

OFFICE OF
INSPECTOR GENERAL

SURVEY REPORT

Survey of
Farm Credit System
Institutions Regarding the
Agency's Examination Function

First Quarter Fiscal Year 2018
(October 1, 2017 -
December 31, 2017)

Issued April 10, 2018



FARM CREDIT ADMINISTRATION



Executive Summary

Survey of Farm Credit System Institutions Regarding the Agency's Examination Function Fiscal Year 2018 First Quarter Summary Report (October 1 – December 31, 2017)

The FCS institutions asked to respond to the survey are those institutions that:

1. Received a Report of Examination during the FY quarter; or
2. Had significant examination activity and interface with OE during the same period.

The survey asks respondents to rate eight survey statements as:

- | | |
|-------------------------------|---|
| Completely Agree | 1 |
| Agree | 2 |
| Neither Agree
nor Disagree | 3 |
| Disagree | 4 |
| Completely Disagree | 5 |
| Does Not Apply | 6 |

Each fiscal year (FY) quarter the Office of Examination (OE) identifies several Farm Credit System (FCS) institutions that were in a position to provide meaningful survey responses for that period. The OE identified nine FCS institutions to survey for the period October 1 – December 31, 2017. The Office of Inspector General (OIG) sent surveys to those institutions in February 2018. Eight of the nine institutions completed the survey (an 89% response rate). The OIG did not receive any responses from prior quarters for this report.

For the first quarter of FY 2018, average numerical ratings ranged from 1.5 to 2.6 (with "1" reflecting a positive rating and "5" reflecting a negative rating). The total average numerical rating for all survey statements was 1.9. For comparison, we provide data from the prior three quarters below.

FY Quarter	Average Numerical Rating Range	Total Average Numerical Rating
1 st Quarter FY 2018	1.5 – 2.6	1.9
4 th Quarter FY 2017	1.6 – 2.4	2.1
3 rd Quarter FY 2017	1.4 – 2.2	1.8
2 nd Quarter FY 2017	1.5 – 2.0	1.7

Consistent with prior quarters' responses, we received more positive than negative comments about the examiners and the examination process.

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ACRONYMS

FCA	Farm Credit Administration
FCS	Farm Credit System
FY	Fiscal Year
OE	Office of Examination
OIG	Office of Inspector General

BACKGROUND AND METHODOLOGY

Each fiscal year (FY) quarter the Office of Examination (OE) identifies several Farm Credit System (FCS) institutions that were in a position to provide meaningful survey responses for that period. The criteria for including an FCS institution in the survey are:

1. The institution received a Report of Examination during the FY quarter; or
2. There was significant examination activity and interface with an institution during the same period.

The Office of Inspector General (OIG) provides a survey report for FY quarters ending December 31, March 31, June 30, and September 30. The fourth quarter report includes FY summary data.

When outstanding responses from prior quarters are received, they are included in the next quarterly report.

The survey asks respondents to rate eight survey statements from "1" (Completely Agree) to "5" (Completely Disagree), or "6" if the statement does not apply. The rating choices are:

Completely Agree	1
Agree	2
Neither Agree nor Disagree	3
Disagree	4
Completely Disagree	5
Does Not Apply*	6

*We do not include ratings of “6” in rating averages because a “6” will skew the numerical average negatively even though the statement is not applicable to the institution.

We provide the current FY quarter’s average numerical rating for survey statements 1-8 and, for comparison, the prior two FYs’ data.

Survey statements 1-4 pertain to the examination process and statements 5-8 pertain to communications during the examination. Statements 9-11 are general questions about the overall process. Respondents may submit comments for each of the 11 survey statements.

Narrative responses are provided verbatim, except any identifying information has been removed and grammatical, punctuation, and spelling errors are usually corrected. Any bracketed text is for the purpose of removing information that identifies an institution or an examiner or providing clarification to a response. Perceived negative comments of any degree are color coded in red.

At the end of the survey we ask whether the respondent would like the OIG to contact the institution confidentially to discuss the submitted responses.

SURVEY RESULTS

EXAMINATION PROCESS

Statement #1

The scope of examination activities was focused on areas of risk to the institution and appropriate for the size, complexity, and risk profile of the institution.

