Farm credit law set for approval

by Susan B. Cohen

Despite a strenuous lobbying effort by the American Bankers Association (ABA), the trade association for the nation's larger commercial banks, legislation amending the laws governing the Farm Credit System and significantly broadening the system's ability to serve the credit needs of the nation's agricultural economy was reported out of the House Rules Committee and scheduled for action with provision for two hours of debate on the House floor this week.

While spokesmen for Cong. Ed Jones (D-Tenn.), sponsor of H.R. 7548, doubt that the bill will actually get acted on in the remaining days before the Oct. 4 recess, they intend to bring it up in November during the lame-duck session and see "no big problems" in its approval, swift passage through conference, and enactment by the President. The Senate version of the bill, S. 1465, has already been passed and the two bills do not differ greatly.

Leading features of the legislation, the first serious revision of the Farm Credit Act of 1971 which governs the Farm Credit System, are as follows. It would:

- Allow the banks of cooperatives to finance agricultural exports which benefit a U.S. cooperative, including the provision of all financial services involved, such as receiving and holding credit balances from banks and borrowers, and trading bankers' acceptances associated with international trade, including the ability to make loans to associated parties when a member co-op stands to benefit;
- Authorize Federal Land Banks and Production Credit Associations to finance processing and marketing undertakings directly related to an applicant's farm, ranch, aquatic operation, etc.;
- Allow Federal Land Banks and Production Credit Associations to finance processing and marketing undertakings directly related to an applicant's farm, ranch, aquatic operation, etc.;
- Allow Farm Credit System institutions to invest and participate in loans of other institutions;
- Allow the Federal Intermediate Credit Banks (FICBs), the discount banks for the Production Credit Associations, to discount the agricultural loans of other financial institutions.

The legislation would also lower from 80 percent to 60 percent the proportion of a cooperative's membership that must be "farmers" to entitle that co-op to Banks for Cooperatives financing. With the numbers of practicing farmers declining significantly, this provision is essential to prevent a cutoff of funding to, for instance, the Rural Electric Cooperatives and Associations that supply power to rural communities.

The provision for export financing by the System and the relationship of so-called other financial institutions to the System have been the most controversial aspects of the legislation. Financing capability is one of the principal roadblocks to any of the several large farmer cooperatives marketing their own grain internationally in direct competition with the five major grain companies that now totally monopolize the trade. Efforts to discover the grain companies' stand on the legislation yielded the standard "no comment"—often in the form of unreturned phone inquiries—that the secretive giants are known for. Sources say that there is no way to tell whether the companies helped finance the opposition to the legislation, but surmise that a decision was probably made that the ABA should carry the ball for all the opponents.

In its capacity as an independent source of funds outside of the Federal Reserve System, the Farm Credit System is eyed jealously by large commercial banks like the Bank of America and the Northwest Bank Corporation of Minneapolis, who have led the charge to gain access to System discount facilities to cash in on interest rate differentials and generally give their own money management operation more flexibility at a cheap price. Many of the smaller commercial banks and their affiliates, as well as credit corporations formed by production associations, on the other hand, that have no access to money markets themselves, rely on the Farm Credit System on a fairly regular basis in addition to their special needs in periods of tight credit such as this past spring.

At any given time from 3 to 5 percent of total FICB discounts are for a total of about 250 other financial institutions. But as a spokesman for the System's regulatory body, the Farm Credit Agency, explained, the System is strictly guided in the initiation and continuation of these relationships, which are permanent, by the needs and interests of the farm and rural economy as opposed to the speculative designs of money center banks.

The 1979 legislation provides for the application of four criteria on considering establishing a discount relationship with another financial institution: 1) the institution must have at least 25 percent of its business in

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agriculture; 2) the institution must show a demonstrated, continuing need for funds; 3) that institution must show that it has limited access to alternative sources of liquidity; and 4) the institution is prohibited from using the discount funds for the purpose of expanding non-agricultural lending. While there is nowhere specified any size limitation on an applicant bank, these parameters tend to rule out the Banks of Americas absolutely, and effectively place a serious "burden of proof" on any bank with more than $100 million in capital.

As recently as one month ago, ABA spokesmen told this writer that they were "very doubtful" that the bill would escape from the Rules Committee without penalties. More than a year ago when the Senate bill was proposed the ABA mounted a full dress campaign to prevent what they have portrayed as "unfair competition" and "encroachment" on banking activities "outside the farm sector" by the FCS. Since that time, however, the FCS has assembled powerful support, winning both the Independent Bankers Association—representing the smaller commercial banks in the country—the several-million-member American Farm Bureau Federation and the Independent Insurance Agents of America to defense of its critical role in the farm economy.

The ABA's claim of "unfair competition" and unfair tax breaks enjoyed by the FCS is belied by the facts. While the FCS's lending activities tend to fluctuate with the cost of money in national money markets, its expanding share of the farm lending market in recent years has not come at the expense of the commercial banks principally concentrated in the operating loan category. Rather, expansion has been by the Federal Land Banks arms of the FCS, as primarily insurance companies and individuals pulled out of the real estate financing market. And, as one spokesman for the System put it, with regard to the tax breaks charge "they couldn't be too substantial because opponents of the System haven't been able to attack the subject directly."

What is the Farm Credit System?

With an annual loan volume of approximately $50 billion, the Farm Credit System is the largest single lender to American agriculture—traditionally splitting operating lending with the commercial banks, and expanding real estate financing significantly in recent years. The System consists of four arms: the Federal Land Banks, the Banks for Cooperatives, the Federal Intermediate Credit Banks, and the Production Credit Associations.

Originally launched by the federal government, the System is now a wholly member-borrower-owned institution. The System has direct access to national money markets, floating its own bonds to raise funds. Farm Credit System bonds are among the highest-rated financial instruments in the nation.

The System was built up piecemeal between 1916, when the Federal Farm Loan Act authorized the establishment and initial capitalization of the 12 Federal Land Banks, and 1933, when the Production Credit Associations and the 12 Banks for Cooperatives were authorized. In 1933 the Farm Credit Administration was created by executive order of the President, and the various farm credit institutions were placed under its supervision. By 1953 all government capital was repaid, and the independent System presently functions under the authority of the Farm Credit Act of 1971, which superceded all previous legislation governing System entities.

An excerpt from the 1971 Farm Credit Act—which the present legislation is amending—outlines clearly the explicit purpose vested in this unique institution:

> It is declared to be the policy of the Congress, recognizing that a prosperous, productive agriculture is essential to a free Nation and recognizing the growing need for credit in rural areas, that the farmer-owned cooperative Farm Credit System be designed to accomplish the objective of improving 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 to selected farm-related businesses necessary for efficient farm operations.

With a stabler rate structure, the FCS has acted generally to shield the farm sector from the violent short-term fluctuations in financial conditions—for instance, this spring the System experienced a boom in lending demand when Volcker's credit policies squeezed off credit to the commercial banking system. Ultimately, of course, since it raises money in the national markets, the System is dependent on the health and conditions of capital flows in the economy generally.