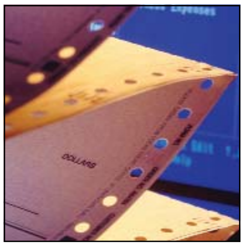
FARM CREDIT SYSTEM INSURANCE CORPORATION

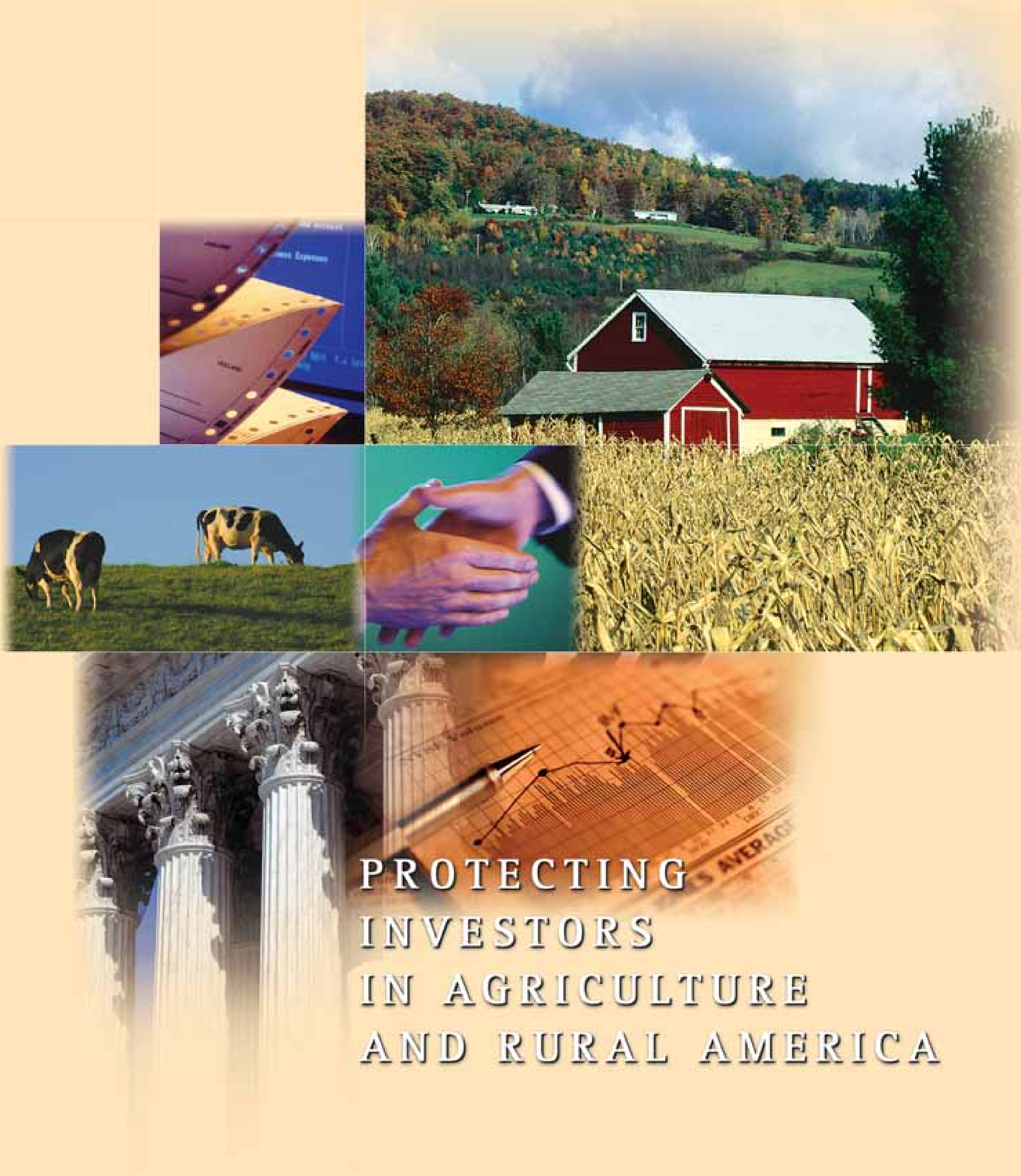








2004 ANNUAL REPORT



PROTECTING INVESTORS IN AGRICULTURE AND RURAL AMERICA

FCSIC

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.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April 29, 2005

Gentlemen:

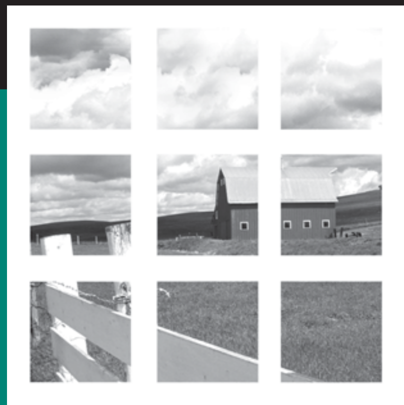
In accordance with the provisions of section 5.64(a) of the Farm Credit Act of 1971 as amended, the Farm Credit System Insurance Corporation is pleased to submit its annual report for calendar year 2004.

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, 2004, was $1.94 billion. The Corporation collected $47 million in insurance premiums from Farm Credit System banks for 2004, and expects to incur $2.5 million in operating costs in 2005.

