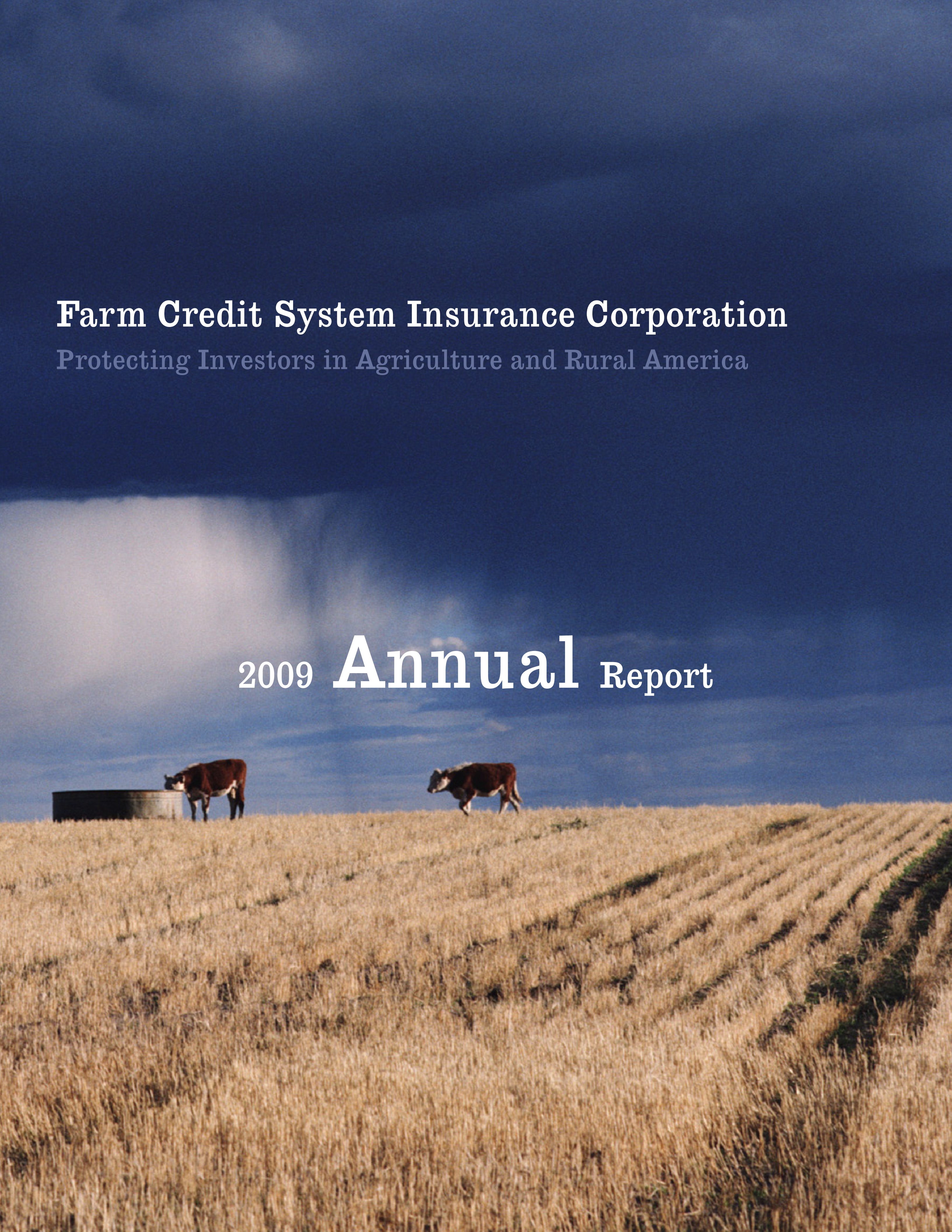
Farm Credit System Insurance Corporation

Protecting Investors in Agriculture and Rural America

2009 Annual Report



Mission Statement

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

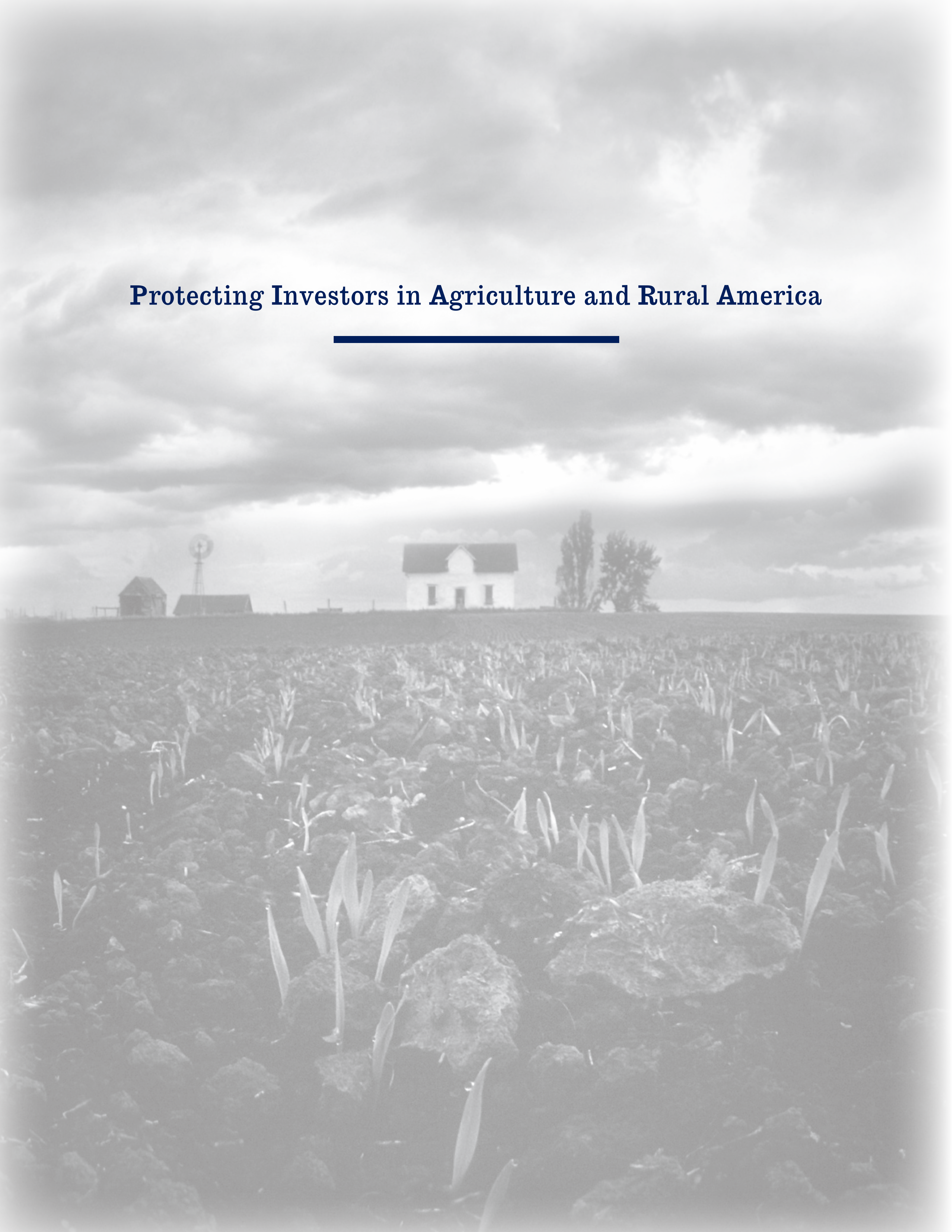
- *protect investors in insured Farm Credit System obligations and taxpayers through sound administration of the Farm Credit Insurance Fund,*

- *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



FARM CREDIT SYSTEM INSURANCE CORPORATION

May 19, 2010

Dear Mr. President and Madam Speaker:

In accordance with section 5.64 of the Farm Credit Act of 1971, as amended, the Farm Credit System Insurance Corporation is pleased to submit its annual report for calendar year 2009.

This report highlights the Corporation's role as the independent Federal corporation established to ensure the timely payment of principal and interest to investors in insured Farm Credit System debt securities. The balance in the Farm Credit Insurance Fund at December 31, 2009, was $3.3 billion. The Corporation collected $319 million in insurance premiums from Farm Credit System banks for 2009, earned $57 million in investment income during the same period, and expects to incur $3.9 million in operating costs in 2010.

Sincerely,

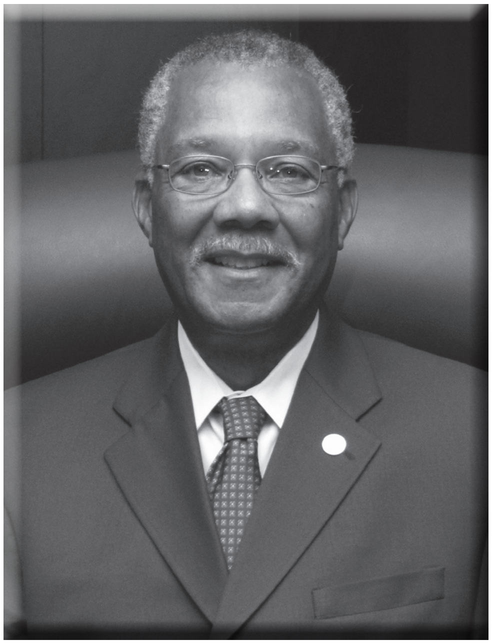
Kenneth A. Spearman
Chairman

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

Board of Directors

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

Kenneth A. Spearman



Kenneth A. Spearman was elected Chairman of the Board of Directors of the Farm Credit System Insurance Corporation on November 4, 2009. He also serves as a member of the Board of the Farm Credit Administration, having been appointed by President Barack Obama on October 13, 2009.

Mr. Spearman brings to his position as Chairman of the FCSIC many years of experience in finance, agriculture, and agricultural cooperatives. He spent 28 years in the citrus industry.

From 1980 to 1991, he was controller of Citrus Central, a $100 million cooperative in Orlando, Florida, where he was responsible for financial management and reporting and the supervision of staff accountants.

He later served as director of internal audit for Florida's Natural Growers, where he designed and implemented the annual plan for reviewing and appraising the soundness, adequacy, and application of accounting, financial, and other operating internal controls.

From January 2006 until his appointment to the FCSIC Board of Directors, Mr. Spearman served as an independently appointed outside director on the AgFirst Farm Credit Bank board in Columbia, South Carolina. During his tenure, he served on the board compensation committee and the board governance committee.

Before entering agriculture, Mr. Spearman was involved with development of a public accounting firm in Chicago, Illinois, and worked as an accountant for a major public accounting firm. He served as chairman of the board of trustees for the Lake Wales Medical Center. He is a member of the Institute of Internal Auditors, as well as the National Society of Accountants for Cooperatives, where he served at one time as president.

