Date: May 12, 2016

TO: CHIEF EXECUTIVE OFFICER
   ALL STATE CHARTERED BANKS

FROM: BRET AFDAHL
   DIRECTOR OF BANKING

RE: CLASSIFICATION GUIDELINES FOR AGRICULTURAL LOANS

The South Dakota Division of Banking (Division) has previously excluded current inspected livestock held as collateral from total adverse classification when classifying an agricultural credit. In addition, the Division has excluded grain from classification, if the loan file contained warehouse receipts.

It has come to the Division’s attention that federal regulatory agencies recently began excluding grain inventories without the required warehouse receipts. Since grain, like livestock, is highly marketable and provides sound protection from credit losses, the Division will allow the value of grain inventories to be excluded from adverse classification if the following conditions are met:

- A formal inspection by the bank is documented and dated within 90 days of the examination start date. The inspection should be signed by the borrower and the inspecting officer.
- All sale proceeds from the grain inspection date to the examination start date must be documented in order for the examiners to reconcile the inspected grain inventories to actual inventories on hand.
- The bank must have a properly perfected and enforceable security interest in the grain inventories. If there are other parties holding lien(s) on grain inventories owned by the borrower, the grain value will not be excluded from classification unless the other lien holder(s) acknowledge and/or agree to subordinate their liens.

The amount to be excluded from classification is based on the daily, published, market value as of the examination start date, less marketing and transportation costs. Grain held as feed for livestock will not be excluded since the inventory amounts change substantially on a daily basis.

There will be no exclusion if the borrower is highly leveraged and operational viability is questionable, or if the bank is in an under-secured position and the borrower is no longer cooperating with bank management.

It should also be noted that the above conditions apply to excluding the value of livestock from adverse classification, with one exception. The formal inspection for breeding livestock can be dated up to 180 days from the examination start date, instead of the 90-day period for grain inventories and market livestock.

Any questions regarding this Guidance may be directed to your institution’s Contact Examiner at the Division of Banking (605-773-3421).