

OFFICE OF
INSPECTOR GENERAL

Survey Report

Survey of
Farm Credit System Institutions
Regarding the Agency's
Examination Function

Fourth Quarter
(July 1—September 30, 2017)
and
Fiscal Year 2017 Summary

Issued January 19, 2018



FARM CREDIT ADMINISTRATION

**Office of Inspector General's Survey of Farm Credit System Institutions
Regarding the Agency's Examination Function
Fourth Quarter Fiscal Year 2017 Summary Report
(July 1 – September 30, 2017)**

Introduction

The Office of Examination identified fifteen Farm Credit System (FCS) institutions that were in a position to provide meaningful survey responses for the period July 1 – September 30, 2017.

The Office of Inspector General (OIG) sent surveys to those institutions in November 2017. Fourteen of the fifteen institutions submitted completed surveys (93% response rate). When outstanding responses from prior quarters are received, they are included in the next quarterly report. The OIG received one response to the third quarter survey after the report was published and we included the narrative comments and numerical ratings in this report.

The OIG will continue to provide a quarterly report to you each Fiscal Year (FY) on December 31, March 31, June 30, and September 30, so that you may timely take whatever action you deem necessary to address the responses. This fourth quarter report includes FY 2017 summary data.

The survey asks respondents to rate the eight survey statements from "1" (Completely Agree) to "5" (Completely Disagree). The rating options are as follows:

Completely Agree	1
Agree	2
Neither Agree nor Disagree	3
Disagree	4
Completely Disagree	5
Does Not Apply (not included in averages)	6

Narrative responses are provided verbatim, except identifying information has been removed and any grammatical, punctuation, and spelling errors may have been corrected. Any narrative in "brackets" is explanatory information provided by the OIG based on conversations with institution management.

Survey Results – Fourth Quarter FY 2017

Average numerical responses to survey statements 1–8 ranged from 1.6 to 2.4 for the fourth quarter.

Average Numerical Response Range to Survey Statements 1–8

4 th Quarter FY17	3 rd Quarter FY17	2 nd Quarter FY17	1 st Quarter FY17
1.6 – 2.4	1.4 – 2.2	1.5 – 2.0	1.6 – 2.0

The average numerical response for all survey statements was 2.1 for the fourth quarter.

Average Numerical Response for all Survey Statements

4 th Quarter FY17	3 rd Quarter FY17	2 nd Quarter FY17	1 st Quarter FY17
2.1	1.8	1.7	1.8

In this quarter, there were both positive and negative narrative comments to survey statements 1–8. Perceived negative comments of any degree are color coded in maroon.

Survey item 9 asks for feedback on the most beneficial aspect of the examination process. Consistent with prior quarters’ responses to this survey item, many very positive comments were provided about the examiners and the examination process.

Survey item 10 asks for feedback on the least beneficial aspect of the examination process. While most were negative, as would be expected, several comments provide a perspective that should prove constructive.

Survey item 11 asks for any additional comments from the board as a whole. This item elicited several thoughtful responses from full boards, which was the objective of the question.

EXAMINATION PROCESS

Survey Statement 1: The scope of examination activities was focused on areas of risk to the institution and appropriate for the size, complexity, and risk profile of the institution.

Average Response: 2.1

Statement 1	1 st Qtr	2 nd Qtr	3 rd Qtr	4 th Qtr	FY Average
FY 2017	1.8	1.6	1.8	2.1	1.8
FY 2016	1.6	1.8	1.9	1.7	1.8
FY 2015	2.4	1.8	1.9	1.9	2.0
FY 2014	2.0	2.2	2.4	1.9	2.1

Comments:

- The scope appropriately focused on major risk areas of the institution. Follow-up on previous recommendations and requirements was thorough and appropriate.
- While the increased focus on internal controls for financial reporting is important, it is also important to maintain the focus on operational controls.
- Seems more interested in non-credit issues that do not impact the bottom line.
- I think this exam focused on areas that were very low risk. The history of our institution and institutions around the United States show the major risk is credit risk. I feel this was barely considered during this exam. The bulk of the exam was on relationships between employees, directors, and members. The feeling during the exam is that this is an area that shows enormous amounts of fraud. While these areas may have some risk, I don't believe they have the extremely dire and immediate consequences that the exam put forth. The same results could have been attained by sending an IM saying policy needs to be changed in these areas. I do not fault the examiners, they were doing what they had been told to do.

