

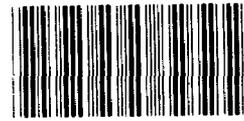
GAO

Fact Sheet for the Chairman, Committee
on Agriculture, House of Representatives

July 1987

FARM FINANCE

Legislative Proposals for Secondary Markets for Farm Real Estate Loans



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United States
General Accounting Office
Washington, D.C. 20548

Resources, Community, and
Economic Development Division

B-220507

July 2, 1987

The Honorable E (Kika) de la Garza
Chairman, Committee on Agriculture
House of Representatives

Dear Mr. Chairman:

As requested in discussions with your office on June 17, 1987, we are providing you with information on nine legislative proposals introduced in the 100th Congress to create an active secondary market for agricultural real estate loans. This is part of our ongoing work on secondary markets for agricultural real estate loans, requested by Representative Richard H. Lehman.

As agreed with Representative Lehman's office, we have limited our work to the nine legislative proposals listed in our testimony on Issues Surrounding a Secondary Market for Agricultural Real Estate Loans (GAO/T-RCED-87-29, June 3, 1987). As agreed with your office, this fact sheet provides information on each proposal's major provisions. The proposals are presented in order of introduction. Our final report, which we expect to issue soon, will include summary information that will facilitate a comparison of the major provisions of each bill.

Some of the bills are essentially reintroductions of bills from the 99th Congress, while others have resulted from the current debate about creating an active national secondary market for agricultural real estate loans. Although several proposals have the same titles, all have some differences. However, S. 1172 and H.R. 2435, both titled the Agricultural Mortgage Marketing Act of 1987, are substantially the same.

We identified the major provisions of each proposal and met with officials of two home mortgage secondary market entities--the Government National Mortgage Association (Ginnie Mae) and the Federal National Mortgage Association (Fannie Mae). We discussed with them the elements that should be considered in order to allow for a better

understanding of each proposal's potential impact on farmers, lenders, and the federal government. As a result, the elements we selected to include in this fact sheet are the following: purpose of the market, market organization and operation, sources of funding for the market, cost to establish and operate the market, eligibility criteria for lenders, loan and underwriting criteria, market volume, regulatory oversight body and cost, targeted investors, risk bearers, and market duration.

Not all of this information is available in each proposal to allow for an understanding of a secondary market's potential impacts on farmers, lenders, and the federal government. Some of the elements, such as cost to operate or volume of activity, are not typically present in legislation. Others, such as eligibility criteria, may be left to the determination of the administering agency within broad legislative guidelines. Even when elements are present in the proposals, they may not lend themselves to a complete understanding of the potential impact each proposal may have on farmers, lenders, and the government. To allow for such an understanding, most elements would have to be fleshed out and refined as the proposals go through the legislative process. Even then, some uncertainty could remain.

The proposals would all require some level of government involvement. For example, three proposals would vest the responsibility of making a secondary market in farm real estate loans with the Secretary of Agriculture. The other six would establish a federally chartered corporation as the secondary market institution. Of the six, four would create such a corporation within the Farm Credit System (FCS), and two would create it outside the FCS.

The government could incur direct and immediate financial liability ranging from providing initial funding to the market to guarantees on the loans and mortgage-backed securities traded in the market. For example, S. 234, the Farm Mortgage Marketing Corporation Act of 1987, would provide initial funding through appropriated funds for the Secretary of the Treasury to purchase \$200 million of the secondary market corporation's stock. The corporation could retire this stock at any time. H.R. 575, the Farm Credit Enhancement Act of 1987, would provide for government loan guarantees of up to \$4 billion to be outstanding at any time. Although many of the bills disclaim any government guarantee on the securities traded in the market, questions

loom over the government's potential implied backing as a result of the federal charter.

In identifying the legislative proposals, we relied primarily on legislative searches of legal data bases. We also held frequent discussions with congressional staff members, financial industry officials, and others who were active in the legislative process involving secondary markets for agricultural real estate loans and surrounding issues.

We plan to send copies of this fact sheet to Representative Richard H. Lehman; the Secretary of Agriculture; the Director, Office of Management and Budget; and other interested parties. Copies will be available to others upon request. Should you need further information, please contact me at (202) 275-5138.

Major contributors to this fact sheet are included in appendix I.

Sincerely yours,



Brian P. Crowley
Senior Associate Director

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SECTION

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ABBREVIATIONS

FCA	Farm Credit Administration
FCS	Farm Credit System
FmHA	Farmers Home Administration
GAO	General Accounting Office
RCED	Resources, Community, and Economic Development Division
SEC	Securities and Exchange Commission

SECTION 1

LEGISLATIVE PROPOSALS FOR A SECONDARY MARKET
FOR AGRICULTURAL REAL ESTATE LOANS

Farm Mortgage Marketing Corporation Act of 1987,

S. 234

Date introduced

January 6, 1987, 100th Congress.

Sponsor

Senator Cranston.

Date to be established

Date of enactment.

Purpose

The purpose of the proposal is to establish a quasi-private corporation chartered by the federal government that would purchase and insure agricultural mortgages and sell pools of such mortgages in order to do the following: facilitate the availability of long-term credit for agricultural borrowers, provide liquidity for financial institutions and other agricultural lenders, and provide an institutional mechanism to allow capital markets to invest in and provide funding for agricultural loans.

Organizational structure/market operation

The proposal would create a mixed-ownership government corporation, to be called the Farm Mortgage Marketing Corporation. The powers of the corporation initially would be vested in a five-member Board of Directors that would consist of the Comptroller of the Currency, the Chairman of the Federal Deposit Insurance Corporation, and three members appointed by the President with the advice and consent of the Senate. The three presidentially appointed members would be representatives of agricultural lending institutions who have substantial experience and expertise in the fields of agricultural lending and mortgage investments.

