Farm Credit System Insurance Corporation

2012 *Annual* Report

Protecting Investors in Agriculture and Rural America

Mission Statement

The Farm Credit System Insurance Corporation (FCSIC or 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.

FARM CREDIT SYSTEM INSURANCE CORPORATION

May 20, 2013

Dear Mr. President and Mr. 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 2012.

This report highlights our 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, 2012, was $3.3 billion.

We collected $84.3 million in insurance premiums from Farm Credit System banks for 2012, earned $46.8 million in investment income during the same period, and expect to incur $4 million in operating costs in 2013.

Sincerely,

Kenneth A. Spearman
Chairman

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

Contents

Board member photos courtesy of Bachrach.

Message from the Chairman

I am pleased to present FCSIC's 2012 Annual Report. It is gratifying to note that, for the twenty-third consecutive year since we began issuing financial statements, our independent public auditor has issued unqualified opinions on those statements. Their opinion letters, which are enclosed, indicate that the financial statements concerning the Farm Credit Insurance Fund, of which we are stewards, are fairly and accurately presented.

The Corporation's net income for 2012 was $127.8 million, compared with $166.6 million for the previous year. The Insurance Fund balance as of December 31, 2012, was $3.30 billion, compared with $3.39 billion at year-end 2011.

Premium revenue was $84.3 million for 2012, compared with $97.3 million for 2011. Interest income for 2012 totaled $46.8 million, compared with $72.6 million in 2011.

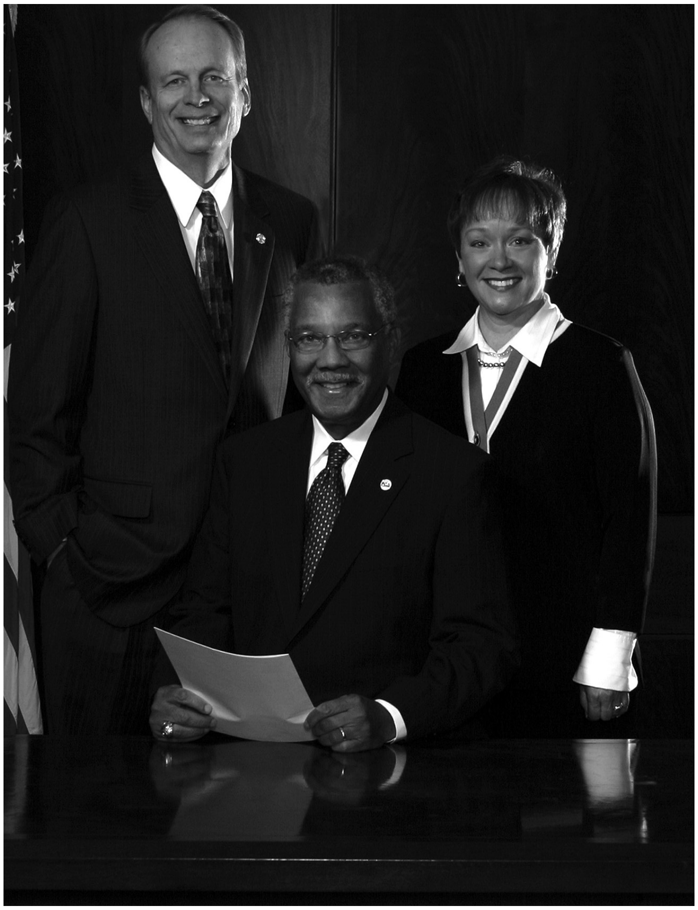
In accordance with the requirements of the Federal Managers' Financial Integrity Act of 1982, our management conducted its annual assessment of the system of internal controls. Its findings show that, in the reviewed areas, internal controls comply with the standards prescribed by the U.S. Government Accountability Office and provide reasonable assurance that program objectives are being met.

In 2013, we will continue to carry out our mission and work towards achieving our strategic goals and objectives. In the process of identifying and addressing risks to the Insurance Fund, we are mindful of our public trust and will ensure that investors, Congress, the Farm Credit System, and other regulatory agencies receive timely and accurate information on issues concerning the Insurance Fund.

Sincerely,

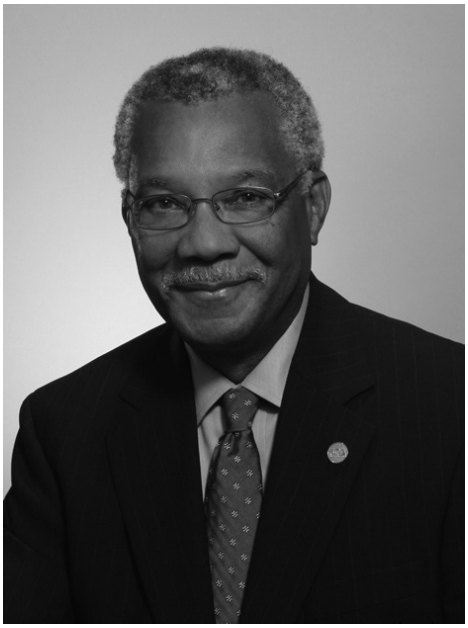
Kenneth A. Spearman

Board of Directors



FCSIC 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, a nationwide network of financial cooperatives that lends to agriculture and rural America.

Kenneth A. Spearman



Kenneth A. Spearman is Chairman of the Board of Directors of the Farm Credit System Insurance Corporation. He also serves as a member of the Board of the Farm Credit Administration.

Mr. Spearman brings to his position as Chairman of 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 Farm Credit Administration Board, 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 in central Florida, Mr. Spearman served with the U.S. Army and is a Vietnam veteran. He later was employed by the public accounting firm Arthur Andersen & Co. and was involved with the development of a public accounting firm in Chicago, Illinois. 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, for which he served a term as national 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. He also attended Harvard Kennedy School Executive Education, where he completed a program with a concentration in Government Agency Strategic Planning.

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 George W. Bush on December 12, 2006. He served as Chairman of the FCSIC Board until he was appointed Chairman and CEO of FCA on May 22, 2008. He served in this position until November 26, 2012, when Jill Long Thompson was appointed Chair and CEO of FCA by President Barack Obama, effective November 27, 2012. He remains a member of FCSIC and FCA boards until the President designates a successor.

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, a Farm Credit System 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 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 and was a member of the Illinois Ag Leadership Program class of 1988.

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.

In 2011, Mr. Strom received the Honorary Doctorate of Humane Letters from Northern Illinois University for his commitment to sustaining agricultural systems and food security. He studied agriculture business at Kishwaukee College and business administration at Northern Illinois University. He also attended the Harvard Kennedy School Executive Education program.

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 three children and two grandchildren.

Jill Long Thompson

Jill Long Thompson is Chair of the Board and CEO of the Farm Credit Administration (FCA) and a member of the Board of Directors of the Farm Credit System Insurance Corporation. Dr. Long Thompson was appointed to the FCA Board by President Barack Obama in March 2010 and was designated Board Chair and CEO on November 27, 2012. Her term expires in May 2014. Long Thompson has 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 Committee on Agriculture, the Committee on Veterans' Affairs, and the Select Committee on Hunger. She also served as Chair of the Rural Caucus. While in Congress, 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, 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, Long Thompson is also the first and only Hoosier woman to be nominated by a major party to run for the U.S. Senate.

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 an 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.

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.

2012 – Year in Review

Allocated Insurance Reserves Accounts (AIRAs)

At year-end 2011, $221.9 million, the calculated excess amount in the Farm Credit Insurance Fund, was transferred to the AIRAs. In April 2012, after completion of FCSIC's year-end audit, our Board of Directors authorized payment of $221.9 million to the accountholders. Payments were made in May 2012. (See Note 4 to the Financial Statements for additional AIRAs information.)

Insurance Fund Finishes 2012 at 1.93 Percent, Slightly Below the Statutory 2 Percent Secure Base Amount

At December 31, 2012, the Farm Credit Insurance Fund was $3.30 billion (1.93 percent of adjusted insured debt outstanding), which was $119 million below the secure base amount. (See "Insurance Fund Management" on page 16 for additional details.) Consequently, no funds were available to transfer to the AIRAs. (See Note 4 to the Financial Statements for additional details.)

FCSIC's Legislative Initiative

As part of the FCSIC 2010–2015 Strategic Plan, we continue to pursue a legislative initiative to strengthen our resolution authorities, including our receivership and conservatorship powers. These changes would improve our ability to protect investors. Also, ensuring that we have express statutory authority comparable to other Federal receivers and conservators would reduce the costs of resolving a troubled Farm Credit System institution.

After consulting with the FCSIC Board and meeting with a workgroup of senior System officials, FCSIC staff delivered a draft of legislative language to our congressional oversight committees for their consideration. In May 2012, our Board of Directors wrote to the House Agriculture Subcommittee on Department Operations, Oversight, and Credit to request these important changes be enacted as part of the next Farm Bill.

Strategic Planning Policy

In April 2012, our Board approved the revised Policy Statement on Strategic Planning originally adopted in 1994. The revision incorporates updates from the Office of Management and Budget Circular No. A-11. The updated Circular A-11 includes a new goal-based structure, a requirement for online submission of agency strategic plans, and more frequent reporting on agency performance. In addition, we reviewed the strategic planning policies and processes used by similar agencies and implemented best practices.

Our strategic plan defines our mission, long-term goals, and the approaches we will use to execute the plan and carry out our mission. It also describes how we will manage any challenges and risks. The strategic plan is our commitment to perform, and our strategic planning process is intended to promote sound corporate decision-making in the use of the Corporation's resources.

Financial Assistance Policy

On April 11, 2013, the FCSIC Board of Directors approved the "Policy Statement Concerning Assistance." The statement replaces the "Policy Statement Concerning Stand-Alone Assistance." The new policy statement provides greater clarity as to when FCSIC might use its statutory authority to provide assistance to a

System institution and provides more discussion of how the statutory least-cost test might be performed. The new policy statement also includes enhanced criteria of what might be included in assistance proposals. These criteria are based on the experience of various Government entities during the recent financial crisis. The policy also includes a new section discussing assistance agreements between FCSIC and a System institution receiving assistance. A draft of the new policy statement was published for comment on June 21, 2012.