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

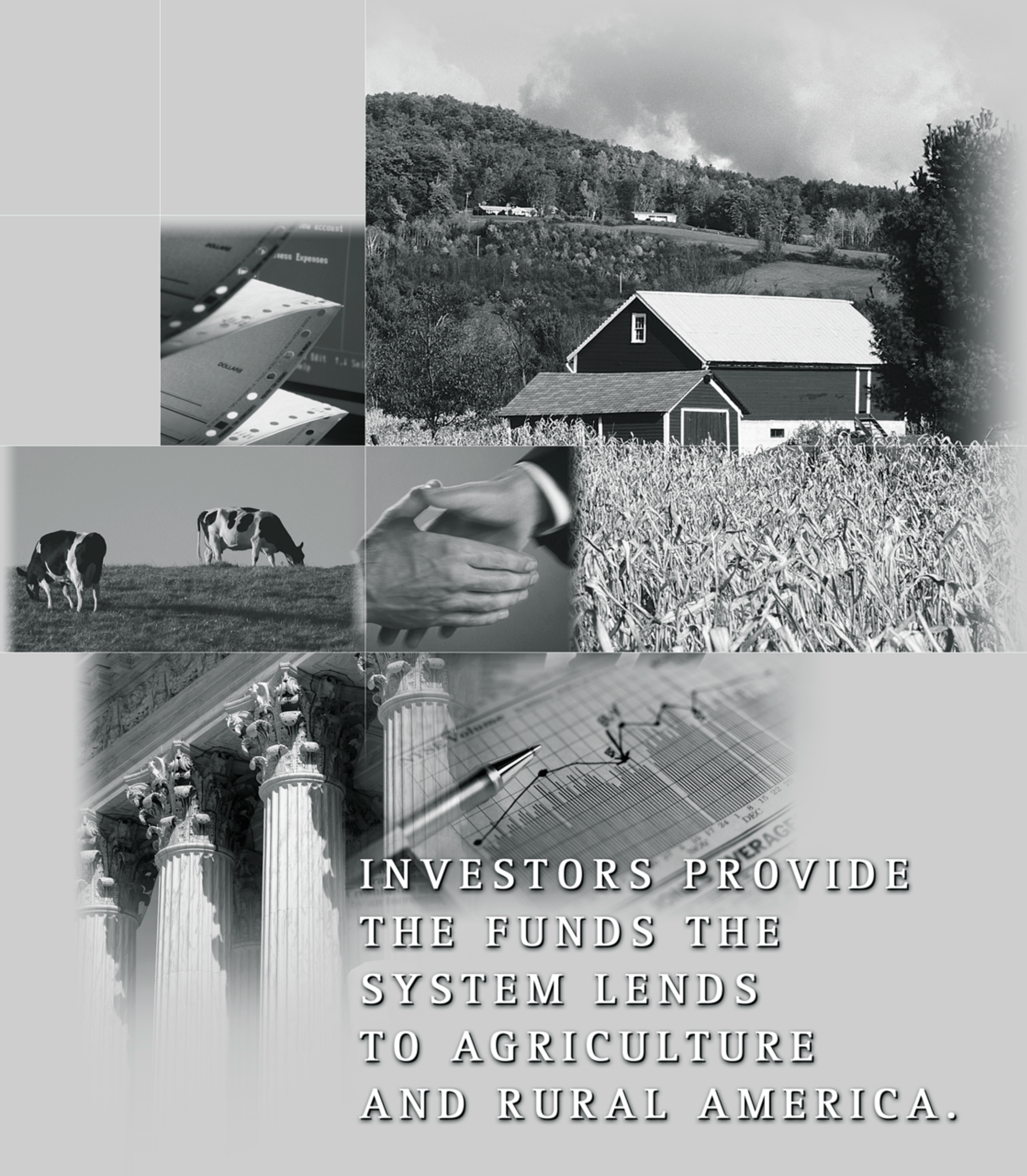
Dallas P. Tonsager was appointed to the FCA and FCSIC Boards by President Bush on December 1, 2004, for a term that expires May 21, 2010. Mr. Tonsager brings extensive experience as an agricultural leader and producer to his position on the FCSIC Board, as well as a commitment to promoting and implementing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



INVESTORS PROVIDE THE FUNDS THE SYSTEM LENDS TO AGRICULTURE AND RURAL AMERICA.

New Insurance Risk Tool

Congress directed the Corporation to build the Fund to a "secure base amount" defined as 2 percent of insured obligations, or another percentage that the Board determines is actuarially sound based on current risk levels and the level of outstanding insured obligations. In 2003, the Corporation began research into the development of an actuarial approach to analyzing the adequacy of the Insurance Fund.

During 2004, the Corporation added Dynamic Capital Adequacy Testing (DCAT) to its risk management practices. Over the next several years the Corporation will test this model as an additional internal risk monitoring tool. This will allow us to gain experience and identify any policy implications for future Board consideration. The DCAT model was developed in consultation with Mercer Oliver Wyman, an international risk management consulting firm, and is a best practice for making capital adequacy assessments in the insurance industry. It allows the Corporation to better quantify sources of risk, focusing management and the Board on areas where the Fund is most vulnerable. The Corporation will continue using its other risk management tools, in concert with the DCAT model, to monitor and evaluate risk. This tool may also be used to assist in developing insurance premium rates and evaluating risks and emerging trends.

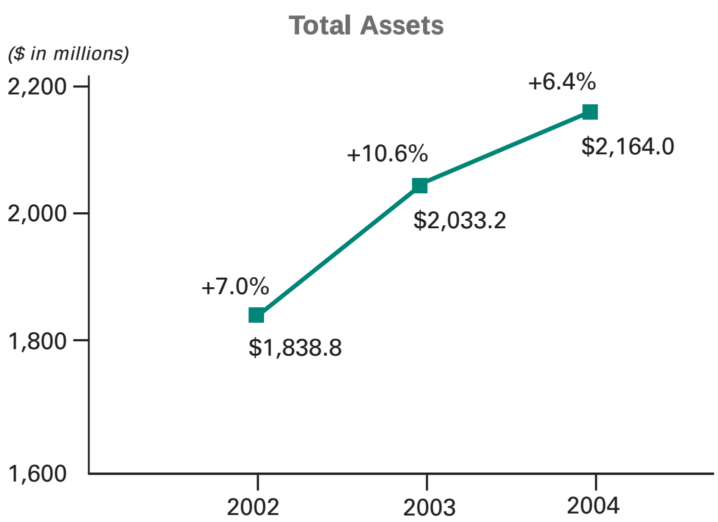
The model uses examination findings, key ratios, financial indicators, as well as current and historical data to forecast the likelihood of defaults. Loss claims to the Insurance Fund can arise when an insured bank defaults on repayment of its insured debt obligations to investors. Monte Carlo simulation techniques, an analytical method used to imitate a real life system, are used to generate a range of potential Insurance Fund loss claims over a 10-year time horizon. Each run of the model algorithm, allows for 20,000 simulations to develop the solvency probability distribution. The dynamic nature of the model allows staff to perform sensitivity testing of the key assumptions including:

- System balance sheet growth over time,
- Regulatory CAMEL institutional risk ratings,
- Insured bank capital levels,
- Insurance premium rates, and
- Insurance Fund investment returns.

The use of a DCAT model has several advantages when making assessments of Insurance Fund adequacy. First, the model generates a range of potential losses, not just a single result such as would occur with scenario testing. Second, the loss model recognizes the potential for loss events that have a low likelihood but would significantly stress the Insurance Fund if they did occur.

