

FCA's Amendments to Regulation Parts 611 and Parts 615 (Adopted by the FCA Board March 8, 2001)

The following are answers to questions that you may have regarding amendments to Parts 611 and 615 of the FCA's regulation. Exhibit 1 provides a table showing the old regulation requirements, the new regulation requirements, and the reason for the amendment.

Part 611 – Service Corporations

What is a service corporation?

A service corporation is an entity organized to perform any function that a Farm Credit bank or association is authorized to perform under the Farm Credit Act of 1971, as amended (Act) and our regulations. However, a service corporation may not extend credit or provide insurance services.

Who organizes service corporations?

Farm Credit banks and associations acting alone or with other Farm Credit banks and associations may organize service corporations. The FCA must charter any new Farm Credit System entity, including service corporations.

How many service corporations exist in the Farm Credit System?

Currently there are four. More service corporations existed in the past.

What are the material amendments to the FCA's service corporation regulations?

We made the following amendments to the regulations:

- We require a service corporation that issues equities to provide adequate disclosures that adhere to our disclosure regulations, and
- We allow a service corporation to issue up to 20 percent of its voting stock to persons that are not Farm Credit System institutions.

What disclosures must be provided when equities are issued?

Purchasers of equities must receive information similar to information contained in a Farm Credit System institution's annual report so that the purchaser has an understanding of the service corporation's business, legal proceedings, financial information, and risks associated with any invested capital. In addition, the purchaser receives information on capitalization bylaws and the terms and conditions under which the equity is issued.

What caused the FCA to consider allowing all service corporations to issue up to 20 percent of their voting stock to persons that are not Farm Credit System institutions?

System institutions requested the amendment when we asked them for ways to reduce regulatory burden.

Prior to these amendments did the FCA allow any Farm Credit System service corporations to issue voting stock to persons that are not Farm Credit System institutions?

Yes. In June of 1992 we adopted regulations to allow service corporations organized to act as agricultural mortgage marketing facilities to sell up to 20 percent of its voting stock to persons that are not Farm Credit System institutions. These type service corporations may be organized

by any Farm Credit institution(s) other than the Federal Agricultural Mortgage Corporation or its affiliates for the purpose of exercising the authorities granted under title VIII of the Act.

Why did the FCA restrict non-System ownership of voting stock to 20 percent?

In order for the System to maintain control of their service corporations even when not all System stockholders vote in the same manner. This level of ownership control is also consistent with our 1992 regulations for agricultural mortgage marketing facilities.

What oversight does the FCA have over service corporations?

We approve the charters and articles of incorporation of service corporations. We also determine the capital requirements for the service corporation. Finally, we have the authority to examine and issue enforcement documents and regulations to govern service corporations

Does this amendment allow service corporations to have additional authorities or service customers that would be otherwise ineligible?

No. The service corporation is only allowed to perform functions that the Farm Credit banks and associations are authorized to perform, except they may not extend credit or provide insurance services.

Part 615 – Capitalization Bylaws

What do FCA's current capitalization bylaw regulations require?

Currently, FCA regulations allow institution bylaws, which must be approved by shareholders, to provide for the issuance of unlimited amounts of equities:

- that are required to be purchased as condition of obtaining a loan, and
- for nonvoting stock into which voting stock is converted after repayment of a loan.

What do FCA's amended capitalization bylaws say?

Our amended regulations also allow institution bylaws to provide for the issuance of unlimited amounts of:

- non-voting stock equities that are issued to an association's funding bank in conjunction with any agreement for a transfer of capital between the association and the bank, and
- equities resulting from the distribution of earnings.

Why is FCA amending this section of its regulations?

So that System institutions can more easily transfer capital and distribute earnings. System institution Boards of Directors will no longer have to estimate the amounts of equities that may be issued for these classes of stock and shareholder votes will not be necessary to approve the amounts.

How does this amendment affect borrower's voting rights?

This amendment does not affect a borrower's voting rights or preferences in the event of liquidation.

Exhibit 1

Comparison of Existing FCA Stock Issuances Regulations and our Final Regulations

Issue	Old Regulation	New Regulation ¹	Reason(s) for Change
Non-System Ownership of Service Corporations owned by Farm Credit banks and associations. (Part 611 of FCA Regulations)	Only Farm Credit Banks and associations may own stock in a service corporation. Section 611.1135 (a)	Service Corporations may issue non-voting and voting stock to persons that are not Farm Credit institutions, provided that at least 80 percent of voting stock is held by Farm Credit institutions. Section 611.1135 (b)	1) System Requested the relief after our Regulation Burden Solicitation. 2) Provides for outside alliances and capital. 3) Little risk of loss of System Control. 4) Treats traditional Service Corp. the same as Secondary Market Service Corps.
Providing Adequate Disclosures When Service Corporations Owned by Farm Credit banks and associations Issue Equities. (Part 611 of FCA Regulations)	Does not require disclosures.	Requires that disclosures are provided in accordance with our Disclosure Regulations. Section 611.1135 (f).	To treat traditional service corporation the same as Secondary Market Service Corporations.
Capitalization Bylaws. Section 615.5220 (a)(3)	Capitalization bylaws must specify the amounts of equities authorized for each class of stock – with two exceptions: 1) equities required to be purchased to obtain a loan, and 2) nonvoting stock into which voting stock is converted when a loan pays off.	Provides for two additional exceptions: 3) non-voting stock issued to a bank in exchange for a transfer of capital, and 4) equities that an institution issues to distribute earnings.	1) System Board must estimate future stock needs associated with transfers of capital and earnings distributions. 2) If the board's estimate too low, a special stockholder vote is necessary. 3) Allowing the two exceptions does not dilute a borrowers voting rights or preference in the event of liquidation.

¹ This new regulation was proposed to the public for comment on December 23, 1999, in the *Federal Register*. See 64 FR 72041 (Dec. 23, 1999).