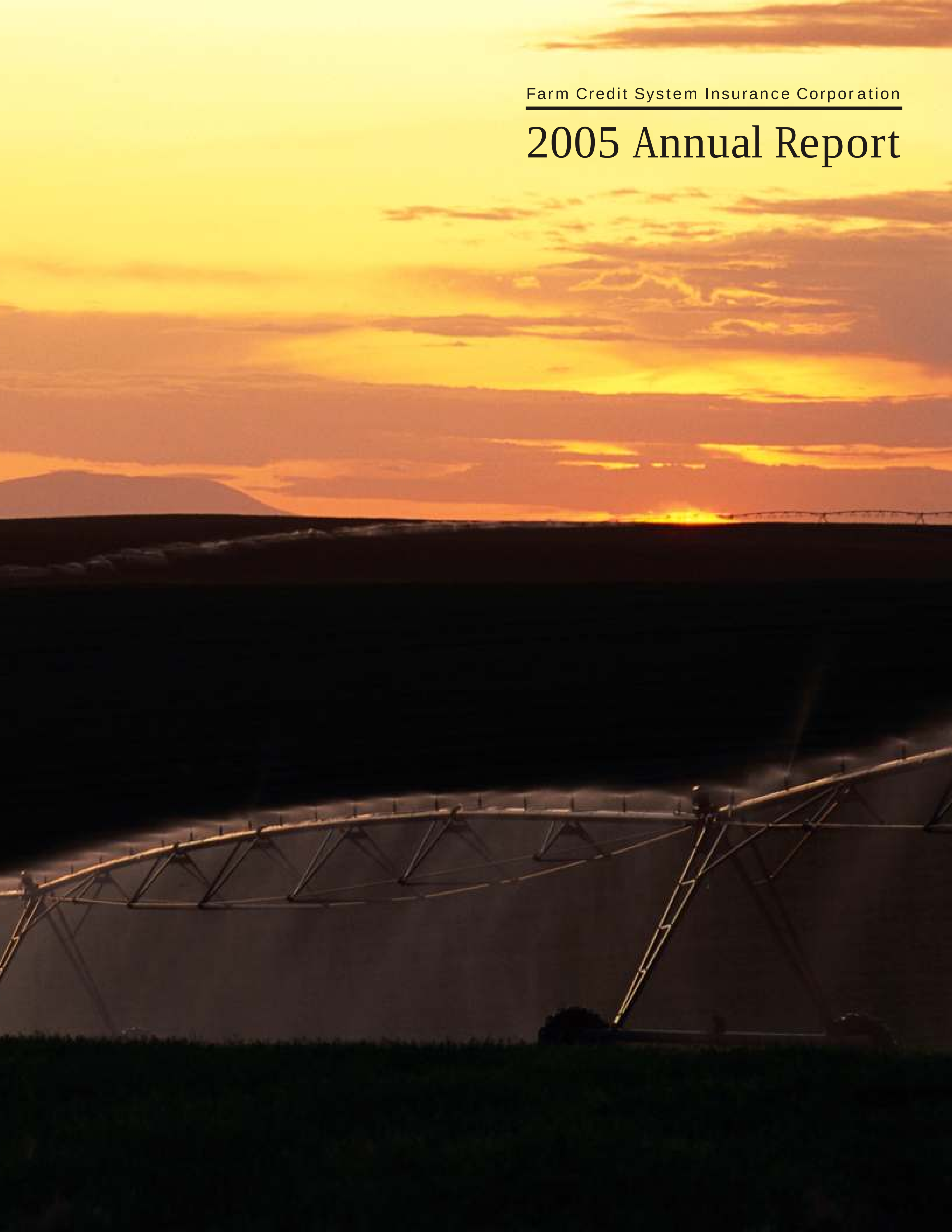
Farm Credit System Insurance Corporation

2005 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

Protecting Investors in Agriculture and Rural America

April 17, 2006

Gentlemen:

In accordance with the provisions of section 5.64(a) 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 2005.

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 Farm Credit System debt securities. The balance in the Insurance Fund at December 31, 2005, was $2.06 billion. The Corporation collected $49 million in insurance premiums from Farm Credit System banks for 2005, and expects to incur $2.6 million in operating costs in 2006.

Sincerely,

Douglas L. "Doug" Flory
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 . . .

. . . is managed by a three-member board of directors composed of the members of the Farm Credit Administration (FCA) Board. The FCA is the independent Federal agency responsible for the regulation and examination of the Farm Credit System, a nationwide financial cooperative that lends to agriculture and rural America. The Chairman of the Corporation's Board of Directors must be an FCA Board Member other than the Chairman of the FCA Board.

Douglas L. “Doug” Flory

Douglas L. “Doug” Flory, Chairman of FCSIC, was appointed to the three-member FCA Board by President Bush on August 1, 2002, for a term that expires October 13, 2006. He was elected Chairman on December 4, 2002.

Mr. Flory brings to his position extensive experience in production agriculture, agribusiness, and both commercial bank and Farm Credit lending. His farming operation includes being half-owner of S & F, L.L.C., a general livestock, grain, poultry, and hay farm in Augusta County, Virginia. Prior to his appointment to the FCA Board, Mr. Flory was a member of the board of directors of AgFirst Farm Credit Bank in Columbia, South Carolina, and a director of Farm Credit of the Virginias, ACA.

Mr. Flory was executive vice president of Dominion Bank from 1971 to 1988, and president, CEO, and director of Dominion Farm Loan Corporation. He chaired the Virginia Bankers Association Committee on Agriculture and was a member of the Executive Committee of the American Bankers Association’s agricultural division. From 1989 to 1992, he was executive vice president, chief operating officer, and a member of the board of WLR Foods, Inc., a publicly traded poultry food company.

Mr. Flory also served on several governing boards for the State of Virginia, including the Virginia Agricultural Council, a state advisory board, and the Virginia Agriculture Credit Committee, which he chaired. He also served as chairman of the Virginia Agricultural Development Authority, which uses “aggie bonds” to finance Virginia farmers.

Throughout his career, Mr. Flory has been an active participant in agricultural industry associations. He was president of the Virginia Turkey Association and president and director of the Rockingham County Fair Association. He also served as a director of the Virginia Poultry Federation, the Virginia Agribusiness Council, the Virginia Beef Cattle Association, and the Virginia Sheep Association.

A native of Augusta County, Virginia, Mr. Flory attended Bridgewater College in Bridgewater, Virginia, and earned a bachelor’s degree from Virginia Polytechnic Institute and State University in Blacksburg. He did graduate work at James Madison University and is a graduate of the Maryland-Virginia School of Bank Management at the University of Virginia. He and his wife, Avery, are the parents of two daughters and a son.

Nancy C. Pellett

Nancy C. Pellett was appointed to the FCA and FCSIC Boards by President George W. Bush on November 14, 2002, for a term that expires May 21, 2008. Ms. Pellett brings extensive experience in production agriculture and agribusiness to her position on the Board. For 23 years she was vice president and secretary of Prairie Hills, Ltd., a feedlot, cow-calf, and row crop operation in Atlantic, Iowa. She was president and treasurer of Fredrechsen Farms, Ltd., a family-owned swine and row crop operation in Walnut, Iowa, for more than 20 years.

A long-time leader in the beef industry, Ms. Pellett has held state and national leadership positions in a range of cattlemen's industry organizations. As a member of the National Cattlemen's Beef Association, she served as the Chairman of the Check-Off Division, Chairman of the Consumer Marketing Group, and most recently as a member of the Cattlemen's Beef Board. She also served as President of the Iowa Beef Industry Council. Ms. Pellett was a partner in Premium Quality Foods, Inc., based in Red Oak, Iowa, which markets branded fresh beef and precooked beef entrees. She served as president and director of consumer marketing 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 currently 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.

Ms. Pellett's dedication to the future of agriculture is reflected in her personal involvement with 4-H and Future Farmers of America at the local and state levels. She has served on the Iowa 4-H Foundation Board and is a founding member of the 4-H/FFA "Sale of Champions" Committee for the Iowa State Fair.

A native of Walnut, Iowa, Ms. Pellett holds a B.S. from ISU at Ames. She is also past President of the ISU Alumni Association, and was awarded the Alumni Medal in 1987. The Pellett family was honored as "Family of the Year" by the University in 1997. The family also received the "Friends of Youth Award" in 2000 from the Knights of AkSarBen, a foundation supporting education, youth programs, and rural development in Nebraska and western Iowa. She and her husband have four children. Together with a son and daughter-in-law, Ms. Pellet and her husband operate a fifth generation family farm in Atlantic, Iowa.

Dallas P. Tonsager

Dallas P. Tonsager was appointed to the FCA and FCSIC Boards by President Bush on December 1, 2004, for a term that expires May 21, 2010. Mr. Tonsager brings extensive experience as an agricultural leader and producer to his position on the FCSIC Board, as well as a commitment to promoting and implementing innovative development strategies to benefit rural residents and their communities.

In partnership with his brother, he owns Plainview Farm in Oldham, South Dakota, a family farming operation that includes corn, soybeans, wheat, and hay. Mr. Tonsager served as Executive Director of the South Dakota Value-Added Agriculture Development Center in Huron from 2002 until his appointment to the FCA Board, where 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, Mr. Tonsager was selected by President Clinton to serve as the South Dakota State Director for Rural Development for the U.S. Department of Agriculture. The Federal agency promotes rural economic development, and helps individuals, communities, and businesses obtain financial and technical assistance for a variety of needs. 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 the 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.

Raised on a dairy farm in South Dakota, Mr. Tonsager is a graduate of South Dakota State University where he earned a B.S. in agriculture in 1976. 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 the Lutheran Social Services of South Dakota. He and his wife, Sharon, have two sons and a daughter-in-law.