Farm Credit System Insurance Corporation
Selected Financial Statistics

($ in millions)	2004	2003	2002
Balance Sheet:			
Total Assets	$ 2,164.0	$ 2,033.2	$ 1,838.8
Total Liabilities	224.5	210.2	196.3
Insurance Fund Balance			
Allocated Insurance Reserve Accounts	39.9	39.9	0
Unallocated Insurance Fund Balance	1,899.3	1,783.1	1,642.5
Operations:			
Revenues	133.1	196.5	123.0
Operating Expenses	2.3	2.2	1.9
Insurance Expense	14.7	13.7	13.6
Net Income	116.1	180.6	107.5



The Farm Credit System

Structure and Funding

The System is owned by the rural customers it serves including farmers, ranchers and other agricultural producers. There are 96 Farm Credit System associations that 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 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. 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 ensure 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 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 below:

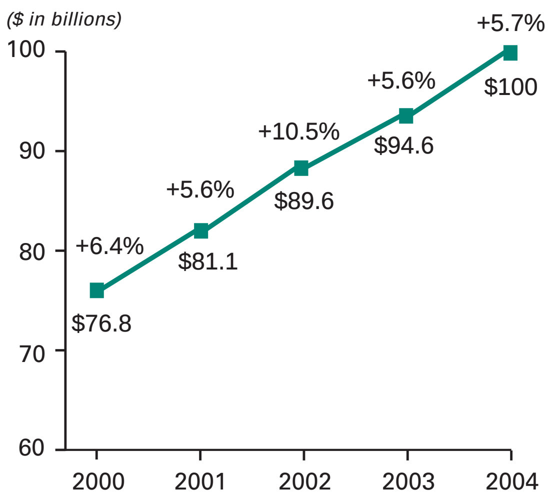
($ in billions)	2004	2003	2002
Insured Debt Outstanding	$100.0	$94.6	$89.6
Farm Mortgage Loans	50.4	46.5	43.5
Agricultural Production Loans	21.1	21.1	20.5
Loans to Agricultural Cooperatives	8.3	9.0	8.9
International Loans	2.6	2.8	3.1
Loans to Rural Utilities	7.1	7.2	7.7
Rural Home Loans	2.6	2.3	2.3
Other Loans	4.3	4.3	4.1
Net Income	2.99[1]	1.83	1.77
Nonperforming Loans as a Percentage of Total Loans	0.8%	1.3%	1.3%

1. Includes a one time loss reversal of $1.167 billion, net of taxes. Excluding this amount, net income would have been $1.825 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 Federal Farm Credit Banks Funding Corporation. Last year, insured debt outstanding rose by more than 5.7 percent to $100 billion. From 2000 through 2004, insured debt outstanding grew at an average annual rate of approximately 6.8 percent.

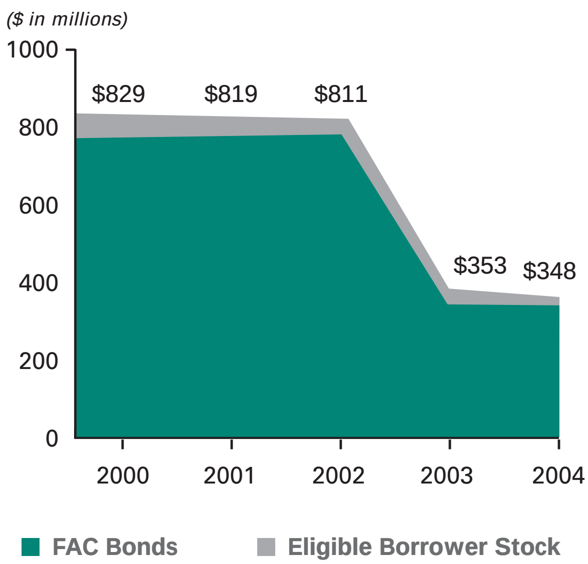
Insured Debt Outstanding

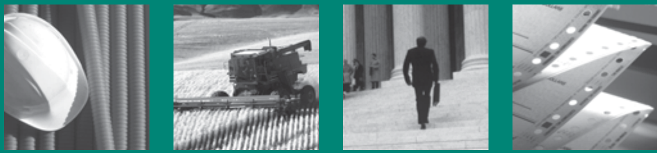


Other obligations include remaining Farm Credit System Financial Assistance Corporation (FAC) bonds and eligible borrower stock. From 1988 to 1992, the FAC provided assistance to the Farm Credit System, issuing $1.26 billion in debt to cover these costs. The Corporation by law must use the Insurance Fund to satisfy any FAC-issued bond defaults. The remaining $325 million issue of FAC bonds outstanding are due in June of 2005. The Corporation estimates its obligation to the FAC at December 31, 2004, to be $224 million. (See Note 5 to the financial statements.)

The Corporation also must ensure the retirement of eligible System borrower stock at par value. This stock was outstanding before October 6, 1988. At yearend 2004, eligible borrower stock outstanding at System institutions totaled $23 million, down from $28 million at yearend 2003.

Other Obligations





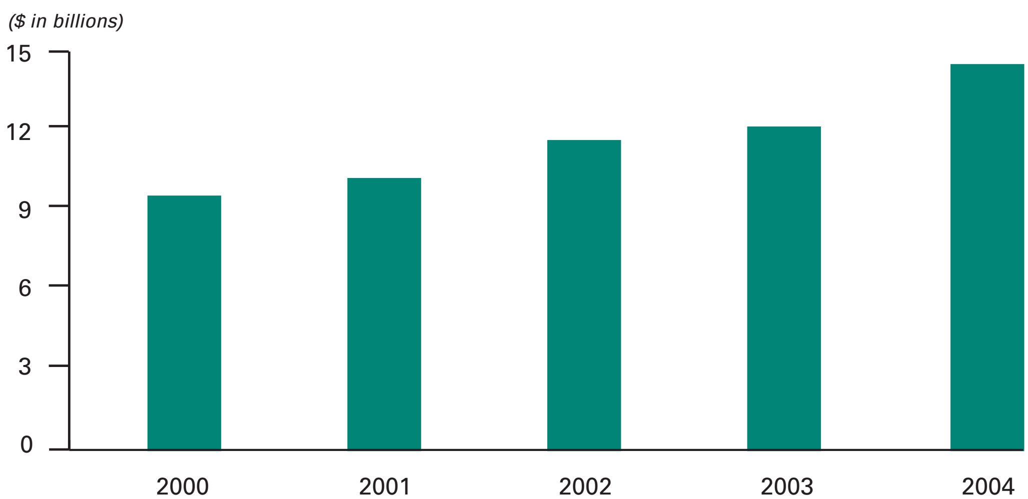
Farm Credit System Capital

Today there are four Farm Credit Banks and one Agricultural Credit Bank (banks), which lend funds to 96 affiliated associations. These associations make loans to rural homeowners, farmers, ranchers and other agricultural entities. The Agricultural Credit Bank also lends to agricultural cooperatives and rural utilities. At yearend 2004, there was $100 billion in insured debt outstanding; and the Corporation had $2.2 billion in assets, $0.22 billion in insurance liabilities, and an unallocated Insurance Fund balance of $1.9 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 rise in capital at the associations reduces the credit exposure the banks have on loans to each of their affiliated associations.