Common stock in the corporation with voting rights would be issued to those selling mortgages to it, in return for capital contributions, and then would be freely transferable. When the President determined that sufficient common stock of the corporation had been sold to qualified agricultural lenders, the interim board would turn over the affairs of the corporation to

regular board members elected by and from holders of common stock. The chairperson of the board would be designated by the members of the board.

The corporation's earnings would be transferred annually to a general surplus account from which dividends on the common stock would be paid. The board would have discretion to transfer funds from the surplus account to a reserve account.

The corporation would purchase farm mortgage loans from any agricultural lender which it deems qualified; sell securities backed by the mortgages, which it would hold in portfolio; and insure the timely payment of principal and interest payments to purchasers of the securities, either itself or by purchasing insurance from private sources. The corporation would set the term and interest rate on the mortgage-backed securities subject to approval of the Secretary of the Treasury. The corporation would be permitted to apply different regulations or fees to different classes of sellers or lenders.

Funding of the market

Mortgage sellers would be required to make a nonrefundable capital contribution of not more than 2 percent of the unpaid principal amounts of mortgages sold to the corporation and would get common stock in return. In addition, charges or fees could be imposed to meet all costs incurred in carrying out the act, and the corporation could issue additional common stock.

Cost to establish

The Secretary of the Treasury would subscribe to \$200 million of the corporation's capital stock, to be funded by appropriated funds. The corporation could retire the stock purchased by the Treasury at any time.

Cost to operate

The proposal does not estimate or limit operating cost.

Eligibility criteria for participating lenders

The corporation would establish criteria for determining the eligibility of an agricultural lender and approve applications from lenders applying for certification as qualified agricultural lenders. Participating agricultural lenders would include any bank, business and industrial development company, savings and loan institution, commercial finance company, trust company, credit union, insurance company, or other person approved by the corporation.

Lending criteria/underwriting standards

The proposal defines a farm mortgage as any loan to an agricultural producer that would be (1) originated after the bill's date of enactment, (2) an obligation of a U.S. citizen (or if the borrower is not an individual, a majority interest in the borrower is held by a U.S. citizen), (3) secured by a fee simple or leasehold mortgage with status as a first lien on agricultural real estate located in the United States, and (4) to borrowers whose training or farming experience would assure a reasonable likelihood of repayment. The mortgaged property would have to be land, used for the production of agricultural commodities and of a minimum annual acreage or producing minimum annual receipts established by the corporation.

The loans to be purchased by the corporation would have a loan-to-value ratio of 80 percent or have the amount over 80 percent guaranteed or insured by a qualified insurer. Before the corporation could purchase a loan, the lender would be required to agree either to retain a 10-percent participation in the mortgage, or to repurchase or replace the loan upon demand if the borrower defaults and no reserves are established to cover losses on such mortgages.

The securities issued by the corporation would be non-bank eligible for purposes of underwriting, selling, and distributing those securities. The term non-bank eligible is not defined in the act.

Volume of activity

The proposal does not estimate or limit volume of activity.

Regulatory oversight body and cost

The securities issued by the Farm Mortgage Marketing Corporation would be regulated under federal securities laws administered by the Securities and Exchange Commission (SEC), including the Securities Act of 1933 and the Securities Exchange Act of 1934. The cost of regulation is not discussed in the proposal.

As a mixed-ownership government corporation, the corporation is required to have its financial transactions audited by the U.S. General Accounting Office (GAO) as long as U.S. capital is invested in the corporation, and to be audited by GAO at least every three years.

Targeted investors

The proposal does not discuss potential investors targeted.

Risk bearers

The securities would not be guaranteed by or represent an obligation of the United States. The corporation would insure the timely payment of principal and interest for the securities either itself or through private insurance.

Market duration

The proposal does not contain a termination date but states that the corporation would continue until dissolved by an act of Congress.

Farm Mortgage Marketing Corporation Act of 1987,

H.R. 497

Date introduced

January 7, 1987, 100th Congress.

Sponsors

Congressman Lehman (California),
Congressman Bereuter,
Congressman Fauntroy,
Congressman Wortley,
Congressman Torres,
Congressman Kleczka,
Congressman Martinez, and
Congressman Jones (Tennessee).

Companion legislation

H.R. 497 is a companion bill to S. 234, the Farm Mortgage Marketing Corporation Act of 1987. (See p. 5.) The only differences between the two bills relate to the eligibility of banks to participate in the secondary market and the sellers' commitment to repurchase loans in default. H.R. 497 is silent on which market participants may underwrite, sell, and distribute securities created by the new secondary market entity. S. 234 states that the securities would be non-bank eligible for those purposes but does not define the term. On the issue of the sellers' commitment to repurchase mortgages in default, S. 234 would require the sellers to agree either to retain a 10-percent interest in the mortgage, or to repurchase or replace the loan upon demand if the borrower defaults and no reserves are established to cover losses on such mortgages. H.R. 497 is silent with respect to the use of reserves.

Farm Credit Enhancement Act of 1987,

H.R. 575

Date introduced

January 8, 1987, 100th Congress.

Sponsor

Congressman Lightfoot.

Date to be established

Date of enactment.

Purpose

The purpose of the proposal is to increase availability of agricultural mortgage credit by authorizing the Secretary of Agriculture to guarantee pools of qualified agricultural mortgage loans and to provide for issuance by approved agricultural loan facilities of securities representing interests in such pools.

Organizational structure/market operation

The Secretary of Agriculture would certify approved agricultural loan facilities. These facilities would then be authorized to issue secondary market securities backed by pools of agricultural mortgage loans.

Each facility would maintain a reserve of U.S. Treasury securities, initially equal to 10 percent of the principal amount of loans comprising each pool, as security for payment of principal and interest to owners of the pool securities. The Secretary, if he concurred in the facilities' certifications of pooled loans, would guarantee timely payment of principal and interest on the securities backed by the pools after the 10-percent reserve was exhausted.

The government guarantee would not be available to any pool in which a single loan constituted more than 5 percent of the pool at the time of the loan guarantee application. Any proceeds from the liquidation of collateral or from judgments, settlements, or guarantees with respect to a loan in the pool would first be used, less costs of collection, to reimburse the Secretary for any guarantee payments made on the pool.

