FARM CREDIT SYSTEM INSURANCE CORPORATION POLICY STATEMENT ON THE SECURE BASE AMOUNT AND ALLOCATED INSURANCE RESERVES ACCOUNTS

Background:

The Farm Credit Act of 1971, as amended (Act) established the Farm Credit System Insurance Corporation (FCSIC or Corporation) to, among other things, insure the timely payment of principal and interest on Farm Credit System obligations.[1] Section 5.55 of the Act mandates that the Corporation build and manage the Farm Credit Insurance Fund (Insurance Fund) to attain and maintain a secure base amount (SBA), defined as 2 percent of the aggregate outstanding insured obligations of all insured System banks (excluding a percentage of State and Federally guaranteed loans and investments) or such other percentage of the aggregate amount as the Corporation in its sole discretion determines is actuarially sound. The Farm Credit System Reform Act of 1996[2], amended section 5.55 of the Act to establish in the Insurance Fund an Allocated Insurance Reserves Account (AIRA) for the benefit of each insured System bank and an AIRA for the Farm Credit System Financial Assistance Corporation (FAC) stockholders; allocate any excess balances above the SBA to these AIRAs; and make partial distributions of the excess funds in the AIRAs. Congress, by enactment of the Food, Conservation, and Energy Act of 2008 (FCE Act),[3] amended the provisions of the Act that govern FCSIC premiums, the SBA, and AIRAs to incorporate the Corporation's recommendations concerning calculation of premiums and the SBA, and the simplification of the provisions governing AIRAs. In 2009, the Corporation adopted final regulations implementing the amended provisions of the Act governing FCSIC premiums, the SBA and AIRAs.

Applicability:

This policy statement will govern the calculation of the secure base amount, the determination of any excess above the SBA, the method for allocating any excess to the AIRAs, and the method for making payments from the AIRAs to accountholders.

Policy Statement:

I. SECURE BASE AMOUNT DETERMINATION

As stated in the Corporation's Policy Statement Concerning Adjustments to the Insurance Premiums, the Corporation's Board of Directors (Board) will review the premium assessments at least semiannually to determine whether to adjust premiums in response to changing conditions. The Board continues to engage in this review even after the Insurance Fund achieves the SBA because the law requires the Corporation to maintain the SBA. Thus, the Corporation must

[1] The Agricultural Credit Act of 1987, Pub. L. No. 100-233 (1988), amended the Farm Credit Act of 1971 to establish the Farm Credit System Insurance Corporation. (12 USC §§ 2277a-1 et seq.)
[2] Pub. L. No. 104-105, 110 Stat. 162 (1996).
[3] Pub. L. No. 110-234, Pub. L. No. 110-246, 122 Stat. 1651 (2008).

ensure that as the Farm Credit System's insured debt grows, or if the Insurance Fund suffers a significant loss, the Insurance Fund builds back to the SBA.

The Farm Credit System Reform Act of 1996 established a process for making partial distributions of the Insurance Fund's balance above the SBA. On March 23, 2007, the Corporation's Board of Directors adopted a legislative proposal requesting that the Congress amend the Act to, inter alia, base premiums on the outstanding insured debt obligations instead of loans, permit the Corporation to collect a broader range of premiums on insured debt, and simplify the provisions concerning allocation of funds to the AIRAs and the payment of funds from the AIRAs to accountholders. Ultimately, enactment of the FCE Act in 2008 amended the provisions of the Farm Credit Act of 1971 that govern FCSIC premiums to include the Corporation's proposed changes.

As amended, the Act's provisions also reduce the total insured debt obligations on which premiums are assessed by 90 percent of Federal government-guaranteed loans and investments and 80 percent of State government-guaranteed loans and investments, and deduct similar percentages of such guaranteed loans and investments when calculating the secure base amount. The amendments also simplified the method of paying out AIRAs, prescribing that, if the aggregate of the amounts in the Farm Credit Insurance Fund exceeds the secure base amount at the end of any calendar year, the Corporation shall allocate to the AIRAs the excess amount less the amount that the Corporation, in its sole discretion, maintains for estimated operating expenses and estimated insurance obligations of the Corporation for the following calendar year.