2005 Highlights

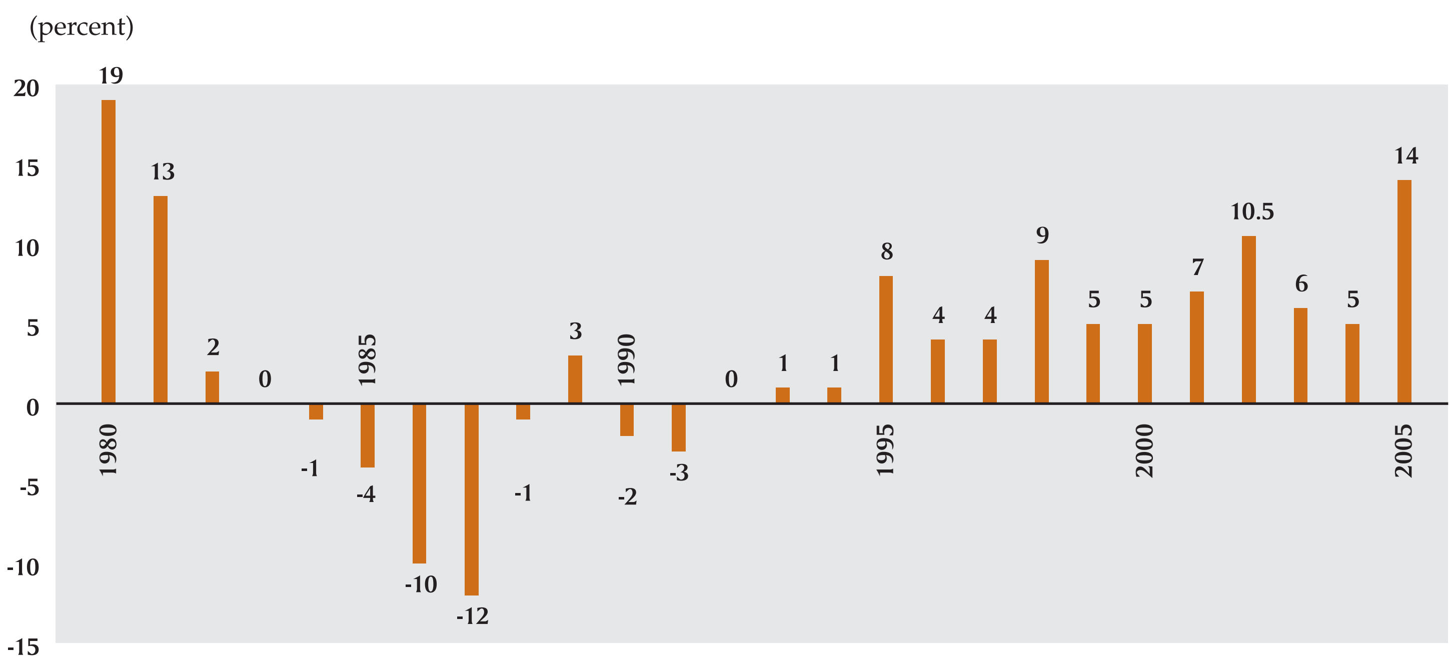
Significant events in 2005 featured substantial growth in insured debt outstanding and the payoff of the remaining Financial Assistance Corporation (FAC) bond. (For additional information, please see Note 5 to the Financial Statements.)

Insured debt outstanding[1] increased 14.3 percent during 2005 to $114.2 billion, the highest annual rate of growth in 24 years. This was only the second year—the other being 2002 when insured debt outstanding grew 10.5 percent—that the annual rate of growth reached double digits during that period.

On June 10, 2005, the Farm Credit System Insurance Corporation (the Corporation) paid $231 million towards the retirement of the final FAC bond, representing the Corporation's remaining share of its outstanding obligation. The Agricultural Credit Act of 1987 required the Corporation to provide any funds necessary to retire this publicly held bond, a $325 million issue, which matured in June 2005.

Mary Creedon Connelly, the Corporation's Chief Operating Officer since 1991, retired after 33 years of Federal Government service. During her tenure, the Corporation developed strong risk management capabilities, implemented a process for establishing loss reserves, developed a model for evaluating the adequacy of the Insurance Fund, and obtained increased premium flexibility. In addition, the Farm Credit Insurance Fund crossed the $2 billion mark for the first time. Ms. Connelly set up an Investment Committee to actively invest the assets in the Insurance Fund. Dorothy Nichols, previously the Corporation's General Counsel, succeeded Ms. Connelly as the Chief Operating Officer effective February 19, 2006. Ms. Nichols has been with the Corporation since 1995 and has more than 20 years of bank regulatory and insurance experience.

Growth in Farm Credit System Debt 1980–2005



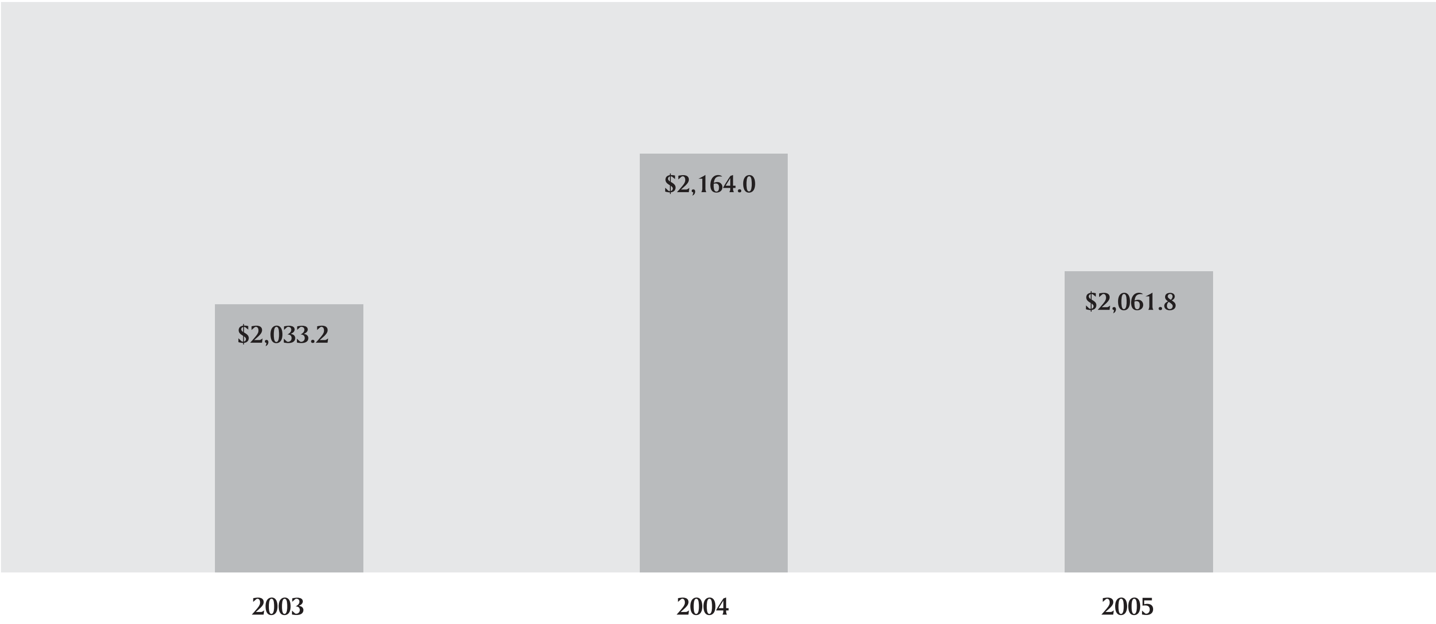
1. Systemwide bonds, medium-term notes, and Systemwide notes at par that have been issued in accordance with the Farm Credit Act of 1971 and regulations and are outstanding as of the report date and includes the amount of accrued interest payable.

Selected Financial Statistics

($ in millions)	2005	2004	2003
BALANCE SHEET:			
Total Assets	$2,061.8	$ 2,164.0	$2,033.2
Total Liabilities	0.4	224.5	210.2
Insurance Fund Balance			
Allocated Insurance Reserve Accounts	39.9	39.9	39.9
Unallocated Portion of the Insurance Fund	2,021.5	1,899.3	1,783.1
OPERATIONS:			
Revenues	130.6	133.1	196.5
Administrative Operating Expenses	2.2	2.3	2.2
Insurance Obligation Expense	6.2	14.7	13.7
Net Income	122.2	116.1	180.6

Total Assets

($ in millions)



The Farm Credit System

FCS

Structure and Funding

The System is owned by the rural customers it serves including farmers, ranchers, and other agricultural producers. Ninety-six Farm Credit System associations lend directly to these borrowers/owners and provide a consistent source of agricultural and rural credit throughout the United States and the Commonwealth of Puerto Rico. Five Farm Credit System banks provide funding to the 96 associations within their chartered territories. The banks receive their funding through the issuance of Federal Farm Credit Banks Consolidated 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 the repayment of investors who purchase the bonds and notes issued by the System's banks. Investors provide the funds the System lends to agriculture and rural America.

Regulatory Oversight

The Farm Credit Administration (FCA) is the safety and soundness regulator responsible for the examination, supervision, and regulation of each Farm Credit System institution. The FCA is an independent agency in the executive branch of the United States Government. The FCA derives its broad authorities from the Act; these 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 the Corporation, the FCA, and the System.

Selected financial statistics for the Farm Credit System on a combined basis are presented on the following page.

