Opening Remarks of the Honorable Michael M. Reyna
Chairman and Chief Executive Officer
Farm Credit Administration
Before the Committee on Agriculture
United States House of Representatives
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Chairman Goodlatte, Ranking Member Stenholm, and Members of the House Agriculture Committee, I am Michael M. Reyna, Chairman and Chief Executive Officer of the Farm Credit Administration (FCA or Agency). Joining me today are my colleagues on the FCA Board, Doug Flory and Nancy Pellett.

On behalf of the FCA Board, I wish to thank you for the invitation to discuss the changing structure of agricultural cooperatives and the challenges that cooperatives face as they seek to increase the income of their farmer-members while, at the same time, finding new ways to finance their operations. These challenges, and how Congress chooses to address them, are of prime importance.

As you know, I have provided the committee detailed written testimony on the topic of today's hearing; hence, my opening remarks will be brief so as to be respectful of the committee's time and the time of other witnesses scheduled to testify.

As you know, the Farm Credit Administration is the independent federal financial regulatory agency that is responsible for overseeing the mission and the safety and soundness of two separate, but related, agricultural Government Sponsored Enterprises (GSEs), including the Farm Credit System (System) and the Federal Agricultural Mortgage Corporation (Farmer Mac). We achieve our objective by conducting periodic financial safety and soundness examinations and by adopting regulations that provide for necessary guidance.

The System is a nationwide cooperative network of borrower-owned financial institutions that lend to agriculture and rural America. Established in 1916, it is the oldest Government Sponsored Enterprise in the United States, and is the only one that engages in lending at the retail level.

The mission of the System is to improve the income and well being of American farmers and ranchers by furnishing sound, adequate, and constructive credit and closely related services to them, their cooperatives, and to selected farm-related businesses necessary for efficient farm operations. It does this by serving all eligible borrowers having a basis for credit and, as required by Congress, by placing a high priority on financing young, beginning and small farmers.

Cooperatives have played a crucial role in making American agriculture prosperous, productive, and efficient. They increase the sales revenue of farmers and lower the costs that farmers pay for supplies and business services. In addition to increasing revenues and lowering costs, cooperatives are a vital and integral part of rural America.

Cooperatives strengthen the agricultural economy and improve living conditions in rural areas in many different ways. For example, earnings in the form of patronage are returned to farmers, who contribute to the local economy. Cooperatives strengthen the economic base of the local community by adding to the tax base, creating new jobs, and spurring retail sales and services. Cooperatives also help provide consumers with more choices and new products.

It is the unique structure of cooperatives that strengthens the market power of farmers so they can earn more and live better. The characteristics of traditional farmer cooperatives include the following:

- Agricultural producers are a large majority of the voting members;
- Each member has only one vote, regardless of the amount of equity capital owned;
- Members earn patronage based on the amount of business they do with the cooperative,
- Dividend payments on equity capital are restricted, and the cooperative does more business with members than non-members.

For more than 80 years, Congress has sought to preserve and expand the benefits that cooperatives have to offer. Specifically, Congress has devised a public policy that grants cooperatives certain legal protections, tax benefits, and other advantages that are not conferred on investor-owned agribusinesses. As a result, farmer cooperatives have direct access to GSE funding that their competitors, which are investor-owned agribusinesses, generally lack.

It is important to note that farmer cooperatives play an important role in America's agricultural economy, with the share of overall farm commodities marketed through cooperatives being fairly steady over the past five years. And, although the number of farmer cooperatives has declined 25 percent in the past decade, the net business volume of cooperatives actually increased.

While no empirical data is available to determine whether farmers have been reducing their use of the traditional cooperative form of structure in recent years, our agency did, however, conduct a limited survey in which we contacted the ten states with the greatest number of cooperatives to identify annual trends in new cooperative filings.

Specifically, FCA staff found no consistent trend in the number of new filings over the period 1993 to 2003. While half of the states did display a declining trend in the number of cooperative filings, two states displayed an increasing trend and one state showed no change. Two states were unable to provide the data. A broader survey, as well as further study, may be warranted.

Notwithstanding numbers, trends, and limited surveys, there are concerns being raised by some individuals and groups that traditional cooperatives are not resilient enough to endure the economic changes facing agriculture today and help farmers overcome new challenges. It is not uncommon for farmers to struggle to find sufficient capital to enable them to invest in their own value-added enterprises. And, when farmers cannot raise sufficient capital on their own, they must turn to outside sources of equity.

To attract outside equity capital or increase their business with nonmembers, some farmer groups are forming hybrid organizations or restructuring existing cooperatives. FCA staff has identified numerous examples of value-added cooperatives that had changed to the LLC form or that had formed a joint venture LLC with other cooperatives or Subchapter C firms. In addition, some groups of farmers have chosen to form new value-added enterprises as LLCs rather than cooperatives.

LLCs offer many advantages that cooperatives do not. Among other advantages for example, LLCs attract outside investors by giving them a say in management and a return in proportion to their investment.

And, while a few well-established cooperatives have been able to attract outside equity successfully, for a host of reasons most outside investors have little incentive to invest in agricultural cooperatives. This is especially true for start-up cooperatives.

Recognizing the limitations of the traditional cooperative structure, Wyoming and Minnesota have enacted new laws that allow farmers and investors to join together to form new types of cooperatives. The two state laws are not identical, and their treatment of certain issues differs. These cooperatives can best be described as hybrids between traditional cooperatives and LLCs.

These laws are newly enacted, and at this early stage it is unknown how many traditional cooperatives plan to convert into hybrid cooperatives, or how many entities will be formed under these new state laws.

The FCA Board is aware that CoBank is developing a legislative proposal that would give it more flexibility to finance cooperatives that are adjusting their structure in response to changing markets.

While Congress is ultimately responsible for deciding the scope of CoBank's lending powers, please rest assured that the FCA is prepared to implement and enforce any policy that Congress enacts.

As always, the FCA is ready to offer you assistance in crafting any changes to the Farm Credit Act, and we look forward to working with this Committee as it considers issues that are important to agriculture and rural America.

Thank you for the opportunity to testify at today's important hearing.