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**H**earings by the Senate and House Agriculture Committees promise to shed light on the shortcomings of the National Chartering proposal being pushed by the Farm Credit Administration (FCA). On February 26, Sen. Richard Lugar (R-IN) chaired a hearing also attended by Sen. Craig Thomas (R-WY), Sen. Tim Hutchinson (R-AK), and Sen. Mike Crapo (R-ID). On March 7, Rep. Frank Lucas (R-OK), chairman

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## Congressional Hearings On National Charters

of the Conservation, Credit, Rural Development and Research Subcommittee of the House Agriculture Committee will chair a similar hearing.

Rep. Jim Leach (R-IA) led off the Senate hearing with extremely strong criticism of the National Chartering proposal as well as of the FCA. While Leach supports the FCS as it now operates, he was unequivocal in his opposition to national chartering. Phil Burns, chairman and CEO of the Farmers & Merchants National Bank in West Point, Neb., testified on behalf of the ABA in opposition to the proposal. (See article, page 28.) FCA chairman Mike Reyna, as well as two representatives of FCS associations, testified on the wrong side of the issue.

Leach asked the committee "whether a system established to serve individual farmers of modest means should be turned upside down

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and directed to serve the nonfarm and large agribusiness community." He stated that "no compelling studies have been provided that show that America's community banks, savings and loans, credit unions, insurance companies, mortgage and a host of special purpose finance companies are unequal to the demands of the new markets that FCS managers want to penetrate." Leach asked a most prophetic question: "Will large businesses, with capacities to tap private credit markets, find it in their, but not the public's interest, to do their financing with 'captive' FCS entities?" That potential is discussed in the next section.

Reyna and the other FCS witnesses offered the usual unsubstantiated rationale for the national chartering proposal, with much emphasis by Reyna on the FCS's

supposed commitment to serve young, beginning and small farmers in LSAs (the present chartered territories of FCS associations). Particularly galling was testimony by Jack Webster, CEO of FCS of America, a \$5 billion association serving Iowa, Nebraska, South Dakota and Wyoming. He had the audacity to claim that his association "is not the dominant player in our area," yet another FCS witness produced data showing Webster's association has a market share well above the national FCS market share. Webster also claimed that "national charters will not change the cooperative nature of Farm Credit institutions," but the geographical expansion of FCS lenders will increase the day-to-day control of the managers of these institutions, lessen the role of their directors, and make member control about as relevant as it is in credit unions.

Comments on the proposed rule for national chartering had to be filed with the FCA by March 19.

### **FCA Drops Another Shoe To Promote FCS Expansion**

As noted above, Rep. Leach asked the Senate if the FCA was not ready to offer up "captive" FCS entities to large agribusinesses. That is an extremely relevant question given that the FCA Board has just authorized the AgFirst Farm Credit Bank to issue "Class A Cumulative Preferred Stock" that will count as permanent capital. The FCA has not been forthcoming about the rationale for authorizing this preferred stock, but it certainly is not because the FCS is undercapitalized – the system as a whole had a 15.5 percent capital ratio at September 30, 2000.

Preferred stock will permit an FCS institution to build its equity capital much faster than it can through retained earnings. Combine three elements: a big capital injection through preferred stock bought by a large agribusiness, an FCS association's national charter, and its ability to purchase loans originated by a non-

FCS lender (such as the agribusiness that bought the preferred stock). Presto, we have a captive FCS lender that can lend anywhere it wants with cheap financing implicitly backed by taxpayers. What a deal!

As Leach stated in his testimony, "no GSE abuse to date comes close to matching the gall of this one." Congress needs to fully explore the implications of "captive" FCS associations.

### Supreme Court Victory In Tax Case

In an important victory for taxpayers and bankers, the U.S. Supreme Court unanimously ruled on February 20 that CoBank and production

credit associations (PCAs) are subject to state and local income taxes. CoBank tried to use a typographical error in a 1985 amendment to the Farm Credit Act to claim that it was exempt from Missouri state income taxes and therefore entitled to a \$1.5 million tax refund.

In reversing the Missouri Supreme Court, the U.S. Supreme Court backed the arguments of numerous states and the ABA in stating that Congress had not intended to create this exemption for either CoBank or the 50 or so PCAs. This decision will cost CoBank and the PCAs at least \$10 million annually in state income taxes.

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