He obtained his master's degree in business administration from Governors State University in University Park, Illinois, and his B.S. in accounting from Indiana University.

Mr. Spearman and his wife Maria of Winter Haven, Florida, have three children—twin daughters, Michelle Springs and Rochelle Puccia, and a son, Dr. Kenneth Spearman.

Leland A. Strom

Leland A. Strom was appointed to the Farm Credit System Insurance Corporation Board of Directors and to the Farm Credit Administration Board by President George W. Bush on December 12, 2006, for a term that expires on October 13, 2012. He served as Chairman of the FCSIC Board until he was appointed Chairman and CEO of the Farm Credit Administration on May 22, 2008.

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

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

Other boards on which Mr. Strom has served include Northern F.S., Inc., a farm service and supply cooperative serving farmers in Northern Illinois; AgriBank, FCB; and the Farm Credit Council, the national trade organization representing the Farm Credit System in Government affairs.

Mr. Strom has served in several capacities with the Illinois Farm Bureau. He also served on his county Farm Bureau board. He was a member of the State Young Farmer Committee from 1981 to 1985. For his overall involvement in agriculture, he received an Outstanding Young Farmer Award.

In his community of Kane County, Illinois, which lies at the edge of suburban Chicago, Mr. Strom helped develop a farmland preservation program. The original Strom Family Farm was the first to be dedicated to permanent agricultural use under the program.

Mr. Strom studied agriculture business at Kishwaukee College and business administration at Northern Illinois University. He was a member of the Illinois Agricultural Leadership Program Class of 1988. His community involvement includes having served as vice president of his local K–12 school district, chairman of his church council, 4-H parent leader, and coach of boys' and girls' sports teams.

Mr. Strom owns a third-generation family farm in Illinois that produces corn and soybeans. He and his wife, Twyla, have two sons, a daughter, and a daughter-in-law.

Jill Long Thompson

Jill Long Thompson is a member of the FCSIC Board of Directors. She also serves as a member of the Farm Credit Administration Board.

Ms. Long Thompson was appointed to both boards by President Barack Obama on March 27, 2010. Her recess appointment is effective through the end of the 2011 legislative session.

Ms. Long Thompson brings to her position on the FCSIC and FCA Boards many years of leadership experience. From 1989 to 1995, she represented northeast Indiana as a Member of the U.S. House of Representatives, serving on the Agriculture Committee and the Committee on Veterans' Affairs. As congresswoman, she introduced one of the nation's first pieces of legislation banning members of Congress from accepting gifts; this legislation also expanded disclosure requirements for lobbying activities.

From 1995 to 2001, she served as Under Secretary for Rural Development in the U.S. Department of Agriculture, where she oversaw an annual budget of $10 billion and a staff of 7,000 employees. In this position, she managed programs that provide services to the underserved areas of rural America.

In addition, Ms. Long Thompson served as chief executive officer and senior fellow at the National Center for Food and Agricultural Policy, a nonprofit research and policy organization in Washington, D.C.

The first and only woman to be nominated by a major party to run for Governor of Indiana, Ms. Long Thompson is also the first and only Hoosier woman to be nominated by a major party to run for the U.S. Senate. She was nominated by the President on October 15, 2009, for a term on the FCA Board and the FCSIC Board of Directors ending May 21, 2014, and is awaiting confirmation by the U.S. Senate.

Ms. Long Thompson also has many years of experience as an educator, having taught at Indiana University, Valparaiso University, and Manchester College. She is also a former fellow at the Institute of Politics at Harvard University's John F. Kennedy School of Government. She holds the M.B.A. and Ph.D. in Business from the Kelley School of Business at Indiana University and a B.S. in Business Administration from Valparaiso University.

Ms. Long Thompson grew up on a family farm outside of Larwill, Indiana; today she lives with her husband Don Thompson on a farm near Argos, Indiana.

2009 – Year in Review

Changes to FCSIC Board of Directors

On November 4, 2009, Kenneth A. Spearman was elected Chairman of FCSIC. Nancy C. Pellett served as the Corporation's Chairman from June 4, 2008, to November 3, 2009. Ms. Pellett played a key role in implementing the new premium authorities the Corporation obtained in the Food, Conservation, and Energy Act of 2008 (FCE Act). On October 15, 2009, President Barack Obama nominated former Indiana Congresswoman Jill Long Thompson to the Board of Directors. On March 27, 2010, President Obama announced his recess appointment of Ms. Long Thompson to the position previously held by Ms. Pellett, whose term had expired.

Insurance Fund Reaches the Statutory 2 Percent Secure Base Amount

For the first time since year-end 2003, at December 31, 2009, the unallocated portion of the Farm Credit Insurance Fund (Insurance Fund or Fund) reached the statutory 2 percent secure base amount (SBA). A combination of factors contributed to this event. Systemwide debt stopped growing after four years of double-digit increases. Changes to the Corporation's premium authority in 2008 allowed a deduction in the calculation of the SBA for full faith and credit Government-guaranteed investment securities. The FCE Act gave the Corporation enhanced premium authority which the Corporation used to increase the annual amount of insurance premiums collected. As a result of these factors, the unallocated portion of the Insurance Fund finished the year with an excess balance of $169 million above the SBA.

Allocated Insurance Reserves Accounts – Additional Allocations and Payments to Accountholders

In accordance with the Farm Credit Act's requirements, the Corporation transferred $165.4 million to the Allocated Insurance Reserves Accounts (AIRAs) at year-end 2009. Separate AIRAs have been established for each bank and a special account has been established for the holders of Farm Credit System Financial Assistance Corporation (FAC) stock. The first 10 percent of calculated excess funds were deposited to the AIRA of FAC stockholders. The remaining 90 percent was prorated into the banks' AIRAs.

On January 22, 2010, the FCSIC's Board authorized the payment of $39.9 million from the AIRAs to the accountholders. This amount, which had been transferred to the AIRAs at year-end 2003, (the last time the unallocated Insurance Fund exceeded the SBA at year-end), was paid in February 2010. In making its decision to pay out the funds, the Board considered a number of factors including the following:

- Current level of the Insurance Fund and projections for growth in insured obligations
- Likelihood and probable amount of any losses to the Insurance Fund
- Financial condition of the Farm Credit System banks and associations
- Health and prospects for the agricultural economy
- Risks in the financial environment that could cause problems, including volatility of interest rates, increased competition, and use of sophisticated investment securities and derivatives

(See Note 7 to the Financial Statements for additional details on the payment.)

Strategic Plan Update

The Corporation's strategic plan defines its mission, goals, and the means by which it measures progress in addressing problems, needs, or challenges related to its mission over the course of five years. The plan evaluates FCSIC's capabilities, assesses the operating environment, and provides for evaluation of its strategy for dealing with internal and external challenges and risks that may hinder the accomplishment of its mission.

In 2009, FCSIC hosted two strategic planning conferences, facilitated by former Congressman Charles W. Stenholm, to gain insight from industry professionals and System representatives regarding issues that may be important to the System. Presentations covered various topics including the housing market, bank liquidity issues, financial product ratings, Federal Reserve Board policy, and the need for System banks to have access to a temporary liquidity pool in situations where external market forces make normal debt market access difficult or impossible. Discussion of these topics helped formulate FCSIC's 2010-2015 Strategic Plan.

Selected Financial Statistics

Farm Credit System Insurance Corporation

(Dollars in Millions)

	2009	2008	2007
BALANCE SHEET:			
Total Assets	**$ 3,288.6**	$ 2,914.9	$ 2,598.9
Total Liabilities	**0.9**	0.3	0.4
Insurance Fund Balance			
Allocated Insurance Reserves Accounts	**205.3**	39.9	39.9
Unallocated Insurance Fund Balance	**3,082.4**	2,874.7	2,558.6
OPERATIONS:			
Revenues	**376.1**	318.7	289.7
Operating Expenses	**3.0**	2.6	2.7
Insurance Expense	**-0-**	-0-	-0-
Net Income	**373.1**	316.1	287.0

The Farm Credit System

Structure and Funding

The System is owned by rural customers it serves, including farmers, ranchers and other agricultural producers. As of December 31, 2009, there were 89 FCS associations that lend directly to these owner-borrowers, providing a consistent source of agricultural and rural credit throughout the United States and the Commonwealth of Puerto Rico. Each association has its own chartered territory and is affiliated with one of the five FCS banks. The banks primarily receive their funding through the issuance of Federal Farm Credit Banks Consolidated Systemwide Debt Securities (Systemwide debt securities or insured debt). These securities are issued through 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

Investors provide the funds the System lends to agriculture and rural America. The Corporation's primary purpose, as defined by the Farm Credit Act, is to insure timely payment of principal and interest on insured debt securities to these investors.

Regulatory Oversight

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

Combined Farm Credit System Statistics

(Dollars in Billions)

	2009	2008	2007
Insured Debt Outstanding[1]	**$177.1**	$177.4	$155.3
Production Agriculture:			
Real Estate Mortgage Loans	**75.4**	71.9	63.5
Production and Intermediate-term Loans	**39.6**	37.5	32.3
Agribusiness Loans[2]	**23.6**	26.9	28.1
Communication Loans	**3.9**	4.5	3.4
Energy, Water and Waste Disposal Loans	**10.7**	9.4	7.5
Rural Residential Real Estate Loans	**5.0**	4.6	4.0
International Loans	**4.0**	4.1	2.1
Lease Receivables	**2.2**	1.9	1.7
Loans to Other Financial Institutions	**0.6**	0.6	0.4
Cash and Investments	**42.2**	43.8	36.5
Net Income	**2.85**	2.92	2.70
Nonperforming Loans as a Percentage of Total Loans	**2.1%**	1.5%	0.4%

1. Insured Debt Outstanding is based on System institution call report information and reflects the book value of insured debt outstanding, excluding fair value adjustments plus accrued interest as of December 31, 2009.
2. At December 31, 2009, agribusiness loans consisted of loans to cooperatives of $10.5 billion, processing and marketing loans of $11.0 billion, and farm-related business loans of $2.1 billion.

