accountant” and add in their place, the words “a qualified public accountant or external auditor” in each place they appear in paragraph (e) and its heading.

Subpart E--Annual Meeting Information Statement

8. Amend § 620.21 by revising the heading and paragraph (f) to read as follows:

§ 620.21 Contents of the information statement and other information to be furnished in connection with the annual meeting or director elections.

* * * * *

(f) *Relationship with qualified public accountant or external auditor.* If an institution of the Farm Credit System has had a change or changes in its qualified public accountant or external auditor since the last annual report to shareholders, or if a disagreement with a qualified public accountant or external auditor has occurred, the institution shall disclose the information required by § 621.4(c) and (d) of this chapter.

PART 621--ACCOUNTING AND REPORTING REQUIREMENTS

9. The authority citation for part 621 continues to read as follows:

Authority: Secs. 5.17, 8.11 of the Farm Credit Act (12 U.S.C. 2252, 2279aa-11); sec. 514 of Pub. L. 102-552.

Subpart A--Purpose and Definitions

10. Amend § 621.2 by revising paragraph (d) to read as follows:

§ 621.2 Definitions.

* * * * *

(d) *Generally accepted auditing standards* means the standards and guidelines that are generally accepted in the United States of America and that are adopted by the authoritative body that governs the overall quality of audit performance.

* * * * *

Subpart B--General Rules

11. Amend § 621.5 by revising paragraph (a) to read as follows:

§ 621.5 Accounting for the allowance for loan losses and chargeoffs.

* * * * *

(a) Maintain at all times an allowance for loan losses that is determined according to generally accepted accounting principles.

* * * * *

Subpart D--Report of Condition and Performance

12. Amend § 621.12 by revising paragraph (c) as follows:

§ 621.12 Applicability and general instructions.

* * * * *

(c) All reports of condition and performance shall be submitted electronically in accordance with the instructions prescribed by the Farm Credit Administration and located on its Web site.

Date: June 12, 2009

**Gaye Calhoun,
Acting Secretary,
Farm Credit Administration Board.**