Farm Credit Administration

Fiscal Year 2013 Budget (Proposed) and Performance Budget

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LIST OF ACRONYMS AND ABBREVIATIONS

ACA	Agricultural Credit Association
B&I	Business & Industry
CAMELS	capital, assets, management, earnings, liquidity, and sensitivity
Dodd-Frank Act	Dodd-Frank Wall Street Reform and Consumer Protection Act
Farm Credit Act	Farm Credit Act of 1971, as amended
Farmer Mac	Federal Agricultural Mortgage Corporation
FBRA	Federal Bank Regulatory Agency
FCA	Farm Credit Administration
Leasing Corporation	Farm Credit Leasing Services Corporation
FCS or System	Farm Credit System
FCSBA	FCS Building Association
FCSIC	Farm Credit System Insurance Corporation
FIRS	Financial Institution Rating System
FLCA	Federal Land Credit Association
FTE	full-time equivalent
FTP	full-time permanent
FY	fiscal year
Funding Corporation	Federal Farm Credit Banks Funding Corporation
GSE	Government-sponsored enterprise
HCP	Human Capital Plan
IDPs	individual development plans
IT	information technology
NCB	National Consumer Cooperative Bank
OSMO	Office of Secondary Market Oversight
PCA	Production Credit Association
RBC	risk-based capital
SBA	Small Business Administration
USDA	U.S. Department of Agriculture
YBS	young, beginning, and small (farmers and ranchers)

INTRODUCTION

The Farm Credit Administration (FCA or Agency) is an independent agency in the Executive branch of the U.S. Government. It is responsible for the regulation and examination of the banks, associations, and related entities that collectively constitute what is known as the Farm Credit System (FCS or System), including the Federal Agricultural Mortgage Corporation (Farmer Mac).[1]

Initially created by an Executive order of the President in 1933, the Agency now derives its powers and authorities primarily from the Farm Credit Act of 1971, as amended (Farm Credit Act). FCA promulgates regulations to implement the Act and examines System institutions for compliance with the Act, regulations, and safe and sound banking practices. FCA's mission is to promote a safe, sound, and dependable source of credit and related services for agriculture and rural America.

This document presents and justifies FCA's proposed budget for fiscal year 2013. It contains key information about FCA's various functions and program activities, along with an overview of the financial condition of the FCS and Farmer Mac, the entities regulated by the Agency. Also included is the fiscal year 2013 performance budget, which ties proposed expenditures to the goals and objectives in FCA's strategic plan.

This document is organized into four sections as follows:

1. Part I contains FCA's budget request. This section presents budget trends that are monitored annually by the Agency.

2. Part II covers the functions, programs, and services that FCA undertakes to fulfill its public mission. It also provides information on actions the Agency has taken to improve internal operations.

3. Part III discusses the System's financial condition and performance.

4. Part IV contains FCA's FY 2013 performance budget, which provides a basis for measuring the Agency's overall effectiveness.

[1] Although Farmer Mac is an FCS institution under the Farm Credit Act (12 U.S.C. 2279aa-1(a)(2)), we discuss Farmer Mac separately from the other entities of the FCS in this document because of the secondary market authorities unique to Farmer Mac. Farmer Mac is not jointly and severally liable on debt issuances with other parts of the FCS.

Part I

FISCAL YEAR 2013 BUDGET (PROPOSED)

FISCAL YEAR 2013 BUDGET OVERVIEW

The FY 2013 proposed budget request, as represented in table 1, includes $63,300,000 in assessments (current-year and carryover funds) from the Farm Credit System (FCS or System) institutions, including the Federal Agricultural Mortgage Corporation (Farmer Mac). Additional sources of funding bring the total proposed Farm Credit Administration (FCA) budget request to $64,130,601.

Table 1. Farm Credit Administration FY 2013 Budget (Proposed)

Description	Amount Proposed	Percentage of Total Budget
Full-time-permanent personnel (FTP)	$38,121,169	59.4
Other than FTP	1,091,840	1.7
Other personnel compensation	386,085	0.6
Total personnel compensation	**$39,599,094**	**61.7**
Personnel benefits	13,429,316	20.9
Benefits for former personnel	25,000	0.0
Total compensation and benefits	**$53,053,410**	**82.7**
Travel and transportation of persons	4,080,605	6.4
Transportation of things	185,371	0.3
Rent, communications, and utilities	1,016,751	1.6
Printing and reproduction	208,930	0.3
Consulting and other services	4,014,467	6.3
Supplies and materials	684,743	1.1
Equipment	886,324	1.4
Total budget	**$64,130,601**	**100.0**
Current-year assessment	$56,800,000	---
Carryover funds	6,500,000	---
Assessments collected from the FCS and Farmer Mac	**$63,300,000**	**---**
Other sources of funding	830,601	---

Note: Obligations for administrative expenses in FY 2013 are not to exceed the amount to be collected in assessments from the FCS and Farmer Mac ($63,300,000). Other sources of funding, such as reimbursements and interest income, do not affect this limitation.

The FY 2013 budget request reflects a 3 percent increase from the FY 2012 proposed budget. It includes a $.6 million increase (1 percent) in assessments of System institutions. The rate of increase in both the total budget and the assessments in FY 2013 is smaller than the rate of increase in the FY 2012 budget and assessments. The 3 percent budget increase is the lowest in six years.

The increase in the FY 2013 budget is necessary to fund an increase in the examination program. This increase will enable the Agency to better manage the risk associated with the Nation’s current financial environment. A robust examination program will ensure that any emerging risk is identified early so that the System’s safety and soundness is maintained.

In the FY 2013 proposed budget, the staffing level increases by 4.30 full-time-equivalent (FTE) staff positions from the FY 2012 proposed budget. This increase provides additional support to the Agency’s safety and soundness program. The 3 percent budget increase is needed to maintain and slightly grow FCA's talent pool so that the Agency will be able to examine and supervise the changing risk environment in the FCS. In addition, these modest increases are needed because the Dodd-Frank Wall Street Reform and Consumer Protection Act has raised the bar for the Agency's responsibility to oversee the safety and soundness of the Farm Credit System.

The budget provides the resources needed to fulfill the Agency's objectives, which are as follows:

- To maintain strong examination and supervisory programs
- To establish the right level of regulatory capital for FCS institutions
- To ensure that the public purpose and mission-related responsibilities of the System are carried out appropriately

The budget continues to implement the FCA Board's philosophy on risk-based examination. Sufficient resources are included to ensure that risks are properly identified, managed, and controlled. These resources will support an increase in the on-site presence of FCA examiners and a greater emphasis on loan review through internal audits, internal controls, and the testing of credit reviews. The increase in the number of examiners and the number of on-site reviews requires an increase in travel-related spending. The budget also reflects contract expenses. The Agency uses contract support for technical expertise and technology advancements.

The budget provides resources for developing regulations and policy positions that implement applicable statutes, for promoting the safety and soundness of the FCS, and for supporting the System's mission as a dependable source of credit and related services for agriculture and rural America.

FCA is making a significant investment in its Human Capital initiative. This includes the development of programs designed to create and sustain a results-oriented culture within the Agency that emphasizes the importance of learning, expertise, and personal growth.

The Agency will focus on providing appropriate training to precommissioned examiners and capturing the knowledge of employees who are eligible to retire. Staff members have identified the competencies needed for precommissioned employees, and they have designed a curriculum and trained instructors to deliver the curriculum. Staff members also provide quality assurance for the Precommission Training Program.

In addition, the budget includes continued funding for several major, multi-year projects that represent investments for the future operations of the Agency. These include the following:

- <u>Agency Infrastructure Hardware Upgrade</u>. The Agency's servers and network routers and switches are on a four-to-five-year replacement cycle. This project involves replacing outdated servers and telecommunications routers and switches. Replacing this equipment every four to five years will ensure fast, reliable communication and computing services.

- <u>Applications Migration Project</u>. The Applications Migration project continues to build on the 2008 Infrastructure Review and Workflow Integration project to ensure that the new infrastructure is being used in the most efficient and effective manner. The project requires that applications be moved to the new infrastructure so that the licensing costs of the old application software (Lotus Notes and Oracle) can be eliminated and the capabilities of the new infrastructure can be integrated into FCA's custom applications.

- Enterprise Documentation Guidance (EDGe) Project. The EDGe initiative will be the central hub for the Office of Examination's oversight and examination program and the Agency's institution-related documentation system. It further leverages the Agency's technology investments and improves communications and coordination. The Agency's new infrastructure, which is built around the Microsoft Office suite of applications, will be used to create the Agency's institution-related documentation system, as well as the documentation itself.

- FCS Loan Database. Phase II of the FCS Loan Database project will further expand the loan portfolio data collected from FCS institutions. Data need to be expanded to facilitate cross-institution analysis. New reports will be required to analyze the data and some standard queries will be developed. This database will facilitate macroanalysis of System characteristics and trends and enhance FCA's oversight of the System.

Background

FCA expects the FCS to continue to evolve in the coming years to meet the demands of an increasingly complex marketplace for agriculture and rural America. As FCS institutions grow and change, their operations become increasingly complex. With recent increased risk in several institutions, mergers and consolidations are expected to continue. The Agency expects the System's asset base to grow at only a moderate pace because of current global economic conditions. The System's growth will increase the average institution's asset base, which currently exceeds $1 billion.

The budget request reflects anticipated changes in the System and financial markets that will require increased resources to ensure the safety and soundness of the FCS. The budget strategy will enable FCA to effectively leverage and build on its most valuable investment—its people. The budget request enables the Agency to continue to implement initiatives to streamline and improve operations and to develop and enhance staff expertise to meet any challenges and opportunities that may arise. The budget request supports the Agency's Human Capital Plan by providing for an increase in the number of Office of Examination staff and by providing for the implementation of the Information Resources Management Plan.

FCA Program Areas

The Agency has two primary programs: (1) policy and regulation and (2) safety and soundness. All FCA office activities support these programs directly or indirectly.

The Policy and Regulation Program

The budget provides resources for developing regulations and policy positions that implement applicable statutes, promote the safety and soundness of the FCS, and ensure that the System carries out its mission as a dependable source of credit and related services for agriculture and rural America. In addition, the budget provides for ongoing activities such as evaluating and recommending regulatory and funding approvals, managing merger and chartering activities, and providing strategic and systemic policy research and analyses of risks and other issues facing the System.

The budget also provides for support activities, including the processing of information, the communication of Agency positions, and the administration of activities associated with the policy and regulation program. In total, policy and regulation activities account for $13.6 million, including 57.31 FTEs in the proposed FY 2013 budget (see table 30 on page 75).

The Safety and Soundness Program

Through the Agency's safety and soundness program, the budget provides resources to protect the safety and soundness of the FCS. The budget resources provided through this program also ensure that FCS institutions comply with applicable laws and regulations and are financially positioned to meet the needs of agriculture and rural America. The budget continues to implement the FCA Board's risk-based approach to oversight and examination, which maximizes the effectiveness of examinations and promotes communication with System institutions.

Sufficient resources are included to ensure that the FCS properly identifies, manages, and controls risk. Examination resources are allocated to matters presenting the highest risk or potential risk to the System. Initiatives include an increased on-site examination presence and greater emphasis on loan review through internal audits, internal controls, and the testing of credit reviews. An increased number of FCS institutions are now requiring special supervision and enforcement actions. These actions are taken as a result of significant input from FCA staff and reflect the weaknesses in the Nation's economy and credit markets, along with a rapidly changing risk environment in agriculture. The budget also includes support activities necessary for carrying out the Agency's safety and soundness program. In total, safety and soundness activities account for $48.6 million, including 239.77 FTEs in the proposed FY 2013 budget (see table 30 on page 75).

Office of Inspector General's FY 2013 Budget Request

Section 6(f)(1) of the Inspector General Act of 1978, as amended, (IG Act) requires an Inspector General (IG) to include specific information in the budget request the IG submits to the head of the department or designated Federal entity to which the IG reports. To fulfill the requirement of Section 6(f)(2) of the IG Act as it pertains to FCA, the FCA Board must in turn include this same information in the budget request that the Agency submits to the President.

The information that the IG Act requires to be included is provided below:

- The aggregate budget request for the Office of Inspector General (OIG) is $1,155,117.
- The amount needed for OIG training is $16,465 (tuition).
- The amount needed to support the Council of the Inspectors General on Integrity and Efficiency is $3,300.

The FCA Board is submitting the IG's budget request as received from the IG.

BUDGET TRENDS

The growth in the FY 2013 budget is necessary to continue to fund increases in the examination program, employee salary and benefit costs, and technology expenditures—all of which represent approximately 87 percent of FCA's total budget. These increases enable the Agency to better manage the risk associated with the Nation's current financial environment. A robust examination program will ensure that any emerging risk is identified early so that the System's safety and soundness is maintained. FCA's actual and budgeted spending levels parallel actual and budgeted FTE usage. FTEs have grown over the past five years because of the Agency's decision to increase its examination and oversight of the Farm Credit System to guard against risks related to credit market turmoil and weaknesses in both the agricultural and the general economy. Tables 2 through 5 provide information on FCA's budget trends.

TABLE 2. FY 2013 Budget (Proposed) Compared with the FY 2012 Budget (Proposed)

	FY 2012 Proposed Budget	FY 2013 Proposed Budget	Increase (Decrease) from FY 2012 Budget
Full-time permanent (FTP)	$37,173,022	$38,121,169	$948,147
Other than FTP	863,569	1,091,840	228,271
Other personnel compensation	379,889	386,085	6,196
Total personnel compensation	**$38,416,480**	**$39,599,094**	**$1,182,614**
Personnel benefits	12,888,221	13,429,316	541,095
Benefits for former personnel	18,000	25,000	7,000
Total compensation and benefits	**$51,322,701**	**$53,053,410**	**$1,730,709**
Travel and transportation of persons	4,074,260	4,080,605	6,345
Transportation of things	210,880	185,371	(25,509)
Rent, communications, and utilities	1,078,322	1,016,751	(61,571)
Printing and reproduction	213,350	208,930	(4,420)
Consulting and other services	3,458,208	4,014,467	556,259
Supplies and materials	765,369	684,743	(80,626)
Equipment	1,176,697	886,324	(290,373)
Total budget	**$62,299,787**	**$64,130,601**	**$1,830,814**
Less other sources of funding	6,099,787	7,330,601	1,230,814
Current-year assessment	**$56,200,000**	**$56,800,000**	**$600,000**

Note: A comparison of FCA's FY 2013 proposed budget request with the FY 2012 proposed budget reflects a 3 percent increase.

**TABLE 3. FY 2012 Budget (Proposed)
Compared with the FY 2012 Budget (Revised)**

	FY 2012 Proposed Budget	FY 2012 Revised Budget	Increase (Decrease)
Full-time permanent (FTP)	$37,173,022	$36,077,773	$(1,095,249)
Other than FTP	863,569	1,107,199	243,630
Other personnel compensation	379,889	384,628	4,739
Total personnel compensation	**$38,416,480**	**$37,569,600**	**$(846,880)**
Personnel benefits	12,888,221	12,161,218	(727,003)
Benefits for former personnel	18,000	25,000	7,000
Total compensation and benefits	**$51,322,701**	**$49,755,818**	**$(1,566,883)**
Travel and transportation of persons	4,074,260	3,913,206	(161,054)
Transportation of things	210,880	180,820	(30,060)
Rent, communications, and utilities	1,078,322	1,023,240	(55,082)
Printing and reproduction	213,350	207,180	(6,170)
Consulting and other services	3,458,208	3,870,807	412,599
Supplies and materials	765,369	696,156	(69,213)
Equipment	1,176,697	1,165,672	(11,025)
Total budget	**$62,299,787**	**$60,812,899**	**$(1,486,888)**
Less other sources of funding	6,099,787	6,712,899	613,112
Current-year assessment	**$56,200,000**	**$54,100,000**	**$(2,100,000)**

Note: A comparison of FCA's FY 2012 proposed budget request with the FY 2012 revised budget reflects a 2.4 percent decrease.

FCA's revised FY 2012 budget was approximately $1.5 million lower than its proposed FY 2012 budget. The Agency achieved this savings by not granting pay raises to employees holding senior-executive-equivalent positions and by reducing employee relocation costs. Prudent travel practices and the use of technology also contributed to the budget savings.

TABLE 4. FCA Obligations, FYs 2009–2013

	FY 2009 Actual	FY 2010 Actual	FY 2011 Actual	FY 2012 Revised Budget	FY 2013 Proposed Budget
Full-time permanent (FTP)	$28,656,751	$31,610,566	$32,540,297	$36,077,773	$38,121,169
Other than FTP	670,400	716,975	919,631	1,107,199	1,091,840
Other personnel compensation	366,771	419,316	416,680	384,628	386,085
Total personnel compensation	**$29,693,922**	**$32,746,857**	**$33,876,608**	**$37,569,600**	**$39,599,094**
Personnel benefits	8,159,418	9,327,654	10,023,189	12,161,218	13,429,316
Benefits for former personnel	22,868	41,932	22,711	25,000	25,000
Total compensation and benefits	**$37,876,208**	**$42,116,443**	**$43,922,508**	**$49,755,818**	**$53,053,410**
Travel and transportation of persons	2,929,569	3,587,507	3,266,038	3,913,206	4,080,605
Transportation of things	95,142	113,678	65,409	180,820	185,371
Rent, communications, and utilities	614,526	761,849	913,871	1,023,240	1,016,751
Printing and reproduction	131,821	131,364	138,140	207,180	208,930
Consulting and other services	3,040,744	3,388,696	3,277,466	3,870,807	4,014,467
Supplies and materials	488,869	565,653	562,863	696,156	684,743
Equipment	510,449	244,829	1,230,157	1,165,672	886,324
Insurance claims and indemnities	39	0	14	0	0
Total obligations	**$45,687,367**	**$50,910,019**	**$53,376,466**	**$60,812,899**	**$64,130,601**

Sources of FCA Revenue and Funding, FYs 2009–2013

FCA maintains a revolving fund primarily financed from assessments to System institutions and Farmer Mac. In addition, FCA provides reimbursable services to a few other entities and earns interest from investments with the U.S. Department of the Treasury. The Agency's reimbursable work is performed for the Farm Credit System Insurance Corporation, U.S. Department of Agriculture (USDA), and the National Consumer Cooperative Bank (NCB). Table 5 shows actual sources of revenue and funding for FYs 2009 to 2011 and projected sources of revenue and funding for FYs 2012 and 2013.

