

FARM CREDIT SYSTEM INSURANCE CORPORATION
POLICY STATEMENT CONCERNING ASSISTANCE
DATED: JULY 12, 2023

Background

The Farm Credit System Insurance Corporation (Corporation or FCSIC), in its sole discretion, is authorized under section 5.61(a) of the Farm Credit Act of 1971, as amended (Act), 12 U.S.C. 2277a-10(a), to provide, on such terms and conditions as the Corporation's Board of Directors may prescribe stand-alone assistance in the form of loans, asset or debt security purchases, assumption of liabilities, or contributions to:

- a) prevent the placing of a Farm Credit System institution¹ into receivership,
- b) restore the institution to normal operation, or
- c) reduce the risk to the Corporation posed by the institution when severe financial conditions threaten the stability of a significant number of other institutions or System institutions possessing significant financial resources.²

The Corporation's Board of Directors may also prescribe assistance to facilitate a merger or consolidation of a "qualifying" troubled System institution with another System institution through loans, loan guarantees, asset or debt security purchases, assumption of liabilities, contributions, or any combination thereof. A "qualifying" troubled System institution is an institution that is:

- a) in receivership,
- b) in danger of being placed in receivership, or
- c) an institution that, when severe financial conditions exist that threaten the stability of a significant number of System institutions or of System institutions possessing significant financial resources, requires assistance to lessen the risk to the Corporation posed by such System institution under such threat of instability.³

Pursuant to section 5.61(a)(3) of the Act, FCSIC may not provide assistance unless the means of providing assistance is the least costly means of providing the assistance by the Farm Credit Insurance Fund of all possible alternatives available to the Corporation, including liquidation.⁴ In making this determination, the Corporation is authorized to gather

¹ Section 5.61(a) of the Act uses the terms "insured System bank" and "bank" but the Act also specifies under section 5.61(e), 12 U.S.C. 2277a-10(e), that such terms also include production credit associations and other associations making direct loans under the authority provided under section 7.6 of the Act, 12 U.S.C. 2279b. Consequently, the terms "troubled System institution," "troubled System bank," or "troubled System association" are used to refer to those institutions specified in sections 5.61(a) and 5.61(e) of the Act, 12 U.S.C. 2277a-10(a) and 2277a-10(e).

² FCSIC is also authorized to provide assistance to bridge System banks under section 5.61C(h)(7). This policy statement does not apply to the provision of assistance in those circumstances.

³ See Act, section 5.61(a)(2)(B), 12 U.S.C. 2277a-10(a)(2)(B).

⁴ The cost of liquidation shall be made as of the earliest of: (1) The date on which a conservator is appointed for the institution, (2) the date on which a receiver is appointed for the institution, or (3) the date on which the Corporation makes any determination to aid the institution. See Act, section 5.61(a)(3)(C)(ii)(I-III), 12 U.S.C.

information necessary to perform the least-cost test⁵ and shall (1) evaluate alternatives on a present-value basis, using a reasonable discount rate, (2) document the evaluation and the assumptions on which the evaluation is based, and (3) retain the documentation for not less than 5 years.⁶

Policy Statement

The Corporation will consider assistance in accordance with the requirements of the Farm Credit Act. Any FCSIC discretionary provision of financial assistance must be consistent with and in support of FCSIC's statutory purpose to insure the timely payment of principal and interest to investors in insured Farm Credit System bank securities. Any assistance proposal may be submitted either directly from a troubled System institution, from System institutions seeking to acquire or assist a troubled System institution, or from the System banks to stem a liquidity crisis. When considering assistance proposals received from System institutions, the Corporation will:

- Maintain flexibility and readiness to respond appropriately on a case-by-case basis;
- Establish a transparent process that independently considers all relevant information;
- Ensure supervisory bank involvement in any assistance request for an association;
- Grant assistance only when there is sufficient information available to justify assistance in accordance with the least-cost test; and
- Coordinate with FCA on troubled institutions prior to granting assistance.

In the event the Corporation exercises its discretion to provide assistance, in most cases assistance would be provided to the supervisory bank, regardless of whether the troubled System institution is a bank or an association.

If the Corporation determines it is appropriate based on the facts and circumstances surrounding the request, the Corporation will provide System institutions the opportunity to submit any information, including information on the cost to the Farm Credit Insurance Fund (Insurance Fund) of a liquidation. The Corporation will then conduct a least-cost test to determine whether the cost of providing assistance is less costly to the Insurance Fund than the cost of liquidating a System institution. If the cost to the Insurance Fund of providing assistance is less than the cost of liquidation, and the Corporation, in its sole discretion, approves assistance, the Corporation will enter into an agreement with the System institution receiving assistance.

2277a-10(a)(3)(C)(ii)(I-III).

⁵ See Act, sections 5.58(8) and 5.59(b), 12 U.S.C. 2277a-7(8) and 2277a-8(b). The Corporation will accord such other System institutions as the Corporation determines to be appropriate the opportunity to submit information relating to the determination. See Act, section 5.61(a)(3)(A), 12 U.S.C. 2277a-10(a)(3)(A).

