



# FCSIC

Farm Credit System Insurance Corporation

## 2018 Annual Report



# Protecting Investors in Agriculture and Rural America



# 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.





July 9, 2019

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 2018. 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 as of December 31, 2018, was \$4.95 billion. In 2018, we earned \$212.5 million in insurance premiums from Farm Credit System banks, and \$73.1 million in investment income. In 2019, we expect to incur \$4.3 million in operating costs.

FCSIC is proud of the role we play in supporting the safety and soundness of the Farm Credit System, and we are committed to faithfully fulfilling our mission.

Sincerely,

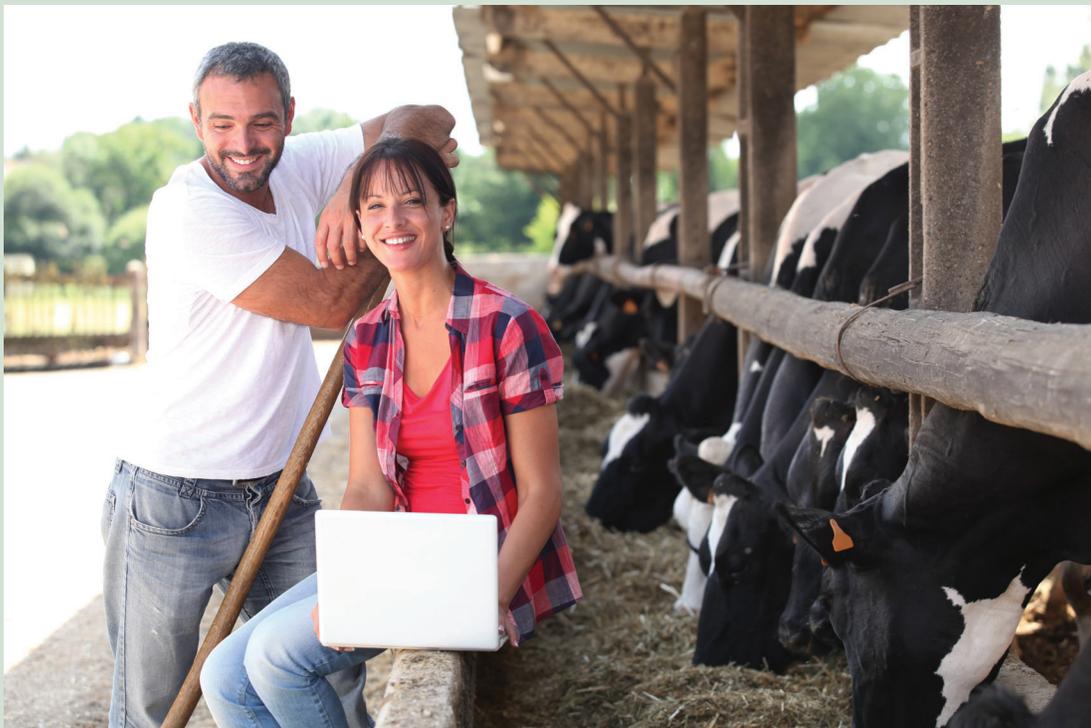
A handwritten signature in black ink, appearing to read "Jeffery S. Hall". The signature is fluid and cursive, with the first name "Jeffery" and last name "Hall" clearly distinguishable.

Jeffery S. Hall  
Chairman

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

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## Message from the Chairman

I am pleased to present the 2018 Annual Report of the Farm Credit System Insurance Corporation. It is gratifying to note that, for the 29th consecutive year since we began issuing financial statements, our independent public auditor has issued unmodified or unqualified opinions on those statements. In 2017, we expanded our audit coverage to include an audit of our internal control over financial reporting. The enclosed opinion letter indicates that the financial statements of the Farm Credit Insurance Fund, of which we are stewards, are fairly and accurately presented and FCSIC maintained effective internal control over financial reporting.

FCSIC's net income for 2018 was \$282.0 million, compared with \$394.8 million for the previous year. The Insurance Fund balance as of December 31, 2018, was \$4.95 billion, compared with \$4.85 billion at year-end 2017.

At the end of 2017, our Insurance Fund exceeded the statutory secure base amount and we transferred \$175.8 million to the allocated insurance reserves accounts (AIRAs). In accordance with the Farm Credit Act of 1971, as amended, the FCSIC board subsequently voted to disburse the AIRAs to System banks and the holders of the Financial Assistance Corporation (FAC) stock. The payment of \$13.1 million to the holders of the FAC stock, originally issued with \$55.8 million par value, fully retired the FAC stock in March 2018.

Revenue from insurance premiums paid by Farm Credit System banks was \$212.5 million for 2018, compared with \$340.8 million for 2017. Premium revenue decreased because assessment rates went down from 15 basis points in 2017 to 9 basis points in 2018. Interest income for 2018 totaled \$73.1 million, compared with \$57.7 million in 2017.

At the end of 2018, our Insurance Fund exceeded the statutory secure base amount and we transferred \$66.1 million to the AIRAs. In accordance with the Farm Credit Act of 1971, as amended, the FCSIC board subsequently voted to disburse the AIRAs to the System banks in March 2019.

In accordance with the requirements of the Federal Managers' Financial Integrity Act of 1982, management conducts an annual assessment of FCSIC's internal controls. The 2018 assessment found 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.

We will continue to carry out our mission and work in 2019 to achieve our strategic goals and objectives. 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,



Jeffery S. Hall

## Board of Directors

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

Currently, the two members of the board of directors are Chairman Jeffery S. Hall and Glen R. Smith. We are sad to report that, in May 2019, Board Member Dallas P. Tonsager passed away. He served two terms on both the FCSIC board of directors and the FCA board — first, from 2004 to 2009 and again from 2015 to 2019. He served as chairman of the FCSIC board from 2015 to 2016 and as chairman and CEO of the FCA board from 2016 to 2019.



## Jeffery S. Hall



Jeffery S. Hall is chairman of the board of directors of FCSIC. He was elected to this position on November 29, 2016. Mr. Hall has served on the FCSIC board and on the FCA board since his appointment by President Barack Obama on March 17, 2015. He is serving a term that expired on October 13, 2018.

Before coming to FCSIC and FCA, Mr. Hall was president of The Capstone Group, an association management and consulting firm that he cofounded in 2009. From 2001 to 2009, he was the state executive director for the U.S. Department of Agriculture's (USDA's) Farm Service Agency in Kentucky. In that role, he was responsible for farm program and farm loan program delivery and compliance.

From 1994 to 2001, Mr. Hall served as assistant to the dean of the University of Kentucky, College of Agriculture, advising the dean on state and federal legislative activities and managing a statewide economic development initiative called Ag-Project 2000.

Mr. Hall also served as a senior staff member in the office of U.S. Senator Mitch McConnell from 1988 to 1994. During that time, he was the legislative assistant for agriculture, accountable for internal and external issue management.

Before joining Senator McConnell's staff, Mr. Hall served on the staff of the Kentucky Farm Bureau Federation. Over his 30-year career in agriculture, he has held leadership positions in the following nonprofits: the Kentucky Agricultural Council, the Agribusiness Industry Network, the Louisville Agricultural Club, the Kentucky Agricultural Water Quality Authority, and the Governor's Commission on Family Farms.

Mr. Hall was raised on a family farm in southern Indiana, which has been in his family for nearly 200 years. He is currently a partner in the farm with his mother and sister. Mr. Hall received a Bachelor of Science degree from Purdue University.

## Glen R. Smith



Glen R. Smith was appointed to the Farm Credit System Insurance Corporation board of directors and Farm Credit Administration board by President Donald Trump on December 8, 2017. Mr. Smith will serve a term that expires May 21, 2022.

Mr. Smith is a native of Atlantic, Iowa, where he was raised on a diversified crop and livestock farm. His farm experience started at a very early age, after his father was involved in a disabling farm accident. He graduated from Iowa State University in 1979 with a Bachelor of Science in agricultural business and accepted a position with Doane Agricultural Services as state manager of the company's farm real estate division.

In 1982, Mr. Smith and his wife, Fauzan, moved back to his hometown and started farming and developing his ag service business. Today, their family farm, Smith Generation Farms Inc., has grown to encompass about 2,000 acres devoted to corn, soybeans, hay, and a small beef cow herd.

Mr. Smith is co-owner and founder of Smith Land Service Co., an ag service company that specializes in farm management, land appraisal, and farmland brokerage, serving about 30 Iowa counties. From 2001 to 2016, he was also co-owner and manager of S&K Land Co., an entity involved in the acquisition, improvement, and exchange of Iowa farmland.

Mr. Smith has served on numerous community, church, and professional boards. He was elected to the Atlantic Community School Board of Education on which he served for nine years; during most of this time, he served as either president or vice president.

In 1990, he earned the title of Accredited Rural Appraiser from the American Society of Farm Managers and Rural Appraisers. In 2000, he served as president of the Iowa chapter of that organization. He is a life-long member of the Farm Bureau, Iowa Corn Growers Association, Iowa Soybean Association, and Iowa Cattlemen's Association.

The Smiths have four grown children and three grandchildren. Three of their children are involved in production agriculture. Their son Peter has assumed managerial responsibilities for both the family farm and business.

# In Memoriam: Dallas P. Tonsager

June 24, 1954 – May 21, 2019



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## 2018 — Year in Review

### FCSIC's 25-Year Anniversary of Full Operations

FCSIC is a federal government-controlled corporation established by the Agricultural Credit Act of 1987. Our first year of full operations was 1993. That year, the Insurance Fund grew to \$642.0 million, insuring \$53.7 billion in System debt. We had a nine-member core staff and relied on a mixture of public- and private-sector contractors for support services.

Twenty-five years later, the Insurance Fund is over seven times larger at \$4.95 billion, insuring \$282.5 billion of System debt. Yet we have continued to operate effectively with a small staff of 11 since 2013. We continue to leverage our resources by purchasing support services from public- and private-sector contractors to ensure the efficient administration of our programs.

Over the past three years, FCSIC's operating costs remained unchanged at \$3.7 million. Our operating costs as a percentage of total assets represented 7 basis points for 2018, an improvement of 1 basis point over 2017. In September 2018, the board of directors approved budgets for 2019 and 2020. The 2019 budget is \$4.3 million, an increase of 2.9 percent over the 2018 budget.

### Legislative Initiative Achieved

As part of our strategic plan, we pursued a legislative initiative to enhance the Corporation's receivership and conservatorship authorities. We achieved our principal goal to ensure that FCSIC's authorities are commensurate with those of other federal receivers and conservators. In December 2018, Congress enacted the Agriculture Improvement Act of 2018 (2018 Farm Bill), which clarified and updated FCSIC's statutory authorities to act as receiver or conservator for a System institution.

Congress stated its intent in the 2018 Farm Bill Conference Report that FCSIC's authorities be "functionally equivalent to the parallel authorities of the Federal Deposit Insurance Corporation." This legislation will improve our ability to protect investors and reduce the cost of resolving a troubled System institution. Currently, the System is in a safe and sound condition and no institution is in danger of failing.

### Payoff of FAC Obligation

In March 2018, the Corporation's board of directors approved a payment of \$175.8 million in excess insurance funds to System institutions. Of this amount, \$13.1 million was used to retire the remaining stock that System institutions held in the Financial Assistance Corporation (FAC), which was established by the Agricultural Credit Act of 1987 to provide financial assistance to the System. FAC stockholders were System institutions that supplied a portion of the funds needed for the System's survival during the 1980s farm crisis.

In 1996, Congress directed FCSIC to allocate 10 percent of any excess insurance funds at the end of each calendar year to FAC stockholders, who held approximately \$55.8 million in outstanding shares. Through distributions of excess insurance funds over the years, FCSIC repaid this amount to FAC stockholders, fulfilling its statutory obligation. With the retirement of this final \$13.1 million in FAC stock, there are no more outstanding shares and the FAC stockholders account was closed.

## Management Changes

In July 2018, C. Richard Pfitzinger became the Corporation's Chief Operating Officer, succeeding Dorothy L. Nichols. Mr. Pfitzinger has been with the Corporation since 1992 and previously served as Director of Risk Management and Chief Financial Officer. He has more than 30 years of financial institution regulatory and insurance experience.

Dorothy L. Nichols served with distinction as FCSIC's second Chief Operating Officer since 2006. She joined FCSIC in 1995, serving as General Counsel. Ms. Nichols guided the Corporation through a period of significant growth. In 2006 the Insurance Fund totaled \$2.3 billion, insuring System obligations of \$135.2 billion. By 2018 the Insurance Fund had grown to \$4.95 billion, insuring \$282.5 billion of System obligations. To enhance FCSIC's ability to help System banks in a liquidity crisis, Ms. Nichols led efforts that resulted in FCSIC obtaining a \$10 billion line of credit agreement with the Federal Financing Bank, a government corporation within the U.S. Department of Treasury that provides funds to eligible federal agencies. During her 12-year tenure as Chief Operating Officer, she established many of the risk management practices we use today. She also chaired the FCSIC Investment Committee, which actively manages the Insurance Fund's investments, which grew from \$1.4 billion in 2006 to \$4.4 billion in 2018. She retired in July 2018 with more than 36 years of federal government service.

