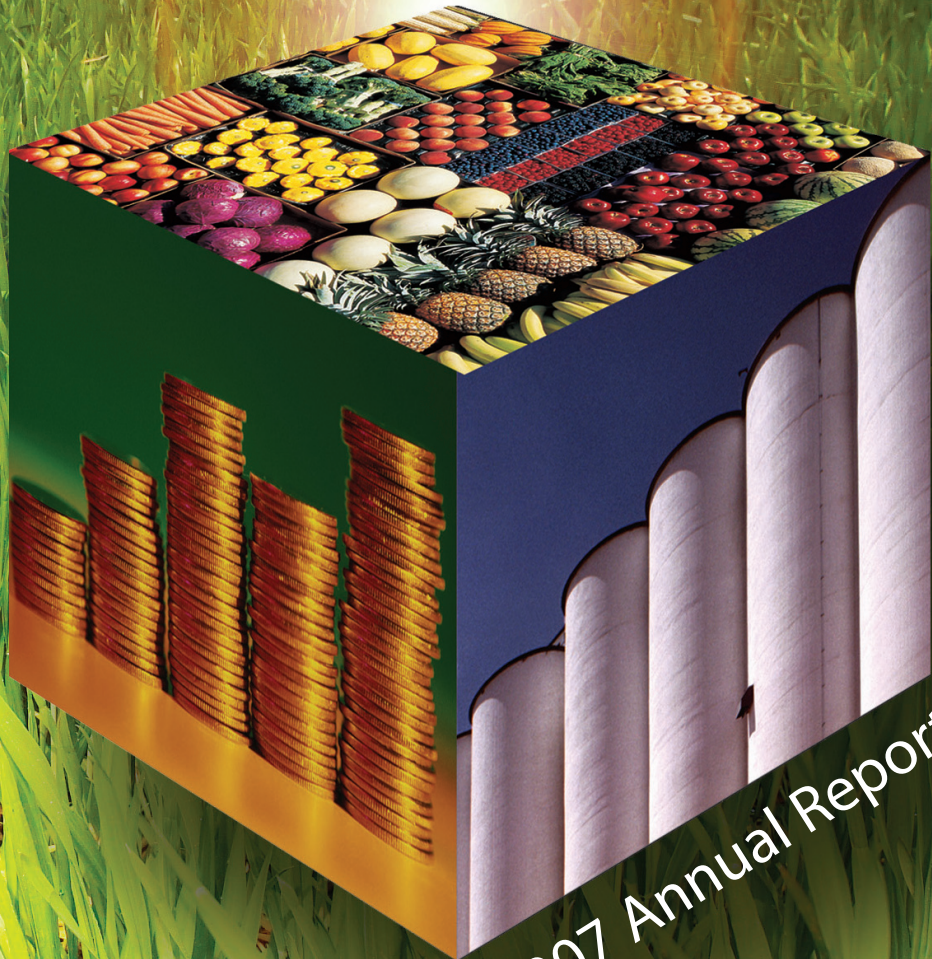


# Farm Credit System Insurance Corporation



2007 Annual Report

# Mission Statement

The Farm Credit System Insurance Corporation, a Government-controlled, independent entity, shall:

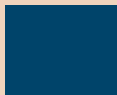
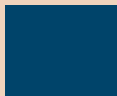
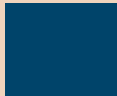
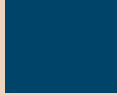
- ♦ Protect investors in insured Farm Credit System obligations and taxpayers through sound administration of the Farm Credit Insurance Fund,
- ♦ Exercise its authorities to minimize Insurance Fund loss, and
- ♦ Help ensure the future of a permanent system for delivery of credit to agricultural borrowers.



# Contents

Board of Directors	2
2007 – Year in Review	6
Selected Financial Statistics	7
The Farm Credit System	8
Insurance Fund Management	12
Risk Management	16
Financial Assistance and Receivership	17
Strategic Goals and Performance Measures	18
Reports of Independent Public Auditors	22
Financial Statements	25
Notes to the Financial Statements	28
Income and Expenses	33
Corporate Staff	34
Contact Information	34

# *Protecting Investors in Agriculture and Rural America*





April 30, 2008

Dear Mr. President and Madam Speaker:

In accordance with section 5.64 of the Farm Credit Act of 1971 as amended, the Farm Credit System Insurance Corporation is pleased to submit its annual report for calendar year 2007.

This report highlights the Corporation's role as the independent Federal corporation established to ensure the timely payment of principal and interest to investors in insured Farm Credit System debt securities. The balance in the Farm Credit Insurance Fund at December 31, 2007, was \$2.6 billion. The Corporation collected \$191 million in insurance premiums from Farm Credit System banks for 2007, earned \$98 million in investment income during the same period, and expects to incur \$3.0 million in operating costs in 2008.

Sincerely,

A handwritten signature in black ink, which appears to read 'Leland A. Strom'. The signature is written in a cursive style.

Leland A. Strom  
Chairman

The President of the United States Senate  
The Speaker of the United States House of Representatives

## Board of Directors



*The Farm Credit System Insurance Corporation (FCSIC or Corporation) is managed by a three-member board of directors composed of the same three individuals who compose the Farm Credit Administration (FCA) Board. However, the same member may not serve as chairman of both entities. FCA is the independent Federal agency responsible for the regulation and examination of the Farm Credit System (FCS or System). The FCS is a nationwide financial cooperative that lends to agriculture and rural America.*

## Leland A. Strom



Other boards Mr. Strom has served on include Northern F.S., Inc., a multimillion-dollar farm service and supply cooperative serving farmers in Northern Illinois; AgriBank, FCB; and the Farm Credit Council, the national trade organization representing FCS in Government affairs. For his overall involvement in agriculture, he received an Outstanding Young Farmer award.

Mr. Strom studied agriculture business at Kishwaukee College and business administration at Northern Illinois University. His community involvement includes having served as vice president of his local K-12 school district, chairman of his church council, 4-H parent leader, and coach of boys' and girls' sports teams. Mr. Strom owns a third-generation family farm in Illinois that produces corn and soybeans. He and his wife, Twyla, have two sons and a daughter.

Leland A. Strom is Chairman of the Farm Credit System Insurance Corporation (FCSIC) Board of Directors. He was elected to this position on December 15, 2006, following his appointment earlier that month to the Farm Credit Administration Board by President George W. Bush.

For more than 30 years, he has been active in the agriculture industry. He served for more than 25 years on the board of 1st Farm Credit Services, an FCS institution in Illinois, holding various positions, including chairman. During the agriculture crisis of the 1980s, he was selected to sit on the Restructuring Task Force of the Sixth Farm Credit District.

From 2000 to 2006, he was on the Federal Reserve Bank of Chicago Advisory Council on Agriculture, Labor, and Small Business. Part of this time he also served on the County Mutual Fund Trust Board, an investment fund of the Illinois Farm Bureau and its Country Financial organization.

## Nancy C. Pellett



Nancy C. Pellett is Chairman of the Board and CEO of FCA. Ms. Pellett was appointed to a six-year term on the FCA Board by President George W. Bush on November 14, 2002, and she was designated Chairman on May 22, 2004. Her term expires on May 21, 2008.

Ms. Pellett also serves as a member of the Board of Directors of the Farm Credit System Insurance Corporation.

Ms. Pellett brings to her position extensive experience in production agriculture and agribusiness. In partnership with her husband, she managed Prairie Hills, Ltd., a feedlot, cow-calf, and row-crop operation in Atlantic, Iowa, from 1966 until her appointment to the Board. While she serves her term as FCA Chairman and CEO, her husband, son, and daughter-in-law continue to operate this fifth-generation family farm.

In addition, for more than 20 years, she served as president and treasurer of Fredrechsens Farms, Ltd., a family-owned swine and row-crop operation in Walnut, Iowa.

A long-time beef industry leader, Ms. Pellett has held State and national leadership positions in cattle industry organizations. As a member of the National Cattlemen's Beef

Association, she has served as the chairman of the Check-Off Division, as chairman of the Consumer Marketing Group, and most recently as a member of the Cattlemen's Beef Board. She has also been president of the Iowa Beef Industry Council.

She is a partner in Premium Quality Foods, Inc., which markets precooked beef entrees. Previously, she served as president and consumer marketing director for the company.

Ms. Pellett served a six-year term as a member of the Board of Regents for the State of Iowa, which oversees the three State universities, as well as the University of Iowa Hospital and its affiliated clinics. She was also selected as a member of the Governor's Student Aid Commission.

She is on the Iowa State University (ISU) Foundation Board of Governors and has been a member of the advisory committees for the College of Agriculture and the College of Family and Consumer Sciences. She is past president of the ISU Alumni Association and was awarded the Alumni Medal in 1987. The Pellett family was honored as the "Family of the Year" by the university in 1997.

Dedicated to the future of agriculture, she worked with 4-H and FFA at the local and State levels, and served on the Iowa 4-H Foundation Board. She is a founding member of the 4-H/FFA "Sale of Champions" committee for the Iowa State Fair.

A native of Walnut, Iowa, she holds a B.S. from Iowa State University at Ames. She and her husband have four children. The Pellett family received the "Friends of Youth Award" in 2000 from the Knights of AkSarBen, a foundation that supports education, youth programs, and rural development in Nebraska and western Iowa.



## Dallas P. Tonsager



Dallas P. Tonsager was appointed to the FCA Board by President George W. Bush on December 1, 2004, for a term that expires May 21, 2010 and serves as a member of the Board of Directors of the Farm Credit System Insurance Corporation.