⁶ See Act, section 5.61(a)(3)(B), 12 U.S.C. 2277a-10(a)(3)(B).

Assistance Proposals

Assistance proposals can include requests for loans, loan guarantees, loss-sharing arrangements, asset or debt security purchases, assumption of liabilities, or cash contributions. The Corporation will consider the nature of the financial assistance requested on a case-by-case basis and may alter the form or amount of assistance as part of its determination. FCSIC shall consider the following criteria when assessing assistance proposals:

- 1) Financial condition and performance criteria to better understand the problem that caused the need for assistance, including the rationale for seeking assistance;
- 2) The type and amount of assistance needed, as well as a reasonable repayment plan.
- 3) Fee arrangements with attorneys, accountants, consultants, and other parties incident to the request for assistance (or projected costs for these arrangements);
- 4) Reasonable projections to assess the future viability of the institution after assistance has been provided. This would include earnings projections and a capital restoration plan to achieve adequate capitalization. Earnings projections and the capital restoration plan must include the impact of repayment of assistance;
- 5) A business plan that would implement written policies and procedures designed to guide operations safely and soundly and to correct the problems that caused the need for assistance. The plan should include an internal control system to monitor ongoing performance with measurable criteria and an operating budget, including compensation arrangements covering directors and senior officers. The business plan should also provide sufficient information to allow the Corporation to evaluate the adequacy of managerial resources of the institution in accordance with the Act. Plans to continue the service and compensation of directors and senior officers must be pre-approved by the Corporation before it provides assistance and until assistance is repaid;⁷ and
- 6) Analysis of the effect of assistance on shareholders, uninsured creditors (e.g., impairment on subordinated debt), other System institutions and the financial markets. If the troubled System institution is an association, the analysis should include the impact on its funding bank's ability to continue meeting its insured obligations.

The Corporation's assessment of assistance requests should incorporate internal FCSIC staff analysis, FCA examination reports, as well as information provided in assistance proposals. Assistance proposals that contain robust information and explanation to address each of the above criteria will facilitate FCSIC staff's review and assessment. FCSIC staff should not recommend the provision of assistance if the proposal does not:

- Include, for stand-alone assistance, a detailed analysis of how such assistance will return the troubled System institution to a financially viable, self-sustaining

⁷ See Act, section 5.61(a)(3)(D).

- operation,
- Demonstrate, when the proposed assistance is to facilitate a merger, that the continuing System institution can safely and soundly absorb the financial and operational impact that will result from the merger, and
 - Include, in the event the assistance is for an association, an explanation and analysis of why the association's supervisory bank is either unable or unwilling to provide the necessary assistance itself.

The Corporation reserves the right to request additional information as needed to conduct the least-cost test.

The Least-Cost Test

The Corporation will conduct a least-cost test to determine whether providing assistance to a troubled System institution is less costly to the Insurance Fund than liquidating the institution.⁸ In conducting the least cost test, Corporation staff shall use a four-step approach as follows:

First, determine the estimated liquidation value of the troubled System institution. In making this determination, the Corporation will use its examination authority under section 5.59(b) of the Act, 12 U.S.C. 2277a-8(b), to collect information from the troubled System institution to calculate the estimated liquidation value of the troubled System institution. This information must, at a minimum, include specific data elements as determined by Corporation staff to conduct a present-value analysis of the troubled System institution's assets, using a reasonable discount rate. As required by the Act, the troubled System institution must provide the Corporation all information necessary to perform a least-cost determination.

Second, the Corporation must reasonably estimate whether the liquidation of the troubled System institution(s) creates a loss to the Insurance Fund. Since the Insurance Fund was primarily established to insure the timely payment of principal and interest on System bank insured debt obligations, a loss to the Insurance Fund occurs when a System bank defaults on an insured obligation and the Corporation must use the Insurance Fund to pay maturing obligations. To conduct the least-cost test, the Corporation must consider whether the troubled System institution's failure will impair a System bank's ability to pay its insured debt obligations. If, however, the Corporation reasonably estimates that the funding bank can sufficiently absorb an association's estimated losses, there would be no cost to the Insurance Fund and little basis for the Corporation to provide assistance.

In conducting this analysis FCSIC staff shall consider all potential direct and indirect losses, to the extent they can be reasonably estimated, to the Insurance Fund. Direct losses include the estimated losses to the Insurance Fund from the liquidation of a troubled System institution. Indirect losses to the Insurance Fund include the consequent effects of liquidating

⁸ This section does not apply to liquidity assistance in exigent market circumstances, since, as noted below, there would be no cost to the Insurance Fund.

a troubled System institution. Indirect losses to the Insurance Fund could result from the following scenarios:

- Meaningful increase in the risk of bank default on insured obligations due to direct note losses from a troubled association;
- Higher levels of risk in association direct notes due to a general broad decline in loan and collateral values caused by the liquidation of a considerable amount of agricultural loans in a relatively short period of time;
- Ongoing losses and capital deterioration at System banks due to a substantial and sustained increase in the cost of funds for System banks resulting from a troubled System institution being placed into receivership;
- Ongoing losses and capital deterioration incurred by a System bank due to the loss of significant revenue and capital resulting from district association failures and the inability of the bank to recoup such losses from remaining district associations; and
- The liquidation of one troubled System institution causes another System institution to default on its insured debt obligations.