Since 2000, combined association capital has increased 53 percent from $9.26 billion to $14.17 billion at yearend 2004.

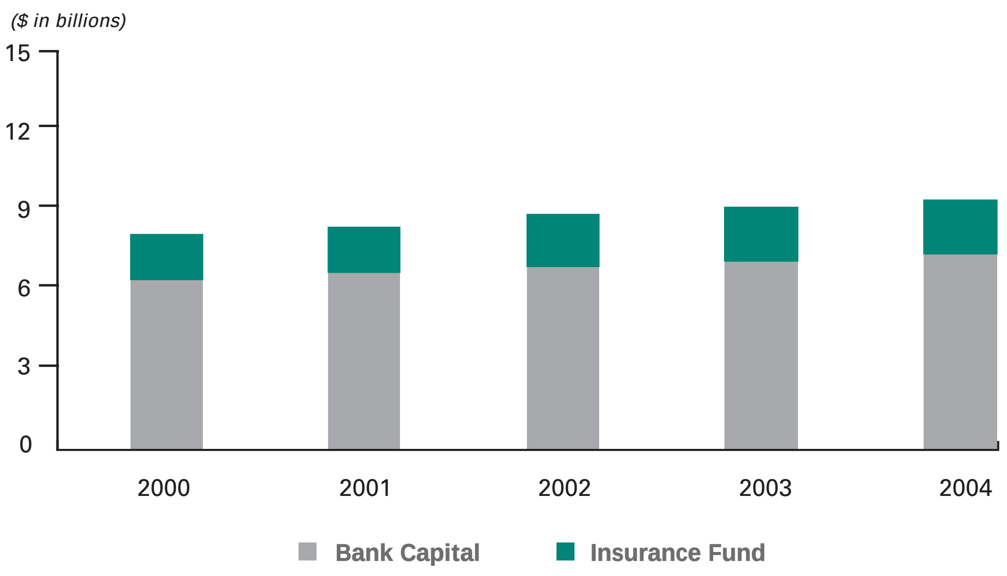
Association Capital



Since 2000, combined bank capital plus the Insurance Fund has increased 25 percent from $7.5 billion to $9.38 billion at yearend 2004.

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 further 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

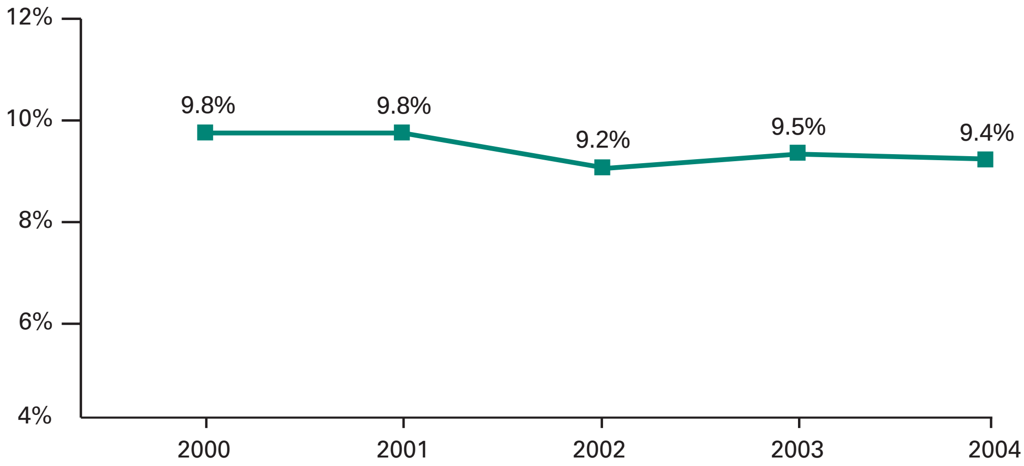
Bank Capital Plus the Insurance Fund



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 debt, bank capital plus the Insurance Fund decreased from 9.8 percent in 2000 to 9.4 percent in 2004. The reason for the decline is that the rate of growth in outstanding debt outpaced growth in bank capital and the Insurance Fund.

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



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. 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.

CORPORATE ASSETS TOTALED $2.2 BILLION AT YEAREND 2004.

Insurance Fund Management

Revenues and Expenses

In 2004, net income declined 36 percent to $116 million, down from $181 million in 2003, due to reduced insurance premiums and lower earnings on investments. Premium rates on accrual loans were lowered from 12 basis points in 2003 to just under 5 basis points in 2004. Premiums were assessed at 10 basis points during January to June of 2004 and zero basis points from July to December.

The Board reviews premium accrual rates semiannually. Five factors are considered:

1. The level of the unallocated 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. Risk in the financial environment.

Although the Corporation ensures repayment to investors who purchase System debt, by law it collects premiums based on the loans made by System banks and associations. Premium rates may vary by type of loan. (See Note 4 to the Corporation's financial statements.)

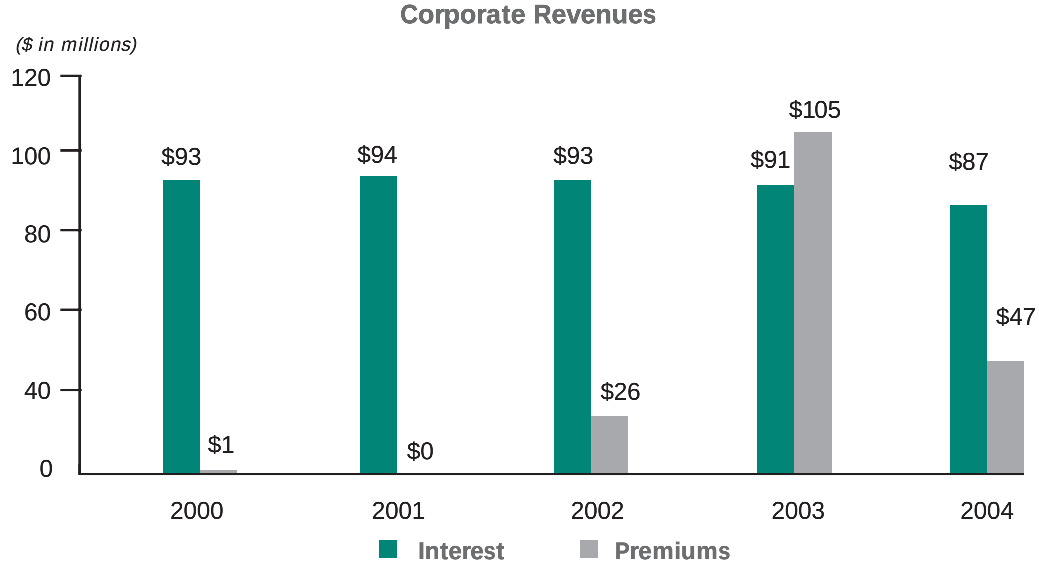
Interest income dropped 4.8 percent in 2004, down from $91 million in 2003 to $87 million, primarily due to low market interest rates. The average portfolio yield was 4.22 percent, down from 4.93 percent at yearend 2003.