TABLE 5. Sources of FCA Revenue and Funding, FYs 2009–2013

Source	FY 2009 Actual	FY 2010 Actual	FY 2011 Actual	FY 2012 Revised Budget	FY 2013 Proposed Budget
ASSESSMENTS					
Banks, associations, and related entities	$42,932,010	$46,825,352	$49,906,192	$51,850,000	$54,550,000
Federal Agricultural Mortgage Corporation	2,050,000	2,250,000	2,200,000	2,250,000	2,250,000
Carryover funds[a]	4,900,000	5,400,000	6,900,000	5,900,000	6,500,000
Assessments available for obligation	**$49,882,010**	**$54,475,352**	**$59,006,192**	**$60,000,000**	**$63,300,000**[b]
REIMBURSEMENTS[c]					
National Consumer Cooperative Bank	122,489	159,261	302,286	72,863	157,424
Small Business Administration	89,359	0	0	0	0
Farm Credit System Insurance Corporation	341,044	360,741	425,032	269,793	242,497
U.S. Department of Agriculture	211,238	412,539	482,493	470,243	430,680
Other miscellaneous income	28,928	46,507	43,567	0	0
OTHER					
Interest income	498,671	554,413	560,206	—[d]	—[d]
Total	**$51,173,739**	**$56,008,813**	**$60,819,776**	**$60,812,899**	**$64,130,601**

[a] Carryover funds are amounts brought forward from prior years' assessments that remain available for obligation.

[b] FCA's proposed obligation limit for FY 2013 is $63,300,000.

[c] From a budget standpoint, reimbursements do not include indirect costs.

[d] As part of FCA's interest reserve strategy, no funds are budgeted from interest earned.

Note: The revolving fund is financed primarily from assessments to System institutions and Farmer Mac, along with money received for reimbursable services that FCA provides to other Federal agencies and the interest earned from investments with the U.S. Treasury.

BUDGET AND ASSESSMENT ISSUES

Farm Credit System

FCA's operating costs are financed from direct assessments to System institutions. FY 2012 assessments to System institutions totaled $54.1 million, an increase of $1.6 million over FY 2011. The proposed assessment to System institutions in FY 2013 is $56.8 million, reflecting a $2.7 million increase over the FY 2012 revised assessment. Table 6 provides information on FCA's assessments and refunds for FYs 2004 through 2013.

TABLE 6. FCS Assessments and Refunds, FYs 2004–2013

Fiscal Year	Assessment (in millions)	Refund (in millions)
2004	$38.4	$2.1
2005	$39.4	$1.5
2006	$40.5	$0.0
2007	$41.5	$0.0
2008	$42.5	$0.0
2009	$45.1	$0.0
2010	$49.1	$0.0
2011	$52.5	$0.0
2012	$54.1	*
2013	$56.8	*

* Refund amount not yet determined.

Federal Agricultural Mortgage Corporation (Farmer Mac)

Farmer Mac's assessment for FY 2012 is $2.25 million. As required by regulation, the assessment will be reconciled and adjusted after the fiscal year end to reflect the actual amount expended. Actual costs for FY 2011 were $2.20 million. The assessment for FY 2013 is not yet available because the Office of Secondary Market Oversight (OSMO) will not complete the FY 2013 budget and estimation of examination, oversight, and regulatory costs pertaining to Farmer Mac until September 2012.

FY 2003 and subsequent assessments for Farmer Mac are presented in table 7 and include costs associated with increased examination and oversight activities. OSMO plans to add additional staff in FY 2012 in response to Farmer Mac's significant growth since 2005 when OSMO's organizational structure last changed.

TABLE 7. Farmer Mac Assessments
FYs 2003–2013

Fiscal Year	Assessment *(in millions)*
2003	$1.78
2004	$2.00
2005	$2.30
2006	$2.35
2007	$2.20
2008	$2.05
2009	$2.05
2010	$2.25
2011	$2.20
2012	$2.25
2013	$2.25

Note: Although it will not be set until September 2012, Farmer Mac's FY 2013 assessment is expected to be about $2.25 million, the same as the FY 2012 figure, though it could change.

Farm Credit Administration

FCS Borrower Costs

FCS borrowers incurred a net cost of 2.2 basis points, or approximately 2.2 cents for every $100 of assets held, to pay for Agency operations in FY 2011. Since FY 2002, the net cost to borrowers has decreased 1.2 basis points.

The FCS held $227.7 billion in total assets as of September 30, 2011, up from $220.5 billion a year earlier. The strong growth of System assets in recent years, combined with controlled growth of the FCA budget, has yielded a fairly steady decline in regulatory costs to FCS borrowers. Table 8 shows the borrower cost trends since FY 2002.

TABLE 8. FCA's Net Cost to System Borrowers, FYs 2002–2011

FY Ended September 30	Basis Points
2002	3.4
2003	2.9
2004	2.9
2005	2.6
2006	2.5
2007	2.2
2008	2.0
2009	2.0
2010	2.1
2011	2.2
Note: The net cost figure is the annual assessment (not including Farmer Mac) adjusted for refunds at the beginning of the fiscal year and divided by total assets at the end of the fiscal year.	

FCA Budget Carryover

FCA ended FY 2011 with a budget carryover from previous years of approximately $23.8 million. Of this amount, $5.9 million was transferred into the FY 2012 budget, and $6.5 million will be used to fund the FY 2013 proposed budget. The carryover includes an increase of $.6 million in interest earned and more than $.5 million in deobligations. The remaining balance will be available for use in an emergency situation or in accordance with the Agency's interest reserve strategy.

The reserve ensures that the Agency can effectively and efficiently respond to unanticipated, material, one-time policy or safety and soundness issues arising within the System. The reserve strategy provides FCA with a proactive plan to respond to these issues without increasing assessments at a time that may be financially problematic for System institutions.

Table 9 presents a 10-year comparison of unobligated balances carried over at the end of each fiscal year.

TABLE 9. FCA's Budget Carryover, FYs 2002–2011

Fiscal Year	Carryover (in millions)
2002	$13.9
2003	$12.0
2004	$10.1[a]
2005	$11.7
2006	$16.3
2007	$20.5
2008	$21.9
2009	$23.1
2010	$23.5
2011	$23.8[b]

[a] FY 2005 audit restatement
[b] Includes earned interest and excludes unfilled customer orders

Staffing

This budget request reflects FCA's commitment to achieving its public mission while adhering to targeted spending levels. It provides the resources needed to support the Board's strategic vision and to invest in Agency programs for policy and regulation development, risk-based examination and supervision, and the proactive management of systemic risks.

The environment in which the FCS operates is dynamic and increasingly complex. As part of our strategic planning to evaluate and address risk to the System, we took careful account of the continuing challenges in the Nation's financial sector. FCA has redirected staff resources in accordance with risk-based examination supervisory principles in order to proactively manage systemic risk and to continually seek cost-effective methods to share Agency resources and leverage technology for greater efficiency. Projected staffing levels for FYs 2012–2013 will also rise because of the increases in the examination program.

The composition of staff is also changing as tenured, experienced people retire and are replaced. Because of continuing retirements and ongoing changes in the technical skills that FCA requires for certain jobs, the Agency will continue to hire and train a number of employees over the next two years. The budget increase for FY 2013 reflects, in part, FCA's commitment to invest in targeted recruiting and training programs for new employees and to maintain safety and soundness in the System.

Table 10 provides the total full-time-equivalent (FTE) levels by office for FYs 2009–2013, whereas table 11 breaks out FCA's budget obligations by office for the same period.

TABLE 10. Full-Time-Equivalent (FTE) Levels by Office
FYs 2009–2013

Organizational Unit	FY 2009 Actual	FY 2010 Actual	FY 2011 Actual	FY 2012 Revised Budget	FY 2013 Proposed Budget
Board	8.9	8.6	9.8	10.4	10.2
Office of the Chief Executive Officer (CEO)	1.9	1.7	2.0	3.0	3.0
Congressional and Public Affairs	5.0	6.1	6.6	7.1	7.1
Examination	149.8	163.6	171.2	178.4	178.9
General Counsel	13.6	12.9	13.6	14.1	14.8
Management Services	48.8	50.7	49.9	54.0	54.0
Inspector General	4.6	4.6	4.6	4.6	4.6
Secondary Market Oversight	4.0	4.0	3.7	5.0	5.0
Regulatory Policy	24.2	24.3	25.0	27.6	27.5
Total	**260.8**	**276.5**	**286.4**	**304.2**	**305.1**
Change from previous year	**9.4**	**15.7**	**9.9**	**17.8**	**.9**

Note: The FTEs in the revised FY 2012 budget reflect an increase of approximately 1 percent, or 3.4 FTEs, from the FY 2012 proposed budget. The FY 2013 proposed FTE ceiling number reflects an increase of 0.9 FTE, from the revised FY 2012 ceiling.

TABLE 11. FCA Obligations by Office
FYs 2009–2013

Organizational Unit	FY 2009 Actual	FY 2010 Actual	FY 2011 Actual	FY 2012 Revised Budget	FY 2013 Proposed Budget
Board	$1,965,735	$2,171,983	$1,990,459	$2,347,722	$2,450,624
Office of the Chief Executive Officer	345,761	404,925	504,666	898,424	909,312
Congressional and Public Affairs	946,256	1,237,042	1,439,798	1,655,159	1,782,255
Examination	23,269,814	26,469,332	27,986,542	30,731,213	32,597,816
General Counsel	2,752,390	2,756,278	2,976,351	3,303,741	3,647,086
Management Services	10,174,396	11,209,513	11,668,502	13,790,426	14,273,044
Inspector General	985,307	1,037,857	1,066,934	1,190,727	1,243,998
Secondary Market Oversight*	1,001,851	1,077,719	966,341	1,329,816	1,416,824
Regulatory Policy	4,245,857	4,545,370	4,776,873	5,565,671	5,809,642
Total obligations	**$45,687,367**	**$50,910,019**	**$53,376,466**	**$60,812,899**	**$64,130,601**

* Excludes costs of certain offices, such as Examination and General Counsel, that assist in the examination and supervisory activities of Farmer Mac.

Note: To realize efficiencies, FCA offices share resources to accomplish various tasks and activities. These shared resources are not reflected in the individual office obligations.

Part II

FARM CREDIT ADMINISTRATION

PROFILE OF THE FARM CREDIT ADMINISTRATION

The Farm Credit Administration (FCA) was created through an Executive order of President Franklin D. Roosevelt and currently derives its powers and authorities primarily from the Farm Credit Act of 1971, as amended (Farm Credit Act). As an independent Agency within the Executive branch of the Federal Government, FCA is responsible for regulating and supervising the banks, associations, and related entities in the Farm Credit System (FCS), as well as the Federal Agricultural Mortgage Corporation (Farmer Mac).[2]

The FCS is the oldest of the financial Government-sponsored enterprises (GSEs). The Farm Credit Act states that the objective of the FCS is to improve the income and well-being of American farmers and ranchers by furnishing sound, adequate, and constructive credit and closely related services to them, their cooperatives, and selected farm-related businesses. In short, the FCS was created to provide an adequate and flexible flow of money to rural areas.

The System consists of a nationwide network of borrower-owned, cooperative financial institutions that provide credit and related services to

- farmers and ranchers,
- producers and harvesters of aquatic products,
- farm-related businesses,
- rural homeowners,
- agricultural and aquatic cooperatives,
- agribusinesses, and
- rural utilities.

The FCS had $170.6 billion in outstanding loans to agriculture and rural America as of September 30, 2011.

Farmer Mac is a stockholder-owned, federally chartered instrumentality of the United States, and its authority is derived from Title VIII of the Farm Credit Act. Farmer Mac was established in 1988 to create a secondary market for agricultural real estate loans and rural housing mortgage loans. In 2008, Farmer Mac's secondary market authorities were expanded to include rural utility loans. It provides secondary market services through a network of agricultural lenders and intermediaries including commercial banks, FCS banks and associations, life insurance companies, mortgage companies, and rural utility cooperatives. As of September 30, 2011, the volume of loans either purchased or guaranteed by Farmer Mac totaled $11.8 billion.

FCA is also required by the National Consumer Cooperative Bank Act of 1978, as amended, to examine and report on the condition of the National Consumer Cooperative Bank (NCB). Since the passage of this law, FCA has conducted safety and soundness examinations of NCB and issued reports of examination to NCB's Board of Directors. NCB is a federally chartered, privately owned banking corporation. It is not a Federal instrumentality, and it is not part of the FCS.

In addition, FCA contracts with the Farm Credit System Insurance Corporation and the U.S. Department of Agriculture to provide examination services.
The U.S. Senate Committee on Agriculture, Nutrition, and Forestry and the U.S. House of Representatives Committee on Agriculture oversee the FCS, Farmer Mac, and FCA. Agency

[2] By statute, Farmer Mac is part of the Farm Credit System; however, in this document, we will use the terms "FCS" and "System" to refer to all the entities in the Farm Credit System except Farmer Mac and affiliates of Farmer Mac.

operations are funded through assessments paid by the System institutions and by FCA's other reimbursable activities; FCA does not receive a Federal appropriation.

Mission Statement

FCA's mission is to ensure a safe, sound, and dependable source of credit and related services for agriculture and rural America. To fulfill its mission, the Agency issues regulations and conducts examinations of FCS institutions and Farmer Mac to evaluate and oversee the safety and soundness of their activities. FCA examinations also evaluate whether institutions are complying with laws and regulations, especially the Congressional mandate requiring System institutions to have programs to make credit and services available to young, beginning, and small (YBS) farmers. In addition, the Agency undertakes the research, development, and adoption of rules, regulations, and other guidelines that govern how institutions conduct their business and interact with customers.

If any System institution, including Farmer Mac, violates laws or regulations, or if operations are determined to be unsafe or unsound, FCA may use its enforcement authority to ensure that the problem is corrected in a timely manner. FCA also ensures that the rights of borrowers are protected.

Other statutory duties require the Agency to issue and amend FCS institution charters, to report to Congress on the System's and Farmer Mac's financial condition and performance, and to approve the issuance of System debt obligations.

FCA Board and Governing Philosophy

FCA policy and its regulatory agenda are established by a full-time, three-person Board whose members are appointed by the President of the United States with the advice and consent of the Senate. They serve staggered six-year terms and may not be reappointed after serving a full term or more than three years of a previous member's unexpired term. A Board member may serve after expiration of his or her term until a successor has been appointed and qualified. The President designates one member as Chairman of the Board; this member serves as Chairman until the end of his or her term. The Chairman also serves as the Agency's Chief Executive Officer.

The FCA Board approves charters of FCS institutions, oversees the Agency's supervision and examination of those institutions, and issues enforcement actions. The governing philosophy of the FCA Board is grounded in the Farm Credit Act. The Board believes that the principles on which the System was founded are just as important today as they were in the early decades of the 20th century. A healthy and strong rural America is a vital component of American society. It benefits the entire Nation by providing the most dependable, safest, and least costly supply of food and fiber in the world.

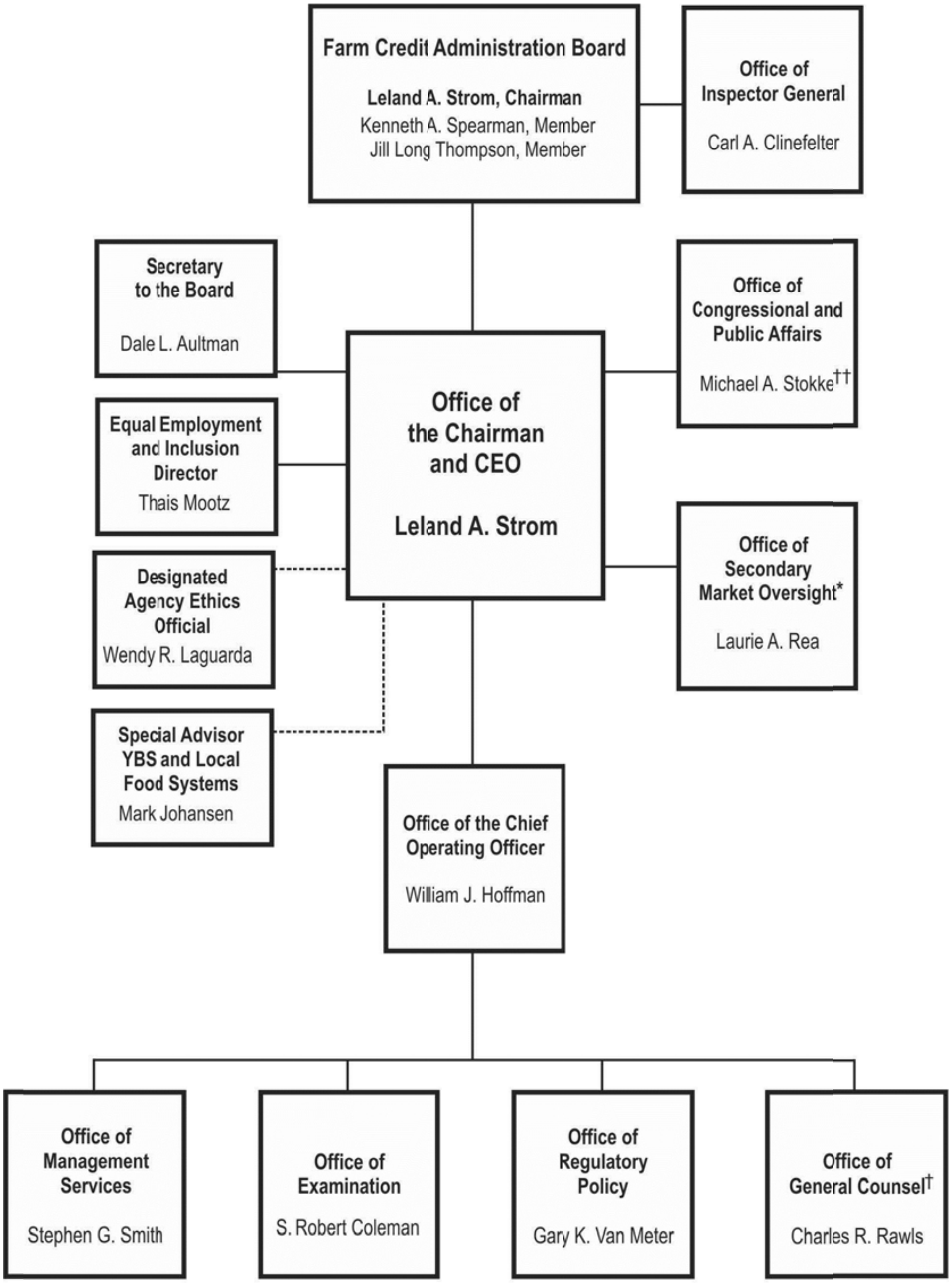
The FCA Board recognizes that changes in the agricultural and financial marketplaces create both risks and opportunities. As the Agency works to address these dynamic forces, the Board is committed to working with all constituencies in a reasonable and responsible manner to find thoughtful solutions to these emerging issues. However, the FCA Board's primary regulatory duty remains constant—overseeing the safety and soundness of the FCS and Farmer Mac.

