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[6705-01-P]

FARM CREDIT ADMINISTRATION

12 CFR Part 652

RIN 3052-AC86

Organization; Funding and Fiscal Affairs, Loan Policies and Operations, and Funding Operations; Farmer Mac Investment Eligibility

**AGENCY:** Farm Credit Administration.

**ACTION:** Proposed rule.

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**SUMMARY:** The Farm Credit Administration (FCA, Agency, us, our, or we) proposes to amend our regulations governing the eligibility of non-program investments held by the Federal Agricultural Mortgage Corporation (Farmer Mac). We propose to revise these regulations to comply with section 939A of the Dodd-Frank Wall Street Reform and Consumer Protection Act (Dodd-Frank Act or DFA) by removing references to, and requirements relating to, credit ratings. We are also proposing a delayed compliance date for the rule.

**DATES:** You may send us comments by [**Insert date that is 60 days after publication in the Federal Register**].

**ADDRESSES:** We offer a variety of methods for you to submit comments on this proposed rule. For accuracy and efficiency reasons, commenters are encouraged to submit

comments by e-mail or through the Agency's Web site. As facsimiles (fax) are difficult for us to process and achieve compliance with section 508 of the Rehabilitation Act, we are no longer accepting comments submitted by fax. Regardless of the method you use, please do not submit your comment multiple times via different methods. You may submit comments by any of the following methods:

- E-mail: Send us an e-mail at [reg-comm@fca.gov](mailto:reg-comm@fca.gov).
- FCA Web site: <http://www.fca.gov>. Select "Public Commenters," then "Public Comments," and follow the directions for "Submitting a Comment."
- Federal eRulemaking Portal: <http://www.regulations.gov>. Follow the instructions for submitting comments.
- Mail: Laurie A Rea, Director, Office of Secondary Market Oversight, Farm Credit Administration, 1501 Farm Credit Drive, McLean, VA 22102-5090.

You may review copies of all comments we receive at our office in McLean, Virginia, or on our Web site at <http://www.fca.gov>. Once you are in the Web site, select "Public Commenters," then "Public Comments," and follow the directions for "Reading Submitted Public Comments." We will show your comments as submitted, but for technical

reasons we may omit items such as logos and special characters. Identifying information that you provide, such as phone numbers and addresses, will be publicly available. However, we will attempt to remove e-mail addresses to help reduce Internet spam.

**FOR FURTHER INFORMATION CONTACT:**

Joseph T. Connor, Associate Director for Policy and Analysis, Office of Secondary Market Oversight, Farm Credit Administration, McLean, VA 22102-5090, (703) 883-4364, TTY (703) 883-4056;

or

Laura McFarland, Senior Counsel, Office of General Counsel, Farm Credit Administration, McLean, VA 22102-5090, (703) 883-4020, TTY (703) 883-4056.

**SUPPLEMENTARY INFORMATION:**

I. Objective

The purpose of this proposed rule is to replace references to credit rating agencies in existing Farmer Mac investment regulations with other appropriate standards to determine the creditworthiness of investments and to revise exposure limits for investments involving one obligor.

Section 939A of the Dodd-Frank Wall Street Reform and Consumer Protection Act (Dodd-Frank Act or DFA) requires agencies to remove references to, and requirements relating to, credit ratings. This proposal would substitute other appropriate standards of creditworthiness. The proposed

rule would also replace the table in existing regulations that sets forth criteria for non-program investment eligibility with standards that place a greater emphasis on management's due diligence responsibility in ascertaining credit quality of non-program investments so that only high quality investments are purchased and held. The proposed rule would also clarify how other non-program investments are treated and revise exposure limits for investments involving one obligor. We are also proposing a delayed compliance date for the rule.

## II. Background

Farmer Mac is an institution of the Farm Credit System, regulated by FCA through the FCA Office of Secondary Market Oversight (OSMO). Farmer Mac was established and chartered by Congress to create a secondary market for agricultural real estate mortgage loans, rural housing mortgage loans, and rural utilities loans, and it is a stockholder-owned instrumentality of the United States. Title VIII of the Farm Credit Act of 1971, as amended, (Act) governs Farmer Mac.<sup>1</sup>

On July 21, 2010, the Dodd-Frank Act was enacted, and section 939A of the Dodd-Frank Act requires Federal

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<sup>1</sup> Pub. L. 92 181, 85 Stat. 583, 12 U.S.C. 2001 et seq.

agencies to review all regulatory references to nationally recognized statistical ratings organizations (NRSRO or credit rating agency) and replace those references with other appropriate standards for determining creditworthiness.<sup>2</sup> The Dodd-Frank Act further provides that, to the extent feasible, agencies should adopt a uniform standard of creditworthiness for use in regulations, taking into account the entities regulated and the purposes for which such regulated entities would rely on the creditworthiness standard.

