Farm Credit Administration

. . . we ensure a dependable source of credit for agriculture and rural America

Performance and Accountability Report
Fiscal Year 2006

Contents

Statement of the Chairman and CEO

November 2006

As Chairman and Chief Executive Officer of the Farm Credit Administration (FCA or Agency), and on behalf of the FCA Board, I invite you to review this Performance and Accountability Report. It details the Agency's accomplishments and program and financial performance for fiscal year (FY) 2006.

I am pleased to report that FCA achieved each of the goals outlined in its Strategic Plan and achieved or exceeded all of the performance measures targeted for FY 2006. FCA's first goal is to ensure that the Farm Credit System (System) and the Federal Agricultural Mortgage Corporation (Farmer Mac) fulfill their public missions for agriculture and rural areas. FCA's second goal is to evaluate risk and provide timely and proactive oversight to ensure the System's and Farmer Mac's safety and soundness. The Agency's third goal, implementation of the President's Management Agenda, requires the periodic reassessment of FCA's structure in order to keep the Agency an efficient and effective organization.

While the results achieved over the past fiscal year demonstrate FCA's achievement of its strategic goals, we recognize that the ultimate measure of the Agency's performance is the ability of regulated institutions to fulfill their mission and remain fundamentally sound in all material respects. The FCA will remain vigilant in its efforts to ensure that the System and Farmer Mac fulfill their respective missions and that FCA will continue to make significant structural improvements, as recommended in the recent strategic study of FCA operations.

In addition to these programmatic results, FCA is also accountable for financial results. I am happy to report that the FCA's FY 2006 financial statements have received an unqualified opinion from an independent auditor. These financial statements provide a fair representation of the FCA's accounting practices and demonstrate its commitment to sound fiscal management. One of my goals as the Chief Executive Officer is to administer the programs of the Agency as efficiently and effectively as possible. I rely on the Agency's systems of management controls to adhere to sound financial management practices, to comply with Federal law, and to protect the Agency's assets.

As another successful year draws to a close, FCA renews its commitment to its mission: to ensure a safe, sound, and dependable source of credit and related services for agriculture and rural America. The Agency has made, and will continue to make, a positive difference, thanks to its highly experienced, hard working, and dedicated staff. Together, we will strive to do what is best for agriculture, rural America, and the American people whom we serve.

Nancy C. Pellett

Nancy C. Pellett
Chairman and CEO
Farm Credit Administration

Management's Discussion and Analysis

FCA at a Glance

The Farm Credit Administration is an independent agency within the executive branch of the U.S. Government responsible for regulating and supervising the banks, associations, and related entities in the Farm Credit System (FCS or System), including the Federal Agricultural Mortgage Corporation (Farmer Mac). The FCS is a nationwide network of borrower-owned financial institutions that provide credit to farmers, ranchers, and agricultural and rural utility cooperatives.

FCA was created by a 1933 Executive order of President Franklin D. Roosevelt; the Agency now derives its powers and authorities from the Farm Credit Act of 1971, as amended (Farm Credit Act or Act). The U.S. Senate Committee on Agriculture, Nutrition, and Forestry and the U.S. House of Representatives Committee on Agriculture oversee the FCA and the FCS.

The FCA is responsible for ensuring a dependable source of credit for agriculture and rural America. We do this in two specific ways. First, we conduct on-site examinations of FCS institutions to monitor and oversee the safety and soundness of their ongoing activities. These examinations also focus on whether System institutions are meeting their public mandate to serve all eligible borrowers. Second, we approve corporate charter changes and research, develop, and adopt rules, regulations, and other guidelines that govern how System institutions conduct their business and interact with their customers.

If a System institution violates a law or regulation, or if its operations are unsafe or unsound, FCA may use its enforcement authority to ensure that the problem is corrected. FCA also protects the rights of borrowers, issues and changes the charters of FCS institutions, reports to Congress on the financial condition and performance of the FCS, and approves the issuance of System debt obligations.

The Agency maintains its headquarters and a field office in McLean, Virginia. There are also field offices in Bloomington, Minnesota; Dallas, Texas; Denver, Colorado; and Sacramento, California.

FCA policy and its regulatory agenda are established by a full-time, three-person Board, whose members are appointed by the President of the United States with the advice and consent of the Senate. They serve 6-year terms and may not be reappointed after serving full terms or more than 3 years of previous members' terms. The President designates one member as Chairman of the Board, who serves until the end of his or her own term. The Chairman also serves as FCA's Chief Executive Officer (CEO).

The FCA does not receive a Federal appropriation. We are funded through assessments paid by System institutions and by reimbursable activities.

Mission

The Farm Credit Administration ensures a safe, sound, and dependable source of credit and related services for agriculture and rural America.

Farm Credit Administration Offices

The 256 full- and part-time employees of the FCA work together to ensure that the FCS remains a dependable source of credit for agriculture and rural America. The following paragraphs explain the functions of each of the Agency's offices.

The **FCA Board** approves the policies, regulations, charters, and enforcement activities that ensure a strong FCS. The Board also provides for the examination and supervision of the FCS, including Farmer Mac, and oversees the activities of the FCS Building Association, which acquires, manages, and maintains FCA headquarters and field office facilities.