FCA Organizational Structure

Figure 1 presents the Agency's organizational structure and shows how the offices provide strategic support to the FCA Board and ensure that the Agency's mission and goals are performed effectively and efficiently. The budgetary information for each office is contained in table 10 on page 18. FCA maintains its headquarters and a field office in McLean, Virginia, with additional field offices in Bloomington, Minnesota; Dallas, Texas; Denver, Colorado; and Sacramento, California.

Figure 1. FCA Organizational Chart

As of January 1, 2012



*Reports to the Board for policy and to the CEO for administration.
†Maintains a confidential advisory relationship with each of the Board members.
††Serves as Executive Assistant to the Chairman.

FCA INTERNAL OPERATIONS

FCA is firmly committed to the continuous development and support of its most valuable asset—its employees. This commitment is at the core of the Agency's five-year Human Capital Plan (HCP), which details activities that sustain a work environment in which FCA can accomplish its mission. The HCP focuses on workforce planning and deployment, leadership and knowledge management, a results-oriented performance culture, professional growth and motivation, and accountability. The framework of the HCP is based on the "Human Capital Standards for Success," a set of measures developed by the Office of Management and Budget, the Office of Personnel Management, and the U.S. Government Accountability Office.

Human Capital Management

Human capital strategies are linked to FCA's strategic plan through clearly defined performance measures. Workforce trends are continually monitored, and best practices are implemented as appropriate. The System's changing environment is also monitored so that FCA can adjust its staffing levels and maintain requisite skill sets by hiring additional staff, providing employee training and development, or transitioning employees from staff positions that are no longer necessary. Workforce planning strategies are reviewed annually. Full-time-equivalent (FTE) staffing levels (rounded to the nearest whole number) from FY 2004 through FY 2013 are depicted in table 12.

TABLE 12. Full-Time-Equivalent (FTE) Staffing Levels, FYs 2004–2013

Fiscal Year	FTE Staffing Level
2004	290
2005	271
2006	252
2007	253
2008	251
2009	261
2010	277
2011	286
2012	304 (authorized)
2013	305 (authorized)

Table 13 provides comparative statistics on the relationship between the number of Agency managers and supervisors to other personnel for FYs 2003–2012.

TABLE 13. Ratio of Managers and Supervisors to Other Personnel, FYs 2004–2013

Fiscal Year	Ratio
2004	1:7
2005	1:8
2006	1:6
2007	1:6
2008	1:6
2009	1:6
2010	1:6
2011	1:6
2012	1:6
2013	1:6

Note: This comparison indicates that the ratio of managers and supervisors to other personnel typically varies within a narrow range.

Workforce assessments are performed annually to obtain information on critical staffing variables, such as the age, grade, and gender of employees. Five-year projections are developed from this analysis to determine and mitigate the impact of employee retirements and separations. As of September 30, 2011, approximately 28 percent of Agency personnel were eligible to retire. As a result of recent hiring, the number of employees who have been employed five years or fewer has risen substantially over the past three years and now constitutes a sizable portion of FCA's workforce. This trend is likely to continue over the next three to five years. Table 14 provides information on retirement eligibility projections at FCA.

TABLE 14. FCA Retirement Eligibility, FYs 2012–2016

Fiscal Year	Eligible Retirements
2012	69*
2013	9
2014	6
2015	11
2016	6

* This number includes 61 staff members who became eligible to retire prior to FY 2012.

Implementing the Human Capital Plan

The challenges of FCA's retirement projections are carefully managed to ensure that a high level of institutional knowledge, job skills, and analytical expertise is sustained. In addition to succession planning and cross-training, the Agency provides a variety of resources and programs for sharing knowledge across the organization. During FY 2010, these efforts were coordinated by an HCP Oversight Group to ensure maximum efficiency and effectiveness.

FCA's continuous learning strategy emphasizes leadership, competencies, and knowledge management. By providing education, training, and other development opportunities, the Agency seeks to attract and retain bright, creative, and enthusiastic people. Identifying the Agency's human capital needs over the next five years, including the optimal size of its workforce and the appropriate skill sets of its employees, is one of its primary goals; assessments take place at all levels to accurately gauge human capital requirements. Assessment results are used to develop, enhance, and redirect training and development programs.

Training goals are coordinated with the leadership skills and competencies that are integral to achieving FCA's mission. The goals are comprehensive, developed at the office level and through individual development plans (IDPs). IDPs serve as the primary means of managing and planning employee training and development activities, projecting short- and long-term goals over a two-year period. They also are used for projecting budget needs for training resources and are linked to FCA's Performance Management System. Supervisors and employees collaborate on ongoing and proposed training and development goals during mid-year and annual performance reviews. Formal training programs support the needs of core occupational groups through a variety of methods, such as in-house training, vendor courses, self-study, rotational assignments, special assignments, shadowing experiences, and e-learning. Each employee has a laptop computer with the technology to support e-learning initiatives. In addition, as a matter of policy, all employees have regular access to training on FCA's computer systems.

FCA demonstrated its commitment to its training and knowledge transfer goals in FY 2011 by providing appropriate training to precommissioned examiners and capturing the knowledge of examiners who are eligible to retire. As more and more employees become eligible to retire, knowledge transfer becomes a greater concern. An internal training website has been established to capture examination knowledge and best practices. The information on the website will be developed by subject-matter experts, and instructor and student materials will be maintained there.

Thus, knowledge management remains a key component of the Agency's continuous learning strategy. As vacancies in critical fields are projected, orientation plans seek to have newly hired employees work closely with experienced employees to transfer critical knowledge and skills. In addition, the Agency's policies on training and employee development further enhance the transfer of knowledge.

FCA's electronic databases, such as the internal training site used by examiners, the Policies and Procedures database, the electronic examination files, and the Training and Evaluations database, are another component of knowledge management and best practices. These databases enable employees to communicate and share knowledge.

In recognition of the value that diversity and inclusion bring to the Agency, FCA continually develops initiatives and events to attract and retain staff with varied backgrounds and skills. The Agency endorses programs that promote equal employment opportunity (EEO), diversity, and inclusion, and it supports an active EEO program.

Long-term rotational assignments enhance employee knowledge and expertise. Through an organized program that encourages offices and employees to participate in rotational assignments, employees gain a deeper understanding of the Agency's mission. Rotational assignments build teamwork and collaboration and enhance the motivation and productivity of employees.

The Agency has established guidelines to select visiting fellows from universities and other organizations to work with its employees. By working closely with visiting fellows, FCA employees will expand their expertise and enhance their ability to conduct the examination and regulatory activities that protect the safety and soundness of the FCS.

FCA Compensation Program

The Financial Institutions Reform, Recovery, and Enforcement Act of 1989 (FIRREA) requires Federal financial regulators to strive to achieve comparability in compensation and benefit programs. Specifically, section 1206 of FIRREA directs FCA and other Federal bank regulatory agencies (FBRAs) to "seek to maintain comparability regarding compensation and benefits." These provisions enable FBRAs to attract and retain qualified staff. The Agency annually surveys the other FBRAs and adjusts its employees' compensation and benefits consistent with FIRREA. The Agency also surveys the private sector, the System banks, and the General Schedule agencies for purposes of general comparison. FCA's compensation policy provides compensation at a level similar to the average market rate provided by other FBRAs.

Salary adjustments

Normally, FCA uses a fully integrated pay-for-performance program that adjusts employee salaries annually using a merit pay matrix that provides for variable adjustments based on each employee's performance rating and salary range position. Each salary range is divided into five positions, or quintiles. The Agency reviews the matrix and makes adjustments each calendar year on the basis of a number of factors, including the salary programs of other FBRAs, available funding, and FCA's overall performance and accomplishments during the previous fiscal year.

Consistent with the Federal pay freeze legislation and the Presidential Memorandum of December 2010, FCA has not increased the salaries of senior management and has not adjusted the pay ranges or the locality-based pay rates for calendar years 2011 and 2012.

External Contracting and Shared Services

Outsourcing

As the table below shows, the Agency outsourced several functions in FY 2011. The Agency's shared-service agreement with the Bureau of the Public Debt began in FY 2006. FCA also outsources its payroll services to USDA's National Finance Center, its Employee Assistance Program services to ComPsych, and its Flexible Spending Account Plan to Benefit Allocation Systems. In FY 2010, the Agency began outsourcing its EEO counseling services through the U.S. Geological Survey. Outsourcing these services has allowed the Agency to manage its employee benefits and other Agency functions without additional personnel costs.

TABLE 15. Outsourcing, FY 2011

Contract	Purpose	Amount
Administrative Service Center (BPD)	To provide full-service accounting, eTravel, credit card, and platform procurement services	$877,698
National Finance Center (USDA)	To provide payroll services	$43,042
ComPsych	To provide Employee Assistance Program services	$6,498
Benefit Allocation Systems	To administer the Flexible Spending Account Plan	$0 (paid out of forfeitures)
U.S. Geological Survey	To provide EEO counseling services	$19,000
Note: FCA functions outsourced during FY 2011 totaled $946,238.		

Single Source and Competitive Consulting Service Contracts

Tables 16 and 17 provide a summary of the Agency's single source and competitive consulting service contracts for FYs 2010 and 2011.

TABLE 16. Competitive Consulting Service (CCS) Contracts of More Than $25,000 and Single Source (SS) Contracts, FY 2010

Contract	Purpose	Amount
McGraw Hill/Standard & Poor's; 10-FCA-450-01 (SS)	To provide Standard & Poor's online rating service	$40,300
A. Greenlee; 10-FCA-301-012 (SS)	To provide examination services	$33,000
A. Greenlee; 10-FCA-301-022 (SS)	Same as above	$42,000
J. Weaver; 10-FCA-301-08 (SS)	Same as above	$81,950
M. Morris; 10-FCA-301-24 (SS)	Same as above	$38,050
TJ Consulting; 10-FCA-301-09 (SS)	Same as above	$50,000
J. Messing; 10-FCA-301-06 (SS)	Same as above	$48,000
A. Sartain; 10-FCA-301-23 (SS)	Same as above	$71,600
J. Garrison; 10-FCA-301-007 (SS)	Same as above	$137,000
S. Weisz Consulting; 10-FCA-301-04 (SS)	Same as above	$27,875
Russells Financial; 10-FCA-301-03 (SS)	Same as above	$52,800
S. Roberson; 10-FCA-301-05 (SS)	Same as above	$34,000
Personnel Decision Research Institute; 10-FCA-C-01 (SS)	To assist in developing the Precommission Test	$67,925
Centrec; 10-FCA-301-27 (SS)	To provide self-study training	$11,477
Ethos; 10-FiFARCA-501-06 (SS)	To provide ethics review	$10,395
Gartner Group; 10-FCA-601-15 (SS)	To provide premier membership for FCA staff in the Gartner Executive Program	$40,200
Murphy Brothers; 10-FCA-601-07 (SS)	To provide taxi services	$16,500
D. Redden; 10-FCA-601-16 (SS)	To provide retirement counseling	$29,000
ComPsych; 10-FCA-601-08 (SS)	To provide employee assistance	$6,468
Powersolve; 10-FCA-601-11 (SS)	To provide maintenance	$22,393
Sybase; 10-FCA-601-54 (SS)	To provide PowerBuilder maintenance	$8,838
Gartner Group; 10-FCA-601-62 (SS)	To purchase tickets for the Gartner Symposium	$20,760
Ed Harshbarger; 10-FCA-911-01 (SS)	To provide consulting services to the Office of Regulatory Policy	$12,600
Towers Watson; 10-FCA-601-038 (SS)	Compensation Consulting Services	$102,000
iFAR; 10-FCA-911-006 (SS)	Consulting and technology assistance	$70,475
iFAR; 07-FCA-C-01, Option Year 3 (SS)	To provide consulting services to the Office of Secondary Market Oversight	$80,455
Thomas Holland; 07-FCA-C-02 Option Year 3 (SS)	Same as above	$20,725
SoftChoice; 10-FCA-601-069 (SS)	Microsoft Enterprise Agreement	$135,189
Cook Ross; 10-FCA-601-073 (SS)	To provide consulting services to the FCA Board for strategic planning	$53,000
Unify Corporation; 10-FCA-601-075 (SS)	To provide IT Consulting Services	$155,775
Brown & Co.; 10-FCA-700-001 (CCS)	To provide Financial Audit Review	$39,695
Informa Economics; 10-FCA-911-003 (SS)	Informa Economics Policy Report subscription	$6,000
Bloomberg; 10-FCA-911-001 (SS)	Bloomberg Data License	$24,000
Financial Information Systems Inc.; 10-FCA-911-004 (SS)	Subscription renewal	$16,000
Note: The Agency's SS and CCS contracts totaled $1,606,445 in FY 2010.		

TABLE 17. Competitive Consulting Service (CCS) Contracts of More Than $25,000 and Single Source (SS) Contracts, FY 2011

Contract	Purpose	Amount
McGraw Hill/Standard & Poor's; 11-FCA-450-001A (SS)	To provide Standard & Poor's online rating service	$46,431
A. Greenlee; 11-FCA-301-009 (SS)	To provide examination services	$40,000
A. Greenlee; 11-FCA-301-014 (SS)	Same as above; reimbursable work	$25,000
J. Weaver; 11-FCA-301-006 (SS)	Same as above	$103,000
J. Enzler; 11-FCA-301-004 (SS)	Same as above	$39,000
TJ Consulting; 07-FCA-C-02 Opt Yr 4 (SS)	Same as above	$24,725
J. Messing; 11-FCA-301-005 (SS)	Same as above	$36,000
A. Sartain; 11-FCA-301-010 (SS)	Same as above	$11,500
J. Garrison; 11-FCA-301-008 (SS)	Same as above	$130,000
S. Weisz Consulting; 11-FCA-301-011 (SS)	Same as above	$35,000
Russells Financial; 11-FCA-301-007 (SS)	Same as above	$80,000
R.Loewe 11-FCA-301-025 (SS)	Same as above	$12,500
Personnel Decision Research Institute; 10-FCA-C-01 (SS)	To assist in developing the pre-commission test	$67,925
Gartner Group; 11-FCA-601-001 (SS)	To provide premier membership for FCA staff in the Gartner Executive Program	$45,940
Ethos; 11-FCA-501-006- (SS)	To provide ethics review	$65,097
Modcomp 11-FCA-601-050 (SS)	Electronic Storage Management	$39,679
Murphy Brothers; 11-FCA-601-002 (SS)	To provide taxi services	$9,210
D. Redden; 11-FCA-601-008 (SS)	To provide retirement counseling	$36,300
ComPsych; 11-FCA-601- 006 (SS)	To provide employee assistance	$6,498
Powersolve; 10-FCA-601-11 (SS)	To provide maintenance	$22,393
Sybase; 11-FCA-601-041 (SS)	To provide PowerBuilder maintenance	$9,249
iFAR; 07-FCA-C-01, Option Year 3 (SS)	To provide consulting services to the Office of Secondary Market Oversight	$80,455
S. Guebert, 11-FCA-911-002 (SS)	Data Analysis	$24,000
SoftChoice; 10-FCA-601-069 Opt Yr 2 (SS)	Microsoft Enterprise Agreement	$156,103
Brown & Co.; 11-FCA-700-001 (CCS)	To provide Financial Audit Review	$40,947
Informa Economics; 11-FCA-911-053	Informa Economics Policy Report subscription	$12,000
Bloomberg; 11-FCA-450-002 (SS)	Bloomberg Data License	$43,560
Oliver Wyman, Inc.; 11-FCA-911-001 (CCS)	Consultant for FCS Merger	$172,500
Note: The Agency's SS and CCS contracts totaled $1,360,012 in FY 2011.		

Other Functions and Activities

Reception and Representation Expenditures
FCA spent $2,650 on reception and representation expenses in FY 2011.

Foreign Travel Expenditures
During FY 2011, no FCA Board members or employees traveled internationally on official business.

Reimbursements
FCA performs various examination, training, and other services for Federal agencies and is reimbursed for this work. The Agency is also reimbursed by the National Consumer Cooperative Bank (NCB) for examining the bank as mandated by 12 U.S.C. 3025. In FY 2011, the Agency performed the following services and was reimbursed as noted:

- USDA—examination, training, and other services; $482,493
- Farm Credit System Insurance Corporation (FCSIC)—examination, training, and other services; $425,032
- NCB—examination services; $302,286

Leveraging FCA Technology

The investments FCA has made in improving its communication technologies have enhanced employee productivity. Now the Agency is turning its focus to helping examiners and analysts acquire the data and tools they need to more proactively analyze and oversee the financial risks in the System. The Office of Management Services supports this goal by enhancing the Agency's ability to use technologies to perform its duties. This includes opening up new streams of financial data and providing the tools that allow employees to analyze and transform data into information to better perform their duties.

FCA continually evaluates new technologies to gain efficiencies in operations and has made significant progress in improving the capability of staff to work and communicate regardless of their location. The Agency maintains an IT infrastructure that delivers dependable, efficient, and secure access to data about the institutions it regulates; automates the exchange of data and information; and provides tools through which staff can effectively monitor and assess financial data and risk. FCA places special emphasis on continuous IT security and the integrity of the Agency's information systems. The Agency monitors and coordinates its IT investments through the annual Information Resources Management Plan.

FCA continually seeks to provide IT services, data sources, and communication tools that complement current technology and increase connectivity for the Agency's mobile workforce. A number of Agency-wide IT projects improved the Agency's capabilities in FY 2011:

- The Agency laptop workstation inventory reached the end of its three-year lifecycle. All Agency laptops were replaced with more powerful and reliable equipment to support FCA staff both in the office and in the field.

- Phase II of the FCS Loan Database project further expanded the loan portfolio data collected from FCS institutions. Improved data facilitate cross-institution analysis. New reports will be required to analyze the data and some standard queries will be developed.

This database will facilitate macroanalysis of System characteristics and trends and will enhance FCA's oversight of the System.

- To enhance its Associate Examiner Competency Evaluation System, FCA provided an application to document associate examiner competencies and progress as employees move through the Agency's associate examiner development process.

- By implementing SharePoint Search, FCA has effectively provided a cross-database index of Agency data. Now FCA staff members can easily locate data wherever it is stored—whether in a Lotus Notes database, a SharePoint site, or the Agency's external website.

- By replacing Agency BlackBerry smartphones with more robust smartphones, FCA has improved the ability of its staff to connect with the Agency's IT systems, including e-mail, calendars, and contacts. The new phones also offer more applications for meeting business needs. In addition, because of high-speed tethering and "hotspot" capabilities, the new smartphones allow employees to connect more easily to the Agency's network.