Insured and Other Obligations

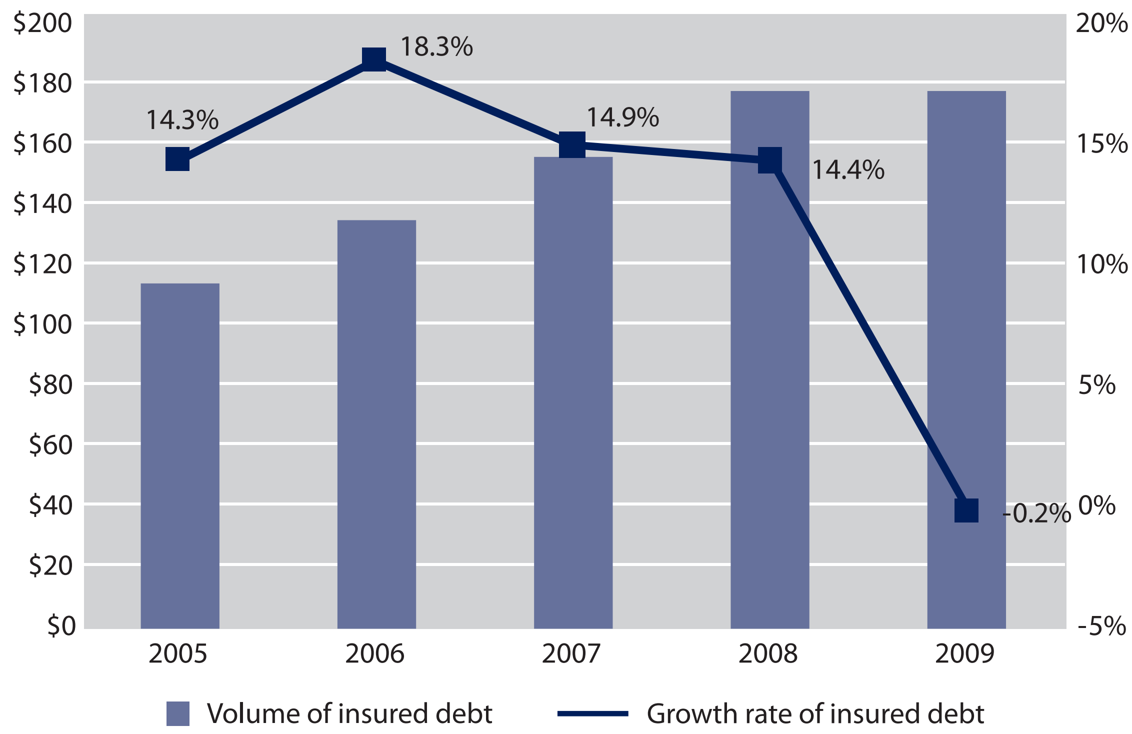
The Corporation insures Systemwide and consolidated bonds, notes, and other obligations issued by the insured System banks through the Funding Corporation under section 4.2 (c) or (d) of the Farm Credit Act. As figure 1 shows, insured debt outstanding decreased less than 1 percent in 2009 to $177.1 billion. From 2005 to 2009, insured debt outstanding grew at an average annual rate of approximately 12.3 percent.

The Corporation is also required by statute to ensure the retirement of eligible borrower stock, as defined in section 4.9A of the Farm Credit Act, at par value. This stock, also known as protected borrower stock, was outstanding prior to October 6, 1988. At year-end 2009, eligible borrower stock outstanding at System institutions totaled $8 million, down from $10 million at year-end 2008.

Figure 1

Insured Debt Outstanding[1] 2005 to 2009

(Dollars in Billions)



1. Insured Debt Outstanding is based on System institution call report information and reflects the book value of insured debt outstanding, excluding fair value adjustments plus accrued interest as of December 31, 2009.

Farm Credit System Capital

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

As figure 2 shows, the amount of FCS bank capital and the balance in the Insurance Fund together increased 44 percent from $9.8 billion at year-end 2005 to $14.1 billion at year-end 2009. Bank capital plus the amount in the Insurance Fund as a percentage of outstanding insured debt decreased from 8.5 percent in 2005 to 7.0 percent in 2008 but increased in 2009 to 8.0 percent (see figure 3). The rate of growth in debt outstanding outpaced growth in bank capital and the Insurance Fund between 2005 and 2008 but declined in 2009 as System institutions reduced overall levels of loan growth. The System's increased profitability between 2005 and 2008 was primarily attributed to loan growth, while profitability in 2009 was primarily attributed to the increase in the net interest spread from favorable loan and debt pricing. The financial performance and condition of the System on a combined basis remains strong, though some individual institutions have experienced significant stress from credit deterioration in certain agricultural sectors as well as from continued stress in the general economy. (See trends in Financial Institution Rating System ratings in the Risk Management section.)

FCS associations have been building capital through the net income they have earned and retained. Association capital helps reduce the credit exposure of the association's affiliated bank. As figure 4 shows, from 2005 to 2009, combined association capital increased $5.1 billion or 33.6 percent with an annual average increase of approximately 7.4 percent. From 2005 to 2008, growth in association assets outpaced growth in capital, causing a steady decline in association capital as a percentage of total assets, from 17.2 percent to 15.5 percent (see figure 5). In 2009, associations collectively preserved capital, causing a slight increase in association capital as a percentage of total assets to 15.8 percent.

Figure 2

Bank Capital Plus Insurance Fund

(Dollars in Billions)

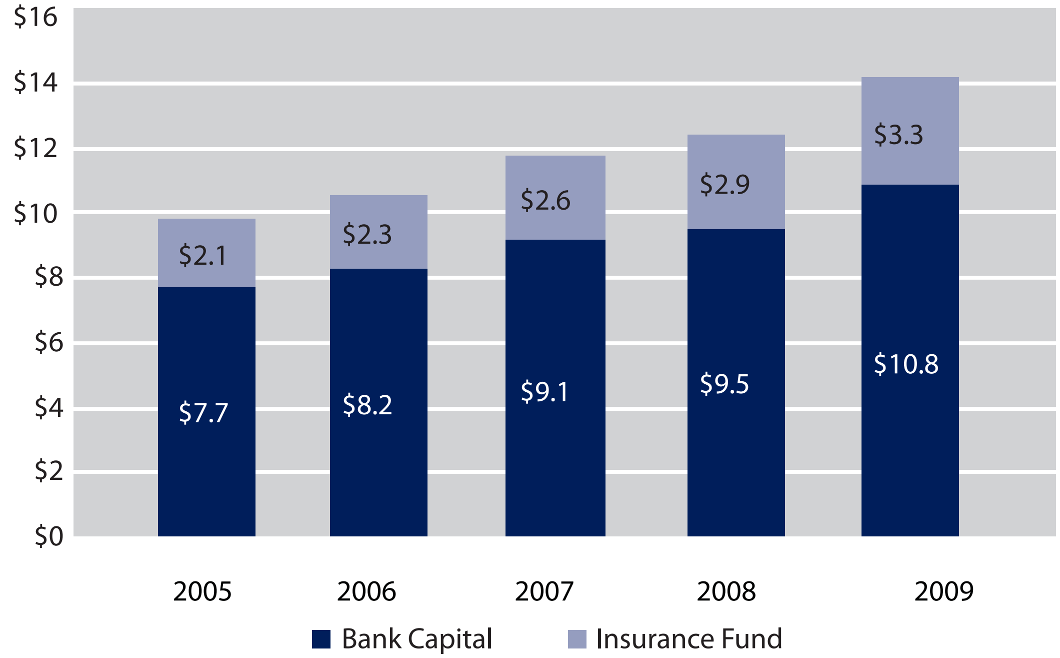


Figure 3

Bank Capital Plus Insurance Fund as Percentage of Insured Debt

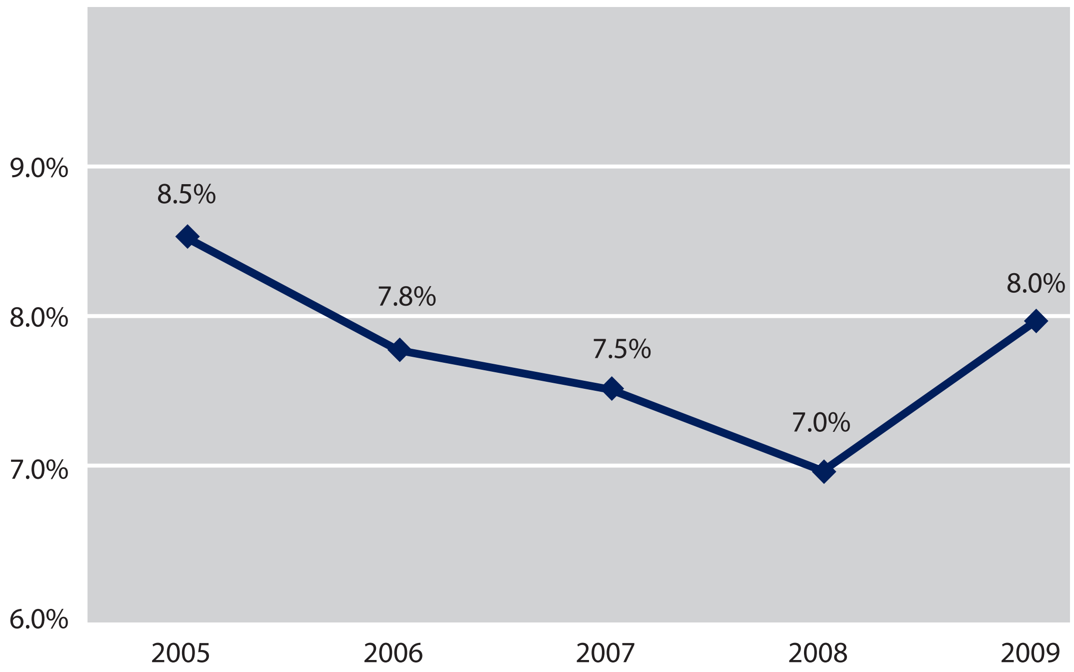


Figure 4
Association Capital
(Dollars in Billions)