To begin the process, the Corporation must define the aggregate outstanding insured obligations of all the System banks. Then it must follow the steps in the statute to determine the SBA. Finally, at the end of any calendar year in which the Insurance Fund attains the secure base amount, the Corporation must determine whether any excess funds exist for allocation to the AIRAs.

The principal calculation for determining whether the Insurance Fund is at the SBA amount will be 2 percent of the aggregate adjusted insured obligations defined as follows:

(1) "Insured obligation" means any note, bond, debenture, or other obligation issued under subsection (c) or (d) of section 4.2 of the Farm Credit Act on or before January 5, 1989, on behalf of any System bank; and after such date which, when issued, is issued on behalf of any insured System bank and is outstanding at the quarter-end. The balance outstanding at the quarter-end shall include principal and accrued interest payable as reported by the banks in the call reports submitted to the Farm Credit Administration.

(2) The aggregate outstanding insured obligations of all insured System banks determined under paragraph (1) of Section I shall be adjusted downward to exclude an amount equal to the sum of (as determined by the Corporation):

(A) 90 percent of each of

(i) the guaranteed portions of principal outstanding on Federal government-guaranteed loans in accrual status made by the banks; and

(ii) the guaranteed portions of the amount of Federal government-guaranteed investments made by the banks that are not permanently impaired; and

(B) 80 percent of each of

(i) the guaranteed portions of principal outstanding on State government-guaranteed loans in accrual status made by the banks; and

(ii) the guaranteed portions of the amount of State government-guaranteed investments made by the banks that are not permanently impaired.

For the purpose of this paragraph (2), the principal outstanding on all loans made by an insured System bank, and the amount outstanding on all investments made by an insured System bank, shall be determined based on

(a) all loans or investments made by any production credit association, or any other association making direct loans under authority provided under section 7.6 of the Act, that is able to make such loans or investments because such association is receiving, or has received, funds provided through the insured System bank;

(b) all loans or investments made by any bank, company, institution, corporation, union, or association described in section 1.7(b)(1)(B)of the Act, that is able to make such loans or investments because such entity is receiving, or has received, funds provided through the insured System bank; and

(c) all loans or investments made by such insured System bank (other than loans made to any party described in paragraph (a) or (b)).

At the end of any calendar year when the Insurance Fund balance exceeds the SBA, calculated using December 31, balances, the Corporation will determine whether any excess funds exist for allocation to the AIRAs.

II. ALLOCATED INSURANCE RESERVES ACCOUNTS

(1) *Determination of Excess Insurance Fund Balances*

An AIRA shall be established in the Insurance Fund for each insured System bank and for FAC stockholders. Amounts representing excess Insurance Fund balances will be allocated to the AIRAs. The AIRAs remain a part of the Insurance Fund and are available to the Corporation.

(a) *Authorized Deductions*

If, at the end of any calendar year, the aggregate of the amounts in the Farm Credit Insurance Fund exceeds the secure base amount, the Corporation shall allocate to the AIRAs the excess amount less the amount that the Corporation, in its sole discretion, determines to be the sum of the estimated operating expenses and estimated insurance obligations of the Corporation for the immediately succeeding calendar year. The Corporation will budget for the next calendar year operating expenses and it will deduct the operating expenses it expects to incur. When determining estimated insurance obligations, the Corporation will include all anticipated allowances for insurance losses, claims, and other potential statutory uses of the Insurance Fund.

The excess Fund balance shall be allocated to the accounts of each insured System bank and to the FAC stockholders. The AIRA balances will be fixed at year-end until paid to account holders or used under (c). The Act provides that, not later than 60 days after receipt of a payment from the AIRAs established for the insured System banks, each insured System bank, in consultation with affiliated associations of the insured System bank, and taking into account the direct or indirect payment of insurance premiums by the associations, shall develop and implement an equitable plan to distribute payments received among the bank and associations of the bank. The Corporation will request that each insured System bank promptly transmit a copy of the plan that the institution develops for the distribution of such AIRA payments.[4]

(b) *Allocation Formula When Excess Funds Are Available*

(1) Ten percent of the excess Insurance Fund balance shall be credited to the AIRAs for all holders, in the aggregate, of FAC stock. The total amount that may be allocated to this AIRA is limited to $35.5 million ($56 million less the $20.5 million that was paid out in 2010).