We expect System banks to provide the Corporation with sufficient information and analysis to demonstrate that indirect losses to the Insurance Fund will result from the liquidation of a System bank or association.

Third, the Corporation must determine the type and amount of assistance. The cost of providing assistance will depend upon the structure of the assistance. For example, the Corporation's purchase or servicing of distressed assets from a troubled System institution may cost the Insurance Fund more than providing the institution a loan with a repayment plan. If the assistance can be structured with a repayment feature, it is likely to be the least costly means of providing assistance of all possible alternatives available to the Corporation. Moreover, if other System institutions are willing to contribute some of their funds to the troubled System institution to reduce the cost of providing assistance, the Corporation will factor this amount into its least-cost test and assistance determination.

The final step in the least-cost test is to compare the cost of liquidation to the cost of providing assistance. If the cost of providing assistance from the Insurance Fund is less than the cost of liquidating a troubled System institution (to the Insurance Fund), the Corporation's Board of Directors, in its discretion, may approve assistance to the troubled System institution. As required by statute, the Corporation shall use the information it receives during its least-cost determination to evaluate the alternatives, document the evaluation and the assumptions on which the evaluation is based, and retain the documentation for not less than 5 years.

Liquidity Assistance in Exigent Market Circumstances

FCSIC may provide short-term liquidity assistance during exigent market circumstances where there is a broad, disruption across U.S. credit markets that originates external to and

independent of the System. The Corporation considers the provision of liquidity assistance in exigent market circumstances to meet the statutory authority of Section 5.61(a)(1)(C) to reduce the risk to the Corporation posed by the institution when severe financial conditions threaten the stability of a significant number of System institutions or System institutions possessing significant financial resources. When such short-term liquidity assistance is provided to a System bank as an appropriately collateralized loan, the Corporation has determined that such assistance satisfies the least-cost test required by Section 5.61(a)(3) of the Act because the cost to the Insurance Fund of providing the assistance is expected to be zero. Additionally, in the context of providing only short-term liquidity assistance in exigent market circumstances, the Corporation will consider the adequacy of managerial resources and the continued service of any bank director or senior ranking officer approval requirements of Section 5.61(a)(3)(D) as satisfied. FCSIC shall maintain procedures for the provision of liquidity assistance in exigent market circumstance and provide periodic training for/consultation with System banks on the application of the procedures.

FCSIC currently has an annually renewable \$10 billion line of credit with the Federal Financing Bank (FFB), which allows FCSIC to provide additional liquidity assistance to System banks than is otherwise available from the Insurance Fund. FCSIC will use the same liquidity assistance procedures whether or not it needs to borrow additional funds from the FFB. Draws under the FFB line of credit may only be made during periods of exigent market circumstances.⁹ FCSIC staff shall make all practicable efforts to maintain a line of credit with the FFB. FCSIC's issuance of an obligation to the FFB to access that line of credit also satisfies the least-cost test required by Section 5.61(a)(3) of the Act because the cost to the Insurance Fund of providing assistance is expected to be zero.¹⁰

Assistance Agreements

If the Corporation provides assistance, it will enter into an agreement with the System institution receiving assistance. In instances where a System association is receiving assistance, the agreement will be among the Corporation, the System association and the association's supervisory bank. The Corporation, in consultation with FCA, will determine the terms and conditions of the agreement on a case-by-case basis and may include limits on (or prior approval of) the types or amounts of activities the institution can engage in while assistance is outstanding. For example, assistance agreements might include capital restoration plans that include the impact of assistance repayment, repayment terms that recoup the costs associated with providing assistance, and limits on concentration risk, patronage and dividend payments, executive compensation, and certain types of expenses. Assistance agreements may also provide the Corporation the right to have a representative attend the institution's board meetings.

⁹ Additionally, in order to draw on the FFB line, FCSIC must certify that it would be extremely doubtful that: (1) the Federal Farm Credit Banks Funding Corporation can issue new System-wide insured debt obligations, and (2) one or more System banks will be able to repay maturing System-wide insured debt obligations without selling available liquidity reserves at a material loss.

¹⁰ FCSIC Board of Director Resolution dated September 23, 2013, notes that the principal and interest paid by FCSIC to the FFB will be equal or less than the principal and interest FCSIC receives from the System Bank(s) to whom FCSIC lends the funds received from the FFB.

Each assistance agreement will be subject to the Corporation's Board of Directors' approval. While assistance agreements are outstanding, the Corporation will use its examination authority to monitor compliance with the agreement. Moreover, the Corporation will require the System institution receiving assistance to certify and publicly disclose compliance with the agreement requirements, including the disclosure of any instances of material noncompliance with the agreement.

Procedures

This Policy Statement shall be supported by procedures that provide detailed instructions and guidance to FCSIC staff on the evaluation and provision of liquidity assistance in exigent market circumstance, and any other assistance procedures as determined by the Chief Operating Officer.