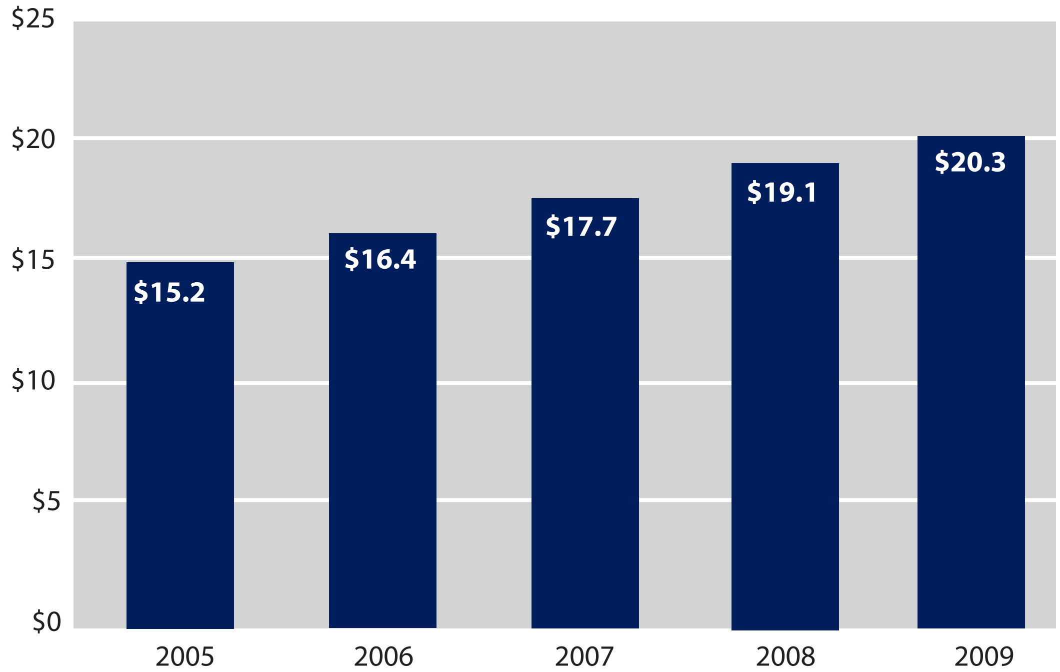
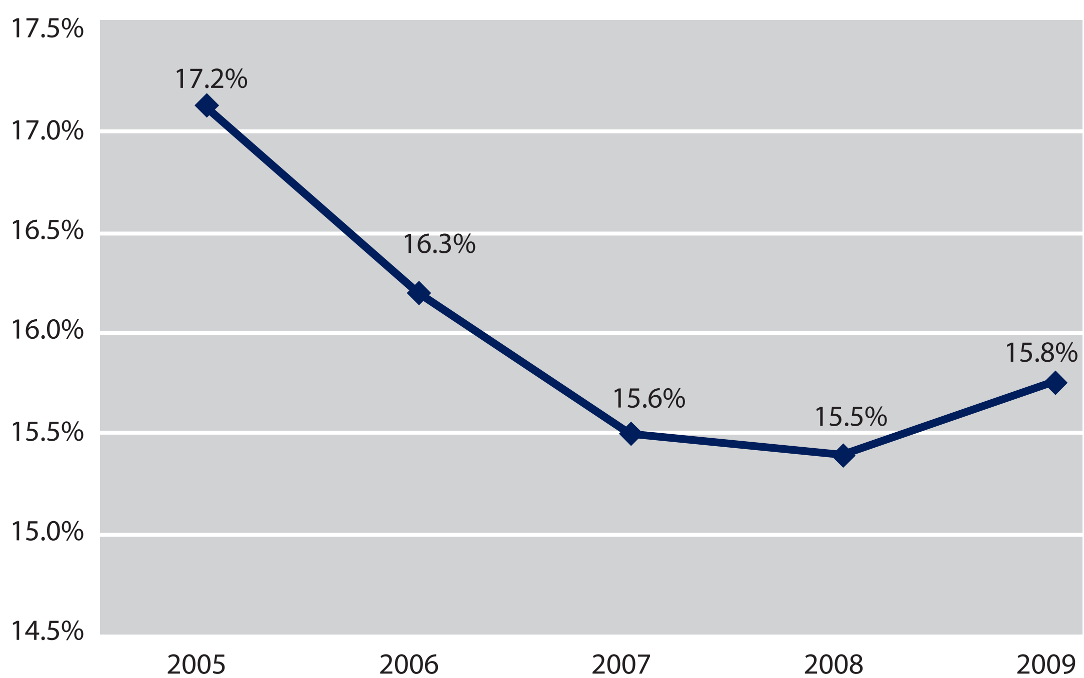


Figure 5
Association Capital as a Percentage of Total Assets



Additional Protections

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

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

The System also has a common minimum liquidity standard. The standard requires each bank to have enough liquidity to operate for at least 90 continuous days without access to the capital markets. For additional information, please see the discussion in the Risk Management section.

Insurance Fund Management

The Insurance Fund and the Secure Base Amount

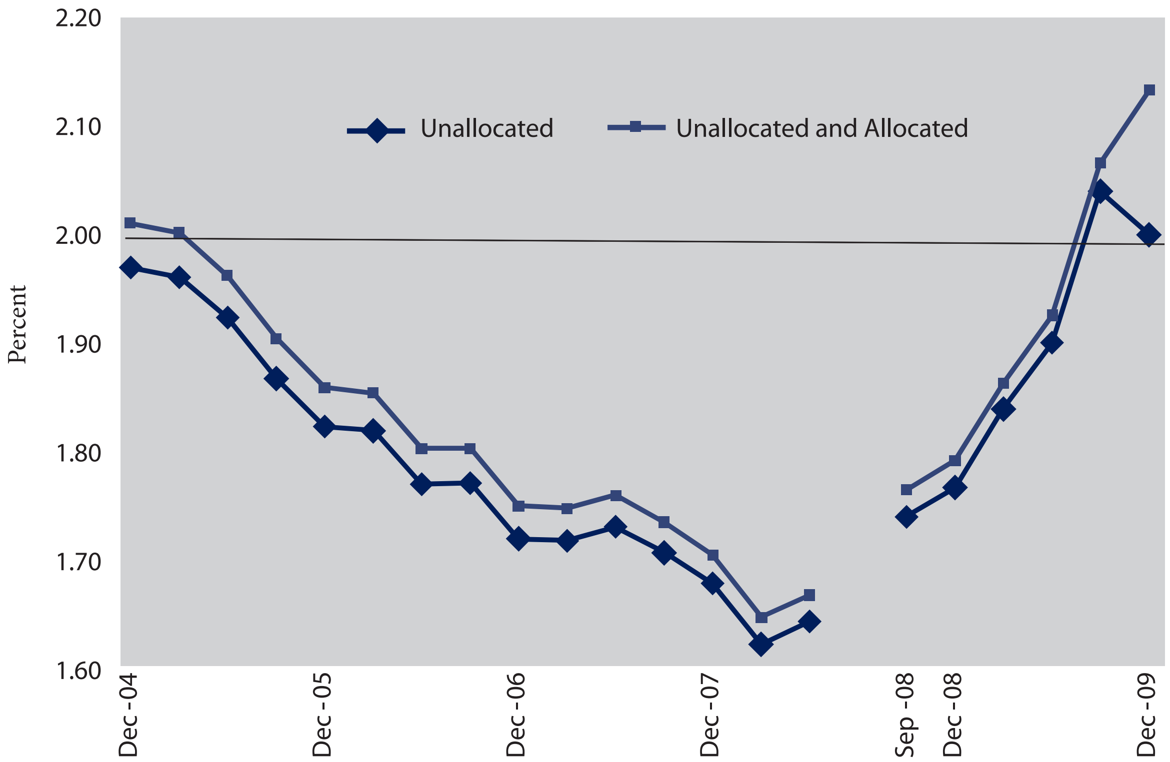
In 2009, both the total Insurance Fund and total assets grew 12.8 percent to $3.3 billion. Over the last five years, the total Insurance Fund and total assets grew at an annual rate of 11.2 percent and 9.0 percent, respectively. In 2009, the Corporation did not accrue a provision for insurance obligations.

The Insurance Fund represents the Corporation's equity, the difference between total assets and total liabilities, including insurance obligations. The Insurance Fund is composed of an unallocated Insurance Fund (the assets in the Insurance Fund for which no specific use has been identified or designated) and an allocated Insurance Fund. Premiums are due until the unallocated portion of the Insurance Fund reaches the SBA. The SBA established by the Farm Credit Act is 2 percent of the aggregate outstanding insured obligations (adjusted to exclude a part of certain Government-guaranteed loans in accrual status and non-impaired Government-guaranteed investments), or another percentage that the Board determines to be actuarially sound.

The unallocated Insurance Fund reached the SBA in 2009 in part because FCSIC promptly implemented new authority the 2008 FCE Act gave it to impose premiums ranging from 0 to 20 basis points on insured debt obligations rather than loans. In addition, growth in insured debt outstanding slowed significantly during 2009. During 2009, insured debt declined by less than 1 percent, well below the previous year's rate of growth of 14.4 percent, and below the five-year average annual growth rate of 12.3 percent. Prior to allocation to the AIRAs, the unallocated Insurance Fund finished 2009 above the 2 percent SBA at 2.11 percent, or $169 million above the SBA. Including the existing AIRAs balances raised the level of the total Insurance Fund to 2.14 percent or $209 million above the SBA. The AIRA balance is recorded as part of the Insurance Fund and is available to satisfy insurance obligations until the Corporation disburses payment to the Farm Credit banks and FAC stockholders (see figure 6).

Figure 6

Insurance Fund Relative to 2 Percent Secure Base Amount



Note: A change in the SBA calculation methodology was included in the FCE Act. The new methodology, which was implemented on July 1, 2008, allows the deduction of a portion of Federal and State-guaranteed investments from the SBA in a manner similar to that used for Federal and State-guaranteed loans.

Premiums

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

- The level of the Insurance Fund relative to the secure base amount
- Projected losses to the Insurance Fund
- The condition of the System
- The health of the agricultural economy
- Risks in the financial environment

The most important factor in determining premium rates for 2009 was the level of the Insurance Fund relative to the SBA. The Insurance Fund remained below the SBA until September 2009. As a result, the Board maintained the premium assessment at 20 basis points on adjusted insured debt. By statute, this was the maximum rate that could be charged. (Note: 1 basis point (bp) = 1/100 of 1 percent.)

Enactment of the FCE Act in 2008 amended the premium provisions of the Farm Credit Act to, among other things, base premiums on the adjusted outstanding insured debt obligations instead of on loans, and to permit the Corporation to collect a broader range of premiums on insured debt.

The amendments reduce the total insured debt obligations on which premiums are assessed by 90 percent of Federal Government-guaranteed loans and investments and 80 percent of State Government-guaranteed loans and investments; the same deductions apply when the SBA is calculated. If the Insurance Fund is below the SBA, the Farm Credit Act requires that each insured System bank pay FCSIC a premium equal to (a) the adjusted average outstanding insured obligations multiplied by 0.0020 and (b) the average principal outstanding on loans in nonaccrual status and average amount outstanding of other-than-temporarily impaired investments multiplied by 0.0010. The premium may be reduced at FCSIC's sole discretion. Once the Insurance Fund exceeds the SBA, the law requires that premiums be reduced to the level necessary to maintain the Fund at the SBA (i.e., 2 percent of adjusted outstanding insured obligations).

From January 1, 2009, to December 31, 2009, premiums were assessed at 20 basis points on adjusted insured debt, plus 10 basis points on the average nonaccrual loans and other-than-temporarily impaired investments.