FCSIC also made several other senior management changes. In March, Andrew Grimaldi became Chief Financial Officer, replacing Emily Dean who retired after serving FCSIC with distinction for five years. In September, Howard Rubin, who was serving as FCSIC's General Counsel, became the new Chief Risk Officer, which includes the duties of the Director of Risk Management position. Lynn Powalski joined FCSIC as General Counsel in February 2019.



Table 1

## Selected Financial Statistics for the Farm Credit System Insurance Corporation

(Dollars in Millions)

BALANCE SHEET	2018	2017	2016
Total assets	\$4,954.2	\$4,848.4	\$4,453.5
Total liabilities	0.4	0.7	0.6
Insurance Fund balance			
Allocated insurance reserves accounts	66.1	175.8	0
Unallocated Insurance Fund balance	4,887.8	4,671.9	4,452.9
OPERATIONS			
Revenues	285.7	398.5	418.4
Operating expenses	3.7	3.7	3.7
Insurance expense	0	0	0
Net income	\$282.0	\$394.8	\$414.7

# The Farm Credit System

## Structure and Funding

The Farm Credit System is a network of federally chartered, cooperative lending institutions owned by the agricultural and rural customers it serves, including farmers, ranchers, producers and harvesters of aquatic products, agricultural cooperatives, and farm-related businesses. As of January 1, 2019, the System had 4 banks and 69 associations. Each association has its own chartered territory and is affiliated with one of the four banks. See Table 2 for the combined financial statistics for the banks and associations.

Table 2

### Combined Farm Credit System Statistics

(Dollars in Billions)

	2018	2017	2016
Insured debt outstanding <sup>1</sup>	\$282.5	\$266.0	\$258.4
Production agriculture:			
Real estate mortgage loans	124.9	119.5	114.5
Production and intermediate-term loans	53.4	51.7	50.3
Agribusiness loans <sup>2</sup>	46.1	42.2	39.6
Communication loans	6.8	6.3	6.0
Energy, water, and waste disposal loans	22.4	21.7	21.4
Rural residential real estate loans	7.3	7.3	7.2
Agricultural export loans	6.6	5.6	5.5
Lease receivables	3.6	3.7	3.5
Loans to other financing institutions	0.8	0.8	0.8
Cash and investments	67.9	61.8	62.6
Net income	5.3	5.2	4.8
Nonperforming loans as a percentage of total loans	0.8%	0.8%	0.8%

1. Insured debt outstanding is based on System institution call report information and reflects the book value of insured debt outstanding plus accrued interest as of December 31, 2018, 2017, and 2016. (Book value excludes fair-value adjustments.)

2. As of December 31, 2018, agribusiness loans consisted of loans to cooperatives of \$17.6 billion, processing and marketing loans of \$24.8 billion, and farm-related business loans of \$3.7 billion.

Associations receive funding from their affiliated bank and lend directly to their owner-borrowers, providing a consistent and reliable source of agricultural and rural credit throughout the United States, including the Commonwealth of Puerto Rico. One of the System banks (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 consolidated Systemwide debt securities. The banks own and use the Federal Farm Credit Banks Funding Corporation (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. Systemwide debt securities are the general unsecured joint and several obligations of the banks. Systemwide debt securities are not obligations of and are not guaranteed by the U.S. government. In addition, Systemwide debt securities are not the direct obligations of the System associations and, as a result, the capital of the associations may not be available to support principal and interest payments on Systemwide debt securities.

### **Investor Protection**

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

### **Regulatory Oversight**

FCA is the regulator of the Farm Credit System, responsible for the examination, supervision, and regulation of each System institution. FCA is an independent agency in the executive branch of the U.S. government and derives its 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 System.

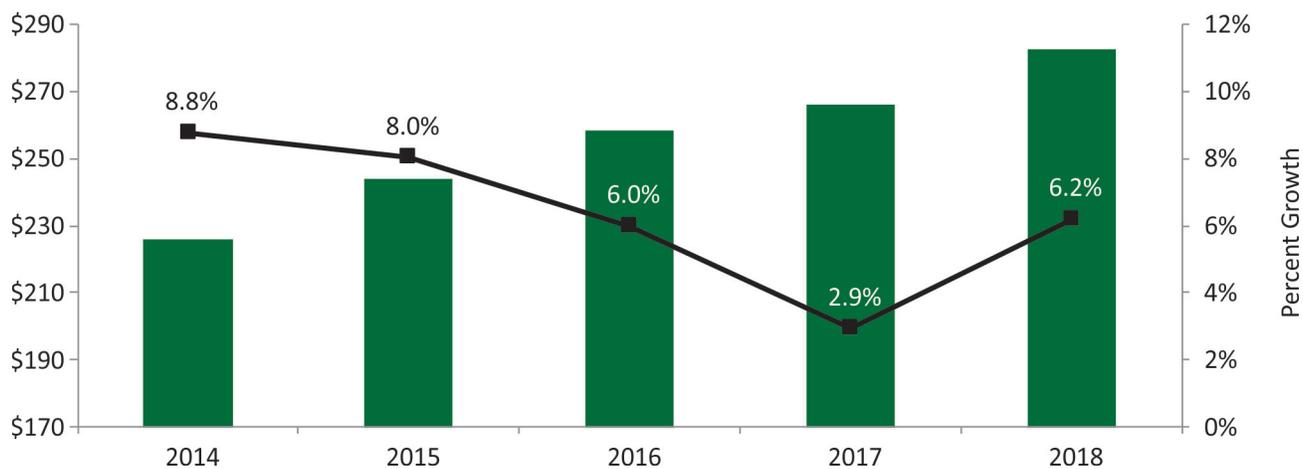
### **Insured Obligations**

FCSIC insures Systemwide and consolidated bonds, notes, and other obligations issued by System banks through the Funding Corporation under section 4.2(c) or (d) of the Farm Credit Act. Figure 1 shows that insured debt outstanding increased by 6.2 percent in 2018 to \$282.5 billion, compared with an increase of 2.9 percent in 2017.

Figure 1

### Insured Debt Outstanding: Growth Averaged 6.4 Percent Over the Past Five Years

(Dollars in Billions)



Note: Insured debt outstanding is based on the call report information provided by System institutions and reflects the book value of insured debt outstanding, plus accrued interest. (Book value excludes fair-value adjustments.)



## 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 to secure the 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, and the banks ultimately repay Systemwide debt securities.

All the banks and associations currently 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, FCSIC would use the Insurance Fund to make the payment on its behalf. If the assets in the Insurance Fund were exhausted, the Farm Credit Act's provisions for joint and several liability would be triggered, requiring the other System banks to repay the defaulting bank's portion of the debt.

As Figure 2 shows, the amount of System bank capital plus the balance in the Insurance Fund increased 23 percent over the past five years, from \$19.6 billion at year-end 2014 to \$24.2 billion at year-end 2018. However, bank capital plus the amount in the Insurance Fund as a percentage of insured debt outstanding decreased from 8.7 percent in 2014 to 8.5 percent in 2018 (see Figure 3). Without the Insurance Fund, bank capital as a percentage of insured debt was 6.9 percent and 6.8 percent at year-ends 2017 and 2018, respectively.

Overall, the financial performance and condition of the System on a consolidated basis remain strong, although some institutions continue to experience stress from credit deterioration in certain agricultural sectors. (See trends in the Financial Institution Rating System (FIRS) in the "Risk Management" section beginning on page 26.)

A bank's credit exposure to borrowing associations is partially mitigated by the associations' capital levels. Increases in System associations' capital levels, the result of higher retention levels of strong association net incomes, further reduces credit risk. As Figure 4 shows, from 2014 to 2018, combined association capital increased \$9.1 billion — an annual average increase of approximately 6.6 percent. Since 2014, the associations have collectively achieved solid earnings and preserved capital, causing association capital as a percentage of total association assets to increase to 19.5 percent in 2018 from 18.8 percent in 2014 (see Figure 5).



Figure 2

**Bank Capital Plus Insurance Fund**

(Dollars in Billions)

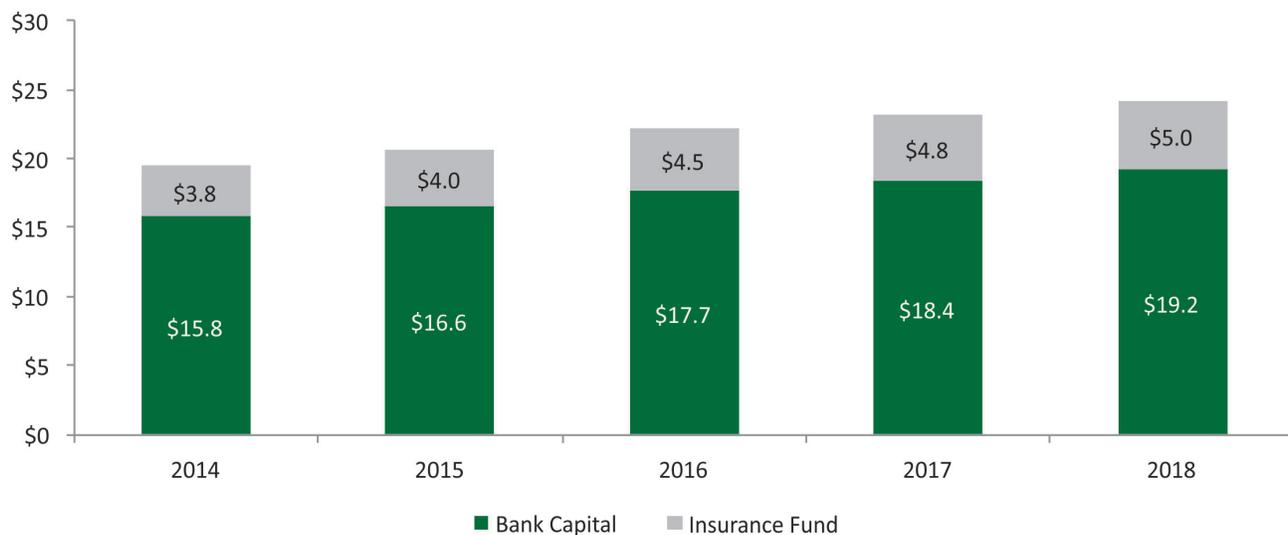


Figure 3

**Bank Capital Plus Insurance Fund as Percentage of Insured Debt**

(Dollars in Billions)

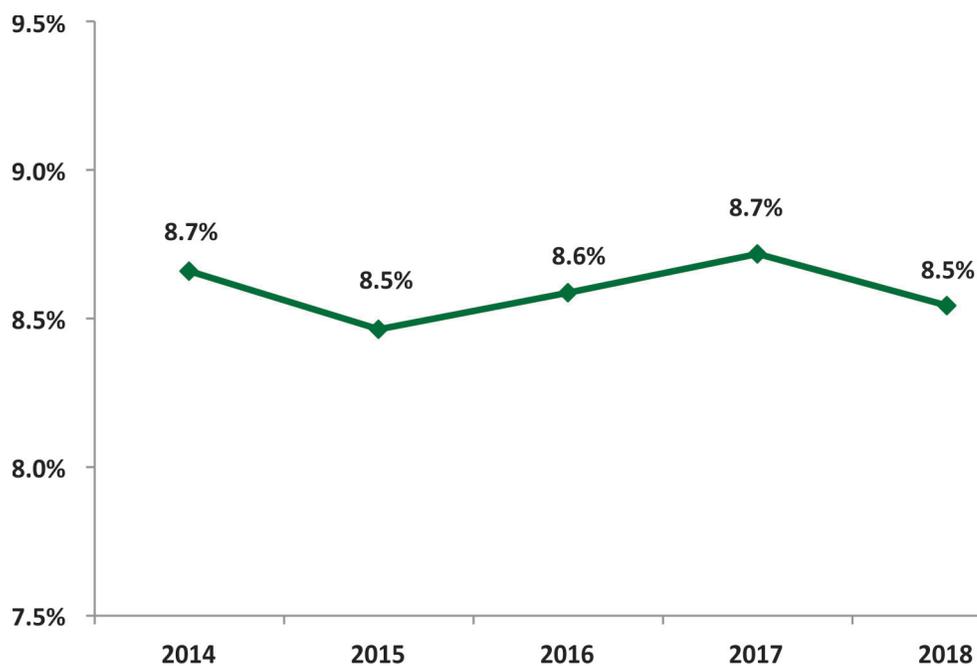


Figure 4

**Combined Association Capital**

(Dollars in Billions)

