

**First Quarter Fiscal Year (FY) 2013 Summary Report
(October 1 – December 31, 2012)**

**Office of Inspector General's (OIG) Survey of Farm Credit System (FCS) Institutions
Regarding the Agency's Examination Function**

Introduction

During the period October 1 – December 31, 2012, the Office of Examination (OE) identified 12 FCS institutions that were in a position to provide meaningful survey responses.

The OIG sent surveys to those 12 institutions on January 28. Of the 12 institutions surveyed, 11 submitted completed surveys. If the outstanding response is received, it will be included in the next quarterly report.

The OIG will continue to provide an email report to you based on each FY quarter-end, i.e., December 31, March 31, June 30, and September 30, so that you may timely take whatever action you deem necessary to address the responses. The fourth quarter report as of September 30 will continue to include FY summary data.

The survey asks respondents to rate the eight survey statements from "1" (Completely Agree) to "5" (Completely Disagree). The rating options are as follows:

Completely Agree	1
Agree	2
Neither Agree nor Disagree	3
Disagree	4
Completely Disagree	5

There is also an available response of "6" (Does Not Apply) for each survey statement. These responses are not included in averages.

Narrative responses are provided verbatim, except that any identifying information has been removed and any grammatical or punctuation errors may have been corrected. Any narrative in "brackets" is explanatory information provided by the OIG based on conversations with institution management. This quarter, there were no conversations held with institution management.

Survey Result – First Quarter FY 2013

Average numerical responses to survey statements 1 - 8 ranged from 1.5 to 2.6.

The average response for all survey statements was 1.9.

In this quarter, there were more positive than negative narrative comments to survey statements 1 - 8. (Negative comments of any degree are color coded in **maroon**.)

Survey item 9 asks for feedback on the most beneficial aspect of the examination process. Consistent with prior quarters' responses to this survey item, many very positive comments were provided about the examiners and the examination process.

Survey item 10 asks for feedback on the least beneficial aspect of the examination process. While most were negative, as would be expected, several comments provide a perspective that should prove constructive.

Survey item 11 asks for any additional comments from the Board as a whole. This is a new survey item inserted at the request of OE. It elicited a number of thoughtful responses from full Boards, which was the objective of the question.

Responses to Survey Statements 1–8

Examination Process

Survey 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 Response: 2.0

Comments:

- The 2012 examinations included some of our higher risk areas such as the Capital Markets Group and newer regions through mergers.
- Focus areas have changed appropriately with the growth of our institution and changes in risk profile.

Survey Statement 2: Examiners appropriately applied laws, regulations, and other regulatory criteria to examination findings and conclusions.

Average Response: 1.9

Comments:

- Using "safety and soundness" to force system institutions to set a FLCA loan to value requirement of 75% or less stretches the regulations and sets a dangerous precedent, allowing the Agency to put in place de facto changes to regulations without going through the process for amending regulations. Our board and management are concerned more with this precedent than with the loan to value requirement itself.

Survey 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 Response: 2.0

Comments:

- Comments by examiners regarding commodity classifications/SIC codes/etc., were helpful.
- While the recommendations and required actions were minimal, the board/management welcomes recommendations that will strengthen our operations.
- The recommendations will be considered and utilized where appropriate.
- Recommendations are generally sound and appropriate.
- **The one required action really had no bearing on risk. Recommendations were questionably useful.**

Survey Statement 4: The examiners were professional and efficiently conducted examination activities.

Average Response: 1.5

Comments:

- **Seemed just a little slow with results.**
- The examiners generally kept the Management team informed of the examination status throughout the year.
- Examination staff was excellent.

Communications

Survey Statement 5: Communications between the Office of Examination staff and the institution were clear, accurate, and timely.

Average Response: 1.9

Comments:

- **Additional clarity regarding FCA's expectations regarding annual report director bio's would be appreciated.**
- Clarity of communications was good, **timeliness was not always so good.**

Survey Statement 6: Examination communications included the appropriate amount and type of information to help the board and audit committee fulfill their oversight responsibilities.