Combined Farm Credit System Statistics

($ in billions)	2005	2004	2003
Insured Debt Outstanding	$114.2	$100.0	$94.6
Production Agriculture:			
Real Estate Mortgage Loans	52.7	48.7	46.5
Production and Intermediate-term Loans	23.9	21.8	21.1
Agribusiness Loans[1]	14.7	12.1	12.1
Communication Loans	2.6	2.4	2.6
Energy and Water/Waste Disposal Loans	5.5	4.8	3.9
Rural Residential Real Estate Loans	3.0	2.5	2.3
International Loans	2.3	2.6	2.8
Lease Receivables	1.3	1.2	1.3
Loans to Other Financial Institutions	0.4	0.4	0.3
Cash and Investments	28.4	24.2	21.3
Net Income	2.10	2.99[2]	1.83
Nonperforming Loans as a Percentage of Total Loans	0.56%	0.77%	1.28%

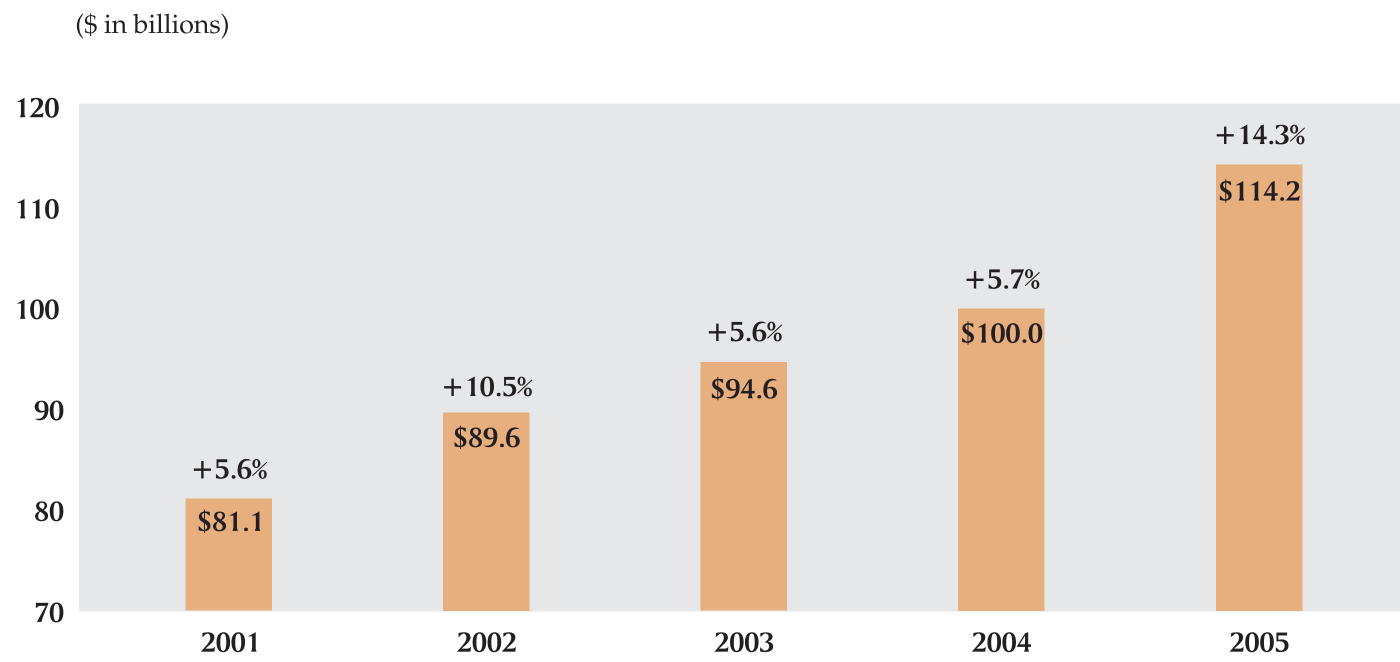
1. At December 31, 2005, agribusiness loans consisted of loans to cooperatives of $8.8 billion; processing and marketing loans of $4.1 billion; and farm-related business loans of $1.8 billion.
2. Includes a one-time reversal of the allowance for loan losses of $1.167 billion, net of a related $95 million deferred tax expense. Excluding this amount, net income would have been $1.826 billion for 2004.

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 debt outstanding increased by just over 14 percent to $114.2 billion. For the five-year period, from 2001 through 2005, insured debt outstanding grew at an average annual rate of approximately 8.3 percent.

Other obligations included the remaining FAC bonds and eligible borrower stock. From 1988 to 1990, the FAC issued $1.261 billion in debt. The proceeds from this debt were used to provide financial assistance to the Farm Credit System, among other things. The Corporation by law must use the Insurance Fund to satisfy any FAC-issued bond to the extent monies in the FAC Trust Fund were insufficient. On June 10, 2005, the Corporation provided $231 million, representing the Corpor-

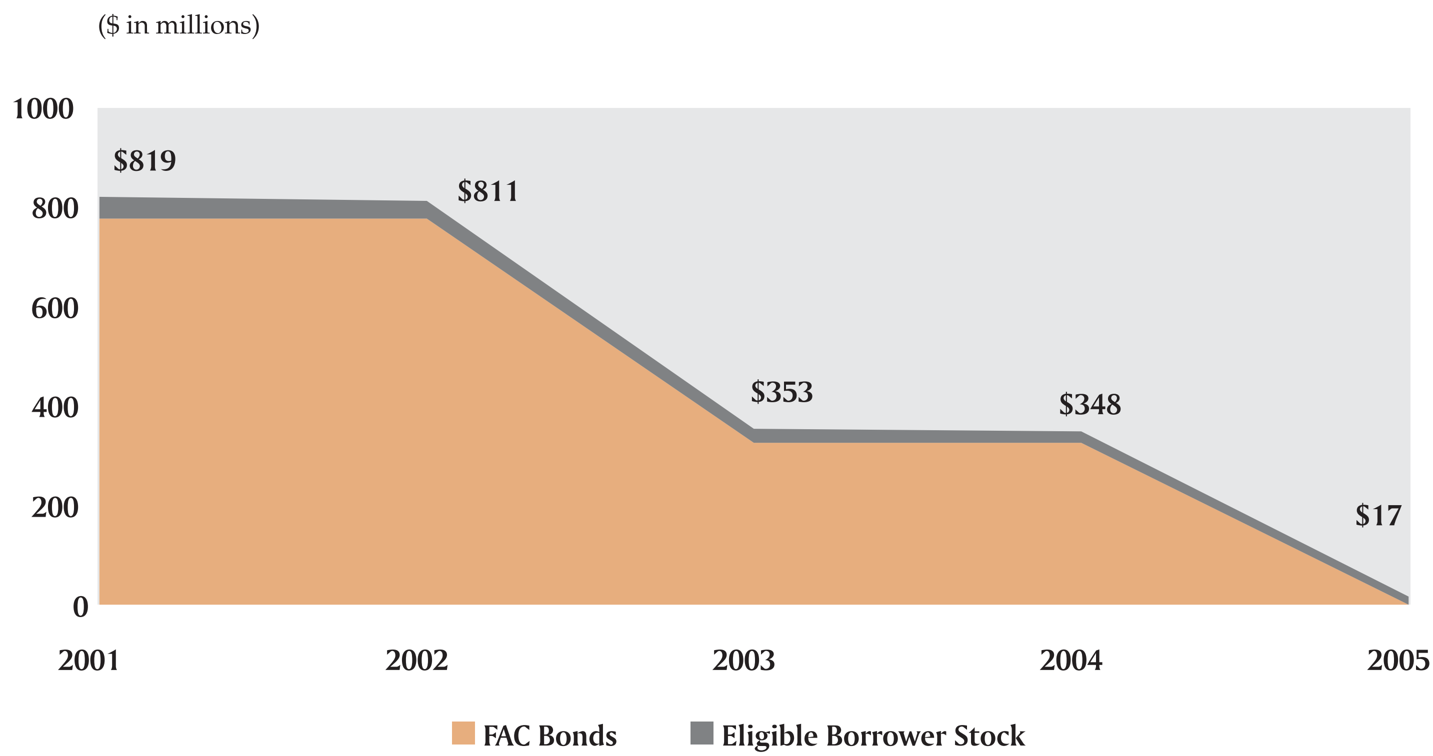
Growth in Insured Debt Outstanding Averaged 8.3% Over the Past 5 Years



ation's remaining share of its outstanding obligations to repay the $325 million issue of FAC bonds outstanding. The remaining $94 million was paid by the FAC Trust Fund and the FAC Assistance Fund, which provided $80 million and $14 million, respectively. (See Note 5 to the financial statements.)

The Corporation is also required by statute to ensure the retirement of eligible System borrower stock at par value. This stock, also known as protected borrower stock, was outstanding prior to October 6, 1988. At yearend, eligible borrower stock outstanding at System institutions totaled $17 million, down from $23 million at yearend 2004.

Other Obligations

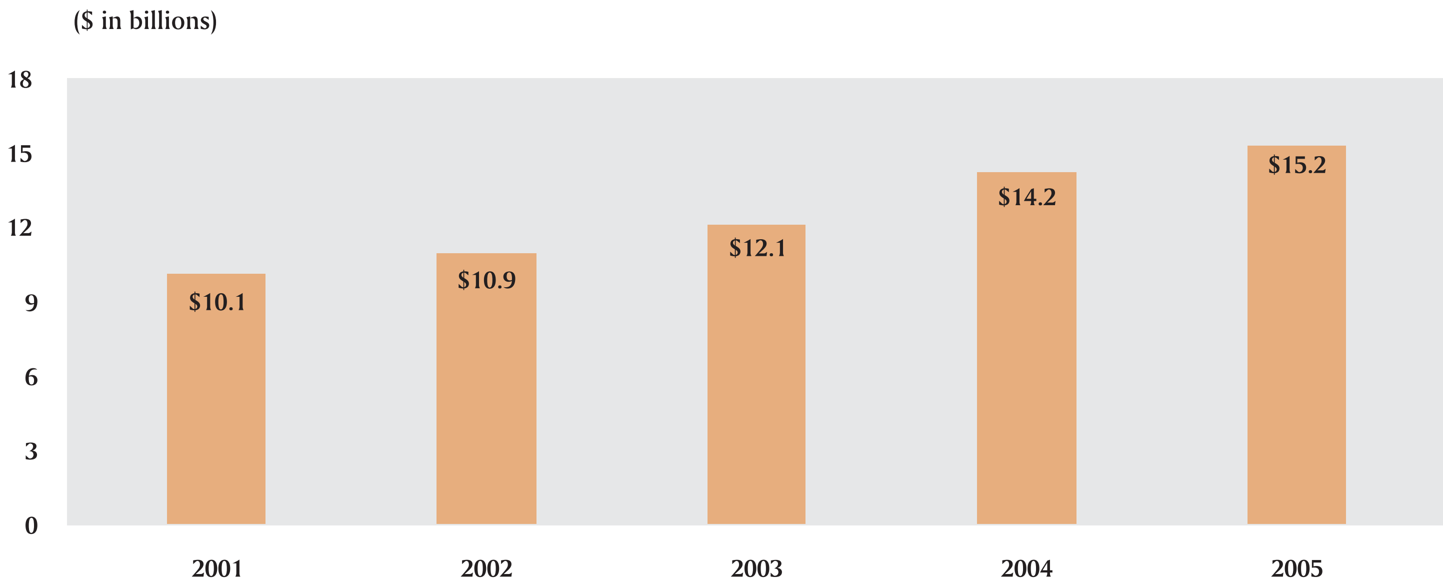


Farm Credit System Capital

At yearend 2005, there was $114.2 billion in insured debt outstanding, and the Corporation had $2.06 billion in assets, and an unallocated portion of the Insurance Fund balance of $2.02 billion. Over the past five years, the Farm Credit System associations have been building capital through net income earned and retained at the associations. The increase in capital at the associations reduces the credit exposure the insured banks have on loans to each of their affiliated associations.