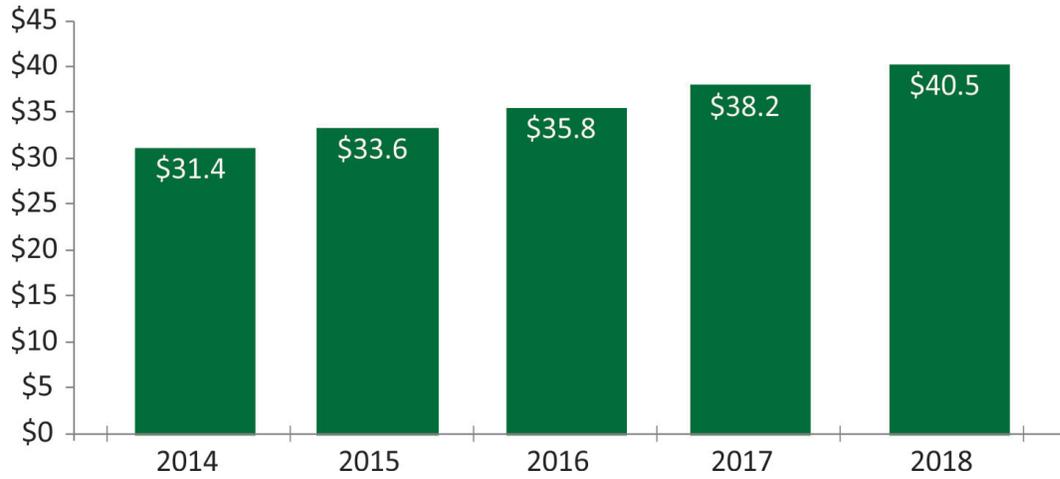
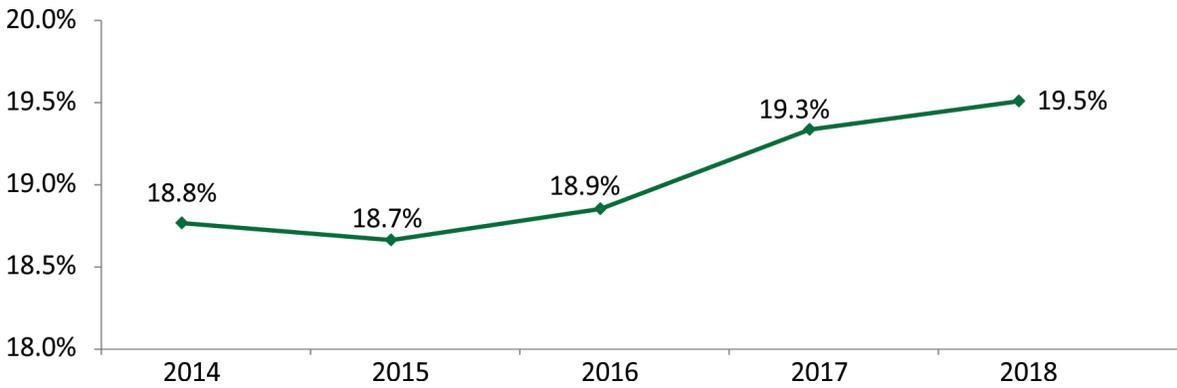


Figure 5

**Combined Association Capital as a Percentage of Total Association Assets**

(Dollars in Billions)



## Risk Management Tools

Farm Credit System banks use risk management tools to protect investors. One 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 contains triggers that financially penalize banks that do not meet performance standards.

The System banks and the Funding Corporation have also entered into the Market Access Agreement. The Market Access Agreement establishes conditions for each bank's continued participation in the debt market. If a bank fails to meet agreed-upon performance measures, it may be restricted from issuing debt. The performance criteria used under the Market Access Agreement are the CIPA scores and the bank's tier 1 leverage and total capital ratios.

The Farm Credit Administration's liquidity regulation requires the banks to effectively manage liquidity risk and maintain a three-tiered liquidity reserve to better withstand a liquidity crisis. Each System bank is authorized to hold eligible investments in an amount not to exceed 35 percent of its total outstanding loans for the purposes of maintaining a liquidity reserve, managing short-term surplus funds, and managing interest rate risk.

The liquidity reserve must always consist of readily marketable instruments that are sufficient to fund at least 90 days of the principal portion of on-balance sheet maturing obligations. The liquidity reserve must consist of level 1 instruments to cover the principal portion of each bank's on-balance sheet maturing obligations for the first 15 days; level 1 and 2 instruments sufficient to cover days 16 to 30; and level 1, 2, and 3 instruments to cover days 31 to 90. Level 1 instruments include cash, overnight money market investments, obligations of U.S. government agencies with a final remaining maturity of 3 years or less, non-System government-sponsored enterprise (GSE) senior debt securities that mature within 60 days and diversified investment funds comprised exclusively of level 1 instruments. Level 2 instruments include obligations of U.S. government agencies with a final remaining maturity of more than 3 years, mortgage-backed securities that are fully guaranteed by a U.S. government agency as to the timely repayment of principal and interest, and diversified investment funds comprised exclusively of level 1 and 2 instruments. Level 3 instruments include non-System GSE senior debt securities with maturities exceeding 60 days, mortgage-backed securities that are fully guaranteed by a GSE as to the timely repayment of principal and interest, money market instruments maturing within 90 days, and diversified investment funds comprised exclusively of level 1, 2, and 3 instruments. All four System banks exceeded these requirements in 2018.



# 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 portion of the Insurance Fund for which no specific use has been designated) and an allocated insurance fund (the portion of the Insurance Fund that has been transferred to the allocated insurance reserves accounts (AIRAs)).

The Farm Credit Act established the secure base amount as 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). Table 3 shows how the secure base amount is calculated. The Act gives FCSIC the discretion to choose another percentage that we determine to be actuarially sound to maintain in the Insurance Fund taking into account the risk of insuring outstanding debt obligations.

FCSIC's premiums are set with the goal of reaching and maintaining the 2 percent secure base amount. However, if growth of insured debt is greater than forecasted when premium rates are established (or the Fund is used for some authorized purpose), the Insurance Fund will end the year below the secure base amount, and FCSIC will need to collect additional premiums in the following year to make up the shortfall. If growth of insured debt is less than forecasted when premium rates are set, then the Insurance Fund may end the year above the secure base amount.

If the Insurance Fund exceeds the secure base amount at the end of any calendar year, FCSIC allocates the excess amounts, minus operating expenses and insurance obligations, to the AIRAs established by Congress for the benefit of the System banks and holders of FAC stock. Once FCSIC determines that the allocation is appropriate and that the AIRA funds are not otherwise needed, FCSIC may pay the amounts in the AIRAs to the account holders in accordance with the formula specified in the Farm Credit Act. FAC stockholders receive 10 percent of any distribution until they have received \$55.8 million under the terms of the Act. In 2010, FCSIC returned a total of \$205.3 million to System institutions, with \$20.5 million paid to FAC stockholders. In 2012, FCSIC returned a total of \$221.9 million, with \$22.2 million paid to FAC stockholders. In 2018, FCSIC returned a total of \$175.8 million, with \$13.1 million paid to FAC stockholders, completing the payoff of outstanding FAC shares.

Table 3

**Calculation of Secure Base Amount**

Results as of December 31, 2018

(Dollars in Millions)

	12/31/2018	5/31/2018	12/31/2017
Total principal and interest of debt outstanding	\$282,543	\$272,366	\$266,008
Less:			
90 percent federal government-guaranteed loans	(5,708)	(5,196)	(5,300)
80 percent state government-guaranteed loans	(20)	(22)	(21)
90 percent federal government-guaranteed investments	(32,641)	(30,382)	(27,303)
80 percent state government-guaranteed investments	-	-	-
Total deduction	(38,369)	(35,600)	(32,624)
Adjusted insured debt	244,174	236,766	233,384
Secure base amount (2.00%)	4,883	4,735	4,668
Unallocated and allocated Insurance Fund balance	4,954	4,787	4,848
Unallocated and allocated Insurance Fund as a percentage of adjusted insured debt	2.03%	2.02%	2.08%

Both total Insurance Fund and total assets increased by 2.2 percent to \$4.95 billion in 2018. Insured debt outstanding grew \$16.5 billion in 2018 (6.2 percent). The Insurance Fund finished 2018 at 2.03 percent, \$70.4 million above the secure base amount (see Figure 6). Consequently, \$66.1 million was transferred to the AIRAs. The Insurance Fund finished 2017 at 2.08 percent, \$180.0 million above the secure base amount (see Figure 6). Consequently, \$175.8 million was transferred to the AIRAs.

Total Insurance Fund growth over the past five years averaged 7.3 percent annually. As a result of our quarterly allowance for loss analysis, we did not accrue a provision for insurance obligations in 2018 (see Figure 7).

Figure 6  
**Insurance Fund Relative to 2 Percent Secure Base Amount**

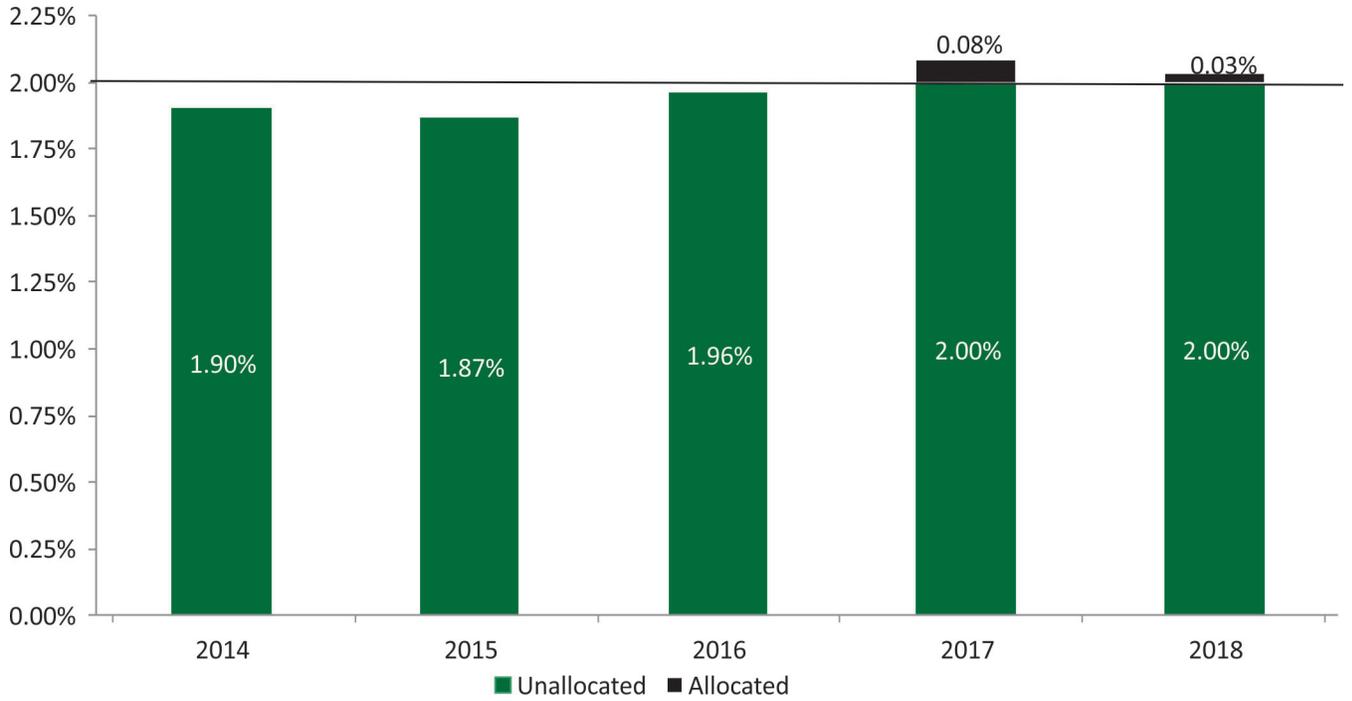
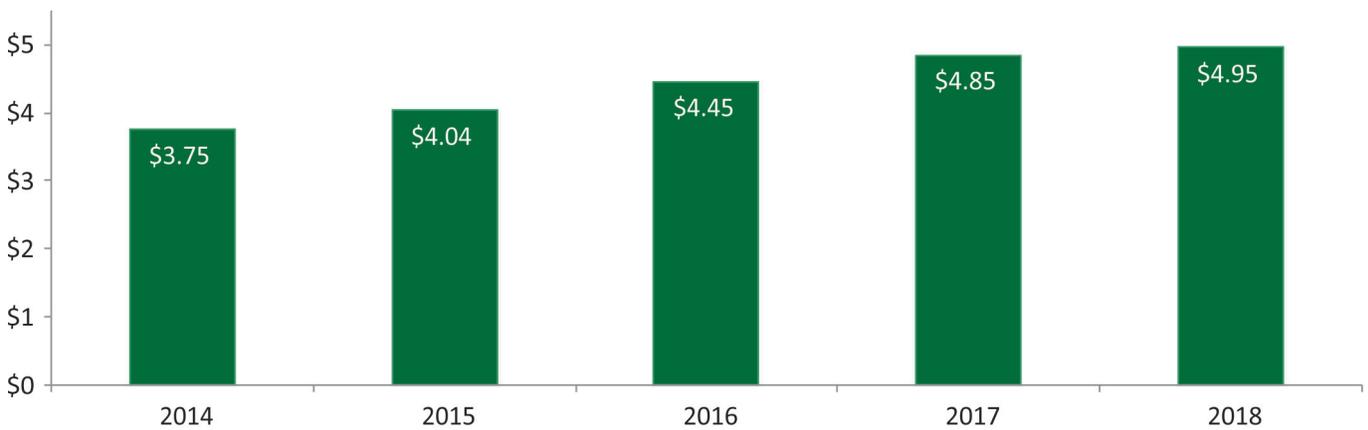