The **Secretary to the Board** ensures that the FCA Board complies with statutory, regulatory, and internal operation procedures and requirements. The Secretary to the FCA Board also serves as Secretary to the Farm Credit System Insurance Corporation Board (FCSIC). In addition, the Secretary serves as the Parliamentarian and the Sunshine Act Official for the FCA Board.

The **Office of the Chief Executive Officer** enforces the rules, regulations, and orders of the FCA Board. The CEO directs the implementation of policies and regulations adopted by the FCA Board. The office plans, organizes, directs, coordinates, and controls FCA operations and leads the Agency's efforts to achieve and manage a diverse workforce.

The **Office of Congressional and Public Affairs (OCPA)** serves as the Agency's principal point of contact for Congress, the media, other government agencies, FCS institutions, employees, System borrowers, and the public. OCPA develops and monitors legislation pertinent to FCA and the FCS, serves as the Agency's congressional liaison, and prepares testimony for the Chairman and other staff members. The office provides information to external audiences through news releases, information brochures and fact sheets, the annual *FCA Performance and Accountability Report,* and other publications. OCPA manages media relations regarding Agency activities and the content of the FCA Web site. The office also coordinates special meetings, briefings for international visitors, and field hearings.

The **Office of Examination** is responsible for programs of examination and supervision of each FCS institution, in accordance with the Farm Credit Act of 1971, as amended, and applicable regulations. The office develops oversight plans; conducts examinations; monitors the System's condition, risks, and emerging risks; and develops supervisory strategies to ensure that the System operates in a safe and sound manner and fulfills its public policy purpose. The FCA Board further defines the Office of Examination's role in Policy Statement 53 available at www.fca.gov.

The **Office of the General Counsel** provides the FCA Board and staff with legal counsel, as well as guidance on general corporate, personnel, ethics, and administrative matters. The office supports the Agency's development and promulgation of regulations, civil litigation, enforcement of applicable laws and regulations, and implementation of conservatorships and receiverships. The office serves as the liaison to the *Federal Register,* creates and maintains the Agency's public rulemaking files, and handles the Agency's submission of the Unified Agenda of Federal Regulatory and Deregulatory Actions. The office also handles Freedom of Information Act requests and matters pertaining to the Privacy Act.

The **Office of the Inspector General** provides independent and objective oversight of Agency programs and operations through audits, inspections, investigations, and the review of proposed legislation and regulations. The office promotes economy and efficiency within FCA and seeks to prevent and detect fraud, waste, and abuse in the Agency's programs and operations.

The **Office of Regulatory Policy** manages all policy and regulation development activities that ensure the safety and soundness of the FCS and support the System's mission as a dependable source of credit and related services for agriculture and rural America. Policy and regulation development activities include the analysis of policy and strategic risks to the System, considering economic trends and other risk factors. The office also evaluates all regulatory and statutory prior approvals for System institutions, including chartering and other corporate approvals, as well as funding approvals on behalf of the FCA Board.

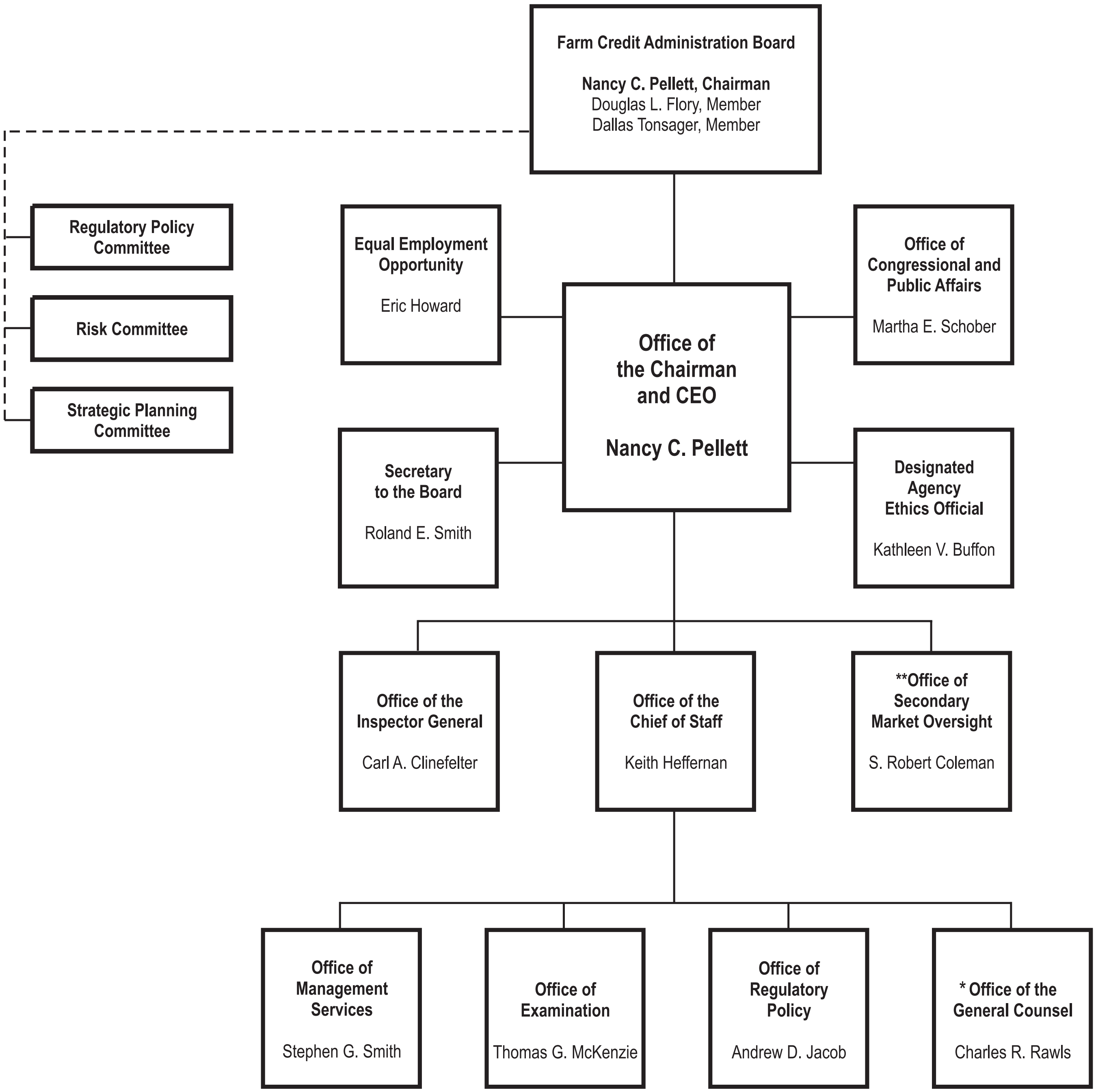
The **Office of Management Services** manages and delivers the Agency's information technology, financial, human capital, and administrative services. The office coordinates planning efforts, including information resources management, security, human capital, and financial plans for the Agency. By centrally planning, managing, and delivering resource services, the Office of Management Services enables the Agency's program offices to fully focus their time and attention on their respective mission-related responsibilities.

