Farm Credit Administration

# Fiscal Year 2016 Proposed Budget and Performance Plan

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# LIST OF ACRONYMS AND ABBREVIATIONS

ACA ..... Agricultural Credit Association
CAMELS ..... capital, assets, management, earnings, liquidity, and sensitivity
Dodd-Frank Act .....Dodd-Frank Wall Street Reform and Consumer Protection Act
Farm Credit Act..... Farm Credit Act of 1971, as amended
Farmer Mac.....Federal Agricultural Mortgage Corporation
FCA..... Farm Credit Administration
Leasing Corporation .....Farm Credit Leasing Services Corporation
FCS or System ..... Farm Credit System
FCSBA .....FCS Building Association
FCSIC ..... Farm Credit System Insurance Corporation
FIRS .....Financial Institution Rating System
FLCA ..... Federal Land Credit Association
FTE.....full-time equivalent
FTP.....full-time permanent
FY ..... fiscal year
Funding Corporation .....Federal Farm Credit Banks Funding Corporation
GSE .....Government-sponsored enterprise
IT..... information technology
NCB ..... National Consumer Cooperative Bank
OSMO.....Office of Secondary Market Oversight
PCA.....Production Credit Association
RBC .....risk-based capital
USDA.....U.S. Department of Agriculture
YBS.....young, beginning, and small (farmers and ranchers)

# PREFACE

The Farm Credit Administration is an independent agency in the Executive branch of the U.S. Government. We are responsible for the regulation and examination of the banks, associations, and related entities that collectively constitute what is known as the Farm Credit System (FCS or System), including the Federal Agricultural Mortgage Corporation (Farmer Mac).[1]

Initially created by an Executive order of the President in 1933, FCA now derives its powers and authorities primarily from the Farm Credit Act of 1971, as amended (Farm Credit Act). We promulgate regulations to implement the Act and examine System institutions for compliance with the Act and regulations, and with safe and sound banking practices. Our mission is to promote a safe, sound, and dependable source of credit and related services for agriculture and rural America.

This document presents and justifies our proposed budget for fiscal year 2016. It contains key information about our functions and program activities, along with an overview of the financial condition of the FCS and Farmer Mac, the entities we regulate. Also included is the fiscal year 2016 performance budget, which ties proposed expenditures to the goals and objectives in our strategic plan.

This document is organized into four sections as follows:

1. Part I contains our budget request. This section presents budget trends that we monitor annually.

2. Part II covers the functions, programs, and services we undertake to fulfill our public mission. It also provides information on actions we have taken to improve internal operations.

3. Part III discusses the System's financial condition and performance.

4. Part IV contains our FY 2016 performance budget, which provides a basis for measuring our overall effectiveness.

[1] Although Farmer Mac is an FCS institution under the Farm Credit Act (12 U.S.C. 2279aa-1(a)(2)), we discuss Farmer Mac separately from the other entities of the FCS in this document because of the secondary market authorities unique to Farmer Mac. Farmer Mac is not jointly and severally liable on debt issuances with other parts of the FCS.

# Part I

# FISCAL YEAR 2016
# PROPOSED BUDGET

# FISCAL YEAR 2016 BUDGET OVERVIEW

The FY 2016 proposed budget request, as shown in table 1, includes $68,800,000 in assessments (current year and carryover funds) from FCS institutions, including Farmer Mac. Reimbursable funding from the U.S. Department of Agriculture, Farm Credit System Insurance Corporation, and the National Consumer Cooperative Bank adds $600,000 to this amount, bringing the total proposed FCA budget request to $69,400,000.

**TABLE 1. Farm Credit Administration FY 2016 Proposed Budget**

| Description | Amount Proposed | Percentage of Total Budget |
|---|---|---|
| Full-time-permanent personnel (FTP) | $41,290,793 | 59.5 |
| Other than FTP | 1,176,544 | 1.7 |
| Other personnel compensation | 374,127 | 0.5 |
| **Total personnel compensation** | **$42,841,464** | **61.7** |
| Personnel benefits | 15,747,015 | 22.7 |
| Benefits for former personnel | 25,000 | 0.0 |
| **Total compensation and benefits** | **$58,613,479** | **84.4** |
| Travel and transportation of persons | 3,658,380 | 5.3 |
| Transportation of things | 217,250 | 0.3 |
| Rent, communications, and utilities | 823,308 | 1.2 |
| Printing and reproduction | 246,000 | 0.4 |
| Consulting and other services | 3,986,860 | 5.7 |
| Supplies and materials | 685,026 | 1.0 |
| Equipment | 1,169,697 | 1.7 |
| **Total budget** | **$69,400,000** | **100.0** |

Note: Obligations for administrative expenses in FY 2016 are not to exceed the amount collected in assessments (current and prior year) from the FCS and Farmer Mac ($68,800,000). The total budget includes an additional $600,000 from anticipated reimbursable activity.

The FY 2016 proposed budget of $69,400,000 increased by $3,800,000 over the FY 2015 revised budget of $65,600,000. By leveraging technology and continually emphasizing savings and efficiencies in operations, we have kept travel costs stable, and we have reduced costs for other contractual services and equipment. As a result, we are able to present a prudent, cost-effective budget.

The FY 2016 budget is necessary to maintain an effective examination program. A robust examination program will help us identify any emerging risks early so that we can better protect the safety and soundness of the Farm Credit System.

The environment in which the FCS operates is dynamic and increasingly complex. The challenges in the nation's financial sector over the past few years were important considerations during our most recent strategic planning period. As a result, we have redirected staff resources to proactively manage systemic risk and to continually seek ways to increase our effectiveness and efficiency. We are also adding staff to our examination program in FYs 2015–2106.

In the FY 2016 proposed budget, the full-time-equivalent (FTE) staffing level increases by approximately seven FTE positions over the FY 2015 revised budget. The FY 2016 budget also

anticipates increases in career-ladder promotions, which will require an increase in spending for salaries and benefits. As an agency covered by the Financial Institutions Reform, Recovery, and Enforcement Act of 1989, we must strive to achieve comparability in compensation and benefit programs with other agencies covered under the act.

In addition, the FY 2016 proposed budget takes into account increases in funded leave, increased reimbursable work, and IT equipment replacements.

The FY 2015 congressional limitation required us to delay hiring additional staff during FY 2015. In FY 2016, however, we plan to hire for those additional positions. As a result, our costs for compensation and benefits will increase in FY 2016, and costs to support those additional employees, such as training, travel, relocation, and contractual support, will also increase.

The budget provides the resources needed to fulfill the objectives of the FCA Board Chair and CEO, which are as follows:

- To maintain strong examination and supervisory programs
- To establish the right level of regulatory capital for FCS institutions
- To ensure that the public purpose and mission-related responsibilities of the System are carried out appropriately

The budget continues to implement the FCA Board's philosophy on risk-based examination. We have included sufficient resources to ensure that risks are properly identified, managed, and controlled. These resources will enable us to send our examiners to the institutions we regulate to perform on-site testing of the institutions' credit reviews, internal audits, and internal controls. In addition, we will continue to invest in IT modeling applications to help us identify risk throughout the System. The budget also includes resources to hire contractors when we need technical specialists and technology upgrades. (For more information about our risk-based examination and supervision, see page 34.)

The budget provides resources for developing regulations and policy positions that implement statutes, for promoting the safety and soundness of the FCS, and for supporting the System's mission as a dependable source of credit and related services for agriculture and rural America.

We also continue to invest in our human capital initiative. During FY 2014, we hired a Learning Officer to support and lead our Human Capital Plan initiative. This initiative promotes learning, expertise, and personal growth among our employees. It is an important part of our strategy to retain our skilled workforce, and it supports our results-oriented culture.

Knowledge management is a key component of our continuous learning strategy. As we foresee vacancies in critical fields, we ask our experienced employees to work with our newly hired employees to transfer critical knowledge and skills.

Our policies on training and employee development further enhance the transfer of knowledge. We will continue to emphasize training for pre-commissioned examiners and the need to capture the knowledge of employees who are eligible to retire.

In addition, the budget includes continued funding for the following multi-year projects.

**Agency Laptop Evaluation and Replacement.** We generally replace our employees' laptops every three years, and we issue the new laptops to all staff at the same time. By adhering to this

schedule, we ensure that the Agency has up-to-date technology and our employees have reliable, powerful computers. New laptops allow faster and more convenient computing services. When we upgrade our hardware, we also refresh and standardize the client software configuration.

**Other Equipment Replacements.** Many Agency machines and IT devices have reached the end of their lifecycles. In FY 2016, we will replace Agency network printers and copier/printer/scanner machines. Scheduled replacement of these units ensures updated printing and copying capabilities, reduces maintenance costs, and may increase energy efficiency. We will also research and purchase smartphones and associated data and voice services to replace aging devices. Newer devices typically offer additional security features and longer battery life. In addition to providing network connectivity for our mobile workforce, smartphones are an integral part of our continuity of operations and emergency response obligations. We will also replace our four-year-old servers with updated equipment. More powerful machines are critical in maintaining our IT infrastructure and supporting Agency data warehouse and risk analysis projects.

**Risk Project.** The goals of the FCA Risk Project are to evaluate and acquire tools that enable us to

- conduct risk and statistical analysis of the FCS; and
- enable users to create reports and dashboards for FCA's Structured Query Language data (which includes the following databases: FCS Loans, Consolidated Reporting System, Enterprise Documentation Guidance (EDGe), and Time Recording System).

We want to turn data into information and make the information quickly available to managers and staff so they can take appropriate action for the oversight of the FCS and management of FCA. This project will enhance our ability to perform our core mission of ensuring the safety and soundness of the FCS.

**EDGe Project.** The EDGe application focused initially on two goals: transitioning the Office of Examination's examination documentation system to SharePoint and, over a three-year period, developing a fully redesigned examination program and Agency documentation system.

We will now focus on the following goals: building management reports and implementing tools for scheduling and enhancing work papers. The EDGe Workgroup will capture key information repositories and import them into a management reporting site. This will enable OE management and supervisors to more efficiently and effectively evaluate System conditions and examination-related progress.

The goal of this management reporting site will be to provide a tool for supervisors to monitor examination work, to automate monthly and quarterly reporting processes, and to make reports available in real time so that they can be viewed at any point throughout the examination cycle. In addition, we plan to incorporate other OE tools into the EDGe environment.

This project promotes efficiency, effectiveness, and retention of corporate knowledge. It also allows us to leverage the Agency's technology investments and improves communications and coordination. The EDGe establishes a more centralized information repository for all examination and supervision activities. The EDGe becomes the central hub for the oversight and examination program and the Agency's institution-related documentation system.

**Management Dashboard.** This project will provide key information for the effective management of programs and activities. It will push information to users and allow them to drill down or look at more detailed information related to a key indicator. This application will benefit all programs and offices by providing timely, easy-to-access information.

**CRS Call Reports.** Every one or two years we make significant changes to maintain and improve our Call Report system. This system provides an electronic source of FCS financial data for the general public, FCS institutions, FCA management, financial analysts, and FCA examiners.

**Application Modernization.** The purpose of this project is to ensure that we can access our applications through a browser from most devices. To take full advantage of new Web-based technologies, we must migrate our legacy applications to the Web. When they are on the Web, we will no longer need the Microsoft Windows Operating System to access the applications, and we can use them from our mobile devices.

**Farmer Mac Data Collection.** This project will create an electronic system to collect, store, and use data from Farmer Mac. It will increase the efficiency and effectiveness of our examination and oversight of Farmer Mac, allowing us to conduct more work off site. It will also make the process of submitting data more efficient for Farmer Mac.

**Telework Database.** The purpose of this project is to streamline the approval process for flexi-place agreements, to reduce paper, and to retain records electronically. The database would allow employees to complete and sign FCA annual flexi-place forms electronically. It would also allow supervisors and the Agency Telework Coordinator to review and approve each form electronically. The project supports the Federal Government's telework initiatives and the Federal Government Paperwork Reduction Act.

**Email Archiving and Discovery.** The major goals of the project are as follows:

- Ensure that FCA staff can quickly and easily find the information they need to meet the business and operational needs of the Agency.
- Ensure that we retain email in accordance with Agency recordkeeping requirements and we make it available to appropriate staff.
- Ensure that our staff can effectively and efficiently respond to legitimate requests for documents and, if appropriate, can place email on litigation hold.
- Facilitate disaster-recovery efforts to restore email communication.
- Enhance productivity and system performance

**Funding Approval SharePoint Site.** The goal of this project is to provide an efficient, interactive working environment for those who are responsible for monitoring, analyzing, and processing funding requests and other approval requests.

**Continuity of Operations Program.** FCA will continue to enhance its test, training, and readiness program to provide staff with the knowledge and training they need to provide continuity of operations in an emergency.

## Background

We expect the FCS to continue to evolve in the coming years to meet the demands of an increasingly complex marketplace for agriculture and rural America. As FCS institutions grow and change, their operations become more complex. Because of increased risk in several institutions, we expect mergers and consolidations to continue; and because of challenges in the global economy, we expect the System's asset base to grow at only a moderate pace. Currently, the average institution's asset base exceeds $1 billion.

Our budget request includes the resources necessary to ensure the safety and soundness of the System as it grows and changes. The budget strategy will enable us to leverage our most valuable investment—our people. It will enable us to continue to streamline and improve operations and to enhance staff expertise to meet any challenges and opportunities that may arise. The budget request supports our Human Capital Plan by allowing us to increase the number of examiners and to implement our Information Resources Management Plan.

## FCA Program Areas

The Agency has two primary programs: (1) policy and regulation and (2) safety and soundness. All FCA office activities support these programs directly or indirectly.

### *The Policy and Regulation Program*

The budget provides resources for developing regulations and policy positions that implement statutes, promote the safety and soundness of the FCS, and ensure that the System carries out its mission. In addition, the budget provides for activities such as evaluating and recommending regulatory and funding approvals, managing merger and chartering activities, and providing strategic and systemic policy research and analyses of risks and other issues facing the System.

The budget also provides for support activities, including the processing of information, the communication of Agency positions, and the administration of activities associated with the policy and regulation program. In total, policy and regulation activities account for approximately $15.0 million, including 58.09 FTEs in the proposed FY 2016 budget (see table 31 on page 75).

### *The Safety and Soundness Program*

Through our safety and soundness program, the budget provides resources to examine the System for safety and soundness. These resources also ensure that FCS institutions comply with applicable laws and regulations. The budget continues to implement a risk-based approach to oversight and examination, which maximizes the effectiveness of examinations by allocating more examination resources to institutions with greater risk.

The budget also includes sufficient resources to ensure that the FCS properly identifies, manages, and controls risk. Initiatives include the development of risk topics, on-site examination presence, and a greater emphasis on loan review through the testing of credit reviews, internal audits, and internal controls.

Our budget also enables us to take special supervisory and enforcement actions when necessary. Weaknesses in the nation's economy and credit markets and volatility in agriculture have weakened some FCS institutions, requiring our examiners to take special action to address areas of concern.

In total, safety and soundness activities account for $52.9 million, including 238.45 FTEs in the proposed FY 2016 budget (see table 31 on page 75).

## Office of Inspector General's FY 2016 Budget Request

Section 6(f)(1) of the Inspector General Act of 1978, as amended, (IG Act) requires an Inspector General (IG) to include specific information in the budget request the IG submits to the head of the department or designated Federal entity to which the IG reports. To fulfill the requirement of section 6(f)(2) of the IG Act, the FCA Board must in turn include this same information in the budget request that we submit to the President.

The information that the IG Act requires to be included is provided below:

- The aggregate budget request for the Office of Inspector General (OIG) is $1,514,785.
- The amount needed for OIG training is $22,100 (tuition).
- The amount needed to support the Council of the Inspectors General on Integrity and Efficiency is $4,100.

The FCA Board is submitting the IG's budget request as received from the IG.

# BUDGET TRENDS

This budget supports the Agency's safety and soundness programs. It maintains and slightly grows our talent pool so that we can examine and supervise the System effectively and monitor the changing risk environment. In addition, these resources keep the bar raised to the level set by the Dodd-Frank Wall Street Reform and Consumer Protection Act. The FY 2016 budget is necessary to continue to fund the examination program, employee salary and benefit costs, and technology expenditures—all of which represent approximately 89 percent of FCA's total budget.

Our actual and budgeted spending levels are consistent with actual and budgeted FTE usage. Actual FTE usage has declined in past years because of challenges in hiring and unexpected attritions. FTE usage did increase in FY 2014 and is expected to increase over the next two years to support the examination and oversight of the Farm Credit System. We must guard against risks related to program changes and weaknesses in both the agricultural and the general economy. Tables 2, 3, and 4 provide information on our budget trends.

**TABLE 2. FY 2016 Proposed Budget Compared with the FY 2015 Revised Budget**

| | FY 2015 Revised Budget | FY 2016 Proposed Budget | Increase (Decrease) from FY 2015 Budget |
|---|---|---|---|
| Full-time permanent (FTP) | $39,508,558 | $41,290,793 | $1,782,235 |
| Other than FTP | 1,120,627 | 1,176,544 | 55,917 |
| Other personnel compensation | 374,191 | 374,127 | (64) |
| **Total personnel compensation** | **$41,003,376** | **$42,841,464** | **$1,838,088** |
| Personnel benefits | 13,522,503 | 15,747,015 | 2,224,512 |
| Benefits for former personnel | 25,000 | 25,000 | 0 |
| **Total compensation and benefits** | **$54,550,879** | **$58,613,479** | **$4,062,600** |
| Travel and transportation of persons | 3,636,940 | 3,658,380 | 21,440 |
| Transportation of things | 238,250 | 217,250 | (21,000) |
| Rent, communications, and utilities | 813,753 | 823,308 | 9,555 |
| Printing and reproduction | 257,000 | 246,000 | (11,000) |
| Consulting and other services | 4,102,531 | 3,986,860 | (115,671) |
| Supplies and materials | 654,337 | 685,026 | 30,689 |
| Equipment | 1,346,310 | 1,169,697 | (176,613) |
| **Total budget** | **$65,600,000*** | **$69,400,000** | **$3,800,000** |

Note: FCA's FY 2016 proposed budget request is $3.8 million more than the FY 2015 revised budget request.