Survey Statement 2: Examiners appropriately applied laws, regulations, and other regulatory criteria to examination findings and conclusions.

Average Response: 2.1

Statement 2	1 st Qtr	2 nd Qtr	3 rd Qtr	4 th Qtr	FY Average
FY 2017	1.8	1.7	1.8	2.1	1.9
FY 2016	1.9	1.8	2.1	1.8	1.9
FY 2015	2.0	1.7	1.5	1.8	1.8
FY 2014	1.8	2.1	1.9	1.8	1.9

Comments:

- Examiners indicated the institution did not follow commonly accepted LGD practices on PCA loans totally secured by chattels. Examiners said the LGD should never exceed a "C" on PCA loans totally secured by chattels and this was a practice followed by the majority of institutions. We could find only one institution who had this practice.
- Reference to regulatory and other guidance was generally clear and concise. There were no disagreements in this area.
- In one area of the examination, there appeared to be a different interpretation of some regulatory rules than had been applied in the past, with no changes noted in the regulations related to this subject matter. Written clarification from FCA is pending and needed.

Survey Statement 3: The recommendations, required actions, and any supervisory agreement with FCA assisted the board and management in addressing the risks of the institution.

Average Response: 2.4

Statement 3	1 st Qtr	2 nd Qtr	3 rd Qtr	4 th Qtr	FY Average
FY 2017	1.8	1.8	2.2	2.4	2.1
FY 2016	2.1	2.2	2.1	2.0	2.1
FY 2015	2.1	1.8	2.0	2.3	2.1
FY 2014	1.7	2.0	2.1	2.1	2.0

Comments:

- Generally yes. There was one recommendation made which had little or no formal guidance to support it. It seemed to be derived more from opinion than guidance. However, management and board agreed with the recommendation.
- Compliance examination team had several newer staff and/or interns which lead to confusion on what was being reviewed and the findings of the review (Policies or procedures, verbiage required by regulation, etc.). It was brought to our attention during the on-site close out which then required an additional examination.
- Still waiting for written guidance from FCA on one item noted in the examination.

Survey Statement 4: The examiners were professional and efficiently conducted examination activities.

Average Response: 1.6

Statement 4	1 st Qtr	2 nd Qtr	3 rd Qtr	4 th Qtr	FY Average
FY 2017	1.8	1.5	1.4	1.6	1.6
FY 2016	1.5	1.5	1.8	1.3	1.5
FY 2015	1.5	1.6	1.9	1.5	1.6
FY 2014	1.4	2.2	1.8	1.6	1.8

Comments:

- Very professional.
- The efficiency of the exam could have been further enhanced with a coordination of the dates on site between the training team and the examination team. The EIC did try to coordinate, however it was not possible, therefore this is mentioned for future visits.
- The most recent examination was efficient when examiners were on site. After leaving the institution, the continuation of the examination seems to be very lengthy, lasting several months.
- Senior examiners were very professional conducting the examination in a thorough and open manner focusing on material findings, if any. Junior examiners need continued training in materiality to ensure a consistent and effective examination.

COMMUNICATIONS

Survey Statement 5: Communications between the Office of Examination staff and the institution were clear, accurate, and timely.