The **Office of Secondary Market Oversight** provides for the examination, regulation, and supervision of the activities of Farmer Mac to ensure its safety and soundness and the accomplishment of its public policy purpose as authorized by Congress. It also ensures that Farmer Mac complies with applicable laws and regulations, and it manages FCA's enforcement activities with respect to Farmer Mac.

The **Equal Employment Opportunity (EEO) Program** directs the Agency's efforts to achieve and manage a diverse workforce and encourages awareness of, and respect for, diversity in the workplace. The office works to prevent employment discrimination, handles employee discrimination complaints, and sponsors training and seminars on EEO issues.

The **Designated Agency Ethics Official** administers the provisions of the Ethics in Government Act of 1978, as modified by the Ethics Reform Act of 1989, for FCA. This office coordinates and manages FCA's ethics program and serves as liaison to the U.S. Office of Government Ethics. The responsibilities of the position include reviewing financial disclosure reports of FCA staff and prospective Presidential appointees to the FCA Board, conducting FCA's ethics training, counseling staff on ethics standards and post-employment conflicts of interest, and assisting managers and supervisors in understanding and implementing Agency ethics programs.

Organization
Farm Credit Administration
As of September 30, 2005



*Maintains a confidential advisory relationship with each of the Board members.
** Reports to the Board for policy and to the CEO for administration.

Highlights of FCA's Performance Goals and Results

The primary goal of the 2004–2009 strategic plan of the Farm Credit Administration is to achieve the objectives for which Congress established the Farm Credit System (FCS or System). As provided in the Farm Credit Act of 1971, as amended, the purpose of the FCS is to enhance the farmer-owned cooperative system by making credit available to farmers and ranchers and their cooperatives, to rural residents for their homes, and to associations and other entities upon which farming operations depend. The FCS provides an adequate and flexible flow of money into rural areas.

The Farm Credit Act states that a prosperous, productive agriculture sector is essential to a free nation. Because Congress recognized the growing need for credit in rural areas, it established the farmer-owned cooperative FCS and mandated the System to improve the income and well-being of American farmers and ranchers. The FCS achieves this by furnishing sound, adequate, and constructive credit and closely related services for farmers and ranchers, their cooperatives, and for selected farm-related businesses necessary for efficient farm operations. Therefore, the mission of the Agency is to ensure that those who engage in agriculture, live in rural areas, or operate farm-related businesses are provided access to the FCS for their credit and financially related needs.

The FCA's regulatory supervision and oversight of the FCS ensures that System institutions operate in a safe and sound manner and provide dependable sources of constructive credit and financially related services to agriculture and rural areas, as Congress intended. The ultimate measures of FCA's performance are whether the intended recipients are afforded access to the credit and services of the FCS, and whether the FCS is fundamentally sound in all material respects. The results achieved in the reporting period ended June 30, 2006, indicate that the Agency met these objectives, as the services of the FCS continued uninterrupted in a safe and sound manner throughout the United States and Puerto Rico.

The FCA strategic plan for 2004–2009 continues to include three goals, each of which has a "desired outcome" and itemized descriptions of the "means and strategies" by which the Agency carries out its mission. There are also 18 performance measures that contain "targeted results" to determine whether the Agency effectively carried out its mission and achieved the desired outcomes of the strategic plan. Based on the results of operations for FY 2006, FCA achieved each of the three goals in the strategic plan, and it achieved or exceeded all of the performance measures. The following is a summary analysis of FCA's goal performance in its mission to serve the public's interest.