*After the FCA Board approved the revised 2015 budget in September, Congress passed legislation capping our administrative expenses to be paid from assessments at $60.5 million. As a result of this cap, we will revise our spending in accordance with the statute.

The Office of Management and Budget (OMB) has issued guidance for agencies to reduce costs and increase efficiencies. We have taken the following actions to reduce costs:

- Implemented and improved audio- and videoconferencing, thereby controlling travel costs.
- Revised and issued the Travel and Relocation Policy to encourage prudent travel practices.
- Issued detailed guidance regarding conference costs, including a new policy that requires the Chief Financial Officer or the Chief Operating Officer to approve higher-cost conferences.
- Allowed employees to use penalty fares to take advantage of lower air fares.
- Reduced travel to the field offices.
- Increased reliance on the FCS Loans Database to help reduce travel costs.
- Installed network copier printers with scanning capabilities to reduce hard copies, promote electronic files, and reduce the number of printers.

In addition, we regularly use the following practices to keep our costs low:

- Use technology devices (such as laptops and smartphones) to keep travel costs down and maintain continuity of operations.
- Ensure that service provider costs are well managed.
- Scrutinize the issuance of information technology devices to ensure that only employees who have a bona fide business need receive the devices.
- Review, on a monthly basis, the usage of smartphones and other wireless devices to ensure the devices are being fully utilized and costs are being minimized.
- Use laptops as our standard platform for computer needs since most of our employees are examiners who travel frequently. The laptops also help us ensure continuity of operations. In addition, the use of laptops supports telecommuting initiatives during normal operating conditions and inclement weather. In FY 2014 we extended the lifecycle of our laptops by one year because of solid performance.
- Continue to expand our use of technology to disseminate publications (such as publishing documents on our website and distributing them by email) and to reduce the amount of printing where appropriate.
- Reduce printing by conducting research online and instituting a “Going Green” initiative for training materials.

- Continue to make our workflow more efficient and integrated by using the EDGe Project.
- Continue to collaborate and share resources across FCA offices to increase efficiency.

**TABLE 3. FCA Budgets, FYs 2014–2016**

| | FY 2014 Revised Budget | FY 2015 Revised Budget | FY 2016 Proposed Budget |
|---|---|---|---|
| Full-time permanent (FTP) | $38,503,256 | $39,508,558 | $41,290,793 |
| Other than FTP | 876,471 | 1,120,627 | 1,176,544 |
| Other personnel compensation | 407,246 | 374,191 | 374,127 |
| **Total personnel compensation** | **$39,786,973** | **$41,003,376** | **$42,841,464** |
| Personnel benefits | 13,103,813 | 13,522,503 | 15,747,015 |
| Former personnel benefits | 25,000 | 25,000 | 25,000 |
| **Total compensation and benefits** | **$52,915,786** | **$54,550,879** | **$58,613,479** |
| Travel and transportation of persons | 3,552,281 | 3,636,940 | 3,658,380 |
| Transportation of things | 282,930 | 238,250 | 217,250 |
| Rent, communications, and utilities | 993,378 | 813,753 | 823,308 |
| Printing and reproduction | 257,150 | 257,000 | 246,000 |
| Consulting and other services | 3,640,024 | 4,102,531 | 3,986,860 |
| Supplies and materials | 727,895 | 654,337 | 685,026 |
| Equipment | 1,530,556 | 1,346,310 | 1,169,697 |
| **Total obligations** | **$63,900,000** | **$65,600,000** | **$69,400,000** |

## Sources of FCA Revenue and Funding

We maintain a revolving fund financed primarily from assessments to System institutions and Farmer Mac. We also earn interest from investments with the U.S. Department of the Treasury, and we perform reimbursable work for the Farm Credit System Insurance Corporation, U.S. Department of Agriculture, and the National Consumer Cooperative Bank. Table 4 shows budgeted sources of revenue and funding for FYs 2014 to 2016.

**TABLE 4. Budgeted Sources of FCA Revenue and Funding, FYs 2014–2016**

| Source | FY 2014 Revised Budget | FY 2015 Revised Budget | FY 2016 Proposed Budget |
|---|---|---|---|
| **ASSESSMENTS** | | | |
| Banks, associations, and related entities | $47,625,000 | $52,100,000 | TBD |
| Federal Agricultural Mortgage Corporation | 2,375,000 | 2,400,000 | TBD |
| Carryover funds[a] | 13,300,000 | 10,600,000 | TBD |
| **Assessments available for obligation** | **$63,300,000** | **$65,100,000** | **$68,800,000**[b] |
| **REIMBURSEMENTS**[c] | | | |
| National Consumer Cooperative Bank | 174,073 | 69,762 | 195,113 |
| Farm Credit System Insurance Corporation | 287,800 | 366,929 | 367,097 |
| U.S. Department of Agriculture | 138,127 | 63,309 | 37,790 |
| | | | |
| Interest income | ----[d] | ----[d] | ----[d] |
| **Total** | **$63,900,000** | **$65,600,000** | **$69,400,000** |

[a] Carryover funds are amounts brought forward from prior years' assessments that remain available for obligation. We will determine assessments and carryover amounts for FY 2016 in September of FY 2015.

[b] Our proposed obligation limit for FY 2016 is $68,800,000.

[c] From a budget standpoint, reimbursements do not include indirect costs.

[d] No funds are budgeted from interest earned.

Note: The revolving fund is financed by three sources: (1) assessments to System institutions and Farmer Mac, (2) income from reimbursable services that we provide to other Federal agencies and the National Consumer Cooperative Bank, and (3) interest earned from investments with the U.S. Treasury.

## FCA Reserve

The institutions we oversee are involved in two volatile industries—agriculture and finance. Volatility can produce financial stress for institutions, creating a need for heightened oversight and supervision. To ensure that we have the resources to provide the necessary supervision and oversight during periods of financial stress, we established a reserve. Congress granted approval for the reserve under section 5.15(a)(1)(B) of the Farm Credit Act, and the FCA Board established guidelines for it.

The reserve ensures that we can effectively and efficiently respond to unanticipated, material, one-time policy or safety and soundness issues arising within the System. The reserve strategy provides us with a proactive plan to respond to these issues without increasing assessments at a time that may be financially difficult for System institutions. At the end of FY 2014, we had approximately $11.8 million in our reserve.

# ASSESSMENTS

FCA's operating costs are financed by direct assessments collected from System institutions, including Farmer Mac. As table 5 shows, assessments grew slowly and steadily until 2009 when financial stress began to affect many System institutions, creating a need for heightened oversight and supervision.

Assessments increased more rapidly through 2012 to cover the costs of the additional resources required for oversight and supervision. In 2013 and 2014, we were able to reduce assessments to System institutions by using carryover from prior-year assessments to help fund our operations.

The lower assessments, however, are not sustainable over the long term. To ensure the safety and soundness of the Farm Credit System, we had to increase our staffing levels. To cover the costs of these additional staff, we raised our assessments by $4.5 million in FY 2015, although this number would have been higher if we had not used carryover to offset the costs.

**TABLE 5. FCS Assessments FYs 2006–2015**

| Fiscal Year | Assessment (in millions) |
|---|---|
| 2006 | $40.5 |
| 2007 | $41.5 |
| 2008 | $42.5 |
| 2009 | $45.1 |
| 2010 | $49.1 |
| 2011 | $52.5 |
| 2012 | $54.1 |
| 2013 | $50.0 |
| 2014 | $50.0 |
| 2015 | $54.5 |

At the direction of Congress, we continue to reduce our carryover. As table 6 shows, we assessed the System $50.0 million in FY 2014. At the end of the year, we also had $1.5 million in reimbursable revenue and deobligations. During the year, we had obligations of $55.8 million. The difference between our obligations and our revenue was –$4.3 million, which allowed us to draw down our carryover amount to $11.7 million. Therefore, from FY 2013 to FY 2014, we reduced our assessment carryover by 27 percent.

Because we have had difficulty in hiring and retaining the staff we need each year, our assessment carryover has not declined as quickly as it otherwise would have. However, we anticipate more hiring in FY 2016. The Office of Examination, where we hire the majority of our entry-level staff, has made significant progress in reaching planned hiring numbers for FY 2016. Therefore, for FY 2016, we expect to have the number of associate examiners for which we have budgeted.

| TABLE 6. FCA Funding, Obligations, and Assessment Carryover FYs 2013 and 2014 | | |
|---|---|---|
| | **FY 2013** | **FY 2014** |
| Current year assessments | $50.0 | $50.0 |
| Reimbursable revenue and deobligations | $1.3 | $1.5 |
| **Total funding** | **$51.3** | **$51.5** |
| Obligations | $51.8 | $55.8 |
| **Total funding minus obligations** | **($0.5)** | **($4.3)** |
| Assessment carryover from prior years | $16.5 | $16.0 |
| **Carryover from assessments at end of fiscal year** | **$16.0** | **$11.7** |

## FCS Borrower Costs

As table 7 shows, FCS borrowers incurred a net cost of approximately 1.8 basis points, or 1.8 cents for every $100 of assets held, to pay for FCA operations in FY 2014. Since FY 2005, the net cost to borrowers has decreased by 0.8 basis points.

FCS borrower costs are based on the relationship between the System's total assessments and assets held (not including Farmer Mac). The FCS held $271.3 billion in total assets as of September 30, 2014, up from $252.9 billion a year earlier.

Borrower costs have declined over the years for the following reasons:

- System assets have grown.
- FCA has used carryover to offset additional costs.
- FCA has taken various measures to reduce operating costs. (See pages 10 and 11 for details.)

| TABLE 7. FCA's Net Cost to System Borrowers FYs 2005–2014 | |
|---|---|
| **FY Ended September 30** | **Basis Points** |
| 2005 | 2.6 |
| 2006 | 2.5 |
| 2007 | 2.2 |
| 2008 | 2.0 |
| 2009 | 2.0 |
| 2010 | 2.1 |
| 2011 | 2.2 |
| 2012 | 2.2 |
| 2013 | 1.9 |
| 2014 | 1.8 |
| Note: The net cost figure is the annual assessment (not including Farmer Mac) at the beginning of the fiscal year divided by total assets at the end of the fiscal year. | |

## Assessments for the Federal Agricultural Mortgage Corporation (Farmer Mac)

Farmer Mac's assessment for FY 2015 is $2.40 million. As required by regulation, we will reconcile and adjust the assessment after the fiscal year-end to reflect the actual amount expended. Actual costs for FY 2014 were $2.29 million. The assessment for FY 2016 is not yet available because the Office of Secondary Market Oversight (OSMO) will not complete the FY 2016 budget and estimation of examination, oversight, and regulatory costs pertaining to Farmer Mac until September 2015.

Table 8 shows assessments for fiscal years 2006 to 2015. These assessments include costs associated with increased examination and oversight activities. OSMO added staff in 2014 because of the increased emphasis on capital adequacy and stress testing among financial regulatory agencies.

**TABLE 8. Farmer Mac Assessments FYs 2006–2015**

| Fiscal Year | Assessment (in millions) |
|---|---|
| 2006 | $2.35 |
| 2007 | $2.20 |
| 2008 | $2.05 |
| 2009 | $2.05 |
| 2010 | $2.25 |
| 2011 | $2.20 |
| 2012 | $2.25 |
| 2013 | $2.38 |
| 2014 | $2.38 |
| 2015 | $2.40 |

Note: Although it will not be set until September 2015, Farmer Mac's FY 2016 assessment is expected to be about $2.40 million, the same as the FY 2015 figure.

# Part II

# FARM CREDIT ADMINISTRATION

# PROFILE OF THE FARM CREDIT ADMINISTRATION

The Farm Credit Administration was created through an Executive order of President Franklin D. Roosevelt and currently derives its powers and authorities primarily from the Farm Credit Act of 1971, as amended (Farm Credit Act). As an independent Agency within the Executive branch of the Federal Government, we are responsible for regulating and supervising the banks, associations, and related entities in the Farm Credit System (FCS), as well as the Federal Agricultural Mortgage Corporation (Farmer Mac).[2]

The FCS is the oldest of the financial Government-sponsored enterprises (GSEs). The Farm Credit Act states that the objective of the FCS is to improve the income and well-being of American farmers and ranchers by furnishing sound, adequate, and constructive credit and closely related services to them, their cooperatives, and selected farm-related businesses. In short, the FCS was created to provide an adequate and flexible flow of money to rural areas.

The System consists of a nationwide network of borrower-owned, cooperative financial institutions that provide credit and related services to

- farmers and ranchers,
- producers and harvesters of aquatic products,
- farm-related businesses,
- rural homeowners,
- agricultural and aquatic cooperatives,
- agribusinesses, and
- rural utilities.

The FCS had $194.2 billion in outstanding loans to agriculture and rural America as of September 30, 2013.

Farmer Mac is a stockholder-owned, federally chartered instrumentality of the United States, and its authority is derived from Title VIII of the Farm Credit Act. Farmer Mac was established in 1988 to create a secondary market for agricultural real estate loans and rural housing mortgage loans. In 2008, Farmer Mac's secondary market authorities were expanded to include rural utility loans. It provides secondary market services through a network of agricultural lenders and intermediaries including commercial banks, FCS banks and associations, life insurance companies, mortgage companies, and rural utility cooperatives. As of September 30, 2013, the volume of loans either purchased or guaranteed by Farmer Mac totaled $13.8 billion.

FCA is also required by the National Consumer Cooperative Bank Act of 1978, as amended, to examine and report on the condition of the National Consumer Cooperative Bank (NCB). Since the passage of this law, we have conducted safety and soundness examinations of NCB and issued reports of examination to NCB's Board of Directors. NCB is a federally chartered, privately owned banking corporation. It is not a Federal instrumentality, and it is not part of the FCS. In addition, we contract with the Farm Credit System Insurance Corporation and the U.S. Department of Agriculture to provide examination services.

[2] By statute, Farmer Mac is an institution of the Farm Credit System; however, in this document, we will use the terms "FCS" and "System" to refer to all the entities in the Farm Credit System except Farmer Mac and affiliates of Farmer Mac.

The U.S. Senate Committee on Agriculture, Nutrition, and Forestry and the U.S. House of Representatives Committee on Agriculture oversee the FCS, Farmer Mac, and FCA. Our operations are funded through assessments paid by the System institutions and by our reimbursable activities; we do not receive a Federal appropriation.

## Mission Statement

As stated in our Strategic Plan for FYs 2013–18, our mission is to ensure a safe, sound, and dependable source of credit and related services for all creditworthy and eligible persons in agriculture and rural America. To fulfill this mission, we issue regulations and conduct examinations of FCS institutions and Farmer Mac to evaluate and oversee the safety and soundness of their activities. Our examinations also evaluate whether institutions are complying with laws and regulations, especially the congressional mandate requiring System institutions to have programs to make credit and services available to young, beginning, and small (YBS) farmers. In addition, we research, develop, and adopt rules, regulations, and other guidelines that govern how institutions conduct their business and interact with customers.

If any System institution, including Farmer Mac, violates laws or regulations, or if operations are determined to be unsafe or unsound, we may use our enforcement authority to ensure that the problem is corrected in a timely manner. We also ensure that the rights of certain borrowers are protected.[3]

Other statutory duties require us to issue and amend FCS institution charters, to report to Congress on the System's and Farmer Mac's financial condition and performance, and to approve the issuance of System debt obligations.

## FCA Board and Governing Philosophy

Our policy and regulations are established by a full-time, three-person Board whose members are appointed by the President of the United States with the advice and consent of the Senate. They serve staggered six-year terms and may not be reappointed to succeed themselves after serving a full term or more than three years of a previous member's unexpired term. A Board member may serve after expiration of his or her term until a successor has been appointed and qualified. The President designates one member as Chairman of the Board; this member serves as Chairman until the end of his or her term. The Board Chairman also serves as the Agency's Chief Executive Officer.

The FCA Board approves charters of FCS institutions, oversees the Agency's supervision and examination of those institutions, and issues enforcement actions. The governing philosophy of the FCA Board is grounded in the Farm Credit Act. The Board believes that the principles on which the System was founded are just as important today as they were in the early decades of the 20th century.

In the Strategic Plan for FYs 2013–18, the Board stressed its commitment to maintaining the safety and soundness of the System and Farmer Mac. The Board also expressed its commitment to ensuring that the System provide opportunities to young, beginning, and small farmers; increase diversity in its customer/owner base; and provide an adequate and flexible flow of

[3] Provisions in the Farm Credit Act regarding borrower rights do not apply to loans to cooperatives.