Mr. Tonsager brings to his position extensive experience as an agriculture leader and producer, and a commitment to promoting and implementing innovative development strategies to benefit rural residents and their communities. As executive director of the South Dakota Value-Added Agriculture Development Center in Huron from 2002 until his appointment to the FCA Board, he coordinated initiatives to better serve producers interested in developing value-added agricultural projects. Services provided by the center include project facilitation, feasibility studies, business planning, market assessment, technical assistance, and education.

In 1993, he was selected by President William J. Clinton to serve as the State director in South Dakota for rural development for the U.S. Department of Agriculture. Mr. Tonsager oversaw a diversified portfolio of housing, business, and infrastructure loans in South Dakota totaling more than \$100 million. In 1999, he was recognized as one of two

outstanding State directors in the nation by then-USDA Under Secretary Jill Long Thompson. His term concluded in February 2001.

A long-time member of the South Dakota Farmers Union, Mr. Tonsager served two terms as president of the organization from 1988 to 1993. He served on the board of National Farmers Union Insurance from 1989 to 1993, and he was a member of the advisory board of the Commodity Futures Trading Commission from 1990 to 1993.

From 1988 to 1993, Mr. Tonsager was a board member of Green Thumb, Inc., a nationwide job training program for senior citizens. He currently serves on the board of Lutheran Social Services of South Dakota.

Mr. Tonsager grew up on a dairy farm near Oldham, South Dakota. In partnership with his brother, he owns Plainview Farm in Oldham, a family farming operation that includes corn, soybeans, wheat, and hay. Mr. Tonsager is a graduate of South Dakota State University where he earned a B.S. in agriculture in 1976. He and his wife, Sharon, have two sons and a daughter-in-law.

# 2007 – Year in Review

## Legislation

Perhaps the Corporation's most significant initiative in 2007 was its legislative proposal to enhance the Corporation's statutory premium authority. During 2005 and 2006, the Farm Credit Insurance Fund (Insurance Fund) decreased as a percentage of outstanding insured debt because sustained growth outstripped the rate at which the Corporation could collect premiums under its current statutory authority. In March 2007 the Board of Directors authorized a legislative initiative to amend the premium authority to better reflect the risk insured and enable the Corporation to collect adequate premiums to maintain the Insurance Fund in periods of sustained System growth.

The Corporation insures the timely payment of principal and interest on insured debt issued by the FCS banks. The Corporation's legislative proposal recommends that the Farm Credit Act of 1971 be amended to generally authorize the Corporation to collect premiums based on the System banks' outstanding insured debt, rather than on loans. This change would increase the premium base and align premiums with the risk the Corporation insures. In addition, in order to enhance investor protection, the proposal recommends that the statute be amended to authorize the Corporation to collect up to 20 basis points annually on insured debt. This change would enable the Corporation to recapitalize the Farm Credit Insurance Fund in a reasonable amount of time, even when there is significant growth in the use of insured borrowings. The proposed amendments would maintain a risk surcharge on non-accrual loans, add a surcharge on other-than-temporarily impaired investments, and make a number of other changes to the premium provisions.

During 2007, the Corporation's staff met on a number of occasions with congressional personnel to discuss the proposed statutory amendments. The Corporation's legislative proposal was in large part incorporated in the provisions of the Farm Bill passed by the House of Representatives on July 27, 2007, as well as in the provisions

of the Farm Bill passed by the Senate on December 14, 2007. At the end of 2007, Congress enacted a short-term extension of the current law. The Senate and the House of Representatives must complete a conferencing process and any subsequent bill must be signed by the President before the new Farm Bill becomes law. Therefore, there is no assurance that the provisions will be enacted.

## Economic Headwinds

The Farm Credit System experienced another year of strong growth in its lending markets, and continued high profitability at its institutions. Conditions in agriculture were favorable as producers benefited from record prices for grains and other commodities. While the outlook for the industry in 2008 is generally bright, we are watching the following trends closely to gauge their effect on the System.

- Last year's turmoil in the capital markets and the housing sector may more directly affect the System as this year unfolds. Major players in the nation's financial system have experienced stress resulting from a significant shift in pricing and investor tolerance for risk. In the late summer of 2007, the Federal Reserve (Fed) began the first of a series of dramatic actions to address the factors that caused the credit markets to stall. The Fed has reduced interest rates and increased liquidity facilities for banks and other financial institutions to ensure the availability of credit. The System relies on the capital markets as the principal source of its funds to finance agriculture and rural America. One consequence of extended turmoil in the capital markets may be more demand for credit from eligible customers who used other financial institutions prior to this credit crunch.
- Costs are rising for energy and other inputs such as feed and fertilizer. These higher costs will affect sectors of the agricultural economy differently.

- The increased use of agricultural commodities to produce energy has had a dramatic effect on crop prices and borrowing levels.
- The declining value of the dollar is proving a boon to the export of farm products internationally. Continued depreciation in dollar exchange rates forecast for 2008 and beyond should make U.S. farm products less expensive for foreign buyers.

### Investment Program Review

In 2007, FCSIC engaged Evaluation Associates (EA), a Milliman Company, to review the Corporation's investment program. The purpose of the periodic study was to determine whether FCSIC's program implements the best practices of the investment management industry. The study evaluated investment policy, operating procedures, internal controls, and the software system that FCSIC uses to manage the investment program. While considering FCSIC's mission, risk tolerance, and regulatory framework, EA also evaluated the investment

strategy and approach to determine whether FCSIC was maximizing its returns. As part of the analysis EA also reviewed portfolio performance and the benchmarks used for performance measurement.

FCSIC's primary objective in managing the Insurance Fund is to ensure adequate liquidity is available to meet the Corporation's statutory obligations. Its secondary objective is to maximize the rate of return and minimize the potential for loss of principal. Investment authority is limited to U. S. Treasury and U. S. Government-guaranteed securities. In addition, FCSIC cannot trade for the purpose of capital gain. Given these constraints, EA concluded that FCSIC has performed well in managing its portfolio.

EA compared the performance of the FCSIC-managed portfolio to a hold-to-maturity laddered approach. EA concluded that FCSIC had produced a cumulative yield advantage of 173 basis points during the period reviewed, resulting in approximately \$24 million of additional revenues.

## Selected Financial Statistics

### Farm Credit System Insurance Corporation

(Dollars in millions)

	2007	2006	2005
<b>BALANCE SHEET:</b>			
Total Assets	\$ 2,598.9	\$ 2,311.9	\$ 2,061.8
Total Liabilities	0.4	0.3	0.4
Insurance Fund Balance			
Allocated Insurance Reserve Accounts	39.9	39.9	39.9
Unallocated Insurance Fund Balance	2,558.6	2,271.7	2,021.5
<b>OPERATIONS:</b>			
Revenues	289.7	252.3	130.6
Operating Expenses	2.7	2.1	2.2
Insurance Expense	-0-	-0-	6.2
Net Income	287.0	250.2	122.2

# The Farm Credit System

## Structure and Funding

The System is owned by the rural customers it serves, including farmers, ranchers and other agricultural producers. As of December 31, 2007, there were 95 FCS associations that lend directly to these owner-borrowers, providing a consistent source of agricultural and rural credit throughout the United States and the Commonwealth of Puerto Rico. Each association has its own chartered territory and is affiliated with one of the five FCS banks. The banks generally receive their funding through the issuance of Federal Farm Credit Banks Consolidated Systemwide Debt Securities (Systemwide Debt Securities). These securities are issued by the Federal Farm Credit Banks Funding Corporation (Funding Corporation). The Funding Corporation distributes these securities in the capital markets via a selling group of selected investment and dealer banks to raise the funds needed by the System.

## Investor Protection

The Corporation's primary purpose, as defined by the Farm Credit Act of 1971, as amended (the Act), is to insure timely payment of principal and interest on insured Systemwide Debt Securities. Investors provide the funds the System lends to agriculture and rural America.

## Regulatory Oversight

The FCA is the safety and soundness regulator responsible for the examination, supervision, and regulation of each FCS institution. It is an independent agency in the executive branch of the U.S. Government and derives its broad authorities from the Act. These authorities include examination and enforcement authorities similar to those of commercial bank regulators. The U.S. Senate Committee on Agriculture, Nutrition and Forestry and the U.S. House of Representatives Committee on Agriculture oversee FCSIC, FCA, and the FCS.

## Combined Farm Credit System Statistics

(Dollars in billions)

	2007	2006	2005 <sup>2</sup>
Insured Debt Outstanding	\$155.3	\$135.2	\$114.2
Production Agriculture:			
Real Estate Mortgage Loans	63.5	56.5	51.7
Production and Intermediate-term Loans	32.3	28.7	24.9
Agribusiness Loans <sup>1</sup>	28.1	21.1	14.7
Communication Loans	3.4	3.3	2.6
Energy and Water/Waste Disposal Loans	7.5	6.3	5.5
Rural Residential Real Estate Loans	4.0	3.4	3.0
International Loans	2.1	2.2	2.3
Lease Receivables	1.7	1.5	1.3
Loans to Other Financial Institutions	0.4	0.4	0.4
Cash and Investments	36.5	33.1	28.4
Net Income	2.70	2.38	2.10
Nonperforming Loans as a Percentage of Total Loans	0.4%	0.5%	0.6%

1. At December 31, 2007, agribusiness loans consisted of loans to cooperatives of \$15.9 billion, processing and marketing loans of \$9.8 billion and farm-related business loans of \$2.4 billion.