Goal 1 Highlights—Public Mission:

Ensure the Farm Credit System and Federal Agricultural Mortgage Corporation (Farmer Mac) fulfill their public mission for agriculture and rural areas.

Twelve means and strategies and six performance measures are established for Goal 1 in the strategic plan. The six performance measures evaluated the following:

- the percentage of FCS institutions with effective business and marketing plans
- the percentage of direct-lender institutions with effective internal controls over consumer and borrower-rights compliance
- the percentage of instances in which the Agency used supplemental approaches to solicit public input on regulatory initiatives
- the percentage of institutions with effective young, beginning, and small (YBS) farmer programs
- the percent change in System use of Federal and State loan guarantee programs
- whether Farmer Mac has maintained an effective marketing program to grow program assets consistent with its mission

For each of the six measures associated with Goal 1, the Agency achieved or exceeded its targets. FCA examiners reviewed business plans of 101 FCS institutions and found that all of them had satisfactory plans. Agency examiners performed compliance reviews of 39 direct-lender institutions and determined that all of them had satisfactory internal controls over consumer and borrower-rights compliance. In addition, FCA examiners reviewed 51 direct-lender institutions to determine whether they had effective programs to meet YBS farmer and rancher needs, and all of them did.

Goal 2 Highlights—Safety and Soundness:

Evaluate risk and provide timely and proactive oversight to ensure the safety and soundness of the Farm Credit System and Farmer Mac.

Seven means and strategies and seven measures exist for Goal 2. The seven performance measures considered the following:

- the number of institutions that FCA placed in receivership
- the total FCS assets that FCA determined were fundamentally sound
- the percentage of institutions with Financial Institution Rating System (FIRS) scores of 3, 4, or 5 that had acceptable corrective action plans
- the percentage of System assets in institutions with adverse assets-to-risk funds of less than 100 percent
- the percentage of institutions complying with all regulatory capital ratio requirements
- the percentage of FCS institutions with acceptable action plans to correct violations identified by FCA examiners

- the percentage of FCA-regulated institutions with satisfactory audit and review programs

The target for FCS institutions to achieve composite FIRS ratings of 1 or 2 was exceeded, as were other safety and soundness targets. These favorable ratings occurred because all direct-lender institutions were well capitalized and maintained sound levels of risk-bearing capacity. No institutions were placed in receivership during the year, nor were any operating under enforcement actions.

Furthermore, all FCS institutions and Farmer Mac complied with FCA capital adequacy regulations. In addition, the targets that measure institution compliance with laws and regulations and the objective to maintain effective audit and review programs were achieved.

One of the Agency's targets is to ensure that all FCS institutions with FIRS ratings of 3, 4, or 5 have satisfactory corrective action plans. Since all FCS institutions had FIRS ratings of 1 or 2, the substance of the measurement was fully achieved without the need for corrective action plans.

Goal 3 Highlights—President's Management Agenda:

Implement the President's Management Agenda.

Goal 3 has five means and strategies and five performance measures. The five measures evaluated the following:

- whether the structure of the Agency was being assessed every 5 years to maintain an efficient and effective organization
- whether the Agency had received an unqualified audit opinion on its financial and accounting records
- the number of material internal control weaknesses reported by the Agency's auditors
- the percentage of the Agency's Web pages and electronic devices that were Section 508 accessibility compliant
- the extent to which the Agency's information and technology services are continuously available

The targets for all of the performance measures for Goal 3 were achieved or exceeded. The structure of the Agency was evaluated through strategic studies conducted in FY 2005, which resulted in numerous structural changes to improve operations and efficiency. The final changes to the organization as a result of the studies conducted were completed in the first quarter of 2006.

With respect to the Agency's financial and accounting records, an unqualified opinion on its financial statements was received for FY 2005; external auditors identified no material internal control weaknesses. Also, the Agency's Web pages and electronic devices remained in compliance with Section 508 accessibility rules throughout the year, and there were no unexpected disruptions to the Agency's computer system services.

Management Challenges

FCA is the Federal regulator for the Farm Credit System. Its primary mission is to ensure that FCS institutions operate safely and soundly and in compliance with all applicable laws and regulations. FCA continues to face external and internal management challenges that reflect changes both in agriculture and in the financial services industry. As producers and lenders must adapt to change, the Agency must also both anticipate and react to change in order to provide a regulatory framework within which the System can fulfill its congressional mandate to provide dependable and constructive credit and related services to agriculture and rural America.

As rapid change occurs in rural America, FCA faces the overarching challenge of adjusting our regulatory and policy guidance based on the dynamic nature of farming, the agricultural marketplace, and agriculture finance generally. FCA must balance its responsibility as an arm's-length regulator—that is, ensuring that the System is fundamentally sound and secure—with its recognition of the need for regulatory flexibility so that the FCS is able to fulfill its Government-sponsored enterprise (GSE) mandate to serve those in agriculture and rural areas.

These are exciting and challenging times for agriculture and for the FCS. Agricultural producers have new capital-intensive opportunities such as the increased demand for alternative energy sources, including ethanol, biodiesel, and wind energy. These positive developments will likely create a significant demand for agricultural commodities and land. On the other hand, external challenges include possible cuts in agriculture subsidies, natural disasters such as hurricanes, high energy prices, and the threat of animal diseases such as avian influenza.