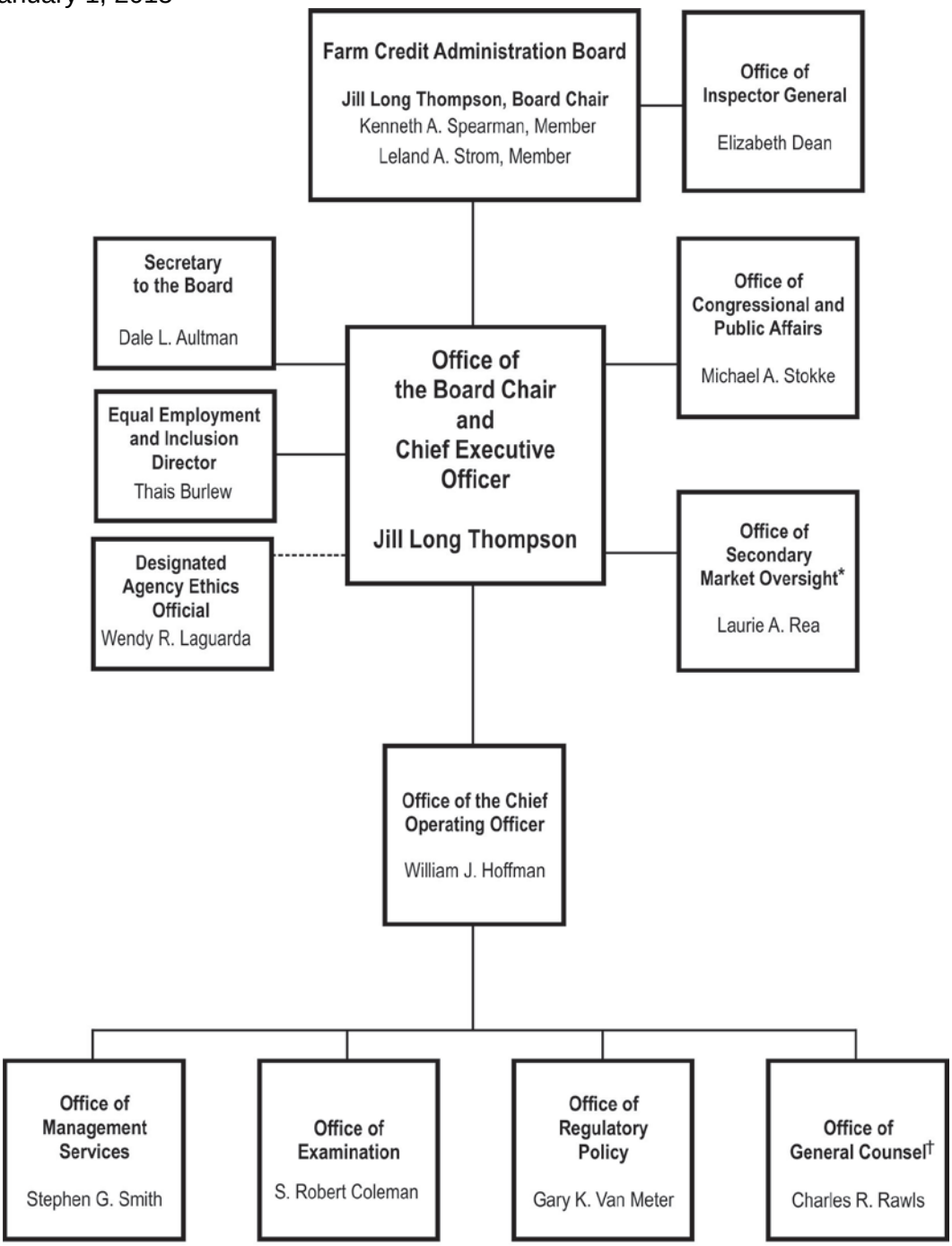
funds into rural America. In addition, because the System's lending institutions are cooperatives, we will continue to advocate for both strong governance and local control.

## FCA Organizational Structure

Figure 1 presents our organizational structure and shows how the offices provide strategic support to the FCA Board and ensure that our mission and goals are performed effectively and efficiently. We have our headquarters in McLean, Virginia, with additional field offices in Bloomington, Minnesota; Dallas, Texas; Denver, Colorado; and Sacramento, California.

## FIGURE 1. FCA Organizational Chart

As of January 1, 2015




***Reports to the Board for policy and to the CEO for administration.**
**†Maintains a confidential advisory relationship with each of the Board members.**

# FCA INTERNAL OPERATIONS

FCA is firmly committed to the continuous development and support of its most valuable asset—its employees. This commitment is at the core of our five-year Human Capital Plan. The plan focuses on workforce planning and talent management, leadership and knowledge management, a results-oriented performance culture, professional growth and motivation, and accountability. The framework of our Human Capital Plan is based on the Human Capital Standards for Success, a collaboration of the Office of Management and Budget, the Office of Personnel Management, and the U.S. Government Accountability Office.

## Human Capital Management

Human capital strategies are linked to our strategic plan through clearly defined strategic initiatives and action plans. We continually monitor workforce trends and implement best practices. We also monitor the System's changing environment so that we can adjust our staffing levels and maintain requisite skill sets by hiring additional staff, providing employee training and development, and transitioning employees from staff positions that are no longer necessary. We review our workforce planning strategies annually; we last revised these strategies in September 2013. See table 9 for full-time-equivalent (FTE) staffing levels (rounded to the nearest whole number) from FYs 2006 through 2016.

**TABLE 9. Full-Time-Equivalent Staffing Levels FYs 2006–2016**

| Fiscal Year | FTE Staffing Level |
|---|---|
| 2006 | 252 |
| 2007 | 253 |
| 2008 | 251 |
| 2009 | 261 |
| 2010 | 277 |
| 2011 | 286 |
| 2012 | 287 |
| 2013 | 273 |
| 2014 | 278 |
| 2015 | 296 (authorized) |
| 2016 | 303 (authorized) |

Note: From FY 2006 to FY 2015, we have maintained a one-to-six ratio of managers and supervisors to other personnel.

We perform workforce assessments annually to obtain information on critical staffing variables, such as the age and grade of employees. From this analysis, we develop five-year projections to determine and mitigate the impact of employee retirements and separations.

As of September 30, 2014, approximately 19 percent of our personnel were eligible to retire. We estimate that this number will increase to 23 percent by the end of FY 2015. As a result of recent hiring, the number of employees who have been employed five years or fewer has risen substantially over the past three years and now constitutes a sizable portion of our workforce. This trend is likely to continue over the next three to five years. See table 10 for retirement eligibility projections at FCA.

**TABLE 10. FCA Retirement Eligibility, FYs 2015–2019**

| Fiscal Year | Eligible Retirements |
|---|---|
| 2015 | 66* |
| 2016 | 9 |
| 2017 | 11 |
| 2018 | 8 |
| 2019 | 12 |

* This number includes 56 staff members who became eligible to retire prior to FY 2015.

### *Implementing the Human Capital Plan*

Identifying our human capital needs over the next five years, including the optimal size of our workforce and the appropriate skill sets of our employees, is one of our primary goals; assessments take place at all levels to accurately gauge human capital requirements. We use the results of these assessments to develop, enhance, and redirect training and development programs.

As we face the retirement of a significant percentage of the FCA workforce, we are working hard to sustain a high level of institutional knowledge, job skills, and analytical expertise. In addition to succession planning and cross-training, we provide a variety of resources and programs for sharing knowledge across the organization.

To ensure maximum efficiency and effectiveness, the Human Capital Steering Committee coordinated these efforts in FY 2014. We also hired a Learning Officer in FY 2014 to more fully develop our training and knowledge retention strategies.

Our continuous learning strategy emphasizes leadership, competencies, and knowledge management. Succession planning is also an important element. By providing education, training, and other development opportunities, we seek to attract and retain bright, creative, and enthusiastic people.

We coordinate training goals with the leadership skills and competencies that are integral to achieving our mission. We establish training projection plans at the office level and the Agency level each year to help us manage employee training and development activities. These plans project budget needs for training and development; they are directly linked to FCA's Performance Management System. Supervisors and employees collaborate on training and development goals during mid-year and annual performance reviews.

Our Learning Officer will help us gauge our training needs and develop efficient and effective methods to acquire outside training and develop internal training courses and learning techniques.

Formal training programs support the needs of core occupational groups through a variety of methods, such as in-house training, vendor courses, self-study, rotational assignments, special assignments, shadowing experiences, and e-learning. Each employee has a laptop computer with the technology to support e-learning initiatives. In addition, all employees have regular access to training on our computer systems.

We demonstrated our commitment to our training and knowledge transfer goals in FY 2014 by providing appropriate training to pre-commissioned examiners and capturing the knowledge of examiners who are eligible to retire. As more and more employees become eligible to retire, knowledge transfer becomes a greater concern. We have created an internal training website to capture examination knowledge and best practices. Subject-matter experts developed the information on the website, which includes both instructor and student materials.

Knowledge management remains a key component of our continuous learning strategy. As vacancies in critical fields are projected, orientation plans seek to have newly hired employees work closely with experienced employees to transfer critical knowledge and skills. We regularly update our policies on training and employee development, and we use mentoring, details, and special projects to provide development opportunities.

FCA's electronic databases, such as the internal training site used by examiners, the Policies and Procedures database, the electronic examination files, and the Training and Evaluations database, are another component of knowledge management and best practices. These databases enable employees to communicate and share knowledge.

We have also established internal SharePoint sites to enhance knowledge transfer and collaboration. All employees have access to most of the sites, including the sites containing resources on contracting, technology, leadership development, and audit and internal controls. Other sites are intended for the use of specific groups of employees, such as credit specialists, operations specialists, and recruiters. Still others are set up for workgroups on topics such as training, planning and reporting, and policy development. Through these sites, we can deliver information in real time to multiple audiences.

In addition, because we recognize the value of diversity and inclusion to the Agency, we work hard to attract and retain staff with varied backgrounds and skills. We endorse programs that promote equal employment opportunity (EEO), diversity, and inclusion, and we have an active EEO program.

Long-term rotational assignments enhance employee knowledge and expertise. Through an organized program that encourages offices and employees to participate in rotational assignments, employees gain a deeper understanding of the Agency's mission. Rotational assignments build teamwork and collaboration and enhance the motivation and productivity of our employees.

### *FCA Compensation Program*

Section 1206 of the Financial Institutions Reform, Recovery, and Enforcement Act of 1989 (FIRREA) requires Federal financial regulators to "seek to maintain comparability regarding compensation and benefits." This provision enables financial regulators to attract and retain qualified staff.

To comply with the FIRREA, we annually survey the other federal bank regulators and adjust our employees' compensation and benefits accordingly. Our compensation rates are similar to the average market rate provided by other agencies covered under the FIRREA. For a general comparison, we also survey the private sector, the System banks, and the General Schedule agencies.

We use a pay-for-performance program to adjust each employee's salary according to his or her performance rating and salary range position. We make salary adjustments each calendar year on the basis of a number of factors, including the compensation programs of other Federal bank regulators and available funding.

On January 16, 2015, the FCA Board approved the FCA Compensation Program for 2015. The program includes pay-for-performance increases based on a 1 percent pay matrix. With a couple of exceptions, the senior executive compensation was not increased. The locality rates were not changed from the prior year.

## External Contracting and Shared Services

### *Outsourcing*

As the table below shows, we continue to outsource several functions. Our shared-service agreement with the Bureau of the Fiscal Service began in FY 2006. We also outsource our payroll services to USDA's National Finance Center. In FY 2010, we began outsourcing our EEO counseling services through the U.S. Geological Survey. Outsourcing these services allowed us to manage our employee benefits and other Agency functions without additional personnel costs.

**TABLE 11. Outsourcing, FY 2014**

| Contract | Purpose | Amount |
|---|---|---|
| Administrative Service Center (BFS) | To provide full-service accounting, eTravel, credit card, and platform procurement services | $590,557 |
| National Finance Center (USDA) | To provide payroll services | $39.000 |
| U.S. Geological Survey | To provide EEO counseling | $14,000 |

Note: FCA's shared-service agreements during FY 2014 totaled $643,557.

### *Single-Source and Competitive Consulting Service Contracts*

Tables 12 and 13 provide a summary of our single-source and competitive consulting service contracts for FYs 2013 and 2014.

| **TABLE 12. Competitive Consulting Service (CCS) Contracts of More Than $25,000 and Single-Source (SS) Contracts, FY 2013** | | |
|---|---|---|
| **Contract** | **Purpose** | **Amount** |
| Brown & Company; 13-FCA-700-001 (CCS) | To provide financial audit services | $35,744 |
| R & R Consulting; 13-FCA-450-001 (CCS) | To assist with updating FCA's risk-based capital model | $55,000 |
| Gartner Inc,; 13-FCA-601-024 (CCS) | To provide technology services | $48,740 |
| PatchAdvisor, Inc.; 13-FCA-601-058 (SS) | To provide recommendations for major applications | $50,050 |
| Personnel Decision Research Institute; 10-FCA-C-01 (SS) | To help develop the pre-commission test | $84,887 |
| Personnel Decision Research Institute; 13-FCA-301-007 (SS) | To develop questionnaire for examiner position | $133,340 |
| Editorial Experts, Inc.; 13-FCA-240-003* | To provide editorial services | $78,987 |
| R. Bridge; 13-FCA-240-002 (SS) | To provide editorial services | $11,250 |
| Personnel Decisions Research Institute;13-FCA-301-007 (SS) | To assist with commission test evaluation | $10,000 |
| AgFirst FCB; 13-FCA-301-004 (SS) | To provide online training by Farm Credit University | $3,900 |
| Expedite Video Conference Service; 13-FCA-301-006 (SS) | To maintain videoconference equipment | $23,387 |
| Avitecture, Inc.; 13-FCA-601-001 (SS) | To maintain audiovisual equipment | $5,350 |
| R. Half International Inc. ; 13-FCA-301-002 (SS) | To provide administrative support | $2,833 |
| ComPsych Employee Assistant; 13-FCA-601-015 (SS) | To provide employee assistance | $6,163 |
| Dave Redden; 13-FCA-601-017 (SS) | To provide retirement counseling | $29,850 |
| Tower Watson Consulting; 13-FCA-601-027 (SS) | To perform compensation study | $19,260 |
| Expedite Video Conference; 13-FCA-601-029 (SS) | To maintain IT equipment | $17,433 |
| Accuvant Federal Solutions Inc.; 13-FCA-601-039 (SS) | To provide storage back-up for servers. | $29,691 |
| PatchAdvisor Inc; 13-FCA-601-040 (SS) | To assess network security | $24,000 |
| World Wide Technology, Inc.;13-FCA-601-041 (SS) | To maintain hardware and software | $21,677 |
| SAP Government Support; 13-FCA-601-043 (SS) | To provide PowerBuilder license | $9,720 |
| R. Half International Inc; 13-FCA-601-045 (SS) | To provide administrative support | $3,023 |
| Gartner, Inc.; 13-FCA-601-048 (SS) | To provide training for IT staff | $91,557 |
| Towers Watson; 13-FCA-601-056 (SS) | To provide compensation consulting | $19,000 |
| PatchAdvisor Inc.; 13-FCA-601-058 (SS) | To accredit major applications | $50,050 |
| Electronic Systems, Inc; 13-FCA-601-061 (SS) | To support network infrastructure | $6,000 |
| SoftChoice Corp; 13-FCA-601-064 (SS) | To provide Microsoft Enterprise Agreement | $540,482 |
| Traid Tech Partners, LLC; 13-FCA-601-072 (SS) | To set up hardware | $12,896 |
| Iron Mountain; 13-FCA-601-003 (SS) | To store magnetic tape | $6,000 |
| Murphy Brothers Inc; 13-FCA-601-005 (SS) | To provide transportation services. | $9,955 |
| Sun Management; 13-FCA-601-034 (SS) | To provide email security application | $9,070 |
| Teracai Corporation; 13-FCA-601-059 (SS) | To maintain information technology | $21,661 |

Note: The Agency's SS and CCS contracts totaled $1,470,956 in FY 2013.

* This contract was inadvertently omitted from last year's report.

| **TABLE 13. Competitive Consulting Service (CCS) Contracts of More Than $25,000 and Single-Source (SS) Contracts, FY 2014** | | |
|---|---|---|
| **Contract** | **Purpose** | **Amount** |
| Editorial Experts, Inc.; 14-FCA-240-001 (SS) | To provide editorial services | $100,725 |
| Personnel Decisions Research Institute; 14-FCA-301-002 (SS) | To conduct job analysis | $49,165 |
| Centrec; 14-FCA-301-005 (SS) | To conduct self-study of on-line training | $16,882 |
| R&R Consulting; 13-FCA-450-002 (CCS) | To help update FCA's capital module (Option year 1) | $100,000 |
| C.B. Harris & Co.; 14-FCA-011 (CCS) | To scan documents for conversion | $60,775 |
| SoftChoice Corporation; 13-FCA-601-064 (SS) | To provide Microsoft Enterprise Agreement | $180,161 |
| Murphy Brothers; 14-FCA-601-013 (SS) | To provide taxi services | $10,995 |
| Digital Office Products; 14-FCA-601-024 (SS) | To provide maintenance | $4,322 |
| Avitecture; 14-FCA-601-028 (SS) | To provide maintenance | $13,990 |
| Dave Redden; 14-FCA-601-033 (SS) | To provide retirement counseling | $38,982 |
| International Business Machines; 14-FCA-601-037 (SS) | To provide consulting for Cognos and SPSS products | $14,736 |
| International Business Machines; 14-FCA-601-042 (SS) | To report studio training and eLabs | $78,215 |
| Happier, LLC; 14-FCA-601-040, 047, 050, 052, 069; 14-FCA-700-002 (SS) | To facilitate training programs | $71,070 |
| Entrust, Inc.; 14-FCA-601-055 (SS) | To renew server certifications | $4,025 |
| Teracai; 14-FCA-601-059 (SS) | To provide maintenance | $12,419 |
| SoftChoice; 14-FCA-601-061 (SS) | To help with file sharing and security analysis | $5,500 |
| Patch Advisor; 14-FCA-601-062 (SS) | To assess external network security | $25,000 |
| Economic Systems; 14-FCA-601-063 (SS) | To provide services for Federal Human Resources (FHR) Navigator | $12,955 |
| SAP National Security Services, Inc.; 14-FCA-601-066 (SS) | To renew software license/maintenance contract | $5,720 |
| Gladis Communications, LLC; 14-FCA-067 (SS) | To facilitate training sessions | $6,500 |
| Economic Systems, Inc.; 14-FCA-601-076 (SS) | To validate accuracy of service information on FHR Navigator retirement module | $19,900 |
| ARX, Inc.; 14-FCA-601-084 (SS) | To cosign support and maintenance contract | $9,792 |
| Towers Watson; 14-FCA-601-091 (SS) | To interpret the 2015 compensation survey of agencies covered by the Financial Institutions Reform, Recovery, and Enforcement Act of 1989 | $19,000 |
| BI Technologies; 14-FCA-601-100 (CCS) | To provide Cognos consulting | $75,000 |
| RDA Corporation; 14-FCA-601-101 (CCS) | To provide Cognos Data Warehouse Consulting | $60,953 |
| Delta Research Associations; 14-FCA-601-102 (CCS) | To provide human resource support | $46,836 |
| Gladis Communications, LLC; 14-FCA-601-105 (SS) | To facilitate follow-up on training | $9,000 |
| Towers Watson; 14-FCA-601-107 (SS) | To provide services for job-leveling project | $72,000 |
| Economic Systems, Inc.; 14-FCA-601-110 (SS) | To integrate FHR Navigator with the electronic Official Personnel Folder system | $9,850 |
| Note: The Agency's SS and CCS contracts totaled $1,134,468 in FY 2014. | | |

## Other Functions and Activities

### *Reception and Representation Expenditures*

FCA spent $311.84 on reception and representation expenses in FY 2014.