Funding of the market

The Secretary of Agriculture would be authorized to borrow from the Treasury to finance outstanding loan guarantees, on terms approved by the Secretary of the Treasury. In addition, a guarantee fee not greater than one-half of 1 percent of the principal amount of the loan pools would be charged the loan facilities for guaranteeing the pools. Entities applying to be approved agricultural lending facilities would be charged a "reasonable" certification fee to cover costs incurred in processing and evaluating the applications.

Cost to establish

The total amount of guarantees outstanding at any time would not exceed \$4 billion.

Cost to operate

The proposal does not estimate or limit operating cost.

Eligibility criteria for participating lenders

The proposal does not provide criteria as to which lenders may sell loans in the market. However, it discusses eligibility criteria for organizations approved to purchase and pool the loans. An approved agricultural loan facility is defined as (1) a corporation, association, or trust under state or District of Columbia law having as its primary business purpose the sale or resale of securities backed by pools guaranteed by the Secretary of Agriculture and (2) being certified by the Secretary. To be certified under rules prescribed by the Secretary, such facilities would be required to have capitalization of at least \$25 million, acceptable managerial ability in relevant areas, adequate agricultural mortgage loan underwriting and servicing procedures, and prior agricultural mortgage origination experience of \$25 million or more during each of 3 preceding years. Certification would be good for 5 years but could be revoked after notice and hearing for noncompliance with rules. Guarantees would not be affected by the revocation.

Lending criteria/underwriting standards

A qualified loan would be: an obligation of a U.S. citizen or a private corporation or partnership whose owners holding a majority interest in that organization are U.S. citizens; originated after enactment of this proposal; secured by a fee simple or leasehold first-lien mortgage on agricultural real estate located in the United States; an obligation not exceeding \$2 million in total principal; made to borrowers whose training or farming experience assure a reasonable likelihood of repayment; and certified by an approved agricultural loan facility as meeting underwriting, security, and repayment standards established by the Secretary in

consultation with agricultural mortgage loan originators. The mortgage property would have to be land, used for the production of agricultural commodities and of a minimum acreage or producing minimum annual receipts established by the Secretary.

Volume of activity

The proposal does not estimate volume of activity. It specifies, however, that the total amount of guarantees outstanding at any time would not exceed \$4 billion.

Regulatory oversight body and cost

The Secretary of Agriculture would be authorized to examine the books, records, and loan files of the approved agricultural loan facilities. Securities under this proposal would be exempt from the federal securities laws administered by the SEC to the same extent as securities that are obligations of or guaranteed by the United States. If the securities are rated among the four highest categories, they would also be exempt from state regulation to the same extent. States could pass laws to override this exemption. The cost of regulation is not discussed in the proposal.

Targeted investors

Targeted investors are not specifically discussed in the proposal. The proposal would require that the securities be authorized investments under federal or state law of any person, trust, corporation, partnership, association, business trust, or business entity to the same extent as federally issued or federally guaranteed obligations, provided the pool securities are rated in one of the four highest rating categories. States could pass laws to override this provision.

Risk bearers

The securities would not be guaranteed by the United States. The approved loan facilities would have to exhaust the reserve equal to 10 percent of the pool principal before the government guarantee would be activated. Then the government's risk exposure would be the amount of the default, less amounts recouped by the facility on all defaulted loans in the pool.

Market duration

The Secretary of Agriculture's authority to guarantee new pools of loans would terminate 5 years after enactment.

Farm Mortgage Guarantee Act of 1987,

S. 427

Date introduced

February 2, 1987, 100th Congress.

Sponsor

Senator Grassley.

Date to be established

Date of enactment.

Purpose

The purpose of the proposal is to encourage agricultural lenders to provide long-term financing for the purchase of agricultural land by providing a secondary market for sound mortgages adequately secured by farm real estate and guaranteed by the Farmers Home Administration (FmHA).

Organizational structure/market operation

The Secretary of Agriculture or his agent would purchase qualifying farm real estate mortgages or interests in such mortgages. The Secretary would guarantee principal and interest payments on purchased loans on terms and conditions that he finds to be prudent and that will assure an adequate market for the loans. The guarantee could not be extended to any loan if at the time of the guarantee the amount borrowed exceeded 70 percent of the "most probable" purchase price of the property securing the loan; the price to be established by the Secretary of Agriculture.

The Secretary, acting for himself or through designated agents, would assure a secondary market for guaranteed loans by selling, reselling, purchasing, and repurchasing the loans or securities backed by the loans. The Secretary would promulgate regulations necessary to carry out the act.

Funding of the market

The market would be funded through two funds created by the bill, the Farm Mortgage Revolving Fund and the Farm Real Estate Insurance Fund. The revolving fund would be used to buy loans and pay costs of administering the law. It would be credited for funds received by the Secretary of Agriculture from the sale of loans, interest

earned from the investments of the revolving fund, and principal and interest payments on loans held for resale.

The insurance fund would receive up to a \$100-million appropriation and earnings on investments of its assets in federally-guaranteed obligations. It would be used, to the extent permitted in appropriation acts, to discharge obligations associated with loan guarantees.

In addition, the Secretary could transfer funds from the revolving fund to the insurance fund as necessary to pay obligations associated with loan guarantees. Fees imposed by the Secretary on sellers and buyers of loans would be allocated between the revolving fund and the insurance fund at the Secretary's discretion. When the insurance fund exceeds 5 percent of the aggregate value of loans and interest on loans for which a guarantee is in effect, the Secretary would use receipts that would otherwise go to the insurance fund to repay the appropriated amounts.

Cost to establish

No initial capitalization is specified for the revolving fund. An appropriation of \$100 million would be authorized for the insurance fund for the purpose of guaranteeing loans purchased and then resold in the secondary market.

Cost to operate

The proposal does not estimate or limit operating cost.