The changing needs of rural communities are becoming a priority for policymakers, and the System's response to these needs raises other issues for FCA. There is a growing recognition that the nation must stimulate and provide capital to rural areas or suffer the negative social and economic consequences. Rural America is now attracting retirees with business experience and liquidity who want to return to their roots, as well as younger people with enthusiasm and ambition who want a better quality of life. Both groups demand amenities that are not typically found in rural America, such as high-speed Internet connections, recreation sites, and cultural opportunities.

Changes in agriculture and rural America will continue to affect the American farmer and rancher and the FCS. In response to these changes in rural America, the Agency will consider new guidance concerning the System's service to farmers and ranchers and concerning the determination of "moderately priced" rural housing limits. The Agency will also begin reviewing how System partnerships and investments could help increase the availability of funds to agriculture and rural America.

FCA is also mindful of its responsibility to maintain the integrity of the System as a GSE. The Agency issued a final regulation on governance in early 2006 and anticipates issuing a final rule on disclosure requirements by the end of the calendar year. In 2007, the Agency will also propose rules on disclosure and accounting requirements and will review and consider appropriate changes to capital adequacy requirements.

As the System adapts to a changing environment, FCA must continue to internally modify its workforce to make certain that the System's safety and soundness remains its first priority and that the Agency retains the expertise and resources to carry out its mission-related responsibilities. Clearly, the FCA's most valuable resource is its employees, and the FCA's human capital strategies rightly focus on ensuring that the Agency continues to employ a highly skilled and competent workforce in spite of projected retirements. To achieve this, the Agency must (1) provide targeted education and technical training for existing staff, (2) identify qualified candidates for career development and leadership training opportunities, and (3) seek to attract new employees with well-defined skill sets to lessen the impact of anticipated retirements.

It is important to note that, with the retirement of senior staff members, the average tenure of FCA employees will decrease—a development that will challenge the Agency to secure the stability and skill level of its workforce through effective succession planning and cross-training. As a small agency, FCA is involved in strategic workforce planning on an ongoing basis. Knowledge management and knowledge-sharing strategies will also be critical tools that the Agency can use to mitigate the loss of institutional knowledge that will occur with the loss of senior staff members. The FCA has embarked upon an electronic knowledge management initiative that has a projected implementation date in early FY 2008.

Knowledge management strategies are also included in the Human Capital Plan, FY 2007–2011, which was developed to ensure that FCA will continue to employ well-trained, dedicated employees to accomplish the Agency's strategic goals and objectives. The Human Capital Plan is reviewed on an annual basis and updated, as necessary, to make certain that it continues to effectively address the human capital needs of the FCA. This review includes an assessment of the Agency's human capital goals; validation of the Human Capital Plan in terms of FCA's strategic alignment; workforce planning and development; leadership and knowledge management; maintaining a results-oriented performance culture; staff expertise; and accountability. In addition, the Human Capital Plan is examined in terms of alignment with performance plans and the budget.

Finally, during the recent Agency reorganization, special emphasis was placed on a client-focused structure and approach to better meet FCA's mission and customer needs. Analyzing FCA's workforce trends and future staffing needs will also help identify the Agency's human capital challenges and ensure that the FCA's investments in staff development are strategic and comprehensive.

FCA management is committed to meeting challenges and improving the Agency's efficiency and effectiveness. Our response to these challenges will ultimately ensure a safe and sound System that serves the changing face of agriculture and rural America as Congress intended.

Analyses and Highlights of FCA's Financial Statements

Financial Highlights

Financial Operation of the FCA

FCA operates under the authority of the Farm Credit Act of 1971, as amended. FCA maintains a revolving fund in which moneys are obtained primarily from assessments received from the Farm Credit System institutions, including the Federal Agricultural Mortgage Corporation and service corporations. Moneys are also received for reimbursable services provided to other Government agencies. FCS institutions, including Farmer Mac, are assessed and charged directly or billed in accordance with a formula established by FCA regulations. Assessments and other income earned in excess of obligations are either refunded or considered in determining the amount to assess System institutions in the subsequent fiscal year. Congress usually imposes a limitation on the amount of obligations that may be incurred in a given fiscal year from assessments collected from the FCS and from Farmer Mac.

Additional information about FCA's financial condition for FYs 2006 and 2005 is included in the following subsections. Fiscal year data summaries of the various asset, liability, and net position accounts are also provided for comparative purposes.

FCA's Assets, Liabilities, and Net Position

The Balance Sheet displayed on page 56 of this report presents the financial condition of FCA as of the 2006 and 2005 fiscal year-ends. It presents the value of FCA's assets and money FCA owes to the public or other Government agencies. The difference between the assets and liabilities represents FCA's net position. Although the total liabilities increased by only 1.9 percent, there were significant increases in the Agency's total assets and net position for FY 2006. The assets increased by 17.1 percent, which can be attributed to the increases in the fund balance, investments, and accounts receivable. However, the percentage increases in these areas were offset by the large decrease in the value of property owned by FCA. As a result of FCA's revised policy to increase the property capitalization threshold to $50,000 for individual purchases, property purchases that would have been established as assets were expensed; and with the normal depreciation of property that was already on hand, the Agency's property value decreased by 59.4 percent. The net position increased by 26.4 percent. This year, the Agency's total revenue exceeded its cost, which represents an improvement in the Agency's net cost of operations. For additional information on the net cost of operations, see the Performance and Financial Results section located on page 16. More detailed

Table 1. Composition of Assets

Fiscal Year	Fund Balance with Treasury	Investments	Accounts Receivable and Prepayments	Property and Equipment	Total
2006	$1,782,919	$22,518,887	$601,934	$386,381	$25,290,121
2005	$1,195,445	$18,980,498	$464,128	$950,965	$21,591,036

information about the Agency's assets, liabilities, net position, and funding for FY 2006 is included in the following paragraphs.