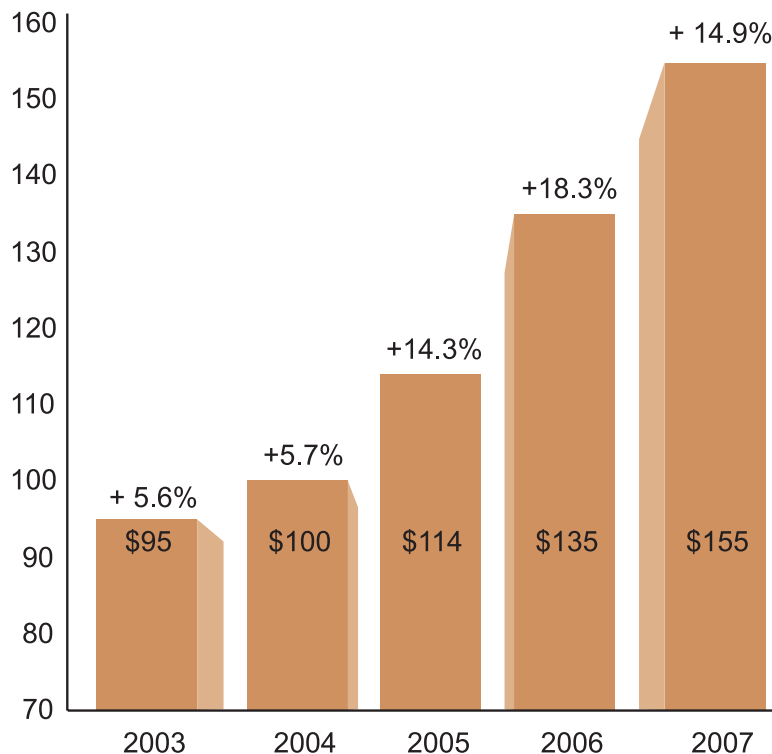
2. Includes post yearend adjustment by the Federal Farm Credit Banks Funding Corporation for prior years.

## Insured and Other Obligations

The Corporation insures Systemwide and consolidated bonds, notes, and other obligations issued by the System banks through the Funding Corporation. Last year, insured obligations outstanding increased by just under 15 percent to \$155.3 billion. For the five-year period from 2003 to 2007, insured debt outstanding grew at an average annual rate of approximately 11.8 percent.

The Corporation is also required by statute to ensure the retirement of “eligible borrower stock,” as defined in section 4.9A of the Act, at par value. This stock, also known as protected borrower stock, was outstanding prior to October 6, 1988. At year-end, eligible borrower stock outstanding at System institutions totaled \$11 million, down from \$13 million at year-end 2006.

## Insured Obligations Outstanding (Dollars in billions)

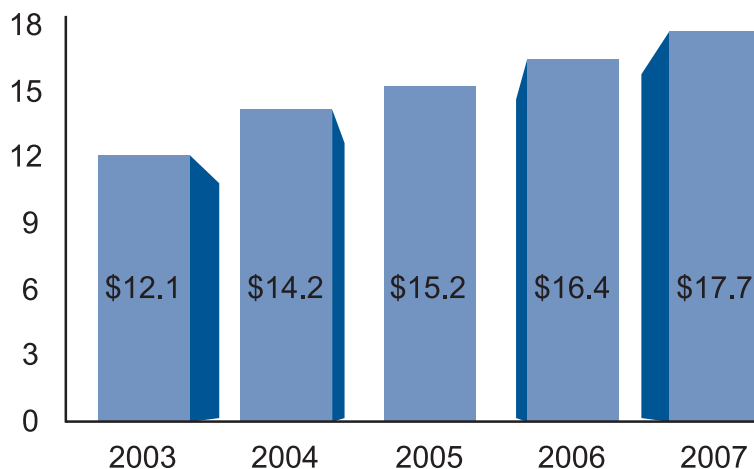


## Farm Credit System Capital

Over the past five years, FCS associations have been building capital through net income earned and retained at the associations. The rise in capital at an association reduces the credit exposure of the association’s affiliated bank. Since 2003 combined association capital has increased 46 percent, from \$12.1 billion to \$17.7 billion at year-end 2007.

Loan growth has been the principal reason for the System’s increased profitability over the past few years. Net interest income has increased, operating efficiency ratios have improved, and credit quality indicators have remained strong. However, this growth has placed, and

## Association Capital (Dollars in billions)



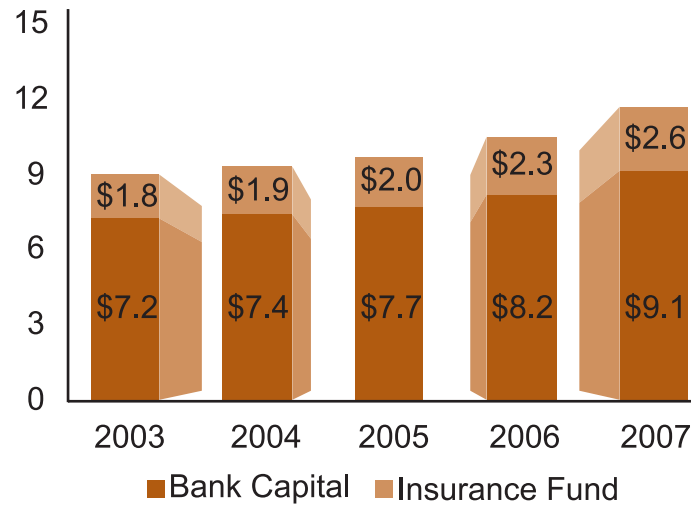
may continue to place, pressure on System institutions' capital ratios, requiring System institutions to continue to evaluate capital management strategies and to seek additional sources of capital.

Since 2003, the amount of FCS bank capital and the balance in the Insurance Fund together has increased 30 percent from \$9 billion to \$11.7 billion at year-end 2007.

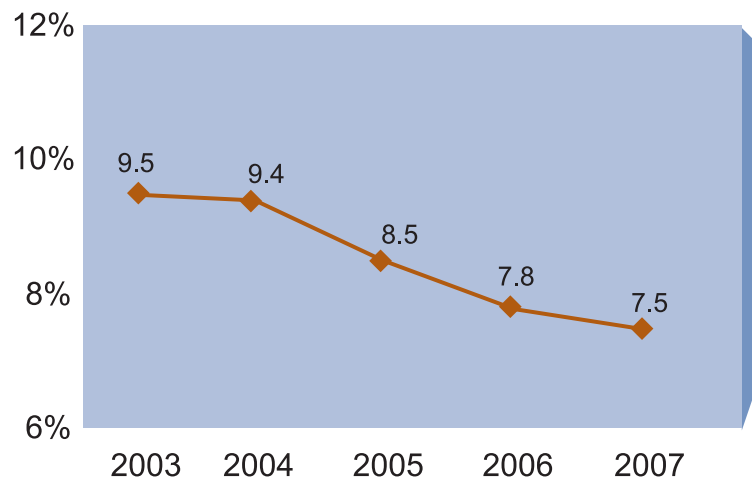
The primary source of funds to repay Systemwide Debt Securities is the System's borrowers. Each borrower is required to have a minimum net worth and, in most cases, collateral posted in connection with his or her loan. The borrower makes payments on the loan to the lending bank or association. The lending association in turn makes payments to its affiliated bank on its loan. Both the banks, which ultimately repay Systemwide Debt Securities, and the associations exceed minimum capital regulatory requirements as protection and support for the repayment of the outstanding debt. If a bank was unable to repay its portion of a security, the Insurance Fund would make that payment. In the event the assets of the Insurance Fund were exhausted, the provisions of joint and several liability of all banks would be triggered, which means the financial resources of the other banks would be used to repay the defaulting bank's portion of the debt issuance.

As a percentage of outstanding insured debt, bank capital plus the amount in the Insurance Fund decreased from 9.5 percent in 2003 to 7.5 percent in 2007. This decline is due to the rate of growth in outstanding debt outpacing growth in bank capital and the Insurance Fund.