Since 2001 combined association capital has increased 51 percent from $10.1 billion to $15.2 billion at yearend 2005.

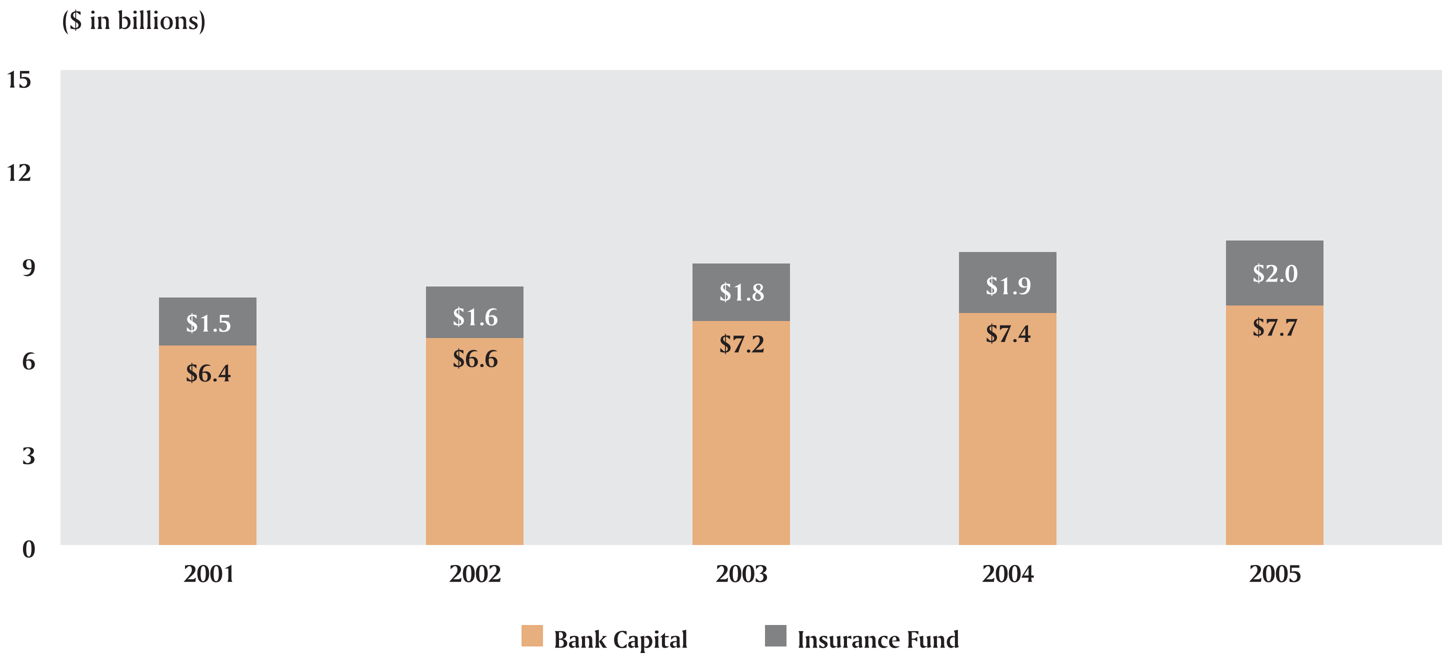
Association Capital



Since 2001, combined bank capital plus the Insurance Fund has increased 23 percent from $7.9 billion to $9.7 billion at yearend 2005.

The primary source of funds to repay Systemwide Debt Securities is the System's borrowers, with each borrower required to have certain minimum levels of net worth and, in most cases, collateral posted in connection with loans made to the borrower. These borrowers make payments on their loans to the lending bank or association. Lending associations in turn make payments on their wholesale loans from their affiliated bank. Both the banks, which ultimately repay Systemwide Debt Securities, and the associations have substantial amounts of capital as protection and sources of support for the repayment of the outstanding debt. If a bank participating in an issue of Systemwide Debt Securities were unable to repay its portion of that security, the Insurance Fund would be required to 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.

Bank Capital Plus the Insurance Fund



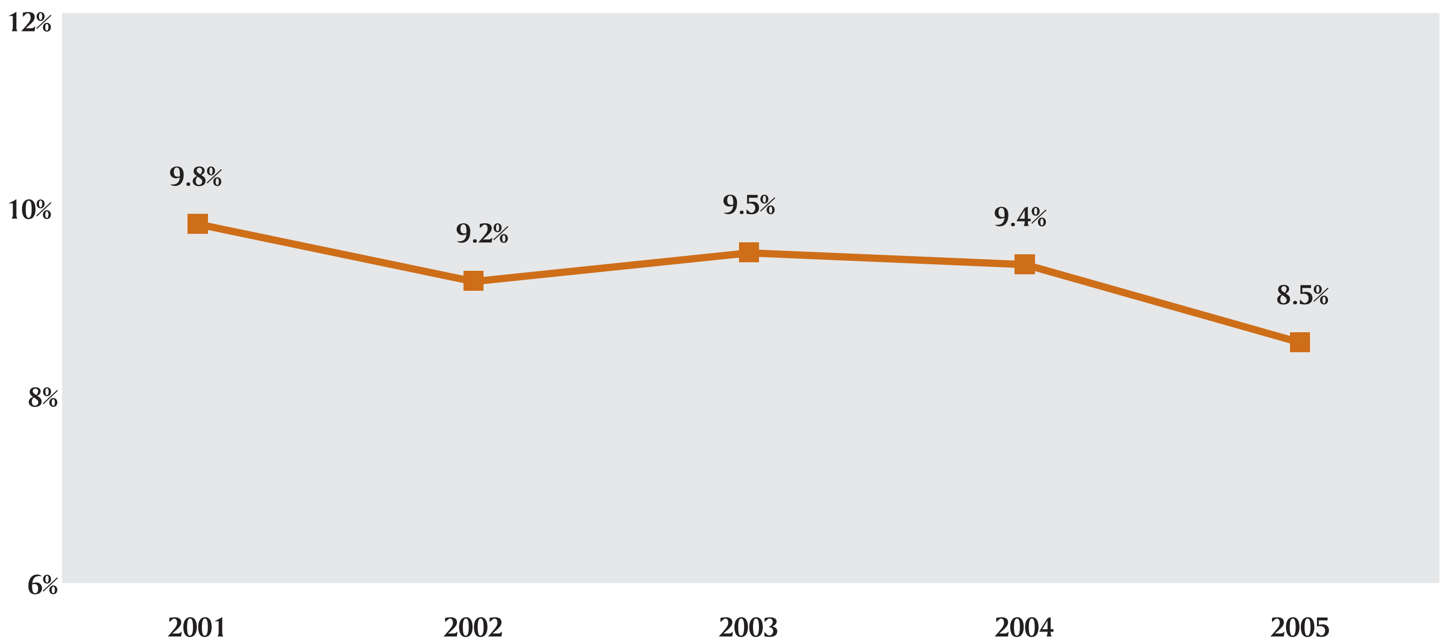
As a percentage of outstanding debt, bank capital plus the Insurance Fund decreased from 9.8 percent in 2001 to 8.5 percent in 2005. This decline is due to the rate of growth in outstanding debt outpacing growth in bank capital and the Insurance Fund.

Additional Elements of Strength

The System has additional risk management tools that protect investors. The banks have entered into the Contractual Interbank Performance Agreement (CIPA). This agreement measures the financial condition and performance of each System bank using various ratios considering capital, asset quality, earnings, interest-rate risk, and liquidity. CIPA contains economic incentives whereby financial penalties are applied if the performance standard is not met.

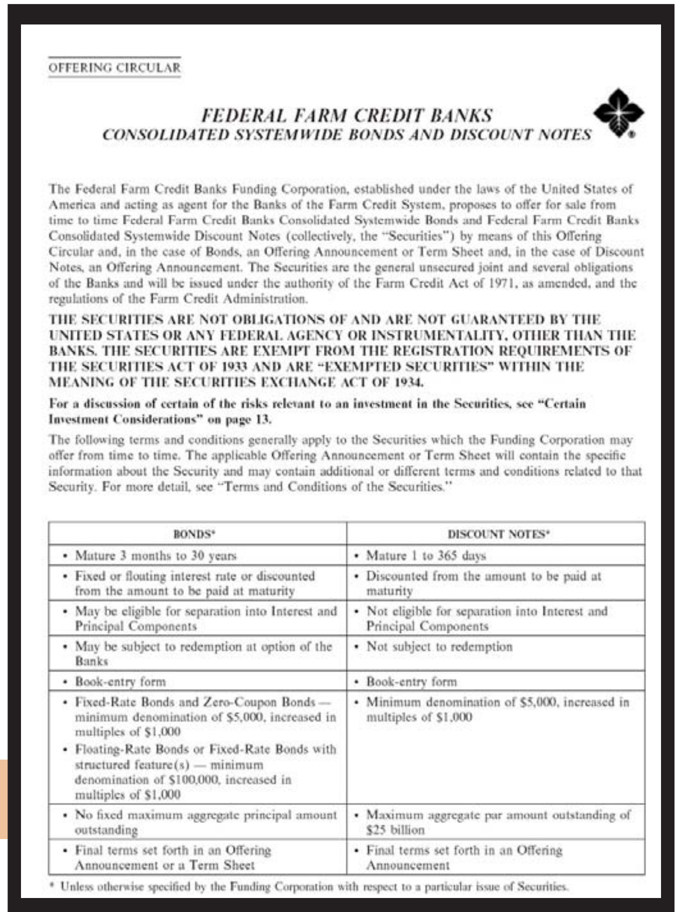
The banks and the Funding Corporation have also entered into a Market Access Agreement (MAA) that establishes conditions for each bank's continued participation in the debt market. If a bank fails to meet agreed upon performance measures, including capital and collateral ratios, their participation in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

Bank Capital Plus the Insurance Fund As a Percentage of Insured Debt



The System also has in place a Common Minimum Liquidity Standard. The standard requires each bank to maintain a minimum of 90 days of liquidity on a continuous basis, assuming no access to the capital markets. All banks have exceeded this liquidity standard since June 30, 2003.