### *Foreign Travel Expenditures*

During FY 2014, there were no foreign travel expenses.

### *Reimbursements*

We perform various examination, training, and other services for Federal agencies, and we are reimbursed for this work. We are also reimbursed by the National Consumer Cooperative Bank (NCB) for examining the bank as mandated by 12 U.S.C. 3025. See table 14 for information about the reimbursable activities we performed in FY 2014.

**TABLE 14: Reimbursements**

| Contracting Agency | Services Performed | Reimbursement Received for FY 2014 |
|---|---|---|
| USDA | Examination, training, and other services | $154,866 |
| Farm Credit System Insurance Corporation | Examination, training, and other services | $397,290 |
| NCB | Examination services | $295,592 |

## Leveraging FCA Technology

FCA's investment in communication technologies continues to pay off. We are now turning our focus to supporting examiners and analysts in acquiring the data and tools necessary to better analyze and oversee financial risks in the System. Our Office of Management Services supports this goal by opening up new streams of financial data and providing the tools that allow our employees to analyze and transform data into information they can use to better perform their duties.

We continually evaluate new technologies to find ways to make our operations more efficient, and we have greatly improved the ability of our staff to work and communicate regardless of their location. Our IT infrastructure provides dependable, efficient access to data about the institutions we regulate, automates the exchange of data and information, and provides tools through which our staff can monitor and assess financial data and risk. We stress IT security and maintaining the integrity of our information systems. Through our annual Information Resources Management Plan, we monitor and coordinate our IT investments.

We continually seek to provide IT services, data sources, and communication tools that complement current technology and increase connectivity for our mobile workforce. A number of Agency-wide IT projects improved our capabilities in FY 2014:

- We migrated databases from Lotus Notes into updated applications, mostly in SharePoint. During this migration, we enhanced many systems to provide information in a more timely manner and to track work processes.

- We developed electronic signatures and forms to move the Agency from paper records to electronic files. Digital records are easier to access and search than paper records. Plus, we can have stronger internal controls over digital records, better records retention management, and greater confidence in their reliability. One example is the agency's property management system. Now we can electronically document annual property certifications and monitor the addition, deletion, or movement of accountable property.

- We updated the travel management system. The new system provides enhancements to the travel reservation and voucher process.

- We created a Lender Locator application on FCA's website to enable visitors to type in their addresses to find the System institutions that can serve them.

- We streamlined our external data portal that allows System institutions to submit data to us. We automated the routing of the information internally and increased the security of the portal by establishing self-service password resets and requiring passwords to be reset every six months.

- We upgraded and expanded the use of SharePoint, which allows staff to share information quickly and to coordinate on projects.

- We added more wireless access points in the conference rooms, allowing our staff to connect Agency laptops to the FCA network without running cables. In addition, approved vendors doing business with FCA can access the Internet through a guest network.

- We migrated the resource reservations system from Lotus Notes to Exchange to make it easier to reserve office space and equipment. Now staff members can reserve rooms and other resources when they send out a meeting invitation from Outlook.

- We continued to transition additional Internet traffic through Managed Trusted Internet Protocol Services (MTIPS). Routing traffic through an approved MTIPS provider is part of the government-wide Trusted Internet Connections mandate designed to increase the security of the Federal Government.

There are numerous, multi-year projects planned for FYs 2015 and 2016 that will further leverage technology to support our mission and achieve our strategic goals. These projects include the Risk Project, Laptop Evaluation and Replacement, EDGe Project, Management Dashboard, CRS Call Reports, Application Modernization, Farmer Mac Data Collection, Telework Database, Email Archiving and Discovery, Funding Approval SharePoint Site and Continuity of Operations Program. For a summary of each of these projects, please see pages 4 to 6.

## Independent Auditing and Accountability

The Office of Inspector General contracted with Harper, Rains, Knight & Company, P.A., to perform the FY 2014 audit of FCA's financial statements. On November 13, 2014, Harper, Rains, Knight & Company issued an opinion letter relating to the audit of our financial statements for the fiscal year ended September 30, 2014.

- First, the auditor opined that the financial statements presented fairly, in all material respects, FCA's financial position as of September 30, 2014, in conformity with generally accepted accounting principles.

- Second, the auditor did not identify any deficiencies in internal control over financial reporting that would be considered material weaknesses.

- Third, the auditor did not identify any instances of noncompliance with selected provisions of laws and regulations or other reportable matters that could have a direct and material effect on the financial statements.

# ENSURING SAFETY AND SOUNDNESS

The Farm Credit Administration's role is to regulate the Farm Credit System and to ensure that System institutions comply with applicable laws and regulations. In doing so, we ensure the safety and soundness of the System, including the Federal Agricultural Mortgage Corporation.

The first section below, titled "The Farm Credit System," summarizes examination and supervisory activities performed for the banks, direct-lending associations, and service organizations of the FCS. Because the role of Farmer Mac is different from the rest of the System, we discuss Farmer Mac separately in the second section below. In addition, we provide examination and other services on a reimbursable basis to certain entities that are not part of the System. These activities are summarized in the third section below, titled "Other Entities."

Our examination and supervision responsibilities are carried out by staff located in five field offices. One field office is in the McLean, Virginia, headquarters; the other field offices are located in Bloomington, Minnesota; Dallas, Texas; Denver, Colorado; and Sacramento, California. We do not expect any changes in the field office structure in FY 2016.

## The Farm Credit System

### *Statutory and Regulatory Requirements*

The Farm Credit Act requires FCA to examine each FCS institution at least once every 18 months. We meet this requirement through a risk-based process of oversight and examination designed to maximize efficiency while addressing System risk effectively.

To monitor and evaluate the System's safety and soundness, we must have loan portfolio and other data from System institutions, and section 5.9(4) of the Farm Credit Act gives us the authority to collect these data. Our regulations include the following reporting requirements:

- Each System institution must prepare and file quarterly reports of condition and performance with FCA in accordance with 12 CFR 621.12. These reports provide detailed information on each institution's financial performance, portfolio quality, and other relevant information.

- The Federal Farm Credit Banks Funding Corporation must prepare consolidated System information and make this information available to investors and the public in accordance with 12 CFR 630.4.

System institutions submit other data to us through our Consolidated Reporting System. Some of the submitted information is available to the public on our website (www.fca.gov). We also collect loan data for all System institutions. Recently we expanded loan data collection and analysis to enhance our evaluation of risk to the System as a whole.

In addition to overseeing and examining the System, we establish policies and regulations to ensure that the System addresses key risk areas. For example, our regulations require System institutions to have effective loan underwriting and loan administration processes, to provide strong asset-liability management, and to establish high standards for governance and transparent disclosures for shareholder oversight.

### *Risk-Based Examination and Supervision*

We design examination and supervision processes to address material risks and emerging issues on an individual-institution and Systemwide basis. We base our examination and supervision strategies on institution size, existing and prospective risk exposure, and the scope and nature of each institution's business model. In evaluating each institution's business model, we must ensure the institution fulfills its public mission as a Government-sponsored enterprise. In addition to overseeing and examining individual institutions, we also identify and evaluate Systemwide emerging risk and allocate examination resources to matters of highest priority and potential risk.

We have developed a comprehensive regulatory and supervisory framework to promote and help ensure the System's safety and soundness and its compliance with laws and regulations. This approach recognizes each institution's responsibility and ability to identify and manage both institution-specific and systemic risks. Our examination and supervision program promotes accountability in System institutions for their programs, policies, procedures, and controls. System institutions have developed effective risk-management cultures in response to our examination and supervision programs and our policies and regulations. These programs, policies, and regulations continue to set high standards for the System.

Because of volatility in the agricultural and credit markets, as well as significant changes in the financial markets, guarding the safety and soundness of the System is more important and challenging than ever. Annually, to help address these challenges, we identify and use risk topics to set examination priorities, identify potential regulatory issues, allocate resources, and evaluate emerging risk exposures. The oversight and examination program includes strategies for addressing these emerging risks and communicating our expectations to both internal and external audiences. Risk topics for 2015 are as follows:

- Portfolio management in volatile times
- Allowance for loan loss in volatile times
- Large, complex, and shared assets
- Board governance and nominating committees

When our examiners identify unsafe and unsound practices within a System institution or find that an institution has failed to comply with a law or regulation, we outline the corrective actions the institution must take in a Report of Examination or other form of communication. If necessary, we will use our enforcement powers to effect changes in an institution's policies and practices to correct unsafe or unsound conditions or violations of law or regulations. However, in most cases, we achieve corrective action without the use of formal enforcement powers.

### *Measuring the Safety and Soundness of the System*

We use our Financial Institution Rating System (FIRS) as a key method to assess the safety and soundness of each FCS institution. The FIRS provides a general framework, consisting of component and composite ratings, for evaluating and assimilating all significant financial, asset quality, and management factors. Similar to systems used by other Federal financial regulators, the FIRS evaluates six key component areas to properly assess the degree of risk in an institution. These key component areas are capital, assets, management, earnings, liquidity, and sensitivity (CAMELS).

On the basis of our CAMELS ratings, we assign an overall composite rating for the institution. The rating system ranges from 1 to 5. A composite rating of 1 indicates that an institution is sound in every respect and that it exhibits the strongest performance and risk management

practices, whereas a rating of 5 represents an extremely high, immediate, or near-term probability of failure.

Our examiners continually evaluate institutional risk and regularly review and update FIRS ratings to reflect current risks and conditions in each System institution. We provide guidance on both quantitative benchmarks and qualitative factors to help examiners apply the FIRS process consistently.

We disclose these confidential FIRS composite and component ratings to the institution's board and management to provide perspective on relative safety and soundness. Examination reports and other forms of communication also provide the institution's board with an assessment of the governance, management, quality of assets, and financial condition and performance of the institution.

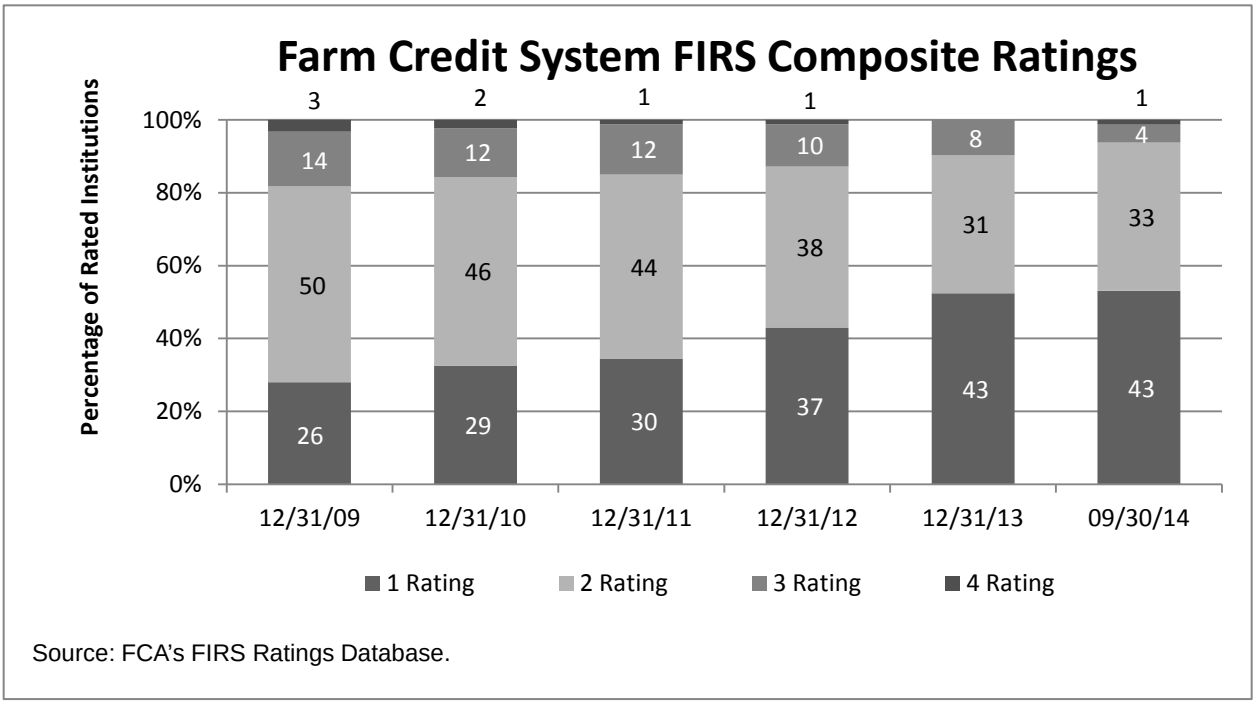
### *Recent Results*

As the composite FIRS ratings over the past several years show, the System's condition and performance have remained satisfactory. Composite FIRS ratings are gradually improving; however, the FIRS ratings have yet to return to the pre-2008 levels. The following summarizes FIRS ratings for System banks and associations as of September 30, 2014:

- Forty-three institutions were rated 1.
- Thirty-three were rated 2.
- Four were rated 3.
- One was rated 4.

See figure 2 for FIRS rating trend information. For a more detailed discussion of the financial condition and performance of the System, see part III of this report.

**FIGURE 2**




Source: FCA's FIRS Ratings Database.

Note: This chart reflects ratings for only the System's banks and direct-lending associations; it does not include ratings for the System's service corporations, Farmer Mac, or the Federal Farm Credit Banks Funding Corporation. Also, the numbers shown on the bars reflect the total number of institutions with a given rating; please refer to the y-axis to determine the percentage of institutions receiving a given rating.

## Federal Agricultural Mortgage Corporation

Through our Office of Secondary Market Oversight (OSMO), we examine and supervise Farmer Mac to ensure both its safety and soundness and mission achievement. OSMO performs annual CAMELS-based examinations, which include examination of capital, assets, management, earnings, liquidity, and sensitivity. Throughout the year, OSMO oversees Farmer Mac's condition and compliance with regulations, and supervises its operations.

### *Statutory Authority*

We regulate Farmer Mac through OSMO, which was established in 1992 by the Food, Agriculture, Conservation, and Trade Act Amendments of 1991 (Public Law 102-237). OSMO provides for the examination and general supervision of Farmer Mac's safe and sound performance of its powers, functions, and duties. The statute requires that OSMO be managed by a full-time director who reports to the FCA Board and that OSMO's activities, to the extent practicable, be carried out by individuals not responsible for supervising the banks and associations of the FCS.

### *Data Reporting Requirements*

Farmer Mac is required to submit quarterly Call Reports to OSMO in addition to meeting several other periodic reporting requirements related to Farmer Mac's regulatory risk-based capital, mission, liquidity, and financial derivatives portfolio. In addition, Farmer Mac is subject to the disclosure and reporting requirements of the Securities and Exchange Commission.

### *Financial Condition and Performance*

Farmer Mac's financial condition and performance trends were generally positive in FY 2014.

- Net income available to common shareholders was $45.1 million for the 12 months ended September 30, 2014, compared with $68.9 million during FY 2013.
- Core earnings, a non-GAAP measure of economic performance, totaled $58.8 million during FY 2014 compared with $51.2 million during FY 2013.
- Farmer Mac's core capital totaled $761.3 million at the end of FY 2014, compared with $578.4 million at the end of FY 2013. The minimum core capital requirement for Farmer Mac's on- and off-balance-sheet exposures is set in the statute and totaled $547.1 million at the end of FY 2014. Thus, Farmer Mac exceeded its minimum core capital requirement by approximately $214.2 million.
- At the end of FY 2014, Farmer Mac had $771.9 million in regulatory capital available to meet the $67.3 million minimum requirement established by FCA's Risk-Based Capital (RBC) Model.

Farmer Mac experienced growth in its program and nonprogram portfolios during FY 2014.

- Program activity increased approximately 1.6 percent and ended FY 2014 at $14.0 billion.
- Cash and nonprogram investments decreased approximately 17.2 percent and ended FY 2014 at $2.6 billion.

Credit quality remained stable and generally good. Real estate owned declined over FY 2014, finishing the year at $1.2 million, down approximately $1.7 million from fiscal year-end 2013.

### *Risk-Based Capital (RBC) Model*

Section 8.32 of the Farm Credit Act requires the RBC Model to be used to determine the amount of regulatory capital that is sufficient for Farmer Mac to maintain positive capital during a 10-year period under certain credit risk and interest rate risk situations. The RBC Model must estimate credit losses on agricultural mortgages owned or guaranteed by Farmer Mac.