Revenues and Expenses

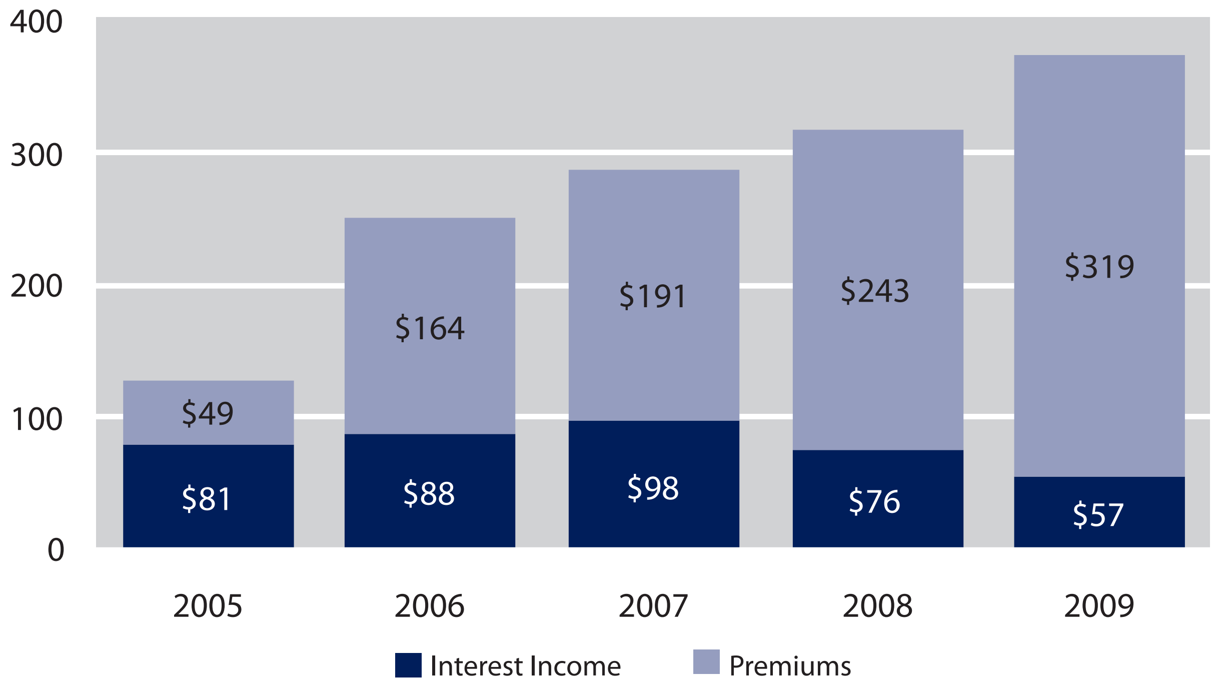
Revenues in 2009 increased 18 percent to $376 million from $319 million in 2008 (see figure 7). The increase in net income resulted from higher premiums. Because of a decrease in the rate of return on the U.S. Treasury securities held in the Corporation's portfolio, interest income decreased 24 percent in 2009 to $57 million from $76 million in 2008.

The Corporation's operating costs as a percentage of its total assets represented 9 basis points for 2009. Fixed costs for staff, travel, rent, and miscellaneous expenses were $2.2 million of the $3 million total for the year. The remaining expenses of $0.8 million were for contract services.

Figure 7

Corporation Revenues

(Dollars in Millions)



Investments

Investments increased 11 percent during the year from $2.7 billion at December 31, 2008, to $2.9 billion at year-end 2009. See figure 8.

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 Farm Credit Act and the Corporation's investment policy.

The average portfolio yield was 2.0 percent, down from 2.9 percent the prior year. The return on the Insurance Fund continued to outperform the benchmark index the Corporation uses to measure performance. This index is composed of Treasuries and private sector mutual funds with holdings of similar type and duration to the Corporation's portfolio. The average return of the benchmark group was 1.4 percent for 2009.

In accordance with the Corporation's investment policy, the portfolio is composed of a liquidity pool and an investment pool. The liquidity pool consists of short-term Treasury securities maturing in less than two years. The investment pool is composed of Treasury securities with maturities that vary from 2 to 10 years. The FCSIC investment policy requires at least 20 percent of the portfolio to be maintained in the liquidity pool, and allows a maximum of 25 percent to be invested in securities with maturities between 5 and 10 years. The weighted average portfolio maturity at year-end was 2.1 years. The composition of the investment portfolio at December 31, 2009, is illustrated in figure 9.

In June 2008, the Corporation purchased Treasury Inflation-Protected Securities (TIPS). Evaluation Associates' (EA), which had completed a study of FCSIC's investment program, recommended FCSIC consider purchasing TIPS to help FCSIC improve the diversity of its investments and to hedge against future inflation. At year-end 2009, FCSIC's TIPS investments totaled $520 million or just over 17.7 percent of the investment portfolio.

Figure 8

Growth in Investment Portfolio

(Dollars in Billions)

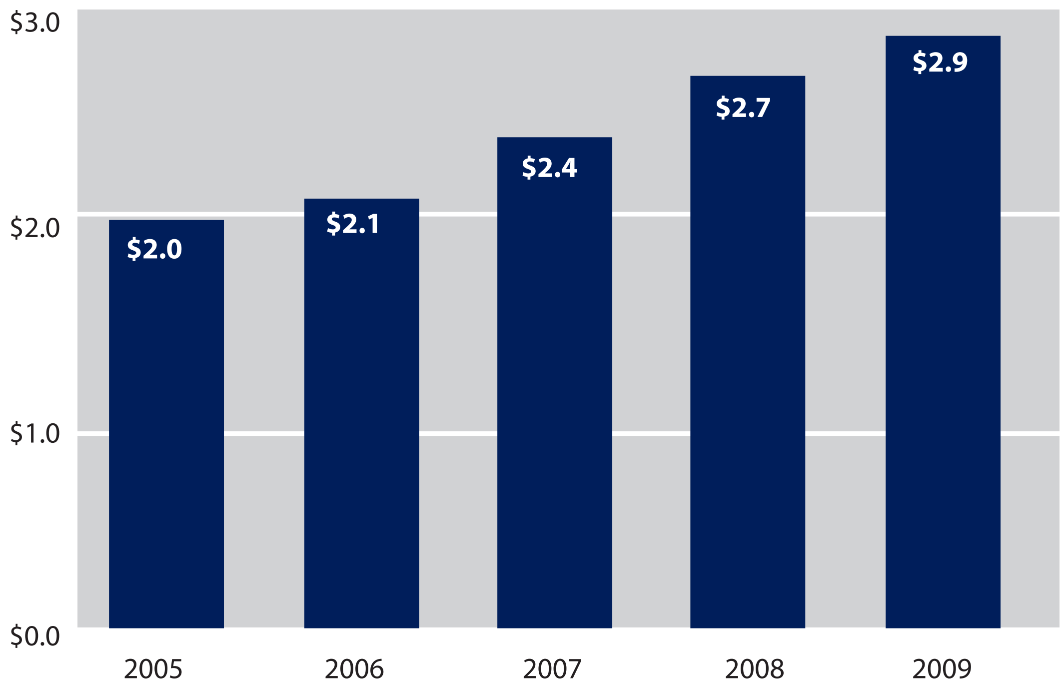
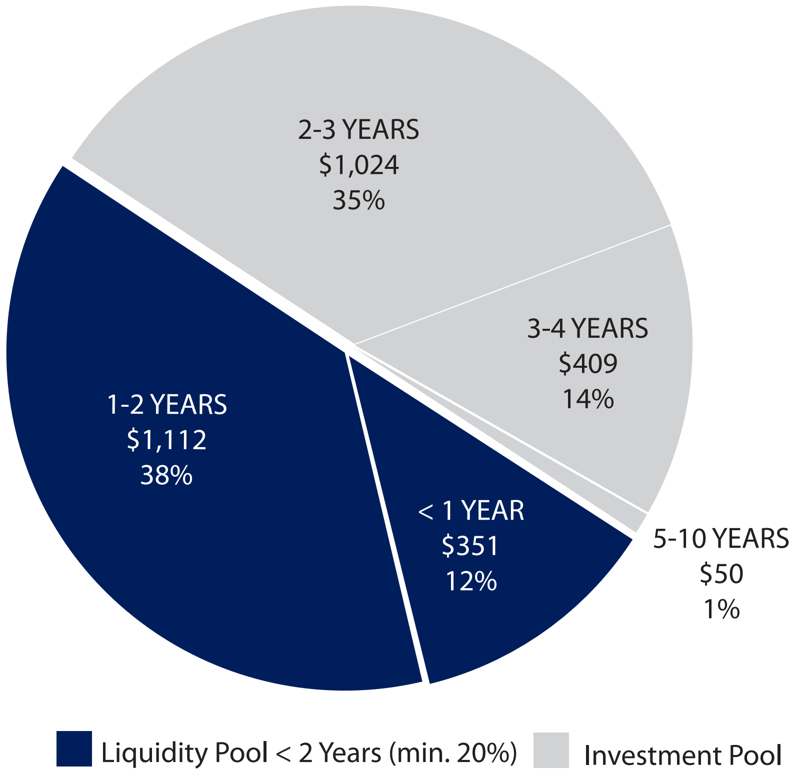


Figure 9

Investment Portfolio by Maturity at December 31, 2009

(Dollars in Millions)



Risk Management

The Corporation actively monitors and manages insurance risk. FCSIC's risk program focuses on minimizing the Fund's exposure to potential losses through early detection and employs strategies to manage and reduce risk to the Insurance Fund. Corporation staff regularly examines key ratios and financial trends; weaker System institutions undergo special examination procedures as needed.

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

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

During 2009, risk management staff monitored and evaluated trends affecting agriculture and System institutions, including

- conditions in the Nation's general economy, particularly the deterioration in the housing sector, rising unemployment, and continued volatility in fixed income and other capital markets;
- stress in several farm sectors affecting the quality of System institutions' loan portfolios including the dairy, swine, poultry, forestry, nursery and biofuels industries;
- trends at specific System institutions with declining Financial Institution Rating System (FIRS) ratings; and
- the continuing decline in values of some structured investment securities reported by System banks.

The Risk Environment in 2009

The System was affected by the severe worldwide recession which reduced demand and prices for certain farm products and caused stress in several sectors of agriculture. Conditions in the Nation's financial system and capital markets which caused asset values to decline in 2007 and 2008, continued during 2009. The U.S. economy suffered from swiftly rising unemployment as numerous firms laid off employees in response to weaker demand. Unemployment rose to 10 percent by year-end 2009. Economic output as measured by real gross domestic product continued to decline during the first two quarters of the year before stabilizing with small increases during the second half of the year. Large numbers of commercial banks continued to fail and the Federal Deposit Insurance Corporation's (FDIC) list of problem banks increased sharply to more than 700 at year-end. The housing sector continued to experience declining home prices and increases in delinquencies and foreclosures.

The U.S. Department of Agriculture reported a drop of $26.7 billion in net cash farm income (a measure of the cash income after payment of business expenses) to $70.8 billion for 2009. Export of U.S. agricultural products fell 16 percent or $19 billion, also contributing to the decline in farm income.

The volatility and uncertainty in the capital markets, where the System raises most of its funds, that characterized the second half of 2008 declined as 2009 progressed. Throughout the year, System banks were able to issue more securities with longer maturities and at narrower spreads to Treasury securities. Financial markets stabilized as the various programs instituted by the Federal Reserve, Treasury Department and FDIC improved investor and depositor confidence. Major financial sector reform is now being debated in Congress, however the shape and content is still uncertain.

