

**Remarks by
The Honorable Dallas P. Tonsager
Board Chairman and CEO
Farm Credit Administration
AgFirst Farm Credit Bank Annual Meeting
Asheville, North Carolina
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Good morning! Thank you for your kind welcome. For his leadership of the AgFirst district, I'd like to recognize President and CEO Tim Amerson, who is also chairman of the Funding Corporation. Tim is leading an important initiative on internal controls over financial reporting, and I appreciate his work in this area. I was sorry to hear that Board Chairman John Langford is on medical leave and can't be with us today. I will keep him in my thoughts and prayers. I would also like to recognize Board Vice Chairman Curtis Hancock for his leadership. Both John and Curtis have served the AgFirst board with distinction for several years.

When Ken Spearman passed away earlier this year, I lost an esteemed colleague and friend. Having served as a director on your board, Ken had a special relationship with AgFirst. His service to the System and the Farm Credit Administration was outstanding, and we will continue to benefit over the years from the leadership he provided.

One of the areas on which Ken focused during his time as FCA chairman was internal controls. I would like to continue this focus because I believe that having strong internal controls is central to building public confidence in the Farm Credit System. A key focus in my speech to the Farm Credit Council earlier this year was the importance of confidence. The System needs the confidence of all its stakeholders, from the farmers and ranchers it was created to serve, to its investors, to the members of Congress who oversee the System and FCA.

As board members and managers of the bank and associations in your district, you hold the key to public confidence in your institutions. It is up to you to provide the oversight necessary to prevent fraud and abuse and to make sure your institutions serve their mission and stay safe and sound.

As part of providing a robust set of internal controls, you must be sure to provide for a separation of duties within your institutions so that multiple individuals are involved in any given loan transaction. For example, a loan officer should never have the authority to override controls designed to provide checks and balances in the loan-making process. I also urge you to carefully consider any incentives you provide your loan officers that might indirectly motivate them to take undue risks or commit fraud.

As the regulator of the Farm Credit System, we will do our part to oversee your institutions. For example, we are considering repropounding our standards of conduct regulation to require each System institution to establish its own benchmarks, policies, and procedures for its

standards of conduct program. We believe that this would place principles of loyalty, fairness, and ethics at the core of each institution's business practices.

In my speech to the Farm Credit Council earlier this year, I laid out five points that I thought were critical to the success of the Farm Credit System. Confidence was the first one. The other four points help to strengthen confidence. The first is to seek the "best possible outcome" for every borrower. System borrowers have experienced increased stress from lower commodity prices and, in many areas, lower farmland prices. These stresses have caused some borrowers, especially those who fall into the categories of young, beginning, and small, to have difficulty making their loan payments. By proactively identifying these borrowers and working with them to find the best ways out of their financial difficulties, you are helping them achieve their best possible outcomes. Working with borrowers in this regard will build the confidence of your stakeholders in the System's safety and soundness and its dedication to its mission.

By encouraging you to work with borrowers in difficulty, I am not, however, suggesting you throw caution to the wind. To be able to serve future generations of borrowers, you must pay close attention to your safety and soundness, and we, as the regulator, must maintain the integrity of our examination function and call the FIRS ratings as we see them.

My third point involves partnerships. Through partnerships you can build the confidence of your stakeholders by making valuable investments in rural communities, where most of your borrowers live. And by the way, the agency has established a fast-track approval process for those investment applications that meet the conditions we've set forth.

The fourth point is to provide all System services to all System borrowers. In any given area of lending, the System has institutional experts. If your institution doesn't offer a particular product or service, look for a System partner so that the people in your territories can get what they need. Although each institution is owned and controlled by its shareholders, all institutions are part of the same network established by Congress to serve agriculture. That's why I believe it makes sense for all System borrowers to have the same access to all System services.

And my fifth point is about System structure. Rather than allowing the System to evolve in a haphazard way, System institutions need to give careful thought to all changes in structure. And by System institutions, I truly mean all System institutions — not just those contemplating mergers. Again, because the System is a network of institutions, the actions of a few impact all others.

I have also called for a year of dialogue between FCA and the System on structure. I would like to expand on that idea now by urging System institutions to continue discussing among yourselves the impact of mergers and other structural changes. The goal of most mergers is to achieve economies of scale, which can offer many benefits, such as making credit more affordable to borrowers. In some ways, however, mergers can impair the ability of institutions to serve their borrowers. By discussing these issues among yourselves, you may be able to find an optimal balance between efficiency and mission fulfillment.

And speaking of mission, the System has a particular mission to serve young, beginning, and small (or YBS) farmers. Congress amended the Farm Credit Act in 1980 to emphasize service to YBS farmers. They recognized that these farmers are not only critical to the future of agriculture but are also more vulnerable to downturns in the farm economy. In other words, they need a little extra help.

I'd like to see a show of hands. How many of us here have ever been a young or beginning farmer? I think all of us, right? And we can probably all remember a time when we could have used a little help — if not in the form of credit, then at least in the form of good, sound advice.

Back in 1976, when I was a 22-year-old dairy farmer, my brother and I decided to build a new free-stall barn and milking parlor. We had a contractor do some of the work, but we also did a lot of it ourselves. When the project was almost finished, we had hundreds of pieces of scrap metal and wood spread out all over the construction site.

Thinking it was time for a good clean-up, I had a guy with a backhoe dig me a hole straight down about 20 feet or so and about 8 feet across. Unfortunately, I underestimated the size of the hole. By the end of the day, the hole was full, but I still had a lot of scrap to get rid of.