Several new IT projects are planned for FY 2012:

- The Applications Migration project continues to build on the 2008 Infrastructure Review and Workflow Integration project to ensure that the new infrastructure is being used in the most efficient and effective manner. The project requires that the applications be moved to the new infrastructure so that the licensing costs of the old application software (Lotus Notes and Oracle) can be eliminated and the capabilities of the new infrastructure can be integrated into FCA's custom applications.

- FCA will complete its implementation of e-mail archiving and e-discovery capabilities in FY 2012. This will help the Agency more efficiently and effectively manage the increasing amount of information stored in electronic format.

- Phase II of the FCS Loan Database project will proceed during FY 2012. We will continue to improve the quality of the loan data as well as to refine the collection process. In addition, we will build applications based on the loan data; these applications will improve the Agency's ability to detect and manage risk across the Farm Credit System.

- FCA will update its infrastructure hardware to provide effective, reliable technology services to our users. Upgrades will include replacement of out-of-lifecycle routers, switches, and servers. We will also enhance our storage area network to provide capacity for our expanding data repository.

- The Enterprise Document and Guidance (EDGe) initiative will be the central hub for the Office of Examination's oversight and examination program and the Agency's institution-related documentation system. It further leverages the Agency's technology investments and improves communication and coordination. The Agency's new infrastructure, which is built around the Microsoft Office suite of applications, will be used to create this new documentation and reporting program system.

- FCA will update its Call Reporting System (CRS) to ensure that relevant data are being captured and that new reporting requirements are being met.

Independent Auditing and Accountability

The Office of Inspector General contracted with the Department of the Treasury's Bureau of the Public Debt for Brown & Company CPAs, PLLC, (Brown & Co.) to perform the FY 2011 audit of FCA's financial statements. On November 7, 2011, Brown & Co. issued opinion letters relating to the audit of the Agency's financial statements for the FYs ended September 30, 2011 and 2010.

- First, Brown & Co. opined that the principal financial statements presented fairly, in all material respects, the financial position of FCA as of the FYs ended September 30, 2011 and 2010, in conformity with generally accepted accounting principles.

- Second, the auditor found no material weaknesses in internal control over financial reporting.

- Third, Brown & Co. noted no reportable instances of statutory or regulatory noncompliance that could have a direct and material effect on the determination of financial statement amounts.

FCA's Inspector General concurred with the auditor's opinion letters and stated that Brown & Co.'s work provided a reasonable basis for its opinions.

ENSURING SAFETY AND SOUNDNESS

The Agency's primary role is to ensure the safety and soundness of the Farm Credit System (FCS or System), including the Federal Agricultural Mortgage Corporation (Farmer Mac). The first section below, titled "The Farm Credit System," summarizes examination and supervisory activities performed for the banks, direct-lending associations, and service organizations of the FCS. Because the role of Farmer Mac is different from the rest of the System, we discuss Farmer Mac separately in the second section below. In addition, FCA provides examination and other services on a reimbursable basis to certain entities that are not part of the System. These activities are summarized in the third section below, titled "Other Entities."

FCA's examination and supervision responsibilities are carried out by staff located in five field offices. One field office is in the McLean, Virginia, headquarters; the other field offices are located in Bloomington, Minnesota; Dallas, Texas; Denver, Colorado; and Sacramento, California. FCA does not expect any changes in the field office structure in FY 2013.

The Farm Credit System

Statutory and Regulatory Requirements

The Farm Credit Act requires FCA to examine each FCS institution at least once every 18 months. FCA meets this requirement through a risk-based process of oversight and examination designed to maximize efficiency while addressing FCS risk effectively. To enable FCA to meet this statutory requirement, section 5.9(4) of the Farm Credit Act establishes the Agency's authority to require any reports it deems necessary from System institutions. FCA regulations include the following reporting requirements:

- Each FCS institution must prepare and file quarterly reports of condition and performance with FCA in accordance with 12 CFR 621.12. These reports provide detailed information on each institution's financial performance, portfolio quality, and other relevant information.

- The Federal Farm Credit Banks Funding Corporation must prepare consolidated FCS information and make this information available to the public in accordance with 12 CFR 630.4.

System institutions submit other data to FCA through the Agency's Consolidated Reporting System; some of the information submitted through this system is available to the public on FCA's website (www.fca.gov). FCA also collects loan data for all System institutions through the Loan Account Reporting System. In fact, FCA has undertaken a project to expand its collection of loan data to allow for more extensive evaluations of FCS systemic risk exposures. The information FCA collects from the FCS is essential to the Agency's ability to monitor the System's safety and soundness.

In addition to overseeing and examining the FCS, FCA establishes policies and regulations to ensure that the System addresses key risk areas. For example, FCA regulations require FCS institutions to have effective loan underwriting and loan administration processes, to provide strong asset-liability management, and to establish high standards for governance and transparent disclosures for shareholder oversight.

Risk-Based Examination and Supervision

FCA designs examination and supervision processes to address material risks and emerging issues on an individual-institution and Systemwide basis. The Agency bases its examination and supervision strategies on institution size, existing and prospective risk exposure, and the scope and nature of each institution's business model. In evaluating each institution's business model, FCA must ensure that the institution fulfills its public mission as a Government-sponsored enterprise. In addition to overseeing and examining individual institutions, FCA also identifies and evaluates Systemwide emerging risk and allocates examination resources to matters of highest priority and potential risk.

FCA has developed a comprehensive regulatory and supervisory framework to promote and help ensure the System's safety and soundness. This approach recognizes each institution's responsibility and ability to identify and manage both institution-specific and systemic risks. FCA's examination and supervision program promotes accountability in FCS institutions for their programs, policies, procedures, and controls, thereby providing the necessary framework for institutions to identify and manage risks. FCS institutions have developed effective risk-management cultures in response to FCA's examination and supervision programs and its policies and regulations. These programs, policies, and regulations continue to set high standards for the System.

Because of the recent unprecedented volatility in the agricultural and credit markets, as well as significant changes in the financial markets, guarding the safety and soundness of the FCS is more important and more challenging than ever. As a tool to help address these challenges, FCA incorporates national risk topics into the oversight and examination program to set examination priorities, identify potential regulatory issues, allocate resources, and evaluate emerging risk exposures. The oversight and examination program includes strategies for addressing these emerging risks and communicating the Agency's expectations to both internal and external audiences. National risk topics for 2013 include risk associated with managing institution loan portfolios, management of collateral risk, and systemic risks affecting borrower profitability and repayment capacity.

When FCA examiners identify unsafe and unsound practices within a System institution or find that an institution has failed to comply with a law or regulation, the Agency outlines the corrective actions the institution must take in a Report of Examination or other form of communication. If necessary, FCA will use its enforcement powers to effect changes in an institution's policies and practices to correct unsafe or unsound conditions or violations of law or regulations. However, in most cases, FCA achieves corrective action without the use of enforcement powers.

Measuring the Safety and Soundness of the System

The Agency uses the Financial Institution Rating System (FIRS) as a key method to assess the safety and soundness of each FCS institution. The FIRS provides a general framework, consisting of component and composite ratings, for evaluating and assimilating all significant financial, asset quality, and management factors. Similar to systems used by other Federal financial regulators, the FIRS evaluates six key component areas to properly assess the degree of risk in an institution. These key component areas are capital, assets, management, earnings, liquidity, and sensitivity (CAMELS). On the basis of its CAMELS ratings, FCA assigns an overall composite rating for the institution. The rating system ranges from 1 to 5. A composite rating of 1 indicates that an institution is sound in every respect and that it exhibits the strongest performance and risk management practices, whereas a rating of 5 represents an extremely high, immediate, or near-term probability of failure.

Examiners continually evaluate institutional risk and regularly review and update FIRS ratings to reflect current risks and conditions in each FCS institution. The Agency maintains guidance on both quantitative benchmarks and qualitative factors to help examiners apply the FIRS process consistently. FCA discloses these confidential FIRS composite and component ratings to the institution's board and management to provide perspective on relative safety and soundness. Examination reports and other forms of communication also provide the institution's board with an assessment of the governance, management, quality of assets, and financial condition and performance of the institution.

Examiners supplement the FIRS with a risk assessment tool that focuses on identifying prospective risks. The tool assesses the following emerging risk areas: credit, interest rate, liquidity, operations, compliance, strategic, and reputation.

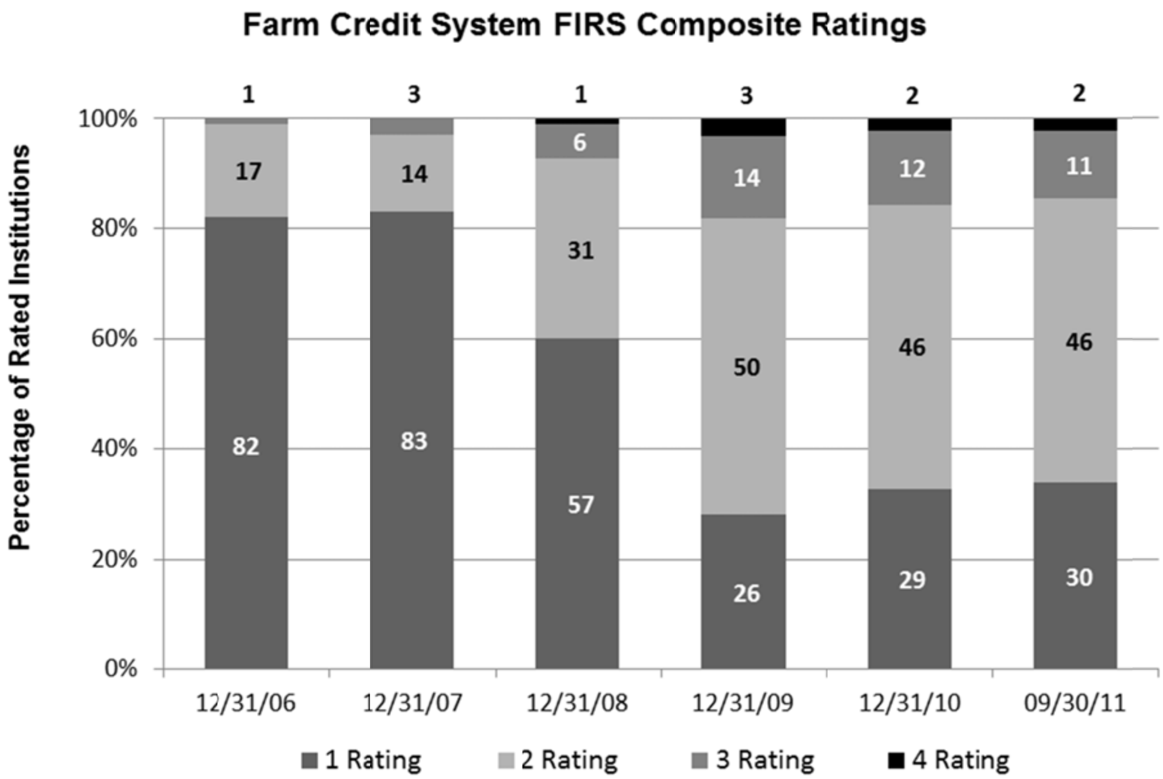
Recent Results

As the composite FIRS ratings over the past several years show, the System's condition and performance have remained satisfactory, but the overall risk profile remains weakened. The following summarizes FIRS ratings for System banks and associations as of September 30, 2011:

- Thirty institutions were rated 1.
- Forty-six were rated 2.
- Eleven were rated 3.
- Two were rated 4.

See figure 2 for FIRS rating trend information. For a more detailed discussion of the financial condition and performance of the System, see part III of this report.

Figure 2



Source: FCA's FIRS Ratings Database.

Note: This chart reflects ratings for only the System's banks and direct-lending associations; it does not include ratings for the System's service corporations, Farmer Mac, or the Federal Farm Credit Banks Funding Corporation. Also, the numbers shown on the bars reflect the total number of institutions with a given rating; please refer to the vertical axis to determine the percentage of institutions receiving a given rating.

Federal Agricultural Mortgage Corporation

FCA, through its Office of Secondary Market Oversight (OSMO), examines and supervises Farmer Mac to ensure both its safety and soundness and its mission achievement. OSMO performs annual CAMELS-based examinations—that is, examinations based on capital, assets, management, earnings, liquidity, and sensitivity. Throughout the year, OSMO reviews Farmer Mac's condition and its compliance with risk-based capital regulations, and supervises its operations.

Statutory Authority

Farmer Mac is regulated by FCA through OSMO, which was established in 1992 by the Food, Agriculture, Conservation, and Trade Act Amendments of 1991 (Public Law 102-237). OSMO provides for the examination and general supervision of Farmer Mac's safe and sound performance of its powers, functions, and duties. The statute requires that OSMO constitute a separate office reporting to the FCA Board and that its activities, to the extent practicable, be carried out by individuals not responsible for supervising the banks and associations of the FCS.

Data Reporting Requirements

Farmer Mac is required to submit quarterly Call Reports to OSMO in addition to meeting several other periodic reporting requirements related to Farmer Mac's regulatory risk-based capital, mission, liquidity, and financial derivatives portfolio. In addition, Farmer Mac is subject to the disclosure and reporting requirements of the Securities and Exchange Commission.

Financial Condition and Performance

Farmer Mac's financial condition and performance trends were generally positive in FY 2011.

- Net income available to common shareholders was $13 million for the 12 months ended September 30, 2011, compared with $15.1 million during FY 2010.
- Core earnings, a non-GAAP measure of economic performance, totaled $35.9 million during FY 2011 compared with $24.0 million during FY 2010.
- Farmer Mac's core capital totaled $461 million at the end of FY 2011, compared with $448 million at the end of FY 2010. The minimum core capital requirement for Farmer Mac's on- and off-balance-sheet exposures is set in the statute and totaled $337 million at the end of FY 2011. Thus, Farmer Mac exceeded its minimum core capital requirement by approximately $125 million.
- At the end of FY 2011, Farmer Mac had $479 million in regulatory capital available to meet the $111 million minimum requirement established by FCA's Risk-Based Capital (RBC) Model.

Farmer Mac experienced growth in its program and nonprogram portfolios during FY 2011.

- Program activity increased approximately 3 percent and ended FY 2011 at $11.8 billion.
- Cash and nonprogram investments increased approximately 43 percent and ended FY 2011 at $2.7 billion.

Credit quality generally improved though problems in permanent planting and ethanol industries persisted. Farmer Mac experienced a significant decline in REO over FY 2010; this decline was driven largely by resolution and liquidation of ethanol plant properties. By comparison, REO was relatively stable over FY 2011, finishing the year at $3.9 million, up approximately $500,000 from fiscal year-end 2010.

Risk-Based Capital (RBC) Model

Section 8.32 of the Farm Credit Act requires the RBC Model to estimate credit losses on agricultural mortgages owned or guaranteed by Farmer Mac. The rate of loan default and severity of losses must be reasonably related to the default rate and severity of losses experienced in contiguous areas of the United States; the contiguous areas considered must contain at least 5 percent of the total U.S. population that experienced the highest rate of default and severity of agricultural mortgage losses during the past two consecutive years or more. The Farm Credit Act also requires the RBC Model to incorporate an interest rate risk stress scenario based on rising and falling interest rates on Treasury obligations of various terms. In addition, the act requires Farmer Mac to maintain capital to protect against management and operational risks. This additional capital must amount to 30 percent of the sum of the credit loss and interest rate risk components of the RBC Model.

The output of the stress test depends on Farmer Mac's risk profile. High-risk loan assets or significant interest rate risk exposure causes the RBC Model to calculate a higher regulatory capital requirement. Conversely, if Farmer Mac maintains a low risk profile in both its loan portfolio and interest rate risk exposure, the stress test will calculate a low capital requirement. FCA regulations require Farmer Mac to have its operation of the RBC Model validated by an independent third party at least every three years. In all such third-party validations, Farmer Mac has been found to be operating the model appropriately.

In May 2008, the Food, Conservation and Energy Act of 2008 (2008 Farm Bill) expanded Farmer Mac's program authorities by allowing it to purchase and guarantee securities backed by rural utility loans made by cooperatives. Farmer Mac is authorized to use these new authorities, along with existing authorities, to provide liquidity to agricultural mortgage lenders and other rural utility cooperative lenders. The Agency published a final rule in early 2011 to amend the regulation to allow for revisions to the model, including a revision that would reflect loan activity involving rural utility cooperatives. An Advance Notice of Proposed Rulemaking was published in June 2011, to solicit public input on further revisions to the model.

Other Entities

On a reimbursable basis, FCA performs examinations of certain entities that are not part of the Farm Credit System.

- As mandated by 12 U.S.C. 3025, FCA examines the National Consumer Cooperative Bank (NCB). NCB, which also owns a Federal savings bank, is chartered by Congress and specializes in non-agriculture cooperative loans.

- The U.S. Department of Agriculture (USDA) contracts with FCA to provide examination services for specific programs USDA administers. The amount of resources dedicated to providing these services is reviewed annually and is currently very limited because of the Agency's need to focus its resources on increased oversight of the FCS.

The Agency also provides services on a reimbursable basis to the Farm Credit System Insurance Corporation, an independent, Government-controlled corporation that insures the timely payment of principal and interest on certain System notes, bonds, and other obligations issued to investors.

DEVELOPING REGULATIONS AND POLICIES

FCA routinely issues regulations, policy statements, and other guidance to ensure that the System complies with the law, operates in a safe and sound manner, and efficiently carries out its statutory mission.

The Agency's regulatory philosophy articulates FCA's commitment to provide a flexible regulatory environment that allows the System to offer high-quality, reasonably priced credit and related services to farmers and ranchers, their cooperatives, rural residents, and other entities on which farming operations depend. As a result of this commitment, FCA strives to develop balanced, well-reasoned, and flexible regulations, always taking into account the benefits and costs of these regulations to System institutions. FCA's objectives are to ensure that the System's activities remain consistent with the law and safety and soundness principles and to encourage participation by member-borrowers in the management, control, and ownership of their institutions.

Regulatory and Policy Projects Active at End of FY 2011

The FCA Board periodically reviews its regulatory agenda to evaluate progress on open projects and to determine the need for additional initiatives to implement statutory changes or to address other regulatory issues. The FCA Board-approved agenda is part of the Federal Unified Agenda, which is published online at www.reginfo.gov. FCA is not obligated to act on its agenda items, and it may propose or promulgate regulations that have not been set forth in the Unified Agenda. The Agency's Regulatory Performance Plan is published on the FCA website to notify the public of its upcoming regulatory actions and to encourage the public to participate in the regulatory process.

The following list summarizes the Agency's current regulatory efforts and other guidance under consideration in FY 2012.