Operating Efficiency and Cost Containment

The Corporation's operating costs as a percentage of its total assets represented 10 basis points for 2012. In September 2012, our Board of Directors approved budgets for 2013 and 2014. The 2013 budget is $4.0 million, which is unchanged from 2011 and 2012. The 2014 budget projects an increase of 1.6 percent over the 2013 budget because of expected increases in personnel costs.

Selected Financial Statistics

Farm Credit System Insurance Corporation
(Dollars in Millions)

	2012	2011	2010
BALANCE SHEET:			
Total Assets	$ 3,298.2	$ 3,392.3	$ 3,225.7
Total Liabilities	0.3	0.4	0.3
Insurance Fund Balance			
Allocated Insurance Reserves Accounts	0	221.9	0
Unallocated Insurance Fund Balance	3,297.9	3,170.1	3,225.3
OPERATIONS:			
Revenues	131.1	169.9	146.1
Operating Expenses	3.3	3.3	3.1
Insurance Expense	0	0	0
Net Income	127.8	166.6	143.0

The Farm Credit System

Structure and Funding

The Farm Credit System (System or FCS) is a federally chartered network of cooperative lending institutions owned by the agricultural and rural customers it serves, including farmers, ranchers, producers or harvesters of aquatic products, agricultural cooperatives, and farm-related businesses. As of December 31, 2012, the System had four banks and 82 associations. Each of the associations has its own chartered territory and is affiliated with one of the four banks.

Each association receives wholesale funding from its affiliated bank and lends directly to its owner-borrowers, providing a consistent and reliable source of agricultural and rural credit throughout the United States and the Commonwealth of Puerto Rico. CoBank also has nationwide authority to make retail loans to cooperatives and other eligible entities.

The banks obtain funds for their operations primarily through the sale of Federal Farm Credit Banks Consolidated Systemwide debt securities. The banks own and utilize the Federal Farm Credit Banks Funding Corporation to issue Systemwide debt securities in the capital markets. As the fiscal agent for the banks, the Funding Corporation partners with a select group of dealers to market and distribute the securities to investors throughout the world to finance the System's operations.

Combined Farm Credit System Statistics

(Dollars in Billions)

	2012	2011	2010
Insured Debt Outstanding[1]	$ 197.5	$ 184.2	$ 188.3
Production Agriculture:			
Real Estate Mortgage Loans	88.3	80.7	78.0
Production and Intermediate-term Loans	43.9	41.3	40.6
Agribusiness Loans[2]	27.1	24.7	29.6
Communication Loans	4.2	3.8	3.6
Energy, Water and Waste Disposal Loans	14.5	11.8	11.5
Rural Residential Real Estate Loans	6.2	5.8	5.5
International Loans	4.7	3.8	4.0
Lease Receivables	2.4	2.1	2.0
Loans to Other Financial Institutions	0.7	0.6	0.5
Cash and Investments	46.9	47.3	46.3
Net Income	4.1	3.9	3.5
Nonperforming Loans as a Percentage of Total Loans	1.4%	1.7%	1.9%

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, 2012.
2. As of December 31, 2012, agribusiness loans consisted of loans to cooperatives of $12.8 billion, processing and marketing loans of $11.5 billion, and farm-related business loans of $2.8 billion.

Investor Protection

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

Regulatory Oversight

The Farm Credit Administration is the safety and soundness regulator responsible for the examination, supervision, and regulation of each FCS institution. FCA 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 FCSIC, FCA, and the FCS.

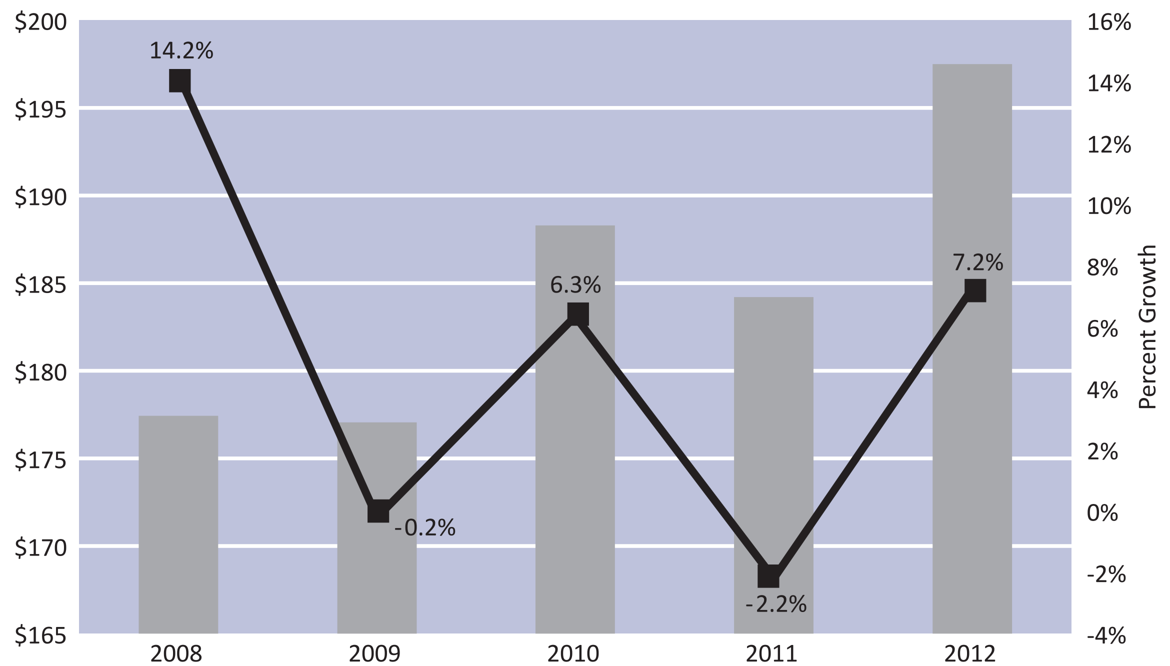
Insured and Other Obligations

FCSIC insures Systemwide and consolidated bonds, notes, and other obligations issued by System banks through the Federal Farm Credit Banks Funding Corporation under section 4.2 (c) or (d) of the Farm Credit Act. Figure 1 shows that insured debt outstanding increased by 7.2 percent in 2012 to $197.5 billion. This is in contrast to a 2.2 percent decrease in insured debt outstanding in 2011.

FCSIC must also ensure the retirement of eligible borrower stock at par value, as required by section 4.9A of the Farm Credit Act. This stock, also known as protected borrower stock, was outstanding prior to October 6, 1988. At year-end 2012, protected borrower stock outstanding at System institutions totaled $2 million, down from $5 million at year-end 2011.

Figure 1

Insured Debt Outstanding
Growth Averaged 5.1 Percent Over the Past 5 Years
(Dollars in Billions)



Note: 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, 2012.

Farm Credit System Capital

The primary source of funds to repay insured Systemwide debt securities is the System's borrowers. Each borrower must 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 on its loan to the lending bank. Both the banks, which ultimately repay Systemwide debt securities, and the associations exceed their minimum regulatory capital requirements as protection and support for the repayment of the outstanding insured debt.

If a bank were unable to repay its portion of an insured Systemwide debt obligation, the Corporation would use the Insurance Fund to make that payment. Since the repayment of Systemwide debt securities is the joint and several obligation of the banks, 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 41 percent, from $12.4 billion at year-end 2008 to $17.5 billion at year-end 2012. Bank capital plus the amount in the Insurance Fund as a percentage of insured debt outstanding decreased from 9.1 percent in 2011 to 8.9 percent in 2012 (see figure 3). Over the past several years, the System banks have reported strong earnings primarily from their ability to re-price debt at favorable rates in the low-interest rate environment. Between 2009 and 2011, the banks retained a significant portion of their earnings to boost capital levels. In 2012, the System's loan growth outpaced its capital growth, causing a slight decline in bank capital as a percentage of insured debt.

Overall, the financial performance and condition of the System on a consolidated basis remains strong, though some individual institutions continue to experience stress from credit deterioration in certain agricultural sectors and from continued stress in the general economy. (See trends in the Financial Institution Rating System in the "Risk Management" section beginning on page 23.)

System associations have boosted capital levels through the net income they have earned and retained. Association capital helps reduce the credit exposure of the association's direct loan with its affiliated bank. As figure 4 shows, from 2008 to 2012, combined association capital increased $7.4 billion or 38.7 percent, with an annual average increase of approximately 8.6 percent. Since 2008, the associations have collectively achieved solid earnings and preserved capital, causing association capital as a percentage of total assets to steadily increase to 17.8 percent in 2011 and 2012 (see figure 5).

