

**Remarks by
The Honorable Nancy C. Pellett
at the
Farm Credit Council Annual Meeting
San Diego, California
January 17, 2005**

Thank you for the very nice introduction and good morning to all of you.

And what a pleasure it is to be here today and to have the chance to interact with so many of you as you begin a new, and probably one of the more important, years in your history as you work to lay the foundation for a new future.

I have noted an excitement among you, and we at FCA are supportive of your efforts to build on your contributions to agriculture.

Before I get into my remarks I want to acknowledge two very special people...my colleagues on the board.

Just last month we welcomed Dallas Tonsager as the newest member of the Board. I'm sure that those of you who have had a chance to interact with Dallas realize what a tremendous addition he will be to the board. His engaging mind and earnest desire to improve agriculture and rural America is a breath of fresh air for all of us.

And then there is Doug Flory whom you all know very well. I cannot tell you how much Doug has meant to me over the past two years. Doug, thank you for everything you have done for me, and for your dedicated efforts to move this Agency forward during some very tough times.

This morning I would like to highlight the results from our regulatory oversight of the System over the past year and then I would like to share with you my major goals for the Agency. First, a strong commitment to improving communications; second, a deep desire to become a more effective regulator; and third, a personal vision to create opportunities for you to become more involved in contributing to rural America.

Let me start with what our examiners concluded about the System over the past year.

First and foremost, all institutions of the Farm Credit System remained fundamentally safe and sound in all material respects.

From a financial and asset quality perspective, the institutions of the Farm Credit System have probably never been in better shape than they are today. System capital is at the highest level it has ever been, and credit quality is similarly sound, reflecting the improved financial condition of borrowers and a positive agricultural economic environment.

Another conclusion reached by the examiners is that institutions continue to make significant positive efforts in serving the credit and related services needs of our young, beginning, and small farmers.

Examiners have found that you have more clearly defined your goals for these important programs and have improved your ability to monitor and report on whether your goals are being achieved.

But more importantly, examiners are reporting a consistent good-faith effort by institutions to ensure these programs meet the special credit needs of these borrowers. Your performance in this area achieves a very important public policy mission, and I encourage you to continually improve your efforts to assist young, beginning, and small farmers. They are your future. They are agriculture's future.

A third area our examiners are reporting on is continued improvement in all aspects of management at System institutions.

Board governance and transparency of your operations must remain a high priority for the future.

I commend you for taking the initiative to strengthen your governance standards and improve your financial disclosure and reporting practices. However, political and public pressure in this area is certain to increase due to accounting irregularities found at other Government-sponsored enterprises (GSEs).

As you know, the FCA Board recently proposed a rule on governance. It is currently under Congressional review but should be published in the *Federal Register* soon. I encourage you to study it, compare it to best practices, and share your thoughts and ideas with us on this very important issue.

At a time of mounting criticism and skepticism about GSEs, and governance in general, I believe it is important to have a regulatory framework in place that assures the public, stockholders, and investors that the System is properly governed by a set of consistent standards. The fact that many, if not most, of these are already in place at many System institutions should make this proposed rule one that is relatively easy to finalize.

In summary, the Farm Credit System and its institutions are safe and sound and are effectively working toward accomplishing their public policy mission.

Even with that in mind, I still would like to comment on a few issues.

As I noted, the overall health of the System is good and credit availability for borrowers is positive. The outlook is so good that it has enticed foreign financial intermediaries to seek access to US markets. This underscores the importance of building strong cooperative shareholder relationships that can survive through both good and bad times.

I have, as you have, learned a lot from the recent termination experience. I learned how passionate you can be about remaining a unified whole, but I also I learned about how deep your frustrations can be. From a regulatory perspective, we identified the need to address several aspects of our termination regulations and we will do so shortly.

Now, on another note, I realize that you have reversed a significant amount from your loan loss allowance accounts at yearend, enhancing even further the capital levels of

most institutions. We are pleased that you have decided to generally retain the capital for risk funds.

While viewed by some as an unexpected windfall to capital, boards must manage capital strategically and determine how they can best fulfill the mission of the institution. I will have some more comments on employing capital a little later in my remarks.

Now, please allow me to talk about my goals.

Commitment to Improved Communication

First, I am committed to improving communication internally as well as externally with all interested parties but in particular with the System.

At all times, we must ensure that we have an open and respectful dialogue on all issues that exist between us. And this cannot be accomplished by me or Agency staff spending all our time in McLean. We need to be out there talking with you, observing your operations and the challenges that you face.

When it comes to regulations, I want to assure you that we will make every attempt to not surprise you. While we may not always agree on every issue, we will make you fully aware of our intentions and we will provide you ample opportunity to weigh in on the regulatory matters we bring forth. I believe strongly that openness is critical to effective regulatory oversight.

Our basic policy is to maintain a flexible and responsive regulatory environment. We will react timely to your requests to clarify or explain our position on the law and regulations under which we expect you to operate. And where appropriate, we will eliminate or revise those regulations that unnecessarily impair your ability to accomplish the mission for which you were created.

I am committed to following President Bush's agenda of reducing the regulatory burden on those whom we regulate. But please remember that we are the arm's length safety and soundness regulator of the System. You, and we, must act accordingly. Trust me...as I have mentioned several times before, safety and soundness is paramount and we will be firm if and when the circumstances call for corrective action.