<u>Operating and Strategic Business Planning</u>: The FCA Board plans to act on a **final rule** that would enhance guidance to FCS institutions related to their operating and strategic business plans. The rule would require the plans to address service and outreach to creditworthy borrowers in all marketplace segments and to give appropriate consideration to diversity in both the workforce and the marketplace.

<u>Liquidity and Funding</u>: The FCA Board plans to act on a **final rule** to ensure that FCS funding and liquidity requirements are safe, sound, and appropriate. The rulemaking would revise regulations to ensure that the discounts applied to investments reflect marketability in volatile financial markets and economic conditions. It would also help ensure that FCS funding is appropriately controlled and flexible enough to raise the capital and funds needed to meet the System's mission in a safe and sound manner.

<u>Rural Community Investments</u>: The FCA Board plans to act on both a **notice of proposed rulemaking** and on a **final rule** to provide guidance on System institutions' statutory and regulatory authority related to rural community investments. The rulemaking would address investments in rural community essential facilities and infrastructure projects involving Federal and State agencies, other rural lenders, and Rural Business Investment Companies licensed by USDA.

<u>Margin and Capital Requirements for Noncleared Swaps</u>: The FCA Board plans to act on an interagency **final rule** that would establish margin and capital requirements for FCS institutions, including Farmer Mac, that engage in noncleared swaps and noncleared security-based swap

transactions. The rulemaking would fulfill a requirement of the Dodd-Frank Wall Street Reform and Consumer Protection Act.

Standards of Conduct: The FCA Board plans to act on both a **notice of proposed rulemaking** and on a **final rule** to clarify and strengthen existing standards-of-conduct regulations. Among other things, the rulemaking would address director fiduciary duties.

Investment Management: The FCA Board plans to act on a **final rule** to revise regulations relating to investment assets. The rule would ensure that prudent practices are in place for the safe and sound management of investment portfolios. As part of the rulemaking, conditions for divestiture also would be reviewed.

Farmer Mac—Investments and Liquidity Management: The FCA Board plans to act on both a **notice of proposed rulemaking** and a **final rule** to consider changes to regulations relating to Farmer Mac's liquidity investment operations. These rulemaking actions will produce guidance on diversification, eligible investment types, and purchase and divestiture procedures.

Limited Liability Subsidiaries of FCS Institutions: The FCA Board plans to act on both a **notice of proposed rulemaking** and a **final rule** that would govern the parameters under which an FCS institution may organize or invest in LLCs, LLPs, and other unincorporated business entities.

Compensation, Retirement Programs, and Related Benefits: The FCA Board plans to act on both a **notice of proposed rulemaking** and a **final rule** to consider regulatory changes addressing disclosure and compliance requirements for executive compensation, pension, and other benefit programs in the System.

Loan Portfolio Data Submissions—Common Identifier: The FCA Board plans to act on a **notice of proposed rulemaking** to consider FCA's minimum data needs for evaluating shared-asset risk in FCS loan portfolios. The rulemaking would propose using a common loan identifier or other alternative.

Mergers of Banks and Associations: The FCA Board plans to act on a **notice of proposed rulemaking** to amend FCA's requirements for FCS bank and association mergers and consolidations.

Capital Adequacy—Capital Components; Basel Accord Tier 1/Tier 2: The FCA Board plans to act on a **notice of proposed rulemaking** to replace FCA's current core and total surplus capital standards with a "Tier 1/Tier 2" capital framework that is more consistent with the Basel Accord and more closely aligned with that of the Federal Financial Regulating Authorities. The proposed rulemaking also would consider establishing a leverage ratio for System institutions.

Capital Adequacy—Risk Weighting: The FCA Board plans to act on a **notice of proposed rulemaking** to establish a new risk-based capital framework based on the standardized approach for credit risk under the Basel Accord.

Investments in Rural America: FCA staff plans to complete its review and evaluation of the pilot programs through which some System institutions have pursued partnerships and investments. Through the review, FCA seeks to determine whether such programs help increase the availability of funds to agriculture and rural America. For more information about Investments in Rural America, see page 49.

Loan Portfolio Data Submissions: FCA staff plans to complete its review on establishing data needs for determining risk in FCS loan portfolios, including sufficiency of data to evaluate shared assets and collateral risk.

Review Agency Lending Guidance: FCA staff plans to begin reviewing and considering changes to policy guidance for providing credit and related services to all eligible creditworthy agricultural producers in an institution's chartered territory. This review will include identifying any barriers to efficiently and cost-effectively providing credit for newer products and marketing systems such as local foods and organic agriculture.

Review Agency Young, Beginning, and Small Farmer (YBS) Guidance: FCA staff plans to begin reviewing and considering further policy guidance for YBS lending. This review will consider the role of banks in supporting association YBS lending and will evaluate alternative means of measuring YBS lending efforts and results.

Update Generally Accepted Accounting Principles (GAAP) References and Other Conforming Amendments: FCA staff plans to begin reviewing FCA's regulations to identify regulations that need to be updated to reflect changes that the Accounting Standards Codification has made to GAAP.

Regulatory and Policy Projects Completed in FY 2011 and Early FY 2012

The following list identifies projects that were completed in FY 2011, along with a description of communications that were recently issued to System institutions to clarify FCA's rules.

Lending and Leasing Limits and Risk Management: The FCA Board adopted a **final rule** to revise the existing lending and leasing limit regulations to ensure that appropriate safety and soundness guidance is in place to limit Systemwide credit exposure to a single borrower/entity. In addition, the rulemaking provides policy guidance to limit exposure to loan portfolio concentrations by industry segment, repayment source, and other factors.

Loan Purchases from the Federal Deposit Insurance Corporation (FDIC): The FCA Board adopted a **final rule** to amend its regulations to permit System institutions to purchase eligible agricultural loans from the FDIC.

Farmer Mac Risk-Based Capital Stress Test, Version 4.0: The FCA Board adopted a **final rule** to revise the Farmer Mac Risk-Based Capital Model to include rural utility loan volume as program business. The rule is in response to provisions of the 2008 Farm Bill that authorize Farmer Mac to invest in securities representing interests in rural electric and telephone cooperatives.

Operating and Strategic Business Planning: The FCA Board published a **notice of proposed rulemaking** that would enhance guidance to FCS institutions related to their operating and strategic business plans. The rulemaking would require plans to address service and outreach to creditworthy borrowers in all marketplace segments and to give appropriate consideration to diversity in both the workforce and the marketplace.

Interagency Questions and Answers Regarding Flood Insurance: The FCA Board acted on an interagency **notice and request for comment** on questions and answers related to loans in areas having special flood hazards. The guidance helps financial institutions meet their responsibilities under Federal flood insurance legislation and helps increase public understanding of flood insurance regulations.

Liquidity and Funding: The FCA Board published a **notice of proposed rulemaking** to revise regulations to ensure that FCS funding and liquidity requirements are safe, sound, and appropriate. The rulemaking would help ensure that the discounts applied to investments reflect marketability in volatile financial markets and economic conditions and that FCS funding is appropriately controlled and flexible enough to raise the capital and funds needed to meet the System's mission in a safe and sound manner.

Margin and Capital Requirements for Noncleared Swaps: The FCA Board published an interagency **notice of proposed rulemaking** that establishes margin and capital requirements for FCS institutions, including Farmer Mac, that engage in noncleared swaps and noncleared security-based swap transactions. The rulemaking addresses a requirement of the Dodd-Frank Act.

Investment Management: The FCA Board published a **notice of proposed rulemaking** to revise regulations relating to investment assets to ensure that prudent practices are in place for the safe and sound management of investment portfolios. As part of the rulemaking, conditions for divestiture also are being considered.

Farmer Mac Risk-Based Capital Stress Test, Version 5.0: The FCA Board published a **notice of proposed rulemaking** to revise the Risk-Based Capital Stress Test to eliminate fields requiring credit ratings data. This change would bring the test into compliance with a provision of the Dodd-Frank Act. This rulemaking action would also revise Farmer Mac's operational and strategic planning regulations to address diversity and inclusion.

Capital Adequacy—Risk Weighting: The FCA Board published a **notice of proposed rulemaking** to amend its regulations to remove references to credit ratings as required by the Dodd-Frank Act.

Joint and Several Liability Debt-Based Reallocation Agreement: The FCA Board published a **notice of approval** of the Joint and Several Liability Reallocation Agreement among the five System banks and the Federal Farm Credit Banks Funding Corporation.

Ethics, Independence, Arm's Length Role, Ex Parte Communications and Open Government: The FCA Board adopted **Policy Statement** FCA-PS-81, Ethics, Independence, Arm's Length Role, Ex Parte Communications and Open Government, which reaffirms the Board's commitment to the ethics laws and regulations, its avoidance of ex parte communications in its judicial and rulemaking roles, its commitment to open Government, and its role as an independent, arm's length safety and soundness regulator.

Off-Exchange Retail Foreign Currency Transactions: FCA staff completed its review of the current FCA foreign exchange rules to determine if changes are necessary to implement provisions of the Dodd-Frank Act relating to off-exchange retail foreign currency transactions.

Farm Credit System Investment Asset Management: FCA issued a **Bookletter** (BL-064) to clarify FCA's regulations and expectations regarding investment asset management. It addresses the key elements of a robust investment asset management framework.

Information and Guidance for Registering Mortgage Loan Originators Under the Secure and Fair Enforcement for Mortgage Licensing Act of 2008: FCA issued an **Informational Memorandum** to address the registration of residential mortgage loan originators employed by System associations.

Loan Underwriting Standards: FCA issued an **Informational Memorandum** to convey FCA's expectations regarding the collection of borrower financial information and the impact of this information on loan underwriting standards.

USDA Guaranteed Investments: FCA issued an **Informational Memorandum** to reiterate and clarify that System institutions have broad authority to invest in obligations (including loans and bonds) that are fully insured or guaranteed by the USDA and its agencies.

Accounting and Disclosure of Troubled Debt Restructurings: FCA issued an **Informational Memorandum** to provide guidance to System institutions on complying with Financial Accounting Standards Board Accounting Standards Codification (ASC) subtopic 310-40, Troubled Debt Restructurings by Creditors, and ASC subtopic 470-60, Troubled Debt Restructurings by Debtors. This Informational Memorandum also provides guidance on disclosing troubled debt restructurings in reports to shareholders.

Nominating Committee Brochures: FCA issued an **Informational Memorandum** to remind System institutions of the important role that nominating committees play in the election of boards of directors.

Serving the Members of Farm Credit System Institutions: FCA issued an **Informational Memorandum** to notify System institutions that the FCA Board had adopted Policy Statement FCA-PS-80, Cooperative Operating Philosophy—Serving the Members of Farm Credit System Institutions. The Policy Statement reaffirms FCA's commitment to System members' participation in their institutions.

Board Resolution on Cooperative Operating Philosophy: The FCA Board adopted a **resolution** to reaffirm its commitment to the cooperative business model and the cooperative structure and principles of System banks and associations.

Preferred Risk Policy Eligibility Extension: FCA issued an **Informational Memorandum** to notify System institutions that Preferred Risk Policy eligibility will be extended for two years beginning January 1, 2011, or the effective date of the flood map revision, whichever is later, for all policies covering buildings newly mapped within a Special Flood Hazard Area by a flood map revision effective on or after October 1, 2008.

Maximum Bank Director Compensation: FCA issued an **Informational Memorandum** to notify Farm Credit banks of the maximum allowable bank director compensation for 2011.

FCS Corporate Activity and Other Prior Approvals and Clearances

In accordance with the Farm Credit Act and FCA regulations, FCA issues prior approvals for corporate and noncorporate applications. Corporate applications include requests from FCS institutions for FCA to issue new or amended charters, as well as to cancel charters because of mergers, consolidations, liquidations, or termination of System status. Noncorporate applications include requests related to preferred stock and subordinated debt offerings and requests for prior approval of funding, mission-related investments, and any new financially related services.

Corporate Activities in FY 2011 and Early FY 2012

During FY 2011, FCA canceled the charters of nine associations—three ACAs and six subsidiaries—as a result of three separate mergers.

1. On November 1, 2010, one ACA affiliated with the Farm Credit Bank of Texas moved its headquarters.

2. On December 1, 2010, two ACAs affiliated with the Farm Credit Bank of Texas merged, resulting in a single ACA with subsidiaries.

3. On January 1, 2011, three ACAs affiliated with AgFirst Farm Credit Bank merged, resulting in a single ACA with subsidiaries.

Thus far in FY 2012, FCA has issued charters for a Farm Credit Bank and a service corporation and has canceled the charters of three associations—one ACA and two subsidiaries—as a result of a merger.

1. On December 12, 2011, a Farm Credit Bank was chartered as a subsidiary of CoBank, ACB.

2. On January 1, 2012, U.S. AgBank, FCB, and CoBank, ACB, merged.

3. On January 1, 2012, two ACAs affiliated with U.S. AgBank, FCB, merged, resulting in a single ACA with subsidiaries.

4. On January 1, 2012, a new service corporation was chartered.

Projected Mergers and FCS Institution Size

As of January 1, 2012, the System had 83 direct-lender associations and 4 banks. Eight service corporations and special-purpose entities (see pages 55 and 56) brought the total number of FCS institutions to 95 (including Farmer Mac). Because of mergers and consolidations, the number of FCS associations has declined 49 percent since 2000, and the number of FCS banks has decreased almost 30 percent.

Although merger activity has slowed in recent years, the Agency estimates that over time the number of direct-lender associations will continue to decline. These mergers, coupled with asset growth, will increase the size of System entities. The average association already exceeds $1 billion in total assets. System institutions will also possess more complex management systems and offer a broader range of financial services to their borrowers.

Security Offerings During FY 2011

The Agency began a review of the proposed offering of AgFirst Farm Credit Bank for the issuance of Class B Noncumulative Perpetual Fixed-to-Floating Rate Subordinated Preferred Stock, Series 2, for sale and transfer to qualified institutional buyers or accredited investors.

Funding Activity

The FCS raises funds for loans and investments primarily by the sale of Systemwide debt securities through the Federal Farm Credit Banks Funding Corporation,[3] the fiscal agent for the Farm Credit banks. In this way, funds flow from worldwide capital-market investors to agricultural producers, agricultural cooperatives, and rural communities, providing them with ready and efficient access to global resources. Systemwide debt securities are issued as discount notes, master notes, bonds, or designated bonds. As required by the Farm Credit Act, the System must obtain FCA approval for all debt issuances.

For the 12 months ended September 30, 2011, the FCS issued $420 billion in Systemwide debt, which was substantially less than the $511 billion issued during FY 2010 and the $506 billion issued during FY 2009. The decrease in Systemwide debt issuance was driven by the decrease in the use of discount notes. Because yields on longer-term debt instruments were similar, less issuance activity was necessary.

The financial markets continued to experience volatility, but investor demand for System debt remained favorable across the yield curve. Because of the combination of market volatility and low interest rates, the System was able to exercise the options on significant quantities of callable bonds to further reduce the cost of funds.

FCA continued to ensure that the System had the necessary flexibility to raise funds. During the volatility in 2010 and 2011, FCA took several significant actions to help the System issue debt. For example, in November 2010, the Agency approved a retail bond program that allowed the System to issue bonds to small investors. This program has enabled the System to broaden its investor base.

Divestiture Plans for Ineligible Investments

As a result of the unfavorable market conditions relating to the current residential home mortgage lending crisis, certain investment securities that had been eligible when the System purchased them later became ineligible. FCA regulations require System institutions to divest themselves of ineligible nonprogram investments within six months unless FCA approves a plan that authorizes the institution to dispose of the investments over a longer period of time. During FY 2011, FCA approved the divestiture plans for eight ineligible investments. Thus far during the first quarter of FY 2012, FCA has approved the divestiture plans for three ineligible investments and is reviewing two approval requests.

Investments in Rural America

In January 2005, FCA issued guidance that gave System institutions an opportunity to participate in pilot programs supporting investments in rural America (see FCA Informational Memorandum dated January 11, 2005, Investments in Rural America—Pilot Investment Programs). The pilot programs are intended to provide FCS institutions greater flexibility to partner with Government agencies and other agricultural and rural lenders in fulfilling FCS mission objectives. In addition, FCA expects to gain a better understanding of the diverse financing needs of agriculture and rural communities and the ways FCS institution investments can help increase the availability and efficiency of funds to these markets.

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[3] See section 4.9 of the Farm Credit Act. The Federal Farm Credit Banks Funding Corporation's primary function is to issue, market, and handle debt securities on behalf of the System banks. In addition, the Funding Corporation assists the System banks with a variety of asset/liability management and specialized funding activities. Headquartered in the greater New York City area, the Funding Corporation is responsible for the System's financial disclosure and the release of public information concerning the financial condition and performance of the System as a whole.

Since initiating this pilot investment program, FCA has approved 10 applications from FCS banks, associations, and districts to initiate pilot programs to make specific investments in rural America. In addition, FCA has placed a number of controls on these pilot investment programs to ensure their safety and soundness and mission focus. Examples of investments made under these pilot programs include investments in rural housing mortgage securities, essential rural community facilities, and rural infrastructure.

In FYs 2012 and 2013, no additional applications for pilot programs are expected because most institutions are now operating under programs authorized by FCA, although specific requests for individual investments may continue. Also, FCA will continue to examine and supervise these investments, enhance reporting processes, and evaluate the types of investments being made and their benefits to agriculture and rural America.

As of September 30, 2011, FCS institutions held approximately $1.5 billion in investments under approved pilot programs. These investments included $744 million in rural housing mortgage-backed securities (RHMS). The rural housing loans backing the RHMS must be conforming first-lien residential mortgage loans originated by non-System lenders in “rural areas” (as defined by the Farm Security and Rural Investment Act of 2002) or eligible rural housing loans originated by System lenders under FCA regulations. This program helps provide additional liquidity for rural housing loans, resulting in more cost-effective credit to rural homeowners by providing economic incentives to lenders to create RHMS for sale in the secondary market. FCS institutions also held $712 million in rural development debt securities. The proceeds of these investments helped fund essential community facilities, such as critical-access hospitals and schools, and basic infrastructure needed for economic development. FCS institutions also held $17 million in other investments primarily related to agriculture under their pilot program authorities.

