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### **Fact Sheet on Investment Management for Farm Credit System Banks and Associations**

The Farm Credit Administration Board today adopted a final rule revising its regulations that govern the investment management of Farm Credit System (FCS or System) banks and associations. FCA had revised these regulations in 1999 and 2005. During the recent financial crisis, FCA recognized that these regulations should be updated and strengthened. These changes should further strengthen investment management activities at FCS institutions. In an upcoming rulemaking, we will be addressing investment eligibility and association investments.

#### **Summary of Changes**

**Section 615.5131 Definitions:** For clarity, we add definitions for “Government agency” and “Government-sponsored agency.” We also make conforming changes to these same definitions in section 615.5201, which provides definitions for our capital adequacy rules.

**Section 615.5132 Investment Purposes:** FCA regulations limit the eligible investments of a Farm Credit bank to 35 percent of the bank’s total outstanding loans. We revise the regulation to allow Farm Credit banks, when calculating the amount of eligible investments they may hold, to exclude collateral posted as margin for derivative transactions. We make this change because Farm Credit banks use derivative products as an integral part of their interest rate risk management activities and as a supplement to the issuance of debt securities in the capital markets. Banks are required to post collateral to counterparties resulting from entering into derivative transactions, and we do not want to discourage them from implementing appropriate risk management practices. We also make changes to the 35 percent calculation; these changes will provide increased investment management flexibility.

**Section 615.5133 Investment Management:** The revised regulation provides additional board policy requirements, enhances internal controls of investments, and strengthens board reporting requirements. It also allows increased investment management flexibility, where appropriate. It requires institutions to stress-test all investments that are structured or that have uncertain cash flows, including all mortgage-backed securities and asset-backed securities, before purchase. (The existing regulation requires pre-purchase stress testing only of mortgage securities.) The

revised regulation also expressly requires quarterly stress testing of the entire investment portfolio, on both an individual security basis and a portfolio-wide basis.

**Section 615.5135 Management of Interest Rate Risk:** We incorporate our interest rate risk management program requirements into a new § 615.5180 and remove § 615.5135 from our regulations.

**Section 615.5136 Emergencies Impeding Normal Access of Farm Credit Banks to Capital Markets:** This provision authorizes FCA, if it determines that an emergency exists, to adopt, in its sole discretion, a resolution providing relief from its eligibility and liquidity requirements. We are finalizing changes that would broaden FCA's discretion in its granting of relief.

**Section 615.5140 Eligible Investments:** We make technical changes to the investment eligibility criteria table.

**Section 615.5141 Stress Tests for Mortgage Securities:** We incorporate our stress-testing requirements into § 615.5133 and remove § 615.5141 from our regulations.

**Section 615.5143 Management of Ineligible Investments and Reservation of Authority to Require Divestiture:** Under the final rule, the eligibility of investments is determined only at the time of purchase; an institution that purchases an ineligible investment must divest within 60 days unless FCA approves a divestiture plan for a longer period. An investment that is eligible when acquired, however, does not lose its eligibility even if its credit quality deteriorates. Instead, the final regulation specifies liquidity requirements and collateral treatment (all of which largely mirror the conditions we currently impose in connection with approving divestiture plans) for investments with deteriorated credit quality. In addition, the final rule requires institutions to develop a plan to reduce the risk from investments as their credit quality deteriorates. The final rule also reserves FCA's authority to require divestiture for failure to comply with FCA regulations regarding permissible purposes of investments, as well as for safety and soundness reasons.

**Section 615.5174 Farmer Mac Securities:** We remove the requirement that a System institution must stress-test Farmer Mac securities backed by loans that the institution originated. However, an institution must perform stress testing on mortgage securities issued or guaranteed by Farmer Mac that are backed by loans it did not originate. In addition, because other investments would no longer have to be divested if they fail a stress test, we remove this requirement for Farmer Mac securities as well.

**Section 615.5180 Bank Interest Rate Risk Management Program:** We combine the requirements of § 615.5135, § 615.5180, and § 615.5181 for clarity purposes. We also rename this section. We strengthen the interest rate risk management program of Farm Credit banks by adding new requirements for the interest rate risk management section of a bank's asset/liability management policy.

**Section 615.5181 Bank Interest Rate Risk Management Program:** We incorporate these interest rate risk requirements into § 615.5180 and remove § 615.5181 from our regulations.

**Section 615.5182 Interest Rate Risk Management by Associations and Farm Credit System Institutions Other Than Banks:** We make technical changes to the regulation.