The existing rules on non-program investments for Farmer Mac are contained in 12 CFR part 652, subpart A, and rely, in part, on NRSRO credit ratings to characterize relative credit quality of various instruments. On June 16, 2011, we issued an Advance Notice of Proposed Rulemaking (ANPRM) soliciting comments on suitable alternatives to NRSRO credit ratings.<sup>3</sup> On November 18, 2011, as part of another rulemaking, we again requested comment on potential sources of market-derived information that could be used to replace NRSRO credit ratings in part

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<sup>2</sup> Pub. L. 111-203, 124 Stat. 1376, (H.R. 4173), July 21, 2010.

<sup>3</sup> 76 FR 35138, June 16, 2011.

652 of our rules.<sup>4</sup> In developing this proposed rule, we considered all suggestions from comments received and incorporated those we believed best addressed the objective of this rulemaking. In addition to these comments, we also considered the creditworthiness standards we proposed in a separate rulemaking for Farm Credit banks and associations<sup>5</sup> in compliance with provisions in the Dodd-Frank Act directing agencies, to the extent feasible, to adopt a uniform standard of creditworthiness among regulated entities.

### III. Section-by-Section

The proposed rule would revise portfolio diversification requirements and revise the credit quality standards for eligible non-program investments that Farmer Mac may hold by replacing the reliance on NRSRO credit ratings and clarifying terminology.

#### A. Definitions [existing § 652.5]

In § 652.5, we propose removing existing terminology, adding new terms, and revising existing definitions. We propose removing as obsolete several terms from the list of definitions in § 652.5. We also propose removing terms

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<sup>4</sup> Refer to Proposed rule, "Federal Agricultural Mortgage Corporation Funding and Fiscal Affairs; Farmer Mac Investments and Liquidity Management" (76 FR 71798, Nov. 18, 2011).

<sup>5</sup> 79 FR 43301, July 25, 2014.

from § 652.5 because they do not require a separate definition. The specific terms we propose removing are:

- "Contingency Funding Plan (CFP)",
- "Eurodollar time deposit",
- "Final maturity",
- "General obligations",
- "Liability Maturity Management Plan (LMMP)",
- "Liquid investments",
- "Liquidity reserve",
- "Nationally Recognized Statistical Rating Organization (NRSRO)",
- "Revenue bond", and
- "Weighted average life (WAL)."

We propose making conforming changes to § 652.20 to remove these terms where they appear.

We next propose adding two new terms to the list of definitions to address other proposed changes in this rulemaking: "Diversified investment fund" and "Obligor." We propose to define a "diversified investment fund" (DIF) as an investment company registered under section 8 of the Investment Company Act of 1940, 15 U.S.C. 80a-8. We selected this definition based on our current use of it in § 615.5140(a)(8) of our investment rules for Farm Credit

banks and associations. We propose to define the term "obligor" because our current regulations use this term but do not define it. We propose defining "obligor" as an issuer, guarantor, or other person or entity who has an obligation to pay a debt, including interest due, by a specified date or when payment is demanded. This definition would include the debtor or immediate party that is obligated to pay a debt, as well as a guarantor of the debt. The proposed definition would also clarify that both a DIF and the entity or entities obligated to pay the underlying debt are treated as a single obligor. This clarification is intended to ensure DIF investments do not become an excessively concentrated part of the investment portfolio.

Lastly, we propose changing three existing terms and their definitions to improve clarity: "Government agency", "Government-sponsored agency", and "mortgage securities." We propose replacing the existing term "Government-sponsored agency" with "Government-sponsored enterprise (GSE)" and defining a GSE as an entity established or chartered by the U.S. Government to serve public purposes specified by the U.S. Congress but whose debt obligations are not explicitly guaranteed by the full faith and credit of the U.S. Government. We also propose replacing

"Government agency" with "U.S. Government agency." The proposed definition for U.S. Government agency would explain that it means an instrumentality of the United States Government whose obligations are fully guaranteed as to the timely payment of principal and interest by the full faith and credit of the U.S. Government. Finally, we propose replacing the term "mortgage securities" with "mortgage-backed securities (MBS)" as this term is more widely used in the financial sector. We propose applying the existing definition for "mortgage securities" to the new MBS term. We propose a conforming change to the definition of "asset-backed securities", which uses "mortgage securities" in its definition.