Figure 7  
**Insurance Fund Balances**  
 (Dollars in Billions)



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## Premiums

The FCSIC board reviews premium assessment 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 Farm Credit Act requires premium assessments to be 20 basis points on adjusted insured debt outstanding unless they are reduced by the board of directors. There is a risk surcharge of up to 10 basis points on nonaccrual loans and on other-than-temporarily impaired investments. In addition, the Act reduces the total insured debt on which premiums are assessed. The Act requires that premiums be based on outstanding insured debt obligations adjusted downward by 90 percent of federal government–guaranteed loans and investments and by 80 percent of state government–guaranteed loans and investments.

The FCSIC board set the assessment rate on adjusted insured debt at 9 basis points for 2018. The most important factors in determining premium rates were the Insurance Fund balance and prospects for Systemwide debt growth during the year. The unallocated Insurance Fund began 2018 at 2.00 percent of the secure base amount.

During 2018, insured debt outstanding increased by 6.2 percent. The Insurance Fund finished 2018 above the 2 percent secure base level, at 2.03 percent of adjusted insured obligations or \$70.4 million above the target level.

The board of directors continued the assessment rate on adjusted insured debt of 9 basis points for 2019. The board also continued the risk surcharge of 10 basis points on nonaccrual loans and other-than-temporarily impaired investments.

## Revenues and Expenses

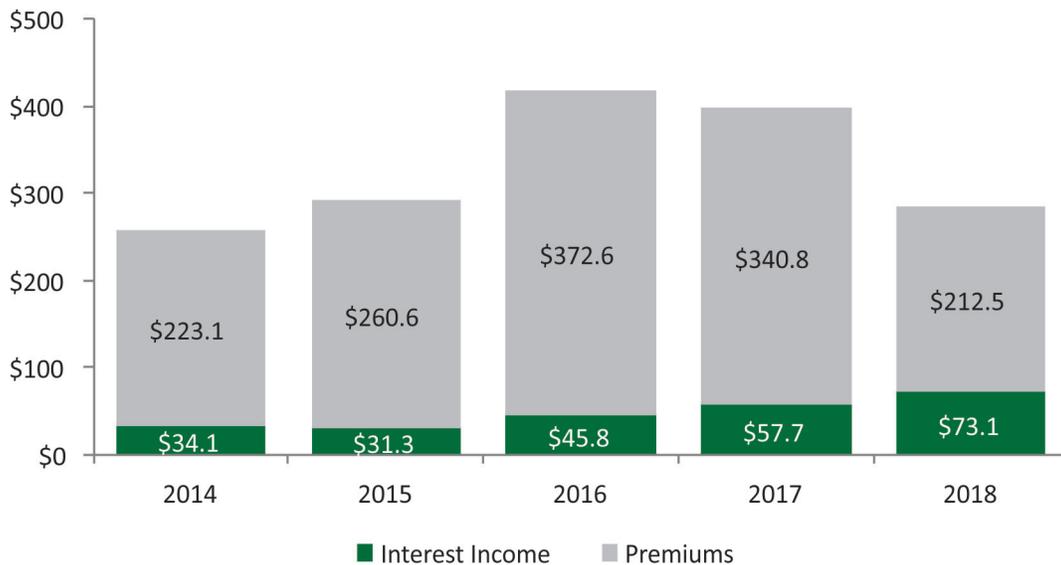
FCSIC operates with no annually appropriated funds. We collect insurance premiums from each Farm Credit System bank. These premiums and the income from our investment portfolio provide the funds necessary to fulfill our mission.

Our revenues decreased by 28 percent to \$285.7 million in 2018 from \$398.5 million in 2017 (see Figure 8). Revenues decreased primarily because of lower insurance premiums in 2018. Interest income increased 27 percent in 2018 to \$73.1 million from \$57.7 million in 2017.

Figure 8

### FCSIC Revenues

(Dollars in Millions)



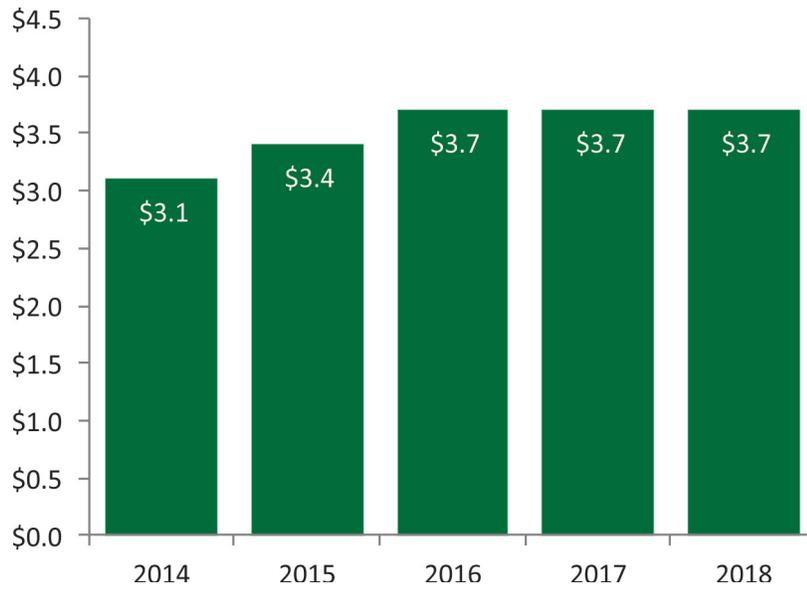
To avoid duplication of effort and to minimize costs, we operate with a small core staff and use private- and public-sector contractors to leverage our efforts. The board of directors and management adopted this model as a cost-effective and efficient way to use available expertise, services, and resources to accomplish our mission.

Our operating costs as a percentage of total assets represented 7 basis points for 2018, down from 8 basis points in 2017. Costs for staff salaries, travel, rent, and miscellaneous expenses were \$2.9 million of the \$3.7 million total for the year (see Figure 9). The remaining expenses of \$0.8 million were for contract services.

Figure 9

### FCSIC Operating Expenses

(Dollars in Millions)



## Investments

FCSIC's investments decreased from \$4.5 billion as of year-end 2017 to \$4.4 billion as of year-end 2018 (see Figure 10). The decrease occurred primarily because an investment of \$200.7 million matured on December 31, 2018, and the funds were placed in the overnight investment account and reclassified as "cash and cash equivalents." In early 2019, the \$200.7 million was invested in accordance with FCSIC board policy.

Our primary investment objective is to ensure adequate liquidity of the Insurance Fund to meet our mission. Our secondary objective is to optimize the rate of return on our investment portfolio. Funds are invested in U.S. Treasury securities in accordance with the Farm Credit Act and our investment policy.

We use benchmarks to enhance our ability to assess portfolio performance. Three weighted-average Treasury yield benchmarks serve as primary benchmarks. Two Treasury index funds serve as secondary benchmarks. These index funds are considered secondary benchmarks because a portion of their returns is generated through trading. The FCSIC Policy Statement Concerning Investments prohibits trading for capital gains purposes.

In 2018, the average FCSIC investment portfolio yield was 1.56 percent, up from 1.31 percent the prior year. The average yield for the primary benchmarks ranged from 1.50 percent to 2.30 percent. The average yield for the secondary benchmarks ranged from 1.85 percent to 1.88 percent for 2018. Most benchmarks exceeded the average fund yield because of the rising rate environment in 2018. Unlike the benchmark portfolios, FCSIC is a hold-to-maturity investor and is precluded from trading for gain.

In accordance with our investment policy, our portfolio is composed of a liquidity pool and an investment pool. The liquidity pool consists of short-term Treasury securities maturing in 2 years or less. The investment pool is composed of Treasury securities with maturities that vary from 2 to 10 years. Our investment policy requires the liquidity pool to be at least 20 percent of the portfolio. The policy also states that securities maturing in 5 to 10 years must not exceed 20 percent of the portfolio.

The weighted-average maturity of the portfolio at year-end was 1.09 years. The composition of the investment portfolio as of December 31, 2018, is shown in Figure 11.

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. TIPS have experienced monthly inflation or deflation adjustments, but the United States has not had an annual deflationary environment since 1954, more than 60 years ago. Because of the volatility of the monthly returns on TIPS and the risk of loss resulting from deflation, the FCSIC Investment Committee limits TIPS to no more than 20 percent of the portfolio. At year-end 2018, our TIPS investments totaled \$85.1 million or 2 percent of the investment portfolio.

Figure 10

**FCSIC Investments**

(Dollars in Billions)

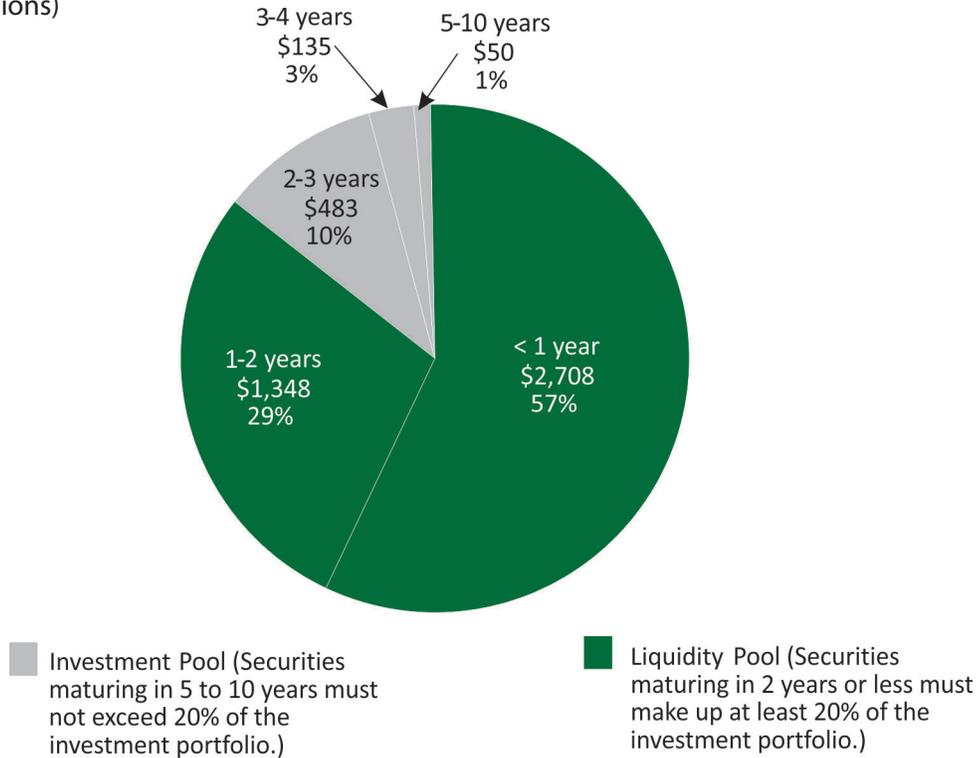


Note: Total investments reflected on this chart do not include overnight investments classified as “cash and cash equivalents” from the balance sheet.

Figure 11

**Investment Portfolio by Maturity as of December 31, 2018**

(Dollars in Millions)



Note: Total investments reflected on this chart include overnight investments classified as “cash and cash equivalents” from the balance sheet.