Part III

FARM CREDIT SYSTEM

PROFILE OF THE FARM CREDIT SYSTEM

The Farm Credit System consists of a network of borrower-owned cooperative financial institutions, as well as related service organizations and the Federal Agricultural Mortgage Corporation (Farmer Mac). The Farm Credit System was created by Congress in 1916 to provide American agriculture with a dependable source of credit. It is the oldest of the financial Government-sponsored enterprises (GSEs). As of January 1, 2012, the System had four banks providing loan funds to

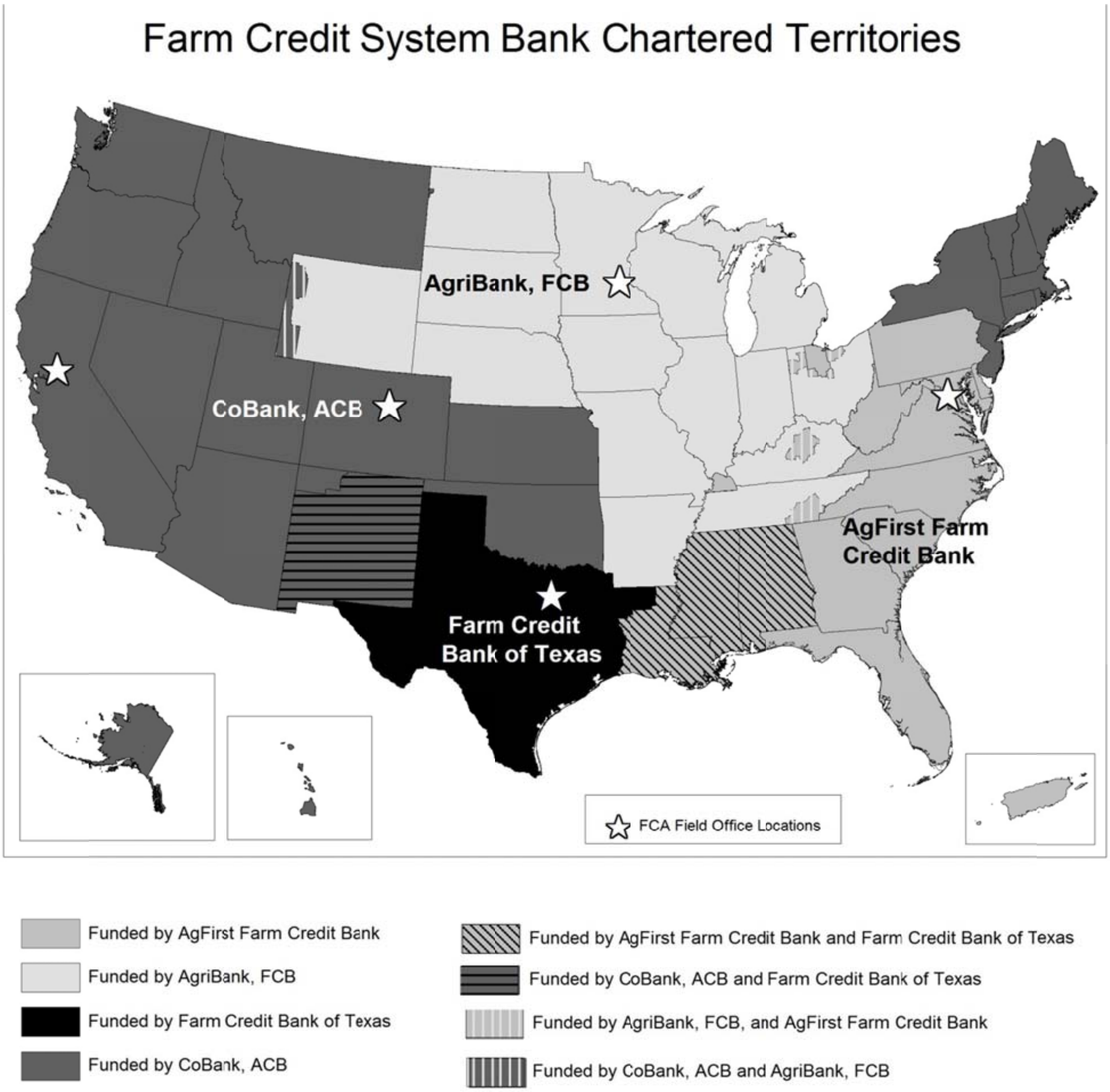
- 80 Agricultural Credit Association (ACA) parent organizations, each of which has two subsidiaries—a Production Credit Association (PCA) and a Federal Land Credit Association (FLCA), and
- 3 stand-alone FLCAs.

The map in figure 3 shows each bank's chartered territory.

Although legally separate, the ACA and its PCA and FLCA subsidiaries operate as an integrated lending business, with loans made through the subsidiaries appropriate to the authority of each subsidiary. The ACA, the PCA, and the FLCA are jointly and severally liable for the full amount of the indebtedness to the funding bank under a General Financing Agreement. In addition, the parent company and its subsidiaries pledge their respective assets as security for each other's debts and obligations and share each other's capital. The three associations have a common board and management and a common set of shareholders. Under the Farm Credit Act, FLCAs originate long-term agricultural mortgages and are exempt from Federal and State income taxes; ACAs and PCAs originate short- and intermediate-term operating loans and are not tax-exempt.

System institutions provide credit and financially related services to farmers, ranchers, producers or harvesters of aquatic products, and farmer-owned cooperatives. Institutions also make loans for agricultural processing and marketing activities; rural housing; certain farm- related business, agricultural, and aquatic cooperatives; rural utilities; and foreign and domestic entities in connection with international agricultural trade. The System raises its loan funds by selling securities in the national and international money markets; these securities are subject to FCA's approval, but they are not guaranteed by the U.S. Government.

Figure 3



NOTE: CoBank, ACB, funds 29 associations in the indicated areas and serves cooperatives nationwide; Farm Credit Bank of Texas funds 17 associations; AgriBank, FCB, funds 17 associations; and AgFirst Farm Credit Bank funds 20 associations. The Farm Credit System contains a total of 87 banks and associations.

Additional System Entities and Service Corporations

In addition to the System's banks and associations, the Agency is responsible for regulating and examining the Federal Agricultural Mortgage Corporation (Farmer Mac) and the Federal Farm Credit Banks Funding Corporation. FCA also regulates and examines the six service corporations organized under section 4.25 of the Farm Credit Act[4]: AgVantis, Inc.; Farm Credit Finance Corporation of Puerto Rico; Farm Credit Leasing Services Corporation; Farm Credit Financial Partners, Inc.; the FCS Building Association (FCSBA); and Farm Credit Foundations.

Federal Agricultural Mortgage Corporation—Farmer Mac[5] is a stockholder-owned, federally chartered instrumentality of the United States created in 1988 to establish a secondary market for agricultural real estate and rural housing mortgage loans. In May 2008, the Food, Conservation, and Energy Act of 2008 (2008 Farm Bill) expanded Farmer Mac's program authorities by allowing it to purchase and guarantee securities backed by rural utility loans made by cooperatives. Farmer Mac conducts its business primarily through two core programs: Farmer Mac I and Farmer Mac II. Under the former, Farmer Mac purchases, or commits to purchase, qualified loans or obligations backed by qualified loans that are not guaranteed by any instrumentality or agency of the United States. Under the latter, Farmer Mac purchases the guaranteed portions of farm ownership and farm operating loans, rural business and community development loans, and certain other loans guaranteed by USDA.

Federal Farm Credit Banks Funding Corporation—The Funding Corporation is owned by System banks; it markets the debt securities that the banks sell to raise funds for loans and other purposes. System institutions obtain the majority of their funds through the sale of these securities in the Nation's capital markets. These securities, chiefly in the form of bonds and discount notes, are offered by the Funding Corporation through a nationwide group of securities dealers and dealer banks. The Funding Corporation's debt issuance programs provide the System banks with funding to process loans to farmers, ranchers, and agricultural cooperatives; debt issuances also provide the banks with funding for their other operations.

AgVantis, Inc.—AgVantis, Inc., provides technology-related and other support services to associations in the CoBank, ACB, district. It was chartered by FCA in 2001 and is owned by CoBank, ACB, and 18 of its affiliated associations.

Farm Credit Finance Corporation of Puerto Rico—The Farm Credit Finance Corporation of Puerto Rico used tax incentives offered to investors to provide low-interest funding (other than that from the Funding Corporation) to Puerto Rico Farm Credit, ACA. Because of changes in the tax treatment of the corporation, AgFirst Farm Credit Bank, the corporation's sole owner, suspended its operations as of December 31, 2005. However, the corporation's charter remains outstanding.

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[4] Section 4.25 of the Farm Credit Act provides that one or more FCS banks or associations may organize a service corporation to perform functions and services on their behalf. These federally chartered service corporations are prohibited from extending credit or providing insurance services.

[5] Farmer Mac is established in law as a part of the FCS. However, Farmer Mac has no liability for the debt of any other System institution, and the other System institutions have no liability for Farmer Mac's debt. Farmer Mac is organized as an investor-owned corporation, not a member-owned cooperative. Investors in voting stock may include commercial banks, insurance companies, other financial organizations, and FCS institutions. Nonvoting stock may be owned by any investor. Farmer Mac is regulated by FCA through the Office of Secondary Market Oversight. The OSMO Director reports directly to the FCA Board on matters of policy.

Farm Credit Leasing Services Corporation—The Leasing Corporation, owned by CoBank, ACB, provides equipment leasing services to eligible borrowers, including agricultural producers, cooperatives, and rural utilities.

Farm Credit Financial Partners, Inc.—Farm Credit Financial Partners, Inc., provides support services to CoBank, ACB; six associations affiliated with CoBank, ACB; one association affiliated with AgriBank, FCB; the Leasing Corporation; and two FCS-related entities.

FCS Building Association—FCSBA, which acquires, manages, and maintains facilities to house FCA's headquarters and field office staff, was formed in 1981. It is owned by System banks but is subject to the oversight and direction of the FCA Board.

Farm Credit Foundations—Farm Credit Foundations provides human resource services to its employer-owners, including payroll processing, benefits administration, centralized vendor management, workforce management and operations, corporate tax and financial reporting services, and retirement workshops. It is owned by AgriBank, FCB, and each of its 17 affiliated associations, as well as 26 associations and one service corporation (AgVantis, Inc.) affiliated with CoBank, ACB.

FCS Mission Fulfillment

The System fulfills its overall mission by using its authority to lend to agriculture and rural America. Through changes in the law since the System's original authorization in 1916, System lending authorities have evolved to include the following:

- Long-term agricultural real estate loans and rural home loans
- Short- and intermediate-term agricultural loans
- Loans to producers and harvesters of aquatic products
- Loans to certain farmer-owned agricultural processing facilities and farm-related businesses
- Loans to farmer-owned agricultural cooperatives
- Loans that finance agricultural exports and imports
- Loans for rural utilities
- Limited portions of loans to entities that qualify under the System's similar-entity authority

In addition to its lending programs, the System is participating in several mission-related pilot investment programs (referred to as Investments in Rural America) to strengthen its ability to provide for an adequate and flexible flow of funds to agriculture and rural communities across the country. These pilot programs often involve partnerships or alliances with other agricultural lenders. Regardless of their scope, they all operate under conditions specified by FCA. (See pages 49 and 50 for a description of the Investments in Rural America program.)

FINANCIAL CONDITION AND PERFORMANCE

In FY 2011, the overall condition and performance of the FCS remained safe and sound. Asset quality generally improved in FY 2011. All banks and most associations continued to maintain capital ratios well in excess of minimum regulatory requirements, and net income increased. Nevertheless, the volatility in commodity prices increased risks to some agricultural operators, creating the potential for future decline in asset quality.

The System's loan portfolio grew at a slightly lower rate because of the recent decrease in demand for agricultural loans and the increase in competition among institutions offering them. For the 12 months ended September 30, 2011, gross loans increased by 1.3 percent, compared with a 3.9 percent gain during the previous 12-month period. The AgriBank district was the only one that experienced growth; its gross loans increased by 6.5 percent. Gross loans declined by about 2.6 percent and 2.4 percent in the Texas and CoBank districts, respectively. Gross loan volume remained the same for the U.S. AgBank and AgFirst districts from FY 2010 to FY 2011.

Earnings

The FCS earned $2.99 billion in the first nine months of 2011, a 13.7 percent increase from the $2.63 billion earned in the same period in 2010. This rise in net income stemmed from an increase in net interest spreads and a decrease in the provision for loan losses. See table 18.

TABLE 18: Net Income
(Dollars in Millions)

	First 9 Months of 2010	First 9 Months of 2011	Dollar Change	Percent Change
Net interest income	$4,323	$4,696	$373*	8.6
- Provision for losses	474	352	(122)	-25.7
= Net interest income after loss provision	$3,849	$4,344	$495	12.9
+ Noninterest income	354	426	72	20.3
- Noninterest expense	1,419	1,579	160	11.3
= Pretax income	$2,784	$3,191	$407	14.6
- Provision for income tax	151	197	46	30.5
= Net income	$2,633	$2,994	$361	13.7

Source: FCS Quarterly Information Statements.

* Of the $373 million increase in net interest income, $322 million was the result of increased volume, and $51 million was the result of increased spreads.

The $373 million increase in net interest income was augmented by a decrease in the provision for loan losses of $122 million and slightly offset by the $160 million increase (11.3 percent) in noninterest expenses in 2011. Interest-earning assets increased from $205 billion to $220 billion during this 12-month period as interest rate spreads widened. The net interest spread rose 7 basis points, from 2.60 percent to 2.67 percent, because interest rates fell more on liabilities than on assets. The yield on interest-earning assets fell by an annualized rate of 23 basis points while the yield on interest-bearing liabilities decreased by an annualized rate of 30 basis points. As a result, the net interest margin—a second operations measurement—increased by 4 basis points during this period. See table 19.

TABLE 19: Interest Margin

Annualized Percentages	First 9 Months of 2010	First 9 Months of 2011	Change (bps)
Total interest-earning assets	**4.29**	**4.06**	**-23**
Loans	4.86	4.61	-25
Investments and other assets	2.00	1.81	-19
Total interest- bearing liabilities	**1.69**	**1.39**	**-30**
Net interest spread	**2.60**	**2.67**	**7**
Effect of noninterest-bearing items	0.21	0.18	-3
Net interest margin	**2.81**	**2.85**	**4**

Source: FCS Quarterly Information Statements.

bps = basis points

The System's net return measures showed mixed results but continued to be relatively strong during the first nine months of 2011. The return on average assets increased in the CoBank, Texas, and U.S. AgBank districts. CoBank and Texas also experienced an increase in their return on average capital. See table 20 below.

TABLE 20: Profitability Across System Districts

First 9 months of year:		AgFirst	AgriBank	Texas	U.S. AgBank	CoBank
Percent return on average assets	2010	1.73	2.00	1.46	1.74	1.36
	2011	1.54	1.84	1.95	1.79	1.38
Percent return on average capital	2010	14.55	13.30	10.53	10.39	13.83
	2011	11.53	12.12	12.29	9.92	13.97

Source: FCS Quarterly Information Statements.

Asset Growth

The System experienced mixed loan and asset growth during the year ended September 30, 2011. Generally stronger agricultural profits reduced the need for farmers to borrow. Increased competition from other financial institutions also decreased loan demand during this period. Livestock prices have rebounded from earlier lows because of tight supply, greater demand, and a drop in feed input cost. FCS assets grew to $227.7 billion as of September 30, 2011, up $7.15 billion (3.2 percent) from September 30, 2010. Increases in loans by $2.1 billion (1.3 percent), investments by $1.9 billion (4.8 percent), and cash by $3.5 billion (55.9 percent) resulted in the moderate increase in total assets.

AgriBank was the only district that experienced loan growth for the year ended September 30, 2011; its gross loan volume increased by $4.1 billion (6.5 percent). The largest loan volume decreases were in the CoBank and Texas districts: $1.2 billion (2.4 percent) and $402 million (2.6 percent), respectively. See table 21.

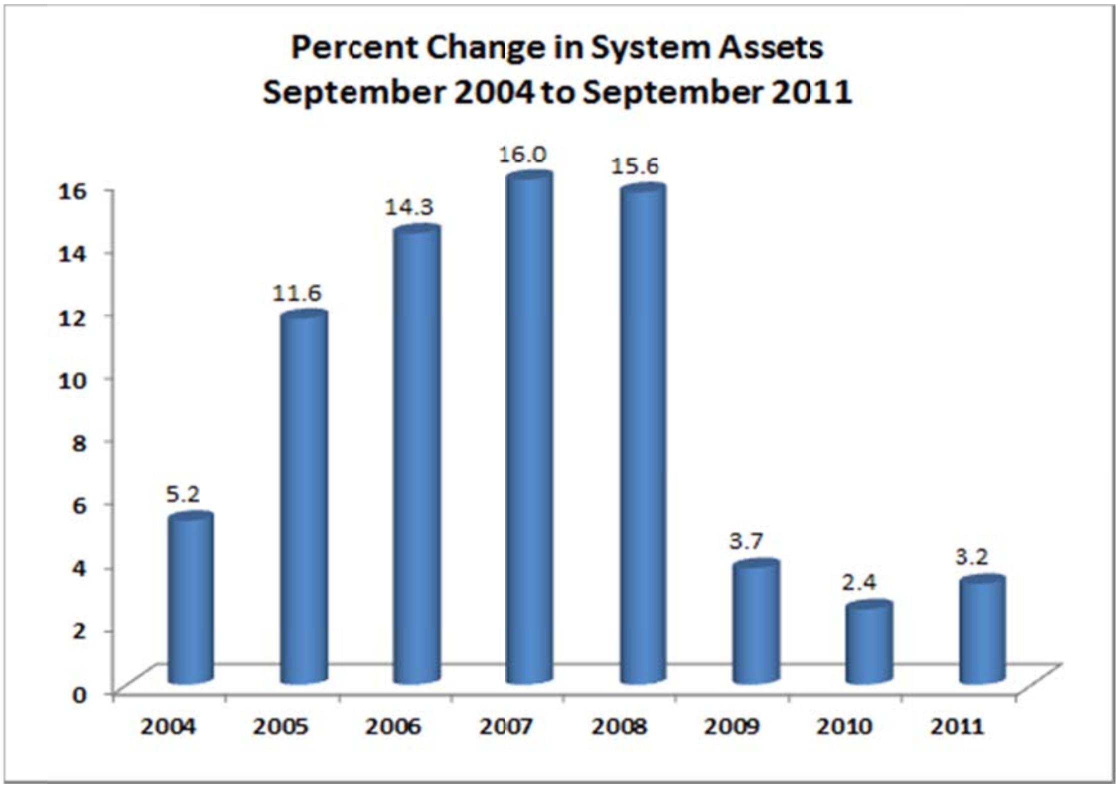
TABLE 21: Gross Loan Growth by District and Systemwide
(Dollars in Millions)

	September 30, 2010		September 30, 2011			
	Gross Loans	**Percent Total**	**Gross Loans**	**Percent Total**	**Change in Dollars**	**Percent Change**
AgFirst	$23,007	13.7	$22,749	13.3	($258)	(1.1)
AgriBank	62,113	36.9	66,177	38.8	$4,064	6.5
Texas	15,668	9.3	15,266	8.9	($402)	(2.6)
U.S. AgBank	23,935	14.2	23,772	13.9	($163)	(0.7)
CoBank	48,239	28.6	47,079	27.6	($1,160)	(2.4)
Intra-System Eliminations	(4,478)	(2.7)	(4,428)	(2.6)	50	(1.1)
Total for System	**$168,484**	**100**	**$170,615**	**100**	**$2,131**	**1.3**

Source: FCS Quarterly Information Statements.