B. Concentration Risk [new § 652.10(c)(5)]

We propose revising existing § 652.10 to address concentration risk through portfolio diversification and obligor limits in new paragraph (c)(5). Portfolio diversification is crucial to safe and sound investment management and is achieved by the appropriate distribution of risk exposures across reasonably uncorrelated industries and obligors. When a portfolio is properly diversified, a crisis within one industry sector or the sudden weakening or default of one obligor should not significantly destabilize the financial condition of the investor. In

new § 652.10(c)(5), we propose specifying that Farmer Mac's investment policies address concentration risk by setting diversification standards. We propose that the diversification calculation used when setting these standards be based on the carrying value of the investment on Farmer Mac's balance sheet. By carrying value, we mean the amount an investment contributes to the asset section of Farmer Mac's balance sheet under GAAP, net of any impairment estimate or valuation allowance. We believe the carrying value would, when applied for this purpose, appropriately capture the value of capital at risk for an investment at any given time. We also propose the following parameters for Farmer Mac's establishment of these standards:

- Basing calculation of an investment's compliance with diversification requirements on the investment's carrying value;
- Limiting investments in one obligor to no more than 10 percent of regulatory capital, unless the investments are obligations backed by U.S. Government agencies or GSEs; and

- Limiting the percentage of GSE-issued mortgage-backed securities that may comprise Farmer Mac's entire investment portfolio to 50 percent.

We believe these parameters will not require changes in the current investment portfolio held by Farmer Mac and discuss them more fully below.

We believe by placing specific diversification limits within the section that generally requires Farmer Mac to set diversification limits will improve the organization of the rule.

We also propose removing the reference to geographic areas in existing § 652.10(c)(1)(i). Farmer Mac should consider diversification by geographic location of issuer as appropriate based on the nature of its investment portfolio. For example, in the case of investments in municipal securities, geographic location might be an important consideration. However, we propose removing this specific category in the regulation to avoid misinterpretation. For example, we do not see the need to restrict obligors solely on the basis of where they happen to be headquartered or the location of an issuer's operations. The proposed change in the level of the single obligor limit is discussed below in section III.B.1.

#### 1. Obligor Limit

We propose to move the obligor limit from § 652.20(d)(1) and reduce the current limit to 10 percent of regulatory capital. The proposed 10-percent obligor limit in new § 652.10(c)(5)(i) would enhance Farmer Mac's long-term safety and soundness by ensuring that if an obligor were to default, only a modest portion of capital would be at risk. Currently, the proposed 10-percent obligor limit equates to an amount that is less than Farmer Mac's capital surplus and well within its risk-bearing capacity based on its current level of regulatory capital. Whereas, the current 25-percent obligor limit could expose Farmer Mac to financial challenges if it experienced an event of multiple defaults in its liquidity portfolio during a short time period (e.g., such as during the 2008 financial crisis), given the historical relationship between Farmer Mac's capital surplus over the minimum requirement and the dollar value of the 25-percent limit. Thus, we expect that the proposed 10-percent maximum will provide reasonable assurance that a single default will not significantly increase the risk of Farmer Mac's being unable to comply with the minimum capital requirement.

This proposed obligor limit would recognize that the credit performance of a single obligor (unlike, for example, a single industry sector) is binary in nature,

(i.e., the investment is either performing or it is in default) with potentially very low recovery rates. For that reason, we believe a cautious approach is warranted regarding the management of exposure concentrations in an individual obligor. We also believe the proposed obligor limit retains sufficient flexibility for Farmer Mac to manage its investment portfolio and still maintain adequate diversification. While the proposed obligor limit would be a regulatory maximum, Farmer Mac should consider establishing lower obligor limits to fit its overall risk profile and risk-bearing capacity, including earnings capacity, as well as the risks in individual types and classes of investments.

We seek specific comments and suggestions on how FCA might modify or adjust the obligor limit to make it more risk sensitive while achieving the overarching objectives of the limit for example, by scaling or risk-weighting assets based on internal or standardized models or other criteria such as the magnitude of Farmer Mac's surplus over the minimum capital requirement.