# Risk Management

## FCSIC's Risk Profile

FCSIC's primary purpose is to insure the timely payment of principal and interest on Systemwide debt securities. The System banks, through the jointly owned Federal Farm Credit Banks Funding Corporation, issue Systemwide debt securities, insured by FCSIC, to fulfill their mission. Anything impairing the System banks' ability to repay their insured debt constitutes an insurance risk. To carry out our mission, FCSIC monitors conditions in the farm, rural, domestic, and global economies that affect the System's ability to repay insured debt obligations.

FCSIC's Insurance Fund is exposed to a variety of risks, some inherent in insuring financial institutions and others specific to the System. Examples of specific events that could increase risk to the Insurance Fund include the following:

- Material reduction in System bank capital
- Material adverse change in the System banks' ability to access debt markets
- Catastrophic operational failure at a System institution related to a control deficiency or cybersecurity breach
- Inadequate governance at a System institution such as a failed business strategy or mismanagement of the organization
- Significant, rapid, or unexpected credit deterioration resulting from adversity in the agricultural sector

Major categories of risk monitored by FCSIC include the following:

**Credit risk** — the risk of default on a debt that may arise from a borrower failing to make required payments. Credit risk includes consideration of loan concentrations and other broad elements of System institution portfolios. FCSIC primarily focuses on credit risk issues affecting the underlying agricultural borrowers' ability to repay their debts to individual System institutions. These risks include the following:

- Changes in farmland values
- Price volatility for agricultural commodities
- Changes in government support programs for agricultural producers
- Changes in supply and demand for U.S. agricultural products
- Changes in international trade and the value of the U.S. dollar
- Changes in production costs
- Changes in the domestic economy that affect incomes from off-farm jobs
- Weather conditions
- Environmental and regulatory costs
- Availability of agricultural workers

**Liquidity risk** — the risk that an institution may be unable to meet short-term financial demands without unacceptable losses. The System relies on its ability to regularly issue new debt obligations, in part to pay maturing obligations. The System banks also hold liquidity investments that are available if needed. A significant disruption in the System banks' ability to issue new debt obligations or sell liquidity investments would impair their ability to repay insured obligations. As further discussed on page 32, FCSIC has procedures in place to provide liquidity assistance to System banks if external market circumstances make it likely that the banks will be unable to repay maturing insured obligations.

**Interest rate risk** — the risk that changes in interest rates may reduce the value of assets with a consequent negative impact on operating results and financial condition.

**Operational risk** — the prospect of losses resulting from inadequate or failed procedures, controls, systems, or policies, including employee errors, systems failures, or fraud or other unauthorized activity. Operational risk also includes inadequate defenses against cyberthreats.

**Strategic risk** — the risk that a failed business strategy, decision, or series of decisions leads to losses.

**Structural risk** — the risk related to the design of the Farm Credit System. For example, as a lender to a single industry (agriculture), the System has a built-in concentration risk. Additionally, any changes to the System's fundamental organization, such as an alteration in the supervisory relationship between System banks and associations, may create risk to the Insurance Fund.

**Reputational risk** — the risk resulting from events that affect the reputation of the System or the agriculture industry. Such events may affect the System's funding costs depending on market reaction.

**Political risk** — the risk of loss of support from federal and state governments. This includes any change in government support for government-sponsored enterprises.

## The Risk Environment

The U.S. economy continued to expand at a moderate pace in 2018. The Bureau of Economic Analysis (U.S. Department of Commerce) reported that real gross domestic product (GDP) grew 2.9 percent in 2018, compared with real GDP growth of 2.2 percent in 2017. The labor market continued to show resilience nine years into the economic expansion as unemployment declined from 10 percent at its peak in October 2009 to 3.9 percent at year-end 2018. Inflation rose throughout most of 2018 before tapering off at the end of the year. The 12-month increase in the seasonally adjusted consumer price index was 1.95 percent as of December 2018.

Consumers benefited from a strong job market, lower tax base, and modest inflation in 2018. Consumer spending increased 2.6 percent, contributing about 1.80 percent to real GDP growth. Tax law changes and a resurgence in the energy sector boosted capital investment in 2018. Business investment increased 5.9 percent, contributing about 1.02 percent to real GDP growth. Government expenditures increased slightly, contributing 0.26 percent to real GDP growth. Net exports continued to be a drag on the economy, with a negative contribution of 0.21 percent to real GDP growth in 2018.

The Federal Open Market Committee (FOMC) of the Federal Reserve Board raised the target range for the federal funds rate four times in 2018, to between 2.25 percent and 2.50 percent as of December 2018. The FOMC signaled a pause on further interest rate increases in early 2019 in view of slower global economic growth, trade uncertainties, and subdued inflation. The FOMC has also announced that it will end its operation to unwind its balance sheet in 2019.

Agriculture continued to experience stress in 2018. The expanding U.S. economy has helped farm household income but falling commodity prices in recent years have weighed on farm income. However, the U.S. Department of Agriculture (USDA) estimates in its February 2019 Farm Sector Income Forecast that net farm income will increase \$6.3 billion (10.0 percent) from 2018 to \$69.4 billion in 2019. Net cash farm income is forecasted to increase \$4.3 billion (4.7 percent) to \$95.7 billion. The expected increase is primarily due to the increase in total farm cash receipts exceeding the increase in total production expenses. The value of U.S. agricultural exports, according to USDA's May 2019 reports, is expected to be \$137.0 billion in 2019, down \$4.5 billion from 2018, largely due to reductions in grains, oilseeds, and livestock and products. The ongoing U.S.–China trade dispute is expected to shift trade patterns and diminish U.S. export prospects in 2019.

Farmland values remained stable in 2018 despite the rising interest rate environment. The USDA projects farm sector assets will rise 1.5 percent to \$3.1 trillion in 2019 with most of that increase coming from a forecasted 1.8 percent increase in farm sector real estate, which comprises about 83.3 percent of farm sector assets. Farm sector debt is expected to grow by 3.9 percent to \$426.7 billion during 2019. As a result, farm sector equity (assets minus debt) is expected to rise 1.1 percent in 2019 to \$2.7 trillion. The farm sector debt-to-asset ratio is expected to rise from 13.5 percent in 2018 to 13.9 percent in 2019 as some farmers continue to use their real estate equity to provide funds for operating activities.

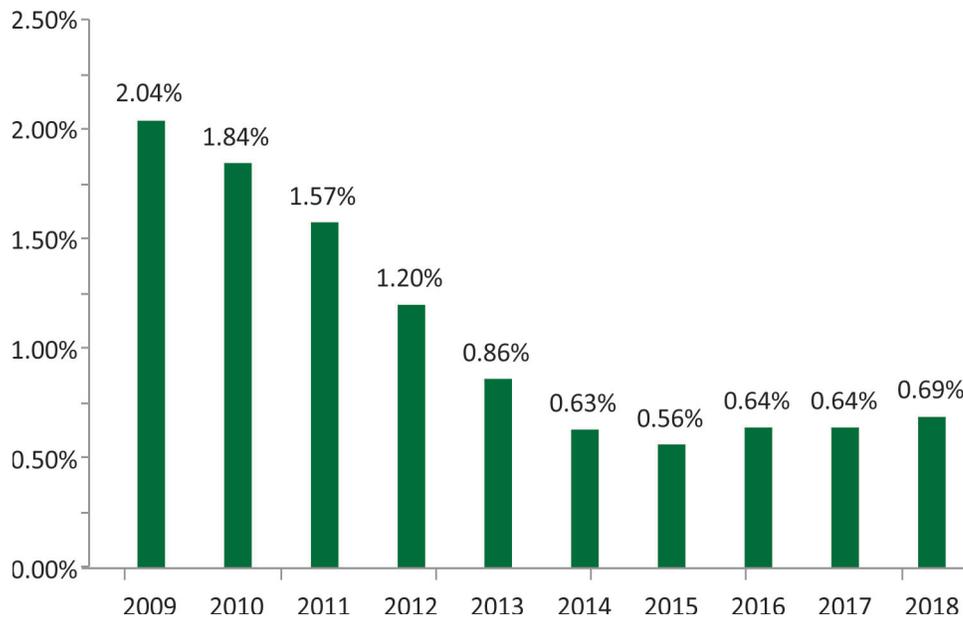
The System reported net income of \$5.3 billion for 2018, up 2.8 percent from \$5.2 billion in 2017. Net interest margin was 2.46 percent for 2018 compared with 2.48 percent for 2017. The net interest rate spread was 2.12 percent for 2018 compared with 2.25 percent in 2017. The decrease in net interest rate spread was largely attributable to an increase in debt costs and lower lending spreads due to competitive pressures.

The System's loan volume increased \$13.2 billion or 5.1 percent to \$271.9 billion at year-end 2018 compared with \$258.8 billion at the end of 2017. The growth was primarily due to increased real estate mortgages and agribusiness, production, and intermediate-term loans.

System credit quality declined slightly in 2018. Nonaccrual loans increased \$223 million, or 13.4 percent, to \$1.9 billion at December 31, 2018. The increase was primarily due to credit quality deterioration affecting a limited number of loans in the agribusiness and rural power sectors. The ratio of nonaccrual loans to total loans outstanding was 0.69 percent at December 31, 2018, up from 0.64 percent at December 31, 2017 (see Figure 12).

Figure 12

### Nonaccrual Loans as a Percentage of Total Loans Outstanding



The allowance for loan losses was \$1.7 billion at December 31, 2018, an increase of \$117 million, or 7.3 percent, above the \$1.6 billion at December 31, 2017. The allowance for loan losses represents the aggregate of each System entity's individual evaluation of its allowance for loan losses requirements. Managements' evaluations consider factors that include, among other things, loan loss experience, portfolio quality, and loan portfolio composition, collateral value, current agricultural production, and economic conditions. Although aggregated for the System's combined financial statements, the allowance of each entity is specific to that institution and is not available to absorb losses at other System entities.

The System continued to have reliable access to the debt markets to support its mission. Investor demand for Systemwide insured debt securities remained favorable across all products. The System is a government-sponsored enterprise that continues to benefit from broad access to domestic and global capital markets providing a dependable source of competitively priced debt.

FCA adopted a capital rule for banks and associations, effective January 1, 2017, which is comparable to the Basel III standardized approach adopted by the federal banking regulatory agencies. FCA's regulatory minimums include a 4.5 percent common equity tier 1 risk-based capital ratio, a 6.0 percent tier 1 risk-based capital ratio, an 8.0 percent total risk-based capital ratio, and a 4.0 percent tier 1 leverage ratio, of which at least 1.5 percent must be composed of unallocated retained earnings (URE) and URE equivalents. The risk-based capital ratios also include a 2.5 percent common equity tier 1 capital conservation buffer. The tier 1 leverage ratio includes a 1.0 percent leverage buffer. As of December 31, 2018, all System institutions exceeded the regulatory minimum and buffer requirements.

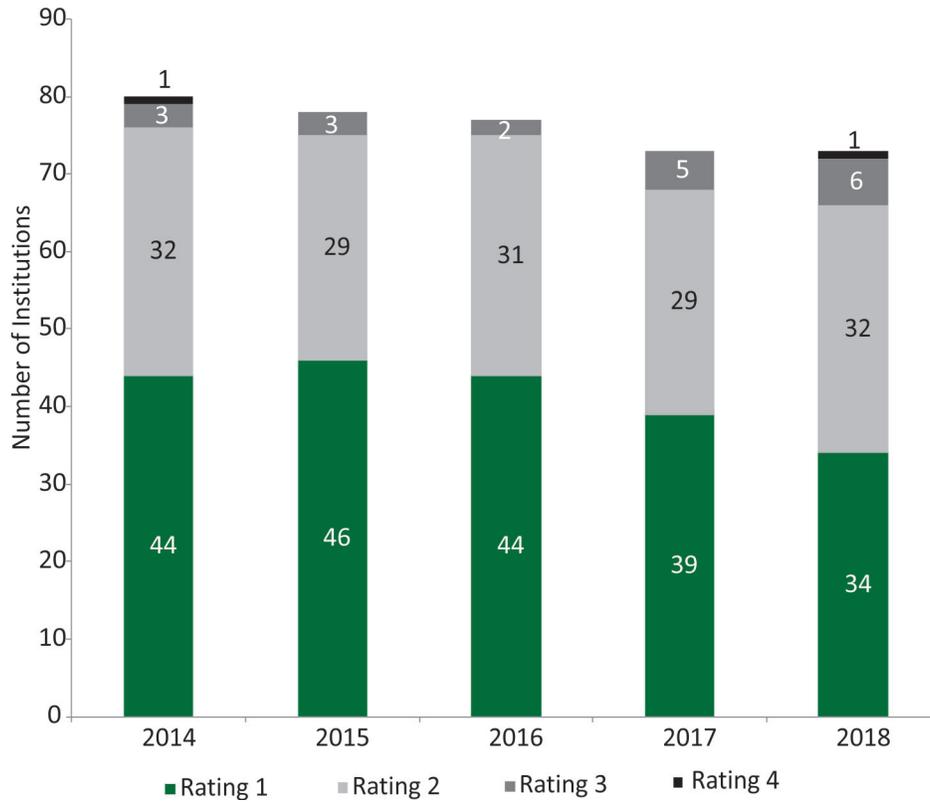
FCA authorizes each System bank to hold eligible investments in an amount not to exceed 35 percent of its total outstanding loans for the purposes of maintaining a liquidity reserve, managing short-term funds, and managing interest rate risk. The liquidity reserve must consist of marketable investments that are sufficient to fund 90 days of on-balance-sheet maturing obligations. The System reported a combined \$64.8 billion in cash and available-for-sale investments with a liquidity position of 182 days at year-end 2018 compared with 175 days at year-end 2017.