Average Numerical Ratings by FY Quarter

FY	First Quarter	Second Quarter	Third Quarter	Fourth Quarter	FY Average
FY 2018	1.8				1.8
FY 2017	1.8	1.6	1.8	2.1	1.8
FY 2016	1.6	1.8	1.9	1.7	1.8

Comments:

- The audit took place 90 days after our merger date. As such much of the work predated the merger with differences in past practices between the three predecessors. The exam team was thoughtful about looking back to the predecessor policies and approaches rather than applying one set of new policies to all past activities.
- The scope of the examination was appropriate. All areas were covered during the exam and were aligned with the risk and size of the institution.
- The board continues to consider it very important for FCA to recognize the size, complexity, and risk profile of the institution when scoping and conducting examinations. **The avoidance of unnecessary and costly administrative activities is a critical issue especially for smaller institutions.**

Statement #2

Examiners appropriately applied laws, regulations, and other regulatory criteria to examination findings and conclusions.

Average Numerical Ratings by FY Quarter

FY	First Quarter	Second Quarter	Third Quarter	Fourth Quarter	FY Average
FY 2018	1.8				1.8
FY 2017	1.8	1.7	1.8	2.1	1.9
FY 2016	1.9	1.8	2.1	1.8	1.9

Comments:

- Appropriate recognition of the practical implementation of regulations.
- The examiners cited specific regulations to support their findings. They were willing to discuss issues with management before reaching a conclusion.

Statement #3

The recommendations, required actions, and any supervisory agreement with FCA assisted the board and management in addressing the risks of the institution.

Average Numerical Ratings by FY Quarter

FY	First Quarter	Second Quarter	Third Quarter	Fourth Quarter	FY Average
FY 2018	2.6				2.6
FY 2017	1.8	1.8	2.2	2.4	2.1
FY 2016	2.1	2.2	2.1	2.0	2.1

Of note, two institutions rated this survey statement a "5" (Completely Disagree).

Comments:

- The institution was required to provide a complete list of stockholders (including stockholders whose loans are classified substandard and nonaccrual) to the nominating committee for consideration of board candidates. If members whose loans are classed substandard and nonaccrual are recommended by the nominating committee, they are immediately disqualified per institution bylaws. This requirement exposes the institution to unnecessary risk and possible liability.
- Our EIC and Senior Examiner had a preliminary close out call with Management and Board Chair/Audit Chair. During the call, FCA asked our two board members to verbally commit to correcting recommended and required actions during the phone call. This attempt to circumvent management and the rest of the board was not received well and put a "black eye" on an otherwise good review. FCA also needs to give a formal expectation of a required action vs. a recommended action.
- Recommendations and required actions adequately addressed risk and were implemented by the institution.

Statement #4

The examiners were professional and efficiently conducted examination activities.

Average Numerical Ratings by FY Quarter

FY	First Quarter	Second Quarter	Third Quarter	Fourth Quarter	FY Average
FY 2018	1.5				1.5
FY 2017	1.8	1.5	1.4	1.6	1.6
FY 2016	1.5	1.5	1.8	1.3	1.5

Comments:

- Good coordination of the requested information and the lead time necessary to gather the documentation.
- Some challenges initially, but the EIC was out sick. Once the EIC returned the challenges were rectified. Some of the younger examiners lack perspective and wisdom.
- Exam as a whole took too long.
- The examiners were professional in their interaction with the board, management and staff. They made every effort to conduct their examination with minimal disruption to employees.

COMMUNICATIONS

Statement #5

Communications between the Office of Examination staff and the institution were clear, accurate, and timely.

Average Numerical Ratings by FY Quarter

FY	First Quarter	Second Quarter	Third Quarter	Fourth Quarter	FY Average
FY 2018	1.8				1.8
FY 2017	1.6	1.5	1.7	2.0	1.7
FY 2016	1.8	1.7	1.8	1.6	1.7

Comments:

- We have no complaints with communication between assigned examination staff and the institution. We did however provide written communication directly to OE and ORP related to our concerns about the nominating committee issue mentioned in [survey statement #3]. To date, over three months later, we have not received a reply. In fact, we have not even received an acknowledgment of our correspondence or concern.
- The exam was in person, but the examiners didn't ask specific questions until they were gone. We wonder why they came to the office in the first place?
- The examination team communicated effectively with all staff. They were clear about objectives prior to the exam and the exit conference covered all findings prior to issuing the report.