Composition of Assets

FCA's assets have increased from the accumulation of cash from revenues generated as a result of improvements in the Agency's net cost. As of September 30, 2006, FCA total assets increased $3,699,085, or 17.1 percent, from the previous year to $25,290,121. See Table 1 for the composition of FCA's assets. Total assets have increased because of growth in FCA's cash, investments, and accounts receivable that mitigated the approximate $565,000 decline in FCA's value of depreciated property and equipment. In FY 2006, FCA updated the criteria for capitalizing property, equipment, and software to conform to the industry's best practices and adjusted the accounting of the applicable assets to comply. The change in the capitalization criteria was also in line with the policy of FCA's financial service provider, the Bureau of the Public Debt. The implementation of the new criteria reduced the FY 2005 gross value of FCA's capitalized property and accumulated depreciation from $3,388,093 to $1,652,441 and from $2,437,128 to $1,266,060, respectively.

During 2006, the revenues from the assessment of FCS institutions, reimbursable activities, and interest from the Agency's investment in U.S. Treasury securities grew and exceeded the Agency's costs and cash disbursements. As a result, cash and investments increased approximately $4.1 million during the 12 months ended September 30, 2006. In addition, accounts receivable net of prepayments increased approximately $138,000. The increase in accounts receivable results from the billing of approximately $182,000 for additional reimbursable services completed for Government agencies in 2006 that was not collected at year-end. The increase in the accounts receivable offsets the decrease in the amount of the prepayments that were made by the Agency during the year, and as reported in the previous year's statements.

The increase in cash, investments, and accounts receivable improves the Agency's ability to meet financial obligations without having to rely on other sources of cash that are available under the statutory authority of the Agency during times of possible adversity. Cash and investments totaled 292.5 percent of the Agency's total liabilities and 96.1 percent of total assets as of September 30, 2006. The Agency continues to review and develop strategies to meet FCA's liquidity demands and ensure an adequate reserve for use through possible adversity. Available cash is also invested to generate additional income to offset the cost to FCS institutions in the funding of the Agency's operations.

Composition of Liabilities

FCA has maintained the same level of total liabilities as that of last year, which has contributed to the strengthening of the Agency's financial position. FCA's total liabilities have increased 1.9 percent, or $155,798, to $8,309,054 as of September 30, 2006. The growth in total liabilities in 2006 is attributed to increases in deferred revenue and advances, workers' compensation, and the accrual of employees' salaries and benefits. The decrease in the Agency's accounts payable partially offset the increase in FCA's liabilities. Accounts payable decreased approximately $143,000 because of a decline in the amount of FCA's current year assessment refunds owed to some FCS service corporations and a reduction in the amount of unpaid employee travel vouchers accrued at year-end.
The liabilities for deferred revenue and advances are primarily composed of next year's assessment

Table 2. Composition of Liabilities

Fiscal Year	Accounts Payable	Accrued Liabilities (Payroll and Benefits)	Employer Contributions and Taxes Payable	Workers' Compensation (Funded and Unfunded)	Deferred Revenue and Advances	Total
2006	$473,739	$3,911,313	$269,345	$1,205,892	$2,448,765	$8,309,054
2005	$616,546	$3,834,720	$229,174	$1,183,429	$2,289,388	$8,153,257

Table 3. Composition of Net Position

Fiscal Year	Adjusted Beginning Balance	Imputed Costs	Net Cost of Operations (+/-)	Ending Balance
2006	$13,437,779	$3,396,854	$146,434	$16,981,067
2005	$12,513,116	$3,747,614	($2,822,951)	$13,437,779

fees received from FCS institutions prior to year-end. According to the FCA regulation, FCA annually provides FCS institutions notice of their next year's annual assessment on September 15 of each year. Some FCS institutions choose to prepay their assessment upon receipt of the notice and before the payments are due at the beginning of the next fiscal year, October 1. In 2006, FCA received approximately $2.4 million in prepaid assessment fees from FCS institutions. The amount of prepaid assessments increased approximately $159,000, or 7.0 percent, from the previous year. The increase in 2006 follows a 31.3 percent increase in prepaid assessments received in 2005.

The remaining increases in the Agency's liabilities have resulted from the raise in employees' salaries and benefits and the estimate of the Agency's actuarial liability. The liability for accrued employees' salaries and benefits rose in 2006 due to increases of approximately $65,000 in employees' accrued leave and $12,000 in the Agency's payroll accrual compared with the previous year. The liability for payroll and benefits includes approximately $2.9 million of accrued leave in 2006 compared with $2.8 million in 2005. FCA employees accrue leave that is payable to them upon their resignation or retirement from the Agency. The actuarial liability and the liability for post-employment compensation under the Federal Employees Compensation Act (FECA) increased slightly due to changes in the estimates for compensation and medical benefits payable to employees with disabilities resulting from work-related injuries. The FECA and actuarial liabilities increased $22,463 to $1.2 million in 2006. This increase follows a $219,686 decrease in the amounts from 2004 to 2005. The actuarial liability is computed annually using a model provided by the U.S. Department of Labor. The increase in the actuarial may be attributed to an increase in medical payments covered during FY 2006.