### Bank Capital Plus Insurance Fund (Dollars in billions)



### Bank Capital Plus Insurance Fund as a Percentage of Insured Debt



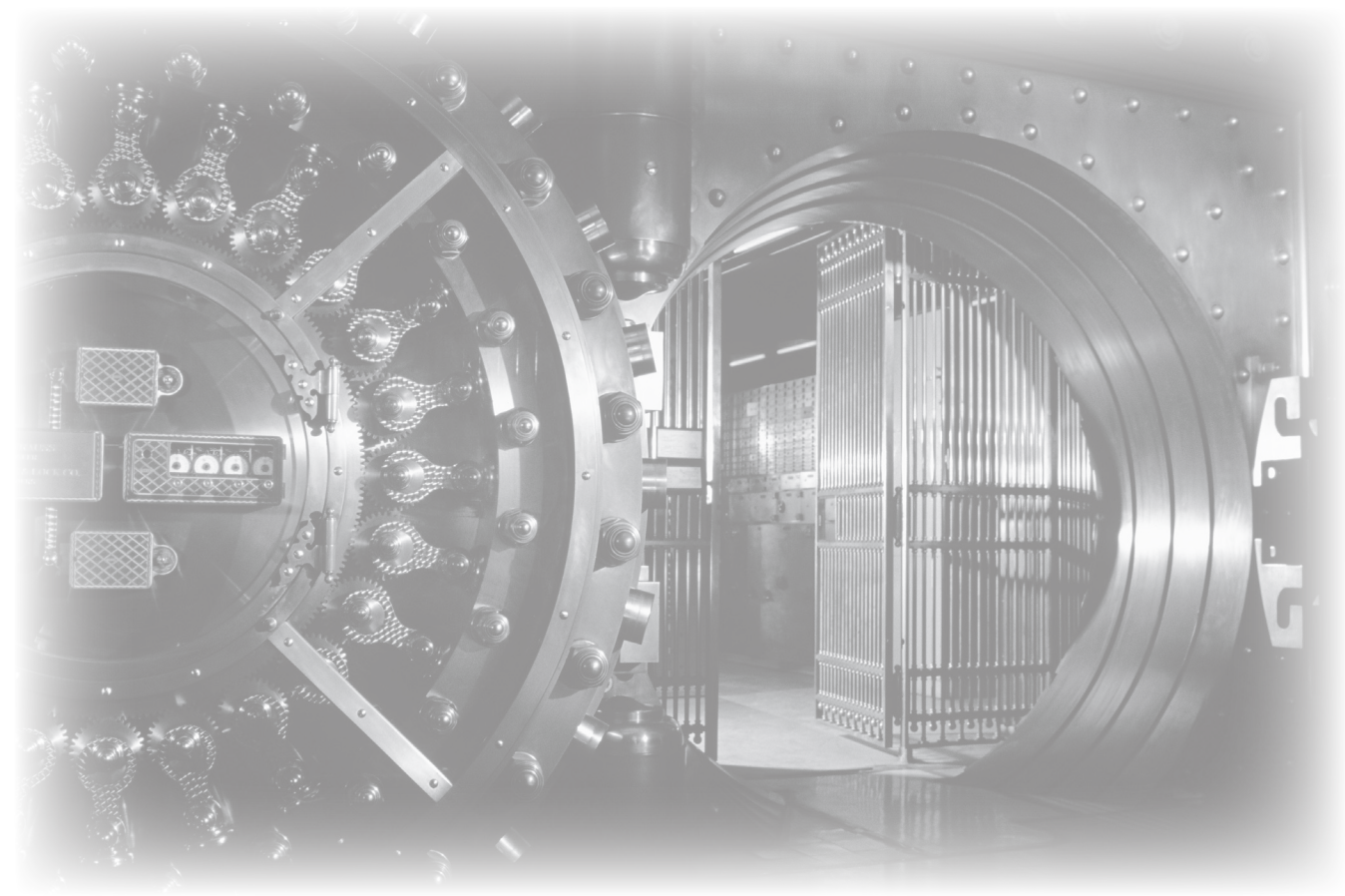
## Additional Protections

The System has additional risk management tools to protect investors. One such tool is the Contractual Inter-bank Performance Agreement (CIPA). All five System banks have entered into this agreement, which measures the financial condition and performance of each bank using ratios that consider capital, asset quality, earnings, interest rate risk, and liquidity. CIPA financially penalizes banks that do not meet performance standards.

The banks and the Funding Corporation have also entered into a Market Access Agreement (MAA) that establishes conditions for each bank's continued participation in the debt market. If a bank fails to meet agreed-upon performance measures, including capital and collateral ratios, its participation in future debt issues could be curtailed. The criteria used under the MAA are the CIPA scores and two capital ratios.

The System also has a common minimum liquidity standard. The standard requires each bank to have enough liquidity to operate for at least 90 continuous days without access to the capital markets.

At December 31, 2007, all banks except one exceeded the minimum 90 days of liquidity, while at December 31, 2006, all banks exceeded the minimum. The bank that failed to meet the 90-day requirement originally calculated it had 106 days of liquidity; after the year-end, the bank determined that its interpretation of the regulation should be modified. When it applied the modified interpretation retroactively, the bank calculated that its liquidity position fell below 90 days for 13 business days. Under the revised calculation, the bank had 84 days of liquidity at December 31, 2007.



# Insurance Fund Management

## The Insurance Fund and the Secure Base Amount

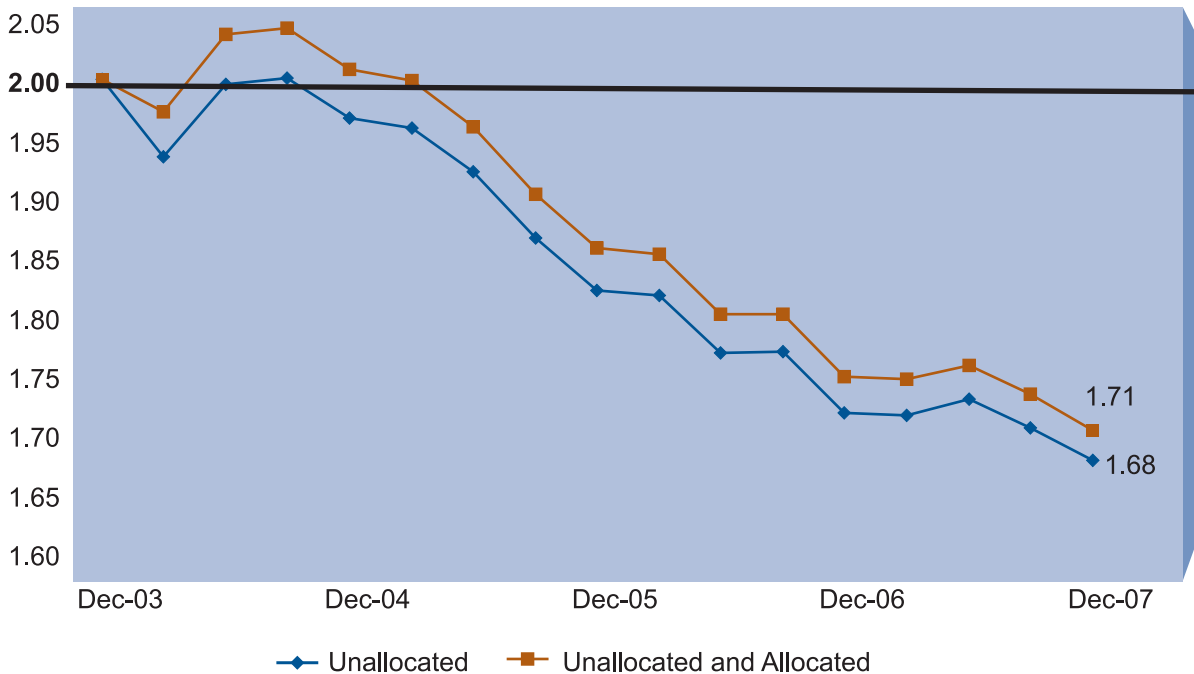
In 2007, both the total Insurance Fund and total assets grew 12.4 percent to \$2.6 billion. Over the last five years, the total Insurance Fund and total assets grew at an annual rate of 9.6 percent and 7.2 percent, respectively. In 2007, the Corporation did not accrue a provision for insurance obligations.

The Insurance Fund represents the Corporation's equity, the difference between total assets and total liabilities, including insurance obligations. The Insurance Fund is comprised of an unallocated Insurance Fund (the assets in the Insurance Fund for which no specific use has been identified or designated) and an allocated Insurance Fund. Premiums are due until the unallocated portion

of the Insurance Fund reaches the secure base amount (SBA). The SBA established by the Act is 2 percent of the aggregate outstanding insured obligations (adjusted to exclude a part of certain Government-guaranteed loans in accrual status) or another percentage that the Board determines to be actuarially sound.

The unallocated Insurance Fund continued to trend further away from the SBA in 2007 because of high growth in insured debt. During 2007, insured debt grew just under 15 percent, below the previous year's rate of growth of just over 18 percent. The unallocated Insurance Fund finished 2007 below the 2 percent SBA at 1.68 percent or \$483 million below the SBA. Including the Allocated Insurance Reserves Accounts (AIRAs) raises the level to 1.71 percent or \$443 million below the SBA.

## Insurance Fund Relative to 2 Percent Secure Base Amount by Quarter (percent)





## Allocated Insurance Reserves Accounts

The unallocated Insurance Fund finished the year below the SBA; therefore, no excess funds were available for transfer to the AIRAs at December 31, 2007. By statute, if the unallocated Insurance Fund is above the SBA, at any year-end, the Corporation must recalculate the SBA using an average daily debt balance method. This amount is then subtracted from the year-end unallocated Insurance Fund balance, less projected insurance and operating expenses for the coming year, to determine the excess amount for transfer to the AIRAs.

In 2003, for the first time, the Corporation closed the year above the SBA. As a result, the Corporation was required to transfer \$39.9 million to the AIRAs. By statute, the Corporation is required to use AIRAs first for insurance claim payments. Separate AIRA accounts have been established for each bank and a special account has been established for the holders of Financial Assistance Corporation (FAC) stock. The first 10 percent of calculated excess funds are deposited to the AIRAs of FAC stockholders. The remaining 90 percent is prorated into the banks' AIRAs. AIRA payments are made at the discretion of the Corporation's Board.

## Premiums

The Board reviews premium accrual rates as often as necessary but at least semiannually. The review focuses on five factors:

1. The level of the Insurance Fund relative to the secure base amount.

2. Projected losses to the Insurance Fund.
3. The condition of the System.
4. The health of the agricultural economy.
5. Risks in the financial environment.

Although the Corporation insures repayment to investors who purchase insured System debt, FCSIC is limited by law to collecting premiums based on the loans made by System banks and associations. Allowable premium rates vary by type of loan. (See Note 4 to the Corporation's financial statements.)

The most important factor in determining premium rates for 2007 was the level of the Insurance Fund relative to the secure base amount. Continued growth in insured debt outstanding has caused the Insurance Fund to trend further away from the SBA. As a result, the Board maintained the premium assessment at 15 basis points on accrual loans for 2007. By statute, this is the maximum rate that can be charged. The Corporation continued to assess 25 basis points on non-accrual loans. To help System institutions budget for 2008, the FCSIC Board notified the System in September 2007 that the 2008 premium assessment rate for accrual loans would remain at 15 basis points. The Board stated that rates for the other loan types, 25 basis points for nonaccrual loans and 0 basis points for Federal and State government-guaranteed loans, would remain the same as in 2007. The Board indicated that if Congress enacted legislation changing the Corporation's premium authorities, the Board would provide further guidance.