As noted in the following figure, the System's total assets grew 3.2 percent during the 12-month period ended September 30, 2011, slightly above the 2.4 percent growth during the previous period but much lower than the growth rates seen from 2005 to 2008.

Figure 4



Source: FCS Quarterly Information Statements.

Assets—Investments

The System's investment activity grew 4.8 percent during FY 2011, with some realignment. The System increased its holding of mortgage-backed, U.S. agency, and U.S. Treasury securities while reducing holdings of money market instruments, other asset-backed securities, and mission-related investments. (See table 22.) All segments of the investment portfolio experienced a decrease in yield during the most recent 12-month period, with other asset-backed securities (held to maturity) experiencing the largest decline—from 3.4 percent to 1.9 percent. The overall yield on securities available for sale decreased from 1.7 percent to 1.6 percent, while the yield on securities held to maturity declined somewhat more, dropping from 3.9 percent to 3.2 percent.

In addition, most ineligible investment securities that the System has on its books are the result of the unfavorable market conditions related to the mortgage lending crisis. An investment may become ineligible if changes occur in its credit rating or in the percentage it represents of an institution's investment portfolio. According to FCA's regulatory standards, an investment must maintain a particular credit rating to remain eligible to be held by the System, and certain investments may represent no more than a limited percentage of an institution's portfolio. If changes occur that place investments in violation of FCA's regulatory standards, they become ineligible. During FY 2011, FCA approved the divestiture plans for 15 ineligible investments with a total fair market value of $121 million as of September 30, 2011. Approval requests were pending on the divestiture plans for five more ineligible investments as of September 30, 2011.

TABLE 22: FCS Investments
(Dollars in Millions)

		September 30, 2010		September 30, 2011		Change		
						Amount		WAY (bps)
		Amount	WAY (%)	Amount	WAY (%)	Dollars	Percent	
Available for sale (fair value)	Money market instruments	$5,295	0.6	$4,893	0.6	($402)	(7.6)	-4
	U.S. Treasury securities	4,464	1.3	4,658	1.1	194	4.3	-21
	U.S. agency securities	931	4.3	1240	3.3	309	3.2	-103
	Mortgage-backed securities	23,832	1.9	26,068	1.9	2,236	9.4	-6
	Other asset-backed securities	1,128	1.5	935	1.3	($193)	(17.1)	-23
	Mission related	591	3.4	555	3.0	($36)	(6.1)	-32
	Total	**$36,241**	**1.7**	**$38,349**	**1.6**	**$2,108**	**5.8**	**-7**
Held to maturity (amortized cost)	Money market instruments	218	6.0	203	6.0	($15)	(6.9)	0
	Mortgage-backed securities	2,077	4.0	3,028	3.2	951	45.8	-78
	Other asset-backed securities	1,515	3.4	377	1.9	($1,138)	(75.1)	-152
	Total	**$3,810**	**3.9**	**$3,608**	**3.2**	**($202)**	**(5.3)**	**-65**

Source: FCS Quarterly Information Statement. WAY = weighted average yield; bps = basis points

Asset Quality

Nonperforming assets declined from $4.15 billion (1.9 percent of total assets) on September 30, 2010, to $3.75 billion (1.6 percent of total assets) on September 30, 2011. The volume of nonperforming loans decreased as the economy improved and the demand for agricultural products increased. While input costs remained relatively high, commodity prices rose with increasing demand, which relieved some stress on agricultural producers. High risk persists among livestock, poultry, and ethanol producers, who use corn or other grains in their products; producers of nursery and forestry products, who rely on the housing industry for business; and borrowers purchasing agricultural land to convert for housing and other nonagricultural uses.

Net charge-offs were slightly lower in the first nine months of 2011 than they were for the same period a year earlier. In the first nine months of 2011, the System had net charge-offs of $332 million compared with $406 million for the same period in 2010.

The allowance for loan losses increased as a fraction of nonperforming and nonaccrual loans while nonperforming loans decreased as shown in the table below.

TABLE 23: FCS Asset Quality

Asset Quality	September 30, 2010	September 30, 2011
Nonaccrual loans as percentage of total loans	2.11	1.80
Nonperforming assets as percentage of capital	12.56	10.44
ALL as percentage of total loans	0.83	0.82
ALL as percentage of nonperforming loans	38	42
ALL as percentage of nonaccrual loans	39	45

Source: FCS Quarterly Information Statements.

ALL = allowance for loan losses

Liabilities, Funding, and Liquidity

The System's funding composition remained relatively constant for the year ended September 30, 2011. Short-term debt securities made up 34.7 percent of total Systemwide debt securities compared with 34.5 percent a year earlier. Debt securities due within one year increased by 2.7 percent while those due after one year increased by 2.2 percent. See table 24 below.

TABLE 24: Systemwide Debt
(Dollars in Millions)

	September 30, 2010	September 30, 2011	Change	
			Dollars	Percent
Systemwide discount notes due within 1 year	$14,921	$15,168	$247	1.7
Systemwide bonds, medium-term notes, and master notes due within 1 year	49,816	51,292	1,476	3.0
Total short-term liabilities	**$64,737**	**$66,460**	**$1,723**	**2.7**
Systemwide bonds, medium-term notes, and master notes due after 1 year	114,365	116,901	2,536	2.2
Other liabilities	8,396	8,394	(2)	(0.02)
Total liabilities	**$187,498**	**$191,755**	**$4,257**	**2.3**
Source: FCS Quarterly Information Statements.				

The System's liquidity position increased from 172 days as of September 30, 2010, to 200 days as of September 30, 2011, remaining significantly above the regulatory minimum.[6]

The duration gap,[7] which derives from the estimated durations of assets and liabilities, is a primary measure of asset-liability risk exposure. A positive duration gap (in which the duration of assets exceeds the duration of liabilities) exposes the System to rising interest rates because liabilities will reprice more quickly than assets. Conversely, a negative duration gap (in which the duration of liabilities exceeds the duration of assets) exposes the System to declining interest rates because assets will reprice more quickly than liabilities.

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[6] The regulatory liquidity standard requires each FCS bank to maintain a minimum of 90 days of liquidity on a continuous basis, with no access to the capital markets. The number of days of liquidity is calculated by comparing maturing Systemwide debt securities and other bonds for which the bank is primarily liable with the total amount of cash, investments, and other liquid assets maintained by that bank. For purposes of calculating liquidity, liquid assets are subject to discounts that reflect potential exposure to adverse market value changes that might be recognized upon liquidation or sale.

[7] Duration is the weighted average maturity of cash flows. It is a useful way to estimate the direction and size of changes in the value of a financial instrument when market interest rates change. Here, "duration gap" is the difference between the duration of assets and the duration of liabilities, measured in months. When the duration gap is small, changing market interest rates pose less interest rate risk than when the gap is large.

The duration gap for the FCS was a positive 1.5 months on September 30, 2011, compared with a positive 0.3 on September 30, 2010, reflecting a slightly increasing interest rate risk in the funding of the System's lending operations. The System is currently in this liability-sensitive position because much of its callable debt is in its repricing interval because of a decline in interest rates. In a rising interest rate environment, the repricing interval of callable bonds would tend to lengthen to reflect the maturity date of the bonds and thus mitigate the impact of a liability-sensitive position or even to move the System to an asset-sensitive position.

Capital

Total capital grew by 8.8 percent during FY 2011 to reach $35.9 billion. Most of the $2.9 billion increase in capital came from net income, but an increase in additional paid-in-capital and a decrease in accumulated other comprehensive loss also added to the total. See table 25 for changes in the capital components.

Surplus still accounts for the overwhelming majority of capital, at 81.9 percent as of September 30, 2011, compared with 81.3 percent as of September 30, 2010. While there were mixed results by district banks and associations, the System's overall capital-to-assets ratio grew from 15.0 percent to 15.8 percent over this 12-month period, reflecting the moderate growth in System assets.

TABLE 25: FCS Capital Composition
(Dollars in Millions)

	September 30, 2010	September 30, 2011	Change	
			Dollars	Percent
Preferred stock	$2,143	$2,146	$3	0.1
Capital stock and participation certificates	1,525	1,585	60	3.9
Additional paid-in-capital	381	401	20	5.2
Restricted capital (Insurance Fund)	3,193	3,356	163	5.1
Accumulated other comprehensive loss	(1,065)	(991)	74	-6.9
Surplus	26,870	29,442	2,572	9.6
Total capital	**$33,047**	**$35,939**	**$2,892**	**8.8**

Source: FCS Quarterly Information Statements.

Table 26 shows that the banks are collectively capitalized well in excess of regulatory requirements. For associations, the range of permanent capital ratios rose from 10.5 to 28.4 percent as of September 30, 2010, to 11.9 to 30.9 percent as of September 30, 2011. At September 30, 2011, all System institutions complied with FCA capital standards.

TABLE 26: Regulatory Capital Ratios of FCS Banks

		AgFirst	AgriBank	Texas	U.S. AgBank	CoBank
Permanent capital ratio	9/30/2010	19.8	20.3	18.8	19.2	16.1
	9/30/2011	23.5	20.5	20.8	21.3	15.7
	Change	3.7	0.2	2	2.1	(0.4)
Total surplus ratio	9/30/2010	19.8	16.4	15.1	15.0	15.7
	9/30/2011	23.5	16.8	17.1	16.7	15.4
	Change	3.7	0.4	2	1.7	(0.3)
Core surplus ratio	9/30/2010	12.5	9.6	9.7	11.4	9.4
	9/30/2011	15.7	9.8	10.3	13.2	9.6
	Change	3.2	0.2	0.6	1.8	0.2
Net collateral ratio	9/30/2010	107.1	106.0	108.4	105.5	108.6
	9/30/2011	107.7	106.3	108.9	105.6	109.0
	Change	0.6	0.3	0.5	0.1	0.4

Source: FCA Consolidated Reporting System.

YOUNG, BEGINNING, AND SMALL FARMERS AND RANCHERS

Congress has mandated that the Farm Credit System serve the credit needs of young, beginning, and small (YBS) farmers and ranchers by directing System associations to set up YBS programs and by requiring the banks to issue annual reports on their associations' programs. To ensure that the System fulfills this responsibility, the FCA Board adopted a final rule in 2004 that

1. amended regulations to provide clear, meaningful, and results-oriented guidelines for System YBS policies and programs;

2. allows associations the flexibility to design YBS programs unique to the needs of their territories and encourages the establishment of advisory committees comprising YBS farmers;

3. requires each System association to include quantitative YBS targets and qualitative YBS goals in its operational and strategic business plan, as well as to establish internal controls over YBS programs; and

4. requires System banks and associations to include information on YBS loans and programs in their annual reports to shareholders and investors.

FCA examiners review the policies and programs of the institutions to ensure that the institutions are complying with the YBS regulations.

In addition, the Agency continues to review and consider regulatory relief options to support YBS programs in the FCS. For example, in August 2007, FCA issued a revised Bookletter to the System that provided guidance on interpreting the phrase "sound and constructive credit," which is used in section 4.19 of the Farm Credit Act, as well as in FCA regulation 12 CFR 614.4165. This guidance is intended to ensure that System institutions make full use of their authorities to assist YBS farmers to begin farming, to expand their operations, or to remain in agricultural or aquaculture production.

The information that follows shows YBS results for calendar year 2010. FCA is currently collecting information for 2011 and estimates it will be available after March 2012. A summary of the System's YBS program results is also available on FCA's website at www.fca.gov.

Tables 27 and 28 provide the YBS results for calendar year 2010. Loans to YBS producers include real estate loans and short- and intermediate-term loans. It is important to note that information is reported separately for each of the three YBS categories because some borrowers fit into two or even all three categories. Therefore, the sum of the numbers in the categories is not an accurate measure of the System's YBS lending activity.

In calendar year 2010, loans made (new loans and renewals) for young (Y), beginning (B), and small (S) categories Nationwide rose in number and dollar volume, reversing the decline in new lending activity that had occurred in 2009. This increase in credit demand was consistent with a stronger general and farm economy and an increase in capital purchases among farmers in 2010. The percentage increases in the numbers of loans made were not as great as the increase in volume, reflecting an increase in the average size of loans made in 2010. The volume of YBS loans outstanding also increased for each of the three borrower categories, as it had for the previous nine years. The dollar volume of loans outstanding to young farmers increased 3.1 percent, followed by a 2.2 percent increase for small farmers and a 0.6 percent increase for beginning farmers. The following information summarizes lending activity for the three separate YBS categories.

Young—At the end of 2010, the System had 162,982 loans outstanding to young farmers, totaling $21.1 billion, up from $20.4 billion for 2009. A “young” farmer is defined as one who is 35 years old or younger when the loan is made. During 2010, 53,470 loans, totaling $7.3 billion, were made to young farmers. These loans represented 16.2 percent of all loans the System made during the year and 11.4 percent of the loan dollar volume.

Beginning—The System had 231,975 loans outstanding to beginning farmers, totaling $34.3 billion at year-end 2010, up from $34.1 billion for 2009. “Beginning” farmers are those with 10 or fewer years of farming experience. During 2010, 65,653 loans, totaling $10.3 billion, were made to beginning farmers. These loans represented 19.9 percent of all loans made and 16.0 percent of loan dollar volume.

Small—At year-end 2010, FCS institutions had 485,148 loans outstanding to small farmers, totaling $43.7 billion, up from $42.8 billion from the 2009 total. “Small” farmers are defined as those with annual gross sales of less than $250,000. During 2010, 155,371 loans, totaling $13.1 billion, were made to small farmers. These loans represented 47.0 percent of all loans made and 20.4 percent of loan dollar volume.

TABLE 27. YBS Loans Outstanding
(as of December 31, 2010)

Type of Farmer	Number of Loans	Percentage of Total Number	Dollar Volume of Loans in Billions	Percentage of Total Dollar Volume	Average Loan Size
Young	162,982	18.3	$21.1	11.7	$129,255
Beginning	231,975	26.1	$34.3	19.1	$147,973
Small	485,148	54.5	$43.7	24.4	$90,110
Note: YBS data for each category are reported separately and should not be added.					

TABLE 28. YBS Loans Made During 2010
(as of December 31, 2010)

Type of Farmer	Number of Loans	Percentage of Total Number	Dollar Volume of Loans in Billions	Percentage of Total Dollar Volume	Average Loan Size
Young	53,470	16.2	$7.3	11.4	$136,917
Beginning	65,653	19.9	$10.3	16.0	$156,557
Small	155,371	47.0	$13.1	20.4	$84,243
Note: YBS data for each category are reported separately and should not be added.					

To help YBS farmers qualify for credit in 2010, most FCS associations offered differentiated loan underwriting standards, or made exceptions to their regular standards, for YBS borrowers. For example, some associations used higher loan-to-appraised-value ratios or lower debt repayment capacity standards for YBS borrowers. Some associations provided concessionary loan fees, and more than a third of all FCS associations offered lower interest rate programs for YBS borrowers.

Most FCS associations used Government loan guarantee programs, primarily those of the USDA Farm Service Agency, to increase their service to YBS farmers. Use of these guarantees reduces credit risks to the lender while enabling associations to make loans to borrowers who would not otherwise meet underwriting standards. Finally, associations employed several outreach measures to reach potential YBS farmers. They also provided various training programs and services to YBS farmers; examples include programs to build leadership and financial management skills, and special conferences for young farmers.

MARKET SHARE OF FARM DEBT

According to the U.S. Department of Agriculture's November 2011 estimate, total farm business debt was $246.9 billion at the end of 2010, up 2.1 percent from a year earlier. Commercial banks and the Farm Credit System are the primary suppliers of credit to farmers; providers also include life insurance companies, USDA programs, individuals, merchants and dealers, and others.

The System's market share of farm business debt was 41.4 percent at the end of calendar year 2010, up from 40.1 percent at the end of 2009.[8] Market share for commercial banks declined from 44.3 percent in 2009 to 43.9 percent in 2010. Both the FCS and commercial lenders experienced modest increases in loan demand in 2010, with FCS volume up more than $4 billion, whereas commercial bank volume was up more than $1 billion from the estimate for 2009. Lender reporting for 2011 thus far suggests that the level of farm business debt for 2011 may not change much from that estimated for 2010. USDA estimates on the market shares of individual lender groups for year-end 2011 will not be available until August 2012.

In recent years, the FCS has been increasing its market penetration, moving from a 32.5 percent market share at year-end 2004 to the current figure of 41.4 percent. The market share estimates for commercial banks show that their share has remained fairly flat, hovering closer to 44 percent during most of the last decade. By market segment, the System experienced a greater percentage gain in real-estate farm debt in 2010 than in non-real-estate farm debt. Historically, except for the unusual period of the 1980s and various market adjustments in the 1990s, FCS institutions have typically dominated the farm real estate market, while commercial banks have dominated non-real-estate lending.

The System's share of debt secured by farm real estate increased at year-end 2010 to 45.3 percent, up from 38.8 percent at the end of 2004. The commercial bank share of farm real estate debt rose less during this six-year period, rising from 36.2 percent to 38.1 percent. The System has had the largest market share of farm real estate debt since 2001.

The System experienced slower growth in the non-real-estate farm debt market in 2010, yet its market share rose from 36.1 percent at year-end 2009 to 36.6 percent. During the late 1990s, its share in this segment tended to be under 20 percent. Commercial banks continue to lead the non-real-estate-secured farm debt market with a 51.2 percent market share at the end of 2010, but this share has eroded from a 56.6 percent share in 2000. Commercial banks have held at least a 50 percent market share in this segment since 1991.

[8] USDA's estimate of farm debt includes debt associated with the farming business and therefore excludes FCS lending associated with cooperatives, rural homes, rural utilities, marketing and processing operations, and other nonfarm-lending activities.