Composition of Net Position

FCA's net position has increased significantly with the significant rise in assets, coupled with the almost unchanged amount of Agency liabilities. Table 3 shows that the net position totaled $16,981,067 for September 30, 2006. The net position increased $3,543,288 and $935,339 in years 2006 and 2005, respectively. The increases in the net position have resulted from significant increases in FCA's revenue while the Agency has maintained cost at almost the same level for the reported 2 years. Revenues from FCA's assessment of the FCS, reimbursable activity, and investments increased $3,097,160 in 2006 and $1,116,513 in 2005. The net cost of operations improved by $2,969,385 and $1,112,654 for each period, respectively, and contributed to the increase in FCA's cash and investments, which has strengthened the net position. Additional information related to FCA's revenue and cost is provided in the subsection on the Performance and Financial Results located on page 16.

Table 4. Available Funding

Funding and Funding Sources	2006	2005
Assessments (current year)	$40,500,000	$39,400,000
Assessments (carryover from prior years)	3,750,000	2,936,716
Reimbursable activity	1,821,568	1,272,885
Interest from investments	1,023,897	634,148
Total	**$47,095,465**	**$44,243,749**

Table 5. Funds Used by Major Budget Category

Budget Category	FY 2006	Percent of Total	FY 2005	Percent of Total
Personnel compensation and benefits	$32,854,075	83.5%	$33,033,087	84.6%
Travel and transportation of persons	2,183,176	5.6%	1,745,296	4.5%
Contractual services	3,089,645	7.8%	2,894,598	7.4%
Property and equipment	183,987	0.5%	265,232	0.7%
Other	1,042,113	2.6%	1,089,029	2.8%
Total	**$39,352,996**	**100.0%**	**$39,027,242**	**100.0%**

The composition of the Agency's net position provides support for the continuance of operations. The net position is primarily composed of cash and investments in U.S. Treasury securities that can be used during unforeseen emergencies without the Agency's having to rely on other sources of cash allowed under the Farm Credit Act, of 1971, as amended. As of September 30, 2006, the net position was 69.9 percent of the Agency's cash and investment balances. In addition, the net position is adequate to cover the Agency's liabilities. The net position is 204.4 percent of the Agency's total liabilities.

FCA's Funding and Fund Sources

FCA maintains a revolving fund from moneys obtained primarily from assessment fees paid by FCS institutions, including Farmer Mac, and from reimbursable services to other Government agencies and the National Cooperative Bank, which the U.S. Congress has commissioned the Agency to annually examine. In addition, FCA earns interest revenue on investments with the U.S. Department of Treasury, which the Agency makes with available cash. Table 4 of this financial report depicts the funding that was available or collected by FCA for FYs 2006 and 2005. The Agency's available funding has increased from the previous year. For 2006, funding and fund sources totaled $47,095,465, compared with $44,243,749 for 2005. The rise in 2006 funding primarily results from increases of $1.1 million and $813,284 in assessment fees from FCS institutions and carryover from prior periods. In addition, the Agency's available funding has benefited from increases in interest revenue from FCA's investments in U.S. Treasury securities and agreements with other Government agencies to provide services. Interest revenue improved approximately $390,000 from the significant rise in interest rates on U.S. Treasury securities from the previous 2 years. Funding from interagency agreements increased approximately $549,000 in 2006 for added services to perform reviews of the U.S. Department of Agriculture and the Small Business Administration loan programs, and to assist the USDA in an international program to form a cooperative farm credit system in a specific foreign country.

FCA performed the Agency's program goals and objectives well within the Board's approved budget and used less of the available funds in 2006 than the previous year. FCA used $39,352,996, or approximately 83.6 percent, of the amount of funds available in 2006, compared with $39,027,242, or 88.2 percent, used in 2005. The amount of funds remaining after the Agency's obligations totaled approximately $7.7 million in 2006, $2.5 million more than the amount remaining in the previous year. Employees' salaries and benefits represent the most significant use of funds. In 2006, funds used for salaries and benefits decreased approximately $179,000 because of a faster than planned reduction in staff due to attrition. The reduction in staff in 2006 partially offsets the costs for employees' annual pay-for-performance, the increase in travel, and the Agency's increased use of contract services implemented under the 5-year strategic plan. These costs were also partially offset by reductions in the funds used for purchases of property and equipment, and other miscellaneous items (e.g., monthly utilities, postage).

The remaining balance of funds for the year is used as a funding source for the Agency. The remaining balance of funds from FCS assessments increases the Agency's assessment carryover, which is used as a source of funding for the Agency's budget and to reduce the annual assessment of FCS institutions. Interest revenues from FCA investments fund the Agency's reserve prescribed under the FCA regulations and according to the FCA Board Interest Reserve Strategy. The fund reserve is used to cover unbudgeted expenses from material unexpected public mission or safety and soundness issues. Unused funds for reimbursable activity terminate with the expiration of the agreements for services with the respective Government agencies.