Statement #6

Examination communications included the appropriate amount and type of information to help the board and audit committee fulfill their oversight responsibilities.

Average Numerical Ratings by FY Quarter

FY	First Quarter	Second Quarter	Third Quarter	Fourth Quarter	FY Average
FY 2018	1.8				1.8
FY 2017	1.8	1.6	1.7	2.1	1.8
FY 2016	1.7	1.7	1.6	1.6	1.7

Comments:

- The report back was at an appropriate level providing a summary view and not getting into detail.
- **We have confusion between recommended and required actions.**
- All relevant items were communicated to the board. All suggestions and recommendations from the team were discussed.

Statement #7

Examiners fairly considered the views and responses of the board and management in formulating conclusions and recommendations.

Average Numerical Ratings by FY Quarter

FY	First Quarter	Second Quarter	Third Quarter	Fourth Quarter	FY Average
FY 2018	1.9				1.9
FY 2017	1.6	1.8	2.1	2.1	1.9
FY 2016	1.9	1.8	1.9	1.8	1.9

Comments:

- **The institution was required to provide a complete list of stockholders (including stockholders whose loans are classified substandard and nonaccrual) to the nominating committee for consideration of board candidates. If members whose loans are classed substandard and nonaccrual are recommended by the nominating committee, they are immediately disqualified per institution bylaws. This requirement exposes the institution to unnecessary risk and possible liability. [same response to survey statement #3]**
- The examiners allowed us to extend our final response 30 days to allow plenty of time for management and the board to deliberate.
- The examiners discussed all issues before reaching a conclusion. They were open to explanation and discussion.

Statement #8

FCS-wide guidance from the Office of Examination was proactive and helpful.

Average Numerical Ratings by FY Quarter

FY	First Quarter	Second Quarter	Third Quarter	Fourth Quarter	FY Average
FY 2018	1.9				1.9
FY 2017	2.0	2.0	1.9	2.3	2.1
FY 2016	1.7	2.2	2.2	1.8	2.0

Comments:

- By their nature these are very general but it is helpful to know of the areas of focus.
- Our EIC gave examples of similar actions in other institutions and we also can utilize the FCA exam manual.
- Every effort was made to understand the institution's processes and incorporate these within system guidance.

GENERAL QUESTIONS

Statement #9

What aspect of the examination process did you find most beneficial?

- Validation of risk identifications was timely given our stress testing submission to FCA to fulfill a condition of merger.
- Allows us another opinion of our risk management.
- Suggestions regarding system access and controls were helpful in addressing potential risk.
- Our EIC was professional and proactive with communications.
- The progress and exit meeting discussions.

Statement #10

What aspect of the examination process did you find least beneficial?

- Length of time to complete the exam process.
- Off site loan reviews.
- No areas showed weakness.

Statement #11

Please provide any comments from the Board as a whole regarding the examination process not provided in the preceding responses.

- Very professional.
- FCA needs to realize that institutions have a Senior Management team that is delegated authority from the Board to operate in a safe and sound manner. Too many times FCA examiners tried to circumvent management by going to either the Audit Committee Chair or Board Chair to get a response or a commitment to address an issue. Our Board does not want to micromanage our Senior Management team, and this year it appears as FCA tried to steer us that way.
- The report was reviewed in detail with the board. Discussions were held in general session as well as with the board in executive session. The examiners were open to discussion and were receptive to the views of the board.
- The exam presentation to the board was clear and effective, and the exam process went smoothly.
- The process was transparent and open.

Request for OIG Contact

Would you like the Office of Inspector General to contact you confidentially to discuss your survey responses and/or the examination?

This quarter no institution indicated they would like a call from the OIG.

**FARM CREDIT ADMINISTRATION
OFFICE OF INSPECTOR GENERAL**



REPORT

Fraud | Waste | Abuse | Mismanagement

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