Eligibility criteria for participating lenders

The proposal indicates that federally- or state-chartered commercial banks, savings and loan associations, credit unions, mutual savings banks, mortgage bankers, cooperative lending agencies, or other legally organized lending agencies, including institutions of the FCS or insurance companies, could be approved to sell loans they have originated. Loans held by FmHA would be eligible to participate.

Lending criteria/underwriting standards

To qualify, farm real estate loans not held by FmHA would have to be (1) initiated by an approved legally organized lending agency, including FCS institutions and insurance companies, (2) secured by farm land adequate to ensure low risk of loss of principal, (3) made to a borrower with sufficient resources or cash flow to ensure a high probability of repayment, (4) secured at the time of the loan guarantee by property having at least a loan-to-value ratio of 70 percent, based on the "most probable" price of the property, and (5) in accordance with such other requirements as the Secretary of

Agriculture would impose. If the loans are held by FmHA, they need meet only the second, third, and fourth requirements.

Volume of activity

The proposal does not estimate or limit volume of activity.

Regulatory oversight body and cost

The Secretary of Agriculture would promulgate regulations to carry out the act and could delegate his authority to oversee secondary market operations to FmHA. The cost of regulation is not discussed in the proposal.

Targeted investors

The proposal does not discuss potential investors targeted.

Risk bearers

The government would assume risks according to the terms of the loan guarantee. Depending on the terms of any securities issued, the government could also assume additional risks. Lenders and/or investors would assume risks not covered by the government.

Market duration

The Secretary's authority to guarantee a loan under provisions of the act would terminate on December 31, 1991. A guarantee made prior to that date would remain in effect for the life of the loan.

Agricultural Mortgage Marketing Act of 1987,

S. 848

Date introduced

March 26, 1987, 100th Congress.

Sponsors

Senator Exon and
Senator Grassley.

Date to be established

Not later than 60 days after date of enactment.

Purpose

The purpose of the proposal is to establish the Agricultural Mortgage Enhancement Corporation as an institution of the FCS. The purposes of the corporation would be to certify agricultural mortgage marketing entities and provide for a secondary marketing arrangement for farm real estate mortgages in order to increase the availability of long-term agricultural credit at a stable interest rate, provide greater liquidity and lending capacity for agricultural lenders, and facilitate the funding of long-term agricultural investments.

Organizational structure/market operation

Not later than 60 days after enactment, the Farm Credit Administration (FCA) would organize and grant a charter to the Agricultural Mortgage Enhancement Corporation (corporation). The Board of Directors of the corporation would consist of nine members appointed by the Chairman of the FCA Board. Of these nine members, three would be representatives of agricultural lending institutions outside the FCS that have substantial experience in agricultural lending; three would be representatives of agricultural lending institutions within the FCS that have substantial experience in agricultural mortgage lending; and three would be representatives of the general public recognized as experts in agricultural lending and mortgage investment, one of whom would be designated by the Chairman of the FCA Board as Chairman of the Board of Directors.

The corporation would certify private agricultural mortgage marketing entities that, in turn, would purchase qualified agricultural real estate mortgage loans from originating lenders. The agricultural mortgage market entities would package the loans into pools and issue securities, backed by the pools and guaranteed

by the corporation, to the investing public. The corporation would not discriminate between or against FCS and non-FCS applicants desiring to become certified agricultural mortgage marketing entities.

To be eligible for certification, an entity would be required to (1) have adequate capitalization, (2) have as its primary business purpose the sale or resale of the agricultural mortgage-backed securities, (3) demonstrate acceptable managerial ability, (4) adopt appropriate underwriting and other standards required by the corporation, (5) permit the corporation to examine the entity's books, records, and loan files, and (6) be a corporation, association, or trust under state or District of Columbia law. Certification would be for 5 years or less and could be revoked after notice and hearings for failure to continue to meet eligibility criteria.

The corporation would be authorized to provide credit enhancement, defined as the assurance of timely payment of principal and interest on the securities representing interests in the pools of qualified agricultural real estate mortgage loans purchased by the entities. Credit enhancement would not be provided unless: the amount of any single loan would not exceed 5 percent of the total principal amount of the pool; the mortgage loan originator would retain the servicing of the loan; and the loans would be purchased by the entity without recourse to the mortgage loan originator. Each certified mortgage marketing entity would be required to maintain for the benefit of the holders of its securities a reserve in U.S. Treasury securities equal to 10 percent of the principal amount of the loans comprising each pool. Before the corporation would pay on its guarantee of principal and interest to security holders, the individual mortgage marketing entity would have to exhaust the 10-percent reserve. Funds for the reserve would come from both the certified entity and the loan originator. Any proceeds received by an entity from the liquidation of collateral or from judgments, settlements, or other guarantees with respect to a loan in the pool, less costs of collection, would first be used to reimburse the corporation for any guarantee payment made on the pool.

Funding of the market

The FCA would provide initial capitalization for the corporation through a revolving fund established by existing law (12 U.S.C. 2151) to fund the Farm Credit System Capital Corporation. The FCA would commit any other funds necessary to meet the corporation's responsibilities that are available to it, including funds originating outside FCS.

The corporation would also have authority with the approval of FCA to borrow from any source. The corporation would be authorized to charge a fee for credit enhancement that would not exceed one-half

of 1 percent of the principal amount of the guaranteed mortgage loans comprising the pool. The corporation also would be authorized to collect a reasonable fee to recover costs incurred for processing applications for certification as agricultural mortgage marketing entities.

Cost to establish

The proposal does not state the amount of initial capitalization.

Cost to operate

The proposal does not estimate or limit operating cost.

Eligibility criteria for participating lenders

The proposal defines an agricultural mortgage loan originator to be any bank, business and industrial development company, savings and loan association, commercial finance company, trust company, credit union, insurance company, or other entity that originates and services agricultural mortgage loans.