Type of Loan	Premium Range (in basis points)
Accrual	0 – 15
Nonaccrual	0 – 25
Federal Government-guaranteed accrual	0 – 1.5
State government-guaranteed accrual	0 – 3
Government-sponsored enterprise-guaranteed accrual	0 – 15

The following chart shows premium rates on accrual loans from 1998 to 2007. Over the 10-year period, premiums ranged from 0 basis points to 15 basis points, the maximum allowed, and averaged 6.47 basis points. The Board policy statement requires the Corporation to review premiums at least semi-annually and establishes the five factors to be considered.

Once the Insurance Fund attains the SBA, the law requires that premiums be reduced to the level necessary to maintain the Fund at the SBA (i.e., 2 percent of adjusted outstanding insured obligations.)

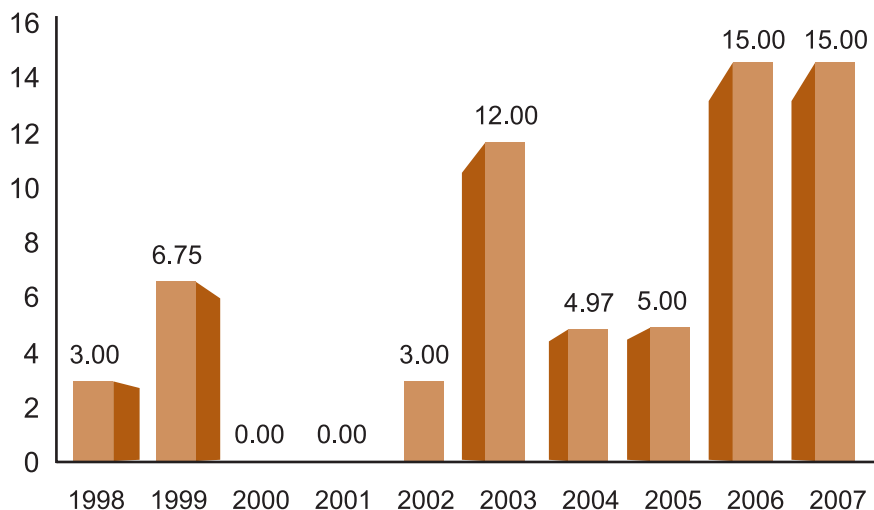
### Revenues and Expenses

Net income in 2007 increased 14.7 percent to \$287 million, up from \$250 million in 2006. The increase in net income resulted primarily from higher premiums. Interest income increased 11.4 percent in 2007 to \$98 million, up from \$88 million in 2006, primarily because of an increase in the investments held in the Corporation's portfolio.

The Corporation's operating costs as a percentage of its total assets represented 10 basis points for 2007. Fixed costs for staff, travel, rent, and miscellaneous expenses were \$1.9 million of the \$2.7 million total for the year. The remaining expenses of \$0.8 million were for contract services.

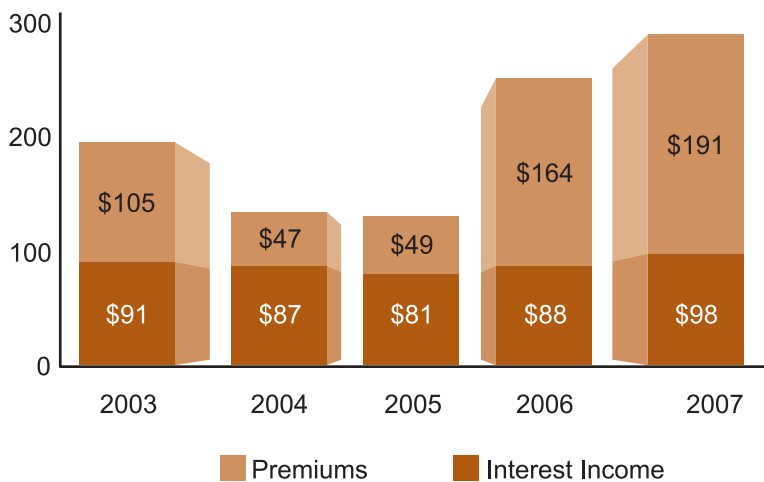
### Accrual Loan Premiums Averaged 6.47 Basis Points Over Past 10 Years

(1 Basis Point = 1/100 of 1 Percent)



### Corporation Revenues

(Dollars in millions)



## Investments

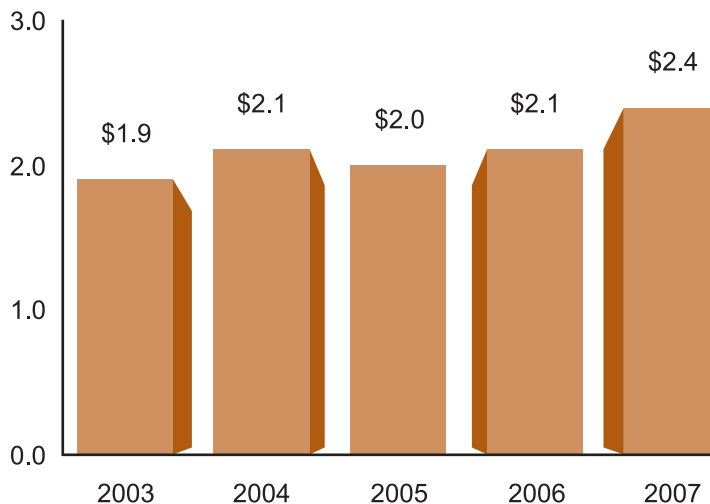
Investments increased 12 percent during the year from \$2.13 billion at December 31, 2006 to \$2.39 billion at year-end 2007.

The Corporation's investment objective is to maximize returns consistent with liquidity needs and to minimize exposure to loss of principal. Funds are invested in U.S. Treasury securities in accordance with the Act and the Corporation's Investment Policy.

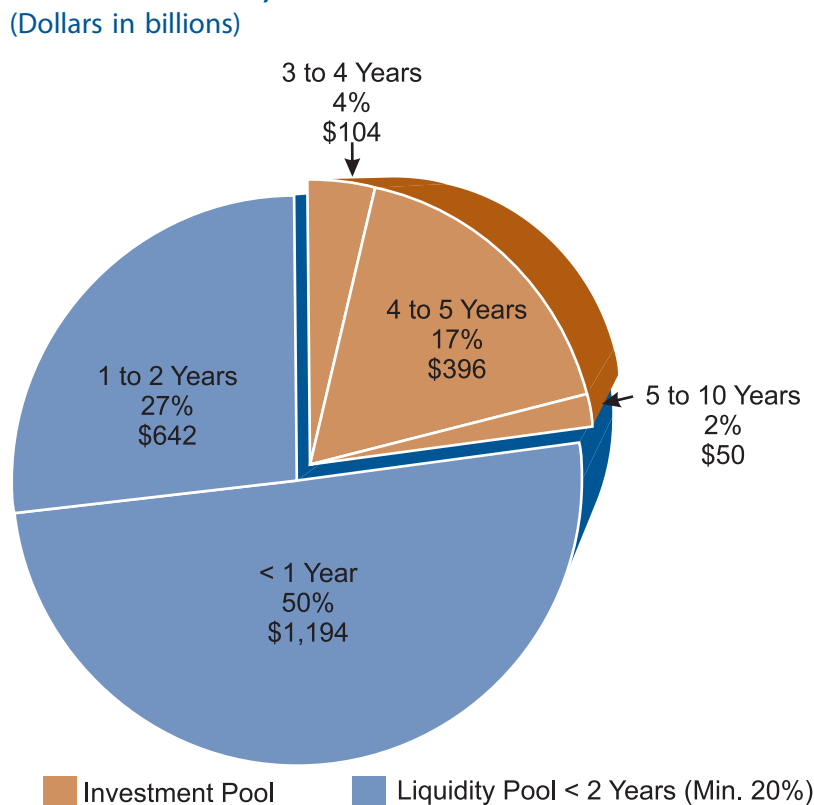
The average portfolio yield was 4.24 percent, up from 4.23 percent the prior year. The return on the Insurance Fund continued to outperform the benchmark index the Corporation uses to measure performance. This index is comprised of private sector mutual funds with holdings of similar type and duration to the Corporation's portfolio. The average return of the benchmark group was 4.16 percent for 2007.

Per the Corporation's Investment Policy, the portfolio is comprised of a liquidity and an investment pool. The liquidity pool consists of short-term securities maturing in less than two years. The investment pool is comprised of maturities that vary from two to ten years. At least 20 percent of the total investment portfolio shall be maintained in the liquidity pool, and a maximum of 25 percent of the investment pool may be invested with maturities between 5 and 10 years. The weighted average portfolio maturity at year-end was 1.61 years. The investment portfolio at December 31, 2007, is illustrated in the accompanying chart.

## Growth in Investment Portfolio (Dollars in billions)



## Investment Portfolio by Maturity at December 31, 2007 (Dollars in billions)



# Risk Management

The Corporation actively monitors and manages insurance risk. This program focuses on minimizing the Fund's exposure to potential losses through early detection of risk. Corporation staff regularly monitors key ratios and financial trends, and weaker System institutions undergo special examination procedures as needed.

The Corporation monitors trends in the System's growth, structure, and financial performance and condition through continual dialogue with FCA examiners and review of reports of examination. On a quarterly basis, the Corporation screens all System institutions using key performance criteria to identify institutions that may pose increasing insurance risk. The Corporation also assesses risk to the Insurance Fund in the following ways:

- Reviewing corporate actions approved by FCA for System institutions;
- Monitoring legislative, judicial, regulatory, and economic trends that could affect the agricultural or financial services industries;
- Using analytical models; and
- Participating as a nonvoting member on FCA's Regulatory Enforcement Committee.

During 2007, corporate staff consulted with FCA on the following requests by System institutions:

- Reduction in the required capital risk weight for a category of loans to cooperative power utilities;
- Regulatory clearance of offering circulars for several banks to issue perpetual preferred stock and subordinated debt, and the related treatment for regulatory capital;
- Proposed merger of several associations; and a
- Synthetic securitization by two associations.