Figure 2

Bank Capital Plus Insurance Fund

(Dollars in Billions)

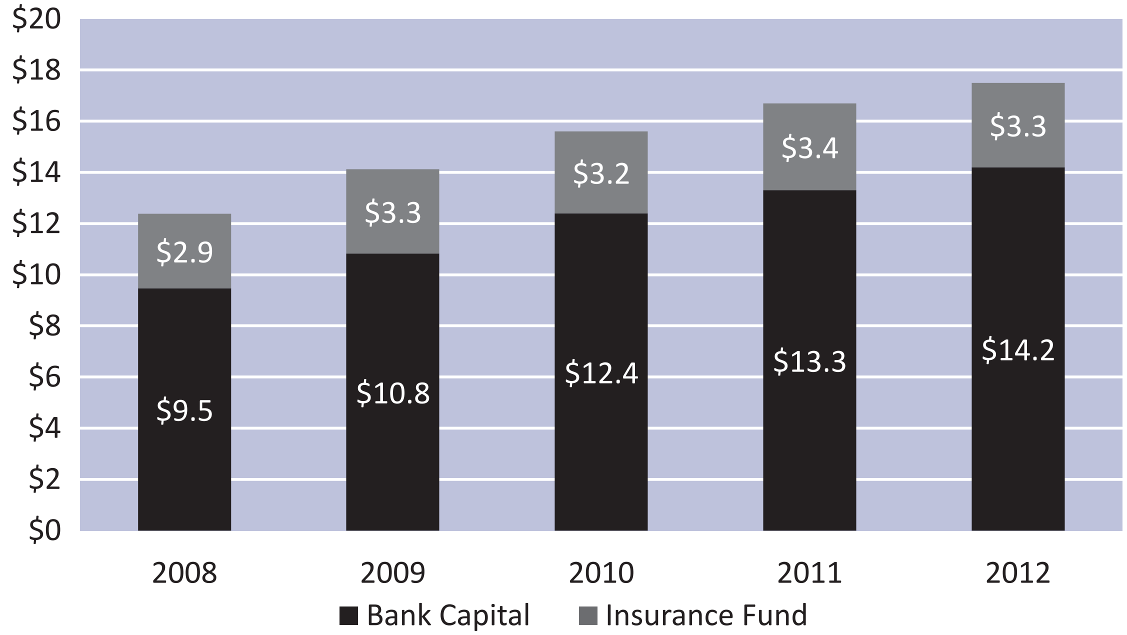


Figure 3

Bank Capital Plus Insurance Fund as Percentage of Insured Debt

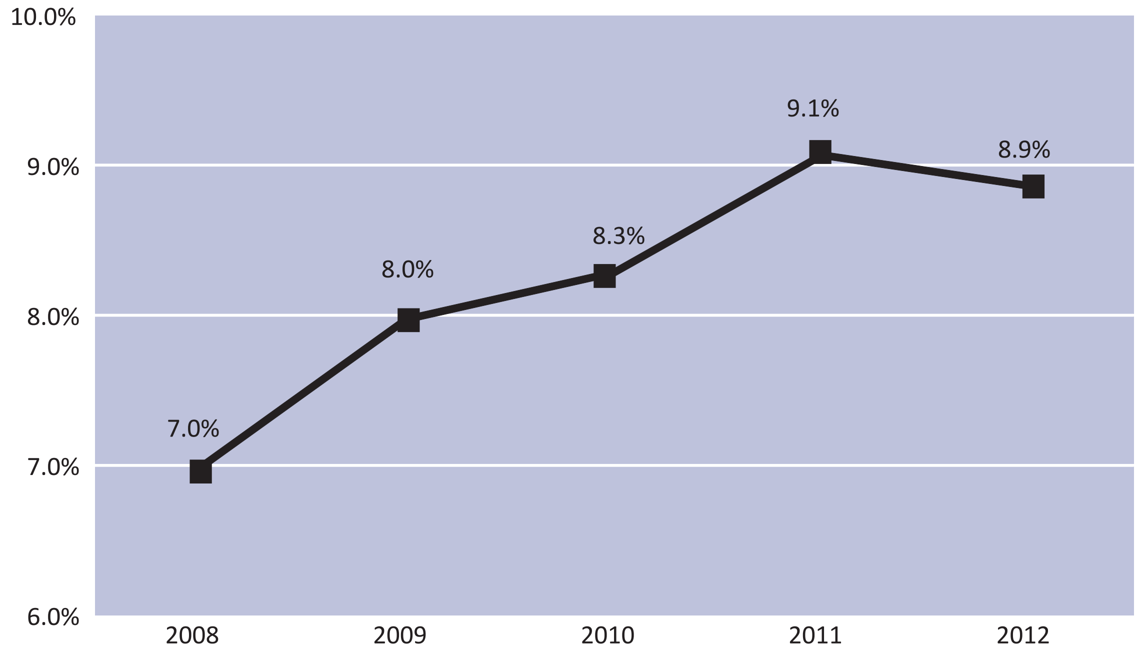


Figure 4

Combined Association Capital

(Dollars in Billions)

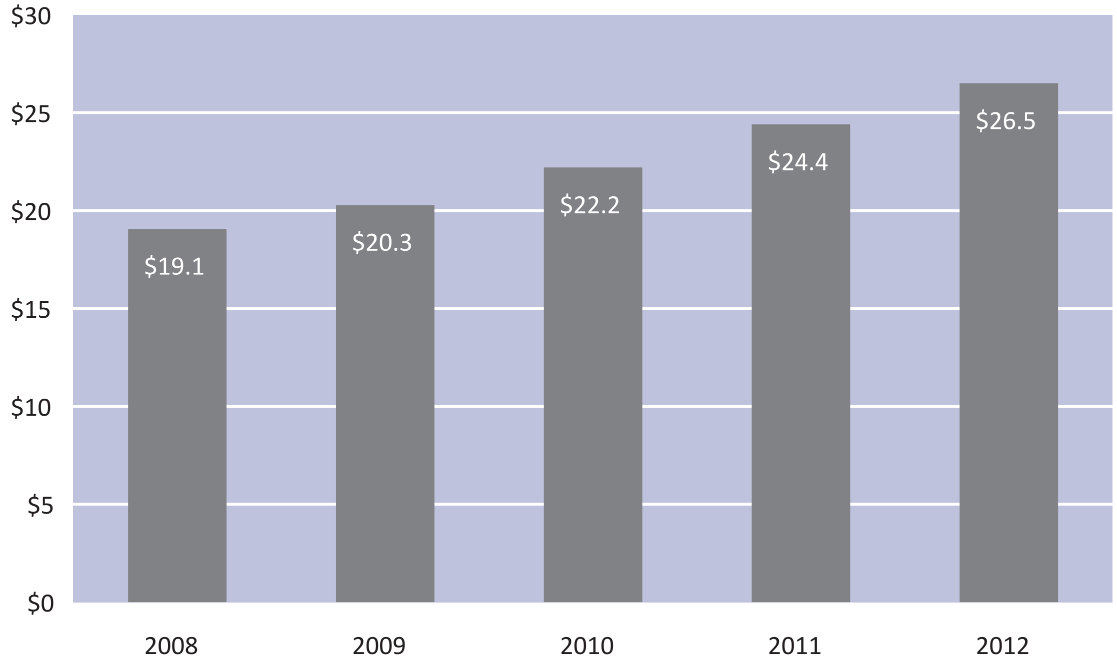
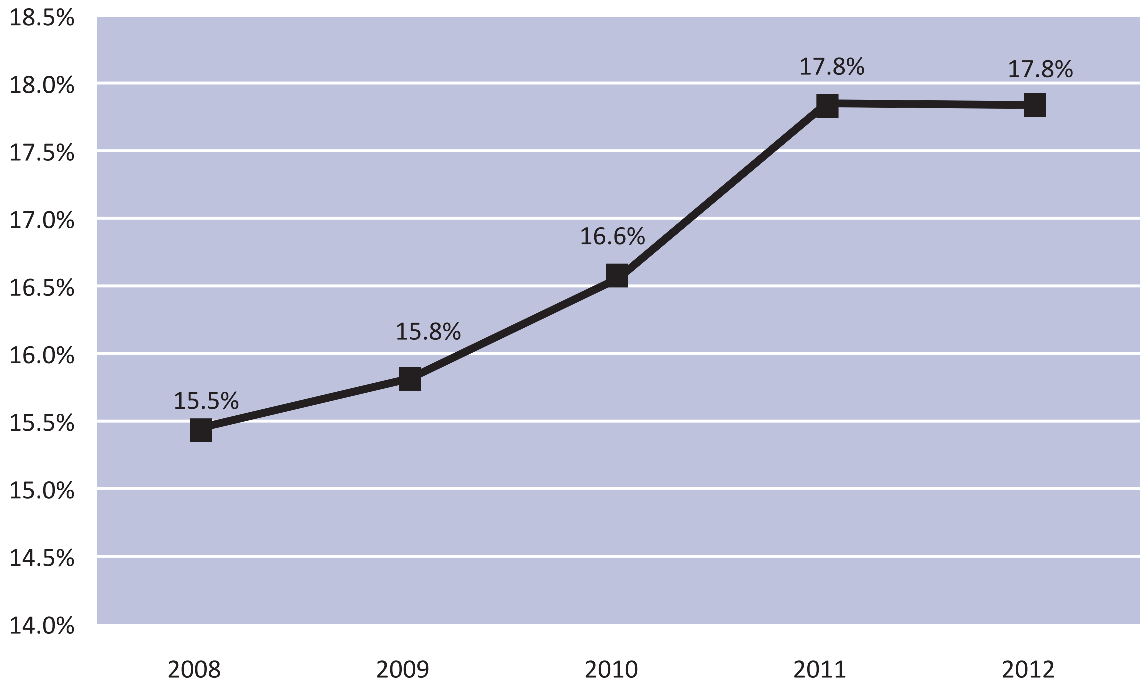


Figure 5

Combined Association Capital as a Percentage of Total Assets



Additional Protections

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

The System and the Federal Farm Credit Banks Funding Corporation have also entered into the Market Access Agreement, which 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, the bank may be restricted from issuing debt. The criteria used under the Market Access Agreement are the CIPA scores and the net collateral and permanent capital ratios.

The System entered into a common minimum liquidity standard in 2010 to improve the quality and quantity of bank liquidity reserves. This standard is designed to maintain and ensure adequate liquidity to meet the business and financial needs of each bank and the System in the event access to the debt market is temporarily impeded.

In April 2013, the Farm Credit Administration issued a final liquidity rule that strengthens the banks' liquidity reserve requirement, promotes liquidity risk management best practices, and better prepares the banks to withstand a liquidity crisis. For additional information on bank liquidity, see the discussion in the "Risk Management" section of this report.

Insurance Fund Management

The Insurance Fund and the Secure Base Amount

The Farm Credit Insurance Fund represents FCSIC'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 (assets transferred to the AIRAs). Premiums are due until the unallocated portion of the Insurance Fund reaches the secure base amount.