The proposed § 652.10(c)(5) would retain the existing exemption from the obligor limit, currently located in § 652.20(d)(1), for investments that are backed by a U.S. Government agency or GSEs.

## 2. Asset Class Limits

Existing § 652.20(a) contains a table identifying nine asset classes with different investment portfolio limits.

These nine asset classes are:

- Obligations of the United States,
- Obligations of GSEs,
- Municipal Securities,
- International and Multilateral Development Bank Obligations,
- Money Market Instruments,
- Mortgage Securities,
- Asset-Backed Securities,
- Corporate Debt Securities, and
- DIFs.

Of these, some asset classes have investment portfolio limits of 15 percent, 20 percent, 25 percent, and 50 percent.

### a. GSE-Issued Mortgage-Backed Securities Limit

We propose moving to new § 652.10(c)(5)(ii) the current § 652.20(a)(6) 50-percent limit on the volume of GSE-issued mortgage-backed securities that may be held in Farmer Mac's investment portfolio. We believe the risk posed by GSE-backed MBS is significantly lower than other

asset classes both in terms of default risk and liquidity risk, which supports retaining this relatively high limit. We also believe this limit is better situated within our rules with other risk tolerance provisions.

b. Other Asset Class Limits

In section III.C.1 of this preamble, we discuss the proposed removal of the investment table at § 652.20(a), while retaining some of its requirements. We have not proposed retaining any of the asset class portfolio limits contained in the table except the previously discussed 50-percent portfolio limit for GSE-issued securities. This is because existing § 652.10(c)(1)(i) already requires Farmer Mac to establish within its investment policy concentration limits for "asset classes or obligations with similar characteristics." We expect that Farmer Mac will review their investment policy limits at least annually and make adjustments based on their current risk profile and risk-bearing capacity, which may suggest lower limits than the current regulatory parameters. Nonetheless, we recognize there may be value in maintaining regulatory limits and, therefore, invite specific comment on whether the following existing asset class limitations should be retained in full or part:

- Municipal Securities: Revenue bonds limit of 15 percent,
- Money Market Instruments: Non-callable term Federal funds and Eurodollar time deposits limit of 20 percent,
- Money Market Instruments: Master notes limit of 20 percent,
- Mortgage Securities: Non-Government agency or Government-sponsored agency securities that comply with 15 U.S.C. 77d(5) or 15 U.S.C. 78c(a)(41) and Commercial mortgage-backed securities combined 15-percent limit,
- Asset-Backed Securities limit of 25 percent, and
- Corporate Debt Securities limit of 25 percent.

We are also interested in whether any of these limits should be changed and, if so, to what degree. We ask that your comment on this issue include the rationale for your suggestion(s).

C. Non-Program Investments [existing §§ 652.20 and 652.25; new § 652.23]

1. Eligible Non-program Investments [§ 652.20]

We propose replacing the existing § 652.20, including removing the "Non-Program Investment Eligibility Criteria

Table," with investment eligibility requirements that place greater responsibility on Farmer Mac management. The replacement of this section will result in removal of all references to NRSRO credit ratings from § 652.20.

a. Eligible Non-Program Investment Categories [§ 652.20(a)]

Our existing regulation at § 652.20(a) contains a detailed listing of eligible investment asset classes and types of investments within each asset class. The existing regulation imposes final maturity limits, investment portfolio limits, and other requirements for many of these investments, including credit rating requirements that are based on NRSRO credit ratings. To replace this provision, we propose general categories of eligible non-program investments that Farmer Mac may purchase and hold. The proposed general categories are:

- Non-convertible senior debt securities,
- Certain money market instruments,
- Certain ABS/MBS backed by a U.S. Government-agency or GSE guarantee,
- Certain senior position mortgage related securities,
- Obligations of development banks where the United States is a voting member of the bank, and
- Certain diversified investment funds.

As proposed in new § 652.20(a)(1), non-convertible senior debt securities (e.g., investments in senior debt securities that cannot be converted to any other type of securities) would be eligible under the proposed provision. This investment category would include non-convertible U.S. Government agency senior debt securities, including U.S. Treasury securities, and senior non-convertible GSE bonds. Senior debt securities could be secured by a specific pool of collateral or may be unsecured with priority of claims over other types of debt securities of the issuer, but would not include those that are convertible into a non-senior security or an equity security.