Because of the drop in agricultural revenues and income, the credit quality of some System loans experienced rising stress with adversely classified loans (substandard, doubtful and loss loans) rising from 2.9 percent to 5.2 percent of total loans. These adversely classified loans are concentrated in the industry sectors experiencing stress, including dairy, swine, poultry, forestry/nursery, and biofuels. The decline in institution FIRS ratings (see figure 10) reflects the weaker asset quality and its effect on institutions' earnings and capital levels. These institutions are receiving higher examination scrutiny and supervisory attention from FCA, the System's regulator.

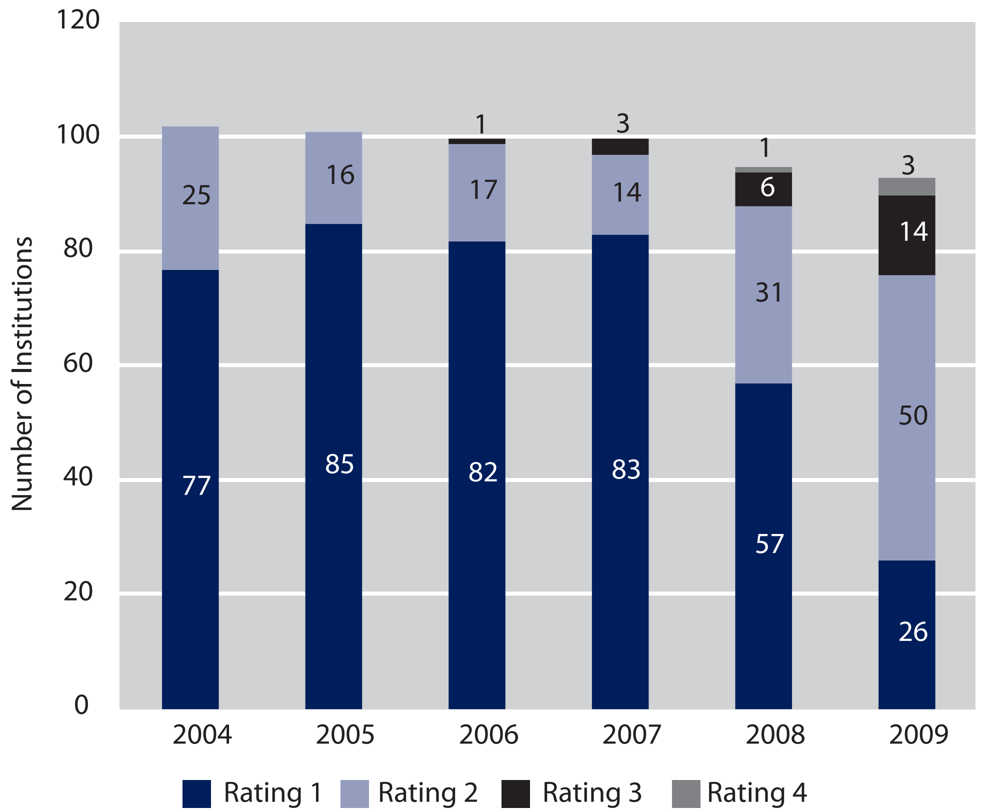
Staff also monitored the continued deterioration in certain structured securities held by System banks. Investments determined to be ineligible under FCA regulations increased to $1.3 billion at year-end 2009 from $529 million at year-end 2008. These were primarily private mortgage and asset-backed securities and represented less than 4 percent of the banks' investment portfolios.

During 2009 the five System banks worked to improve the quality of their respective liquidity portfolios by purchasing short-term U.S. Treasury securities and corporate debt securities with explicit U.S. Government guarantees. These more-highly-liquid investments increased to 16 percent of the banks' eligible investment portfolios from less than 1 percent the prior year.

Figure 10

FCS Institution FIRS Ratings

As of December 31, 2009



Source: FCA

Note: Figure 10 reflects ratings for only the System's banks and direct-lending associations; it does not include ratings for the System's service corporations, the Federal Agricultural Mortgage Corporation, or the Federal Farm Credit Banks Funding Corporation.

Financial Assistance and Receivership

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

When appointed by the FCA, the Corporation has the statutory responsibility to serve as receiver or conservator for System institutions. Upon appointment as receiver, the FCSIC shall take possession of a Farm Credit institution to settle the business operations of such institution, collect the debts owed to the institution, liquidate its property and assets, pay its creditors, and distribute the remaining proceeds to stockholders. The receiver is authorized to exercise all powers necessary to the efficient termination of an institution's operation.

There are no active receiverships or conservatorships currently in the System. To maintain the capability to act as receiver or conservator while continuing to operate with a small core staff, the Corporation uses contractors on an as-needed basis. These contractors provide knowledgeable and readily available staff resources, while allowing the Corporation to contain costs during periods of limited or no activity.

During the year, FCSIC contracted with several firms to test their capability to support potential resolution activities in loan portfolio valuation and marketing and evaluation of complex investment securities.

Corporation staff also maintains contact with the resolution staff of the FDIC and the National Credit Union Administration to stay informed about best practices and exchange information concerning receivership management.

During the year, the FCSIC engaged a consulting firm for assistance in planning for the potential resolution of any troubled FCS institutions and for help in enhancing resolution processes. The initial phase of the project includes:

- Evaluating and recommending revisions to FCSIC's Type II Pre-Resolution Examination Procedures
- Creating a profile and staffing plan to maintain readiness for various resolution alternatives
- Recommending procedures to conduct bidders' conferences

Strategic Goals and Performance Measures

Performance measures associated with the following three broad goals are used to evaluate the effectiveness of the Corporation's operations.

1. **Manage the Insurance Fund to maintain the 2 percent SBA to protect investors.**

The Corporation assesses the effectiveness of its performance by the following:

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

As a result of the premium enhancements authorized in the FCE Act, the total Insurance Fund surpassed the SBA by $209 million. Throughout the year, the total Insurance Fund ranged from 1.9 percent to 2.1 percent, finishing the year at 2.1 percent.

The investment return on the Corporation's portfolio of 2.0 percent exceeded the average return on the benchmark group (1.4 percent). Consisting of Treasuries and private sector mutual funds, the benchmark group possesses characteristics similar to the Corporation's portfolio.

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

Program effectiveness is measured by the following:

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

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

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

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

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

No receiverships or conservatorships existed in the Farm Credit System in 2009.

Corporation personnel are trained periodically to maintain readiness, ensuring proficiency in the performance of receivership responsibilities.


1991

Reports of Independent Public Auditors

Clifton Gunderson LLP

Clifton Gunderson LLP
Certified Public Accountants & Consultants

Independent Auditor's Report

To the Board of Directors
Farm Credit System Insurance Corporation
McLean, Virginia

We have audited the accompanying statements of financial condition of the Farm Credit System Insurance Corporation (the "Corporation") as of December 31, 2009 and 2008, and related statements of income and expenses and changes in insurance fund, and statements of cash flows for the years then ended. 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 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. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Corporation as of December 31, 2009 and 2008, and the results of its operations and cash flows, for the years then ended in conformity with accounting principles generally accepted in the United States of America.

In accordance with *Government Auditing Standards*, we have also issued our report dated March 26, 2010 on our consideration of the Corporation's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts and grant agreements and other matters. 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.

Our audits were conducted for the purpose of forming an opinion on the basic financial statements taken as a whole. The accompanying schedule of income and expenses by year is presented for purposes of additional analysis and is not a required part of the basic financial statements. Such information has been subjected to the auditing procedures applied in the audit of the basic financial statements and, in our opinion, is presented fairly, in all material respects, in relation to the basic financial statements taken as a whole.

Clifton Gunderson LLP

Calverton, Maryland
March 26, 2010

Clifton Gunderson LLP
Certified Public Accountants & Consultants

Independent Auditor's Report 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
McLean, Virginia

We have audited the financial statements of the Farm Credit System Insurance Corporation (the Corporation) as of and for the year ended December 31, 2009, and have issued our report thereon dated March 26, 2010. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. The management of the Corporation is responsible for maintaining effective internal control over financial reporting and for compliance with laws and regulations.

Internal Control Over Financial Reporting

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

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

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

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

11710 Beltsville Drive
Suite 300
Calverton, Maryland 20705-3106
tel: 301-931-2050
fax: 301-931-1710
www.cliftoncpa.com

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*.

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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 these specified parties.

Clifton Gunderson LLP

Calverton, Maryland
March 26, 2010

Farm Credit System Insurance Corporation
Statements of Financial Condition
As of December 31, 2009 and 2008
(Dollars in thousands)

	2009	2008
Assets		
Cash and cash equivalents	$ 12,533	$ 61,991
Investments in U.S. Treasury Obligations (Note 3)	2,933,270	2,588,890
Accrued interest receivable	23,513	21,062
Premiums receivable (Note 4)	319,286	242,970
Total assets	**$ 3,288,602**	**$2, 914,913**
Liabilities and Insurance Fund		
Accounts payable and accrued expenses (Note 6)	$ 906	$ 290
Total liabilities	**906**	**290**
Farm Credit Insurance Fund		
Allocated Insurance Reserves Accounts		
Allocated in 2003	39,888	39,888
Allocated in 2009	165,432	0
Unallocated Insurance Fund Balance	**3,082,376**	**2,874734**
Total Insurance Fund	**3,287,696**	**2,914,623**
Total liabilities and Insurance Fund	**3,288,602**	**$ 2,914,913**

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, 2009 and 2008
(Dollars in thousands)

	2009	2008
Income		
Premiums (Note 4)	$ 318,802	$ 242,970
Interest income	57,330	75,736
Other Income	0	8
Loss on the Disposition of Investments	(4)	0
Total income	**$ 376,128**	**$ 318,714**
Expenses		
Administrative operating expenses (Note 6)	$ 3,055	$ 2,634
Total expenses	**$ 3,055**	**$ 2,634**
Net income	**$ 373,073**	**$ 316,080**
Farm Credit Insurance Fund – beginning of year	**$ 2,914,623**	**$ 2,598,543**
Farm Credit Insurance Fund – end of year	**$ 3,287,696**	**$ 2,914,623**

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, 2009 and 2008
(Dollars in thousands)

	2009	2008
Cash flows from operating activities		
Net income	$ 373,073	$ 316,080
Adjustments to reconcile net income to net cash provided by operating activities		
(Increase) decrease in premium receivable	(76,317)	(51,629)
(Increase) decrease in accrued interest receivable	(2,451)	154
Net amortization and accretion of investments	37,671	8,786
Increase (decrease) in accounts payable and accrued expenses	616	(103)
Net cash provided by operating activities	332,592	273,288
Cash flows from investing activities		
Payments for purchase of U. S. Treasury Obligations	$ (1,407,377)	$(1,404,110)
Proceeds from maturity of U.S. Treasury Obligations	1,003,716	712,887
Proceeds from sale of U. S. Treasury Obligations	21,611	0
Net cash (used) provided in investing activities	(382,050)	(691,223)
Net change in cash and cash equivalents	(49,458)	(417,935)
Cash and cash equivalents, beginning of year	61,991	479,926
Cash and cash equivalents, end of year	$ 12,533	$ 61,991

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

Notes to the Financial Statements

Note 1 — Insurance Fund: Statutory Framework

The Agricultural Credit Act of 1987 (1987 Act) established the Farm Credit System Insurance Corporation (Corporation) for the purpose of ensuring the timely payment of principal and interest on notes, bonds, debentures, and other obligations issued under subsection (c) or (d) of section 4.2 of the Farm Credit Act of 1971, as amended (Act), (insured obligations). Each bank in the Farm Credit System (System) participating in insured obligations is an insured System bank. At December 31, 2009, there were five insured System banks and 89 direct lender associations.