The rate of loan default and severity of losses on agricultural mortgages must be reasonably related to the default rate and severity of losses experienced in contiguous areas of the United States; the contiguous areas considered must contain at least 5 percent of the total U.S. population that experienced the highest rate of default and severity of agricultural mortgage losses during the past two consecutive years or more. The rate of loan default and severity of losses on rural utility loans must be reasonably related to risks in electric and telephone facility loans.[4]

The Farm Credit Act also requires the RBC Model to incorporate an interest rate risk stress scenario based on rising and falling interest rates on Treasury obligations of various terms. In addition, the Farm Credit Act requires Farmer Mac to maintain capital to protect against management and operational risks. This additional capital must amount to 30 percent of the sum of the credit loss and interest rate risk components of the RBC Model.

The output of the stress test depends on Farmer Mac's risk profile. High-risk loan assets or significant interest rate risk exposure causes the RBC Model to calculate a higher regulatory capital requirement. Conversely, if Farmer Mac maintains a low risk profile in both its loan portfolio and interest rate risk exposure, the stress test will calculate a low capital requirement. Our regulations require Farmer Mac to have its operation of the RBC Model validated by an independent third party at least every three years. In all of these third-party validations, Farmer Mac has been found to be operating the model appropriately.

We published a final rule in early 2011 to amend our RBC Model regulation to allow for revisions to the model, including a revision that would reflect loan activity involving rural utility cooperatives. An Advance Notice of Proposed Rulemaking was published in June 2011 to solicit public input on further revisions to the model. We are considering a revision to the software platform on which the model runs. Currently, the model uses a Microsoft Excel platform. A different platform could significantly streamline the processing of model runs as Farmer Mac's portfolio grows and its product mix broadens.

[4] Farmer Mac's express program activities were expanded in the Food, Conservation, and Energy Act of 2008 to include rural utilities.

## Other Entities

On a reimbursable basis, we perform examinations of certain entities that are not part of the Farm Credit System.

- As mandated by 12 U.S.C. 3025, we examine the National Consumer Cooperative Bank, which owns a Federal savings bank, has a congressional charter, and specializes in nonagricultural cooperative loans.

- From time to time, the U.S. Department of Agriculture contracts with us to provide examination services for specific USDA programs. We annually review the amount of resources dedicated to providing these services. Currently, the amount is limited.

- We also provide services on a reimbursable basis to the Farm Credit System Insurance Corporation (FCSIC), an independent, Government-controlled corporation that insures the timely payment of principal and interest on certain System notes, bonds, and other obligations issued to investors. The FCSIC Board consists of the members of the FCA Board. Section 5.59(5) of the Farm Credit Act provides that, to the extent practicable, FCSIC must use FCA personnel and resources to minimize duplication of effort and reduce costs.

For more information about reimbursable activities in 2014, see table 14 on page 30 under "Other Functions and Activities."

# DEVELOPING REGULATIONS AND POLICIES

FCA routinely issues regulations, Informational Memoranda, policy statements, and other guidance to ensure that the System complies with the law, operates in a safe and sound manner, and efficiently carries out its statutory mission.

We are committed to providing a flexible regulatory environment that allows the System to offer high-quality, reasonably priced credit and related services to farmers and ranchers, their cooperatives, rural residents, and other entities on which farming operations depend. We strive to develop balanced, well-reasoned, and flexible regulations, always taking into account both the benefits and the costs of these regulations to System institutions. Our objectives are to ensure that the System's activities remain consistent with the law and safety and soundness principles and to encourage participation by member-borrowers in the management, control, and ownership of their institutions.

## Regulatory and Policy Projects Active at End of FY 2014

The FCA Board periodically reviews its regulatory agenda to evaluate progress on open projects and to determine the need for additional initiatives. The FCA Board-approved agenda is part of the Federal Unified Agenda, which is published online at www.reginfo.gov. We are not obligated to act on our agenda items, and we may propose or issue regulations that have not been set forth in the Unified Agenda. We publish our Regulatory Projects Plan on our website to notify the public of our upcoming regulatory actions and to encourage the public to participate in the regulatory process.

The following list summarizes our current regulatory efforts and other guidance under consideration in FY 2015 and FY 2016.

**Loans in Areas Having Special Flood Hazards:** We plan to publish a final rule to amend our regulations on flood insurance to conform to the Biggert-Waters Flood Insurance Reform Act of 2012.

**Investment Eligibility:** We plan to publish a final rule to revise the eligibility requirements for investments by System institutions. To comply with a provision of the Dodd-Frank Act, this rule would also remove references to credit ratings in the regulations and substitute an appropriate standard of creditworthiness.

**Capital—Basel III:** We plan to publish a final rule to revise sections of the capital rules to make them consistent with Basel III where appropriate.

**Standards of Conduct:** We plan to publish a final rule to clarify and strengthen regulations related to the standards of conduct of directors, employees, and agents of System institutions.

**Mergers, Consolidations, and Charter Amendments:** We plan to publish a final rule to amend regulations pertaining to mergers, consolidations, and charter amendments of System banks and associations.

**Farmer Mac—Corporate Governance and Standards of Conduct:** We plan to issue a notice of proposed rulemaking in early 2015 to clarify and strengthen Farmer Mac's board governance regulations and to establish standards-of-conduct regulations.

**Farmer Mac—Investment Eligibility:** We plan to publish a proposed rule and a final rule to change eligible investment asset classes. To comply with the Dodd-Frank Act, this rule would also remove references to credit ratings in the regulations and substitute an appropriate standard of creditworthiness.

**Farmer Mac—Risk-Based Capital Stress Test, Version 5.0:** We plan to conduct a review to determine how to remove credit ratings data from the Risk-Based Capital Model. The Dodd-Frank Act requires agencies to remove references to credit ratings in their regulations and to substitute other creditworthiness standards.

**Institution Stockholder Voting Procedure:** We plan to publish a final rule to clarify and enhance voting procedures related to the tabulation of votes, the use of teller committees, and the handling of ballots.

**Appraisal Regulations:** We plan to complete our review to consider whether changes in appraisal regulations are necessary in light of changing credit and economic conditions.

**Territorial Concurrence:** We plan to conduct a review of current regulations requiring associations to notify each other and obtain concurrence when they extend loans in the chartered territories of other associations. The purpose of the review is to determine whether the regulations are appropriate for the System's current structure, lending practices and operating environment, and whether the regulations support safety and soundness, operational efficiency, cooperative principles, and customer service.

**Bank Review of Insider Loans:** We plan to complete a review to consider whether current regulations requiring bank review of association insider loans are appropriate for the System's current structure and whether the bank review ensures compliance with applicable standards-of-conduct regulations.

**Crop Insurance Sales Compensation:** We plan to complete a review to consider whether current limitations on compensation from crop insurance sales should be modified.

**Eligibility Criteria for Directors:** We plan to begin a review to consider the eligibility criteria for directors, particularly when a candidate for a director position owns an interest in an entity that borrows or holds stock in a System bank or association.

**Removal of Stockholder-Elected Directors:** We plan to begin a review to consider whether, and under what circumstances, a stockholder-elected director of a System bank or association can be removed by the bank's or association's board of directors.

**Financing Farm-Related Service Businesses:** We plan to complete our evaluation of the System's lending to farm-related service businesses to determine whether our regulations provide the appropriate framework for determining borrower eligibility and purposes of financing. Among the businesses to be considered are service providers within local food systems.

**Amortization Limits—Agricultural Credit Associations and Production Credit Associations:** We plan to complete our review of amortization limits for Agricultural Credit Associations and Production Credit Associations.

**Bank-Association Lending Relationship:** We plan to complete our review to evaluate the regulatory requirements of general financing agreements between banks and associations. As part of this review, we will consider whether we should enhance the banks' authorities to address safety and soundness issues in affiliated associations.

**Criminal Activity Referrals and Related Internal Controls:** We plan to begin a review of our regulatory guidance on internal controls designed to prevent, identify, and monitor fraud and criminal activity. We will also review the processes for referring known or suspected criminal violations.

**Director Election Nomination Procedures:** We plan to begin a review of our regulations and guidance related to the director nomination process. As part of this review, we will consider the kind of information to which nominating committees should have access when considering potential nominees.

**Attribution Rules:** We plan to begin a review of the attribution rules that institutions must use when they determine whether loans to a borrower should be combined and attributed to a related borrower's outstanding loans. Attribution rules affect calculations for lending and leasing limits.

## Regulatory and Policy Projects Completed in FY 2014 and Early FY 2015

Following is a list of projects we completed in FY 2014 and early FY 2015, along with a list of communications we issued to System institutions to clarify our rules.

**Flood Insurance:** We published a proposed rule to require System institutions to escrow premiums and fees for flood insurance for any loan secured by residential improved real estate or a mobile home.

**Mergers, Consolidations, and Charter Amendments:** We published a proposed rule to amend regulations pertaining to mergers, consolidations, and charter amendments of System banks and associations.

**Pension Benefits Disclosure:** We published a proposed rule to exclude certain employees and their compensation amounts from the compensation disclosure requirement for System institutions.

**Institution Stockholder Voting Procedure:** We published a proposed rule to clarify and enhance voting procedures related to the tabulation of votes, the use of teller committees, and the handling of ballots.

**Margin and Capital Requirements for Noncleared Swaps:** We published an interagency proposed rule that would establish margin and capital requirements for FCS institutions, including Farmer Mac, that engage in noncleared swaps and noncleared security-based swap transactions. The rulemaking would fulfill a requirement of the Dodd-Frank Act.

**Regulatory Burden Final Notice:** We published a Final Notice responding publicly to comments we received from the 2013 Regulatory Burden Solicitation.

**Investment Eligibility:** We published a proposed rule to revise the eligibility requirements for investments by System institutions.

**Capital—Basel III:** We published a proposed rule to revise sections of the capital rules to modernize them and make them consistent with Basel III where appropriate.

**Repealing Nonbinding Advisory Votes:** We published an interim final rule and a final rule to remove regulatory provisions on nonbinding advisory votes.

**Farmer Mac—Corporate Governance and Standards of Conduct:** We published an Advance Notice of Proposed Rulemaking requesting public input on possible regulatory changes addressing board governance and standards of conduct at Farmer Mac.

**Rural Community Investments and Investments in Rural America:** We withdrew the proposed rule on System institutions' statutory and regulatory authority to make rural community investments. We also concluded the Investments in Rural America pilot programs effective December 31, 2014. System institutions may hold any authorized investments outstanding at that date until maturity.

**Farmer Mac—Liquidity Management:** We published a final rule to provide guidance on policies, procedures, and best practices related to liquidity investment operations. The rule also revised regulatory limits on liquidity risk.

**Reports of Accounts and Exposures:** We published a final rule that established our minimum data requirements for evaluating risk in FCS loan portfolios.

**Cybersecurity Framework and Other Recent Guidance:** We issued an Informational Memorandum to System institutions outlining best practices and recent guidance for managing cybersecurity risk. All System institutions should be taking appropriate actions to monitor and manage cybersecurity threats and vulnerabilities.

**Lending, Training, and Outreach Opportunities with the Farm Service Agency:** We issued an Informational Memorandum to System institutions to provide information on lending, training, and outreach opportunities available through the U.S. Department of Agriculture's Farm Service Agency. These opportunities may benefit an institution when trying to reach a broader segment of the agricultural community.

**Investment Requests:** We issued an Informational Memorandum to provide guidance to System institutions on submitting approval requests for investment purchases. For example, any request must explain the purpose of the investment and any risks it poses to the institution.

**Farm Credit System Operating Expenses:** We issued an Informational Memorandum to System institutions to provide guidance on properly managing operating expenses to help ensure safe and sound performance of System institutions.

**Increased Maximum Flood Insurance Coverage for Other Residential Buildings:** We issued an Informational Memorandum to notify System institutions of the flood insurance coverage increase and to provide them a copy of the "Interagency Statement on Increased Maximum Flood Insurance Coverage for Other Residential Buildings."

**Revised Guidelines on Submission of Proposals to Merge or Consolidate Farm Credit System Associations:** We issued an Informational Memorandum to notify System institutions of revisions to our guidelines on the submission of proposals to merge or consolidate.

**Social Media: Consumer Compliance Risk Management:** We issued an Informational Memorandum to notify System institutions of our expectations regarding the supervisory guidance issued by the Federal Financial Institutions Examination Council, titled "Social Media: Consumer Compliance Risk Management Guidance."

**Interagency Statement on the Impact of Biggert-Waters Act:** We issued an Informational Memorandum to notify System institutions that the force placement and civil money penalty provisions of the Biggert-Waters Act became effective upon enactment and that the private flood insurance and escrow provisions of the Biggert-Waters Act will not be effective until regulations are issued.

**Maximum Bank Director Compensation:** We issued an Informational Memorandum to notify Farm Credit banks of the maximum allowable bank director compensation for 2014.

## FCS Corporate Activity and Other Prior Approvals and Clearances

In accordance with the Farm Credit Act and our regulations, we issue prior approvals for corporate and noncorporate applications. Corporate applications include requests from FCS institutions for us to issue new or amended charters, as well as to cancel charters because of mergers, consolidations, liquidations, or terminations of System status.

Noncorporate applications include requests related to preferred stock and subordinated debt offerings and requests for prior approval of funding, mission-related investments, and any new financially related services.

### *Corporate Activities in FY 2014 and Early FY 2015*

During FY 2014, we canceled the charters of twelve associations—four ACAs and eight subsidiaries—as a result of four mergers. We also approved a name change.

- On January 1, 2014, four ACAs affiliated with CoBank, ACB, merged, resulting in two ACAs with subsidiaries.
- On January 1, 2014, four ACAs affiliated with the Farm Credit Bank of Texas merged, resulting in two ACAs with subsidiaries.
- On January 1, 2014, an ACA affiliated with AgriBank, FCB, changed its name.

Thus far in FY 2015, we canceled the charters of six associations—two ACAs and four subsidiaries—as a result of two mergers, and we approved one name change.

- On October 1, 2014, two ACAs affiliated with CoBank, ACB, merged, resulting in an ACA with subsidiaries.
- On January 1, 2015, two ACAs affiliated with the Farm Credit Bank of Texas merged, resulting in an ACA with subsidiaries.
- On January 1, 2015, an ACA affiliated with CoBank, ACB, changed its name.

### *Projected Mergers and FCS Institution Size*

As of January 1, 2015, the System had 76 direct-lender associations and 4 banks. Seven service corporations and special-purpose entities (see pages 51 and 52) brought the total number of FCS institutions to 87 (including Farmer Mac). Because of mergers and consolidations, the number of FCS associations has declined by 56 percent since 2000, and the number of FCS banks has decreased by 43 percent.

Although merger activity has slowed in recent years, we estimate that over time the number of direct-lender associations will continue to decline. These mergers, coupled with asset growth, will increase the size of System entities. System institutions will also possess more complex management systems and offer a broader range of financial services to their borrowers.

### *Security Offerings During FY 2014*

We reviewed and did not object to the following proposed offering circulars for issuing Class H cumulative preferred stock:

- A circular from American Ag Credit, ACA
- A circular from Farm Credit of Southern Colorado, ACA

In addition, we authorized CoBank to use a Base Form Disclosure Document under specified terms (preclearance) to issue noncumulative perpetual preferred stock until the end of 2014.

### *Funding Activity*

The FCS raises funds for loans and investments primarily by selling Systemwide debt securities through the Federal Farm Credit Banks Funding Corporation,[5] the fiscal agent for the Farm Credit banks. In this way, funds flow from worldwide capital-market investors to agricultural producers, agricultural cooperatives, and rural communities, providing them with ready and efficient access to global resources. Systemwide debt securities are issued as discount notes, master notes, bonds, or designated bonds. As required by the Farm Credit Act, the System must obtain FCA approval for all debt issuances.

For the 12 months ended September 30, 2014, the FCS issued $346 billion in Systemwide debt, which was $30 billion less than the debt issued in FY 2013 and FY 2012. In general, Systemwide debt issuance declined as call opportunities for outstanding FCS debt instruments subsided when interest rates started to trend upward—the exception being debt instruments with maturities of one year and less. The decline in Systemwide issuance was tempered by the continued steady growth in overall FCS debt outstanding, which tallied $213.7 billion at the end of FY 2014.

The financial markets exhibited much greater stability, with intermittent volatility caused by geopolitical events. Regardless, investor demand for System debt remained favorable across the yield curve.

[5] See section 4.9 of the Farm Credit Act. The Federal Farm Credit Banks Funding Corporation's primary function is to issue, market, and handle debt securities on behalf of the System banks. In addition, the Funding Corporation assists the System banks with a variety of asset/liability management and specialized funding activities. Headquartered in the greater New York City area, the Funding Corporation is responsible for the System's financial disclosure and the release of public information concerning the financial condition and performance of the System as a whole.

### *Investments in Rural America*

In January 2005, we issued guidance that gave System institutions an opportunity to participate in pilot programs supporting investments in rural America (see FCA Informational Memorandum dated January 11, 2005, Investments in Rural America—Pilot Investment Programs).

The pilot programs gave FCS institutions greater flexibility to partner with Government agencies and other agricultural and rural lenders in fulfilling FCS mission objectives. In addition, through the programs, we gained a better understanding of the diverse financing needs of agriculture and rural communities and the ways FCS institution investments can help increase the availability of funds to these markets.

On November 14, 2013, the Farm Credit Administration Board voted to conclude, effective December 31, 2014, each pilot program approved after 2004 as part of the Investments in Rural America program. The Board's action permits each System institution that is participating in a pilot program to continue to hold its investments through the maturity dates for the investments, provided the institution continues to meet all approval conditions.

Although we have concluded these pilot programs, we will consider investment requests on a case-by-case basis under the existing investment regulations. The information gathered and experience gained through the pilot programs will be useful when we evaluate future investment requests.