And, when a regulatory solution to your requests is not possible I urge you to go to Congress to further clarify the authorities you think you need to better serve a rapidly changing agriculture, marketplace, and rural America. And I suggest you do so soon.

Your statute has not received a general update since 1971. As a result, it does not address the needs of rural America today, nor does it accommodate many of the market conditions and economic forces that exist today. I believe your case is strong and most certainly your cause is honorable.

Improving Effectiveness

My second goal is a commitment to ensure that FCA accomplishes its mission more effectively. I have initiated several internal projects that are intended to streamline FCA

operations, make us more responsive to your needs, and better manage the cost of our operation to the System.

Let me take a moment to thank so many of you for taking the time to interact with us as we reshape ourselves to better respond to the demands of the future. Your input has been invaluable.

Our work in this area supports President Bush's initiatives to achieve greater efficiency and effectiveness within the government, and I have high aspirations for what the results of our self-examination will accomplish for us.

I want us to become the model of efficiency for regulatory agencies and I know we can do it because, bureaucratically, we are small, but more importantly, because we have a solid core of talented and dedicated professionals to make it happen. Many of our key managers are here for the conference and I hope your discussions with them have been and will be productive. Let me assure you, they do listen.

Since nothing ages so quickly as yesterday's vision of the future, following our studies we will update our strategic plan to better focus our efforts, and concurrently we will develop processes that are more responsive to changes in the environment within which we operate.

We recognize that the Agency faces substantial challenges in reshaping itself. However, the nature of these challenges only makes the task more important and the achievement of positive results more rewarding. I believe how we handle these challenges will clearly signal our professionalism and integrity to others and, more importantly, to ourselves.

I also want to compliment you for undertaking the Horizons initiative. Getting the System together on its strategic thinking will be highly beneficial as you address the future. We take your effort very seriously and I really do encourage you to make this effort a priority.

Overall, I believe you are at a crossroads in deciding what kind of a GSE you will be. And we in turn are deciding how best to structure ourselves as your regulator. As we progress through our studies and address the issues before us over the next few years we will all be working very hard to better ourselves. Striving for success without hard work is like trying to harvest where you have not planted. Hard work is not foreign to us who are engaged in agriculture and we are all up to the challenge.

I do believe we can learn from each other's work and I look forward to some informative results as we face future challenges in agriculture and rural America...together.

Investments in Rural America

The last goal I want to talk about involves creating opportunities for you to invest in rural America. Throughout my term I intend to be a strong advocate not only for agriculture but also for our rural communities.

In my opinion, supporting rural communities is vital to the success of agriculture and to those who engage in it. While there are only about 2 million farmers and ranchers

nationwide, there are about 65 million people living in rural America. Rural America is obviously a larger market segment to serve.

I am convinced that vibrant rural communities are the most critical factor in keeping farmers on the land and in getting new people into farming, both that young farmer and their spouse. If I am wrong about this I need you to convince me otherwise. So, to better support agriculture, I think you should focus on, and fund or invest in, activities that benefit rural America.

A stated intent of the Farm Credit Act is to provide for an adequate and flexible flow of money into rural areas and I believe investments are certainly a logical, supportable way to do so.

You have been a model GSE for helping and strengthening agriculture....I believe you could also establish a similar legacy for helping rural communities and rural Americans. I know that you spend a lot of time studying and assessing your marketplace and identifying the lending and related services needs of your borrowers. That is good business sense.

I would encourage you to also assess the condition of the rural areas and the needs of rural Americans within your chartered territory. Identify what you can do to improve it, to strengthen it, to return to it all that it has done for you in the past, and can do for you in the future. That makes good public policy sense.

You have come to me often with your ideas on how to further clarify your lending authorities. I ask you to look more at the broad authorities available under your seldom used investment authorities versus your well used lending authorities. Now, I ask you to come to me with your ideas on how you can play a greater role in rebuilding and revitalizing rural communities.

And I ask you to come to me with your ideas on how you can partner with others in your local area, region, or on a national basis, to make an impact on rural America through the broad charge available to you under your investment authorities.

I believe it is not just the System, it is not just USDA, it is not just the commercial bankers...it is all of you, in partnership with each other, that will make the most difference in strengthening the rural America of the future. And I encourage and challenge you to take the lead in this area.

Just last week we issued an Informational Memorandum that provides you with additional guidance on the development of pilot investment programs that could be used to meet the varying needs of agriculture and rural areas. The Memorandum includes specific guidance on what factors we will consider when we evaluate your requests to approve pilot investment programs. It also includes examples of programs that you might consider to help agriculture and rural communities meet their ongoing debt and equity financing needs.

We are also looking to gather additional information on your ideas, thoughts and suggestions through roundtable discussions and other meetings.

We are truly committed to helping you develop the right tools to make a difference in your local rural areas. I encourage you to embrace this unique opportunity and challenge you to develop innovative solutions for the rural communities you serve.

The future of this initiative is largely in your hands. If my message strikes a chord of innovation in your mind about how you might reach 65 million rural Americans, how you might improve the well-being of 65 million rural Americans, or how you might become a GSE that rewrites the landscape of rural America...then come talk to me and my staff and we will do what we can to help you achieve such a vision.

In closing, I would again like to compliment you on a very successful past year and wish you the best for an even brighter future.

Thank you very much for having me on the program.