(2) The remaining amount of the excess Insurance Fund balance shall be credited to the AIRA for each insured System bank. There shall be credited to the AIRA of each insured system bank an amount that bears the same ratio to the total amount (less any amount credited under paragraph (1)(b)(1) of this Section II) as--
(i) the average principal outstanding for the calendar year on insured obligations issued by the bank (after deducting from the principal the percentages of the guaranteed portions of loans and investments described in paragraph (2) of Section I above); bears to
(ii) the average principal outstanding for the calendar year on insured obligations issued by all insured System banks (after deducting from the principal the percentages of the guaranteed portions of loans and investments described in paragraph (2) of Section I above).

(3) An example of the allocation formula is shown in the attached Exhibit 1.

(c) *Use of Funds in AIRAs When Reductions Are Required*

To the extent that the sum of the operating expenses of the Corporation and the insurance obligations of the Corporation for a calendar year exceeds the sum of operating expenses and insurance obligations determined under paragraph (1)(a) of this Section II for the calendar year, the Corporation shall cover the expenses and obligations by reducing each AIRA by the same proportion, and expending the amounts so obtained before expending other amounts in the Fund.

When the Corporation's actual operating expenses and insurance obligations exceed the estimated amounts used to determine any year's AIRA balances, the Act requires AIRA balances to absorb such excess expenses before using other amounts in the Insurance

[4] *See*, Act, section 5.55(e)(6)(D), 12 U.S.C. 2277a-4(e)(6)(D).

Fund.[5] To the extent reductions are made in AIRA balances to absorb Corporation expenses and actual insurance obligations, each AIRA will be reduced by its proportional amount in accordance with the statute. The same formula used to make allocations of excess Insurance Fund balances shall be used to reduce AIRA balances when necessary. Ten percent of any necessary AIRA reduction will be applied to the FAC stockholder AIRA. The remaining 90 percent will be applied to the System insured banks' AIRAs on the basis of the ratio of described in paragraph (1)(b)(2) of this Section II.

DATED THIS 8TH DAY OF DECEMBER, 2011

BY ORDER OF THE BOARD OF DIRECTORS

Attachment:
Exhibit 1- Recent Example of Allocation and Payment

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[5] *See*, Act, section 5.55(e)(5), 12 U.S.C. 2277a-4(e)(5).

Exhibit 1

Recent Example - AIRAs Allocation and Payment

Insurance Fund Balance @ 12/31/2009 (including $39,888,432 allocated to AIRAs in 2003)	$	3,287,696,411
Less: FCSIC's Prospective Operating Expenses for 2010	$	(3,863,892)
Insurance Fund Balance for Calculation of AIRAs	$	3,283,832,519
Less: Secure Base Amount at 12/31/2009 (see page 3 of example)	$	(3,078,512,000)
Excess Insurance Fund Balance	$	205,320,519
Less: Amount Allocated to AIRAs in 2003	$	(39,888,432)
Amount Allocated to AIRAs in 2009	$	165,432,087

Apportionment of Amount Allocated to AIRAs in 2009	$	165,432,087
FAC Stockholders in aggregate (10% of Allocable Amount) - Apportioned Based on Number of Shares Held (see page 2 of example for details)	**$**	**16,543,209**
Banks (90% of Allocable Amount) - Apportioned Based on Average Adjusted Debt Outstanding	**$**	**148,888,878**

Bank Apportionment

	Percentage		Amount Allocated
AgFirst FCB	14.87%	$	22,141,337
AgriBank, FCB	36.30%	$	54,044,812
U.S. AgBank, FCB	13.61%	$	20,260,392
FCB of Texas	7.47%	$	11,121,022
CoBank, ACB	27.75%	$	41,321,315
Total	100%	$	148,888,878