# Part III

# FARM CREDIT SYSTEM

# PROFILE OF THE FARM CREDIT SYSTEM

The Farm Credit System consists of a network of borrower-owned cooperative financial institutions, as well as related service organizations and the Federal Agricultural Mortgage Corporation. The Farm Credit System was created by Congress in 1916 to provide American agriculture with a dependable source of credit. It is the oldest of the financial Government-sponsored enterprises (GSEs). As of January 1, 2015, the System had four banks providing loan funds to

- 74 Agricultural Credit Association (ACA) parent organizations, each of which has two subsidiaries—a Production Credit Association (PCA) and a Federal Land Credit Association (FLCA), and
- 2 stand-alone FLCAs.

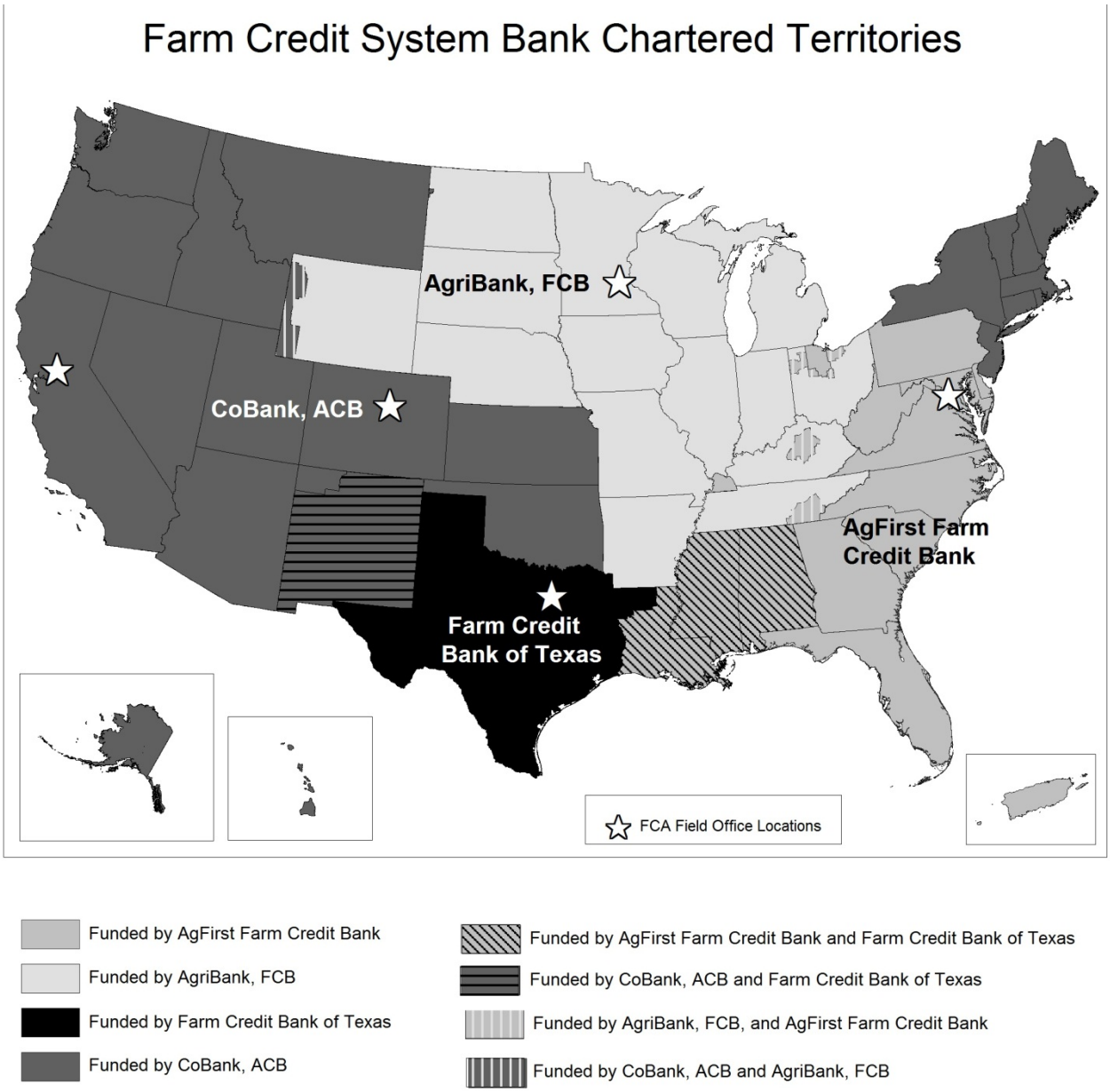
The map in figure 3 shows each bank's chartered territory.

Although legally separate, the ACA and its PCA and FLCA subsidiaries operate as an integrated lending business, with loans made through the subsidiaries appropriate to the authority of each subsidiary. The ACA, the PCA, and the FLCA are jointly and severally liable for the full amount of the indebtedness to the funding bank under a General Financing Agreement. In addition, the parent company and its subsidiaries pledge their respective assets as security for each other's debts and obligations and share each other's capital.

The three associations have a common board and management and a common set of shareholders. Under the Farm Credit Act, FLCAs are Federal Land Bank Associations that originate long-term agricultural mortgages and are exempt from Federal and State income taxes; ACAs and PCAs originate short- and intermediate-term operating loans and are not tax-exempt.

System institutions provide credit and financially related services to farmers, ranchers, producers or harvesters of aquatic products, and farmer-owned cooperatives. Institutions also make loans for agricultural processing and marketing activities, rural housing, certain farm-related businesses, agricultural and aquatic cooperatives, rural utilities, and foreign and domestic entities in connection with international agricultural trade. The System raises its loan funds by selling debt securities in the national and international money markets; these securities are subject to FCA's approval, but they are not guaranteed by the U.S. Government.

**FIGURE 3**




NOTE: CoBank, ACB, funds 26 associations in the indicated areas and serves cooperatives nationwide; Farm Credit Bank of Texas funds 14 associations; AgriBank, FCB, funds 17 associations; and AgFirst Farm Credit Bank funds 19 associations. The Farm Credit System contains a total of 80 banks and direct-lending associations.

## Additional System Entities and Service Corporations

In addition to the System's banks and associations, we are responsible for regulating and examining the Federal Agricultural Mortgage Corporation and the Federal Farm Credit Banks Funding Corporation. We also regulate and examine the five service corporations organized under section 4.25 of the Farm Credit Act[6]: AgVantis, Inc.; Farm Credit Leasing Services Corporation; Farm Credit Financial Partners, Inc.; the FCS Building Association (FCSBA); and Farm Credit Foundations.

**Federal Agricultural Mortgage Corporation—**Farmer Mac[7] is a stockholder-owned, federally chartered instrumentality of the United States created in 1988 to establish a secondary market for agricultural real estate and rural housing mortgage loans. In May 2008, the Food, Conservation, and Energy Act of 2008 expanded Farmer Mac's program authorities by allowing it to purchase and guarantee securities backed by rural utility loans made by cooperatives.

Farmer Mac conducts its business primarily through four core programs:

- Farm & Ranch
- USDA Guarantees
- Rural Utilities
- Institutional Credit

Under the Farm & Ranch and Rural Utilities segments, Farmer Mac purchases, or commits to purchase, qualified loans, or obligations backed by qualified loans, that are not guaranteed by any instrumentality or agency of the United States. Under USDA Guarantees, Farmer Mac purchases the guaranteed portions of farm ownership and farm operating loans, rural business and community development loans, and certain other loans guaranteed by USDA. Under Institutional Credit, Farmer Mac purchases bonds backed by eligible debt obligations of agricultural and rural utility lenders.

**Federal Farm Credit Banks Funding Corporation—**The Funding Corporation is owned by System banks; it sells debt securities on behalf of the banks to raise funds for loans and other purposes. System institutions obtain the majority of their funds through the sale of these securities in the Nation's capital markets. These securities, chiefly in the form of bonds and discount notes, are offered by the Funding Corporation through a nationwide group of securities dealers and dealer banks. The Funding Corporation's debt issuance programs provide the System banks with funds to lend to farmers, ranchers, and agricultural cooperatives; debt issuances also provide the banks with funding for their other operations.

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[6] Section 4.25 of the Farm Credit Act provides that one or more FCS banks or associations may organize a service corporation to perform functions and services on their behalf. These federally chartered service corporations are prohibited from extending credit or providing insurance services.

[7] Farmer Mac is established in law as a part of the FCS. However, Farmer Mac has no liability for the debt of any other System institution, and the other System institutions have no liability for Farmer Mac's debt. Farmer Mac is organized as an investor-owned corporation, not a member-owned cooperative. Investors in voting stock may include commercial banks, insurance companies, other financial organizations, and FCS institutions. Nonvoting stock may be owned by any investor. Farmer Mac is regulated by FCA through the Office of Secondary Market Oversight. The OSMO Director reports directly to the FCA Board on matters of policy.

**AgVantis, Inc.—**AgVantis, Inc., provides technology-related and other support services to associations in the CoBank, ACB, district. It was chartered by FCA in 2001 and is owned by CoBank, ACB, and 16 of its affiliated associations.

**Farm Credit Leasing Services Corporation—**The Leasing Corporation, owned by CoBank, ACB, provides equipment leasing services to eligible borrowers, including agricultural producers, cooperatives, and rural utilities.

**Farm Credit Financial Partners, Inc.—**Farm Credit Financial Partners, Inc., provides support services to CoBank, ACB; five associations affiliated with CoBank, ACB; one association affiliated with AgriBank, FCB; the Leasing Corporation; and two FCS-related entities.

**FCS Building Association—**FCSBA, which acquires, manages, and maintains facilities to house our headquarters and field office staff, was formed in 1981. It is owned by System banks and is subject to the oversight and direction of the FCA Board.

**Farm Credit Foundations—**Farm Credit Foundations provides human resource services to its employer-owners, including payroll processing, benefits administration, centralized vendor management, workforce management and operations services, corporate tax and financial reporting services, and retirement workshops. It is owned by 41 Farm Credit associations, one service corporation (AgVantis, Inc.), and one Farm Credit Bank (AgriBank, FCB).

## FCS Mission Fulfillment

The System fulfills its overall mission by lending to agriculture and rural America. Through changes in the law since the System's original authorization in 1916, System lending authorities have evolved to include the following:

- Long-term agricultural real estate loans and rural home loans
- Short- and intermediate-term agricultural loans
- Loans to producers and harvesters of aquatic products
- Loans to certain farmer-owned agricultural processing facilities and farm-related businesses
- Loans to farmer-owned agricultural cooperatives
- Loans that finance agricultural exports and imports
- Loans for rural utilities
- Limited portions of loans to entities that qualify under the System's similar-entity authority

In addition to its lending programs, System institutions participated (until December 31, 2014) in several mission-related pilot investment programs (referred to as Investments in Rural America). The programs allowed us to evaluate the ability of System institutions to provide a

flexible flow of funds to agriculture and rural communities across the country. (See page 46 for a description of the Investments in Rural America program.)

# FINANCIAL CONDITION AND PERFORMANCE

In FY 2014, the overall condition and performance of the FCS remained safe and sound. As the drop in nonaccrual loan activity shows, asset quality continued to improve in FY 2014. All banks and associations continued to maintain capital ratios in excess of minimum regulatory requirements, and net income increased.

The decline in grain and soybean prices is expected to have a negative impact on crop producers, but these lower prices will generally be positive for producers and processors in the livestock, dairy, poultry, and ethanol industries. This shift in the commodity outlook could create shifts in the System's risk profile.

The System's loan portfolio continued to grow because of continued demand for cropland and the overall demand for new loans. For the 12 months ended September 30, 2014, gross loans increased by 7.1 percent, compared with a 4.7 percent gain during the previous 12-month period.

## Earnings

The FCS earned $3.6 billion in the first nine months of 2014, a 2.0 percent increase from the $3.5 billion earned in the same period in 2013. As table 15 shows, net income rose primarily because of an increase in net interest income and a decrease in the provision for loan losses. This was partially offset by an increase in the provision for income taxes and an increase in noninterest expense.

**TABLE 15: Net Income (Dollars in Millions)**

| | First 9 Months of 2013 | First 9 Months of 2014 | Dollar Change | Percent Change |
|---|---|---|---|---|
| Net interest income | $4,981 | $5,056 | $75* | 1.5 |
| - Provision for losses | 9 | 7 | (2) | (22.2) |
| = Net interest income after loss provision | $4,972 | $5,049 | 77 | 1.5 |
| + Noninterest income | 444 | 489 | 45 | 10.1 |
| - Noninterest expense | 1,749 | 1,795 | 46 | 2.6 |
| = Pretax income | $3,667 | $3,743 | 76 | 2.1 |
| - Provision for income tax | 168 | 174 | 6 | 3.6 |
| = Net income | $3,499 | $3,569 | $70 | 2.0 |

Source: FCS Quarterly Information Statements.
*The change in the volume of interest income was $327 million, but changes in interest rates caused a loss of $252 million, resulting in a total net change increase of $75 million in net interest income.

An increase in average interest-earning assets, from $238.3 billion at September 30, 2013, to $255.0 billion a year later, primarily drove the increase in net interest income. However, the net interest margin declined 15 basis points because of a decrease in the net interest spread. The net interest spread declined 15 basis points to 2.50 percent from the same period one year ago. The

net interest margin also decreased because of competitive pressures and an increase in the average loan volume in lower-spread lines of business. The yield on interest-earning assets fell by an annualized rate of 14 basis points, while the yield on interest-bearing liabilities increased by an annualized rate of 1 basis point. See table 16.

**TABLE 16: Interest Margin in Annualized Percentages**

| | First 9 Months of 2013 | First 9 Months of 2014 | Change (bps) |
|---|---|---|---|
| **Total interest-earning assets** | **3.60** | **3.46** | **(14)** |
| Total loans | 4.11 | 3.98 | (13) |
| Investments and other assets | 1.45 | 1.33 | (12) |
| **Total interest-bearing liabilities** | **0.95** | **0.96** | **1** |
| **Net interest spread** | **2.65** | **2.50** | **(15)** |
| Impact of noninterest-bearing items | 0.14 | 0.14 | (0) |
| **Net interest margin** | **2.79** | **2.64** | **(15)** |

Source: FCS Quarterly Information Statements, pg. 12.
bps = basis points

The System's net return measures remained satisfactory across all the districts during the first nine months of 2014. As table 17 shows, the return on average assets and the return on average capital weakened in all System districts except the Texas district.

**TABLE 17: Profitability Across System Districts for First 9 Months of Year**

| | | AgFirst | AgriBank | Texas | CoBank |
|---|---|---|---|---|---|
| Percentage return on average assets | 2013 | 2.11 | 1.92 | 2.03 | 1.56 |
| | 2014 | 1.97 | 1.83 | 2.11 | 1.46 |
| Percentage return on average capital | 2013 | 13.87 | 12.00 | 12.40 | 11.82 |
| | 2014 | 12.01 | 10.85 | 12.86 | 11.07 |

Source: FCS Quarterly Information Statements, pg. F-58.

## Asset Growth

The System's loans and assets grew moderately during the year ended September 30, 2014. Strong demand for cropland in the Midwest helped spur the increase in assets and loans. The demand for new loans and increased lending to food and agribusiness companies also contributed to this growth.

FCS assets grew to $271.3 billion as of September 30, 2014, up $18.4 billion (7.3 percent) from September 30, 2013. Increases in loans by $13.8 billion (7.1 percent), investments by $4.2 billion (9.0 percent), and cash by $370 million (18.5 percent), produced the moderate increase in total assets.

All System districts experienced loan growth for the year ended September 30, 2014. Loan volume in the CoBank district grew by $6.3 billion, an increase of 8.0 percent over its loan volume a year earlier. Gross loan volume in the Texas and AgriBank districts increased by $1.4 billion (7.8 percent) and $5.2 billion (6.5 percent), respectively. The AgFirst district experienced the smallest increase; its gross loan volume increased by $1.0 billion (4.5 percent). See table 18.

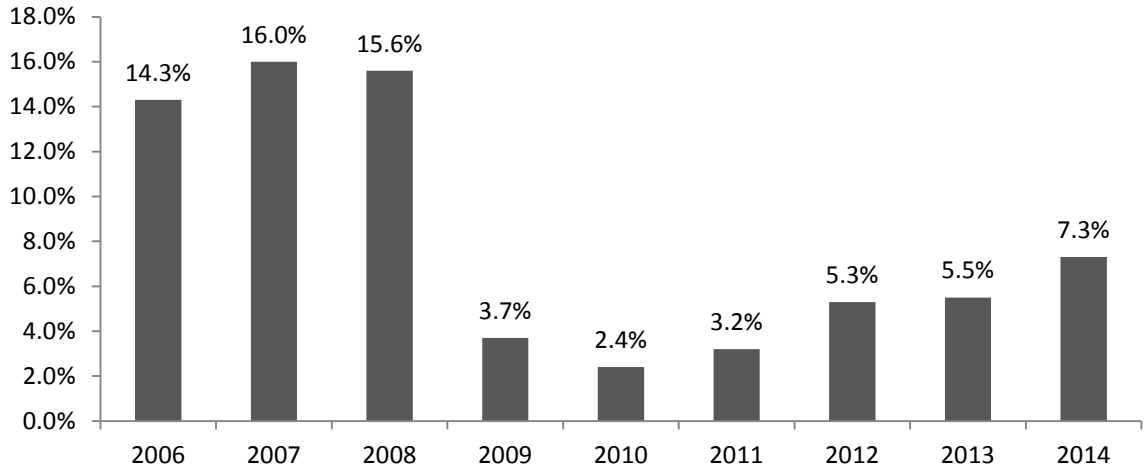
**TABLE 18: Gross Loan Growth by District and Systemwide (Dollars in Millions)**

| | September 30, 2013 | | September 30, 2014 | | | |
|---|---|---|---|---|---|---|
| | Gross Loans | Percent Total | Gross Loans | Percent Total | Change in Dollars | Percent Change |
| AgFirst | $23,082 | 11.9 | $24,117 | 11.6 | 1,035 | 4.5 |
| AgriBank | 80,015 | 41.2 | 85,210 | 41.0 | 5,195 | 6.5 |
| Texas | 17,334 | 8.9 | 18,692 | 9.0 | 1,358 | 7.8 |
| CoBank | 78,086 | 40.2 | 84,350 | 40.5 | 6,264 | 8.0 |
| Intra-System Eliminations | (4,306) | (2.2) | (4,318) | (2.1) | (12) | NM* |
| **Total for System** | **$194,211** | **100** | **$208,051** | **100** | **$13,840** | **7.1** |

* Not meaningful.
Source: FCS Quarterly Information Statements, pg. F-54, 2014, and pg. F-52, 2013.

