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The National Chartering Train Is Rolling, Rolling

(May 2000)

Even in this Internet Age, trains remain a favorite way to draw analogies in Washington, such as “That bill has a powerful locomotive pulling it through Congress.” An express train is the perfect analogy to describe the Farm Credit Administration’s (FCA) “national chartering” initiative first reported in last month’s *FCW*. Forty-seven days after announcing national chartering, the FCA published a slick, 12-page booklet describing exactly how this revolutionary restructuring of the FCS would work; it can be found on the FCA web site at www.fca.gov/Download/42095c.pdf.

Let’s discuss this latest taxpayer-subsidized assault on the ag lending business at two levels — its specifics and, more fundamentally, the troubling regulatory precedent the FCA is trying to set.

Regulation by Booklet — a Most Troubling Precedent

Even with a cursory reading, National Chartering is the successor to the “Lender’s Choice” proposal the FCA announced on Nov. 10, 1998. Issued as a proposed regulation, Lender’s Choice would have allowed FCS associations to lend anywhere within the United States. That proposal triggered a hail storm of protest from within the FCS, with almost one-half of the FCS institutions expressing opposition to it for one reason or another.

Responses to the proposed regulation were summarized in the Summer 1999 *Journal of Agricultural Lending*. Clearly, FCA blundered with Lender’s Choice, which is why the

FCA let it die quietly — it simply never made the proposed regulation a final regulation.

After reading the carefully crafted National Chartering booklet, it increasingly appears that this successor to Lender's Choice was cooked up last year when the FCA realized that Lender's Choice had bombed. Burned once, and possibly under pressure from FCS's empire builders, FCA was not about to issue a similar proposed regulation that would draw lots of fire. Instead, the FCA is moving ahead quite audaciously with "regulation by booklet." That is, rather than proceeding under well-established administrative law, which prescribes the process by which federal agencies establish regulations, the FCA is sidestepping the law by issuing a booklet that is tantamount to a regulation.

By not issuing a new proposed regulation, the FCA avoids giving the public, specifically bankers and FCS associations, an opportunity to comment on its National Charter initiative. Congress should be troubled by the FCA's thumbing its nose at the administrative law as well as by the substance of National Chartering. Bankers should be concerned that banking regulators could just as easily adopt "regulation by booklet."

Key Features of National Chartering

Despite the booklet's many comforting words and phrases, National Chartering will give the FCS's aggressive lenders nearly carte blanche to do whatever they want wherever they want while riding roughshod over less-aggressive FCS associations as well

as the FCS's public purpose.

Here are key features of National Chartering:

- If an FCS association files a National Charter application with the FCA by Sept. 30 of this year, it can begin lending outside of its present chartered territory (now called a local service area, or LSA) after Jan. 1 2001. Incredibly, the entire application consists of just a six-paragraph corporate resolution that the association's member-borrowers will not even have to approve. The association also must file a business plan with the FCA, but the FCA does not have to approve that plan before an association can begin lending outside of its LSA. Instead, the feasibility of the plan will be reviewed only in the context of the association's next safety-and-soundness examination.

- The business plan must specify the territory beyond its LSA that it will "target," be it "neighboring counties, states, or the entire national chartered territory." These should be areas or "market segments" where the association "can take advantage of its special skills or expertise, broaden its lending base, or diversify its loan portfolio" by matching "its skills, expertise and financial capacity with the opportunities provided by a national charter." FCS lenders will be able to capitalize more than ever on their tax and funding advantages.

- Even if an FCS lender "chooses not to apply for a national charter, it still should consider revising its business plan to reflect changes in its operating environment." Translation: Prudent lenders within the FCS need to prepare for an invasion by the FCS

empire builders who will be intent on cream-skimming the business of the more conservative FCS lenders. In fact, the FCA booklet makes the understatement of the year when it advises, "As other associations with national charters begin to offer products and services to customers in its territory, the competitive environment may change significantly."

• The National Chartering booklet states that expanding associations must continue to serve their LSAs. Yet that lip-service is merely a fig leaf. In fact, as USDA's Economic Research Service has documented repeatedly, FCS lenders increasingly serve agriculture's larger, older, wealthier farmers. As the empire builders plunge into other markets, where they will focus on larger borrowers, they will be less interested than ever in meeting any pretext of serving a

public mission, specifically serving small, young and beginning farmers.

• As associations expand under national charters, they may seek to change their "funding and supervisory bank," if their present bank consents. In other words, the seven FCS banks will start competing for customers among the associations. Because the banks have the same cost of funds, their only basis of competition is easier supervision. Interestingly, the National Chartering booklet does not explain how an association can appeal to the FCA if its present bank won't let it switch. This could become a new hot potato for the FCA.

National Chartering will dramatically alter the FCS, at great risk to taxpayers. Congress should take a close look at this proposal before the train leaves the station.

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