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

Insurance expenses grew to $14.7 million from $13.7 million in 2003. The increase was due to the annual provision for the insurance obligation to repay the FAC for assistance-related bonds that will mature in 2005. (See Note 5 to the financial statements.)

The Corporation's operating costs as a percent of total assets dropped half a basis point, falling from 11 basis points on assets to 10.5 basis points on assets for 2003 and 2004, respectively. Operating costs for 2004 were slightly under the three-year average, from 2002 to 2004, of 10.6 basis points. Fixed costs for staff, travel, rent, and miscellaneous expenses were $1.6 million of the $2.3 million total for the year. The remaining expenses of $0.7 million were for contract services.

Corporate Revenues



Growth in the Insurance Fund and the Secure Base Amount

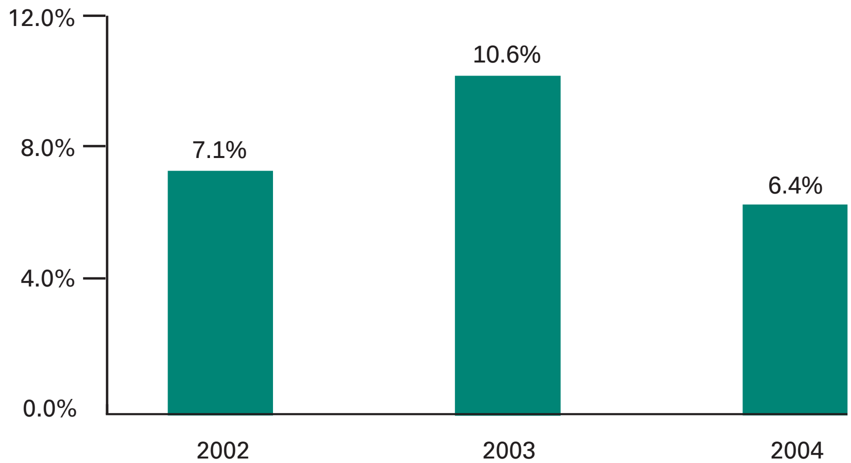
In 2004, the total Insurance Fund and total assets grew 6.4 percent to $1.9 billion and $2.2 billion, respectively.

Over the last five years, the Corporation's total assets have grown at an annual rate of 6.6 percent. During this time period, the strongest one-year growth occurred in 2003 when total assets grew 10.6 percent.

At yearend, the unallocated Insurance Fund was slightly below the secure base amount (SBA). The Insurance Fund represents the Corporation's equity, the difference between total assets and total liabilities, including insurance obligations. The unallocated Insurance Fund is the portion of the Fund for which no specific use has been identified or designated by the Corporation. The SBA established by the Act is 2 percent of all outstanding insured obligations or another percentage that the Board determines is actuarially sound.

The unallocated Insurance Fund fell short of the SBA in 2004 due to higher growth in the month of December. Insured debt for the first eight months of 2004 grew at 4.1 percent (annualized basis), which was lower than the forecasted growth estimate of 5 to 9 percent and also below the five-year average growth rate of approximately 7 percent. As a result, at the September premium review, the Board decreased the premium accrual rate from 10 basis points on accrual loans during the first six months of 2004 to 0 basis points for the

Percentage Growth in Total Assets



remainder of the year. The rates for other loan types remained unchanged. The overall growth rate of insured debt and percentage increase in the Insurance Fund—both unallocated and allocated—for 2004 were 5.7 percent and 6.4 percent, respectively.

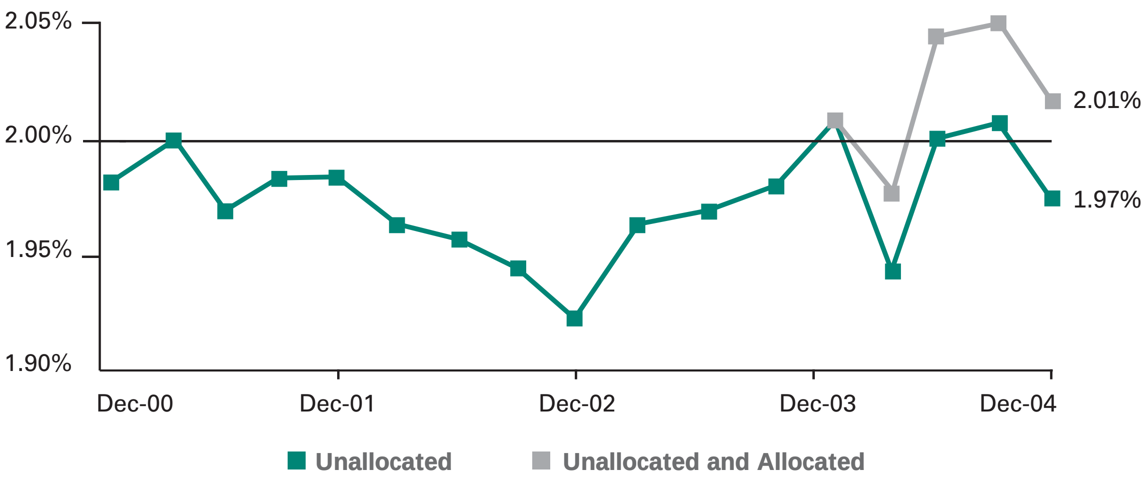
For the first time, in 2003 the Corporation closed the year above the SBA. As a result, the Corporation was required by statute to transfer $39.9 million to the Allocated Insurance Reserve Accounts (AIRAs). By statute, the Corporation is required to use AIRAs first for Insurance Fund claim payments. The total Insurance Fund, including both the unallocated and allocated amounts, exceeded the SBA by $5 million and $14 million for yearend 2003 and 2004, respectively.