Lending criteria/underwriting standards

The proposal defines a qualified agricultural mortgage loan to mean an obligation (1) originated after date of enactment of the bill and secured by a fee simple or leasehold mortgage with status as a first lien on agricultural real estate located in the United States, (2) not exceeding \$2 million in total principal, with a loan-to-value ratio not exceeding 65 percent, (3) approved by a certified agricultural mortgage marketing entity, and (4) of a U.S. citizen, or a corporation or partnership of which a majority interest is held by U.S. citizens, who has training or farming experience that is sufficient to assure a reasonable likelihood of repayment. The bill defines agricultural real estate to mean a parcel or parcels of land, used for the production of one or more agricultural commodities or products, consisting of a minimum acreage or producing minimum annual receipts as determined by the corporation. The corporation would establish uniform underwriting, security appraisal, and repayment standards for qualified loans. The proposal requires that the standards would not discriminate against small agricultural mortgage loan originators or small agricultural mortgage loans of at least \$50,000.

Volume of activity

The proposal does not estimate or limit volume of activity.

Regulatory oversight body and cost

The corporation would be an institution of the FCS subject to the regulations and oversight of the FCA. The securities guaranteed by

the corporation would be exempt from federal securities laws administered by the SEC, to the same extent as securities that are obligations of or guaranteed by the United States. They would also be exempt from state securities laws if rated in one of the four highest rating categories. States could pass laws to override this exemption. The cost of regulation is not discussed in the proposal.

Targeted investors

Securities guaranteed by the corporation would be designated as qualified investments under state or federal law for any person, trust, corporation, partnership, association, business trust, or business entity, provided such securities are rated in one of the four highest rating categories. States could pass laws to override this provision.

Risk bearers

The securities would carry a statement that they are not guaranteed by or an obligation of the United States. The 10-percent reserve funded by the certified mortgage marketing entities and the loan originators would be looked to first for the timely payment of principal and interest. When drawing on the reserve to meet losses, except for the portion of losses absorbed by the certified entity's contributions to the reserve, losses would be charged first to the total contribution to the reserve of the originator of the loan in default, before charging the contributions of other originators. The corporation would guarantee the timely payment of the remaining principal and interest for the securities comprising guaranteed pools of agricultural mortgage loans.

Market duration

The authority of the corporation to provide guarantees for new pools of qualified agricultural mortgage loans would terminate 5 years after date of enactment.

Farmers Home Administration Guaranteed Loan
Improvements Act of 1987,

H.R. 2179

Date introduced

April 27, 1987, 100th Congress.

Sponsor

Congressman Thomas.

Date to be established

Upon issuance of final regulations by the Secretary of Agriculture.

Purpose

The purpose of the proposal is to improve the operation of the secondary market for loans guaranteed by FmHA, including agricultural real estate loans.

Organizational structure/market operation

The proposal applies generally to loans guaranteed by the FmHA under Title III of the Consolidated Farm and Rural Development Act, including real estate, operating, and rural development loans. The portion of such loans made by private-sector lenders that is guaranteed by the FmHA may be sold by the lender, and by any subsequent holder, in accordance with regulations on such sales issued by the Secretary of Agriculture, provided (1) all fees due the Secretary with respect to a guaranteed loan are paid in full before any sale and (2) the loan is fully disbursed to the borrower before the sale. After a loan is sold in the secondary market, the lender remains obligated under the guarantee agreement with FmHA and is required to continue to service the loan according to the guarantee agreement. The Secretary is to develop the necessary procedures for the facilitation, administration, and promotion of secondary market operations and for assessing the increase of farmers' access to capital at reasonable rates and terms as a result of secondary market operations.

The Secretary may issue pool certificates representing ownership of part or all of the guaranteed portion of any loan guaranteed by the FmHA under Title III. Such certificates are to be backed by a pool composed solely of the entire FmHA-guaranteed portion of such loans. The Secretary may permit approved market makers to issue pool certificates on his behalf and may guarantee the timely payment of the principal and interest on such certificates. Such

guarantee is limited to the extent of principal and interest on the guaranteed portions of loans that comprise the pools. The full faith and credit of the United States is pledged to the payment of all amounts required to be paid under any guarantee of pool certificates issued by approved market makers.

On the adoption of final regulations, the Secretary would (1) provide for the central collection of registration information from all participating market makers for all loans and pool certificates sold by them; (2) before any sale of pool certificates, require the seller to disclose to each prospective purchaser information on the terms, conditions, and yield; (3) require each market maker to service all pools formed and participations sold and to provide specific information to the Secretary relating to collection and disbursement of funds; and (4) regulate market makers with regard to pool certificates sold. The Secretary can charge fees for these functions.

Funding of the market

The proposal speaks of a reserve fund, to be established by the Secretary to enable the guarantee to be self-funding, but does not explain the mechanism for the reserve fund. The Secretary is authorized to collect fees for the functions he is to perform after the adoption of final regulations, provided that he is not to collect any fee for the guarantee of a pool certificate. The fees are not available to finance the program. Two existing revolving funds, the Agricultural Credit Insurance Fund and the Rural Development Insurance Fund, both currently available to meet the Secretary's obligations on guaranteed loans under Title III, would apparently also be available to satisfy guarantees of pool certificates.

Cost to establish

The proposal does not discuss the cost to establish the various provisions.

Cost to operate

The proposal does not estimate or limit operating cost.

Eligibility criteria for participating lenders

The proposal does not discuss eligibility criteria for participating market makers. For lenders, existing law provides that the Secretary may guarantee loans by any federally- or state-chartered bank, savings and loan association, cooperative lending agency, or other legally organized lending agency. (See 7 U.S.C. 1928(h).)

Lending criteria/underwriting standards

The proposal does not discuss lending criteria/underwriting standards for participating market makers. Generally, borrowers must be farmers or ranchers in the United States who are citizens with training or experience that the Secretary judges assures reasonable prospects of success, who are operating a family farm, and who cannot get credit elsewhere at reasonable rates and terms. (See 7 U.S.C. 1922.)

Volume of activity

The proposal does not estimate or limit volume of activity.