These measures, in conjunction with bank capital and the Insurance Fund, provide protection for investors who purchase Systemwide bonds and notes.



OFFERING CIRCULAR

FEDERAL FARM CREDIT BANKS

CONSOLIDATED SYSTEMWIDE BONDS AND DISCOUNT NOTES

The Federal Farm Credit Banks Funding Corporation, established under the laws of the United States of America and acting as agent for the Banks of the Farm Credit System, proposes to offer for sale from time to time Federal Farm Credit Banks Consolidated Systemwide Bonds and Federal Farm Credit Banks Consolidated Systemwide Discount Notes (collectively, the "Securities") by means of this Offering Circular and, in the case of Bonds, an Offering Announcement or Term Sheet and, in the case of Discount Notes, an Offering Announcement. The Securities are the general unsecured joint and several obligations of the Banks and will be issued under the authority of the Farm Credit Act of 1971, as amended, and the regulations of the Farm Credit Administration.

THE SECURITIES ARE NOT OBLIGATIONS OF AND ARE NOT GUARANTEED BY THE UNITED STATES OR ANY FEDERAL AGENCY OR INSTRUMENTALITY, OTHER THAN THE BANKS. THE SECURITIES ARE EXEMPT FROM THE REGISTRATION REQUIREMENTS OF THE SECURITIES ACT OF 1933 AND ARE "EXEMPTED SECURITIES" WITHIN THE MEANING OF THE SECURITIES EXCHANGE ACT OF 1934.

For a discussion of certain of the risks relevant to an investment in the Securities, see "Certain Investment Considerations" on page 13.

The following terms and conditions generally apply to the Securities which the Funding Corporation may offer from time to time. The applicable Offering Announcement or Term Sheet will contain the specific information about the Security and may contain additional or different terms and conditions related to that Security. For more detail, see "Terms and Conditions of the Securities."

BONDS*	DISCOUNT NOTES*
• Mature 3 months to 30 years	• Mature 1 to 365 days
• Fixed or floating interest rate or discounted from the amount to be paid at maturity	• Discounted from the amount to be paid at maturity
• May be eligible for separation into Interest and Principal Components	• Not eligible for separation into Interest and Principal Components
• May be subject to redemption at option of the Banks	• Not subject to redemption
• Book-entry form	• Book-entry form
• Fixed-Rate Bonds and Zero-Coupon Bonds — minimum denomination of $5,000, increased in multiples of $1,000 • Floating-Rate Bonds or Fixed-Rate Bonds with structured feature(s) — minimum denomination of $100,000, increased in multiples of $1,000	• Minimum denomination of $5,000, increased in multiples of $1,000
• No fixed maximum aggregate principal amount outstanding	• Maximum aggregate par amount outstanding of $25 billion
• Final terms set forth in an Offering Announcement or a Term Sheet	• Final terms set forth in an Offering Announcement

* Unless otherwise specified by the Funding Corporation with respect to a particular issue of Securities.

Insurance Fund Management

The Insurance Fund and the Secure Base Amount

In 2005, the total Insurance Fund grew 6.3 percent to $2.06 billion. Approximately two thirds of this growth is attributable to investment income with the remainder from premiums. Total assets declined 4.7 percent, dropping from $2.16 billion at yearend 2004 to $2.06 billion at December 31, 2005. This decline was due to the use of $231 million that had previously been set aside to retire a portion of the maturing FAC obligation. (See Note 5 to the financial statements.)

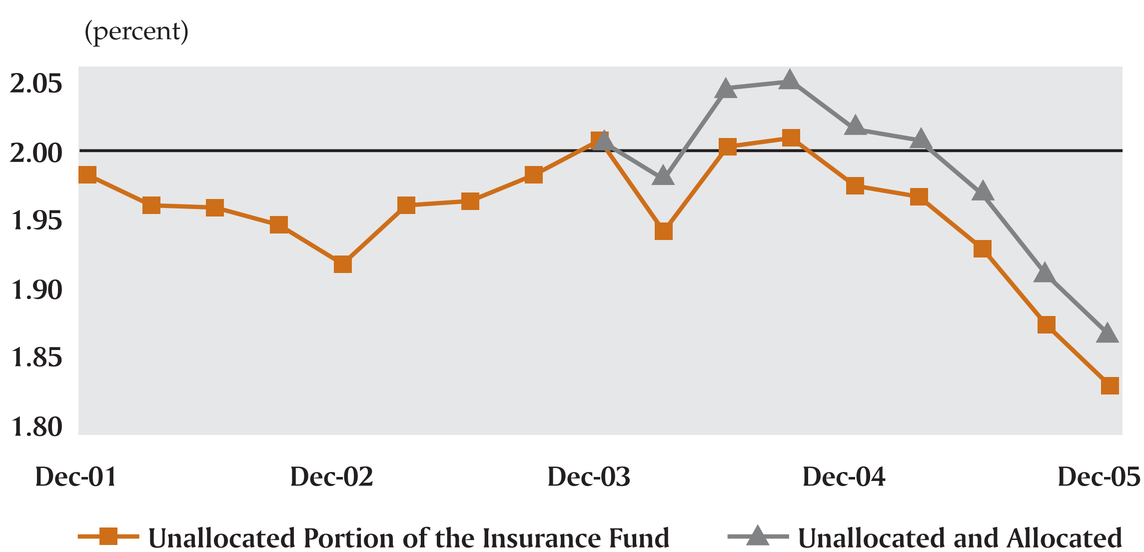
The Insurance Fund represents the Corporation's equity, the difference between total assets and total liabilities, including insurance obligations. Premiums are due until the assets in the Insurance Fund for which no specific use has been identified or designated (unallocated portion of the Insurance Fund) reach the "secure base amount" (SBA). The secure base amount is defined in the Farm Credit Act as 2 percent of the aggregate outstanding insured obligations (adjusted to reflect the System's reduced risk on loans guaranteed by the Federal or state governments) or such other percentage of the aggregate insured obligations as the Insurance Corporation in its sole discretion determines to be actuarially sound.

The unallocated portion of the Insurance Fund continued to trend downward below the SBA in 2005 due to higher than anticipated growth in insured debt. During 2005, insured debt grew 14.3 percent, surpassing the forecasted growth range of 5 to 8 percent and doubling the preceding five-year average growth rate of approximately 7 percent. The unallocated portion of the Insurance Fund finished 2005 below the 2 percent SBA at 1.83 percent or $191 million below the SBA. Including the Allocated Insurance Reserve Accounts (AIRAs) raises the level to 1.86 percent or $151 million below the SBA.

Allocated Insurance Reserve Accounts

The unallocated portion of the Insurance Fund finished the year below the SBA; therefore, no excess funds were

Insurance Fund Relative to 2 Percent Secure Base Amount By Quarter



available for transfer to the AIRA accounts at December 31, 2005. By statute, at any yearend, if the unallocated portion of the Insurance Fund is above the SBA, the Corporation must recalculate the SBA using an average daily debt balance method. This amount is then subtracted from the yearend unallocated portion of the 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 for the holders of FAC stock. The first 10 percent of calculated excess funds are deposited to the FAC stockholders' AIRA. The remaining 90 percent is prorated into the banks' AIRAs. The earliest possible payout date is April 2006; however, any AIRA payments are 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, and
5. Risks in the financial environment.

Although the Corporation insures repayment to investors who purchase System debt, by law it is limited to collecting premiums 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.)

Insurance Premium Rates

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

In September 2004, the Board, in order to allow System institutions to budget for the subsequent year's premium, notified the System that the 2005 premium assessment rate for accrual loans would likely be in the 3 to 6 basis points range as long as growth in insured debt for the year was at or below 7 percent. During the first six months of 2005, the Board set the premium assessment rate at 4 basis points and increased the assessment rate to 6 basis points, the high end of the range, for the second half of the year. The result was a blended premium assessment rate of 5 basis points on accrual loans for 2005. The rates for other loan types, 25 basis points for nonaccrual loans and 0 basis points for Federal Government and state government-guaranteed loans, remained unchanged throughout the year.

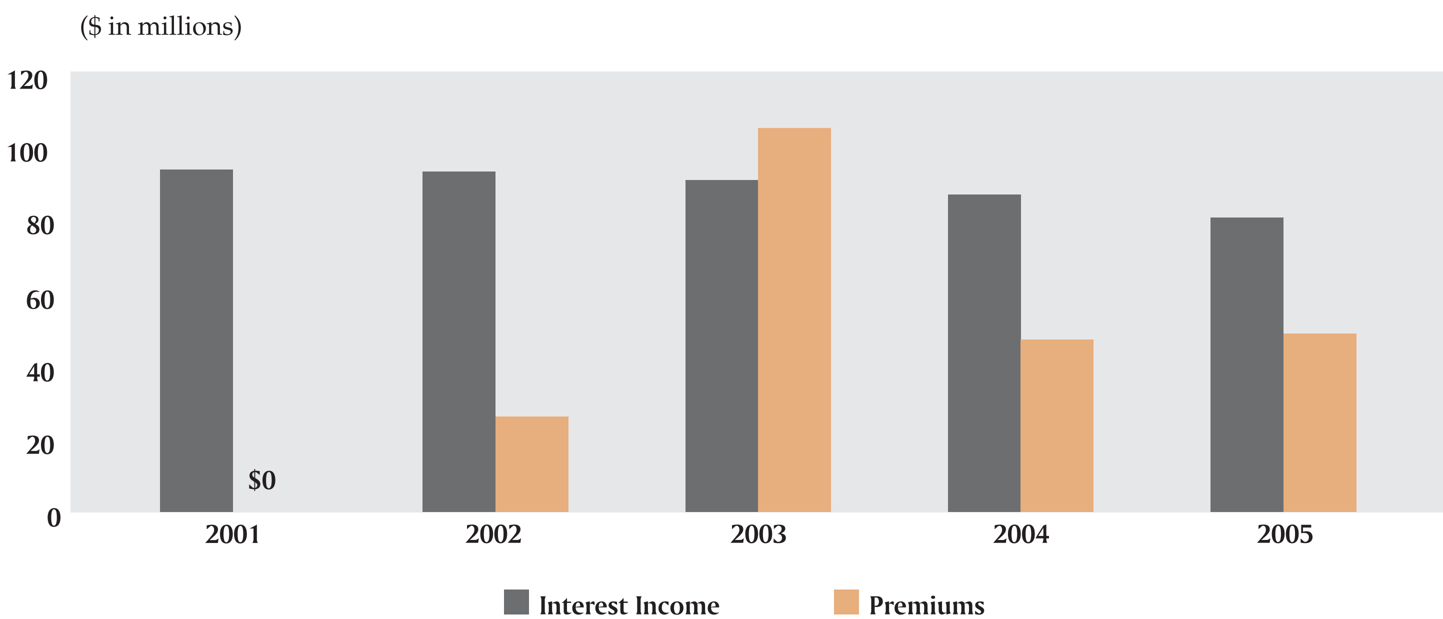
Revenues and Expenses

Net income in 2005 increased 5.2 percent to $122 million, from $116 million in 2004. The increase in net income resulted from lower insurance obligation expense, partially offset by lower investment earnings.

