

**Third Quarter Fiscal Year 2009
(April 1 – June 30, 2009)**

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

Introduction

Based on the interface FCS institutions had with the Agency's examination function during the period April 1 – June 30, 2009, the Office of Examination identified 15 FCS institutions that were in a position to provide meaningful survey responses.

The OIG sent surveys to those 15 institutions on July 28, 2009. A follow-up e-mail was sent to nonresponding institutions on August 31. Of the 15 institutions surveyed, 14 submitted completed surveys. If the nonresponding institution subsequently sends a completed survey, it will be included in the next quarterly report.

One response to the survey issued for the second quarter of FY 2009 was received subsequent to the second quarter report and is included in this report. As a result, this report covers 15 responding institutions.

The OIG will continue to provide an e-mail report to you based on each fiscal year 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 fiscal year summary data.

The survey asks respondents to rate the 9 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.

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 communication with the institution.

Survey Results – 3rd Quarter FY 2009

The average numerical responses to survey statements 1 - 9 ranged from 1.8 to 2.1.

Average Numerical Responses to Survey Statements 1 – 9		
3rd Qtr	2nd Qtr	1st Qtr
1.8 – 2.1	1.7 – 2.1	1.6 – 2.2

The average response for all survey statements was 1.9.

Average Response for all Survey Statements		
3rd Qtr	2nd Qtr	1st Qtr
1.9	1.9	2.0

The majority of narrative comments to survey statements 1 - 9 were positive. However, there were a number of negative comments that should provide opportunities for you to refine examination methodology and communications, and examiner training. **These are color coded in red.**

Survey item 10a asks for feedback on the most beneficial aspects of the examination process. Consistent with prior quarters’ survey responses to this survey item, many very positive comments were provided about the examiners and the examination process.

Survey item 10b asks for feedback on the least beneficial aspects of the examination process. Many of these comments should also provide opportunities for you to refine examination methodology and communications, and examiner training.

Survey item 11 asks for any other comments. There were several positive comments, but also a few negative comments.

Responses to Survey Statements 1–9

Examination Process

Survey Statement 1: The scope and frequency of examination activities focused on areas of risk to the institution and were appropriate for the size, complexity, and risk profile of the institution.

Average Response: 1.8 (2nd quarter was 1.8, 1st quarter was 2.0)

Comments:

- The recent FCA exam focused on the appropriate risk areas considering the size and complexity of our institution.

- A targeted and risk based approach is evident and appropriate. **Could even be more effective if exam activities were based on more forward looking risks and issues.**
- **Scope of sampling for loan portfolio was not a random sampling (skewed for selection of troubled loans);** however, the results were projected over the entire loan portfolio.
- **The focus of our exam was on our Scorecard program. Loans in this program comprise less than 10% of our outstanding volume and our history with the smaller card has been excellent. Concerns were raised with the larger scorecard, but our use of that program has been extremely limited. As credit stress is becoming more prominent, a risk based scope may have been more appropriate.**

Survey Statement 2: The examination process helped the institution understand its authorities and comply with laws and regulations.

Average Response: 1.9 (2nd quarter was 2.0, 1st quarter was 2.2)

Comments:

- Exam activities and recommendation provided insight and understanding of compliance issues and institution authority.
- A few items were appropriately brought to our attention that we were not in compliance with. This guidance has proven helpful and was appreciated.

Survey Statement 3: The results and recommendations of the examination process covered matters of safety and soundness, and compliance with laws and regulations.

Average Response: 1.8 (2nd quarter was 1.8, 1st quarter was 2.0)

Comments:

- Results and recommendations from the recent FCA exam focused on the safety and soundness of the institution.
- The Board appreciates the Executive Session with Exam Team leaders and the discussion this time recognizing a movement from a growth centric environment to a capital centric focus.
- The required action was in accordance with compliance with regulation. The recommendations ranged from compliance with regs to suggestions on how to mitigate or monitor risks and were primarily related to Scorecard loans.

Survey Statement 4: Examiners were knowledgeable and appropriately applied laws, regulations, and other regulatory criteria.

Average Response: 2.1 (2nd quarter was 2.1, 1st quarter was 1.9)

Comments:

- Most had preconceived opinions of individual asset quality based on the overall industry stress, i.e., biofuels, pork, dairy.
- The examination team seemed to be very knowledgeable and experienced in laws, regulation and other regulatory issues.
- Most of the examination staff possessed limited experience and knowledge (were in training). Proper application of laws, regulations, etc., occurred due to EIC experience/knowledge.
- Lead examiners were knowledgeable. Appears that scope and eligibility was interpreted narrowly.
- This is a difficult area to rate. The regs were appropriately applied as written. However, the exam team was not well tenured and we feel that this led to conclusions by the team that were not necessarily proven in fact, but rather by their interpretation. This may have skewed the importance level attached to certain recommendations.

Communications and Professionalism

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

Average Response: 1.9 (2nd quarter was 1.8, 1st quarter was 1.6)

Comments:

- Communications with management during and after the exam were timely, clear and accurate.
- The Exam team and Leaders do a very good job in communicating up front, staying in touch during the review including assuring they have all the information on areas examined and discuss observations with institution leadership before the final report is issued. They have also handled themselves with a high degree of professionalism in their interactions with staff and the Board.
- Some delay in scope communication, however, the agency had interim booklet advisement during the review.
- Timeliness was the main concern as the audit began on site the week of January 26th and our report was issued electronically on May 18th.