Recent Example - AIRAs Allocation and Payment

FAC Shareholders Balances		Shares Outstanding	Percentage	Adjusted Shares Retired [1]	Amount Paid to FAC Stockholders [2] Payment 1	Shares Remaining After Payment 1	Percentage	Adjusted Shares Retired [1] Approved Mar 2010	Amount Paid to FAC Stockholders [2] Payment 2	Shares Remaining After Payment 2
FCB of Texas		**2,487,975**	**22.28%**	**177,727**	**$ 888,635.00**	**2,310,248**	**22.00%**	**727,901**	**$ 3,639,506**	**1,582,347**
AgriBank, FCB		**2,812,507**	**25.18%**	**200,910**	**$ 1,004,550.00**	**2,611,597**	**25.00%**	**827,160**	**$ 4,135,802**	**1,784,437**
CoBank		**712,660**	**6.38%**	**50,909**	**$ 254,545.00**	**661,751**	**6.00%**	**198,519**	**$ 992,593**	**463,232**
U.S. AgBank		**1,727,833**	**15.47%**	**123,427**	**$ 617,135.00**	**1,604,406**	**16.00%**	**529,383**	**$ 2,646,913**	**1,075,023**
AgFirst Associations (Total)		**3,426,889**	**30.69%**	**244,806**	**$ 1,224,030.00**	**3,182,083**	**31.00%**	**1,025,679**	**$ 5,128,395**	**2,156,404**
	MidAtlantic	770,209	22.48%	55,020	$ 275,100.00	715,189	22.48%	230,526	$ 1,152,630	484,663
	FC of the Virginias	571,525	16.68%	40,827	$ 204,135.00	530,698	16.68%	171,059	$ 855,296	359,639
	Colonial Farm Credit	448,912	13.10%	32,068	$ 160,340.00	416,844	13.10%	134,361	$ 671,804	282,483
	Chattanooga	257,737	7.52%	18,412	$ 92,060.00	239,325	7.52%	77,142	$ 385,708	162,183
	Puerto Rico Farm Credit	243,042	7.09%	17,362	$ 86,810.00	225,680	7.09%	72,743	$ 363,716	152,937
	Jackson Purchase	221,845	6.47%	15,848	$ 79,240.00	205,997	6.47%	66,399	$ 331,995	139,598
	AgChoice Farm Credit	210,042	6.13%	15,005	$ 75,025.00	195,037	6.13%	62,866	$ 314,331	132,171
	Central Kentucky	201,347	5.88%	14,384	$ 71,920.00	186,963	5.88%	60,264	$ 301,319	126,699
	AgGeorgia Farm Credit	106,773	3.12%	7,628	$ 38,140.00	99,145	3.12%	31,958	$ 159,788	67,187
	Ag Credit	97,918	2.86%	6,995	$ 34,975.00	90,923	2.86%	29,307	$ 146,536	61,616
	AgCarolina	94,692	2.76%	6,765	$ 33,825.00	87,927	2.76%	28,342	$ 141,708	59,585
	Carolina Farm Credit	83,163	2.43%	5,941	$ 29,705.00	77,222	2.43%	24,891	$ 124,455	52,331
	AgSouth Farm Credit	77,850	2.27%	5,562	$ 27,810.00	72,288	2.27%	23,301	$ 116,504	48,987
	ArborOne	41,834	1.22%	2,989	$ 14,945.00	38,845	1.22%	12,521	$ 62,605	26,324
FAC Stockholder Totals		**11,167,864**		**797,779**	**$ 3,988,895.00**	**10,370,085**		**3,308,642**	**$ 16,543,209**	**7,061,443**

[1] The number of shares retired has been rounded upwards to the next full $5 par value share.
[2] The amount paid to FAC shareholders has been increased to allow for the retirement of full shares.
Payment 1 was authorized by the FCSIC Board in January 2010. Payment 2 was authorized in March 2010.