Allocated Insurance Reserve Accounts

The unallocated Insurance Fund finished the year below the SBA; therefore, no excess funds were transferred in 2004 to the AIRA accounts at yearend. By statute, at any yearend, if the unallocated Insurance Fund is over the SBA, the Corporation must recalculate the SBA using an average daily debt balance method. This amount is then subtracted from the yearend unallocated Insurance Fund balance, less projected insurance and operating expenses for the coming year, to determine the excess amount for transfer to the AIRAs.

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

Insurance Fund Relative to 2% Secure Base Amount By Quarter



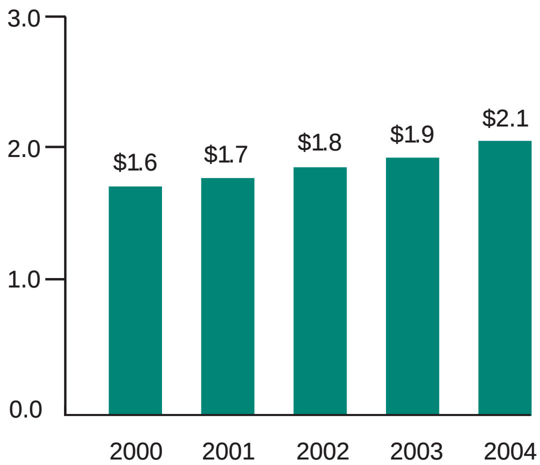
stockholders' AIRA. The remaining 90 percent is prorated into the banks' AIRAs. The earliest possible payout date is April 2006; however, any future AIRA payments are at the discretion of the Corporation's Board.

Investments

Investments increased 10.5 percent during the year to $2.1 billion at December 31, 2004.

Growth in Investment Portfolio

($ in billions)

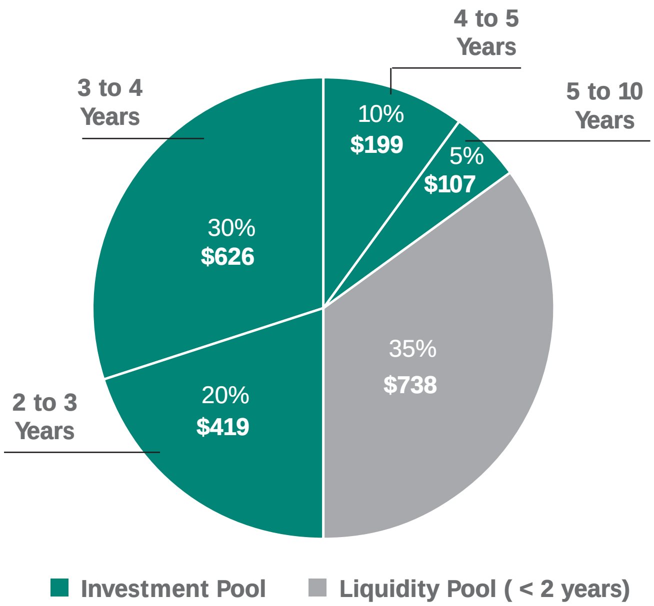


The Corporation's investment objective is to maximize returns consistent with liquidity needs and to minimize exposure to loss of principal. Funds are invested in U.S. Treasury securities in accordance with the Act and the Corporation's Investment Policy. During 2004, the investment yield dropped due to the lower interest rate environment that prevailed throughout the year. The average portfolio yield was 4.22 percent, down from 4.93 percent the prior year.

The Corporation's investment strategy is to purchase a ladder of maturities and hold them to maturity. The portfolio is comprised of a liquidity and an 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 2.63 years. The balances and maturities of the liquidity and investment pools at December 31, 2004, are illustrated in the following chart.

Investment Portfolio Maturity Groups

($ 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 and activities, including consolidations and new forms of financing. For example, in 2004, staff analyzed trends in System bank investments including those held in other Government Sponsored Enterprises. Staff also analyzed the effect on insurance risk from the proposed termination of one of the largest associations. This transaction ultimately was withdrawn.

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 renewed its working relationship with Mercer Oliver Wyman in 2004 to further the analysis conducted in 2003. Efforts focused on the development of a model to dynamically evaluate the adequacy of the Insurance Fund over a longer time period. As a result of this study, they concluded that the most significant factors affecting the Corporation's insurance risk exposure were:

1. System balance sheet growth,
2. Risk profiles 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. When considering providing financial assistance, the statute requires the Corporation to ensure that it is 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.

There are no receiverships or conservatorships in the Farm Credit 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 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. Periodically, the Corporation conducts readiness exercises to maintain its ability to serve in this capacity should the need arise.

Regulations and Policy

In June, we proposed 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 proposed 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 ERISA 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 of control. The proposed regulation also covers indemnity payments.

In August, we issued a joint letter with the Farm Credit Administration that establishes a limit on our special receivership and conservatorship powers. We agreed that the FCSIC, acting as receiver or conservator, would not exercise its authority to reclaim, recover or recharacterize as property of an institution in conservatorship or receivership any financial assets transferred in connection with a participation or securitization, as long as the transfer meets the necessary conditions for a “true sale” under generally accepted accounting principles. FCA has issued a proposed rule that would codify the position taken in the joint letter.

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 2004, the total Insurance Fund maintained the 2 percent secure base amount. Premium rates were adjusted to a blended rate of 5 basis points for the year due to moderating growth.

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. Also, the Corporation proactively screens the financials of all System institutions to detect risk and identify institutions that may require special examinations. As part of a program to evaluate risks, the Corporation is testing 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 2004. Corporation personnel are trained periodically to maintain readiness, ensuring proficiency in the performance of receivership responsibilities.

The President's Management Agenda

The Corporation is one of 35 agencies designated a significant Government entity for reporting purposes due to the size of the Insurance Fund. As a result, the Corporation is required to submit data for the *Financial Report of the United States* (FR) using the Governmentwide Financial Report System (GFRS) and the Federal Agencies' Centralized Trial-Balance System (FACTS I).

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

- Managed an organizational transition that filled three corporate officer positions while continuing to operate with a small, diversified staff focusing on core competencies.
- Used the commercial marketplace to keep operating costs low and contracted for specialized expertise when needed.
- Decreased compensation costs through staff transition and realignment.

2. Competitive Sourcing

- Continued the extensive use of competitively sourced contractor support to perform administrative functions including personnel, information systems, and financial systems support.
- Selected a new contractor for financial management services. The selected contractor offers a fully compliant system that is expected to meet the financial services needs for the Corporation. The new vendor's fee for system support and accounting services for 2005 will be approximately 20 percent below the previous contractor's costs in 2004.

3. Improved Financial Performance

- Managed an investment portfolio with an average yield of 4.22 percent, which compares favorably with the 2.5 percent return from similar private sector Treasury investment funds with durations of 10 years or less.
- Actual 2004 expenses were under budget.