The secure base amount established by the Farm Credit Act of 1971, as amended, is 2 percent of the aggregate outstanding insured obligations (adjusted to exclude 90 percent of Federal Government-guaranteed loans and investments and 80 percent of State Government-guaranteed loans and investments), or another percentage that FCSIC determines to be actuarially sound to maintain in the Insurance Fund, taking into account the risk of insuring outstanding insured obligations.

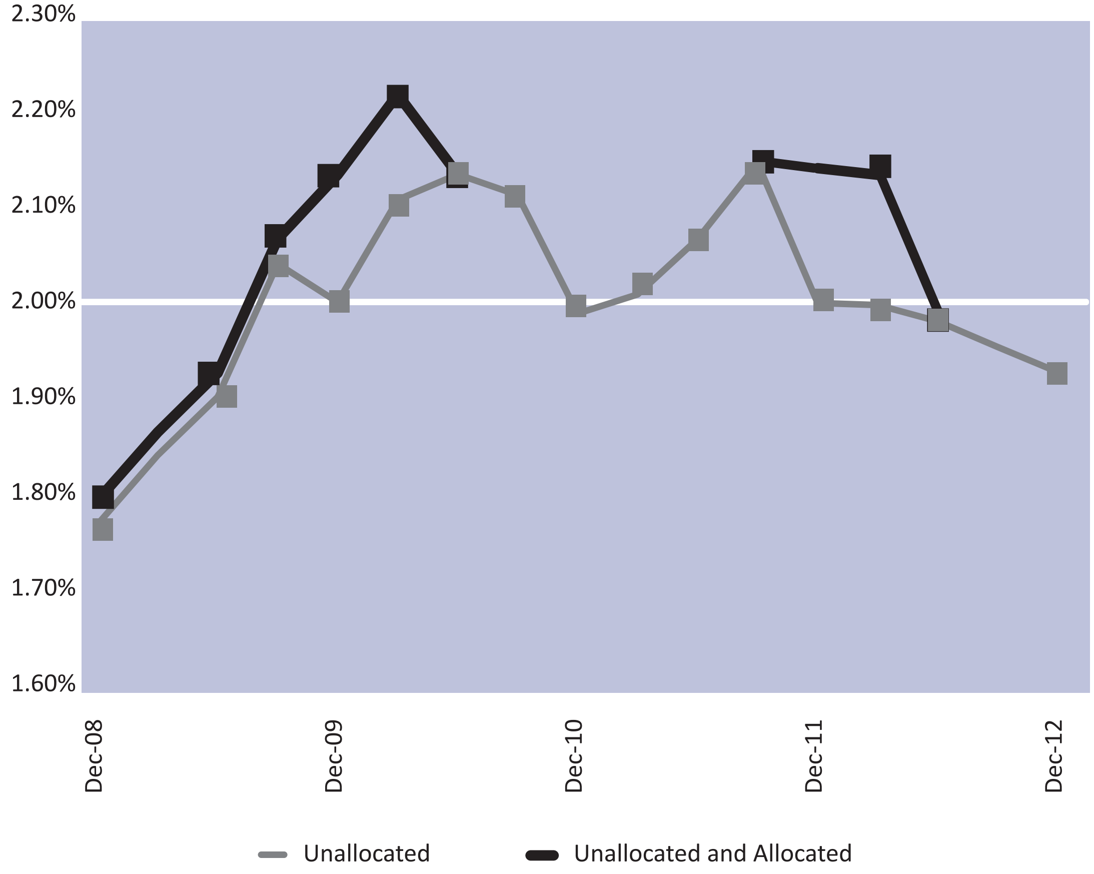
In 2012, both the total Insurance Fund and total assets declined by 2.8 percent to $3.30 billion as a result of AIRA payments of $221.9 million. Insured debt outstanding grew $13.4 billion in 2012 (7.2 percent). The Insurance Fund finished 2012 at 1.93 percent, which was $119.1 million below the secure base amount (see figure 6). Consequently, no excess funds were available for allocation to the AIRAs at year-end.

At year-end 2011, $221.9 million, the calculated excess amount in the Insurance Fund, was transferred to the AIRAs. In April 2012, after completion of our year-end audit, the Board of Directors authorized the payment of the $221.9 million to the account holders. Payments were made in May 2012. (See Note 4 to the Financial Statements for additional details.)

Over the past five years, the total Insurance Fund and total assets each grew at an annual rate of 5.1 percent. We did not accrue a provision for insurance obligations in 2012.

Figure 6

Insurance Fund Relative to 2 Percent Secure Base Amount



Note: In April 2012, the Board of Directors authorized payment of $221.9 million, which had been allocated to the AIRAs at year-end 2011.

Premiums

FCSIC's Board of Directors reviews premium assessment rates as often as necessary but at least semiannually. The Board 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 Farm Credit Act allows us to collect from 0 to 20 basis points on adjusted insured debt outstanding. A risk surcharge of up to 10 basis points on nonaccrual loans and on other-than-temporarily impaired investments is also authorized. In addition, the Act reduces the total insured debt on which premiums are assessed. It bases premiums on outstanding insured debt obligations adjusted downward by 90 percent of Federal Government-guaranteed loans and investments and 80 percent of State Government-guaranteed loans and investments.

The most important factor in determining premium rates for 2012 was the level of the Insurance Fund relative to the secure base amount. Based on System growth projections ranging from 3 to 5 percent, our Board set the assessment rate on adjusted insured debt at 5 basis points in January 2012. Through May 2012, insured debt grew by 2.2 percent, and System institutions indicated that growth for the year would likely be lower than estimated in January, but still within the 3 to 5 percent range. As a result, the Board, at its scheduled mid-year premium review in June, maintained the premium assessment on adjusted insured debt at 5 basis points for 2012. (Note: 1 basis point (bp) = 1/100 of 1 percent.)

Premium Rates January to December 2012	Premiums (in basis points)
Adjusted insured debt	5
Nonaccrual loans	10
Other-than-temporarily impaired investments	10

Because the Insurance Fund finished 2012 $119 million below the secure base amount, our Board set the assessment rate on adjusted insured debt at 10 basis points for 2013. We project that premium assessments for 2013 will total approximately $184 million.

Revenues and Expenses

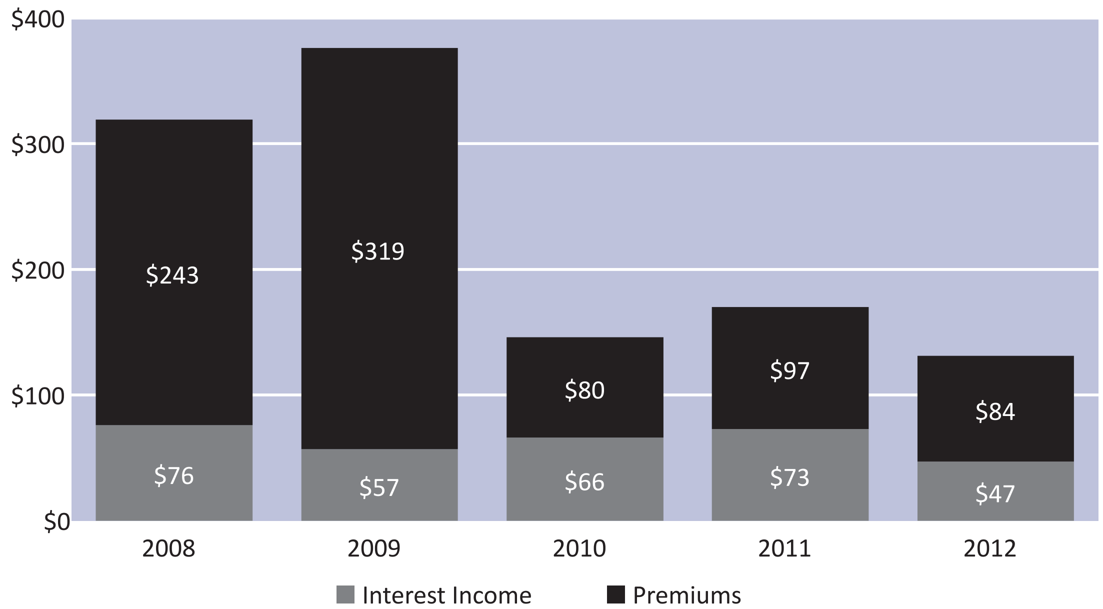
FCSIC operates with no appropriated funds. We collect insurance premiums from each Farm Credit System bank that issues insured obligations. These premiums and the income from our investment portfolio provide the funds necessary to fulfill our mission.

Our revenues in 2012 decreased 22.8 percent to $131.1 million from $169.9 million in 2011 (see figure 7). The decrease in revenues resulted from two factors: lower premiums and the continued historically low interest rates. Interest income decreased 36 percent in 2012 to $46.8 million from $72.6 million in 2011.

Figure 7

Corporation Revenues

(Dollars in Millions)



To avoid duplication of effort and to minimize costs, since 1993 we have operated with a small core staff and used private- and public-sector contractors to leverage our efforts. The Corporation's Board of Directors and management have adopted this model as a cost-effective and efficient way to use available expertise, services and resources to accomplish FCSIC's mission.

Our operating costs as a percentage of total assets represented 10 basis points for 2012. Fixed costs for staff, travel, rent, and miscellaneous expenses were $2.5 million of the $3.3 million total for the year (see figure 8). The remaining expenses of $0.8 million were for contract services.

On December 22, 2010, President Obama signed legislation prohibiting statutory annual pay adjustments for most Federal civilian employees and freezing base pay for senior executives for two years. President Obama also issued a memorandum stating that agencies should forgo similar increases to pay schedules and rates that are set by administrative discretion. We complied with the President's memorandum. Pay adjustments not covered by the freeze include promotion increases and individually based merit increases for nonexecutive employees. In March 2013, President Obama signed legislation extending the pay freeze through 2013.

Figure 8

Corporation Expenses

(Dollars in Millions)

Investments

FCSIC investments decreased during the year from $3.3 billion at December 31, 2011, to $3.2 billion at year-end 2012 (see figure 9).