Interest income dropped 6.9 percent in 2005, down from $87 million in 2004 to $81 million, primarily due to the loss in interest income on the $231 million used to pay FCSIC's portion of the FAC obligation in June 2005.

Insurance expenses dropped to $6.2 million from $14.7 million in 2004. Again, the decrease was due to the payoff of the remaining FAC obligation and the related reduction in the annual provision for the insurance obligation during the second half of 2005. (See Note 5 to the financial statements.)

Corporation Revenues



The Corporation's operating costs as a percentage of total assets represented 0.11 basis points for 2005. Fixed costs for staff, travel, rent, and miscellaneous expenses were $1.7 million of the $2.2 million total for the year. The remaining expenses of $0.5 million were for contract services.

Investments

Investments decreased 4.8 percent during the year from $2.1 billion at December 31, 2004, to $2.0 billion at yearend 2005 due to the use of $231 million from the investment portfolio to fully repay the Corporation's remaining share of the FAC obligation in June 2005.

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.

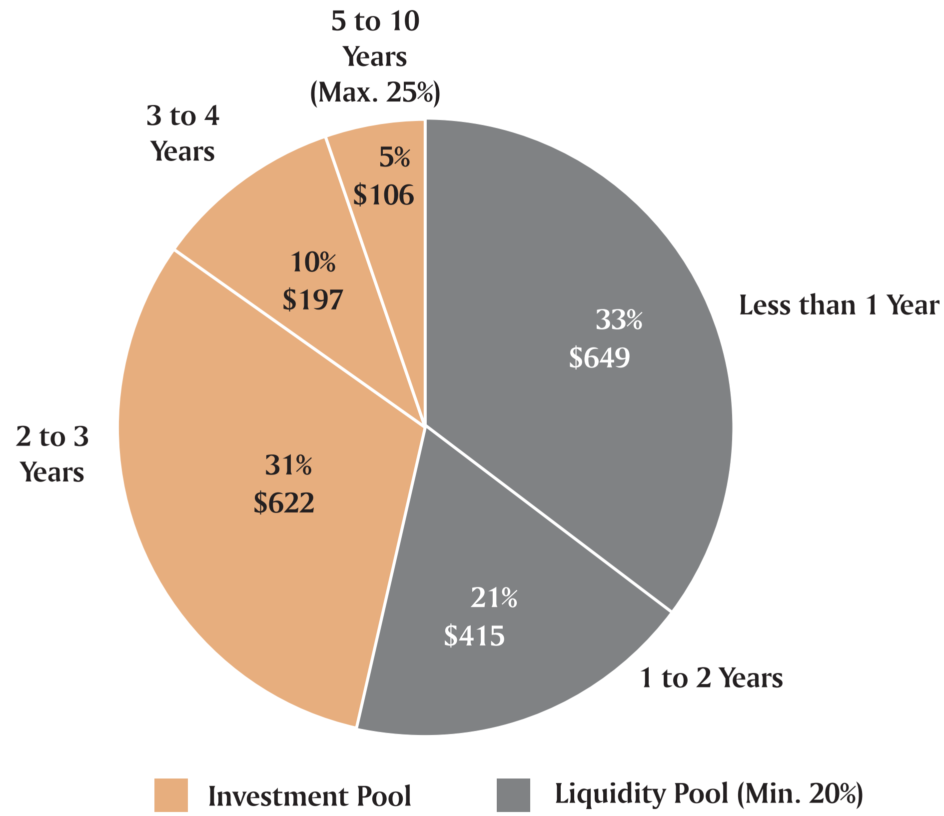
The average portfolio yield was 3.96 percent, down from 4.22 percent the prior year. However, the yield on the Insurance Fund continued to outperform the benchmark index the Corporation uses to measure performance. This index is composed of private sector mutual funds with holdings of similar type and duration to the Corporation's portfolio. The average return of the benchmark group was 2.22 percent for 2005.

Growth in Investment Portfolio

The portfolio is composed of a liquidity and investment pool. The liquidity pool maintains a minimum of 20 percent of the portfolio in short-term securities, while the balance is invested in longer-term maturities of up to 10 years. The weighted average portfolio maturity at yearend was 2.09 years. The balances and maturities of the liquidity and investment pools at December 31, 2005, are illustrated in the following chart.

Investment Portfolio Average Yield of 3.96% — $1.99 Billion at December 31, 2005

($ in millions)



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. Corporation staff regularly monitor key ratios and financial trends; weaker System institutions undergo special examination procedures as needed.

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

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

The Corporation continued to work with an insurance risk tool initially developed in 2004 by FCSIC's contractor, Mercer Oliver Wyman (Mercer). From their work, Mercer concluded that the most significant factors affecting the Corporation's insurance risk exposure were:

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.

During the year, staff met with several groups of System officials to share the results of this phase of the effort and to obtain industry feedback.

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. When considering providing financial assistance, the statute requires the Corporation to ensure that it's the "least costly" method for resolving a troubled System institution. Financial assistance cannot be provided if the cost of liquidation is determined to be lower. During the year, the Corporation field tested an update to its special examination procedures and Cost Test model at a healthy association to ensure its readiness for this responsibility.

There are no active receiverships or conservatorships currently in the System. When appointed by the 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 ongoing 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.

Early in 2005, the Corporation became involved in the dissolution of the Rural Telephone Bank pursuant to a request for advisory services from the United States Department of Agriculture's Under Secretary of Agriculture for Rural Development. An interagency agreement to provide technical assistance to the Rural Telephone Bank as it considered dissolution strategies was executed. The Corporation assisted in developing the dissolution plan that addressed key issues, a timeline, and options for the dissolution. Corporation staff also helped prepare the presentation that bank staff used to brief their board of directors as they considered approving the transaction. In addition, FCSIC provided examples of key documents required for loan transfers and capital stock retirement. The Corporation received $19,000 in reimbursement for its consulting assistance.

Regulations and Policy

In December, we finalized a regulation that will provide a framework for exercising our statutory authority to regulate the payment of golden parachutes at troubled Farm Credit System institutions. The regulation places limits on certain golden parachute payments to employees and agents who terminate their relationship with a troubled institution. It includes several exceptions to the limitations, including: payments under the Employee Retirement Income Security Act qualified plans, nonqualified "bona fide" deferred or supplemental compensation plans, payments made by reason of death or disability, payments to a "white knight," payments required under state and Federal law, and payments made upon a change in control. The regulation also covers indemnity payments.

The Farm Credit Administration issued a regulation that amended the existing receivership and conservatorship regulations. These regulations provide FCSIC, which acts as receiver or conservator for Farm Credit System institutions, with special powers to reclaim assets of a failed institution. The new rule indicates that the Corporation, when acting as receiver or conservator, will not seek to reclaim, recover or recharacterize certain assets transferred as long as the transfer meets the necessary conditions for a "true sale" under generally accepted accounting principles.

Strategic Goals, Performance Measures and the President's Management Agenda

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 2005, the total Insurance Fund trended below the 2 percent secure base amount. Throughout the year, the Insurance Fund ranged from 2.024 to 1.863, and finished the year at 1.863 due to higher than anticipated growth in insured debt. Premium rates were reviewed three times and adjusted from 4 to 6 basis points (an annual rate of 5 basis points), which represented the high end of the range communicated to the System for budgeting purposes. The Corporation's investment yield of 3.96 percent outperformed the index of similarly invested private sector funds used to benchmark investment performance, which returned 2.22 percent.

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 Corporation proactively screens the financials of all System institutions to detect risk and identify institutions that may require special examinations. As an additional tool to evaluate risks, the Corporation continued 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.

The standards used to measure the effectiveness of receivership operations are:

- Completing 90 percent of initial claims processed within a specified period, which will depend on the size and complexity of the failed institution,
- Keeping operating costs comparable to other insurers, as a percentage of total assets, and
- Keeping asset recovery values comparable to other insurers, as a percentage of asset values.

No receiverships or conservatorships existed in the Farm Credit System in 2005. Corporation personnel are trained periodically to maintain readiness, ensuring proficiency in the performance of receivership responsibilities. The next receivership readiness exercise is scheduled for 2007.

The President's Management Agenda

The Corporation, one of 35 agencies designated a significant Government entity for reporting purposes, is required to submit data for the Financial Report of the United States using the Governmentwide 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 governmentwide goals to encourage improvements in specified areas of operations. The Corporation's accomplishments in those five areas are:

1. Strategic Management of Human Capital

- Continued to operate with a small core staff, contracting for specialized expertise when necessary, keeping operating costs low, while offering flexibility to leverage resources.
- Focused on staff cross-training to ensure continuity of operations by empowering multiple staff to be capable of fulfilling a variety of critical roles in day-to-day operations.
- Participated in the Federal Human Capital Survey satisfying the annual requirement established by the National Defense Authorization Act of 2004 and providing agency metrics within the human capital accountability system.

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.
- Decreased contracting expenses for 2005 by 27 percent from 2004, while contractor support increased.

3. Improved Financial Performance

- Managed an investment portfolio with an average yield exceeding benchmark.
- Actual Operating Expenses for 2005 were 12 percent below Budgeted Operating Expenses.