4. Expanded Electronic Government

- Implemented the eGovernment Initiative for electronic travel services (eTS) ahead of schedule. Conversion to eTS is required by September 30, 2006 for all Federal agencies. The Corporation began using eTS January 1, 2005.

5. Budget and Performance Integration

- Provided timely and accurate financial information on a quarterly basis to assist senior management and the Board in making informed decisions regarding strategic programs and key operations.
- Evaluated programs on an ongoing basis to determine efficiency, and met new and growing demands without increasing permanent staff levels.

PRICEWATERHOUSECOOPERS

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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 the Farm Credit System Insurance Corporation (the "Corporation") at December 31, 2004 and 2003, 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 the 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 February 24, 2005 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, 2004. 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

February 24, 2005

PRICEWATERHOUSECOOPERS

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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 the Farm Credit System Insurance Corporation (the "Corporation") as of and for the year ended December 31, 2004, and have issued our report thereon dated February 24, 2005. 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 the 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, regulations, contracts and grant agreements, 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 the 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.

February 24, 2005

PricewaterhouseCoopers LLP

Statements of Financial Condition as of December 31, 2004 and 2003

($ in thousands)

	2004	2003
ASSETS		
Cash and Cash Equivalents	$ 2,279	$ 186
Investments in U.S. Treasury Obligations (Note 3)	2,087,702	1,899,095
Accrued Interest Receivable	27,505	28,807
Premiums Receivable (Note 4)	46,520	105,079
Other Receivables	0	4
TOTAL ASSETS	$ 2,164,006	$ 2,033,171
LIABILITIES AND INSURANCE FUND		
Accounts Payable and Accrued Expenses (Note 7)	$ 371	$ 361
Liability for Estimated Insurance Obligations (Note 5)	224,489	209,802
TOTAL LIABILITIES	224,860	210,163
Farm Credit Insurance Fund		
Allocated Insurance Reserve Accounts	39,888	39,888
Unallocated Insurance Fund Balance	1,899,258	1,783,120
TOTAL INSURANCE FUND	1,939,146	1,823,008
TOTAL LIABILITIES AND INSURANCE FUND	$ 2,164,006	$ 2,033,171

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

Statements of Income and Expenses and Changes in Insurance Fund for the Years Ended December 31, 2004 and 2003

($ in thousands)

	2004	2003
INCOME		
Premiums (Note 4)	$ 46,520	$ 105,079
Interest Income	86,567	91,405
Other Income	0	20
TOTAL INCOME	$ 133,087	$ 196,504
EXPENSES		
Administrative Operating Expenses (Note 7)	$ 2,263	$ 2,218
Provision for Estimated Insurance Obligations (Note 5)	14,686	13,725
TOTAL EXPENSES	$ 16,949	$ 15,943
NET INCOME	$ 116,138	$ 180,561
Farm Credit Insurance Fund Beginning of Year	1,823,008	1,642,447
Farm Credit Insurance Fund End of Year	$ 1,939,146	$ 1,823,008

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

Statements of Cash Flows for the Years Ended December 31, 2004 and 2003

($ in thousands)

	2004	2003
CASH FLOWS FROM OPERATING ACTIVITIES		
Net Income	$ 116,138	$ 180,561
Adjustments to Reconcile Net Income to Net Cash Provided by Operating Activities:		
Decrease (Increase) in Premium Receivable	58,559	(78,724)
Decrease (Increase) in Accrued Interest Receivable	1,302	(165)
Net Amortization and Accretion of Investments	21,443	25,200
Decrease (Increase) in Other Receivables	4	(4)
Increase in Accounts Payable and Accrued Expenses	11	100
Increase in Liability for Estimated Insurance Obligations	14,686	13,725
TOTAL NET CASH PROVIDED BY OPERATING ACTIVITIES	$ 212,143	$ 140,693
CASH FLOWS FROM INVESTING ACTIVITIES		
Payments for Purchase of U.S. Treasury Obligations	$ (496,266)	$ (475,903)
Proceeds from Maturity of U.S. Treasury Obligations	286,216	254,289
TOTAL NET CASH USED IN INVESTING ACTIVITIES	(210,050)	(221,614)
Net Change in Cash and Cash Equivalents	2,093	(80,921)
CASH AND CASH EQUIVALENTS BEGINNING OF YEAR	186	81,107
CASH AND CASH EQUIVALENTS END OF YEAR	$ 2,279	$ 186

The accompanying notes are an integral part of these 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, 2004, 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, 2004, for each of the components of the Corporation's insurance responsibilities were $100 billion of insured obligations, $325 million of FAC bonds (of which $15 million in repayments have been provided for), and $23 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, 2004, the Corporation held $2.23 million in overnight Treasury Certificates maturing on January 3, 2005, with an investment rate of 1.65 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 of 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 2004 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 $145,573 in 2004 and $141,245 in 2003.

Note 3 — Investments

At December 31, 2004 and 2003, investments in U.S. Treasury obligations consisted of the following:

($ in thousands)

December 31, 2004	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Market Value
U.S. Treasury Notes	$2,087,702	$34,626	$(9,955)	$2,112,373
December 31, 2003				
U.S. Treasury Notes	$1,899,095	$81,525	$(2,889)	$1,977,731

The amortized cost and estimated market value of U.S. Treasury obligations at December 31, 2004, by contractual maturity, are shown below.

($ in thousands)	Amortized Cost	Estimated Market Value
Due in one year or less	$ 377,356	$ 380,847
Due after one year through five years	1,602,963	1,624,771
Due after five years through 10 years	107,383	106,755
	$ 2,087,702	$ 2,112,373

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 four 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 0.0015; (2) average annual nonaccrual loans outstanding may be from zero to 0.0025; (3) average annual portions of Federal Government-guaranteed accrual loans may be from zero to 0.00015; and (4) average annual portions of state government-guaranteed accrual loans may be from zero to 0.0003.

Insurance premium rates are reviewed semiannually in March and September. For 2004, premium rates were set at the Board's September 2003 meeting at 10 basis points for accrual loans, 25 basis points for non-accrual loans and zero for Federal and state government guaranteed loans. Due to moderate growth in insured debt outstanding, in September 2004, the Board decreased the insurance premium rate on accrual loans to zero basis points beginning July 1, 2004, and left other rates unchanged. The Board deferred setting premium rates for 2005 until January 13, 2005, when the Board set the rate for accrual loans at 4 basis points. The rates for non-accrual loans remained at 25 basis points and for Government-guaranteed loans zero basis points. 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 amount of the Insurance Fund exceeds the secure base amount, the Corporation is required to reduce the premiums, but it still must ensure that reduced premiums are sufficient to maintain the level of the Insurance Fund at the secure base amount.