Our 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 our investment policy.

The average portfolio yield was 1.44 percent, down from 2.25 percent the prior year. The return on the Insurance Fund continued to outperform the benchmark index we use to measure performance. This index is composed of Treasuries and a private sector mutual fund with holdings that are similar in type and maturity to holdings in our portfolio. The average return of the benchmark group was 0.55 percent for 2012.

In accordance with our 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. Our investment policy requires that the liquidity pool must account for at least 20 percent of the portfolio and that no more than 25 percent of the investment pool may be invested in securities with maturities between 5 and 10 years. The weighted average portfolio maturity at year-end was 2.6 years. The composition of the investment portfolio at December 31, 2012, is shown in figure 10.

In June 2008, we began purchasing Treasury Inflation Protected Securities (TIPS). TIPS have a stated rate of interest, payable semiannually, which is applied to the inflation-adjusted principal. TIPS provide a hedge against inflation, in terms of both yield and market value, which we believe is particularly important during the current historically low interest rate environment. TIPS have experienced monthly inflation or deflation adjustments, but the U.S. has not had an annual deflationary environment since 1954, nearly 60 years ago. Because of the volatility of the monthly returns on TIPS, the FCSIC Investment Committee limits TIPS to no more than 20 percent of the portfolio. At year-end 2012, our TIPS investments totaled $631 million or 19.7 percent of the investment portfolio. On average, over the past five years, TIPS have earned 39 basis points more per year than our traditional Treasury instruments, a gain of $10.2 million over the five-year period; at year-end 2012 the market value of TIPS was $6.1 million above book value.

Figure 9

Corporation Investments

(Dollars in Billions)

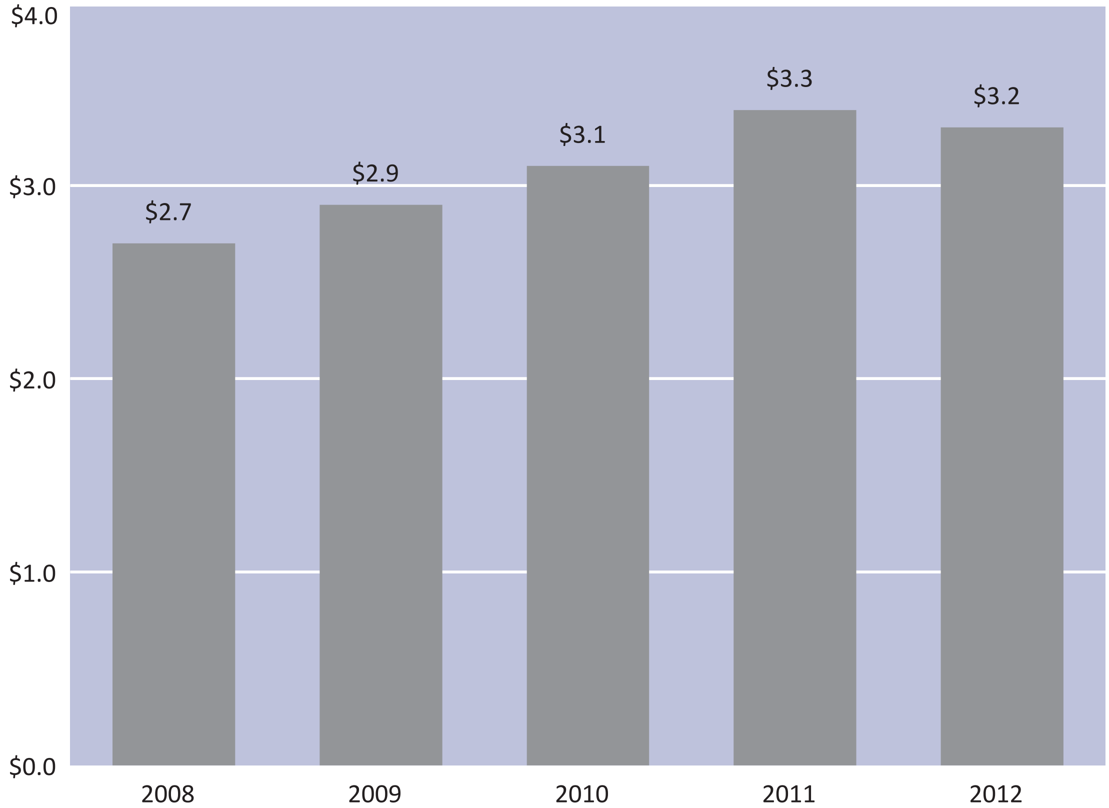
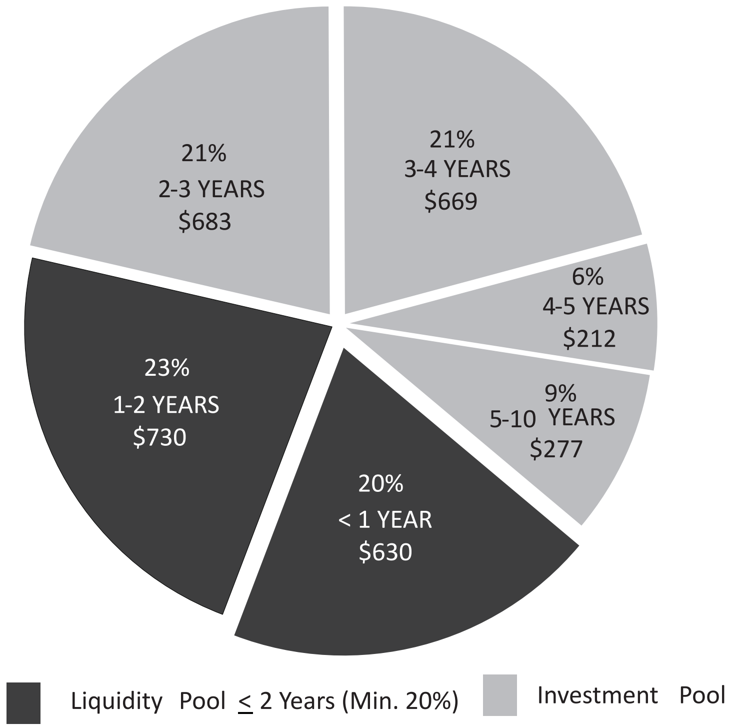


Figure 10

Investment Portfolio by Maturity at December 31, 2012

(Dollars in Millions)



Risk Management

FCSIC monitors and manages insurance risk to minimize the Farm Credit Insurance Fund's exposure to potential losses. Our staff analyzes and evaluates the financial performance and condition of System institutions, maintains continual dialogue with Farm Credit Administration examiners, and reviews reports of examination. When necessary, we request special examinations at System institutions of concern. On a quarterly basis, we screen all System institutions against key performance criteria to identify those institutions that may pose increasing insurance risk.

We also assess risk to the Insurance Fund by

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

During 2012, risk management staff monitored and evaluated trends and other information affecting agriculture and System institutions, including

- conditions in the global and domestic economy, capital markets, and the agricultural and financial sectors;
- trade policy and Government programs that support U.S. agriculture;
- the effects of commodity price volatility on agricultural operations and farmland values in the Midwest;
- the prolonged effects of the housing crisis on agricultural real estate values in certain regions of the country;
- stress in several farm sectors affecting the quality of System institutions' loan portfolios, including the dairy, swine, poultry, forestry, nursery, and biofuels industries;
- negative trends at specific System institutions with declining Financial Institution Rating System ratings; and
- the performance and condition of the four System banks.

The Risk Environment in 2012

The effects of the most recent recession were still evident in 2012. Since mid-2009, the U.S. economy has been on a path of unusually weak recovery, with growth at a moderate but uneven pace. Economic output as measured by real gross domestic product increased by 1.8 percent in 2011 and 2.2 percent in 2012. Employment gains have been modest. While the unemployment rate has fallen from its peak of 10.1 percent in October of 2009, it remained high at 7.8 percent at year-end 2012 and well above pre-recession levels. The housing market showed signs of sustained recovery, but credit availability remained tight for many households and businesses in 2012.

The U.S. banking sector continued to strengthen as asset quality improved. For 2012 institutions insured by the Federal Deposit Insurance Corporation reported the highest level of annual industry profits since 2006, primarily from higher noninterest income and lower provisions for loan losses. Nonetheless, net interest margins continued to compress in the low interest rate environment. The number of problem institutions (that is, those with CAMELS ratings of 4 and 5) declined from 813 in 2011 to 651 in 2012. Fifty-one commercial banks failed in 2012.

The Federal Open Market Committee continued its policy of maintaining the target range for the Fed funds rate of 0 to 0.25 percent. In September 2012, the committee initiated its third round of quantitative easing to put downward pressure on longer-term interest rates, support mortgage markets, and help make broader financial conditions more accommodative.

In December 2012, the Federal Open Market Committee announced that it would maintain its target range for the Fed funds rate as long as the unemployment rate remains above 6.5 percent and the outlook for inflation is no more than 2.5 percent. The timing and magnitude of a change in the direction of interest rates may significantly affect the profitability of agricultural producers who use debt financing in their operations, as well as the market value of the System's liquidity portfolio.

The agricultural sector remained strong in 2012 despite slow growth in the domestic economy and the most severe drought in decades. In February 2013, the U.S. Department of Agriculture estimated that national net farm income in 2012 was $112.8 billion, down 4.3 percent from 2011, and it estimated that net cash income was $135.6 billion, up 0.7 percent from 2011.

Crop production shortfalls from the drought kept crop prices elevated. Crop producers generally fared well because most had Federal crop insurance to mitigate much of the impact of the drought on their operations and their ability to repay loans. Livestock and dairy prices were also elevated, but profit margins were squeezed by high input costs.

USDA projects record-high net farm income of $128 billion for 2013 but also expects the lingering effects of the drought to spill over into 2013.

The System continued to report strong earnings. As of December 31, 2012, it reported $4.1 billion in net income. The increase can be attributed to favorable agricultural conditions and low interest rates, which allowed the banks to re-price debt at favorable rates. Total loans and total assets equaled $191.9 billion and $246.7 billion, respectively.