In proposed new paragraph (a)(3) and (a)(4), fully government-guaranteed ABS or MBS that are guaranteed as to the payment of principal and interest by a U.S. Government agency or GSE would be eligible securities because of their high credit quality. Farmer Mac would have to verify that securities labeled "government guaranteed" are fully guaranteed as to the payment of principal and interest. Similarly, a GSE "wrap" (guarantee) would not make a security eligible under this proposed provision unless it is a guarantee of all principal and interest of the security. While partial guarantees would not satisfy this

proposed requirement, they could be eligible under other criteria.

We propose in new paragraph (a) (5) permitting investments in ABS and MBS that are not fully guaranteed, but only the senior-most position of such instruments. By senior-most position, we mean the tranche of a structured instrument that is last to experience losses in the event of default and that such losses be shared on a pro rata basis by investors in that tranche. In addition, we propose that for a position in an MBS to be eligible, the MBS must satisfy the securities law definition of "mortgage related security".<sup>6</sup> Collateralized debt obligations (CDOs), which are re-securitizations that have evolved for the MBS market, would be eligible under this criterion if their underlying collateral is comprised only of the senior-most positions of other securitizations. The underlying collateral of most CDOs consists of lower-rated tranches from other securitizations, and these CDOs would not be eligible under this criterion. Further, private placements may be eligible under this proposed criterion, as long as they satisfy all of the proposed investment

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<sup>6</sup> 15 U.S.C. 78c(a)(41).

eligibility requirements.<sup>7</sup> We note, however, that private placements are generally not liquid and would therefore need to be acquired for an authorized purpose unrelated to liquidity.

We also propose in new paragraph (a) (7) that shares of a DIF would be eligible if the DIF's portfolio consists solely of securities that are eligible under these eligibility criteria. While the proposal for DIF eligibility is unchanged from the existing regulation, we are proposing more restrictive portfolio diversification limits on DIF investments than currently exist.

b. Investment Quality [§ 652.20(b)]

We want to retain high creditworthiness standards for Farmer Mac eligible non-program investments.<sup>8</sup> Accordingly, we propose in § 652.20(b) (1) requiring that obligors (whether debtor or guarantor) have strong capacity to meet the financial commitment for the expected life of the investment. This standard would apply to all investments, including those that are currently not subject to a NRSRO

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<sup>7</sup> Private placement refers to the sale of securities to a relatively small number of sophisticated investors without registration with the Securities and Exchange Commission and, in many cases, without the disclosure of detailed financial information or a prospectus.

<sup>8</sup> Our existing regulations governing Farmer Mac require that certain eligible investments meet the highest or the second highest whole-letter NRSRO rating (e.g., "AAA" or "AA" for Standard & Poors ratings, without regard to "+" or "-" levels within individual whole-letter ratings).

credit rating requirement. In general, we would view an investment as having met this standard if the expected average cumulative default rate of issuers of similar credit quality is low based on historical default data.<sup>9</sup> We would expect Farmer Mac to document the source of its historical data and basis for investment criteria.

In addition to imposing standards on obligors, we also propose in § 652.20(b)(2) requiring an eligible investment to exhibit low credit risk and other risk characteristics consistent with the purposes for which it is held. We are not proposing to require that other risks in the investment be low in all cases. Instead, the risk characteristics in the investment must be consistent with the purposes for which the investment is held. For instance, if an investment is held for the purpose of liquidity, it would have to be readily marketable<sup>10</sup> and would generally have to have low price volatility. On the other hand, an investment that is high quality but has high price volatility and questionable marketability may not be appropriate for a liquidity investment. Instead, it might

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<sup>9</sup> One potential source of historical data for this purpose is the publicly available report entitled "Annual Default Study: Corporate Bond Default and Recovery Rates" which includes data since 1920 and is published by Moody's Investors Service. However, other sources including internally modeled forecasts could be used.

<sup>10</sup> Under § 652.40(b), investments used to satisfy the liquidity reserve requirement must be "readily marketable," as defined by that provision.

be used effectively to manage interest rate risk. Finally, we propose moving to paragraph (b) (3) the existing requirement that the denomination of all investments must be in U.S. dollars.

2. Other Non-Program Investments [new § 652.23]

We propose moving the existing § 652.20(e) provisions on seeking FCA approval for non-program investments that are not already identified in the regulation as an “eligible non-program investment” to new § 652.23. The proposed new § 652.23 explains the minimum considerations we give to such requests and reiterates our authority to impose in writing and enforce conditions of approval. We also add clarifying language that these investments, once approved, will be considered “eligible non-program investments” for purposes of applying the provisions in subpart A of part 652. We believe moving this aspect of the rule to its own section will make the provision easier to find and, along with the proposed clarifications, will facilitate the process by which such requests are submitted and reviewed.