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: 2.1 (2nd quarter was 1.7, 1st quarter was 1.9)

Comments:

- Communications to the board and audit committee were informative and provided the appropriate information to fulfill oversight responsibilities.
- Many of the recommendations cited were related to lack of documentation and plans were already in place to address the issues cited in most instances.
- The report was written in enough detail to give guidance and the verbal presentation allowed for further explanation.

Survey Statement 7: The examiners were organized and efficiently conducted examination activities.

Average Response: 1.9 (2nd quarter was 2.0, 1st quarter was 2.1)

Comments:

- Arrangements were such that the audit committee chair was not able to participate in the exit conference call.
- The exam was organized and conducted very effectively.
- Good here.
- Efficiency is somewhat compromised by the manner in which examinations are conducted. After the exam team leaves the site there still remains the need to communicate on unfinished items. We understand that examiners have duties involving multiple institutions as well. Unfortunately, future communications generally require a bit of time to “get back up to speed on” the issues at hand for both parties. We also believe the experience level of the exam team led to some inefficiency in our audit. This is understood given the tenure level and only time will help.

Survey Statement 8: Examiners fairly considered the views and responses of the board and management in formulating conclusions and recommendations.

Average Response: 1.9 (2nd quarter was 1.9, 1st quarter was 1.9)

Comments:

- Saw little opportunity for discussion or debate. Reminiscent of the old Capital Corporation days.
- Examiners listen and engaged in discussion with board and management before any conclusions or recommendations were considered.

- The exam team asked for responses to the findings and incorporated them into their final work product.
- Board and management have no authority to overrule conclusions and recommendations.
- EIC considered our input and gave us credit for actions taken.
- For most part-yes. The narrow interpretation of the other needs appears to create a challenge for the FCS to maintain a sound image with the most progressive operations that are focused on diversification in their business model.
- Agree for management. Don't agree for board.
- There were a few items noted in our review where we feel that our views were not considered. An example would be the Scorecard recommendations. We do not utilize the score as the only determinant of approval. We actually complete a significant amount of additional analysis to complement the score. We do not believe much consideration was given to our supporting argument in this instance.

Survey Statement 9: FCS-wide examination guidance from the Office of Examination (e.g., examination bulletins, informational memoranda, etc.) was timely, proactive and helpful.

Average Response: 2.0 (2nd quarter was 2.0, 1st quarter was 2.2)

Comments:

- FCA communications are generally very timely and helpful.
- It seems that there have been more Bookletters lately. The only area of feedback we'd have here is that it does not always seem that FCA is consistent in their approach to the examination of shared credits. They are looked at in several places across the System and there is not a consistency in the Agency's approach in loan classification, accounting status, and allowances.
- The IM's are very timely and provide adequate guidance with consideration to the size and complexity of each institution.

Responses to Additional Survey Items 10a, 10b, and 11

Survey Item 10a: What aspects of the examination process did you find **most** beneficial?

- Interaction with FCA examination staff is always useful to discuss current and emerging issues.
- Helps me determine if our internal controls are adequate and working.
- Opportunity to review institution's risk management and monitoring capabilities.
- Conversations with examiners regarding a variety of topics including "best practice" observations from other FC institutions.

- The highest risks appear to be targeted. The Agency brings an independent safety and soundness approach, and the opportunity to have dialog during the process is very much appreciated.
- In relation to the Board and Audit Committee, the exit interview and Report discussion was very proactive and realistic. Questions were answered with knowledge and reflected a particular involvement in the specific institution examined.
- FCA has recognized the actions we have taken to address issues, and assisted by providing guidance in future actions we need to address.
- Clarity on documentation of planning process and dialog regarding various risks.
- The examination consisted of offsite review on an ongoing basis and that was very helpful as disruption to the daily operation was minimal.
- The recommendations (11) were beneficial so that the board and management could narrow the focus on what's most needed.
- Focus areas of examination.
- The Exam team brought to our attention a few points in regulation that we were not in compliance with. The institution believes that these findings have proven beneficial.
- We thought the examination process was well run and hope it continues in the same manner.

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

- Having staffers who did not participate in the review attend the exit conference.
- The FIRS ratings are very important and appear to be showing more focus on what might be anticipated versus actual entity performance at a particular point in time.
- As Board member, we are not involved in the day to day examination process, so it is beyond the scope of our duties to opine on this specific matter.
- Examiners in training were not able to provide as much useful input/feedback.
- Scope and eligibility seems to be a moving target and the narrow interpretation will increase system risk as we begin to lose the customers with diversified income streams.
- Unfounded pessimism.
- We feel a "broad brush" approach was taken to the examination of the Scorecard program. The extra analysis we do to support the approval and mitigate risk that may come with a scored portfolio was not given consideration. This may have been impacted by the experience level of the team.

Survey Item 11: Please provide any additional comments about the examination process and related communications.

- We continue to appreciate the professional, courteous, and open manner in which the exam is conducted.
- I don't have any issues with FCA audit at this time. I do like the periodic monitoring. If I have an issue I can call or likewise if they have an issue they call. Today we have a good relationship.
- The recent FCA exam was conducted very professionally with good communication between the exam team and management.

- The open and clear communication from the Agency and especially the Exam team and its leaders is greatly appreciated.
- We appreciate the professional manner in which the examination was conducted and hope it continues.
- **More timely feedback.**
- **Repetitive requests for same information.**
- This survey is certainly not intended to be derogatory in nature toward the exam team. We feel the team was comprised of very capable examiners who fully understand the application of regulations and who overall do very good work. **Yet, we also believe that the tenure level lead to some conclusions being made due to a lack of experience in the lending business.**