Average Response: 2.0

Statement 5	1 st Qtr	2 nd Qtr	3 rd Qtr	4 th Qtr	FY Average
FY 2017	1.6	1.5	1.7	2.0	1.7
FY 2016	1.8	1.7	1.8	1.6	1.7
FY 2015	1.5	2.0	1.7	1.8	1.8
FY 2014	1.6	2.2	2.0	1.7	1.9

Comments:

- Examiners indicated the institution did not follow commonly accepted LGD practices on PCA loans totally secured by chattels. Examiners said the LGD should never exceed a "C" on PCA loans totally secured by chattels and this was a practice followed by the majority of institutions. We could find only one institution who had this practice. [duplicate response to statement #2]
- EIC was committed to clear and timely communication. There were no surprises.
- The Examiner-in-Charge maintained excellent communication with the institution as such examination activities and agency expectations were clearly outlined and results of examination activities were fully understood.

Survey Statement 6: Examination communications included the appropriate amount and type of information to help the board and audit committee fulfill their oversight responsibilities.

Average Response: 2.1

Statement 6	1 st Qtr	2 nd Qtr	3 rd Qtr	4 th Qtr	FY Average
FY 2017	1.8	1.6	1.7	2.1	1.8
FY 2016	1.7	1.7	1.6	1.6	1.7
FY 2015	2.0	1.8	1.7	1.9	1.9
FY 2014	2.1	2.2	1.8	1.9	2.0

Comments:

- Appropriate comments between FCA and the Board and Audit Committee were provided so the Board and Audit Committee are able to responsibly complete their oversight.

Survey Statement 7: Examiners fairly considered the views and responses of the board and management in formulating conclusions and recommendations.

Average Response: 2.1

Statement 7	1 st Qtr	2 nd Qtr	3 rd Qtr	4 th Qtr	FY Average
FY 2017	1.6	1.8	2.1	2.1	1.9
FY 2016	1.9	1.8	1.9	1.8	1.9
FY 2015	1.8	1.6	1.9	2.1	1.9
FY 2014	1.8	2.2	1.9	2.1	2.0

Comments:

- Ample opportunity was given to discuss all areas of the examination.
- Senior examiners did an excellent job of asking questions, reviewing documents and remaining open to the institution's position prior to reaching a conclusion. Presentation to the Board was informative, concise and fair.
- **It's generally accepted by all institutions in our district that views and responses of the Board and management hold no value to FCA.**

Survey Statement 8: FCS-wide guidance from the Office of Examination was proactive and helpful.

Average Response: 2.3

Statement 8	1 st Qtr	2 nd Qtr	3 rd Qtr	4 th Qtr	FY Average
FY 2017	2.0	2.0	1.9	2.3	2.1
FY 2016	1.7	2.2	2.2	1.8	2.0
FY 2015	1.9	1.9	2.0	2.2	2.0
FY 2014	2.0	2.2	2.0	2.1	2.1

Comments:

- A few minor inconsistencies from FCA Examiners were relayed to institution staff regarding information required in Policies and best business practices.
- Generally guidance issued provides sufficient insight on the Agency’s risk concerns and expectations.

GENERAL QUESTIONS

Survey Item 9: What aspect of the examination process did you find **most** beneficial?

Comments:

- We highly value the open communication we have with the FCA staff assigned to our institution.
- Close interaction with the EIC - ongoing communication before during and after the examination.
- The new EIC provided positive enhancements in both efficiency and communications to the examination process and the reporting to the board.
- The time and dialogue provided by FCA staff in discussing the Regulator's interpretation of regulations and ways to further enhance our policies and procedures.
- Improved interaction with the agency personnel during the examination process - credit given to the direction and example set by the EIC.
- The most beneficial aspect of the examination process continues to be providing management with an assessment of their regulatory compliance and risk management ability which in turn provides the board with information to assist in effectively overseeing the institution.
- FCA clearly communicated what information was needed from the institution. FCA staff was efficient during the on-site portion of the exam. Examination was comprehensive, thorough, and reasonable.
- Good communication with EIC and the supervisor.
- The exam team did a good job and was very professional.
- I have been on the Board for 17 years. **This is the first exam that I remember that I can't name any part that was beneficial.**

Survey Item 10: What aspect of the examination process did you find **least** beneficial?