The unallocated Insurance Fund was below the secure base amount during most of 2004. At December 31, 2004, the unallocated Insurance Fund was 1.97 percent of adjusted insured obligations outstanding. 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 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 AIRAs, which provides guidelines for implementing this statutory authority.

At December 31, 2003, because the Insurance Fund was at the 2.0 percent secure base amount, the Corporation determined that there were balances to allocate. To determine the amount to allocate, the statute requires the Corporation to recalculate the secure base amount on an average daily balance basis and compare that with the yearend Insurance Fund balance adjusted downward by the Corporation's estimated expenses for the following year.

The amount of Insurance Fund balance to be allocated to the Allocated Insurance Reserve Accounts was determined to be $39.89 million as follows:

FAC Stockholders	(10%)	$ 3.99 million
Farm Credit System Banks	(90%)	$35.90 million
		$39.89 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. Consequently, the unallocated Insurance Fund balance was reduced to 1.96 percent of adjusted insured obligations at December 31, 2003.

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 1992, 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 statutorially authorized purposes. From 1998 through 2004, $936 million in FAC bonds have been retired, leaving one remaining issue of $325 million outstanding, which matures in June 2005. Repayment of the remaining FAC bond in accordance with the Act is being provided for by the FAC Trust Fund (Trust Fund), FAC Assistance Fund and the Insurance Corporation. (See *Estimated Insurance Obligation* on the following page.)

Financial Assistance to Certain System Banks

During the period from 1988 to 1992, assistance was provided to four open banks through the purchase by the FAC of $419 million in preferred stock issued by these institutions. Similar assistance totaling $374 million was provided to the Federal Land Bank of Jackson in Receivership to facilitate its closing and liquidation. Subject to Assistance Board approval, these assistance funds were used by the FAC to purchase preferred stock issued by an institution experiencing financial difficulty.

Prior to the maturity of the related 15-year debt obligations, each institution can redeem its preferred stock, pursuant to Section 6.26 of the Act, so as to allow the FAC to pay the principal of the maturing obligation. While an institution that issues preferred stock to the FAC is primarily responsible for providing funds for payment of the FAC bonds (through redemption of the preferred stock), the institution may be prohibited from redeeming, or may elect not to redeem, the preferred stock pursuant to section 6.26 of the Act. If this occurs, then the FAC must use funds from its Trust Fund, to the extent available, to retire the debt. The Trust Fund represents the funds received from System institutions' purchase of stock in the FAC. The Trust Fund totaled approximately $79 million and $74 million at December 31, 2004 and 2003, respectively. The Trust Fund is composed of zero coupon Treasury securities which mature in 2005 and have a par value of $79 million. The FAC also must use funds from its Assistance Fund that totaled $15 million at December 31, 2004, to retire the remaining FAC bond. If the FAC Trust Fund and Assistance Fund balances are not sufficient to retire the FAC debt, then the Corporation must purchase preferred stock from the FAC to provide funds to retire such debt.

If the Corporation does not have sufficient funds, the U.S. Treasury must retire the debt. If this should occur, the Corporation is required to repay the U.S. Treasury as funds become available from the payment of premiums. At December 31, 2004, the only preferred stock held by the FAC was associated with the assistance provided to the Federal Land Bank of Jackson.

On May 20, 1988, the FCA placed the Federal Land Bank of Jackson and the Federal Land Bank Association of Jackson in Receivership (collectively the FLBJR) and appointed a receiver to liquidate their assets. As of April 27, 1990, the FCA, the receiver of the FLBJR, the FAC, the System banks, the Assistance Board, and the Corporation entered into an agreement which called for the FAC to issue 15-year U.S. Treasury-guaranteed bonds to purchase preferred stock in the FLBJR. Upon the maturity in 2005 of the FAC bonds used to purchase preferred stock in the FLBJR, the Corporation will provide funds to repay the principal of these debt obligations, to the extent that the Trust Fund is not sufficient for such purpose. In January 1995, the FLBJR was terminated by the FCA and the receiver was discharged after transferring the remaining receivership assets to the FAC.

Estimated Insurance Obligation

The Corporation estimated the present value of its liability to provide funds for payment of the $231 million non-callable 15-year maturing debt to be approximately $224 million and $210 million at December 31, 2004 and 2003, respectively. This liability is reflected in the accompanying statements of financial condition. The present value of this obligation is 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 has been estimated by management using discount rates based upon U.S. Treasury securities of similar durations (2.4 percent for 2004 and 1.4 percent for 2003). The fair value was approximately $229 million and $227 million as of December 31, 2004 and 2003, respectively. Provisions for changes in the Corporation's liability are reflected in the statements of income and expenses in the amount of $14.7 million and $13.7 million for the years ended December 31, 2004 and 2003, respectively. The Corporation cannot predict the effects of future events upon System operations and upon the amount of the Trust Fund that will ultimately be available to reduce the Corporation's liability for FLBJR-related FAC bonds.

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 must repay Treasury for this obligation following the final maturity in June 2005 of the last FAC bond issue outstanding.

The 1992 Act also 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 is also required to satisfy defaults on the annual payments to the FAC to permit the repayment of Treasury-paid interest. During 1992 through 2004, all System banks made their annual annuity payments as scheduled. The Corporation is not aware of any events or circumstances which will prevent System banks from meeting their remaining FAC obligations.

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 FLBJR, as described above, 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 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 $118,938 for 2004, $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 $120,795 and $111,717 for 2004 and 2003, respectively.

Note 7 — Related Parties

The Corporation purchases services from the FCA under an Interagency Agreement. These include examination and administrative support services. The Corporation had payables due to the FCA of $1,687 at December 31, 2004, and $39,351 at December 31, 2003. The Corporation purchased services for 2004 which totaled $70,332 compared with $74,506 for 2003.

The Corporation provided assistance to the FCA under a related Interagency Agreement, recognizing revenue in 2003 of $19,765. At December 31, 2004 and 2003, the Corporation had receivables from the FCA of zero and $4,515, respectively.

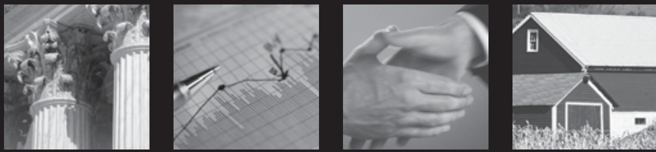
Income and Expenses

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	0	$ 118	$ 80,923
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

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 effective 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

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 Communications 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
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