3. Ineligible Investments [existing § 652.25]

We are proposing revisions to existing § 652.25 to conform with other proposed changes in this rulemaking and to add clarity. We propose adding language to clarify that

this section applies to both those eligible non-program investments identified in the rule and to individual non-program investments that we approved on request. We also propose clarifying that those investments that were ineligible when purchased may not be used for liquidity purposes, but must still be included as part of the investment portfolio limit until their divestiture. We further propose removing the quarterly reporting requirements for investments that lose their eligibility after purchase.

4. Reservation of FCA Authority [existing § 652.25(d); new § 652.27]

We propose moving the existing § 652.25(d) provisions addressing FCA-required divestiture of an investment to new § 652.27. We believe moving this aspect of the rule to its own section will make the provision easier to find and reduce confusion on its applicability. In addition, we propose to make explicit our authority, on a case-by-case basis, to determine that a particular investment imposes inappropriate risk, notwithstanding that it satisfies the investment eligibility criteria. The proposal also provides that FCA will notify Farmer Mac as to the proper treatment of any such investment. We also propose conforming changes due to other proposed changes in this

rulemaking to clarify that FCA-required divestiture may be based on a failure to comply with applicable regulations or written conditions of approval issued in connection with individual non-program investments that we approved on request.

D. Liquidity Reserve Requirements [Table to § 652.40(c)]

We propose to make conforming changes in the Table to § 652.40(c). These changes would incorporate the proposed terminology changes of § 652.5. In addition, we propose changes to clarify that MBS must be fully guaranteed by a U.S. Government agency to qualify for Level 2 liquidity and fully guaranteed by a GSE to qualify for Level 3 liquidity.

IV. Compliance Date

In order to provide Farmer Mac with sufficient time to bring itself into compliance with these new requirements, we are proposing a 6-month compliance transition period. We invite your specific comments on this compliance timeframe.

V. Regulatory Flexibility Act

Pursuant to section 605(b) of the Regulatory Flexibility Act (5 U.S.C. 601 et seq.), FCA hereby certifies that this proposed rule will not have a significant economic impact on a substantial number of small entities. Farmer Mac has assets and annual income in

excess of the amounts that would qualify it as a small entity. Therefore, Farmer Mac is not a "small entity" as defined in the Regulatory Flexibility Act.

List of Subjects

12 CFR Part 652

Agriculture, Banks, banking, Capital, Investments, Rural areas.

For the reasons stated in the preamble, part 652 of chapter VI, title 12 of the Code of Federal Regulations is proposed to be amended as follows:

PART 652—FEDERAL AGRICULTURAL MORTGAGE CORPORATION FUNDING AND FISCAL AFFAIRS

1. The authority citation for part 652 is revised to read as follows:

Authority: Secs. 4.12, 5.9, 5.17, 8.11, 8.31, 8.32, 8.33, 8.34, 8.35, 8.36, 8.37, 8.41 of the Farm Credit Act (12 U.S.C. 2183, 2243, 2252, 2279aa-11, 2279bb, 2279bb-1, 2279bb-2, 2279bb-3, 2279bb-4, 2279bb-5, 2279bb-6, 2279cc); sec. 514 of Pub. L. 102-552, 106 Stat. 4102; sec. 118 of Pub. L. 104-105, 110 Stat. 168; sec. 939A of Pub. L. 111-203, 124 Stat. 1326, 1887 (15 U.S.C. 78o-7 note) (July 21, 2010).

2. Amend § 652.5 by:

a. Removing the definitions for "Contingency Funding Plan (CFP)", "Eurodollar time deposit", "Final maturity", "General obligations", "Government agency", "Government-sponsored agency", "Liability Maturity Management Plan (LMMP)", "Liquid investments", "Liquidity reserve", "Mortgage securities", "Nationally recognized statistical rating organization (NRSRO)", "Revenue bond", and "Weighted average life (WAL)";

b. Revising the last sentence to the definition for "Asset-backed securities (ABS)"; and

c. Adding alphabetically five definitions to read as follows:

§ 652.5 Definitions.