FCSIC staff also participated in several interagency work groups examining System growth, investment authorities and capitalization requirements.

The Corporation continued to work with an insurance risk tool initially developed in 2004 by FCSIC's contractor, Mercer Oliver Wyman (now called Oliver Wyman), a management consulting firm. From its earlier work, the firm concluded that the most significant factors affecting the Corporation's insurance risk exposure were as follows:

1. System balance sheet growth;
2. The financial condition and performance of the System's insured banks and associations; and
3. Capital levels at the five insured System banks.



## Financial Assistance and Receivership

The Insurance Corporation is authorized to provide assistance to System institutions to prevent default, restore normal operations, or facilitate a merger or consolidation. At present, no assistance agreements are outstanding. Before financial assistance may be provided, the statute requires the Corporation to ensure that the proposed assistance is the least costly method for resolving a troubled institution. Financial assistance cannot be provided if the cost of liquidation is determined to be lower.

There are no active receiverships or conservatorships currently in the System. When appointed by FCA, the Corporation has the statutory responsibility to serve as receiver or conservator for System institutions. To fulfill this role and continue to operate with a small core staff, the Corporation uses contractors on an as-needed basis. These contractors provide knowledgeable and readily

available resources, while allowing the Corporation to contain costs during periods of limited or no activity. Corporation staff also maintains contact with the receivership staff of the Federal Deposit Insurance Corporation and the National Credit Union Administration to exchange information and stay abreast of best practices in receivership management.

During the year, staff continued work on a project to ensure FCSIC readiness to respond to a potential default at a bank or large association(s). This project will:

- Develop a staffing plan for potential receiverships;
- Identify funding strategies for various resolution options; and
- Review sources for specialized expertise.



# Strategic Goals and Performance Measures

Three broad goals with performance measures are used to evaluate the effectiveness of the Corporation's operations.

## 1. Manage the Insurance Fund to maintain the 2 percent secure base amount to protect investors.

The Corporation assesses the effectiveness of its performance by:

- Reviewing premium rates semiannually and making necessary adjustments; and
- Comparing the investment portfolio's average yield to peer investment funds with similar quality and maturity.

In 2007, the total Insurance Fund trended below the 2 percent SBA. Throughout the year, the total Insurance Fund ranged from 1.77 percent to 1.71 percent, and finished the year at 1.71 percent. Premium rates were reviewed three times and the rate on accrual loans was maintained at 15 basis points in 2007 due to high growth in insured debt. By statute, 15 basis points is the maximum that FCSIC can assess on accrual loans. The Corporation is pursuing a legislative proposal to amend the statutory framework for insurance premium assessment to make certain technical but important changes to the Farm Credit Act. The changes would enhance investor protection by increasing the amount FCSIC can collect to recapitalize the Fund. Key amendments would base premium assessments on outstanding insured debt obligations, instead of basing them on loans. The proposal would permit the FCSIC Board to impose premiums ranging from 0 to 20 basis points on insured debt obligations. FCSIC ensures timely payment of principal and interest on insured debt obligations, and this change would align its premiums with the risks it insures.

The investment return on the Corporation's portfolio (4.24 percent) exceeded the average return on the benchmark (4.16 percent) that is used to measure performance. The benchmark consists of private sector mutual funds that have the same characteristics as the Corporation's investment objectives. The Corporation, as part of its Strategic Plan, contracted with Evaluation Associates

(EA) to conduct an external review of its investment program. The firm reviewed FCSIC policies, procedures, internal controls, and investment performance. The review was completed in May 2007. EA concluded that, given the constraints of the program, FCSIC has performed well in managing its portfolio.

## 2. Detect, evaluate, and manage risks to the Insurance Fund to protect it from losses.

Program effectiveness is measured by:

- Evaluating how promptly emerging risks are detected;
- Determining the accuracy of the evaluation of risk; and
- Appraising the extent of loss minimization, if applicable.

The Corporation assesses the need for any insurance loss allowance quarterly. The financials of all System institutions are proactively screened to detect risk and identify institutions that may require special examinations. In addition, the Corporation continued its development of a model for dynamically evaluating the adequacy of the current Insurance Fund under various scenarios.

## 3. Maintain the capability to manage receiverships and/or conservatorships.

Receivership operations are considered effective if the following standards are met.

- Ninety percent of initial claims processed are completed within a specified period, depending on the size and complexity of the failed institution;
- The ratio of operating costs to total assets is comparable with that of other insurers; and
- The ratio of asset recovery values to asset values is comparable with that of other insurers.

No receiverships or conservatorships existed in the Farm Credit System in 2007.

Corporation personnel are trained periodically to maintain readiness, ensuring proficiency in the performance of receivership responsibilities. The next receivership readiness exercise is scheduled for 2008.

## The President's Management Agenda

The Corporation, one of 35 agencies designated as a significant Government entity for reporting purposes, is required to submit data for the Financial Report of the United States using the Government-wide Financial Report System and the Federal Agencies' Centralized Trial-Balance System.

In 2001, President Bush established a policy for improving the management and performance of the Federal Government. The President's Management Agenda focuses on five Government-wide goals to encourage improvements in specified areas of operations. The Corporation's accomplishments in those five areas are provided below:

### 1. Strategic Management of Human Capital

- Operated with a small core staff, contracting for specialized expertise when necessary, which kept operating costs low while offering flexibility to leverage resources.
- Continued to provide cross-training to ensure continuity of operations by empowering multiple staff members to fulfill a variety of critical roles in day-to-day operations.
- Participated in the 2007 Federal Human Capital Survey (FHCS), which satisfied the annual requirement established by the National Defense Authorization Act of 2004 and provided agency metrics within the human capital accountability system.
- Consistently scored higher than the Government-wide average on the 2007 FHCS in job satisfaction and leadership.

### 2. Competitive Sourcing

- Continued the extensive use of competitively sourced public and private sector contractor support to perform administrative functions, including personnel, information systems, and financial systems support.

### 3. Improved Financial Performance

- Managed an investment portfolio with an average yield that exceeded benchmarks.
- Kept actual operating expenses below budgeted operating expenses because of (1) unexpended contingency funds to deal with potential insurance issues, (2) the use of cost-effective shared services and (3) a staff vacancy during part of the year.

### 4. Expanded Electronic Government

- Continued to use the Corporation's Web site as the primary vehicle for providing information to our stakeholders, other Government entities, and the public.
- Sent all communications to the Farm Credit System electronically.

### 5. Budget and Performance Integration

- Continued to provide timely and accurate financial information to assist senior management and the Board in making decisions on strategic programs and key operations.
- Evaluated programs on an ongoing basis to determine efficiency, measuring results against Annual Performance and Strategic Plan objectives and reporting quarterly to the Board. Met new and growing demands without increasing permanent staff levels.
- Received an unqualified opinion on the Corporation's financial statements from our external auditor.
- The annual report on FCSIC's control over Reporting and Compliance did not disclose any internal control weaknesses or any instances of noncompliance.





# Reports of Independent Public Auditors





**PricewaterhouseCoopers LLP**  
1800 Tysons Boulevard  
McLean, VA 22102-4261  
Telephone (703) 918 3000  
Facsimile (703) 918 3100

### Report of Independent Auditors

To the Board of Directors  
Farm Credit System Insurance Corporation:

In our opinion, the accompanying statements of financial condition and the related statements of income and expenses and changes in insurance fund, and statements of cash flows present fairly, in all material respects, the financial position of Farm Credit System Insurance Corporation (the "Corporation") at December 31, 2007 and 2006, and the results of its operations and its cash flows for the years then ended, in conformity with accounting principles generally accepted in the United States of America. These financial statements are the responsibility of Corporation's management. Our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audits of these statements in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In accordance with *Government Auditing Standards*, we have also issued our report dated March 13, 2008 on our consideration of the Corporation's internal control over financial reporting and on our tests of its compliance with certain provisions of laws and regulations for the year ended December 31, 2007. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be considered in assessing the results of our audit.

*PricewaterhouseCoopers LLP*

March 13, 2008



**PricewaterhouseCoopers LLP**  
1800 Tysons Boulevard  
McLean VA 22102  
Telephone (703) 918 3000  
Facsimile (703) 918 3100

**Report of Independent Auditors on Internal Control over Financial Reporting and on Compliance and Other Matters Based on an Audit of Financial Statements Performed in Accordance with *Government Auditing Standards***

To the Board of Directors  
Farm Credit System Insurance Corporation:

We have audited the financial statements of Farm Credit System Insurance Corporation (the "Corporation") as of and for the year ended December 31, 2007, and have issued our report thereon dated March 13, 2008. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. The management of the Corporation is responsible for maintaining effective internal control over financial reporting and for compliance with laws and regulations.

**Internal Control Over Financial Reporting**

In planning and performing our audit, we considered the Corporation's internal control over financial reporting as a basis for designing our auditing procedures for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the Corporation's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of the Corporation's internal control over financial reporting.

A control deficiency exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect misstatements on a timely basis. A significant deficiency is a control deficiency, or combination of control deficiencies, that adversely affects the entity's ability to initiate, authorize, record, process, or report financial data reliably in accordance with generally accepted accounting principles such that there is more than a remote likelihood that a misstatement of the entity's financial statements that is more than inconsequential will not be prevented or detected by the entity's internal control.

A material weakness is a significant deficiency, or combination of significant deficiencies, that results in more than a remote likelihood that a material misstatement of the financial statements will not be prevented or detected by the entity's internal control.

Our consideration of internal control over financial reporting was for the limited purpose described in the first paragraph of this section and would not necessarily identify all deficiencies in internal control that might be significant deficiencies or material weaknesses. We did not identify any deficiencies in internal control over financial reporting that we consider to be material weaknesses, as defined above.