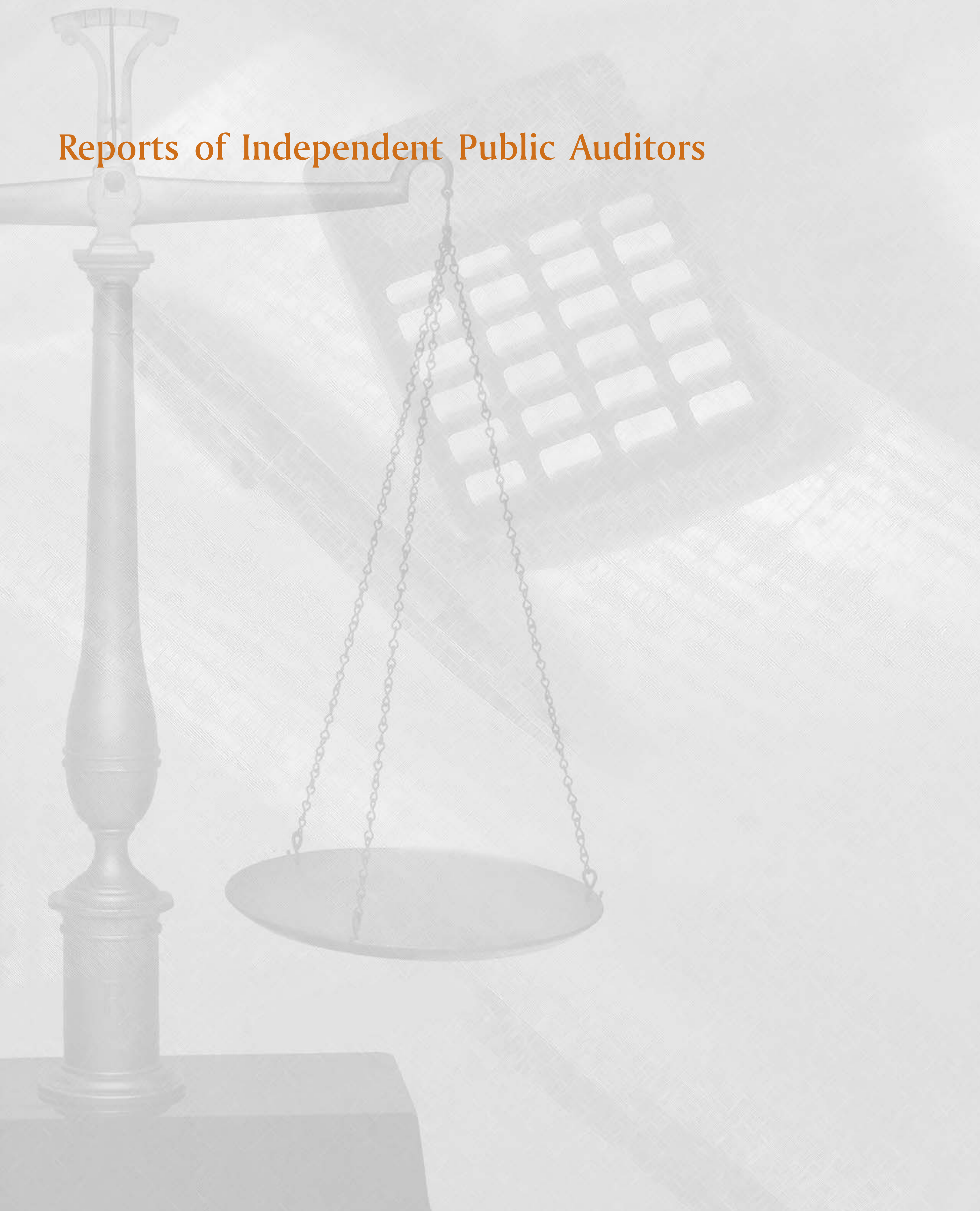
4. Expanded Electronic Government

- Used the Corporation's Web site as the primary vehicle for providing information to our stakeholders, other government entities, and the public.
- Began sending all communications to the Farm Credit System electronically.
- Increased the participation rate of member institutions responding to the annual FCSIC System survey by 224 percent by sending and receiving the survey 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 versus Annual Performance and Strategic plans 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 independent external auditor.
- The annual report on the Corporation's control over Reporting and Compliance issued by our independent external auditor did not disclose any internal control weaknesses or any instances of noncompliance.
- The agreed upon procedures performed by our independent external auditor in accordance with instructions provided by the U.S. Treasury with respect to Federal Intergovernmental Activity and Balances for FY 2005 did not disclose any exceptions.

Reports of Independent Public Auditors



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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 cash flows present fairly, in all material respects, the financial position of Farm Credit System Insurance Corporation (the "Corporation") at December 31, 2005 and 2004, 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 audit provides a reasonable basis for our opinion.

In accordance with *Government Auditing Standards*, we have also issued our report dated March 9, 2006 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, 2005. 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 9, 2006

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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, 2005, and have issued our report thereon dated March 9, 2006. 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.

Internal Control Over Financial Reporting

In planning and performing our audit, we considered Corporation's internal control over financial reporting in order to determine our auditing procedures for the purpose of expressing our opinion on the financial statements and not to provide an opinion on the internal control over financial reporting. Our consideration of the internal control over financial reporting would not necessarily disclose all matters in the internal control over financial reporting that might be material weaknesses. A material weakness is a reportable condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that misstatements caused by error or fraud in amounts that would be material in relation to the financial statements being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. We noted no matters involving the internal control over financial reporting and its operation that we consider to be material weaknesses.

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 9, 2006

Financial Statements

FARM CREDIT SYSTEM INSURANCE CORPORATION
Statements of Financial Condition as of December 31, 2005 and 2004
($ in thousands)

	2005	2004
ASSETS		
Cash and Cash Equivalents	$ 273,887	$ 2,279
Investments in U.S. Treasury Obligations (Note 3)	1,715,586	2,087,702
Accrued Interest Receivable	22,856	27,505
Premiums Receivable (Note 4)	49,493	46,520
Other Receivable	-	-
TOTAL ASSETS	**$ 2,061,822**	**$ 2,164,006**
LIABILITIES AND INSURANCE FUND		
Farm Credit Liabilities		
Accounts Payable and Accrued Expenses (Note 7)	$ 440	$ 371
Liability for Estimated Insurance Obligations (Note 5)	-	224,489
TOTAL LIABILITIES	**440**	**224,860**
Farm Credit Insurance Fund		
Allocated Insurance Reserve Accounts	39,888	39,888
Unallocated Insurance Fund Balance	2,021,494	1,899,258
TOTAL INSURANCE FUND	**2,061,382**	**1,939,146**
TOTAL LIABILITIES AND INSURANCE FUND	**$ 2,061,822**	**$ 2,164,006**

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, 2005 and 2004
($ in thousands)

	2005	2004
INCOME		
Premiums (Note 4)	$ 49,393	$ 46,520
Interest Income	81,253	86,567
Other Income	20	-
TOTAL INCOME	$ 130,666	$ 133,087
EXPENSES		
Administrative Operating Expenses (Note 7)	$ 2,202	$ 2,263
Provision for Estimated Insurance Obligations (Note 5)	6,228	14,686
TOTAL EXPENSES	**$ 8,430**	**$ 16,949**
NET INCOME	**$ 122,236**	**$ 116,138**
Farm Credit Insurance Fund - Beginning of Year	$ 1,939,146	$ 1,823,008
Farm Credit Insurance Fund - End of Year	$ 2,061,382	$ 1,939,146

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, 2005 and 2004
($ in thousands)

	2005	2004
CASH FLOWS FROM OPERATING ACTIVITIES		
Net Income	$ 122,236	$ 116,138
Adjustments to Reconcile Net Income to Net Cash Provided by Operating Activities:		
(Increase) Decrease in Premium Receivable	(2,973)	58,559
Decrease in Accrued Interest Receivable	4,649	1,302
Net Amortization and Accretion of Investments	17,378	21,443
Decrease in Other Receivables	-	4
Increase in Accounts Payable Accrued Expenses	69	11
(Decrease) Increase in Liability for Estimated Insurance Obligations	(224,489)	14,686
Total Net Cash Provided By Operating Activities	$ (83,130)	$ 212,143
CASH FLOWS FROM INVESTING ACTIVITIES		
Payments for Purchase of U. S. Treasury Obligations	$ -	$ (496,266)
Proceeds from Maturity of U.S. Treasury Obligations	354,737	286,216
Total Net Cash Used in Investing Activities	$ 354,737	$ (210,050)
Net Change in Cash and Cash Equivalents	$ 271,607	$ 2,093
Cash and Cash Equivalents - Beginning of Year	$ 2,279	$ 186
Cash and Cash Equivalents - End of Year	$ 273,886	$ 2,279

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

Notes to the Financial Statements

AS OF DECEMBER 31, 2005, AND DECEMBER 31, 2004

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, 2005, there were five insured System banks and 96 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;

2. Satisfy, pursuant to section 6.26(d)(3) of the Act, defaults by System banks on obligations related to the issuance of U.S. Treasury-guaranteed bonds by the Farm Credit System Financial Assistance Corporation (FAC) (FAC bonds) (see Note 5); and

3. Ensure the retirement of eligible borrower stock at par value.

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, 2005, for each of the components of the Corporation's insurance responsibilities were $114 billion of insured obligations and $16 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(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, 2005, the Corporation held $273.84 million in overnight Treasury Certificates maturing on January 3, 2006, with an investment rate of 3.46 percent.

*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. (Also see Note 5.)

The insured System banks' primary lending markets are borrowers engaged in farming, ranching, and 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.

*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 2005 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 $155,572 in 2005 and $145,573 in 2004.

Note 3—Investments

At December 31, 2005 and 2004, investments in U.S. Treasury obligations consisted of the following:

($ in thousands)

	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Market Value
December 31, 2005				
U.S. Treasury Notes	$ 1,715,586	$ 5,689	$ (28,426)	$ 1,692,849
December 31, 2004				
U.S. Treasury Notes	$ 2,087,702	$ 34,626	$ (9,955)	$ 2,112,373

The amortized cost and estimated market value of U.S. Treasury obligations at December 31, 2005, by contractual maturity, are shown below.

($ in thousands)

	Amortized Cost	Estimated Market Value
Due in one year or less	$ 374,947	$ 376,538
Due after one year through five years	1,234,252	1,212,862
Due after five years through 10 years	106,387	103,449
	$ 1,715,586	**$ 1,692,849**

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) average annual accrual loans outstanding (other than the guaranteed portions of Government-guaranteed accrual loans) for the year may be from zero to 15 basis points (0.0015); (2) average annual nonaccrual loans outstanding may be from zero to 25 basis points (0.0025); (3) average annual portions of Federal Government-guaranteed accrual loans may be from zero to 1.5 basis points (0.00015); and (4) average annual portions of state government-guaranteed accrual loans may be from zero to 3 basis points (0.0003).