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

The Corporation must spend the amounts necessary to:

1. Ensure the timely payment of interest and principal on insured obligations in the event of default by an insured System bank; and

2. Ensure the retirement of eligible borrower stock at par value under section 4.9A of the Act.

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

The balances outstanding at December 31, 2009, for each of the components of the Corporation's insurance responsibilities were $177.1 billion of insured obligations, and $8 million of eligible borrower stock.

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

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

Note 2 — Summary of Significant Accounting Policies

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

Cash and Cash Equivalents—Cash and cash equivalents include investments in U.S. Treasury obligations with original maturities of 90 days or less. At December 31, 2009, the Corporation held $12.46 million in overnight Treasury Certificates maturing on January 4, 2010, with an investment rate of 0.02 percent, and $75,963 in cash.

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

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

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

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

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

Retirement Plan—All permanent Corporation employees are covered by the Civil Service Retirement System (CSRS) or the Federal Employees Retirement System (FERS). The Corporation's contribution during 2009 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 $227,763 in 2009 and $209,996 in 2008.

New Accounting Pronouncements—In June 2009, the Financial Accounting Standard Board ("FASB") Accounting Standards Codification (ASC or Codification) was issued. The Codification is the source of authoritative U.S. GAAP recognized by the FASB to be applied by nongovernmental entities. The Codification is effective for financial statements issued for interim and annual periods ending after September 15,

2009. The implementation of this standard did not have a material impact on the financial position and results of operations.

In May 2009, the FASB issued ASC 855, Subsequent Events. This interpretation is intended to establish general standards of accounting for and disclosure of events that occur after the balance sheet date but before financial statements are issued or are available to be issued. ASC 855, Subsequent Events is effective for the financial periods ending after June 15, 2009. The adoption of ASC 855, Subsequent Events did not have a material impact on the Corporation's financial statements.

Note 3 — Investments

In addition to the amounts referenced in Note 2, Cash and Cash Equivalents, at December 31, 2009 and 2008, investments in U.S. Treasury obligations which are carried at amortized cost consisted of the following:

($ in thousands)

	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Market Value
December 31, 2009				
U.S. Treasury Notes	$2,933,270	$49,021	$(9,667)	$2,972,624
December 31, 2008				
U.S. Treasury Notes	$2,588,890	$82,037	$(22,321)	$2,648,606

The amortized cost and estimated market value of U.S. Treasury obligations at December 31, 2009, by contractual maturity, are shown below.

($ in thousands)

	Amortized Cost	Estimated Market Value
Due in one year or less	$ 375,489	$ 377,161
Due after one year through five years	2,508,099	2,543,043
Due after five years through ten years	49,682	52,420
	$2,933,270	$2,972,624

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 Food, Conservation, and Energy Act of 2008 amended the Farm Credit Act of 1971 (12 U.S.C. § 2001 et seq.) to generally assess premiums based on each bank's pro rata share of insured debt (rather than on loans), aligning premiums with what FCSIC insures. The changes were implemented beginning July 1, 2008. Now FCSIC may collect from 0 to 20 basis points annually on adjusted insured debt outstanding. The amendments also authorize a risk surcharge of up to 10 basis points on non-accrual loans and on other-than-temporarily impaired investments. The amendments reduce the total insured debt on which premiums are assessed by 90 percent of Federal government-guaranteed loans and investments and 80 percent of state government-guaranteed loans and investments, and deduct similar percentages of such guaranteed loans and investments when calculating the SBA. The amendments clarify that FCSIC may collect premiums more frequently than annually.

In addition, the Farm Credit Act no longer specifies how the Farm Credit System banks pass premiums to associations and other financing institutions, although it requires that the banks do so in an equitable manner. This change allows the banks flexibility in allocating premium costs to associations. The amendments clarify that, in addition to FCSIC's regulatory authority under Title V of the Farm Credit Act, FCSIC has authority to adopt rules and regulations concerning provisions in Title I of the Farm Credit Act related to banks passing along the cost of insurance premiums. Finally, the amendments change Farm Credit Act provisions regarding certified statements and simplify the formula for payments from the Farm Credit Insurance Fund Allocated Insurance Reserves Accounts (AIRAs) to allow more immediate distribution of excess Insurance Fund balances to insured banks and the Financial Assistance Corporation stockholders.

The Act sets a base amount for the Insurance Fund to achieve. The statutory SBA 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 and a similar percentage of government-guaranteed investments that are not permanently impaired) 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 SBA, the Corporation is required to reduce the premiums, but it still must ensure that reduced premiums are sufficient to maintain at the secure base amount the assets in the Insurance Fund for which no specific use has been designated (the unallocated Insurance Fund).

Insurance premium rates are reviewed semiannually. For 2009, the Board set premium rates at its January 15, 2009, meeting at 20 basis points on average adjusted insured debt and continued the assessment of the 10 basis point premium on the average principal balance outstanding for nonaccrual loans and other-than-temporarily impaired investments. The Board again reviewed premiums at its June 10, 2009 meeting. The Board voted to maintain premiums for the second half of 2009. In 2009, outstanding insured obligations decreased by $368 million (0.2 percent). At December 31, 2009, after the 2009 AIRAs allocation, the unallocated Insurance Fund was 2.00 percent as a percentage of adjusted insured debt. At December 31, 2009, the total Insurance Fund, including the AIRAs was 2.14 percent.

On January 21, 2010, the Board set premium rates for 2010, decreasing the premium rate on adjusted insured debt outstanding to 10 basis points. The Board continued the 10 basis point premium on the average principal outstanding for nonaccrual loans and other-than-temporarily impaired investments.

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

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

Currently, if at the end of any calendar year, the aggregate of the amounts in the Corporation Insurance Fund exceeds the secure base amount, the Corporation shall allocate to the Allocated Insurance Reserves Accounts the excess amount less the amount that the Corporation, in its sole discretion, determines to be the sum of the estimated operating expenses and estimated insurance obligations of the Corporation for the immediately succeeding calendar year.

At year-end 2009, the unallocated portion of the Insurance Fund was above the secure base amount. This resulted in the transfer of $165.43 million to the AIRAs. The amount was allocated as follows:

FAC Stockholders	(10%)	$ 16.54 million
Farm Credit System Banks	(90%)	$148.89 million

The AIRA balances are recorded as part of the Insurance Fund until approved for payment by the Corporation's Board. AIRA balances may be used to absorb any insurance losses and claims.

Furthermore, the Board of Directors has discretion to limit or restrict the AIRA payments. In accordance with the Corporation's policy statement, any AIRA balances do not count in measuring the Insurance Fund's compliance with the secure base amount. No AIRA payments were made during 2009 or 2008.

Note 5 — Operating Lease

On November 30, 2009, the Corporation executed a six-year lease with the Farm Credit System Building Association for office space. The terms of the lease provide for an annual minimum base rent for office space for the remaining term of $134,075 for 2010 and $138,097 for 2011. The Corporation recorded lease expense (including operating cost assessments) of $127,459 and $125,866 for 2009 and 2008, respectively.

Note 6 — Related Parties

The Corporation purchases services from the FCA under an Interagency Agreement. These include examination and administrative support services. The intention of the parties as stated in the agreement is that specified rates and fees will reimburse the party providing services for all reasonable costs associated with provision of the services. The Corporation had payables due to the FCA of $105,483 at December 31, 2009 and $57,419 at December 31, 2008. The Corporation purchased services for 2009 which totaled $345,573 compared with $134,639 for 2008.

The Corporation provides assistance to the FCA under the same Interagency Agreement, recognizing revenue of zero for 2009 and 2008. At December 31, 2009, and 2008, the Corporation did not have any receivables from the FCA.

Note 7 – Subsequent Event: Payment from AIRAs

Management evaluated subsequent events through March 26, 2010, the date the financial statements were available to be issued. Events or transactions occurring after December 31, 2009, but prior to March 26, 2010 that provided additional evidence about conditions that existed at December 31, 2009, have been recognized in the financial statements for the year ended December 31, 2009. Events or transactions that provided evidence about conditions that did not exist at December 31, 2009, but arose before the consolidated financial statements were available to be issued have not been recognized in the financial statements for the year ended December 31, 2009.

On January 22, 2010, the Board voted to pay $39.89 million held in the six AIRAs since yearend 2003 to the accountholders. Below is a schedule showing the amounts paid to the five banks as well as to the FAC stockholders. On March 25, 2010, the Board voted to pay out the $165.43 million transferred to the AIRAs at yearend 2009.

AIRAs Accounts	Payment Distribution
Payout of 2003 AIRAs	
FCB of Texas	$ 2,779,339
AgriBank, FCB	$ 12,022,474
CoBank	$ 9,681,998
U.S. AgBank	$ 5,808,564
AgFirst	$ 5,607,214
FAC Shareholders	$ 3,988,843
Total AIRAs Distribution	**$ 39,888,432**

The Act provides in part that: "If, at the end of any calendar year, the aggregate of the amounts in the Farm Credit Insurance Fund exceeds the secure base amount, the Corporation shall allocate to the [AIRAs] the excess amount less the amount that the Corporation, in its sole discretion, determines to be the sum of the estimated operating expenses and estimated insurance obligations of the Corporation for the immediately succeeding calendar year."

Since yearend 2003, the Corporation has held $39.89 million in the AIRAs. At year-end 2009, the Insurance Fund was above the secure base amount. This resulted in the transfer of an additional $165.43 million to the AIRAs (see note 4).

The Act established six AIRAs; one for each of the five banks and a sixth account for the benefit of the FAC stockholders. The FAC stockholder account is jointly held by all FAC stockholders on a proportionate basis. This account received 10 percent of any funds allocated to the AIRAs and will continue to do so until $56 million is paid to the FAC stockholders. Pursuant to section 5.55(e) payments were made to the four banks and certain AgFirst District associations. Each institution's payment is based on the number of shares held by the institution divided by the total shares outstanding at the time of termination.