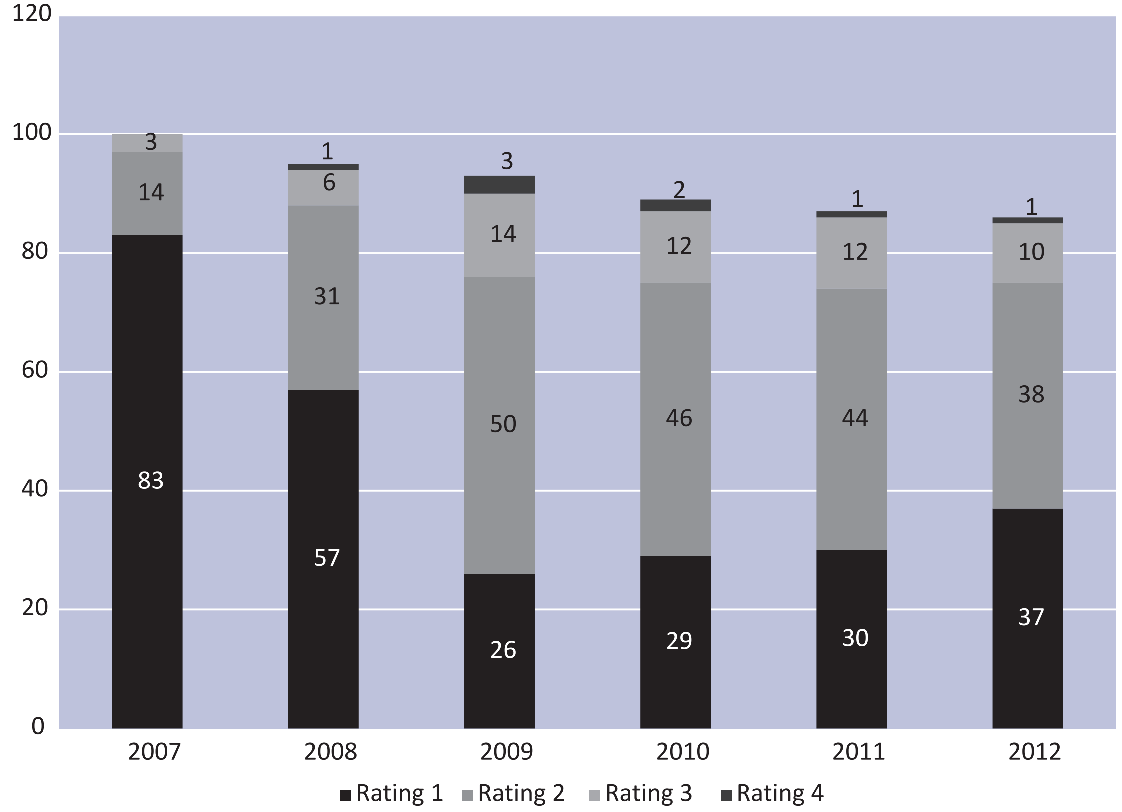
The credit quality of the System's loan portfolio continued to improve in 2012. System loans classified under FCA's Uniform Loan Classification System as "acceptable" or "other assets especially mentioned" increased. As a percentage of total loans, these loans increased to 96.8 percent in 2012 from 96.2 percent in 2011. Nonperforming loans as a percentage of total loans declined to 1.4 percent in 2012 from 1.7 percent in 2011. The primary source of credit quality deterioration remained in cattle, dairy, poultry, biofuels, and housing-related sectors.

Figure 11 shows a summary of composite year-end FIRS ratings for the System banks and associations. The improvement reflects the strong agricultural sector and improving financial conditions and performance at numerous institutions. Institutions with performance-related issues continued to receive higher examination scrutiny and supervisory attention from FCA.

Figure 11

FCS Institution Financial Institution Rating System Composite Year-end Ratings

As of December 31, 2012



Source: The Farm Credit Administration.

Note: Figure 11 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.

Despite Standard and Poor's downgrade of System debt in 2011 (in relation to the downgrade of U.S. sovereign debt), investor demand for System insured obligations remained favorable across the maturity spectrum in 2012. The System continued to benefit from the low interest rate environment, which has enabled the banks to call and issue new debt at lower interest rates. This, in turn, has lowered the cost of funds for the System and improved net interest margins and spreads.

The banks also maintained the quality of their respective liquidity portfolios by purchasing and holding enough high-quality liquid investments, including cash, cash equivalents, and Treasury securities with maturities of less than three years, to cover 15 days of maturing debt. The banks also agreed that the next 30 days of liquidity would come from additional investments that consist of U.S. Government-guaranteed instruments and top-rated commercial paper and Fed funds that mature in 45 days or less. These more highly liquid securities equaled 16 percent of the System's eligible investment portfolio at December 31, 2012.

The Federal Government's fiscal situation became a significant uncertainty during the year. Federal farm programs, which provide benefits to certain agricultural producers, are at risk of being cut or modified. Another aspect of the Federal budget deficit is taxation. Federal Government revenues have been sharply lower over the past several years and were seen as a major issue in the 2012 elections. The Government tightened Federal tax policy for the bioenergy sector at the end of 2011, allowing the ethanol tax credit program to expire.

Long-term resolutions to the Federal Government's current fiscal situation remain uncertain. The American Taxpayer Relief Act of 2012 reauthorized most of the 2008 Farm Bill through September 30, 2013. However, across-the-board reductions in the Federal budget occurred under an automatic sequestration process in early 2013. While many Farm Bill programs are exempt, budget cuts to the USDA could disrupt some programs and related agricultural markets.

In view of these budget cuts and other measures lawmakers may take to reduce the Federal deficit, farm policy could be redesigned, and significant reductions could be made to farm programs in the new Farm Bill. Several proposals for deficit reduction have specifically targeted agricultural programs with mandatory funding, but questions remain about how much and when the Farm Bill baseline may be reduced.

Financial Assistance and Receivership

FCSIC 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. If a System institution were to need financial assistance, we would first have to ensure that the proposed assistance is the least costly means for resolving the institution's problems. By law, we may not provide financial assistance if the cost of liquidation is lower.

We have updated FCSIC's policy statement concerning assistance. At the June 2012 meeting, the FCSIC Board of Directors approved the publication of the draft policy statement for public comment. The comment period ended in October 2012, and a final policy statement was approved in April 2013.

When appointed by FCA, FCSIC has the statutory responsibility to serve as receiver or conservator for System institutions. Upon appointment as receiver, we will take possession of a Farm Credit institution to settle the business operations of the institution, collect the debts owed to the institution, liquidate its property and assets, pay its creditors, and distribute any remaining proceeds to stockholders. 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, we use contractors on an as-needed basis. These contractors provide knowledgeable and readily available staff resources while allowing us to contain costs during periods of limited or no activity.

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

As discussed earlier, we are pursuing a legislative initiative to modernize our resolution authorities. Since 1987, there have been no substantive amendments of the Farm Credit Act relating to FCSIC's resolution authorities. During 2011 and continuing into 2012, we developed proposed legislative language to enhance FCSIC's receivership and conservatorship authorities contained in the Farm Credit Act. The proposal is modeled after FDIC's current resolution powers, but tailored for the Farm Credit System.

Clarifying and enhancing these powers, which have not been substantially updated since FCSIC's creation in 1988, will make any receivership or conservatorship that might occur less costly and more efficient. We have developed a detailed legislative proposal clarifying the receivership claims process, the authority to repudiate contracts, and the treatment of certain "qualified financial contracts." The proposal would also limit judicial power to attach receivership property, to review claims, or to restrain a conservator's or receiver's powers; it would also authorize organization of "bridge" banks—temporary institutions useful in resolution of troubled financial institutions.

During the year, we hired a consulting firm to assist in planning for the potential resolution of any FCS institutions that may become troubled and to help enhance resolution processes and authorities.

We have a number of Board-approved policy statements that provide guidance related to resolution activities, including appraisals of real estate securing nonperforming assets, insurance of assets that come under FCSIC control, and environmental hazards assessments of real estate securing nonperforming assets.

FARM CREDIT SYSTEM INSURANCE CORPORATION
McLean, Virginia

FINANCIAL STATEMENTS
December 31, 2012 and 2011

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INDEPENDENT AUDITOR'S REPORT

Board of Directors
Farm Credit System Insurance Corporation
McLean, Virginia

We have audited the accompanying financial statements of Farm Credit System Insurance Corporation, which comprise the statements of financial position as of December 31, 2012 and 2011, and the related statements of income and expenses and changes in insurance fund, and cash flows for the years then ended, and the related notes to the financial statements.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with accounting principles generally accepted in the United States of America; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditors' Responsibility

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 from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditors' judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Farm Credit System Insurance Corporation as of December 31, 2012 and 2011, and the results of its operations and its cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

Other Reporting Required by *Government Auditing Standards*

In accordance with *Government Auditing Standards*, we have also issued our report dated April 11, 2013 on our consideration of Farm Credit System Insurance Corporation's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, 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 result of that testing, and not to provide an opinion on internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering Farm Credit System Insurance Corporation's internal control over financial reporting and compliance.

CliftonLarsonAllen LLP

Calverton, Maryland
April 11, 2013

CliftonLarsonAllen

CliftonLarsonAllen LLP
www.cliftonlarsonallen.com

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, in accordance with the 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 financial statements of Farm Credit System Insurance Corporation, which comprise the statement of financial condition as of December 31, 2012, and the related statements of income and expenses and changes in insurance fund, and cash flows for the year then ended, and the related notes to the financial statements, and have issued our report thereon dated April 11, 2013.

Internal Control Over Financial Reporting

In planning and performing our audit of the financial statements, we considered Farm Credit System Insurance Corporation's internal control over financial reporting (internal control) to determine the audit procedures that are appropriate in the circumstances for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of Farm Credit System Insurance Corporation's internal control. Accordingly, we do not express an opinion on the effectiveness of Farm Credit System Insurance Corporation's internal control.