For purposes of this subpart, the following definitions will apply:

\* \* \* \* \*

Asset-backed securities (ABS) \* \* \* For the purpose of this subpart, ABS excludes mortgage-backed securities that are defined below.

\* \* \* \* \*

Diversified investment fund (DIF) means an investment company registered under section 8 of the Investment Company Act of 1940.

\* \* \* \* \*

Government-sponsored enterprise (GSE) means an entity established or chartered by the United States Government to serve public purposes specified by the United States Congress but whose debt obligations are not explicitly guaranteed by the full faith and credit of the United States Government.

\* \* \* \* \*

Mortgage-backed securities (MBS) means securities that are either:

(1) Pass-through securities or participation certificates that represent ownership of a fractional undivided interest in a specified pool of residential (excluding home equity loans), multifamily or commercial mortgages, or

(2) A multiclass security (including collateralized mortgage obligations and real estate mortgage investment conduits) that is backed by a pool of residential, multifamily or commercial real estate mortgages, pass through MBS, or other multiclass MBS.

(3) This definition does not include agricultural mortgage-backed securities guaranteed by Farmer Mac itself.

\* \* \* \* \*

Obligor means an issuer, guarantor, or other person or entity who has an obligation to pay a debt, including

interest due, by a specified date or when payment is demanded. For a DIF, both the DIF itself and the entities obligated to pay the underlying debt are considered a single obligor.

\* \* \* \* \*

U.S. Government agency means an instrumentality of the U.S. Government whose obligations are fully guaranteed as to the payment of principal and interest by the full faith and credit of the U.S. Government.

3. Amend § 652.10 by:

a. Removing the word "four" in the last sentence of the paragraph (c) introductory text;

b. Removing the phrase "geographical areas," in paragraph (c) (1) (i); and

c. Adding a new paragraph (c) (5) to read as follows:

§ 652.10 Investment management.

\* \* \* \* \*

(c) \* \* \*

(5) Concentration risk. Your investment policies must set risk diversification standards. Diversification parameters must be based on the carrying value of investments.

(i) The Corporation's maximum allowable investments in any one obligor may not exceed 10 percent of Regulatory

Capital. Only investments in obligations backed by U.S. Government agencies or GSEs may exceed the 10-percent single obligor limit.

(ii) Not more than 50 percent of the Corporation's entire investment portfolio may be comprised of GSE-issued MBS.

\* \* \* \* \*

4. Section 652.20 is revised to read as follows:

§ 652.20 Eligible non-program investments.

(a) Eligible investments consist of:

(1) A non-convertible senior debt security.

(2) A money market instrument with a maturity of 1 year or less.

(3) A portion of an ABS or MBS that is fully guaranteed by a U.S. Government agency.

(4) A portion of an ABS or MBS that is fully and explicitly guaranteed as to the timely payment of principal and interest by a GSE.

(5) The senior-most position of an ABS or MBS that is not fully guaranteed by a U.S. Government agency or fully and explicitly guaranteed as to the timely payment of principal and interest by a GSE, provided that the MBS satisfies the definition of "mortgage related security" in 15 U.S.C. 78c(a)(41).

(6) An obligation of an international or multilateral development bank in which the U.S. is a voting member.

(7) Shares of a diversified investment fund, if its portfolio consists solely of securities that satisfy investments listed in paragraphs (b)(1) through (b)(4) of this section.

(b) Farmer Mac may only purchase those eligible investments satisfying all of the following:

(1) The obligor(s) of the investment have strong capacity to meet financial commitments for the life of the investment. A strong capacity to meet financial commitments exists if the risk of default by the obligor(s) is very low. Investments whose obligors are located outside the U.S., and whose obligor capacity to meet financial commitments is being relied upon to satisfy this requirement, must also be fully guaranteed by a U.S. Government agency.

(2) The investment must exhibit low credit risk and other risk characteristics consistent with the purpose or purposes for which it is held. At a minimum, obligors must have strong capacity to meet financial commitments and generally have a very low probability of default throughout the term of the investment even under severely adverse, stressful conditions in the obligors' business environment.

(3) The investment must be denominated in U.S. dollars.

5. Add a new § 652.23 to read as follows:

§ 652.23 Other non-program investments.

(a) Farmer Mac may make a written request for our approval to purchase and hold other non-program investments that do not satisfy the requirements of § 652.20. Your request for our approval to purchase and hold other non-program investments at a minimum must:

(1) Describe the investment structure;

(2) Explain the purpose and objectives for making the investment; and

(3) Discuss the risk characteristics of the investment, including an analysis of the investment's impact to capital.