The System banks are further required to maintain a three-tiered liquidity reserve, consisting of level 1 instruments to cover each bank's maturing obligations for the first 15 days, level 1 and 2 instruments sufficient to cover days 16 to 30, and level 1, 2, and 3 instruments to cover days 31 to 90. All four System banks exceeded these requirements in 2018.

The System banks have established contingency funding plans to provide for events that could impede access to the debt markets. The System banks also regularly perform credit and liquidity stress testing to determine their ability to withstand severe market events while continuing to fulfill their mission. Figure 13 shows a summary of composite year-end FIRS ratings for System banks and associations. Institutions with performance-related issues continued to receive greater examination scrutiny and supervisory attention from FCA.



Figure 13

**FIRS Composite Year-End Ratings for Banks and Associations of the Farm Credit System**

Source: FCA

## Financial Assistance and Resolutions

FCSIC has statutory authority to provide “stand-alone assistance” to a System bank or association to (1) prevent the placing of the institution in receivership, (2) restore the institution to “normal operation,” or (3) reduce the risk to FCSIC posed by the institution when “severe financial conditions” threaten the stability of the banks. FCSIC may also provide assistance to facilitate mergers or consolidations.

At present, no assistance agreements are outstanding. If a System institution needs financial assistance, FCSIC must ensure that the proposed assistance is the least costly means for resolving the institution’s problems; by law, FCSIC cannot provide financial assistance if the cost of liquidation is lower than the cost of providing assistance.

FCSIC has procedures in place in the event System banks require liquidity assistance because severe financial conditions threaten the banks’ ability to repay maturing insured debt. The procedures implement FCSIC’s Policy Statement Concerning Assistance. Along with the procedures, we developed a model assistance agreement, drafted necessary forms related to valuation of collateral and liquidity reserves, and entered into a collateral pledge agreement with each bank and a collateral custodian. We review the procedures annually to determine whether changes are needed.

When appointed by FCA, FCSIC has the statutory responsibility to serve as receiver or conservator for System banks and associations. As conservator, we will operate the institution as a going concern. Upon appointment as receiver, we will take possession of a System institution to settle its business operations, collect the debts owed to it, liquidate its property and assets, pay its creditors, and distribute any remaining proceeds to stockholders. The Agriculture Improvement Act of 2018 (2018 Farm Bill) clarified and updated FCSIC’s statutory authorities to act as receiver or conservator for a System institution. Congress stated its intent in the 2018 Farm Bill Conference Report that FCSIC’s authorities be “functionally equivalent to the parallel authorities of the Federal Deposit Insurance Corporation.” The 2018 Farm Bill also provided new authority for FCSIC to create, and FCA to charter, a System bridge bank, which is an important tool for resolving a failed bank. There are no active receiverships or conservatorships in the System.

We use contractors on an as-needed basis so that we can continue to operate with a small core staff while also maintaining our readiness to act as receiver or conservator. These contractors provide knowledgeable and readily available staff resources while allowing us to contain costs during periods of limited or no activity.

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

We have several board-approved policy statements that provide guidance related to resolution activities, including appraisal of real estate securing nonperforming assets, insurance of assets that come under our control, and environmental hazards assessments of real estate securing nonperforming assets. The FCSIC board must review and approve policy statements every five years.



# Farm Credit System Insurance Corporation

Audited Financial Statements  
For the Years Ended December 31, 2018 and 2017

The report accompanying these financial statements was issued by BDO USA, LLP, a Delaware limited liability partnership and the U.S. member of BDO International Limited, a UK company limited by guarantee.



# Farm Credit System Insurance Corporation

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Suite 800  
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## Independent Auditor's Report

Board of Directors  
Farm Credit System Insurance Corporation  
McLean, Virginia

### Report on the Financial Statements and Internal Control

We have audited the accompanying financial statements of the Farm Credit System Insurance Corporation (FCSIC), which comprise the statement of financial condition as of December 31, 2018, 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. We also have audited FCSIC's internal control over financial reporting as of December 31, 2018, based on the criteria established in *Internal Control-Integrated Framework (2013)* issued by the Committee of Sponsoring Organizations of the Treadway Commission.

#### ***Management's Responsibility for the Financial Statements and Internal Control over Financial Reporting***

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 effective internal control over financial reporting relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error. Management is also responsible for its assessment about the effectiveness of internal control over financial reporting, which is included in the accompanying *Management's Report on Internal Control Over Financial Reporting*.

#### ***Auditor's Responsibility***

Our responsibility is to express an opinion on these financial statements and an opinion on the entity's internal control over financial reporting based on our audit. We conducted our audit in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States; and Office of Management and Budget (OMB) Bulletin No. 19-01, *Audit Requirements for Federal Financial Statements*. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement and whether effective internal control over financial reporting was maintained in all material respects.

An audit of financial statements involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's 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. An audit of financial statements also includes evaluating the appropriateness of

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accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

An audit of internal control over financial reporting involves performing procedures to obtain evidence about whether a material weakness exists. The procedures selected depend on the auditor's judgment, including the assessment of the risk that a material weakness exists. An audit of internal control over financial reporting also involves obtaining an understanding of internal control over financial reporting and testing and evaluating the design and operating effectiveness of internal control over financial reporting based on the assessed risk.

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

#### ***Definition and Inherent Limitations of Internal Control over Financial Reporting***

An entity's internal control over financial reporting is a process effected by those charged with governance, management, and other personnel, designed to provide reasonable assurance regarding the preparation of reliable financial statements in accordance with generally accepted accounting principles in the United States of America. An entity's internal control over financial reporting includes those policies and procedures that (1) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the entity; (2) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles in the United States of America, and that receipts and expenditures of the entity are being made only in accordance with authorizations of management and those charged with governance; and (3) provide reasonable assurance regarding prevention, or timely detection and correction of unauthorized acquisition, use, or disposition of the entity's assets that could have a material effect on the financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent, or detect and correct, misstatements. Also, projections of any assessment of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

#### ***Opinion***

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial condition of the Farm Credit System Insurance Corporation as of December 31, 2018, and the results of its operations and its cash flows for the year then ended in accordance with accounting principles generally accepted in the United States of America. Also, in our opinion, the Farm Credit System Insurance Corporation maintained, in all material respects, effective internal control over financial reporting as of December 31, 2018 based on the criteria established in *Internal Control-Integrated Framework (2013)* promulgated by the Committee of Sponsoring Organizations of the Treadway Commission.



### ***Compliance and Other Matters***

As part of obtaining reasonable assurance about whether the Farm Credit System Insurance Corporation's financial statements are free from material misstatement, we also 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 U.S. *Government Auditing Standards* and OMB Bulletin No. 19-01.

### **Other Matter**

The 2017 financial statements of FCSIC were audited by other auditors, whose report dated February 9, 2018, expressed an unmodified opinion on those financial statements.

BDO USA, LLP

McLean, Virginia  
February 11, 2019

# Farm Credit System Insurance Corporation

## Statements of Financial Condition

(Dollars in thousands)

<i>December 31,</i>	<b>2018</b>	<b>2017</b>
<b>Assets</b>		
Cash and cash equivalents	\$ 287,767	\$ 1,613
Investments in U.S. Treasury obligations	4,436,617	4,454,235
Premiums receivable	212,524	340,565
Accrued interest receivable	17,259	21,894
Other receivables	-	30,012
General property, plant, equipment, and software, net	60	78
<b>Total assets</b>	<b>\$ 4,954,227</b>	<b>\$ 4,848,397</b>
<b>Liabilities and Insurance Fund</b>		
Accounts payable and accrued expenses	\$ 367	\$ 679
<b>Total liabilities</b>	<b>367</b>	<b>679</b>
<b>Insurance Fund</b>		
Allocated Insurance Reserves Accounts (AIRAs)	66,061	175,832
Unallocated Insurance Fund	4,887,799	4,671,886
<b>Total Insurance Fund</b>	<b>4,953,860</b>	<b>4,847,718</b>
<b>Total liabilities and Insurance Fund</b>	<b>\$ 4,954,227</b>	<b>\$ 4,848,397</b>

*See accompanying notes to the financial statements.*

# Farm Credit System Insurance Corporation

## Statements of Income and Expenses and Changes in Insurance Fund

(Dollars in thousands)

<i>Year ended December 31,</i>	<b>2018</b>	<b>2017</b>
<b>Income</b>		
Premiums	\$ 212,524	\$ 340,762
Interest income	73,141	57,720
<b>Total income</b>	<b>285,665</b>	<b>398,482</b>
<b>Expenses</b>		
Administrative operating expenses	3,691	3,668
<b>Total expenses</b>	<b>3,691</b>	<b>3,668</b>
<b>Net income</b>	<b>281,974</b>	<b>394,814</b>
<b>Insurance Fund - Beginning of year</b>	<b>4,847,718</b>	<b>4,452,904</b>
Payments to AIRAs accountholders	(175,832)	-
<b>Insurance Fund - End of year</b>	<b>\$ 4,953,860</b>	<b>\$ 4,847,718</b>

*See accompanying notes to the financial statements.*

# Farm Credit System Insurance Corporation

## Statements of Cash Flows

*(Dollars in thousands)*

<i>Year ended December 31,</i>	<b>2018</b>	<b>2017</b>
<b>Cash flows from operating activities</b>		
Net income	\$ 281,974	\$ 394,814
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation	18	13
Net amortization and accretion of investments	3,627	11,849
Decrease in premiums receivable	128,041	32,156
Decrease (increase) in accrued interest receivable	4,635	(4,560)
Decrease in other receivables	30,012	16,344
(Decrease) increase in accounts payable and accrued expenses	(312)	118
<b>Net cash provided by operating activities</b>	<b>447,995</b>	<b>450,734</b>
<b>Cash flows from investing activities</b>		
Payments for purchase of U.S. Treasury obligations	(1,436,080)	(1,246,440)
Proceeds from maturity of U.S. Treasury obligations	1,450,071	797,169
Payment for purchase of depreciable assets	-	(91)
<b>Net cash provided by (used in) investing activities</b>	<b>13,991</b>	<b>(449,362)</b>
<b>Cash flows from financing activity</b>		
Payment to AIRAs Accountholders	(175,832)	-
<b>Net cash used in financing activity</b>	<b>(175,832)</b>	<b>-</b>
Net change in cash and cash equivalents	286,154	1,372
Cash and cash equivalents, beginning of year	1,613	241
<b>Cash and cash equivalents, end of year</b>	<b>\$ 287,767</b>	<b>\$ 1,613</b>

*See accompanying notes to the financial statements.*

# Farm Credit System Insurance Corporation

## Notes to the Financial Statements

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### Note 1: Organization and Summary of Significant Accounting Policies

#### *Farm Credit Insurance Fund (Insurance Fund): Statutory Framework*

The Agricultural Credit Act of 1987 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 (the Farm Credit Act). Each bank in the Farm Credit System (System) participating in insured obligations is an insured System bank. At December 31, 2018, there were four insured System banks and 69 direct lender associations, unchanged from December 31, 2017.

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 amounts in the Insurance Fund necessary to:

1. Ensure the timely payment of interest and principal on insured obligations; 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 System banks and direct lender associations. The Corporation may also act as receiver or conservator of a System bank or association.

As of December 31, 2018, there were \$283 billion of insured obligations compared to \$266 billion as of December 31, 2017, and less than \$1 million of eligible borrower stock outstanding as of December 31, 2018 and 2017.

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. The insurance provided by the Insurance Fund is not an obligation of and is not guaranteed by the U.S. government.

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: Basis of Accounting

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.

# Farm Credit System Insurance Corporation

## Notes to the Financial Statements

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### ***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, 2018, the Corporation held \$287.6 million in overnight Treasury certificates maturing on January 2, 2019, with an interest rate of 2.39 percent, and \$200 thousand in cash. At December 31, 2017, the Corporation held \$1,413 thousand in overnight Treasury certificates maturing on January 2, 2018, with an interest rate of 1.18 percent, and \$200 thousand 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 Financial Accounting Standards Board Accounting Standards Codification 320, *Investments - Debt and Equity Securities* 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.