A *deficiency in internal* control 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 and correct, misstatements on a timely basis. A *material weakness* is a deficiency, or a combination of deficiencies, in internal control, such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected on a timely basis. A *significant deficiency* is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance.

Our consideration of internal control was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies. Given these limitations, during our audit we did not identify any deficiencies in internal control that we consider to be material weaknesses. However, material weaknesses may exist that have not been identified.

Compliance and Other Matters
As part of obtaining reasonable assurance about whether Farm Credit System Insurance Corporation's financial statements are free from material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, and contracts, 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*.

Purpose of this Report
The purpose of this report is solely to describe the scope of our testing of internal control and compliance and the result of that testing, and not to provide an opinion on the effectiveness of the entity's internal control or on compliance. This report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the entity's internal control and compliance. Accordingly, this communication is not suitable for any other purpose.

CliftonLarsonAllen LLP

Calverton, Maryland
April 11, 2013

FINANCIAL STATEMENTS

Farm Credit System Insurance Corporation
Statements of Financial Condition
As of December 31, 2012 and 2011
(Dollars in thousands)

	2012	2011
Assets		
Cash and cash equivalents	$ 5,079	$ 1,101
Investments in U.S. Treasury Obligations (Note 3)	3,196,211	3,266,285
Accrued interest receivable	12,667	26,264
Premiums receivable (Note 4)	84,266	98,699
Total assets	**$ 3,298,223**	**$ 3,392,349**
Liabilities and Insurance Fund		
Accounts payable and accrued expenses (Note 6)	$ 287	$ 385
Total liabilities	287	385
Farm Credit Insurance Fund		
Allocated Insurance Reserves Accounts Allocated in 2012	0	221,851
Unallocated Insurance Fund Balance	3,297,936	3,170,113
Total Insurance Fund	3,297,936	3,391,964
Total liabilities and Insurance Fund	**$ 3,298,223**	**$ 3,392,349**

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, 2012 and 2011
(Dollars in thousands)

	2012	2011
Income		
Premiums (Note 4)	$ 84,298	$ 97,257
Interest income	46,842	72,616
Total income	**131,140**	**169,873**
Expenses		
Administrative operating expenses (Note 6)	3,317	3,255
Total Expenses	**3,317**	**3,255**
Net Income	**127,823**	**166,618**
Farm Credit Insurance Fund – beginning of year	**3,391,964**	**3,225,346**
Payments to AIRAs Accountholders	**221,851**	**0**
Farm Credit Insurance Fund – end of year	**$ 3,297,936**	**$ 3,391,964**

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, 2012 and 2011
(Dollars in thousands)

	2012	2011
Cash flows from operating activities		
Net income	$ 127,823	$ 166,618
Adjustments to reconcile net income to net cash provided by operating activities:		
(Increase) decrease in premium receivable	14,433	(18,730)
(Increase) decrease in accrued interest receivable	13,597	(4,720)
Net amortization and accretion of investments	25,957	26,681
Increase (decrease) in accounts payable and accrued expenses	(98)	46
Net cash provided by operating activities	**181,712**	**169,895**
Cash flows from investing activities		
Payments for purchase of U. S. Treasury Obligations	(1,653,663)	(1,291,379)
Proceeds from maturity of U.S. Treasury Obligations	1,697,780	972,754
Net cash provided by (used in) investing activities	**44,117**	**(318,625)**
Cash flows from financing activities		
Payment to AIRAs Accountholders	(221,851)	0
Net cash used in financing activities	**(221,851)**	**0**
Net change in cash and cash equivalents	3,978	(148,730)
Cash and cash equivalents, beginning of year	1,101	149,831
Cash and cash equivalents, end of year	**$ 5,079**	**$ 1,101**

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 (the Corporation or FCSIC) 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 (Farm Credit Act), (insured obligations). Each bank in the Farm Credit System (System) participating in insured obligations is an insured System bank. At December 31, 2012, there were four insured System banks and 82 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 Farm Credit 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, 2012, for each of the components of the Corporation's insurance responsibilities were $197.5 billion of insured obligations, and $2 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 Farm Credit Act.

Under section 5.63 of the Farm Credit 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.

This information is an integral part of the accompanying financial statements.

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, 2012, the Corporation held $4.9 million in overnight Treasury Certificates maturing on January 2, 2013, with an investment rate of zero percent, and $178,885 in cash.

Investments in U.S. Treasury Obligations—Section 5.62 of the Farm Credit 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 FASB ASC 320 (formerly Statement of Financial Accounting Standard 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 2012 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 $264,533 in 2012 and $249,895 in 2011.

This information is an integral part of the accompanying financial statements.

Note 3 — Investments

In addition to the amounts referenced in Note 2, Cash and Cash Equivalents, at December 31, 2012 and 2011, 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, 2012				
U.S. Treasury Notes	$ 3,196,211	$ 41,496	$ (433)	$ 3,237,274
December 31, 2011				
U.S. Treasury Notes	$ 3,266,285	$ 56,045	$ (581)	$ 3,321,749

The amortized cost and estimated market value of U.S. Treasury obligations at December 31, 2012, by contractual maturity, are shown below.

($ in thousands)	Amortized Cost	Estimated Market Value
Due in one year or less	$ 625,019	$ 629,800
Due after one year through five years	2,294,540	2,322,353
Due after five years through ten years	276,652	285,121
	$ 3,196,211	$ 3,237,274

This information is an integral part of the accompanying financial statements.

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 Farm Credit 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 secure base amount (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 will require 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 the 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 Farm Credit System Financial Assistance Corporation (FAC) stockholders.

The Farm Credit 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 certain government-guaranteed loans and investments) 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 SBA 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 2012, the Board of Directors set premium rates at its January 19, 2012, meeting at 5 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 of Directors again reviewed premiums at its June 14, 2012 meeting. The Board of Directors voted to maintain the premium accrual rate on average adjusted insured debt at 5 basis points 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 for the remainder of 2012. In 2012, outstanding insured obligations increased by $13.3 billion (7.2 percent). At December 31, 2012, both of the unallocated Insurance Fund and the total Insurance Fund were 1.93 percent of adjusted insured obligations.

On January 24, 2013, the Board of Directors set premium rates for 2013, increasing the premium rate on adjusted insured debt outstanding from 5 basis points 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 Farm Credit Act requires the Corporation to establish Allocated Insurance Reserves Accounts (AIRAs) for each System bank and an account for the stockholders of the FAC. If at the end of any calendar year the unallocated Insurance Fund is at the SBA, the Corporation is to segregate any excess balances into these AIRAs. In 2011, the Corporation's Board revised the Policy Statement on the Secure Base Amount and Allocated Insurance Reserves Accounts which provides guidelines for implementing this statutory authority. If at the end of any calendar year, the aggregate of the amounts in the Insurance Fund exceeds the SBA, 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 2011, this resulted in the transfer of $221.85 million to the A1RAs. The amount was allocated as follows:

FAC Stockholders	(10%) $ 22.18 million
Farm Credit System Banks	(90%) $ 199.67 million

The AIRAs balances are recorded as part of the Insurance Fund until approved for payment by the Corporation's Board. AIRAs balances may be used to absorb any insurance losses and claims. Furthermore, the Board of Directors has discretion to limit or restrict the AIRAs payments. In accordance with the Corporation's policy statement, any AIRAs balances do not count in measuring the Insurance Fund's compliance with the SBA.

In April 2012, after completion of the Corporation's year-end audit, the Board of Directors authorized the payment of the $221.85 million transferred at year-end 2011 to the account holders. Payments were made in May 2012.

At yearend 2012, the Insurance Fund was below the SBA by $119 million. Consequently no funds were available to transfer to the AIRAs.

This information is an integral part of the accompanying financial statements.

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 the office space for the remaining term of $146,531 for 2013 and $150,899 for 2014. The Corporation recorded lease expense (including operating cost assessments) of $145,157 and $138,443 for 2012 and 2011, 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 zero payables due to the FCA at December 31, 2012 and $92,330 at December 31, 2011. The Corporation purchased services for 2012 which totaled $401,176 compared with $336,387 for 2011.

The Corporation provides assistance to the FCA under the same Interagency Agreement, recognizing revenue of zero for 2012 and 2011. At December 31, 2012, and 2011, the Corporation did not have any receivables from the FCA.

Note 7 — Subsequent Events

Management evaluated subsequent events through April 11, 2013, the date the financial statements were available to be issued. Events or transactions occurring after December 31, 2012, but prior to April 11, 2013, that provided additional evidence about conditions that existed at December 31, 2012, have been recognized in the financial statements for the year ended December 31, 2012. Events or transactions that provided evidence about conditions that did not exist at December 31, 2012, but arose before the financial statements were available to be issued have not been recognized in the financial statements for the year ended December 31, 2012.

This information is an integral part of the accompanying financial statements.

Management Report on Internal Control Over Financial Reporting

April 11, 2013

FCSIC's management is responsible for establishing and maintaining adequate internal control over financial reporting for the Corporation.

FCSIC is an independent U.S. Government-controlled corporation. Our primary purpose is to ensure the timely payment of principal and interest on insured debt obligations issued on behalf of System banks. The System is a nationwide Government-sponsored enterprise of privately owned banks and affiliated associations that serve borrowers and related entities in the agricultural sector. By protecting investors, we help maintain a dependable source of funds for the farmers, ranchers, and other borrowers of the System.

FCSIC actively monitors and manages insurance risk in order to minimize the Farm Credit Insurance Fund's exposure to potential losses. We also must be prepared to serve as conservator or receiver of any System bank or association when appointed by the Board of the Farm Credit Administration.