(b) We may impose written conditions in conjunction with our approval of your request to invest in other non-program investments.

(c) For purposes of applying the provisions of this subpart, except § 652.20, investments approved under this section are treated the same as eligible non-program investments unless our conditions of approval state otherwise.

6. Section 652.25 is revised to read as follows:

§ 652.25 Ineligible investments.

(a) Investments ineligible when purchased. Non-program investments that do not satisfy the eligibility criteria set forth in § 652.20(a) or have not been approved by the FCA pursuant to § 652.23 at the time of purchase are ineligible. You must not purchase ineligible investments. If you determine that you have purchased an ineligible investment, you must notify us within 15 calendar days after such determination. You must divest of the investment no later than 60 calendar days after you determine that the investment is ineligible unless we approve, in writing, a plan that authorizes you to divest the investment over a longer period of time. Until you divest of the investment, it may not be used to satisfy your liquidity requirement(s) under § 652.40, but must continue to be included in the § 652.15(b) investment portfolio limit calculation.

(b) Investments that no longer satisfy eligibility criteria. If you determine that a non-program investment no longer satisfies the criteria set forth in § 652.20 or no longer satisfies the conditions of approval issued under § 652.23, you must notify us within 15 calendar days after such determination. If approved by the FCA in writing, you may continue to hold the investment, subject to the following and any other conditions we impose:

(1) You may not use the investment to satisfy your § 652.40 liquidity requirement(s);

(2) The investment must continue to be included in your § 652.15 investment portfolio limit calculation; and

(3) You must develop a plan to reduce the investment's risk to you.

7. Add a new § 652.27 to read as follows:

§ 652.27 Reservation of authority for investment activities.

FCA retains the authority to require you to divest of any investment at any time for failure to comply with applicable regulations, for safety and soundness reasons, or failure to comply with written conditions of approval. The timeframe set by FCA for such required divestiture will consider the expected loss on the transaction (or transactions) and the effect on your financial condition and performance. FCA may also, on a case-by-case basis, determine that a particular non-program investment poses inappropriate risk, notwithstanding that it satisfies the investment eligibility criteria or received prior approval from us. If so, we will notify you as to the proper treatment of the investment.

8. Amend § 652.40 by revising the table in paragraph (c) to read as follows:

§ 652.40 Liquidity reserve requirement and supplemental  
liquidity.

\* \* \* \* \*

Table to § 652.40(c)

Liquidity level	Instruments	Discount (multiply market value by)
Level 1	• Cash, including cash due from traded but not yet settled debt	100 percent
	• Overnight money market instruments, including repurchase agreements secured exclusively by Level 1 investments	100 percent
	• Obligations of U.S. Government agencies with a final remaining maturity of 3 years or less	97 percent
	• GSE senior debt securities that mature within 60 days, excluding securities issued by the Farm Credit System	95 percent
	• Diversified investment funds comprised exclusively of Level 1 instruments	95 percent
Level 2	• Additional Level 1 investments	Discount for each Level 1 investment applies
	• Obligations of U.S. Government agencies with a final remaining maturity of more than 3 years	97 percent
	• MBS that are fully guaranteed by a U.S. Government agency	95 percent
	• Diversified investment funds comprised exclusively of Level 1 and 2 instruments	95 percent
Level 3	• Additional Level 1 or Level 2 investments	Discount for each Level 1 or Level 2 investment applies
	• GSE senior debt securities with maturities exceeding 60 days, excluding senior debt securities of the Farm Credit System	93 percent for all instruments in Level 3
	• MBS that are fully guaranteed by a GSE as to the timely repayment of principal and interest	
	• Money market instruments maturing within 90 days	
	• Diversified investment funds comprised exclusively of levels 1, 2, and 3 instruments	
	• Qualifying securities backed by Farmer Mac program assets (loans) guaranteed by the United States Department of Agriculture (excluding the portion that would be necessary to satisfy obligations to creditors and equity holders in Farmer Mac II LLC)	

Supplemental Liquidity	• Eligible investments under § 652.20 and those approved under § 652.23	90 percent except discounts for Level 1, 2 or 3 investments apply to such investments held as supplemental liquidity
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Date: February 12, 2016\_

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Dale L. Aultman,  
Secretary,  
Farm Credit Administration Board.

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