## Compliance and Other Matters

As part of obtaining reasonable assurance about whether the Corporation's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws and regulations, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit and, accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

This report is intended solely for the information and use of Corporation's Board of Directors and management, and is not intended to be and should not be used by anyone other than those specified parties.

*PricewaterhouseCoopers LLP*

March 13, 2008

**Farm Credit System Insurance Corporation**  
**Statements of Financial Condition**  
**For the years ended December 31, 2007 and 2006**  
**(Dollars in thousands)**

	2007	2006
<b>Assets</b>		
Cash and cash equivalents	\$ 479,926	\$ 700,839
Investments in U.S. Treasury Obligations (Note 3)	1,906,452	1,428,746
Accrued interest receivable	21,216	17,908
Premiums receivable (Note 4)	191,341	164,402
Total assets	<u>\$2,598,935</u>	<u>\$2,311,895</u>
<b>Liabilities and Insurance Fund</b>		
Accounts payable and accrued expenses (Note 6)	\$ 392	\$ 300
Total liabilities	<u>392</u>	<u>300</u>
Farm Credit Insurance Fund		
Allocated Insurance Reserve Accounts	39,888	39,888
Unallocated Insurance Fund Balance	2,558,655	2,271,707
Total Insurance Fund	<u>2,598,543</u>	<u>2,311,595</u>
Total liabilities and Insurance Fund	<u>\$2,598,935</u>	<u>\$2,311,89</u>

*The accompanying notes are an integral part of these financial statements.*

**Farm Credit System Insurance Corporation**  
**Statements of Income and Expenses and Changes in Insurance Fund**  
**For the years ended December 31, 2007 and 2006**  
**(Dollars in thousands)**

	2007	2006
<b>Income</b>		
Premiums (Note 4)	\$ 191,336	\$ 164,417
Interest income	98,352	87,927
Total income	<u>\$ 289,688</u>	<u>\$ 252,344</u>
<b>Expenses</b>		
Administrative operating expenses (Note 6)	<u>\$ 2,740</u>	<u>\$ 2,131</u>
Total expenses	<u>\$ 2,740</u>	<u>\$ 2,131</u>
Net income	<u>\$ 286,948</u>	<u>\$ 250,213</u>
Farm Credit Insurance Fund – beginning of year	<u>\$ 2,311,595</u>	<u>\$ 2,061,382</u>
Farm Credit Insurance Fund – end of year	<u>\$ 2,598,543</u>	<u>\$ 2,311,595</u>

*The accompanying notes are an integral part of these financial statements.*

**Farm Credit System Insurance Corporation**  
**Statements of Cash Flows**  
**For the years ended December 31, 2007 and 2006**  
**(Dollars in thousands)**

	2007	2006
<b>Cash flows from operating activities</b>		
Net income	\$ 286,948	\$ 250,213
Adjustments to reconcile net income to net cash provided by operating activities		
(Increase) in premium receivable	(26,939)	(114,909)
(Increase) decrease in accrued interest receivable	(3,307)	4,948
Net amortization and accretion of investments	7,779	12,956
Increase (decrease) in accounts payable and accrued expenses	92	(140)
Net cash provided by operating activities	<u>264,573</u>	<u>153,068</u>
<b>Cash flows from investing activities</b>		
Payments for purchase of U. S. Treasury Obligations	\$ (893,404)	\$ (99,204)
Proceeds from maturity of U.S. Treasury Obligations	407,918	373,089
Net cash (used) provided in investing activities	<u>(485,486)</u>	<u>273,885</u>
Net change in cash and cash equivalents	(220,913)	426,953
Cash and cash equivalents, beginning of year	<u>700,839</u>	<u>273,886</u>
Cash and cash equivalents, end of year	<u>\$ 479,926</u>	<u>\$ 700,839</u>

*The accompanying notes are an integral part of these financial statements.*

# Notes to the Financial Statements

## Note 1—Insurance Fund: Statutory Framework

The Agricultural Credit Act of 1987 (1987 Act) established the Farm Credit System Insurance Corporation (Corporation) for the purpose of ensuring the timely payment of principal and interest on notes, bonds, debentures, and other obligations issued under subsection (c) or (d) of section 4.2 of the Farm Credit Act of 1971, as amended (Act), (insured obligations). Each bank in the Farm Credit System (System) participating in insured obligations is an insured System bank. At December 31, 2007, there were five insured System banks and 95 direct lender associations.

The Corporation is managed by a board of directors consisting of the same individuals as the Farm Credit Administration (FCA) Board except that the Chairman of the FCA Board may not serve as the Chairman of the Corporation's Board of Directors.

The Corporation must spend the amounts necessary to:

1. Ensure the timely payment of interest and principal on insured obligations in the event of default by an insured System bank; and
2. Ensure the retirement of eligible borrower stock at par value under section 4.9A of the Act.

The Corporation, in its sole discretion, is authorized to expend amounts to provide financial assistance to certain insured institutions.

The balances outstanding at December 31, 2007, for each of the components of the Corporation's insurance responsibilities were \$155 billion of insured obligations, and \$11 million of eligible borrower stock.

If the Corporation does not have sufficient funds to ensure payment on insured obligations, System banks will be required to make payments under joint and several liability, as required by section 4.4 (a)(2) of the Act.

Under section 5.63 of the Act, the Corporation is exempt from all Federal, state, and local taxes with the exception of real property taxes.

## Note 2—Summary of Significant Accounting Policies

**Accounting Principles and Reporting Practices**—The accounting and reporting policies of the Corporation conform to accounting principles generally accepted in the United States of America (GAAP) and, as such, the financial statements have been prepared using the accrual basis of accounting. The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amount of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amount of revenues and expenses during the reporting period. Actual results could differ from those estimates.



**Cash and Cash Equivalents**—Cash and cash equivalents include investments in U.S. Treasury obligations with original maturities of 90 days or less. At December 31, 2007, the Corporation held \$479.70 million in overnight Treasury Certificates maturing on January 2, 2008, with an investment rate of 1.23 percent, and \$226,476 in cash.

**Investments in U.S. Treasury Obligations**—Section 5.62 of the Act requires that funds of the Corporation, not otherwise employed, shall be invested in obligations of the United States or in obligations guaranteed as to principal and interest by the United States. The Corporation has classified its investments as held to maturity in accordance with the Statement of Financial Accounting Standard (SFAS) No. 115 and carries them at amortized cost. Amortization of premium and accretion of discount on investments has been computed under the interest method since 2002. Fair value of investments is estimated based on quoted market prices for those or similar instruments.

**Liability for Estimated Insurance Obligations**—The liability for estimated insurance obligations is the present value of estimated probable insurance payments to be made in the future based on the Corporation's analysis of economic conditions of insured System banks.

The insured System banks' primary lending markets are borrowers engaged in farming, ranching, and the producing or harvesting of aquatic products, and their cooperatives. Financial weaknesses in these market segments and the effect of general market conditions on the System's borrowers could adversely affect the banks' financial condition and profitability. Insured System banks also face risks from changing interest rate environments and the need to maintain ongoing access to financial markets. Adverse changes in the financial condition and profitability of insured System banks resulting from increased levels of credit, financial, or other risks could occur in the future which would have a material effect on the liability for estimated insurance obligations.

The Corporation actively monitors the creditworthiness and financial position of the insured System banks. Management is not aware of any events or circumstances at this time which would require a liability for estimated insurance obligations to be recorded.

**Premiums**—Annual premiums are recorded as revenue during the period on which the premiums are based. All premiums are due on or before January 31 of the year subsequent to the year in which they are earned.

**Retirement Plan**—All permanent Corporation employees are covered by the Civil Service Retirement System (CSRS) or the Federal Employees Retirement System (FERS). The Corporation's contribution during 2007 to the CSRS plan was 8.5 percent of base pay. For those employees covered by FERS, the Corporation's contribution was 10.7 percent of base pay. In addition, for FERS-covered employees, the Corporation automatically contributes 1 percent of base pay to the employee's Thrift Savings Plan account, matches the first 3 percent contributed by the employee, and matches one-half of the next 2 percent contributed by the employee. Retirement plan expenses amounted to \$197,331 in 2007 and \$165,029 in 2006.

### Note 3—Investments

In addition to the amounts referenced in Note 2, Cash and Cash Equivalents, at December 31, 2007 and 2006, investments in U.S. Treasury obligations which are carried at amortized cost consisted of the following:

(Dollars in thousands)

	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Market Value
December 31, 2007				
U.S. Treasury Notes	\$ 1,906,452	\$ 18,842	\$ (589)	\$ 1,924,705
December 31, 2006				
U.S. Treasury Notes	\$ 1,428,746	\$ 610	\$(25,660)	\$ 1,403,696

The amortized cost and estimated market value of U.S. Treasury obligations at December 31, 2007, by contractual maturity, are shown below.

(Dollars in thousands)

	Amortized Cost	Estimated Market Value
Due in one year or less	\$ 714,153	\$ 714,516
Due after one year through five years	1,142,450	1,160,062
Due after five years through ten years	<u>49,849</u>	<u>50,127</u>
	<u>\$ 1,906,452</u>	<u>\$ 1,924,705</u>

Due to the inverted shape of the interest yield curve during 2007, the Corporation continued to pursue a strategy of investing a portion of maturing funds, as well as interest income and revenues, in overnight U.S. Treasury securities. The Corporation continues to actively monitor the interest rate environment and make adjustments as appropriate.

### Note 4—Premiums, the Secure Base Amount and Excess Insurance Fund Balances

Each System bank which issues insured obligations under subsection (c) or (d) of section 4.2 of the Act is an insured System bank and may be required to pay premiums to the Corporation.