As noted in figure 4 below, the System's total assets increased slightly faster during the 12-month period ended September 30, 2014, than during the previous period but much slower than during the 2006 to 2008 period, the three years prior to the recession.

**Figure 4: Percent Change in System Assets (Twelve months ended in September)**




Source: FCS Quarterly Information Statements

## Assets—Investments

The System's investments grew 9.0 percent during FY 2014. As table 19 shows, the System increased its holdings of money market instruments, U.S. Treasury securities, U.S. agency securities, and other asset-backed securities while reducing holdings of mortgage-backed securities and mission-related investments.

All segments of the investment portfolio available for sale experienced a decrease in yield during the most recent 12-month period except for U.S Treasury securities available for sale, which increased from 0.59 percent to 0.94 percent. The yield on total nonmission-related securities available for sale decreased from 1.31 percent to 1.24 percent.

All segments of the investment portfolio held to maturity except for other asset-backed securities decreased in yield during the most recent 12-month period, with money market instruments (held to maturity) experiencing the largest decline—from 5.82 percent to 5.75 percent. The yield for other asset-backed securities increased 12 basis points to 2.38 percent at September 30, 2014, from the previous year. The yield on total nonmission-related securities held to maturity increased slightly, from 3.15 percent to 3.16 percent.

Ineligible investments held by the System declined from $1.6 billion at September 30, 2013, to $1.2 billion at September 30, 2014. Most ineligible investment securities that the System has on its books became ineligible as a result of the unfavorable market conditions caused by the financial crisis.

According to FCA's regulatory standards, certain investments must maintain the highest credit rating by at least one Nationally Recognized Statistical Rating Organization, such as Moody's Investors Service, Standard & Poor's Ratings Services, or Fitch Ratings, to be eligible to be held by the System. In addition, certain investments may represent no more than a limited percentage of an institution's portfolio.

Under our former regulations, an investment can become ineligible even though it was an eligible investment when purchased. However, under the Investment Management final rule, which became effective on December 31, 2012, System institutions may now continue to hold, subject to certain conditions, investments that no longer satisfy eligibility criteria that they met when they were purchased. Previously the ineligible investment had to be divested within six months unless FCA approved a plan to hold the investments for a longer period of time.

**Table 19: FCS Investments**
**(Dollars in Millions)**

| | | September 30, 2013 | | September 30, 2014 | | Change | | |
|---|---|---|---|---|---|---|---|---|
| | | | | | | Amount | | |
| | | Amount | WAY (%) | Amount | WAY (%) | Dollars | Percent | WAY (bps) |
| **Available for sale (fair value)** | Money Market instruments | $3,732 | 0.32 | $5,713 | 0.28 | 1,981 | 53.1 | -4 |
| | U.S. Treasury Securities | 8,772 | 0.59 | 10,002 | 0.94 | 1,230 | 14.0 | 35 |
| | U.S. agency securities | 4,438 | 1.6 | 5,354 | 1.59 | 916 | 20.6 | -1 |
| | Mortgage-backed securities | 24,970 | 1.66 | 24,908 | 1.52 | (62) | (0.25) | -14 |
| | Other asset-backed securities | 1,495 | 1.23 | 2,040 | 1.07 | 545 | 36.5 | -16 |
| | **Total** | **$43,407** | **1.31** | **$48,017** | **1.24** | **4,610** | **10.6** | **-7** |
| | | | | | | | | |
| | **Mission-related** | **488** | **2.99** | **416** | **3.05** | **(72)** | **(14.8)** | **6** |
| | | | | | | | | |
| **Held to maturity (amortized cost)** | Money market instruments | 198 | 5.82 | 191 | 5.75 | (7) | (3.5) | -7 |
| | Mortgage-backed securities | 2,497 | 3.03 | 2,216 | 3.01 | (281) | (11.3) | -2 |
| | Other asset-backed securities | 252 | 2.26 | 219 | 2.38 | (33) | (13.1) | 12 |
| | **Total** | **$2,947** | **3.15** | **$2,626** | **3.16** | **(321)** | **(10.9)** | **1** |

Source: FCS Quarterly Information Statement.

WAY = weighted average yield; bps = basis points

## Loan Quality

Nonperforming assets declined from $2.497 billion (1.28 percent of total loans) on September 30, 2013, to $1.903 billion (0.91 percent of total loans) on September 30, 2014. The decline in nonperforming loans reflects improvements in the credit quality of loans (mainly real estate mortgage loans) to borrowers in certain agricultural sectors.

Favorable weather conditions for the 2014 season resulted in record-high grain and bean harvests, leading to significant reductions in crop prices. As a result, producers of livestock, dairy, poultry, and biofuels (ethanol and biodiesel), who endured high grain and oilseed prices for the past three years, should have lower costs and, therefore, higher profit margins. On the other hand, the lower crop prices will negatively affect grain and oilseed producers as their receipts decline relative to their cost of production.

The slow recovery of the general U.S. economy continues to negatively affect those producers who depend on off-farm employment to supplement their farm earnings. Furthermore, some farmers may experience additional stress as the Federal Reserve implements a less accommodative monetary policy and raises interest rates. With the decline in crop prices to near four-year lows, farmland values could also deteriorate, which would reduce equity positions for farmers and ranchers.

Net charge-offs were lower in the first nine months of 2014 than they were for the same period a year earlier. In the first nine months of 2014, the System had net charge-offs of $17 million compared with $99 million for the same period in 2013. Reflecting improvements in loan performance, the allowance for loan losses (ALL) decreased as a share of total loans and increased as a percentage of nonperforming loans and nonaccrual loans. See table 20.

**TABLE 20: FCS Loan Quality**

| Loan Quality | September 30, 2013 | September 30, 2014 |
|---|---|---|
| Total nonperforming assets as percentage of total loans | 1.28 | 0.91 |
| Nonperforming assets as percentage of capital | 5.98 | 4.15 |
| Nonaccrual loans as percentage of total loans | 0.99 | 0.68 |
| ALL as percentage of total loans | 0.64 | 0.57 |
| ALL as percentage of nonperforming loans | 55.3 | 67.1 |
| ALL as percentage of nonaccrual loans | 64.2 | 83.6 |

Source: FCS Quarterly Information Statements.
ALL = allowance for loan losses

## Liabilities, Funding, and Liquidity

For the year ended September 30, 2014, the System's overall liabilities increased by 7 percent to $225.5 billion. Short-term debt securities (due within one year) made up 35.0 percent of total Systemwide liabilities compared with 31.3 percent a year earlier. Debt securities due within one year increased by 19 percent and those due after one year increased by 1 percent. See table 21 below.

**TABLE 21: Systemwide Debt**
**(Dollars in Millions)**

| | September 30, 2013 | September 30, 2014 | Change | |
|---|---|---|---|---|
| | | | Dollars | Percent |
| Systemwide discount notes due within 1 year | $15,394 | $ 21,583 | $6,189 | 40 |
| Systemwide bonds, medium-term notes, and master notes due within 1 year | 50,695 | 57,296 | 6,601 | 13 |
| **Total short-term liabilities** | **$66,089** | **$78,879** | **$12,790** | **19** |
| Systemwide bonds, medium-term notes, and master notes due after 1 year | 134,799 | 135,473 | 674 | 1 |
| Other liabilities | 10,243 | 11,156 | 913 | 9 |
| **Total liabilities** | **$211,131** | **$225,508** | **$14,377** | **7** |

Source: FCS Quarterly Information Statements.

The System's liquidity position decreased from 202 days as of September 30, 2013, to 174 days as of September 30, 2014, but remained significantly above the regulatory minimum.[8]

The duration gap,[9] which derives from the estimated durations of assets and liabilities, is a concise and simple measure of interest rate risk inherent in the balance sheet, but it is not directly linked to expected future earnings performance. A positive duration gap (in which the duration of assets exceeds the duration of liabilities) exposes the System to rising interest rates. Conversely, a negative duration gap (in which the duration of liabilities exceeds the duration of assets) exposes the System to declining interest rates.

The duration gap for the FCS was a positive 3.2 months on September 30, 2014, compared with a positive 1.4 months a year earlier. The banks' duration gap grew in 2014 because of balance

[8] The regulatory liquidity standard requires each FCS bank to maintain a minimum of 90 days of liquidity on a continuous basis. (As a condition of its 2012 merger with U.S. AgBank, CoBank had to maintain a 130-day liquidity minimum through December 31, 2014.) The number of days of liquidity is calculated by comparing the principal portion of a given bank's maturing Systemwide debt securities, as well as its other borrowing, with the total amount of the bank's cash, cash equivalents, and investments. For the purpose of calculating liquidity, liquid assets are subject to discounts that reflect potential exposure to adverse market value changes that might be recognized upon liquidation or sale.

[9] Duration is the average maturity of cash flows, weighted by the present value of this cash flow. It is a useful way to estimate the direction and size of changes in the value of a financial instrument when market interest rates experience small changes. Here, "duration gap" is the difference between the duration of assets and the duration of liabilities, measured in months. When the duration gap is small, changing market interest rates pose less interest rate risk than when the gap is large.

sheet management strategies designed to take advantage of changing interest rates. A duration gap of a positive three months to a negative three months generally indicates a small exposure to interest rate risk. An institution's overall exposure to interest rate risk is a function not only of its duration gap but also of the financial leverage of its capital position.

## Capital

The System's total capital grew by 10 percent during FY 2014 to reach $45.8 billion. Most of the $4.1 billion increase in capital came from net income earned and retained (surplus), but increases in preferred stock, capital stock and participation certificates, additional paid-in capital, and restricted capital (Insurance Fund) also added to the total. See table 22 for changes in the capital components.

Surplus still accounts for the overwhelming majority of capital, at 82.0 percent as of September 30, 2014, compared with 83.2 percent as of September 30, 2013. While results were mixed for district banks and associations, the System's overall capital-to-assets ratio grew from 16.5 percent to 16.9 percent over this 12-month period, mostly because of relatively stable loan volume and earnings retained by System institutions.

**TABLE 22: FCS Capital Composition**
**(Dollars in Millions)**

| | September 30, 2013 | September 30, 2014 | Change | |
|---|---|---|---|---|
| | | | Dollars | Percent |
| Preferred stock | $2,378 | $2,559 | 181 | 8 |
| Capital stock and participation certificates | 1,637 | 1,667 | 30 | 2 |
| Additional paid-in capital | 738 | 1,073 | 335 | 45 |
| Restricted capital (Insurance Fund) | 3,447 | 3,684 | 207 | 6 |
| Accumulated other comprehensive income (loss) | (1,171) | (720) | (451) | 39 |
| Surplus | 34,720 | 37,553 | 2,833 | 8 |
| **Total capital** | **$41,749** | **$45,816** | **$4,067** | **10** |

Source: FCS Quarterly Information Statements.

Table 23 shows that the banks are collectively capitalized well in excess of regulatory requirements. For associations, the range of permanent capital ratios rose from 13.2 percent to 36.1 percent as of September 30, 2013, to 13.5 percent to 35.9 percent as of September 30, 2014. At September 30, 2014, all System institutions complied with FCA capital standards.

| TABLE 23: Regulatory Capital Ratios of FCS Banks | | | | | |
|---|---|---|---|---|---|
| | | **AgFirst** | **AgriBank** | **Texas** | **CoBank** |
| Permanent capital ratio | 9/30/2013 | 22.9 | 21.4 | 20.8 | 17.3 |
| | 9/30/2014 | 22.7 | 20.9 | 18.6 | 16.4 |
| | Change | (0.2) | (0.5) | (2.2) | (0.9) |
| Total surplus ratio | 9/30/2013 | 22.9 | 17.9 | 16.7 | 16.3 |
| | 9/30/2014 | 22.7 | 18.3 | 15.8 | 15.4 |
| | Change | (0.2) | 0.4 | (0.9) | (0.9) |
| Core surplus ratio | 9/30/2013 | 20.1 | 10.7 | 9.9 | 11.0 |
| | 9/30/2014 | 20.2 | 11.8 | 10.0 | 10.9 |
| | Change | 0.1 | 1.1 | 0.1 | (0.1) |
| Net collateral ratio | 9/30/2013 | 108.0 | 106.2 | 110.8 | 107.9 |
| | 9/30/2014 | 107.9 | 106.1 | 108.8 | 107.4 |
| | Change | (0.1) | (0.1) | (2.0) | (0.5) |
| Source: FCA Consolidated Reporting System. | | | | | |

# YOUNG, BEGINNING, AND SMALL FARMERS AND RANCHERS

Congress has mandated that the Farm Credit System serve the credit needs of young, beginning, and small (YBS) farmers and ranchers by directing System associations to set up YBS programs and by requiring the banks to issue annual reports on their associations' programs. To ensure that the System fulfills this responsibility, FCA issued a final rule in 2004 that

1. amended regulations to provide clear, meaningful, and results-oriented guidelines for System YBS policies and programs;

2. allows associations the flexibility to design YBS programs unique to the needs of their territories and encourages associations to establish advisory committees composed of YBS farmers;

3. requires each System association to include quantitative YBS targets and qualitative YBS goals in its operational and strategic business plan, as well as to establish internal controls over its YBS program; and

4. requires System banks and associations to include information on YBS loans and programs in their annual reports to shareholders and investors.

Our examiners review the policies and programs of the institutions to ensure that the institutions are complying with the YBS regulations.

In addition, we continue to consider regulatory options to support YBS programs. In October 2012, we issued a Bookletter to the System that provides guidance on how associations can meet the credit and related services needs of farmers who market their agricultural products through local and regional food systems. Because of their age, farming experience, or the size of their operations, many local food farmers will qualify as YBS farmers under Section 4.19 of the Farm Credit Act, as well as under FCA regulation 12 CFR 614.4165.

In November 2014, we issued an Informational Memorandum to System institutions explaining how they can increase their outreach and service to YBS farmers by coordinating with USDA Farm Service Agency loan programs. The guidance we provide helps ensure that System institutions make full use of their authorities to assist YBS farmers to begin farming, to expand their operations, or to remain in agricultural or aquaculture production.

The information that follows shows YBS results for calendar year 2013. We are currently collecting information for 2014, and we expect this information to be available after April 2015. A summary of the System's YBS program results is also available on our website at www.fca.gov.

Tables 24 and 25 provide the YBS results for calendar year 2013. Loans to YBS producers include real estate loans and short- and intermediate-term loans. Please note that information is reported separately for each of the three YBS categories because some borrowers fit into two or even all three categories. Therefore, the sum of the numbers in the categories is not an accurate measure of the System's YBS lending activity.

During calendar year 2013, the number of loans (new loans and renewals) that the Farm Credit System made to young and beginning farmers rose from 2012, while the number to small

farmers fell slightly. The number of loans to young and beginning farmers increased by 2.3 percent and 5.0 percent, respectively, but fell by 0.5 percent to small farmers.

The dollar volume of new loans to each of the three YBS categories fell in 2013 from 2012 along with the decline in the System's overall volume of new farm loans made. Loan volume to small farmers decreased the most, representing a 13.3 percent drop from 2012. The dollar volume of loans to young and beginning farmers declined more modestly. The dollar volume to young farmers fell by 6.0 percent, and the dollar volume to beginning farmers fell by 4.2 percent from 2012 to 2013. The volume of YBS loans outstanding increased for each of the three borrower categories, as it has since 2009.

The following information summarizes lending activity for the three separate YBS categories.

**Young—**At the end of 2013, the System had 175,583 loans outstanding to young farmers, totaling $23.8 billion. A "young" farmer is defined as one who is 35 years old or younger when the loan is made. During 2013, 57,854 loans, totaling $8.3 billion, were made to young farmers. These loans represented 16.3 percent of all farm loans the System made during the year and 11.0 percent of the loan dollar volume.

**Beginning—**The System had 253,272 loans outstanding to beginning farmers, totaling $37.0 billion at year-end 2013. "Beginning" farmers are those with 10 or fewer years of farming experience. During 2013, 72,662 loans, totaling $11.0 billion, were made to beginning farmers. These loans represented 20.5 percent of all farm loans made and 14.6 percent of loan dollar volume.

**Small—**At the end of 2013, FCS institutions had 484,745 loans outstanding to small farmers, totaling $44.9 billion. "Small" farmers are defined as those with annual gross sales of less than $250,000. During 2013, 142,357 loans, totaling $11.4 billion, were made to small farmers. These loans represented 40.1 percent of all farm loans made and 15.2 percent of loan dollar volume.