Comments:

- Examiners giving their personal opinions on how credit should be administered rather than quoting or referring to actual regulation.
- It seems every exam has a high number of staff that is in training. FCA must be mindful that using the institutions as a "training ground" provides additional energy on staff. The institution recognizes this training can't be accomplished without the field experience, but believes it points to a larger concern of turnover in the FCA that needs to be addressed. We do believe when FCA disseminates information back to the institution it should be mindful of those receiving the communication, respecting the sensitivity of the content and impact on staff.
- As stated previously, due to the inability to coordinate the two teams (training and examination), there was a duplicative effort on staff to provide information and explanations to questions. In addition, a greater transfer of knowledge could be accomplished if the schedules coincided.
- The experience level of a few examiners led to some misunderstanding on what information was necessary or needed.
- Hours and energy spent on non-credit issues.
- This exam was a little unusual with the focus being so heavily weighted on ICFR. Thus, it appeared there was an awful lot of attention placed there, even though the exam came out well for us.
- I don't know where to start.

Survey Item 11: Please provide any comments from the **Board as a whole** regarding the examination process not provided in the preceding responses.

Comments:

- Two way communication has been positive.
- The board was appreciative of the executive session. The board was also appreciative of comments made regarding capital planning of the institution.
- We were pleased with the efforts shown by [examiner names removed] to improve the exam experience via improved processes and communications with both the board and management team.
- The Board will work with management to assure any and all recommendations are accomplished.
- As a board, we appreciate the candor and constructive comments provided by the examiner staff. The ability to have open two-way conversations with the examiners is extremely helpful.
- The Board found the examination process to be satisfactory and the results reasonable.
- Good communication between FCA and the board. Board was appreciative of that and report was appropriate length and written professionally.
- The upside for the Board in the change in focus is we got a fresh look in an area that often doesn't get the attention it probably deserves.
- This exam was exhausting.

FY 2017 Summary Report

Numeric Responses to Survey Statements 1–8

The table below provides cumulative data for the FY 2017 numeric ratings for survey statements 1-8. During FY 2017, the OIG sent surveys to 57 FCS institutions and we received 52 responses. This is a 91% response rate, up 5% from FY 2016. The overall average response for all survey statements was 1.9. It is noteworthy that 90.2% of the numerical ratings were either “completely agree” (1), or “agree” (2), for FY 2017, compared to FY 2016, which was 86.7% for the total of those ratings. This shows an improvement in the FCS institutions’ view of the examination process and experience.

Statement	PERCENTAGE OF TOTAL RESPONSES												Average Response
	Completely Agree (1)		Agree (2)		Neither Agree nor Disagree (3)		Disagree (4)		Completely Disagree (5)		Does Not Apply * (6)		
1	13	25%	35	67%	3	6%	1	2%	0	0%	0	0%	1.8
2	11	22%	38	73%	1	2%	1	2%	0	0%	1	2%	1.9
3	8	16%	35	66%	6	12%	3	6%	0	0%	0	0%	2.1
4	22	44%	27	50%	3	6%	0	0%	0	0%	0	0%	1.6
5	19	38%	28	52%	5	10%	0	0%	0	0%	0	0%	1.7
6	12	24%	37	70%	3	6%	0	0%	0	0%	0	0%	1.8
7	13	26%	34	64%	3	6%	1	2%	1	2%	0	0%	1.9
8	5	10%	38	72%	8	16%	1	2%	0	0%	0	0%	2.1
Total Responses	103	24.8%	272	65.4%	32	7.7%	7	1.7%	1	0.2%	1	0.2%	1.9

Note: Responses of “6” (Does Not Apply) were not included in average response numbers.