Average Response: 1.7

Comments:

- Outstanding communication with audit chairman and audit committee.
- The chair of the audit committee agrees with this statement.
- Communications were clear and appropriate.
- Rationale supporting requirements and recommendations was generally helpful and appropriate, although in some cases potential risk exposures associated with findings appear to be over-stated, presumably to add weight to the findings. The institution would be better served with accurate risk assessments as over-reaction to relatively minor issues can effectively increase risk.

Survey Statement 7: Examiners fairly considered the views and responses of the board and management in formulating conclusions and recommendations.

Average Response: 1.8

Comments:

- Findings were discussed professionally and examiners were always willing to receive comments.

Survey Statement 8: FCS-wide guidance from the Office of Examination was proactive and helpful.

Average Response: 2.6

Comments:

- The Collateral Risk module refers to “raw land” meaning “land to be developed” without once explaining that it doesn’t refer to “crop land” or “pasture land.” This should be corrected.
- Say on pay regs were inappropriate for Farm Credit institutions as currently structured and governed.
- Communications dealing with technical issues (i.e., application of regulations or law) are generally adequate. There appears to be a growing tendency to regulate via booklet or other guidance versus through the regulatory process. This practice, sometimes characterized as “proactive,” may increase the risk of ill-conceived regulation and confusion among institutions.
- Information was useful in understanding FCA’s expectations.

General Questions 9, 10, and 11

Survey Item 9: What aspect of the examination process did you find **most** beneficial?

- The EIC was helpful in guidance.
- Exit interview with staff, board chair, and audit chair.
- Transition to a competent new EIC has gone well. We appreciate the sharing of best practices to improve management of the institution.
- Overall results appear to validate that the institution is operating in a safe and sound manner.
- Actual credit review and credit admin review.
- Our institution most benefited from interaction by our senior staff with the senior examiners. Each provided valuable insights and advice based on their years of experience in the system. Assistance in understanding the Collateral Risk module and its reporting requirements may have been the single most valuable aspect.
- Open and frequent communications with examination leadership is very beneficial.
- The interaction with the examiners was the most beneficial aspect.
- Clear communications including IMs from FCA related to regulation interpretation is very helpful.
- Having a third party evaluation of conditions and practices.

Survey Item 10: What aspect of the examination process did you find **least** beneficial?

- The exam isn't the problem – it's the heavy regulatory burden on time and resources that is least beneficial for a small institution.
- As in the past, while we are happy to provide space in our facility to bring "new examiners" into our institution for training purposes, it appears that many if not all 2012 examinations were for training.
- The physical security review – it was unnecessary and out of FCA's scope of responsibility.
- Our exam team included a number of trainees. While we recognize that training is as necessary for the Agency as it is for our institution, our staff spent a good deal of time responding to questions that more experienced staff would not have asked.
- In this case, the presentation of the Report of Examination to the board was not useful. The absence of critical findings did not make a formal presentation necessary.

Survey Item 11: Please provide any comments from the **Board as a whole** regarding the examination process not provided in the preceding responses.

- Felt good about the openness and honesty from the staff of FCA, have not always felt that way.
- The board found the examiners and process helpful and informative.

- The board as a whole takes the examinations seriously and sees the benefits of having such examinations. Any recommendations resulting from such examinations are considered and welcomed if they help to improve our operations and strengthens our internal controls.
- As a whole, the exam was very fair.
- To our knowledge and as we observed, the exam team conducted themselves in a professional manner while fulfilling their obligation to the institution and the system for oversight during the exam, in their report, and during their presentation to the board.
- The process was well received and helpful.
- FCA has expressed concern that some institutions' boards need to be better engaged. While we agree that board engagement is necessary, we have observed instances in which boards are being driven to a depth of detail that goes well beyond governance and into management. While well-intentioned, this could have some very unfavorable consequences. Institutions need strong governance and effective professional management. Blurring the two could compromise both the effectiveness of governance and management.
- The Audit Committee and the board as a whole will use the required/recommended actions to strengthen our institution's operations.
- Additional clarity regarding FCA's expectations regarding annual report director bio's would be appreciated.
- The Board of Directors was satisfied with the process.