**TABLE 24. YBS Loans Outstanding (as of December 31, 2013)**

| Type of Farmer | Number of Loans | Percentage of Total Number of System Farm Loans | Dollar Volume of Loans in Billions | Percentage of Total Volume of System Farm Loans | Average Loan Size |
|---|---|---|---|---|---|
| Young | 175,583 | 17.8 | $23.8 | 11.2 | $135,478 |
| Beginning | 253,272 | 25.7 | $37.0 | 17.3 | $145,960 |
| Small | 484,745 | 49.3 | $44.9 | 21.1 | $92,613 |

Note: YBS data for each category are reported separately and should not be added.
Source: FCA 2013 Annual Report on the Farm Credit System.

| TABLE 25. YBS Loans Made During 2013 (as of December 31, 2013) | | | | | |
|---|---|---|---|---|---|
| **Type of Farmer** | **Number of Loans** | **Percentage of Total Number of System Farm Loans** | **Dollar Volume of Loans in Billions** | **Percentage of Total Volume of System Farm Loans** | **Average Loan Size** |
| Young | 57,854 | 16.3 | $8.3 | 11.0 | $143,360 |
| Beginning | 72,662 | 20.5 | $11.0 | 14.6 | $151,228 |
| Small | 142,357 | 40.1 | $11.4 | 15.2 | $80,310 |

Note: YBS data for each category are reported separately and should not be added.
Source: FCA 2013 Annual Report on the Farm Credit System.

To help YBS farmers qualify for credit in 2013, FCS associations offered differentiated loan underwriting standards for YBS borrowers or made exceptions to their regular standards. For example, some associations used higher loan-to-appraised-value ratios or lower debt repayment capacity standards for YBS borrowers. More than a third of associations provided concessionary loan fees, and more than half offered lower interest rate programs for YBS borrowers.

Many associations partnered with State and Federal programs to provide interest rate reductions, guarantees, or loan participations for YBS borrowers. About two-thirds of associations indicated they had used Government loan guarantee programs, primarily those of the USDA Farm Service Agency, to increase their service to YBS farmers. Using these guarantees reduces the risk associations face when lending to individuals who cannot otherwise meet underwriting standards.

In addition, FCS institutions are using various approaches and sources of information to improve their YBS performance and outreach. For example, in 2013, 41 percent of System associations used YBS advisory committees to provide input on YBS-related issues to their boards of directors.

Finally, associations employed a range of outreach measures to reach potential YBS farmers, such as sponsorship of local farmers markets and various agricultural events. They also provided training programs and services to YBS farmers, often in partnership with State or national young farmer groups or colleges of agriculture; examples include programs to build leadership and financial management skills, and special conferences geared for young, beginning, or small farmers. In addition, most FCS associations provide financial support for college scholarships or for FFA, 4-H, and other agricultural organizations.

# MARKET SHARE OF FARM DEBT

According to the U.S. Department of Agriculture's November 2014 forecast, total farm business debt will be $317.7 billion at the end of 2014, up 3.1 percent from a year earlier and up 13.9 percent since 2010. Commercial banks and the Farm Credit System are the primary suppliers of credit to farmers; other providers include life insurance companies, USDA programs, Farmer Mac, individuals, and merchants and dealers.

The System's market share of the $308.2 billion in farm business debt at the end of calendar year 2013 was 42.5 percent, up from 40.7 percent at the end of 2012.[10] The market share for commercial banks increased from 39.6 percent in 2012 to 40.1 percent in 2013. USDA estimates on the market shares of individual lender groups for year-end 2014 will not be available until August 2015.

In recent years, the System's market share has been increasing. The market share estimates for commercial banks show that their share has also increased in recent years. Historically, except for the unusual period of the 1980s and various market adjustments in the 1990s, FCS institutions have typically held the largest share of the farm real estate debt market, while commercial banks have held the largest share of non-real estate farm lending.

As the System's real estate lending grew, its share of farm business debt secured by farm real estate increased at year-end 2013 to 48.7 percent, up from 46.1 percent the previous year. Farm real estate lending by commercial banks grew at a slower pace during the year, with their share of farm real estate debt slipping from 34.1 percent to 33.9 percent. The System has had the largest market share of farm business debt secured by farm real estate since 2001.

The System experienced modest growth in non-real estate farm debt in 2013, yet its market share still rose from 33.4 percent at year-end 2012 to 33.9 percent. Commercial banks continue to lead the non-real-estate-secured farm debt market with a 48.5 percent market share at the end of 2013, up from a 47.0 percent share the previous year. Historically, commercial banks have had the greatest share of this debt segment.

[10] USDA's estimate of farm debt includes debt associated with the farming business and therefore excludes FCS lending associated with cooperatives, rural homes, rural utilities, marketing and processing operations, and other nonfarm-lending activities.

# Part IV

# PERFORMANCE BUDGET
# FY 2016

# PERFORMANCE BUDGET OVERVIEW

Our FY 2016 Performance Budget reflects our commitment to maintaining a flexible regulatory environment that meets current and future rural credit needs while ensuring the safety and soundness of the FCS. The total Performance Budget (table 26) is $69.4 million and reflects a 5.79 percent increase from FY 2015.

**TABLE 26. FCA Performance Budget, FYS 2014–2016**

| | FY 2014 Revised | FY 2015 Revised | FY 2016 Proposed |
|---|---|---|---|
| Policy and regulation | $13,787,655 | $14,433,003 | $14,968,083 |
| Safety and soundness | 48,631,895 | 49,911,992 | 52,921,209 |
| Reimbursable activities[1] | 1,480,450 | 1,255,005 | 1,510,708 |
| **Total** | **$63,900,000** | **$65,600,000**[2] | **$69,400,000** |

[1] In contrast to the reimbursement numbers in table 4, these totals include indirect costs.

[2] After the FCA Board approved the revised 2015 budget in September, Congress passed legislation capping our administrative expenses to be paid from assessments at $60.5 million. As a result of this cap, we will revise our spending in accordance with the statute.

## Policy and Regulation

Our Performance Budget includes $15.0 million for the policy and regulation program, a 3.71 percent increase from FY 2015. Most of the funds requested for policy and regulation in FY 2016 will support regulatory projects that were published in the Unified Agenda in the fall of 2014. Generally, we open about a dozen regulatory projects each year. Funds are also used to support other statutory and regulatory activities, including policy studies and market research; management of our Consolidated Reporting System; and approvals of corporate applications, System funding requests, and mission-related investment programs.

## Safety and Soundness

The Performance Budget includes $52.9 million for the safety and soundness program, a 6.03 percent increase from FY 2015. This increase is necessary because of staff increases and a reallocation of examination resources from reimbursable activities to examination activities to meet System needs.

By statute, we are required to examine each FCS institution at least once every 18 months except Farmer Mac, which we must examine at least once a year.[11] Examiners evaluate the overall condition and performance of these institutions and communicate the results to the boards of directors and management through discussions and Reports of Examination. The Financial Institution Rating System ratings are evaluated and assigned to individual institutions at least quarterly. In addition, FY 2016 budgeted monies will support development of examination guidance and systemic risk oversight of the System, including Farmer Mac.

[11] Section 5.19(a) of the Farm Credit Act requires FCA to examine Federal Land Bank Associations (FLBAs) at least once every three years; however, the two stand-alone FLBAs in the System are direct lenders and are examined at least once every 18 months.

## Reimbursable Activities

The Performance Budget includes $1,510,708 for reimbursable activities. The reimbursable activities are summarized below and include indirect costs.

- **Farm Credit System Insurance Corporation (FCSIC)—**$924,301 for administrative support services to be provided under FCSIC contract. The administrative support services in FY 2016 include support for examination, information technology, human resources, and communication and public affairs, as well as assistance in completing one premium audit.

- **National Consumer Cooperative Bank (NCB)—**$491,158 for examining NCB. FY 2016 activities involve conducting the annual safety and soundness examination and performing interim monitoring and CAMELS (capital, assets, management, earnings, liquidity, and sensitivity) assessments.

- **USDA—**$95,249 for potential work completed under contract with USDA. The work in FY 2016 will involve supporting USDA in its performance of the Business and Community Program Assessment Review and a review of the Rural Business Investment Programs.

Table 27 summarizes the costs associated with our program activities, broken down by products and services.

**TABLE 27. FY 2016 Proposed Budget and Full-Time Equivalents for Program Activities**

| | Products and Services | Budget Amount | FTEs |
|---|---|---|---|
| ***Program activity: Policy and regulation*** | | | |
| | Regulation and policy development | $13,478,360 | 51.11 |
| | Statutory and regulatory approvals | 1,489,723 | 6.98 |
| **Total for policy and regulation** | | **$14,968,083** | **58.09** |
| ***Program activity: Safety and soundness*** | | | |
| | Examination | $48,564,593 | 220.58 |
| | Economic, financial, and risk analysis | 2,790,579 | 11.36 |
| | FCS data management | 1,566,037 | 6.51 |
| **Total for safety and soundness** | | **$52,921,209** | **238.45** |
| ***Program activity: Reimbursable activities*** | | | |
| **Total for reimbursable activities** | | **$1,510,708** | **6.05** |
| **TOTAL** | | **$69,400,000** | **302.59** |

# DESIRED OUTCOMES FOR STRATEGIC GOALS

Our strategic goals and desired outcomes, which are detailed in table 28, help us measure whether we have achieved our public mission. The information that follows provides

- the strategies we use to accomplish the outcomes;
- the measures for each outcome, with targets that reflect our desired performance for FYs 2015 through 2016; and
- a historical summary of the costs of accomplishing the desired outcomes.

**TABLE 28. Desired Outcomes for Strategic Goals**

| Strategic Goal | Desired Outcome |
|---|---|
| 1. Ensure that the FCS and Farmer Mac fulfill their public mission for agriculture and rural areas. | A regulatory environment that provides for fulfilling the public missions of the System and Farmer Mac. |
| 2. Evaluate risk and provide timely and proactive oversight to ensure the safety and soundness of the FCS and Farmer Mac. | Effective risk identification and timely corrective action |

**Policy and Regulation—**We established the Policy and Regulation program to track the product and service costs of achieving a flexible regulatory environment. The products and services we provide to support this program are

- regulation and policy development, and
- statutory and regulatory approvals.

**Safety and Soundness—**We established the Safety and Soundness program to track the product and service costs of identifying risk and taking timely corrective action. The products and services we provide to support this program are

- examination;
- economic, financial, and risk analysis; and
- FCS data management.

## Flexible Regulatory Environment

### *Strategies*

For goal 1, we are using the following strategies to achieve a flexible regulatory environment that enables the System and Farmer Mac to fulfill their public missions.

1. Develop regulatory capital rules within the FCA's regulatory framework for the System and Farmer Mac that are clearly defined, easily understood, and consistent with industry standards.

2. Within the framework of the Farm Credit Act, continuously update policies and regulations to provide an operating environment for the System and Farmer Mac that meets the changing needs of agriculture and rural America.

3. Emphasize the public purpose and mission-related responsibilities of the agricultural GSEs to serve all of agriculture and rural America, including the use of innovative programs for serving the credit and related service needs of young, beginning, and small (YBS) farmers, ranchers, and producers or harvesters of aquatic products.

4. Encourage System institutions to evaluate their YBS programs to ensure that the programs also meet the credit and financial service needs of producers seeking to enter urban agriculture, to produce local foods, or to use direct-to-consumer marketing channels.

5. Encourage the System and Farmer Mac to find and develop both public and private partnerships and alliances with other financial service providers to address the changes in agriculture through new and existing programs.

6. Promote System business practices, including outreach activities to all creditworthy eligible potential customers, emphasizing minority and socially disadvantaged farmers and ranchers and minority-owned entities.

7. Promote public trust in FCA's regulatory framework for the System and Farmer Mac by developing policy guidance that supports mission achievement, financial stability, and transparency.

8. Consistent with cooperative principles and the Farm Credit Act, enable the agricultural GSEs to structure themselves to best serve their customers and rural America.

9. Encourage full participation of stakeholders in the development and review of regulatory proposals as appropriate.

### *Measuring the Achievements*

Table 29 summarizes the results of our efforts to maintain a flexible regulatory environment for the FCS and Farmer Mac. We achieved or exceeded the goals we identified for FY 2014.

**TABLE 29. Flexible Regulatory Environment—Performance Measures and Achievements**

| Measure | FY 2014 (Actual) | | FYs 2015–2016 |
|---|---|---|---|
| | Target | Result | Target |
| 1. Percentage of FCS institutions with satisfactory operating and strategic plans for providing products and services to all creditworthy and eligible persons. | ≥90% | 99% | ≥90% |
| 2. Whether Farmer Mac's business plan contains strategies to promote and encourage the inclusion of all qualified loans, including loans to small farms and family farmers, in its secondary market programs, and whether its business activities further its mission to provide a source of long-term credit and liquidity for qualifying loans. | Yes | Yes | Yes |
| 3. Percentage of direct-lender institutions with satisfactory consumer and borrower rights compliance. | ≥90% | 99% | ≥90% |
| 4. Percentage of direct-lender institutions with YBS programs that are in compliance with the YBS regulations. | ≥90% | 100% | ≥90% |
| 5. Whether institutions meet the objectives of our mission-related regulations and whether institutions have made observable progress in meeting the objectives of any new mission-related regulations that have been in effect for at least one year. | Yes | Yes | Yes |
| 6. Whether FCA reached out to nontraditional commenters to request input on GSE mission-related rulemaking actions. | Yes | Yes* | Yes |

* We did not approve any proposed rules during the reporting period that were related to GSE mission.

### *Budgets*

Table 30 provides the budgeted amounts we need to achieve a flexible regulatory environment from FYs 2014 to 2016.

**TABLE 30. Budgets to Achieve a Flexible Regulatory Environment**

| | FY 2014 Revised | FY 2015 Revised | FY 2016 Proposed |
|---|---|---|---|
| Regulation and policy development | $12,388,208 | $12,991,536 | $13,478,360 |
| Statutory and regulatory approvals | 1,399,447 | 1,441,467 | 1,489,723 |
| **Total** | **$13,787,655** | **$14,433,003** | **$14,968,083** |

Note: We expect our budget to achieve a flexible regulatory environment will increase in FY 2016 because of staff seniority, additional hiring, salary and benefit increases, training, information technology costs, and our regulatory initiatives.

## Effective Risk Identification and Timely Corrective Action

### *Strategies*

For goal 2, we are using the following strategies to achieve effective risk identification and timely corrective action.

1. Ensure that staff provides prompt and comprehensive information to the FCA Board and remains flexible and responsive to the Board's priorities so that the Board will be better able to make fully informed, arm's-length decisions.

2. Recruit and retain a diverse and highly skilled workforce to meet FCA's current and future risk analysis, examination, and oversight needs.

3. Continue proactive oversight of institution-specific and systemic risks.

4. Promote a vibrant program of Systemwide risk supervision that uses stress testing, research, and analysis to identify emerging systemic risks, and provides proactive examination direction and policy guidance for use internally and externally.

5. Use Agency supervisory and enforcement authorities effectively to remediate weakened institutions.

6. Promote the continued importance and improvement in the quality of System loan data for use by both the Agency and the System in risk management and business planning.
7. Develop regulatory guidance and examination procedures that keep pace with evolving strategies and new programs in meeting the changing needs of agriculture and rural America.

8. Continue to integrate standards of conduct rules and codes of ethical behavior into the organizational culture that are consistent with Government ethics guidelines, universally understood, and consistently applied.

### *Measuring the Achievements*

Table 31 provides the results of our examinations and oversight efforts to effectively identify risk and take timely corrective action. We met or exceeded our goals as of the end of FY 2014 (September 30, 2014).

**TABLE 31. Effective Risk Identification and Timely Corrective Action—Performance Measures and Achievements**

| Measure | FY 2014 (Actual) | | FYs 2015–2016 |
|---|---|---|---|
| | Target | Result | Target |
| 1. Percentage of System assets in institutions with composite CAMELS ratings of 1 or 2. | ≥90% | 99% | ≥90% |
| 2. Percentage of requirements in supervisory agreements with which FCS institutions have at least substantially complied within 18 months of execution of the agreements. | ≥ 80% | 91% | ≥ 80% |
| 3. Percentage of institutions complying with regulatory capital ratio requirements (permanent capital ratio, total surplus ratio, core surplus ratio, and net collateral ratio). | ≥90% | 100% | ≥90% |
| 4. Whether the Office of Secondary Market Oversight's examination and oversight plan and activities effectively identify emerging risks, and whether appropriate supervisory and corrective actions have been taken to effect change when needed. | Yes | Yes | Yes |
| 5. Percentage of institutions with satisfactory audit and review programs, including institutions with acceptable corrective action plans. | 100% | 100% | 100% |
| 6. Percentage of FCS institutions providing FCA with consolidated loan data. (Target for 2014: ≥90 percent; target for 2015: 100 percent) | ≥90% | 100% | ≥100% |

### *Budgets*

Table 32 provides the budgeted amounts we need to identify risk in the FCS and to take timely corrective action from FYs 2014 to 2016.

**TABLE 32. Budgets to Identify Risk and Take Timely Corrective Action**

| | FY 2014 Revised | FY 2015 Revised | FY 2016 Proposed |
|---|---|---|---|
| Examination | $45,323,175 | $45,740,951 | $48,564,593 |
| Economic, financial, and risk analysis | 1,932,582 | 2,658,738 | 2,790,579 |
| FCS data management | 1,376,138 | 1,512,303 | 1,566,037 |
| **Total** | **$48,631,895** | **$49,911,992** | **$52,921,209** |

Note: FCA's budget to identify risk and take timely corrective action is projected to increase in FY 2016 because of additional hiring, salary and benefit increases, training, and information technology costs.

# PERFORMANCE MEASUREMENT AND REPORTING

Our performance measurement system evaluates our progress in achieving the goals of our Strategic Plan for FYs 2013 to 2018. We provide a balanced view of our overall performance, taking into account the inputs used, the products and services produced, and the achievement of desired outcomes. As we have shown in this report, the Agency-level measures are linked to our strategic goals.

Our Chief Executive Officer, with assistance from our Chief Operating Officer and designated office directors, is responsible for measuring performance by collecting and analyzing performance data. The Chief Executive Officer monitors the Agency's progress and results relative to the Agency-level measures on a quarterly basis throughout each fiscal year. Periodic performance reports are provided to the FCA Board. The year-end performance report is incorporated in the FCA Performance and Accountability Report, which is submitted to the President and Congress.

Copies are available from
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