### ***Other Receivables***

The Corporation reports receivables for securities when investments mature at the end of an accounting period and proceeds are received in the following month.

### ***Premium Receivable - Concentration of Credit Risk***

The Farm Credit Act requires that the System banks pay premiums to FCSIC. The premium receivable balances consists of amounts due from the four System banks and as such are exposed to risks due to concentration. Historically, FCSIC has not experienced any losses related to premium receivable balances. FCSIC performs a quarterly analysis related to estimating an allowance for premium receivable which continues to indicate that no allowance is warranted.

### ***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 require a liability for estimated insurance obligations to be recorded.

# Farm Credit System Insurance Corporation

## Notes to the Financial Statements

The Corporation actively monitors the creditworthiness and financial condition 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 at December 31, 2018.

### *Premiums*

Annual premiums are recorded as revenue during the 12-month period on which the premiums are based starting in January each year. All premiums are due on or before January 31st of the year subsequent to the year in which they are earned.

### *Use of Estimates*

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.

### **Note 3: Investments in U.S. Treasury Obligations**

In addition to the amounts referenced in Note 2, Cash and Cash Equivalents, at December 31, 2018 and 2017, investments in U.S. Treasury obligations, which are carried at amortized cost, consisted of the following:

<i>(Dollars in thousands)</i>	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Fair Value
<b>December 31, 2018</b>				
U.S. Treasury obligations	\$ 4,436,617	\$ 311	\$ (40,782)	\$ 4,396,146
<b>December 31, 2017</b>				
U.S. Treasury obligations	\$ 4,454,235	\$ 304	\$ (35,858)	\$ 4,418,681

The amortized cost and estimated fair value of U.S. Treasury obligations at December 31, 2018, by contractual maturity, are shown below:

<i>(Dollars in thousands)</i>	Amortized Cost	Estimated Fair Value
Due in one year or less	\$ 2,520,392	\$ 2,510,255
Due after one year through five years	1,866,752	1,837,080
Due after five years through ten years	49,473	48,811
	<b>\$ 4,436,617</b>	<b>\$ 4,396,146</b>

# Farm Credit System Insurance Corporation

## Notes to the Financial Statements

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The Corporation follows GAAP for measuring, reporting, and disclosing fair value. These standards apply to all assets and liabilities that are measured, reported, and/or disclosed on a fair value basis. The fair value of FCSIC's investments in U.S. Treasury obligations are estimated based on quoted market prices for those instruments.

### **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 Farm Credit Act requires FCSIC to assess premiums based on each bank's pro rata share of insured debt (rather than on individual loans). FCSIC may collect from 0 to 20 basis points annually on adjusted insured debt outstanding. The Farm Credit Act also authorizes a risk surcharge of up to 10 basis points on non-accrual loans and on other-than-temporarily impaired investments. The Farm Credit Act reduces 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 deducts similar percentages of such guaranteed loans and investments when calculating the secure base amount (SBA).

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 to maintain in the Insurance Fund taking into account the risk of insuring outstanding insured obligations. 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 2018, the board of directors set premium rates at its January 18, 2018 meeting at 9 basis points on average adjusted insured debt and continued the assessment of the 10 basis point surcharge 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, 2018 meeting. The board of directors voted to maintain the premium accrual rate on average adjusted insured debt at 9 basis points and continued the assessment of the 10 basis point surcharge on the average principal balance outstanding for nonaccrual loans and other-than-temporarily impaired investments for the remainder of 2018. In 2018, outstanding insured obligations increased by \$16.5 billion (6.2 percent). At December 31, 2018, the unallocated Insurance Fund and the total Insurance Fund were 2.00 percent and 2.03 percent of adjusted insured obligations, respectively.

For 2017, the board of directors set premium rates at its January 26, 2017 meeting at 15 basis points on average adjusted insured debt and continued the assessment of the 10 basis point surcharge 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 8, 2017 meeting. The board of directors voted to maintain the premium accrual rate on average adjusted insured debt at 15 basis points and continued the assessment of the 10 basis point surcharge on the average principal

# Farm Credit System Insurance Corporation

## Notes to the Financial Statements

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balance outstanding for nonaccrual loans and other-than-temporarily impaired investments for the remainder of 2017. In 2017, outstanding insured obligations increased by \$7.6 billion (3 percent). At December 31, 2017, the unallocated Insurance Fund and the total Insurance Fund were 2.00 percent and 2.08 percent of adjusted insured obligations, respectively.

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 Financial Assistance Corporation (FAC). If, at the end of any calendar year, the aggregate of the amounts in the Insurance Fund exceed the SBA, the Corporation is to allocate to the AIRAs any excess balances 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.

As the total Insurance Fund exceeded the 2 percent SBA at December 31, 2018, and December 31, 2017, there was an allocation of \$66.1 and \$175.8 million, respectively, to the Farm Credit System banks AIRAs.

At December 31, 2017, \$175.8 million of AIRAs was allocated as follows:

FAC Shareholders	\$ 13.1 million
Farm Credit System banks	\$ 162.7 million

With the \$13.1 million payment from the 2017 AIRAs, FCSIC completed its statutory obligation to pay all outstanding FAC shares and the FAC stockholders' AIRA accounts have been closed. At December 31, 2018 no such allocations of AIRAs were necessary.

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

# Farm Credit System Insurance Corporation

## Notes to the Financial Statements

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### Note 5: Operating Lease

The Corporation is committed under a ten-year lease with the FCS Building Association for office space expiring on November 30, 2025. The Corporation recorded lease expense (including operating cost assessments) of \$144 thousand for 2018 and 2017. The following is a schedule by year of the future minimum lease payments required under this lease as of December 31, 2018:

*Years ending December 31,  
(Dollars in thousands)*

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2019	\$	146
2020		149
2021		151
2022		155
2023		158
Thereafter		311
	\$	1,070

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### Note 6: Line of Credit

On September 24, 2013, the Corporation entered into an agreement with the Federal Financing Bank (the FFB), a United States government corporation subject to the supervision and direction of the U.S. Treasury. Pursuant to this agreement, the FFB may advance funds to the Corporation when exigent market circumstances make it extremely doubtful that insured System banks will be able to pay maturing debt obligations. The Corporation will in turn use the funds advanced by the FFB to provide assistance to the System banks until market conditions improve. The agreement provides for a short-term revolving credit facility of up to \$10 billion, is renewable annually and terminates on September 30, 2019, unless otherwise further extended.

Under the agreement, each provision of funds by the FFB is subject to certain terms and conditions. The interest rate for each advance will be established by the FFB at the time the respective advance is made. Each advance cannot have a maturity date longer than twelve months and the maturity date cannot be later than the final termination date of the agreement.

The Corporation paid no commitment fee to secure this line of credit. There were no amounts drawn on this line of credit during 2018 and 2017.

### Note 7: 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 to the CSRS plan during 2018 and 2017 was 7 percent of base pay. For those employees covered by FERS, the Corporation's contribution was 13.7 percent of base pay for 2018 and 2017. 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. In 2015, the Corporation began a 401K plan for both CSRS and FERS employees. The Corporation automatically contributes 1

# Farm Credit System Insurance Corporation

## Notes to the Financial Statements

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percent of base pay to the employee's 401K account and matches the first 2 percent contributed by the employee. Retirement plan expenses amounted to \$393 thousand in 2018 and \$385 thousand in 2017.

### **Note 8: 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 purchased services for 2018 which totaled \$339 thousand, compared with \$322 thousand for 2017.

The Corporation may also provide services to the FCA under an Interagency Agreement; however, the Corporation provided no services and recognized no revenue for 2018 and 2017. At December 31, 2018, and 2017, the Corporation did not have any receivables from the FCA.

### **Note 9: Subsequent Events**

FCSIC evaluated subsequent events from the date of the statement of financial condition through February 11, 2019, the date at which FCSIC's financial statements were issued. No material subsequent events were identified for either recognition or disclosure.



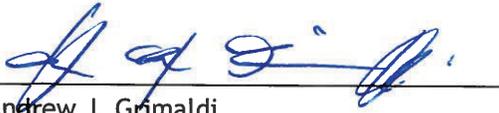
## Management's Report on Internal Control Over Financial Reporting

The Farm Credit System Insurance Corporation's (FCSIC) internal control over financial reporting is a process effected by those charged with governance, management, and other personnel, designed to provide reasonable assurance regarding the preparation of reliable financial statements in accordance with generally accepted accounting principles in the United States of America. Our internal control over financial reporting includes those policies and procedures that (1) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect our transactions and dispositions of our assets; (2) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles and that receipts and expenditures of FCSIC are being made only in accordance with authorizations of FCSIC management and those charged with governance; and (3) provide reasonable assurance regarding prevention, or timely detection and correction, of unauthorized acquisition, use, or disposition of FCSIC's assets that could have a material effect on our financial statements.

Management of FCSIC is responsible for designing, implementing, and maintaining effective internal control over financial reporting. Management assessed the effectiveness of FCSIC's internal control over financial reporting as of December 31, 2018 using the criteria established in the *Internal Control - Integrated Framework (2013)*, issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO). Based on that assessment, management concluded that as of December 31, 2018, FCSIC's internal control over financial reporting is effective, based on the COSO criteria.

Internal control over financial reporting has inherent limitations. Internal control over financial reporting is a process that involves human diligence and compliance and is subject to lapses in judgement and breakdowns resulting from human failures. Internal control over financial reporting also can be circumvented by collusion or improper management override. Because of its inherent limitations, internal control over financial reporting may not prevent, or detect and correct, misstatements. Also, projections of any assessment of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

  
C. Richard Pfitzinger  
Chief Operating Officer

  
Andrew J. Grimaldi  
Chief Financial Officer

  
Howard I. Rubin  
Chief Risk Officer/General Counsel

February 11, 2019

## Management Assurances

March 14, 2019

The management of the Farm Credit System Insurance Corporation is responsible for managing risk and maintaining effective internal control to meet the objectives of the Federal Managers' Financial Integrity Act (FMFIA).

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 cooperative lending institutions owned by the agricultural and rural customers it serves. 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 to minimize the Farm Credit Insurance Fund's exposure to potential losses. When appointed by the Farm Credit Administration, we also serve as receiver or conservator of any System bank or association.

Our management has completed an assessment of the effectiveness of FCSIC's enterprise risk management and internal control systems in effect during 2018 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 Enterprise Risk Management and 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 are reliable, complete, and timely.

On the basis of established guidelines and the assessment performed, we concluded that as of December 31, 2018, the internal control over financial reporting was effective and meets the objectives of FMFIA.

In addition, as stated in the accompanying report, FCSIC's independent auditor, BDO, indicated that the financial statements of the Farm Credit Insurance Fund as of December 31, 2018, of which we are stewards, are fairly presented in all material respects. BDO also conducted testing on the effectiveness of FCSIC's internal control over financial reporting and issued an opinion that it was effective in all material aspects.

  
C. Richard Pfitzinger  
Chief Operating Officer

  
Andrew J. Grimaldi  
Chief Financial Officer

  
Howard I. Rubin  
Chief Risk Officer/General Counsel

## Compliance with the Federal Civil Penalty Inflation Adjustment Act Improvements Act of 2015

FCSIC has authority under section 5.65(c) of the Farm Credit Act (12 U.S.C. §2277a-14) to impose civil money penalties against a Farm Credit System bank that willfully fails or refuses to file any certified statement or pay any required premium.

In addition, section 5.65(d) of the Farm Credit Act provides that, except with the prior written consent of FCA, it shall be unlawful for any person convicted of any criminal offense involving dishonesty or a breach of trust to serve as a director, officer, or employee of any System institution and authorizes FCSIC to recover penalties for a willful violation of this prohibition. Sections 5.65(c) and (d) provide for a penalty of not more than \$100 for each day during which the violation continues.

The Federal Civil Penalties Inflation Adjustment Act Improvements Act of 2015 (the 2015 Act) amended the Federal Civil Penalties Inflation Adjustment Act of 1990 (28 U.S.C. §2461 note) to provide for regular evaluation of civil penalties and required every applicable federal agency to adopt, through an interim final rule, a one-time “catch-up” adjustment to be effective no later than August 1, 2016, and annual adjustments thereafter.

FCSIC published, on January 26, 2018, a final rule making the annual adjustment required by the 2015 Act that increased our civil money penalties to not more than \$205 for each day during which a violation continues (83 FR 3563). On February 7, 2019, we published a final rule making the required annual adjustment that increased our civil money penalties to not more than \$210 for each day during which a violation continues (84 FR 2437).