Regulatory oversight body and cost

The Secretary of Agriculture would be required to issue regulations governing the operations of a secondary market for FmHA-guaranteed loans. The Secretary would be required to transmit an annual report to the Senate and House Committees on Agriculture including specific information on the operations of the secondary market. The cost of regulation is not discussed in the proposal.

Targeted investors

The proposal does not discuss potential targeted investors.

Risk bearers

The United States bears the credit, or default, risk of pool certificates issued by approved market makers and guaranteed by the Secretary of Agriculture. Such guarantee is limited to the extent of principal and interest on the guaranteed portions of loans that comprise the pools. Since the unguaranteed portion of a loan is not included in a pool, it appears that the owner of the unguaranteed portion, whoever that is, bears the credit risk.

Market duration

The proposal does not contain a termination provision.

Agricultural Mortgage Marketing Act of 1987,

S. 1172

Date introduced

May 8, 1987, 100th Congress.

Sponsors

Senator Pryor,
Senator Cochran,
Senator Exon,
Senator Grassley,
Senator Simpson,
Senator McClure,
Senator Baucus,
Senator Harkin,
Senator Symms, and
Senator Durenberger.

Date to be established

Not later than 60 days after date of enactment.

Purpose

The purpose of the proposal is to establish the Federal Agricultural Mortgage Corporation as an institution of the FCS. The purposes of the corporation would be to certify agricultural mortgage marketing facilities and to provide for a secondary marketing arrangement for farm real estate mortgages in order to increase the availability of long-term agricultural credit at a stable interest rate, provide greater liquidity and lending capacity for agricultural lenders, and facilitate capital market investment in long-term agricultural funding.

Organizational structure/market operation

Within 60 days of enactment, the President would appoint a nine-member interim board of directors and designate one of them as interim chairman. Of the nine interim directors, three would be representatives of banks, other financial institutions, or insurance companies; three would be representatives of the FCS; two would be farmers; and one would be a representative of the general public. The interim board's primary duty would be to arrange for an initial offering of the corporation's voting common stock to banks, other financial institutions, life insurance companies, and members of the FCS on an equitable and nondiscriminating basis so that no institution or group of institutions acquires a

disproportionate amount. Stock may be issued only to agricultural mortgage loan originators or certified agricultural mortgage marketing facilities. However, the stock is fully transferable. The voting common stock would be divided equally between member institutions of the FCS and nonmember institutions. The interim board would also be authorized to take whatever actions are necessary for the corporation to proceed with its operations.

After \$20 million of initially offered voting common stock was purchased and fully paid, a 15-member permanent board of directors would be chosen. Six members would be elected by the banks, other financial institutions, and insurance companies; six members would be elected by FCS institutions; and three members would be appointed by the President. The FCS stockholders and the non-FCS stockholders would each vote as a class. Two of the presidentially appointed directors would be farmers, and one would be a representative of the general public.

Not later than 120 days after the permanent Board of Directors is chosen, the corporation would be required to issue standards for certification of agricultural mortgage marketing facilities, including eligibility standards. The certified facilities in turn would purchase qualified agricultural real estate mortgage loans from originating lenders and package the loans into pools that would serve as collateral for securities purchased by the investing public. The corporation would not discriminate between or against FCS and non-FCS applicants desiring to become certified agricultural mortgage marketing facilities.

A certified facility would be required to do the following: (1) be an affiliate of an institution of the FCS or a corporation, association, or trust under state or District of Columbia law; (2) have adequate capitalization; (3) have as one of its purposes the sale or resale of securities representing interests in pools of qualified agricultural mortgage loans that have been provided credit enhancement by the corporation; (4) demonstrate acceptable managerial ability; (5) adopt appropriate agricultural mortgage loan underwriting, appraisal, and servicing standards in conformity with those established by the corporation; and (6) permit the corporation to examine the facility's books, records, and loan files. Certification would be for 5 years or less and could be revoked after notice and hearings for failure to continue to meet eligibility criteria.

The corporation would be authorized to provide credit enhancement --the assurance of timely payment of principal and interest--on securities representing interests in pools of qualified agricultural mortgage loans, on application by certified agricultural mortgage marketing facilities. Credit enhancement would be provided through agreement with the existing Federal Farm Credit Banks Funding Corporation (Funding Corporation). The

maximum liability of the Funding Corporation with respect to credit enhancement would not exceed a total amount of \$500 million.

The issuance of any credit enhancement would be subject to provisions among which are the following: (1) the credit enhancement would be issued to cover an individual pool of qualified mortgage loans pursuant to the application of a certified agricultural mortgage marketing facility; (2) the amount of any single loan could not exceed 5 percent of the total principal amount of the pool; (3) the mortgage loan originator would retain the servicing of the loan; (4) the loans would be purchased by the facility without recourse to the mortgage loan originator; (5) a reserve equal to 10 percent of the principal amount of the loans comprising each pool would be established by the certified mortgage marketing facility, with optional participation by agricultural mortgage loan originators; (6) the individual mortgage marketing facility would have to exhaust its 10-percent reserve, before the Funding Corporation's credit enhancement for the timely payment of principal and interest to security holders would be activated; and (7) any proceeds received by a facility from the liquidation of collateral, judgments, settlements, or guarantees with respect to a loan in the pool, less costs of collection, would first be used to reimburse the Funding Corporation for any credit enhancement payment made on the pool. With regard to the 10-percent reserve, agricultural mortgage loan originators that exercise their option to contribute to the pool would be paid semiannually any earnings on their contributions to the reserve, to the extent the distribution would not cause the reserve to fall below 10 percent of the outstanding aggregate principal and accrued interest of loans remaining in the pool. The reserve would have to be exhausted first before any payments were made to security holders.

Agricultural loans by loan originators or certified facilities pursuant to this act would be exempt from state laws or constitutions limiting interest, discount points, finance charges, or other charges. States could pass laws to override this exemption.