What was I going to do? Of course, I could have the guy come back and widen the hole, but that would have taken another day or so. And I was 22 — patience was not one of my virtues. As I studied the contents of the hole, the answer dawned on me. Since most of the scrap was wood, I would just burn it! Then there would be plenty of room for the rest of the scrap.

So I splashed about five gallons of gasoline in the hole, stepped back a few feet, lit a match, and tossed it in.

The explosion was so big that it knocked the breath out of me and hurled me backwards about 10 feet. I scrambled to my feet as the contents of the hole rained down around me.

I learned a lot of life lessons that day. Not the least of which was, the quickest solution is not always the best one.

As this story illustrates, young and beginning farmers tend to need a little guidance. At least I did. That's why training is an important part of the service that institutions can provide YBS producers. YBS seminars help producers develop smart business plans, find cost savings, and consider operational changes that can help them weather downturns. Unfortunately, I don't think these seminars cover how to avoid blowing yourself up when getting rid of construction waste. That's a lesson you learn from the School of Hard Knocks.

I would like to take this time now to commend the AgFirst district for doing a really good job of serving YBS producers. I understand that most of your associations have extensive outreach programs for YBS borrowers and that you actively support youth programs such as FFA and 4-H.

In 2016, both the number of loans and the dollar volume of new and outstanding loans in the AgFirst district increased in each YBS category. Also in 2016, 162 borrowers and prospective borrowers across your district participated in the Ag Biz Planner program designed to prepare young, beginning, small, and minority farmers for success. I understand that some of your institutions even provide financial incentives to YBS borrowers who complete your training programs. These efforts are important. They help ensure the success not only of the producers to whom they are targeted but also the long-term success of our nation's ag industry.

And now I'd like to turn to FCA's regulatory agenda, which you've asked me to address. As a regulator, it's our job to provide regulations that help you meet your mission, preserve your safety and soundness, and comply fully with all laws. But we also want to make sure that we never go beyond these three goals.

In the spirit of President Trump's initiative to ease regulatory burden, we have issued our regulatory burden notice one year earlier than we are required to do under the Farm Credit Act. In fact, we're currently accepting comments on this notice on our website, so I invite you to share any recommendations you have for the removal or revision of outdated, unnecessary, or burdensome regulations. The comment period for this notice closes on August 16.

Our goal is always to issue regulations that strengthen the System's ability to meet its congressional mission. For example, I believe the proposed rule we are developing on standards of conduct will help protect the System against wrongdoing or the appearance of wrongdoing. This is important to the mission because it will strengthen confidence in the System so that more farmers will turn to System institutions for their credit needs and more investors will turn to the System for sound investments.

We are also seeking to finalize the investment eligibility rule, which would allow associations to make government-guaranteed investments for specific risk management purposes within certain portfolio limits.

We are reviewing our collateral evaluation regulations to determine where updates are needed, and we are reviewing the ways System institutions use stress testing in their business planning and risk management.

Of course, we also provide guidance to the System through means other than regulations. Recently we issued guidance on identifying and reporting suspected criminal activities; we plan to issue further guidance on this topic in the future.

I would like to thank the AgFirst district for your willingness to accept our guidance, listen to our concerns, and take the corrective actions called for in reports of examination. We are also grateful to the AgFirst associations for reaching out to us when you've had issues involving standards of conduct and information technology. And I would like to commend you for being proactive in developing loan servicing strategies for borrowers who are experiencing financial difficulties due to low commodity prices.

Since there's no relief in sight from low commodity prices, I'd like to encourage you to continue being proactive in this way. You'll need to be especially attentive regarding borrower rights, which all institutions are required by law to provide. By carefully adhering to the regulatory processes for identifying and handling distressed customers, you can protect your institution from both legal and reputation risks. And what's more, you can help these borrowers achieve their best possible outcomes.

Since our examiners have identified some instances of noncompliance with borrower rights, I would encourage you to consider providing refresher training in this area, including the role of credit review committees in providing these rights.

I'll close with just a few parting thoughts. The AgFirst district has experienced some significant challenges over the past year or so. As if an extended period of low commodity prices were not enough, your district faced some major weather-related challenges.

After parts of South Carolina experienced severe drought in the spring of 2015, catastrophic flooding occurred in the fall. Then, in late 2016, Hurricane Matthew brought trouble to producers in both North and South Carolina. Later, in March 2017, a freeze hit some Georgia producers hard. As a result, even some associations with diverse portfolios are starting to see declines in credit quality.

So far this year, rainfall has been sufficient, and conditions for many of the major crops in your district — corn, soybeans, winter wheat, cotton, peanuts, and hay — look favorable. Crop price expectations for 2017 are similar to those of last year although peanut prices are expected to be somewhat higher and cotton prices somewhat lower. The livestock sector, including broiler, dairy, and hog enterprises, have a modest profit outlook for the rest of this year.

So, in general, your district is doing well. Your financial condition is strong. Your service to YBS producers is growing. And the term limits you've established for your bank's board of directors serves you well by providing for new perspectives and leadership opportunities.

By further strengthening your internal controls, by paying close attention to borrower rights provisions, and by closely monitoring credit quality, your district can continue to improve in condition and performance, even in the face of today's challenging farm economy. And your district's dedication to cooperative principles will help ensure that you continue to meet the mission for which the System was created more than a century ago.

Again, thank you for the opportunity to join you today.