# Performance Management Program

FCSIC's mandate is to ensure the timely payment of principal and interest on insured Farm Credit System debt securities and to serve as receiver or conservator when appointed by the Farm Credit Administration board. To fulfill our mandate, we have three fundamental program goals:

- Manage the Insurance Fund to protect investors
- Monitor, evaluate, and report insurance risk
- Maintain the capability to manage assistance requests, receiverships, and conservatorships

## Performance Measures

### 1. Manage the Farm Credit Insurance Fund to maintain the secure base amount to provide protection for investors and taxpayers against identified risks

We adjust insurance premium assessments when appropriate and manage assets to optimize investment returns to build and maintain the Insurance Fund at the statutory 2 percent secure base amount. At the same time, we must maintain appropriate liquidity to carry out our mission.

We assess the effectiveness of our 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
- Comparing the level of the Insurance Fund every month with the secure base amount and reporting the results to the board of directors

Our ability to maintain the Insurance Fund at the secure base amount may be affected by events beyond our control, such as insurance losses.

### 2. Monitor, evaluate, and report risks that could generate losses to the Insurance Fund

We measure progress toward this program goal by how promptly we detect emerging problems and how effectively we minimize insurance losses. We use financial indicators to monitor conditions and trends, and we analyze and report data before losses become likely. In periods when there are insurance claims or the probability of claims, the ratio of estimated losses to actual losses helps measure our ability to assess prospective loss exposure.

As guidance, our management uses criteria specified in our policy for allowance for losses and in 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. We use FCA reports of examination to evaluate risks to the Insurance Fund. When necessary, we independently examine and require information from System institutions.

### 3. Maintain the capability to manage assistance requests, receiverships, and conservatorships

FCSIC has statutory authority to provide financial assistance to System institutions, including loans. Any assistance agreement is subject to the board's approval. We have a policy statement on assistance and we have adopted procedures for providing assistance in a liquidity crisis. We measure effectiveness by periodically testing our procedures and updating our policy statement, so we remain ready to provide financial assistance in a timely and cost-effective manner.

FCSIC is required to serve as receiver or conservator of System banks and associations when appointed by FCA. This program goal requires us to maintain readiness through periodic staff training and evaluation of support 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:

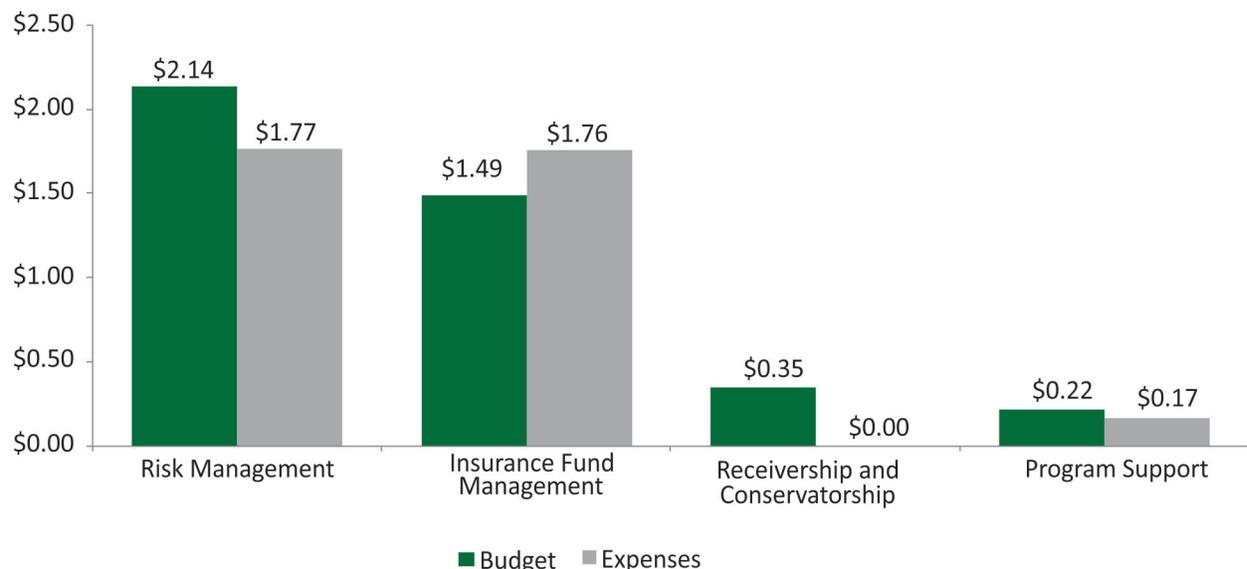
- Timeliness of initial processing of all claims (Processing should occur within a period of time warranted by the size and complexity of each case.)
- The ratio of operating costs to total assets
- The ratio of actual asset recovery returns to net realizable asset values

FCSIC has three major program areas with corresponding strategic goals and objectives. We have implemented performance measures to help us evaluate the effectiveness of these goals and objectives. It is important to note that some of these measures use management estimates that may be affected by the performance and condition of System institutions. Also, unforeseen events may have a material effect on performance measures over time. Figure 14 illustrates each program's 2018 budget and expenditures, including program support.

Figure 14

#### 2018 Budget and Expenditure by Program

(Dollars in Millions)



The Government Performance and Results Act of 1993, as amended, requires all federal government organizations to report on the results of program performance. Performance results are included in regular reports to the board of directors and in our annual report. Information for each of the three major program areas is presented in Table 4.

Table 4

### Strategic Goals and Objectives by Program Area

FCSIC's Mission	Program Areas	Strategic Goals	Strategic Objectives	For More Information
<p>Protect investors in insured Farm Credit System obligations and taxpayers through sound administration of the Farm Credit Insurance Fund (Insurance Fund).</p> <p>Exercise its authorities to minimize Insurance Fund loss.</p> <p>Help ensure the future of a permanent system for delivery of credit to agricultural borrowers.</p>	Insurance Fund management	Manage the Farm Credit Insurance Fund to maintain the secure base amount to provide protection for investors and taxpayers against identified risks.	<ol style="list-style-type: none"> <li>1. Manage the Insurance Fund to ensure adequate liquidity while optimizing investment returns and ensuring premium collections and refunds reflect anticipated changes in adjusted insured debt levels and potential insurance claims.</li> <li>2. Use actuarial tools to evaluate the adequacy of investor protections and risk exposures to the Insurance Fund.</li> <li>3. Ensure that System banks have adequate temporary liquidity in situations where external market factors make normal debt market access extremely doubtful.</li> <li>4. Communicate accurate and easily understood information about the insurance program to the public, insured investors, and System institutions.</li> </ol>	See pages 18-23 for 2018 results
	Risk management	Monitor, evaluate and report risks that could generate losses to the Insurance Fund.	<ol style="list-style-type: none"> <li>1. Use analytical models and other risk management tools and processes to identify and respond to potential risks to the Insurance Fund. Conduct trend analysis on the System's growth, funding needs, condition and performance. Regularly report to the board of directors on identified risk exposures.</li> <li>2. Monitor conditions in the agricultural and financial sectors that may affect insurance risk and integrate the results into the process for setting annual insurance premium rates.</li> </ol>	See pages 26-31 for 2018 results
	Receivership and conservatorship readiness	Maintain the capability to manage assistance requests, receiverships and conservatorships.	<ol style="list-style-type: none"> <li>1. Subject to the provisions of the Farm Credit Act, including the least-cost test, provide assistance when appropriate to a troubled System bank or association.</li> <li>2. Ensure receiverships and conservatorships are managed to fulfill the purposes of the Farm Credit Act, protect creditors, and are terminated in an orderly and timely manner.</li> </ol>	See page 32 for 2018 results

## Glossary

**Farm Credit Act** — The Farm Credit Act of 1971, as amended, (12 U.S.C. §2001 *et seq.*) is the statute under which the Farm Credit System, FCSIC, and the Farm Credit Administration operate.

**Farm Credit Administration** — FCA was established in 1933 to regulate the System. It is governed by a three-member presidentially appointed board. To ensure the safety and soundness of the System, FCA 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 System institutions. It uses a network of bond dealers to market the System's securities.

**Federal Open Market Committee** — This committee of the Federal Reserve Board 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 System 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. Because 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, these institutions may be vulnerable to the onset of adverse business conditions and could easily deteriorate if weaknesses are not corrected. Institutions that are in significant noncompliance with laws and regulations may also be given 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 taken.

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 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.

**Government-sponsored enterprise (GSE)** — A GSE is typically a federally chartered corporation created by Congress 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. The System is the oldest financial GSE.



## Acronyms and Abbreviations

AIRAs	allocated insurance reserves accounts
CIPA	Contractual Interbank Performance Agreement
FAC	Financial Assistance Corporation
Farm Credit Act	Farm Credit Act of 1971, as amended
FCA	Farm Credit Administration
FCSIC	Farm Credit System Insurance Corporation
FIRS	Financial Institution Rating System
FMFIA	Federal Managers' Financial Integrity Act
FOMC	Federal Open Market Committee
Funding Corporation	Federal Farm Credit Banks Funding Corporation
GAAP	generally accepted accounting principles
GDP	gross domestic product
GSE	government-sponsored enterprise
OMB	Office of Management and Budget
System	Farm Credit System
TIPS	Treasury inflation-protected securities
URE	unallocated retained earnings
USDA	United States Department of Agriculture



## Corporate Staff

C. Richard Pfitzinger  
Howard I. Rubin  
Andrew J. Grimaldi  
Lynn M. Powalski  
Wade Wynn  
Gregory J. Smith  
Tanya L. Renica  
Mark E. Bowen  
Matthew Morgan  
Barbara Loggins  
Molly Sproles

Chief Operating Officer  
Chief Risk Officer  
Chief Financial Officer  
General Counsel  
Chief Investment Officer and Senior Risk Analyst  
Senior Resolution Specialist  
Accountant  
Accountant  
Financial Analyst  
Senior Administrative Specialist  
Administrative Management Assistant

## Contact Information

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

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



## Banks Insured by FCSIC

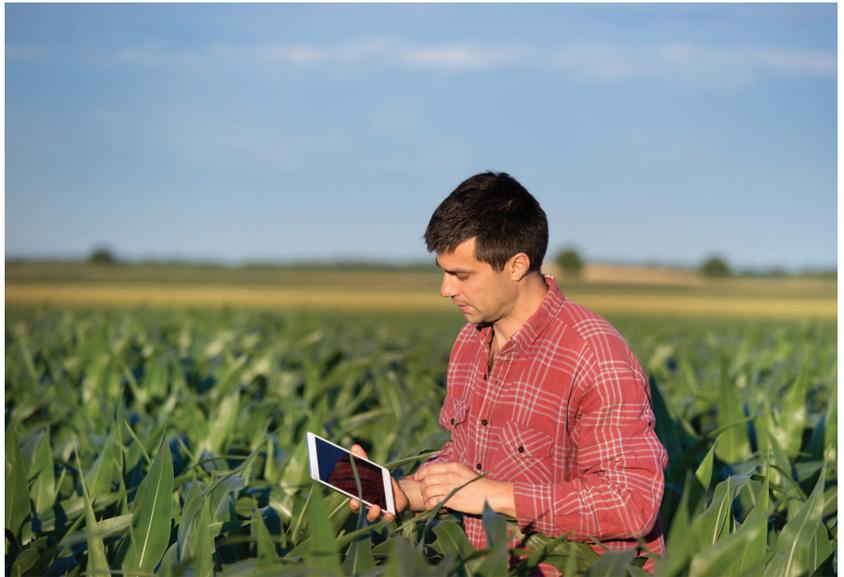
To obtain copies of quarterly and annual reports of a Farm Credit System bank and its affiliated associations, please contact the bank directly. The mailing addresses, website addresses, and telephone numbers of all four System banks are provided below.

AgFirst Farm Credit Bank  
P.O. Box 1499  
Columbia, SC 29202-1499  
(803) 799-5000  
[www.agfirst.com](http://www.agfirst.com)

AgriBank  
30 E. 7th Street, Suite 1600  
St. Paul, MN 55101-4914  
(651) 282-8800  
[www.agribank.com](http://www.agribank.com)

CoBank  
P.O. Box 5110  
Denver, CO 80217-5110  
(303) 740-4000  
[www.cobank.com](http://www.cobank.com)

Farm Credit Bank of Texas  
P.O. Box 202590  
Austin, TX 78720-2590  
(512) 465-0400  
[www.farmcreditbank.com](http://www.farmcreditbank.com)



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

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## Additional 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  
101 Hudson Street  
Suite 3505  
Jersey City, NJ 07302  
(201) 200-8000

These documents are also available on the Funding Corporation's website at [www.farmcreditfunding.com](http://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](http://www.fca.gov).



Farm Credit System Insurance Corporation  
1501 Farm Credit Drive  
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