The Act establishes the range of insurance premium rates that the Corporation's Board may assess for any calendar year based on five classes of an insured bank's loan assets. The asset classes and the range that may be assessed for each are: (1) annual average accrual loans outstanding (other than the guaranteed portions of Government-guaranteed accrual loans) for the year may be assessed from zero to 0.0015; (2) annual average nonaccrual loans outstanding may be assessed from zero to 0.0025; (3) annual average guaranteed portions of Federal Government-guaranteed accrual loans may be assessed from zero to 0.00015; (4) annual average guaranteed portions of state government-guaranteed accrual loans may be assessed from zero to 0.0003; and (5) annual average guaranteed portions of Government Sponsored Enterprise (GSE) guaranteed loans in accrual status may be assessed from zero to 0.0015.

The Act sets a base amount for the Insurance Fund to achieve. The statutory secure base amount is equivalent to 2.0 percent of the aggregate outstanding insured obligations of all insured System banks (adjusted downward by a percentage of the guaranteed portions of principal outstanding on government guaranteed loans in accrual status) or such other percentage as determined by the Corporation, in its sole discretion, to be actuarially sound. When the assets in the Insurance Fund for which no specific use has been designated exceed the secure base amount, the Corporation is required to reduce the premiums, but it still must ensure that reduced premiums are sufficient to maintain at the secure base amount the assets in the Insurance Fund for which no specific use has been designated (the unallocated Insurance Fund).

Insurance premium rates are reviewed semiannually. For 2007, the Board set premium rates at its January 11, 2007, meeting at 15 basis points for accrual loans, 25 basis points for nonaccrual loans and zero for Federal and state government-guaranteed loans, and did not exercise its discretionary authority to grant a lower rate for GSE-guaranteed loans. The Board again reviewed premiums at its June and September 2007 meetings. Due to continued high growth levels, the Board voted to maintain the premium rate on accrual loans at 15 basis points, the rates for nonaccrual loans at 25 basis points and for government-guaranteed loans, zero basis points. In 2007, outstanding insured obligations increased by \$20 billion or 14.9 percent. At December 31, 2007, the unallocated Insurance Fund was 1.682 percent as a percentage of adjusted insured debt. At December 31, 2007, the total Insurance Fund, including the Allocated Insurance Reserves Accounts (AIRAs) was 1.708 percent.

On January 10, 2008, the Board set premium rates for 2008, leaving unchanged the premium rate for accrual loans at 15 basis points, the maximum allowed by statute. The rates for nonaccrual loans remained at 25 basis points and for government-guaranteed loans, zero basis points. Again, the Board did not exercise its discretionary authority to grant a lower rate for GSE-guaranteed loans. The Corporation has requested changes to its statutory premium authorities. It remains uncertain whether these changes will be enacted, and if they are, the Corporation's Board of Directors will consider implementation of any changes at its June meeting, at the earliest.

A 1996 amendment to the Act requires the Corporation to establish Allocated Insurance Reserves Accounts (AIRAs) for each System bank and an account for the stockholders of the Farm Credit System Financial Assistance Corporation (FAC). If at the end of any calendar year the unallocated Insurance Fund is at the secure base amount, the Corporation is to segregate any excess balances into these AIRAs. In 1999, the Corporation's Board adopted the Policy Statement on the Secure Base Amount and Allocated Insurance Reserve Accounts which provides guidelines for implementing this statutory authority. If at the end of any calendar year the amount in the unallocated Insurance Fund exceeds the 2 percent secure base target, the statute requires the Corporation to recalculate the secure base amount on an average daily balance basis and compare that amount with the year-end Insurance Fund balance adjusted downward by the Corporation's estimated expenses for the following year. At year-end 2003, this resulted in the transfer of \$39.89 million to the AIRAs. The amount was allocated as follows:

FAC Stockholders	(10%)	\$ 3.99 million
Farm Credit System Banks	(90%)	\$ 35.90 million

The AIRA balances are recorded as part of the Insurance Fund until approved for payment by the Corporation's Board. The statute provided that amounts in the AIRAs could not be paid prior to April 2006 (eight years after the Insurance Fund first attained the secure base amount). The Corporation's Board of Directors has discretion to adopt a later payment cycle. AIRA balances may be used to absorb any insurance losses and claims.

Furthermore, the Board of Directors has discretion to limit or restrict the AIRA payments. In accordance with the Corporation's policy statement, any AIRA balances do not count in measuring the Insurance Fund's compliance with the secure base amount. No AIRA payments were made during 2007 or 2006.

#### **Note 5—Operating Lease**

On October 21, 2003, the Corporation executed a six-year lease with the Farm Credit System Building Association for office space. The terms of the lease provide for an annual minimum base rent for office space for the remaining term of \$123,262 for 2008 and \$124,344 for 2009. The Corporation recorded lease expense (including operating cost assessments) of \$125,695 and \$139,007 for 2007 and 2006, respectively.

#### **Note 6—Related Parties**

The Corporation purchases services from the FCA under an Interagency Agreement. These include examination and administrative support services. The intention of the parties as stated in the agreement is that specified rates and fees will reimburse the party providing services for all reasonable costs associated with provision of the services. The Corporation had payables due to the FCA of \$155,555 at December 31, 2007 and \$17,530 at December 31, 2006. The Corporation purchased services for 2007 which totaled \$377,187 compared with \$64,938 for 2006.

The Corporation provides assistance to the FCA under the same Interagency Agreement, recognizing revenue of zero for 2007 and 2006. At December 31, 2007, and 2006, the Corporation did not have any receivables from the FCA.

# Income and Expenses

## Farm Credit System Insurance Corporation By Year (Dollars in thousands)

	Income		Expenses		Net Income
	Premiums	Investment	Provision for Insurance Obligations	Administrative and Operating Expenses	Changes in Insurance Fund
1990	\$ 72,000	\$ 25,705	\$ 140,000	\$ 243	(\$ 42,538)
1991	\$ 77,463	\$ 31,483	\$ 15,555	\$ 953	\$ 92,438
1992	\$ 73,902	\$ 37,198	\$ 12,062	\$ 1,200	\$ 97,838
1993	\$ 74,100	\$ 41,277	(\$ 39,444) <sup>1</sup>	\$ 1,278	\$ 153,543
1994	\$ 76,526	\$ 46,389	\$ 8,890	\$ 1,482	\$ 112,543
1995	\$ 79,394	\$ 54,688	(\$ 14,329) <sup>2</sup>	\$ 1,379	\$ 147,032
1996	\$ 85,736	\$ 61,471	\$ 8,509	\$ 1,469	\$ 137,229
1997	\$ 71,242	\$ 71,088	\$ 9,105	\$ 1,511	\$ 131,714
1998	\$ 19,972	\$ 79,545	\$ 9,743	\$ 1,525	\$ 88,249
1999	\$ 45,496	\$ 81,719	\$ 10,424	\$ 1,631	\$ 115,203
2000	\$ 1,040	\$ 92,776	\$ 11,154	\$ 1,797	\$ 80,878
2001	\$ 0	\$ 94,112	\$ 11,935	\$ 2,127	\$ 80,051
2002	\$ 26,355	\$ 93,499	\$ 13,643	\$ 1,906	\$ 107,545 <sup>3</sup>
2003	\$ 105,079	\$ 91,405	\$ 13,725	\$ 2,218	\$ 180,561
2004	\$ 46,520	\$ 86,567	\$ 14,686	\$ 2,263	\$ 116,138
2005	\$ 49,393	\$ 81,253	\$ 6,228	\$ 2,202	\$ 122,236
2006	\$ 164,417	\$ 87,927	\$ 0	\$ 2,131	\$ 250,213
2007	\$ 191,336	\$ 98,352	\$ 0	\$ 2,740	\$ 286,948

1. In 1993, the FAC Trust Fund was initially considered available to pay a portion of the Insurance Corporation's FAC obligation for assistance to the FLB of Jackson.
2. In 1995, this provision was adjusted to reflect a change in the FAC Trust Fund's investment strategy and the termination of the FLB Jackson receivership making available additional funds to reduce the Insurance Corporation's related FAC obligation.
3. In 2002, the Corporation changed its method of amortizing investment premiums and discounts from the straight line to the interest method. The cumulative effect on prior years of \$3.2 million was included in 2002 net income.

# Corporate Staff



<b>Dorothy L. Nichols</b>	<b>Chief Operating Officer</b>
<b>Alan J. Glenn</b>	<b>Director of Risk Management</b>
<b>C. Richard Pfitzinger</b>	<b>Chief Financial Officer</b>
<b>James M. Morris</b>	<b>General Counsel</b>
<b>Phyllis Applebaum</b>	<b>Financial Analyst</b>
<b>William Fayer</b>	<b>Financial Analyst/Asset Assurance Manager</b>
<b>Pam Ngorskul</b>	<b>Accountant</b>
<b>Anna Lacey</b>	<b>Administrative Specialist</b>
<b>Molly Sproles</b>	<b>Administrative Management Assistant</b>

---

## Contact Information

---

Copies of Farm Credit System Annual Reports to Investors and Quarterly and Annual Information Statements may be obtained from:

Federal Farm Credit Banks Funding Corporation  
 10 Exchange Place  
 Suite 1401  
 Jersey City, NJ 07302  
 (201) 200-8000

Copies of the Annual Performance and Accountability Reports of the Farm Credit Administration and the FCA's Annual Report on the Farm Credit System may be obtained from:

Office of Congressional and Public Affairs  
 Farm Credit Administration  
 1501 Farm Credit Drive  
 McLean, VA 22102  
 (703) 883-4056

Farm Credit System Insurance Corporation  
1501 Farm Credit Drive  
McLean, VA 22102

703-883-4380 Voice  
703-790-9088 Fax  
[www.fcsic.gov](http://www.fcsic.gov)