Part IV

Performance Budget FY 2013

PERFORMANCE BUDGET OVERVIEW

FCA's FY 2013 Performance Budget reflects its commitment to maintaining a flexible regulatory environment that meets current and future rural credit needs while ensuring the safety and soundness of the Farm Credit System (FCS). The total Performance Budget for FY 2013 is $64.1 million and reflects a 5 percent increase from the FY 2012 revised budget. Table 29 shows the agency's programs and activities and their respective budget allocations.[9]

TABLE 29. FCA Performance Budget
FYs 2011–2013

	FY 2011 Actual*	FY 2012 Revised	FY 2013 Proposed
Policy and regulation	$13,231,444	$12,720,082	$13,567,235
Safety and soundness	38,879,792	46,203,898	48,600,141
Reimbursable activities	1,265,230	1,888,919	1,963,225
Total	**$53,376,466**	**$60,812,899**	**$64,130,601**

* Rather than the approved budget amounts, actual expenditures for FY 2011 are provided for comparison purposes.

Policy and Regulation

The Agency's Performance Budget includes $13.6 million for the policy and regulation program, a 6 percent increase from FY 2012. Most of the funds requested for policy and regulation in FY 2013 will support regulatory projects that were published in the Unified Agenda in the fall of 2011. Generally, FCA opens about a dozen regulatory projects each year. Funds are also used to support other statutory and regulatory activities, including policy studies and market research; management of the Agency's Consolidated Reporting System; and approvals of corporate applications, System funding requests, and mission-related investment programs.

Safety and Soundness

The Performance Budget includes $48.6 million for the safety and soundness program, a 5 percent increase from FY 2012. This increase results from staff increases and a reallocation of examination resources from reimbursable activities to examination activities to meet System needs.

By statute, FCA is required to examine each direct-lender FCS institution at least once every 18 months and to examine the Federal Agricultural Mortgage Corporation (Farmer Mac) at least once a year. Examiners evaluate the overall condition and performance of these institutions and communicate the results to the boards of directors and management through discussions and Reports of Examination. Examiners assign Financial Institution Rating System ratings to each institution at least quarterly. In addition, monies budgeted for FY 2013 will support the development of examination guidance and systemic risk oversight of the System, including Farmer Mac.

[9] The 2013 Cuts, Consolidations, and Savings Volume of the President's Budget identifies the lower-priority program activities under the Government Performance and Results Act (GPRA) Modernization Act, 31 U.S.C. 1115(b)(10). You can access the volume at www.whitehouse.gov/omb/budget.

Reimbursable Activities

The Performance Budget includes $1,963,225 for reimbursable activities. Reimbursable activities are summarized below and include indirect costs.

- Farm Credit System Insurance Corporation (FCSIC)—$596,238 for administrative support services to be provided under FCSIC contract. Services in FY 2013 include examination assistance; technology and information support; human resource support; support for communication and public affairs activities; and assistance in completing one premium audit.

- National Consumer Cooperative Bank (NCB)—$381,727 for examining NCB. FY 2013 activities involve conducting the annual safety and soundness examination and performing interim monitoring and CAMELS (capital, assets, management, earnings, liquidity, and sensitivity) assessments.

- USDA—$985,260 for work completed under contract agreement with USDA. The work in FY 2013 will involve supporting USDA in conducting its Business and Community Program Assessment Review and its Rural Business Investment Programs.

Table 30 summarizes the costs associated with FCA's program activities, broken down by products and services.

TABLE 30. FY 2013 Budget (Proposed) and Full-Time Equivalents (FTEs) for Program Activities

	Products and Services	Budget Amount	FTEs
Program activity: Policy and regulation			
	Regulation and policy development	$10,925,152	45.86
	Statutory and regulatory approvals	2,642,083	11.45
Total for policy and regulation		**$13,567,235**	**57.31**
Program activity: Safety and soundness			
	Examination	$46,329,579	228.75
	Economic, financial, and risk analysis	1,288,923	5.87
	FCS data management	981,639	5.15
Total for safety and soundness		**$48,600,141**	**239.77**
Program activity: Reimbursable activities			
Total for reimbursable activities		**$1,963,225**	**7.98**
TOTAL		**$64,130,601**	**305.06**

DESIRED OUTCOMES FOR STRATEGIC GOALS

FCA uses the strategic goals and desired outcomes listed in table 31 to measure the achievement of its public mission. The information that follows provides (1) the strategies that are used to accomplish the outcomes; (2) the measures for each outcome, with targets/performance goals that reflect the Agency's desired performance for FYs 2012 and 2013; and (3) a historical summary of the costs of accomplishing the desired outcomes.

Please note that the strategies listed below reflect the strategies provided in the FCA Strategic Plan for FYs 2011–2016, which was published in May 2011. These strategies differ somewhat from the "means and strategies" published in FCA Budgets for the past few years.

Likewise, the performance measures changed somewhat when the Strategic Plan was updated. Because the revised Strategic Plan was published during FY 2011, the Agency used two separate sets of Performance Measures in FY 2011. During the first three quarters of the fiscal year, the Agency used the performance measures in effect prior to the revision of the Strategic Plan (see tables 32 and 34); during the last quarter of FY 2011, FCA used the updated measures (see tables 32a and 34a).

TABLE 31. Desired Outcomes for Strategic Goals

Strategic Goal	Desired Outcome
1. Ensure that the FCS and Farmer Mac fulfill their public mission for agriculture and rural areas.	A flexible regulatory environment and a proactive examination program to monitor System institutions
2. Evaluate risk and provide timely and proactive oversight to ensure the safety and soundness of the FCS and Farmer Mac.	Effective risk identification and timely corrective action

Policy and Regulation—FCA established the Policy and Regulation program to track the costs of the products and services that we use to achieve a flexible regulatory environment. These products and services include regulation and policy development and statutory and regulatory approvals.

Safety and Soundness—FCA established the Safety and Soundness program to track the costs of identifying risk and implementing timely corrective action. Products and services associated with this program include examination; economic, financial, and risk analysis; and FCS data management.

Flexible Regulatory Environment

Strategies

For goal 1, FCA is using the following strategies to achieve a flexible regulatory environment that enables the System and Farmer Mac (the agricultural GSEs) to fulfill their public mission.

1. Within the framework of the Farm Credit Act, continuously update policies and regulations to provide an operating environment for the System and Farmer Mac that meets the changing needs of agriculture and rural America.

2. Emphasize the public purpose and mission-related responsibilities of the agricultural GSEs serving rural America, including the use of innovative programs for serving the credit and related service needs of young, beginning, and small (YBS) farmers, ranchers, and producers or harvesters of aquatic products.

3. Encourage System institutions to find and develop both public and private partnerships and alliances with other financial service providers to address the changes in agriculture through new and existing programs.

4. Promote System business practices, including outreach activities to all creditworthy and eligible potential customers, emphasizing minority and socially disadvantaged farmers and ranchers and minority-owned entities.

5. Promote public trust and investor confidence in the System and Farmer Mac by developing policy guidance that helps them achieve their missions.

6. Consistent with cooperative principles and the Farm Credit Act, enable the agricultural GSEs to structure themselves to best serve their customers and rural America.

7. Encourage full participation from stakeholders in the development and review of regulatory proposals.

Measuring the Achievements

Tables 32 and 32a summarize the results of the Agency's efforts to maintain a flexible regulatory environment for the FCS and Farmer Mac. FCA achieved the goals it identified for FY 2011. As noted above, table 32 contains the performance measures that were in effect for the first three quarters of the fiscal year. Table 32a contains revised performance measures, which were first published in the FCA Strategic Plan for FYs 2011–2016; these measures were in effect during the last quarter of the fiscal year.

TABLE 32. Flexible Regulatory Environment Performance Measures and Achievements October 1, 2010, through June 30, 2011

Measure	FY 2011 (Actual) Target	FY 2011 (Actual) Result
1. Percentage of FCS institutions[a] with satisfactory business plans[b] and management systems for providing constructive credit and related services to all potential customers, including institutions with acceptable corrective action plans	≥90%	100%
2. Whether Farmer Mac has developed and implemented a marketing program to appropriately grow program assets consistent with its mission and whether it has received a satisfactory rating from the Office of Secondary Market Oversight (OSMO) or is operating under a corrective action plan acceptable to OSMO	Yes	Yes
3. Percentage of direct-lender institutions with satisfactory internal controls over consumer compliance and borrower-rights compliance, including institutions with acceptable corrective action plans	≥90%	100%
4. Percentage of instances in which the Agency solicits public comment and input on applicable regulatory initiatives using supplemental approaches[c] to the notice and comment rulemaking process	≥40%	100%
5. Percentage of direct-lender institutions that have satisfactory programs[d] to furnish sound and constructive credit and related services to young, beginning, and small (YBS) farmers, ranchers, and producers or harvesters of aquatic products, including institutions with acceptable corrective action plans	≥90%	100%

[a] For purposes of performance measurement, the term "institutions" does not include the FCS service corporations, the National Consumer Cooperative Bank, Farmer Mac (unless specifically noted), or institutions that FCA examines on behalf of the Small Business Administration and the U.S. Department of Agriculture on a contract basis.

[b] Satisfactory business plans are those that received a satisfactory rating from FCA examiners and comply with 12 CFR 618.8440.

[c] Supplemental approaches include advance notices of proposed rulemaking, comment period reopenings and extensions, constituent/congressional committee meetings, public meetings, focus groups, town meetings, and other approaches to gathering a broad range of public input. To ensure technical accuracy, the results were calculated by dividing the number of regulatory initiatives that used supplemental approaches by the total number of regulatory projects published in the Regulatory Performance Plan. The process for reporting performance results for supplemental approaches was addressed in a recent report by the Office of Inspector General (IG). The results reported herein are in accordance with the IG's recommendations.

[d] An effective program is one that received a satisfactory rating from FCA examiners for the most recent review of an institution's YBS program.

Note: The above measures were revised in FCA's Strategic Plan for FYs 2012–2016. See table 32a for the revised measures, which took effect during the last quarter of FY 2011.

TABLE 32a. Flexible Regulatory Environment Performance Measures and Achievements July 1, 2011, through September 30, 2011

Measure	FY 2011 (Actual)		FYs 2012–2013
	Target	Result	Target
1. Percentage of FCS institutions with satisfactory operating and strategic plans for providing products and services to all creditworthy and eligible persons. (Target: 90 percent)	≥90%	98%	≥90%
2. Whether Farmer Mac's business plan contains strategies to promote and encourage the inclusion of all qualified loans, including small and family farm loans, in its secondary market programs, and whether its business activities further its mission to provide a source of long-term credit and liquidity for qualifying loans. (Target: Yes)	Yes	Yes	Yes
3. Percentage of direct-lender institutions with satisfactory consumer and borrower-rights compliance. (Target: ≥90 percent)	≥90%	99%	≥90%
4. Percentage of direct-lender institutions with satisfactory YBS programs. (Target: ≥90 percent)	≥90%	100%	≥90%
5. Follow-up evaluation on appropriate rules and regulations issued related to GSE mission will demonstrate they meet the intended outcome. (Establish baseline in 2013–minimum one year after new rules are established, 5 percent improvement per year thereafter.)	N/A	N/A[a]	N/A[a]
6. Percentage of times the Agency reaches out to nontraditional commenters to solicit their input on regulations related to GSE mission. (Target: 100 percent)	100%	N/A[b]	100%

[a] Baseline will not be established until 2013.

[b] The Agency did not approve any proposed rules during the reporting period that were related to GSE mission.

Note: These performance measures were adopted in May 2011 when FCA published its Strategic Plan for FYs 2011–2016.

Costs

Table 33 provides an assessment of FCA's costs to achieve a flexible regulatory environment from FYs 2009 to 2011, as well as projections to achieve this desired outcome in FYs 2012 and 2013.

TABLE 33. Costs to Achieve a Flexible Regulatory Environment

	FY 2009 Actual Expenses	FY 2010 Actual Expenses	FY 2011 Actual Expenses	FY 2012 Budget (Revised)	FY 2013 Budget (Proposed)
Regulation and policy development	$9,251,153	$8,618,840	$10,496,206	$10,226,937	$10,925,152
Statutory and regulatory approvals	1,604,515	2,059,712	2,735,238	2,493,145	2,642,083
Total	**$10,855,668**	**$10,678,552**	**$13,231,444**	**$12,720,082**	**$13,567,235**
Note: The costs incurred by FCA to achieve a flexible regulatory environment are trending higher because of staff seniority and the Agency's regulatory initiatives.					

Effective Risk Identification and Timely Corrective Action

Strategies

For goal 2, FCA is using the following strategies to achieve effective risk identification and timely corrective action.

1. Ensure that staff provides prompt and comprehensive information to the FCA Board and remains flexible and responsive to the Board's priorities so that the Board will be better able to make fully informed, arm's length decisions.

2. Recruit and retain a diverse and highly skilled workforce to meet FCA's current and future needs.

3. Continue proactive oversight of institution-specific and systemic risks.

4. Promote a vibrant program of Systemwide risk supervision that uses early-warning systems, research, and analyses to identify emerging systemic risks and yields proactive examination direction and policy guidance for use internally and externally.

5. Use Agency supervisory and enforcement authorities effectively to remediate weakened institutions.

6. Promote the continued importance and improvement in the quality of System loan data for use by both the Agency and the System in risk management and business planning.

7. Develop regulatory guidance and examination procedures that keep pace with evolving strategies and new programs to meet the changing needs of agriculture and rural America.

Measuring the Achievements

Tables 34 and 34a provide the results of FCA's examinations and oversight efforts to effectively identify risk and take timely corrective action. The Agency met its goals as of the end of FY 2011 (September 30, 2011).

TABLE 34. Effective Risk Identification and Timely Corrective Action— Summary of Strategic Goal Measures and Achievements October 1, 2010 through June 30, 2011

Measure	FY 2011 (Actual)	
	Target	Result
1. Number of institutions that FCA placed in receivership because of financial failure during the previous 12 months	≥90%	98%
2. The total assets of FCS institutions that FCA has determined are fundamentally sound in all material respects	Yes	Yes
3. Percentage of FCS institutions with composite Financial Institution Rating System (FIRS) ratings of 3, 4, or 5 with acceptable corrective action plans in place to address the problems identified by FCA examiners[a]	≥90%	99%
4. Percentage of System assets in institutions with ratios of adverse assets to risk funds of less than 100 percent	≥90%	100%
5. Percentage of institutions complying with regulatory capital ratio requirements (permanent capital ratio, total surplus ratio, core surplus ratio, net collateral ratio, risk-based capital), including institutions with acceptable corrective action plans	100%	100%
6. Percentage of FCS institutions with acceptable action plans to correct violations of laws and regulations identified by FCA examinations	100%	100%
7. Percentage of institutions that have satisfactory audit and review programs, including institutions with acceptable corrective action plans[b]	≥90%	98%

[a] As of September 30, 2011, 30 institutions were rated 1; 46 institutions were rated 2; 11 were rated 3; and 2 were rated 4. No institution received a rating of 5.

[b] An effective audit and review program has a satisfactory rating from FCA examiners on the most recent internal control review.

Note: The above measures were revised in FCA's Strategic Plan for FYs 2012–2016. See table 34a for the revised measures, which took effect during the last quarter of FY 2011.

TABLE 34a. Effective Risk Identification and Timely Corrective Action—Summary of Strategic Goal Measures and Achievements July 1, 2011, through September 30, 2011

Measure	FY 2011 (Actual) Target	FY 2011 (Actual) Result	FYs 2012–2013 Target
1. Percentage of System assets in institutions with composite CAMELS ratings of 1 or 2. (Target: ≥90 percent)	≥ 90%	98%	≥ 90%
2. Percentage of requirements in supervisory agreements with which FCS institutions have at least substantially complied within 18 months of execution of the agreements. (Target: ≥80 percent)	≥ 80%	100%	≥ 80%
3. Percentage of institutions complying with regulatory capital ratio requirements (permanent capital ratio, total surplus ratio, core surplus ratio, net collateral ratio). (Target: 90 percent)	≥ 90%	100%	≥ 90%
4. Whether the Office of Secondary Market Oversight examination and oversight plan and activities effectively identify emerging risks, and whether appropriate supervisory and corrective actions are implemented to effect change when needed. (Target: Yes)	Yes	Yes	Yes
5. Percentage of institutions with satisfactory audit and review programs, including institutions with acceptable corrective action plans. (Target: 100 percent)	100%	100%	100%
6. Percentage of employees who report in the annual FCA employee viewpoint survey of being committed to, and engaged in, the Agency's work. (Target: Increase average score by 2 percent annually until it reaches at least 80 percent).	≥ 80%	81.05%	≥ 80%
7. Percentage of FCS institutions providing FCA with consolidated loan data. (Target for 2012: ≥80 percent; target for 2013: ≥90 percent; target for 2014: 100 percent)	≥80%	100%*	≥80%

* This result is based on results from the database for FCSLoans1 submissions.

Costs

Table 38 provides information on the Agency's costs to identify risk in the FCS and to take timely corrective action from FYs 2009 to 2011, as well as projections to do so in FYs 2012 and 2013.

TABLE 35. Costs to Identify Risk and Take Timely Corrective Action

	FY 2009 Actual Expenses	FY 2010 Actual Expenses	FY 2011 Actual Expenses	FY 2012 Budget (Revised)	FY 2013 Budget (Proposed)
Examination	$32,511,686	$36,973,416	$36,604,451	$44,016,686	$46,329,579
Economic, financial, and risk analysis	1,084,613	1,178,208	1,243,538	1,237,260	1,288,923
FCS data management	518,429	1,073,457	1,031,803	949,952	981,639
Total	**$34,114,728**	**$39,225,081**	**$38,879,792**	**$46,203,898**	**$48,600,141**

Note: FCA's costs to identify risk and take timely corrective action are projected to increase in FYs 2012 and 2013 because of additional hiring, travel, training, and information technology costs.

PERFORMANCE MEASUREMENT AND REPORTING

FCA's performance measurement system evaluates the Agency's progress in achieving the goals of FCA's Strategic Plan for FYs 2011 to 2016.[10] The Agency provides a balanced view of its overall performance, taking into account the inputs used, the products and services produced, and the achievement of desired outcomes. As demonstrated in this document, the Agency-level measures are linked to FCA's strategic goals.

The Chief Executive Officer, with assistance from the Chief Operating Officer and designated office directors, is responsible for measuring performance by collecting and analyzing performance data. The Chief Executive Officer monitors the Agency's progress and results relative to the Agency-level measures on a quarterly basis throughout each fiscal year. Periodic performance reports are provided to the FCA Board. The year-end performance report is incorporated in the *FCA Performance and Accountability Report*, which is submitted to the President and Congress.

[10] As noted above, FCA used an earlier set of performance measures to evaluate the Agency's performance in the first three quarters of FY 2011. After publishing its revised Strategic Plan in May 2011, FCA used the revised set of performance measures to evaluate performance in the last quarter of FY 2011. The revised measures apply to FYs 2012 and 2013.

Copies are available from
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