Insurance premium rates are reviewed semiannually. For 2005, premium rates were set at the Board's January 2005 meeting at 4 basis points for accrual loans, 25 basis points for non-accrual loans, and zero for Federal and state government guaranteed loans. The Board 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 2005 meetings. At the September meeting the Board increased premiums on accrual loans to 6 basis points for the second half of 2005, the top of the previously announced guidance range and left other rates unchanged. This resulted in a blended rate of 5 basis points on accrual loans for 2005. The increase was due to the high growth in insured debt outstanding during the year. In 2005, outstanding insured obligations increased by $14.2 billion or 14.3 percent. At December 31, 2005, the unallocated portion of the Insurance Fund was 1.83 percent as a percentage of adjusted insured debt. Including the AIRAs raised the level to 1.86 percent.

On January 19, 2006, the Board increased the premium rate for accrual loans to 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 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 identified or designated (the unallocated portion of the Insurance Fund).

A 1996 amendment to the Act requires the Corporation to establish reserve accounts for each System bank and an account for the stockholders of the FAC. If at the end of any calendar year the unallocated portion of the Insurance Fund is at the secure base amount, the Corporation is to segregate any excess balances into these allocated insurance reserve accounts (AIRAs). In 1999, the Corporation's Board adopted a 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 portion of the Insurance Fund exceeds the 2 percent secure base amount, the Corporation recalculates the secure base amount on an average daily balance basis and compares that amount with the yearend Insurance Fund balance adjusted downward by the Corporation's estimated expenses for the following year. At yearend 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 provides that amounts in the AIRAs may 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.

Note 5—Financial Assistance to System Banks and Estimated Insurance Obligations

The 1987 Act required that the FCA charter the Farm Credit System Assistance Board (Assistance Board) and the FAC (see Note 1) to carry out a program of financial assistance to the Farm Credit System. In order to raise funds to provide this assistance, the FAC had the authority to issue debt obligations with a maturity of 15 years. During 1988 to 1990, the FAC issued $1.261 billion in bonds. These funds were used to provide assistance to certain System banks experiencing financial difficulty and for other statutorily authorized purposes. From 1998 through 2004, $936 million in FAC bonds have been retired, leaving one remaining issue of $325 million outstanding, which matured and was repaid on June 10, 2005. Repayment of the remaining FAC bond in accordance with the Act was provided for by the FAC Trust Fund, FAC Assistance Fund, and the Insurance Corporation. See Insurance Obligation below.

Insurance Obligation

On June 10, 2005, the FAC repaid its remaining outstanding issue of $325 million. Funding for the payment was provided as follows:

FAC Trust Fund	$ 80 million
FAC Assistance Fund	$ 14 million
FCSIC	$ 231 million
Total	$ 325 million

The Corporation had estimated the present value of its liability to provide funds for payment of the $325 million non-callable 15-year maturing debt to be approximately $224 million at December 31, 2004. The present value of this obligation was based on a discount rate of 7 percent to maturity, which was established at the time this liability was originally recorded. In accordance with SFAS No. 107, the fair value of this liability was estimated by management using discount rates based upon U.S. Treasury securities of similar durations (2.4 percent for 2004). The fair value was approximately $229 million as of December 31, 2004.

Other Financial Assistance Provided to System Institutions

From 1988 to 1998, the U.S Treasury paid interest on certain FAC bonds totaling $440 million. System banks repaid Treasury for this obligation on June 10, 2005, as required. The 1992 Amendment to the Act expanded the potential uses of the Trust Fund to satisfy System institution defaults on the principal and interest of other FAC obligations and required System banks to make annual annuity payments to the FAC to provide funds for the retirement of the Treasury-paid interest at maturity. The Corporation was required to satisfy defaults on the annual payments to the FAC to permit the repayment of Treasury-paid interest.

The Corporation actively monitors the creditworthiness and financial position of the insured System banks. Other than obligations that have occurred as a result of resolving the Federal Land Bank of Jackson in Receivership, management is not aware of any events or circumstances at this time which would require a liability for estimated insurance obligations to be recorded.

Note 6—Operating Lease

On October 21, 2003, the Corporation executed a new six-year lease with the FCS 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 $120,019 for 2005, $121,100 for 2006, $122,181 for 2007, $123,262 for 2008, and $124,344 for 2009. The Corporation recorded lease expense (including operating cost assessments) of $122,245 and $120,795 for 2005 and 2004, respectively.

Note 7—Related Parties

The Corporation purchases services from the FCA under an Inter-Agency Agreement. These include examination and administrative support services. The Corporation had payables due to the FCA of $28,250 at December 31, 2005, and $1,687 at December 31, 2004. The Corporation purchased services for 2005 which totaled $109,589 compared with $70,332 for 2004.

The Corporation provided assistance to the FCA under a related Inter-Agency Agreement, recognizing revenue in 2005 of 1,125 and in 2004 of zero. At December 31, 2005 and 2004, the Corporation did not have any receivable from the FCA.

Income and Expenses

Farm Credit System Insurance Corporation By Year

($ in thousands)

	Income		Expenses		Net Income
	Premiums	Investment	Provision for Insurance Obligations	Administrative and Operating Expenses	Changes in Insurance Fund
1989	$ 65,000	$ 16,041	—	$ 118	$ 8,923
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)[1]	$ 1,278	$ 153,543
1994	$ 76,526	$ 46,389	$ 8,890	$ 1,482	$ 112,543
1995	$ 79,394	$ 54,688	($ 14,329)[2]	$ 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[3]
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

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 of 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

Mary Creedon Connelly*	Chief Operating Officer
Alan J. Glenn	Director of Risk Management
C. Richard Pfitzinger	Chief Financial Officer
Dorothy L. Nichols*	General Counsel
Phyllis Applebaum	Financial Analyst
William Fayer	Financial Analyst/Asset Assurance Manager
Gary Stover	Financial Analyst
Pam Ngorskul	Accountant
Anna Lacey	Administrative Specialist
Molly Sproles	Clerical Assistant

* In March 2006, Mary Creedon Connelly, who served with distinction as the Chief Operating Officer since 1991, retired. Dorothy Nichols, who served as General Counsel, became the Chief Operating Officer effective February 19, 2006.

Acknowledgements:
Linda M. Toki
Anna Lacey
Molly Sproles

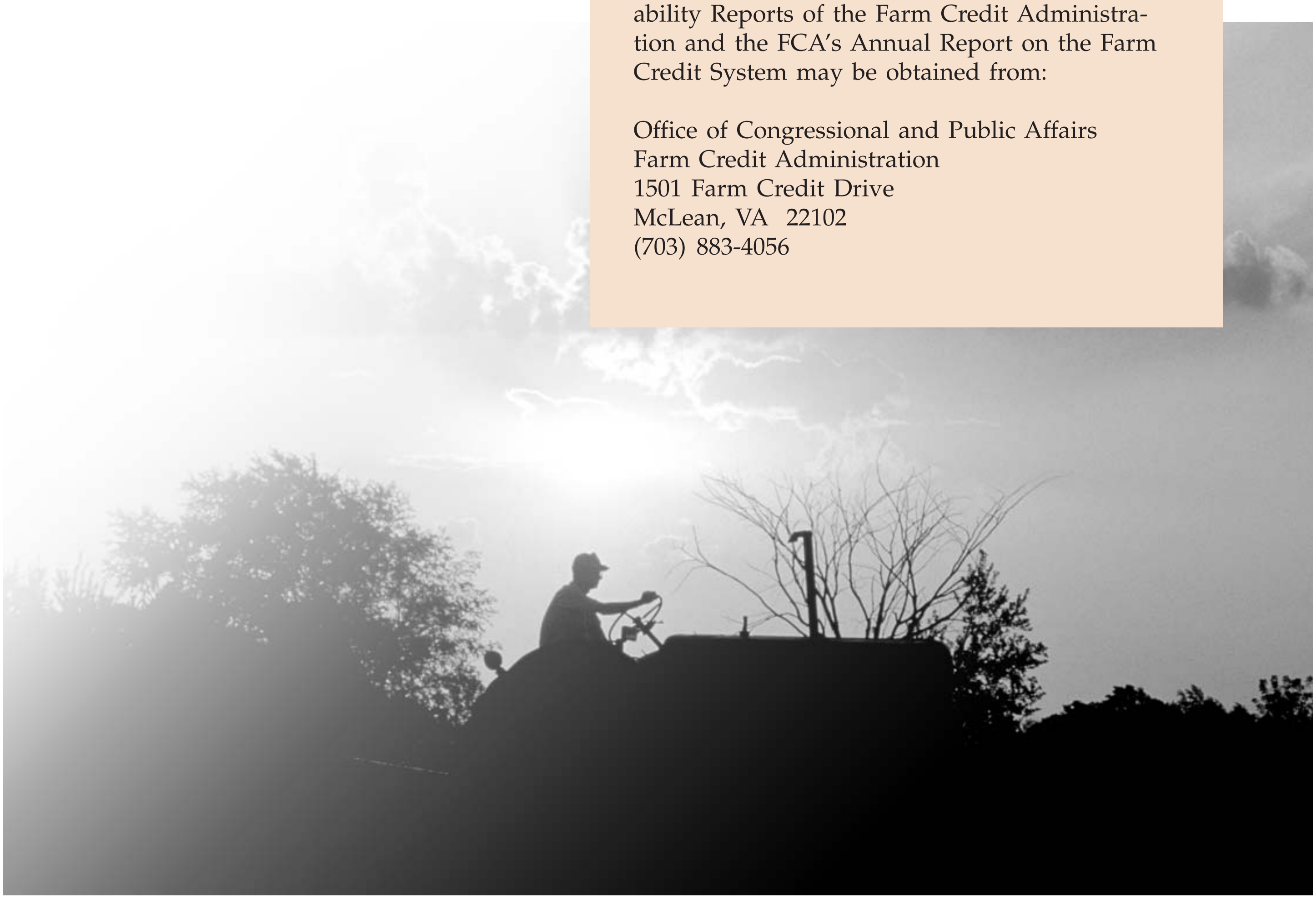
References

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



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