The five bank AIRAs received the remaining 90 percent of the funds allocated in 2003 based on each bank's proportionate share of the average daily balance of adjusted loans outstanding for the three year period prior to yearend 2003 (at that time premiums were based on adjusted loans outstanding rather than adjusted debt). The Act requires each bank, in consultation with its affiliated associations, to develop a plan for distribution of payments received from the AIRAs within 60 days of receipt of payment.

The Board has discretion to payout funds held in the AIRAs. The Act also provides in part that, "As soon as practicable during each calendar year, the Corporation may . . . pay to each insured System bank, in a manner determined by the Corporation, an amount equal to the balance in the [AIRA] of the System bank." The Act further provides that as soon as practicable during each calendar year, the Corporation may pay to each System bank and association holding FAC stock a proportionate share of the balance in the AIRA established for holders of FAC stock.

Income and Expenses

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

	Income		Expenses		Net Income
Year	Premiums	Investment	Provision for Insurance Obligations	Administrative and Operating Expenses	Changes in Insurance Fund
1989	$ 65,000	$ 16,041	—	$ 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
2005	$ 49,393	$ 81,253	$ 6,228	$ 2,202	$ 122,236
2006	$ 164,417	$ 87,927	$ 0	$ 2,131	$ 250,213
2007	$ 191,336	$ 98,352	$ 0	$ 2,740	$ 286,948
2008	$ 242,970	$ 75,736	$ 0	$ 2,634	$ 316,080
2009	**$318,802**	**$57,326**	**$ 0**	**$ 3,055**	**$ 373,073**

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

Glossary

A

Adversely Classified Loans – consist of the following types:

Substandard
These assets are inadequately protected by the repayment capacity, equity, and/or collateral pledged. Assets so classified must have a well-defined weakness or weaknesses that could hinder normal collection of the debt. They are characterized by the distinct possibility that the lender will sustain some loss if the deficiencies are not corrected. Loss potential, while existing in the aggregate amount of substandard assets, does not have to exist in individual assets.

Doubtful
Assets classified as doubtful have all the weaknesses inherent in those classified as substandard with the added characteristic that weaknesses make collection or liquidation in full, on the basis of currently existing facts, conditions, and values, highly questionable and improbable. The possibility of loss is extremely high. Because of certain important, specific, pending factors that may work to the advantage or disadvantage of the assets, classification as substandard or loss is deferred until a more exact status can be determined. Pending factors might include a proposed merger, acquisition, liquidation, capital injection, perfection of liens on additional collateral, or plans for refinancing.

Loss
Assets classified as loss are considered uncollectible and of such little value that their continuance as bookable assets is not warranted. This classification does not mean the asset has absolutely no recovery or salvage value, but rather that it is not practical or desirable to defer writing off this basically worthless asset even though partial recovery may be effected in the future.

Agricultural Credit Association – An Agricultural Credit Association (ACA) results from the merger of a Federal Land Bank Association or an Federal Land Credit Association (FLCA) and a Production Credit Association (PCA) and has the combined authority of the two institutions. An ACA borrows funds from an FCB or ACB to provide short-, intermediate-, and long-term credit to farmers, ranchers, and producers and harvesters of aquatic products. It also makes loans to these borrowers for certain processing and marketing activities, to rural residents for housing, and to certain farm-related businesses.

Agricultural Credit Bank – An Agricultural Credit Bank (ACB) results from the merger of a Farm Credit Bank and a Bank for Cooperatives and has the combined authorities of those two institutions. An ACB is also authorized to finance U.S. agricultural exports and provide international banking services for farmer-owned cooperatives. CoBank is the only ACB in the FCS.

B

Bank for Cooperatives – A Bank for Cooperative (BC) provided lending and other financial services to farmer-owned cooperatives, rural utilities (electric and telephone), and rural sewer and water systems. It was also authorized to finance U.S. agricultural exports and provide international banking services for farmer-owned cooperatives. The last remaining BC in the FCS, the St. Paul Bank for Cooperatives, merged with CoBank on July 1, 1999.

F

Farm Credit Act – The Farm Credit Act of 1971, as amended, (12 U.S.C. §2001 et seq.) is the statute under which the FCS operates.

Farm Credit Bank – The Farm Credit Banks (FCBs) provide services and funds to local associations that, in turn, lend those funds to farmers, ranchers, producers and harvesters of aquatic products, rural residents for housing, and some agriculture- related businesses. On July 6, 1988, the Federal Land Bank and the Federal Intermediate Credit Bank in 11 of the 12 then-existing Farm Credit districts merged to become FCBs. The mergers were required by the Agricultural Credit Act of 1987. Currently there are four FCBs: AgFirst Farm Credit Bank; AgriBank, FCB; Farm Credit Bank of Texas; and U.S. AgBank, FCB.

Farm Credit Administration – The Farm Credit Administration (FCA) was established in 1933 to regulate the Farm Credit System. It is governed by a three-member presidentially appointed board. To ensure the safety and soundness of the System, the Agency examines and supervises System institutions and develops regulations to govern them.

Federal Farm Credit Banks Funding Corporation – The Funding Corporation, based in Jersey City, New Jersey, manages the sale of Systemwide debt securities to finance the loans made by FCS institutions. It uses a network of bond dealers to market the System's securities.

Financial Institution Rating System – The FIRS is similar to the Uniform Financial Institutions Rating System used by other Federal banking regulators. However, unlike the Uniform Financial Institutions Rating System, the FIRS was designed to reflect the nondepository nature of FCS institutions. The FIRS provides a general framework for assimilating and evaluating all significant financial, asset quality, and management factors to assign a composite rating to each System institution. The ratings are described below.

Rating 1 – Institutions in this group are basically sound in every respect; any negative findings or comments are of a minor nature and are anticipated to be resolved in the normal course of business. Such institutions are well managed, resistant to external economic and financial disturbances, and more capable of withstanding the uncertainties of business conditions than institutions with lower ratings. Each institution in this category exhibits the best performance and risk management practices for its size, complexity, and risk profile. These institutions give no cause for regulatory concern.

Rating 2 – Institutions in this group are fundamentally sound but may reflect modest weaknesses correctable in the normal course of business. Since the nature and severity of deficiencies are not material, such institutions are stable and able to withstand business fluctuations. Overall risk management practices are satisfactory for the size, complexity, and risk profile of each institution in this group. While areas of weakness could develop into conditions of greater concern, regulatory response is limited to the extent that minor adjustments are resolved in the normal course of business and operations continue in a satisfactory manner.

Rating 3 – Institutions in this category exhibit a combination of financial, management, operational, or compliance weaknesses ranging from moderately severe to unsatisfactory. When weaknesses relate to asset quality or financial condition, such institutions may be vulnerable to the onset of adverse business conditions and could easily deteriorate if concerted action is not effective in correcting the areas of weakness. Institutions that are in significant noncompliance with laws and regulations may also be accorded this rating. Risk management practices are less than satisfactory for the size, complexity, and risk profile of each institution in this group. Institutions in this category generally give cause for regulatory concern and require more than normal supervision to address deficiencies. Overall strength and financial capacity, however, still make failure only a remote possibility if corrective actions are implemented.

Rating 4 – Institutions in this group have an immoderate number of serious financial or operating weaknesses. Serious problems or unsafe and unsound conditions exist that are not being satisfactorily addressed or resolved. Unless effective actions are taken to correct these conditions, they are likely to develop into a situation that will impair future viability or constitute a threat to the interests of investors, borrowers, and stockholders. Risk management practices are generally unacceptable for the size, complexity, and risk profile of each institution in this group. A potential for failure is present but is not yet imminent or pronounced. Institutions in this category require close regulatory attention, financial surveillance, and a definitive plan for corrective action.

Rating 5 – This category is reserved for institutions with an extremely high, immediate, or near-term probability of failure. The number and severity of weaknesses or unsafe and unsound conditions are so critical as to require urgent external financial assistance. Risk management practices are inadequate for the size, complexity, and risk profile of each institution in this group. In the absence of decisive corrective measures, these institutions will likely require liquidation or some form of emergency assistance, merger, or acquisition.

Food, Conservation, and Energy Act – This law, enacted in 2008, amended the Farm Credit Act to reform the Insurance Corporation's insurance premium authority to generally assess premiums on insured FCS banks' adjusted outstanding insured debt (rather than on loans).

G

Government-sponsored Enterprise – A GSE is typically a federally chartered corporation that is privately owned, designed to provide a source of credit nationwide, and limited to servicing one economic sector. Each GSE has a public or social purpose. GSEs are usually created because the private markets did not satisfy a purpose that Congress deems worthy either to fill a credit gap or to enhance competitive behavior in the loan market. Each is given certain features or benefits (called GSE attributes) to allow it to overcome the barriers that prevented purely private markets from developing. In some cases, the GSE receives public assistance only to get started, as the FCS did; in other cases, the assistance is ongoing. The FCS is the oldest financial GSE.

Acronyms and Abbreviations

ACA—Agricultural Credit Association
ACB—Agricultural Credit Bank
CIPA—Contractual Interbank Performance Agreement
FAC—Farm Credit System Financial Assistance Corporation
Farm Credit Act, the Act—Farm Credit Act of 1971, as amended
FCA—Farm Credit Administration
FCB—Farm Credit Bank
FCE Act—Food, Conservation, and Energy Act of 2008
FCS—Farm Credit System
FCSIC—Farm Credit System Insurance Corporation
FDIC—Federal Deposit Insurance Corporation
FIRS—Financial Institution Rating System
FHCS—Federal Human Capital Survey
FLCA—Federal Land Credit Association
Funding Corporation—Federal Farm Credit Banks Funding Corporation
GSE—Government-sponsored enterprise
MAA—Market Access Agreement
PCA—Production Credit Association
SBA—Secure Base Amount

Contact Information

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

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

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

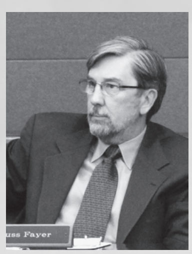
Office of Congressional and Public Affairs
Farm Credit Administration
1501 Farm Credit Drive
McLean, VA 22102
(703) 883-4056

Corporate Staff

Dorothy L. Nichols	Chief Operating Officer
Alan J. Glenn	Director of Risk Management
C. Richard Pfitzinger	Chief Financial Officer
James M. Morris	General Counsel
William Fayer	Senior Resolution Specialist
Wade Wynn	Senior Financial Analyst
Pam Ngorskul	Accountant
Jeremy Del Moral	Financial Analyst
Anna Lacey	Administrative Specialist
Molly Sproles	Administrative Management Assistant










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

703-883-4380 Voice
703-790-9088 Fax
www.fcsic.gov