Funding of the market

In addition to the initial \$20 million of common stock sold, the corporation would be authorized to require each agricultural mortgage loan originator and each certified mortgage marketing facility to make nonrefundable capital contributions, in exchange for stock, that are reasonable and necessary to carry out the purposes of the act. The corporation could issue additional common stock but only to mortgage loan originators or certified agricultural mortgage facilities.

Further, at the time a Funding Corporation credit enhancement would be issued, the corporation would impose a fee on the certified agricultural mortgage marketing facility not greater than one-half

of 1 percent of the initial principal amount of securities backed by each pool of qualified loans covered by the Funding Corporation's credit enhancement. The corporation would also impose additional charges or fees in reasonable amounts to recover its administrative costs.

Cost to establish

An initial capitalization of \$20 million is to be provided from purchase of stock by banks, other financial institutions, insurance companies, and FCS institutions.

Cost to operate

The proposal does not estimate or limit operating cost.

Eligibility criteria for participating lenders

The proposal defines an agricultural mortgage loan originator to be any FCS institution, bank, insurance company, business and industrial development company, savings and loan association, commercial finance company, trust company, credit union, or other entity that originates and services agricultural mortgage loans.

Lending criteria/underwriting standards

The proposal defines a qualified agricultural mortgage loan to mean, among other things, an obligation (1) secured by a fee simple or leasehold mortgage with status as a first lien on agricultural real estate located in the United States; (2) approved by a certified agricultural mortgage marketing facility as meeting the underwriting, security appraisal, and repayment standards established by the corporation in consultation with agricultural mortgage loan originators; and (3) of a U.S. citizen (or a corporation or partnership the majority of which is held by U.S. citizens) that has training or farming experience sufficient to assure a reasonable likelihood that the loan will be repaid according to its terms. The bill defines agricultural real estate to mean a parcel or parcels of land, used for the production of one or more agricultural commodities or products and consisting of a minimum acreage or producing minimum annual receipts as determined by the corporation. These standards established by the corporation are not to be used to discriminate against small agricultural mortgage loan originators or small agricultural mortgage loans of at least \$50,000.

Volume of activity

The proposal does not estimate or limit volume of activity.

Regulatory oversight body and cost

The corporation would be an institution of the FCS and subject to the regulatory authority of the FCA. However, that authority would be confined to providing for examination of the condition of the corporation and to the general regulation of the safe and sound performance of the powers, functions, and duties vested in the corporation. The corporation would have to publish an annual report containing financial statements prepared in accordance with generally accepted accounting principles and audited by an independent public accountant, as well as any other information required by the FCA. The FCA would be required to audit the financial transactions of the corporation at least annually. The securities representing an interest in a pool of qualified agricultural mortgage loans for which credit enhancement had been provided by the Funding Corporation would be exempt from federal securities laws administered by the SEC and from state securities laws to the same extent as U.S.-issued or -guaranteed securities. States could pass laws to override the exemption. The cost of regulation is not discussed in the proposal.

Targeted investors

Securities representing an interest in pools of qualified agricultural loans for which the Funding Corporation has provided credit enhancement, would be designated as qualified investments for any person, trust, corporation, partnership, association, business trust, or business entity to the same extent as U.S.-issued or -guaranteed securities. States could enact laws to override the provision. The securities would be eligible for unlimited purchase, sale, and underwriting by national banks.

Risk bearers

Securities issued would carry a statement that they are not guaranteed by or an obligation of the United States. The 10-percent reserve created by the certified mortgage marketing facilities would be looked to first for the timely payment of principal and interest. When drawing on the reserve to meet losses, except for the portion of losses absorbed by the certified facility's contribution to the reserve, losses would be charged first to the contribution to the reserve of the originator of the defaulted loan before charging the contributions of other originators. The Funding Corporation's credit enhancement would provide for the timely payment of the remaining principal and interest for the securities backed by pools of qualified agricultural mortgage loans.

Market duration

The proposal does not contain a termination provision. The proposal states that the corporation would continue until dissolved by an act of Congress.

Agricultural Mortgage Marketing Act of 1987,

H.R. 2435

Date introduced

May 14, 1987, 100th Congress.

Sponsors

Congressman Stallings,
Congressman Gunderson,
Congressman English,
Congressman Bereuter,
Congressman Lehman (California),
Congressman Craig,
Congressman Penny,
Congressman Jontz,
Congressman Lightfoot,
Congressman Morrison (Washington),
Congressman Weber,
Congressman Nagle,
Congressman Evans, and
Congressman Roberts.

Companion legislation

H.R. 2435 is a companion bill to S. 1172, the Agricultural Mortgage Marketing Act of 1987. (See p. 23.) Although the wording of the bills differs slightly, they are in substance identical.

Federal Farm Credit Mortgage Corporation Act of 1987
(Title IV, Farm Credit Borrower Stock Protection
and System Restoration Act of 1987),

S. 1219

Date introduced

May 15, 1987, 100th Congress.

Sponsors

Senator Leahy and
Senator Lugar.

Date to be established

Date of enactment.

Purpose

The purposes of the proposal are to (1) increase the availability of agricultural credit; (2) stimulate the flow of investment capital into the agricultural sector; and (3) increase the liquidity and lending capacity of agricultural lenders by creating the Federal Farm Credit Mortgage Corporation, which would foster, develop, and maintain a nationwide secondary market for agricultural loans.

Organizational structure/market operation

The proposal would amend the Farm Credit Act of 1971 (12 U.S.C. 2001 et seq.) to create the Federal Farm Credit Mortgage Corporation. The corporation would be a federally chartered instrumentality of the United States and an institution of the FCS. The corporation would have an initial Board of Directors consisting of nine members: six elected by FCS banks to represent FCS, and three elected by the other six to represent non-FCS institutions that sold agricultural loans to the corporation or that issued securities guaranteed by the corporation. When the board determines that voting rights are sufficiently dispersed to permit representative elections of non-FCS directors, non-FCS institutions will be allowed to elect directors to represent them. The board would be authorized to increase the number of directors to 12 or 15, provided that the ratio of 2 directors elected by FCS banks for each director elected by non-FCS institutions was maintained. The board would elect, on an annual basis, a chairman from among the members of the board.