Our management has completed an assessment of the effectiveness of the internal controls and financial management systems in effect during 2012 in accordance with guidelines provided by the Office of Management and Budget (OMB) in consultation with the Comptroller General (OMB Circular A-123, "Management's Responsibility for Internal Control"). The objective of these controls and systems is to provide reasonable assurance that

- obligations and costs comply with applicable laws;
- all assets are safeguarded against waste, fraud, unauthorized use, and mismanagement;
- revenues and expenditures applicable to our operations are recorded and accounted for properly; and
- financial and statistical reports will be reliable, complete, and timely, and accountability of the assets will be maintained.

Based on the established guidelines and the assessment performed, we concluded that as of December 31, 2012, the internal control over financial reporting was effective.

In addition, as stated in the accompanying report, the Corporation's independent auditor, Clifton Larson Allen LLP, did not identify any material weaknesses in the effectiveness of FCSIC's internal control over financial reporting as of December 31, 2012.

Dorothy L Nichols

Dorothy L. Nichols
Chief Operating Officer

C Richard Pfitzinger

C. Richard Pfitzinger
Chief Financial Officer

Alan J. Glenn

Alan J. Glenn
Director of Risk Management

Performance Management Program

FCSIC has a mandate to ensure the timely payment of principal and interest on insured Farm Credit System debt securities, and to serve as receiver or conservator of any institution placed into conservatorship or receivership by the Farm Credit Administration Board. As a result, we have three fundamental program goals:

1. Building and managing the Insurance Fund to protect investors
2. Detecting, evaluating, and managing insurance risk
3. Maintaining the capability to act as receiver or conservator as the need arises

Performance Measures

1. Building and managing the Insurance Fund to protect investors

To maintain the solvency of the Insurance Fund, we must adjust insurance premium assessments when appropriate and manage assets to optimize investment returns, while maintaining appropriate liquidity to carry out our mission. Congress established a statutory requirement for the Insurance Fund to be maintained at a secure base amount equal to 2 percent of adjusted insured obligations or such other percentage as FCSIC in its sole discretion determines to be actuarially sound.

FCSIC assesses the effectiveness of its performance in achieving this goal through the following:

- Reviewing semiannually the need for adjustments to insurance premium assessments
- Measuring investment performance by comparing the portfolio's average yield with peer investment funds that have similar investment parameters for quality and maturity
- Monitoring the level of the Insurance Fund every month as compared with the secure base amount target level and reporting results to the Board of Directors

The ability of FCSIC to maintain the Insurance Fund at the secure base amount may be affected by events beyond the control of the Corporation, such as insurance losses.

2. Detecting, evaluating, and managing insurance risk

We measure progress towards this program goal by the extent to which emerging problems are promptly detected and insurance losses are minimized. We use financial indicators to monitor conditions and trends, and we analyze and report data before losses become likely. In periods of probable or actual insurance claims, the ratio of estimated losses to actual losses is an indicator of our ability to assess prospective loss exposure. As guidance, management uses criteria specified in FCSIC's allowance for loss procedure and the Financial Accounting Standards Board's Accounting Standards Topic 450, Contingencies. Timely evaluation of the Insurance Fund's risk exposure is critical to preserving the Insurance Fund's solvency. FCSIC uses Farm Credit Administration reports of examination to evaluate risks to the Insurance Fund. From time-to-time we independently examine and require information from System institutions.

3. Maintaining the capability to act as receiver or conservator as the need arises

FCSIC is required to serve as receiver or conservator of System banks and associations when appointed by the Farm Credit Administration. This program goal requires us to maintain readiness through periodic staff training and evaluation of contractors' capabilities. We must ensure that we have the resources we need to manage receiverships or conservatorships in case the need arises.

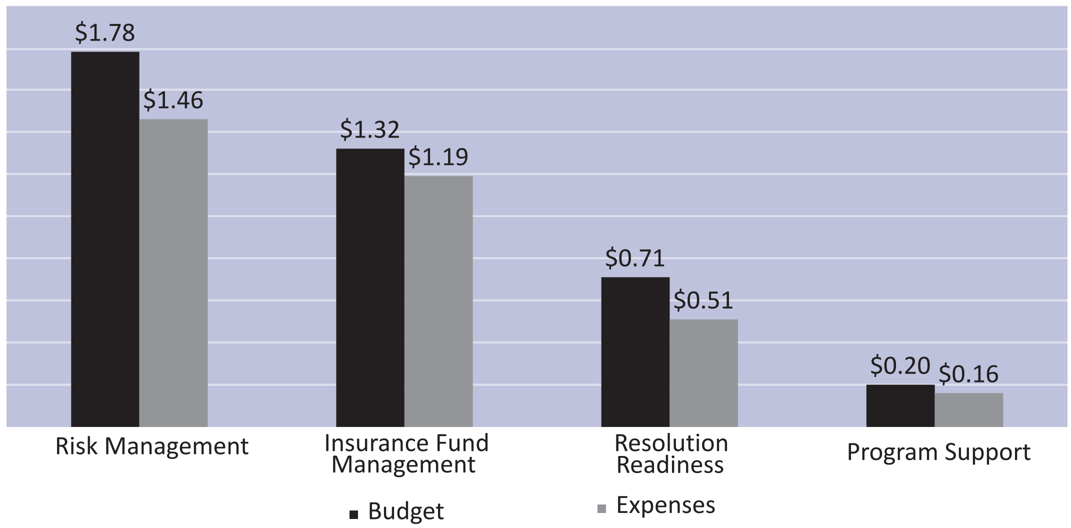
We use the following measures to determine the effectiveness of our receivership operations:

- Whether all claims received initial processing within a period specified according to the size and complexity of the individual case
- Operating costs as a percentage of total assets
- Actual asset recovery returns as a percentage of net realizable asset values

Figure 12

2012 Budget and Expenditure by Program

(Dollars in Millions)



Strategic Goal	Strategic Objectives	High Priority Performance Goals	
Investors in insured debt are protected from loss without recourse to a joint and several liability call	The Farm Credit Insurance Fund remains strong and adequately financed.	Maintain the Insurance Fund at the statutory 2 percent secure base amount.	See pages 16-18 for 2012 results.
	FCSIC promptly identifies and responds to potential risks to the Insurance Fund.	Identify and address risks to the Insurance Fund.	See pages 23-26 for 2012 results.
		Disseminate data and analyses on issues to the FCSIC Board, the public, and other stakeholders.	See pages 8-9 and 23-26 for 2012 results.
		Effectively administer temporary financial assistance programs subject to the statutory least-cost requirements.	See page 27 for 2012 results.
	FCSIC resolves failure of FCS institutions in the manner least-costly to the Insurance Fund.	Market failing institutions to qualified and interested potential bidders.	See page 27 for 2012 results.
	The public, insured investors, and FCS institutions have access to accurate and easily understood information about our insurance program.	Provide information about the benefits of the insurance program through our website, annual report, and other outlets.	See the FCSIC website for additional information.

Glossary

C

CAMELS—A system that supervisory authorities use to rate banking institutions. The system considers six factors, each of which supplies a letter in the acronym: capital adequacy, asset quality, management quality, earnings, liquidity, and sensitivity to market risk.

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, FCSIC, and FCA operate.

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—Based in Jersey City, New Jersey, the Funding Corporation 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.

Federal Open Market Committee—The branch of the Federal Reserve Board that determines the direction of monetary policy. The committee is composed of the Board of Governors, which has seven members, and five Federal Reserve Bank presidents. The president of the Federal Reserve Bank of New York serves continuously, while the presidents of the other Reserve Banks rotate their service of one-year terms.

Financial Institution Rating System (FIRS)—The FIRS is similar to the Uniform Financial Institutions Rating System used by other Federal banking regulators except that the FIRS reflects 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.

G

Government-sponsored enterprise (GSE)—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

AIRAs	Allocated Insurance Reserves Accounts
CAMELS	**C**-Capital adequacy; **A**-Asset quality; **M**-Management quality; **E**-Earnings; **L**-Liquidity; and **S**-Sensitivity to Market Risk
CIPA	Contractual Interbank Performance Agreement
Farm Credit Act, the Act	Farm Credit Act of 1971, as amended
FCA	Farm Credit Administration
FCS	Farm Credit System
FCSIC	Farm Credit System Insurance Corporation
FDIC	Federal Deposit Insurance Corporation
FIRS	Financial Institution Rating System
Funding Corporation	Federal Farm Credit Banks Funding Corporation
Systemwide debt securities	Federal Farm Credit Banks Consolidated Systemwide debt securities
TIPS	Treasury Inflation-Protected Securities
USDA	U.S. Department of Agriculture

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 R. Fayer	Senior Resolution Specialist
Wade Wynn	Senior Risk Analyst
Pam Ngorskul	Accountant
Jeremy L. Del Moral	Financial Analyst
Barbara Loggins	Senior Administrative Specialist
Molly Sproles	Administrative Management Assistant

Contact Information

To obtain Farm Credit System quarterly and annual information statements, contact the Federal Farm Credit Banks Funding Corporation at the following address:

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

These documents are also available on the Funding Corporation's website at www.farmcreditfunding.com.

To obtain copies of the Farm Credit Administration's Annual Report on the Farm Credit System and the FCA Annual Performance and Accountability Report, contact FCA at the following address:

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

These documents are also available on the FCA website at www.fca.gov.

FCSIC — Insured Banks (as of January 1, 2013)

To obtain copies of quarterly and annual reports of a Farm Credit System bank and its affiliated associations, please contact the bank directly. The mailing addresses, website addresses, and telephone numbers of all four System banks are provided below.

AgFirst Farm Credit Bank	P.O. Box 1499 Columbia, SC 29202-1499 (803) 799-5000 www.agfirst.com
AgriBank, FCB	30 E. 7th Street, Suite 1600 St. Paul, MN 55101-4914 (651) 282-8800 www.agribank.com
CoBank	P.O. Box 5110 Denver, CO 80217-5110 (303) 740-4000 www.cobank.com
Farm Credit Bank of Texas	P.O. Box 202590 Austin, TX 78720-2590 (512) 465-0400 www.farmcreditbank.com

Note: Information contained on these websites is not incorporated by reference into this annual information statement and you should not consider information contained on these websites to be part of this annual information statement.

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