The corporation would have Class A voting common stock, which would be issued to and held only by FCS banks. The initial capitalization of the corporation, which would be determined by the board, would be provided by each FCS bank, with each bank required to purchase an equal number of shares of Class A common stock at a price set by the board. The FCS banks that sell loans to the corporation or issue securities guaranteed by the corporation may be required to buy additional Class A stock, on the basis of the nature and volume of their transactions with the corporation. The corporation would be authorized to issue additional Class A stock to FCS banks and to issue additional classes of nonvoting common stock and nonvoting preferred stock.

The corporation would be authorized to purchase, service, sell, or lend on the security of, or otherwise deal in, agricultural loans. The corporation would require, as far as is practicable, equal access to full participation in its programs by each type of eligible seller.

The operations of the corporation would be confined so far as practicable to agricultural loans of such quality, type, and class as to meet standards imposed by private institutional agricultural loan investors. The corporation would establish underwriting standards as it deems appropriate to implement this requirement. The corporation would not be authorized to require recourse to the loan seller as a prerequisite to buying a loan but would be authorized to consider the extent of recourse and the nature of the seller's guarantees as an element of pricing.

The corporation would be authorized to guarantee timely payment of principal and interest on securities (1) issued by any issuer approved by the corporation and (2) backed by a trust or pool of eligible agricultural loans. The corporation's guarantee would be limited to pools containing only loans of such quality, type, and class which meet purchase standards imposed by private institutional agricultural loan investors.

The corporation would make payments to holders of guaranteed securities when the issuer defaults and would be empowered to contract with issuers, that in the event of the issuer's default, the loans would become property of the corporation, subject only to the unsatisfied rights of the holders of the securities. State law could not override this provision.

Funding of the market

The initial capitalization of the corporation would be provided by each FCS bank, as determined by the board. Each FCS bank would purchase an equal number of shares of Class A voting common stock at a price set by the board. FCS banks selling loans to or issuing securities guaranteed by the corporation could be required to buy

additional Class A stock. The board also would be authorized to issue additional classes of nonvoting common stock and nonvoting preferred stock.

The corporation would impose a reasonable guarantee fee and make other charges to recover costs of its loan and security review and analysis. The corporation could also impose different fees for different classes of sellers or services as long as the distinction was related to the purposes of the act. Fee requirements could not discriminate solely on the basis of FCS membership.

Cost to establish

The proposal does not specifically discuss the amount it would cost to establish the corporation and to implement its secondary market operations. However, the corporation could not exercise its powers to retire any of the Class A stock if the necessary payment reduced capital, reserves, and surplus of the corporation below \$100 million.

Cost to operate

The proposal does not estimate or limit operating cost.

Eligibility criteria for participating lenders

The corporation would purchase an agricultural loan from any FCS bank, regulated insurance company, financial institution whose deposits are insured by an agency of the United States, and any other class of institutional agricultural lenders that the board may deem appropriate. The corporation would establish requirements for sellers consistent with the purposes of the act. Among other factors that the corporation could take into account would be minimum net worth, supervisory mechanisms, warranty compensation mechanisms, prior approval of facilities, and prior experience.

Lending criteria/underwriting standards

The proposal defines an agricultural loan to either mean an obligation secured by a fee simple or leasehold mortgage with status as a first lien on agricultural real estate located in the United States, which is used for the production of one or more agricultural commodities or products and which consists of minimum acreage or produces minimum annual receipts, as determined by the corporation and meeting any other requirements as to amount, term, repayment provisions, status prescribed by the corporation or alternatively to mean any loan originated or purchased by a FCS member under the Farm Credit Act or that was not originated by a FCS member but could have been, except for the requirement to purchase stock in the originating institution as a condition of the

loan. On the basis of its requirements, the corporation would determine if an institution would be eligible to sell agricultural loans to the corporation.

The corporation would buy or guarantee only agricultural loans of such quality, type, and class that meet purchase standards imposed by private institutional agricultural investors. The corporation would be required to establish underwriting standards it deems appropriate to implement this requirement.

Volume of activity

The proposal does not estimate or limit volume of activity.

Regulatory oversight body and cost

All securities issued or guaranteed by the corporation would be exempt from federal securities laws administered by the SEC and from state law to the same extent as U.S. government-issued or -guaranteed securities. States could pass laws to override this exemption.

The regulatory authority of the FCA with respect to the Federal Farm Credit Mortgage Corporation would be confined to providing for the examination of the condition and the general regulation of the safe and sound performance of the powers, functions, and duties vested in the corporation.

The corporation's financial transactions would be audited at least annually by FCA, and FCA would report the results to the Congress. The corporation would prepare an annual report of its condition, including financial statements prepared in accordance with generally accepted accounting principles, and audited by an independent public accountant.

FCA may order the corporation to cease and desist from practices that FCA considers unsafe or unsound and may remove directors or officers of the corporation that it finds have violated a cease-and-desist order, engaged in an unsafe or unsound practice, or committed a breach of fiduciary duty (if certain other conditions are met). Judicial review of these actions is available. Civil penalties can also be imposed for unsafe or unsound practices. The cost of regulation is not discussed in the proposal.

Targeted investors

Any person, trust, or organization created under the laws of the United States or any state would be authorized to purchase, hold, and invest in agricultural loans, obligations, or other securities that are issued, sold, or guaranteed by the corporation to the same

extent securities issued or guaranteed by the United States. States could pass laws to override this provision.

Risk bearers

Securities issued by the corporation or by issuers approved by the corporation and backed by pools of eligible agricultural loans would be guaranteed by the corporation with respect to the timely payment of principal and interest. The FCS banks would be required, to the extent prescribed by the corporation's board, to guarantee the corporation's obligations with respect to any agricultural loan or security.

Market duration

The proposal does not contain a termination provision.

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