Performance and Financial Results

The following is a description of FCA's financial condition and the results of its efforts to meet its performance goals and objectives for the fiscal years ended September 30, 2006, and September 30, 2005. This information should be read in conjunction with the financial statements, notes to the financial statements, and other sections of the Performance and Accountability Report.

FCA continues to perform its mission to ensure that the institutions of the FCS operate in a safe and sound manner and provide a dependable source of credit and related financial services to U.S. agriculture and rural areas. Furthermore, we provide reimbursable services to other Government agencies and nongovernment entities. The business growth and sound condition of FCS institutions and the Agency's accomplishment of the goals and objectives of the strategic plan confirm the quality of FCA products, services, and operations.

The FCA Board and management have implemented the strategy to annually review the Agency's 5-year strategic plan to update expectations for FCA's operations with the challenges faced by the FCS to remain competitive in a changing agricultural and rural economy. As part of our strategic planning, we have developed human capital and information resource plans to address FCA staffing and technological needs to gain efficiency and remain effective.

Costs have been maintained through sound business planning and efficient use of resources. The annual assessment of FCS institutions, which is the primary source of funding for FCA, has increased almost $1.2 million, or 3.0 percent, in 2006 and $1 million, or 2.6 percent, in 2005 after a $1.7 million, or 4.6 percent increase, in 2004. The assessment remained virtually the same for the 3 years before 2004.

FCA program costs increased slightly with the changes implemented in the strategic plan. The total cost of FCA's programs for FY 2006 is $42,948,683, compared with $42,820,908 for FY 2005. Employee salaries and benefits represent the Agency's most significant cost. For 2006, employee compensation totals $31,631,990, or 73.6 percent, of total cost. These costs decreased $765,433 from 2005 because of staff attrition. The decrease in salaries and benefits, accompanied by decreases in equipment depreciation and imputed cost for building rent and Federal employee pensions, partially offset the increases from travel and contractual services.

FCA's ability to maintain effective operations will require our staff to obtain new skill sets, appropriate to meeting regulatory demands for an evolving FCS and the overcoming of a significant loss of expertise due to high attrition. FCA strategic studies completed in 2005 concluded that the FCS, including Farmer Mac, will evolve in the next 5 years to fewer—but much larger and more complex—institutions. During this period, the FCS is expected to maintain a healthy loan growth while reducing the number of its institutions by a third. Greater pressure will be placed on FCA examiners and analysts to have new skill sets that are appropriate for the changing agricultural and rural marketplace.

One of the challenges FCA faces in meeting its regulatory responsibilities is the attrition of FCA staff: by 2011, approximately 60 percent of the staff will be eligible to retire. In 2005, the FCA implemented various organizational and functional changes with examination and regulatory processes to accommodate anticipated FCS changes and to better utilize staff skill sets for meeting demands to examine and regulate FCS risks. Further, FCA adopted in 2006 a comprehensive Human Capital Plan that addresses staff resource needs through the recruitment, mentoring, training, and promotion of staff; the plan also incorporates career intern programs to attract promising new employees.

We have maintained competitive employee compensation by periodically performing compensation studies in accordance with the Financial Institution Reform, Recovery, and Enforcement Act of 1989 to keep FCA salaries comparable with salaries of other Federal financial institution regulators. We believe our plans for staff resources and compensation should provide adequate means for the Agency to continue to perform its mission to provide the FCS with effective regulation and oversight.

Earned revenues increased in 2006 and mitigated the increase in the Agency's program cost. For 2006, earned revenues totaled $43,095,117, up $3,097,160 from the previous year. Earnings are generated by the assessment fees paid by FCS institutions, including Farmer Mac; the reimbursable services provided to non-FCS entities; and interest income from the investment of Agency cash in U.S. Treasury securities. The growth in earned revenue resulted from the increased assessment of FCS institutions and a higher rate of return from the Agency's investment of funds in U.S. Treasury securities. The increased revenue improved the net cost of FCA programs for the 12 months ended September 30, 2006. The net cost of FCA programs improved $2,969,385 to a negative $146,434 from the same period ended September 30, 2005.

The Agency draws almost all of its cash from FCS assessments, reimbursable activity, and interest earned on invested funds. FCA earned revenue exceeded its obligations and increased its cash and investments from 2005 to 2006. As of September 30, 2006, cash and investments totaled $24,301,806, compared with $20,175,943 for September 30, 2005. Cash received from assessments and reimbursable activity in any given year is based on FCA Board-approved budgets that are expected to be adequate to fund operations for that year. FCA utilizes the cash carryover from prior years to partially fund the Agency's annual budget and reduce the assessment of FCS banks and associations. In addition, FCA maintains an interest reserve from interest earned from investments for unbudgeted expenses arising from material unexpected FCS policy or safety and soundness issues. The U.S. Congress has imposed a limitation on the amount of administrative expenses that can be obligated from FCS assessments in the FCA Board-approved budgets.

Public Mission Program

The FCA is investing more of its resources in its policymaking and regulatory functions in order to ensure that the FCS fulfills its public mission as mandated by the U.S. Congress. As a result, the Agency improved the performance of this goal from the previous year. For fiscal period ended September 30, 2006, program cost for public mission is $8,274,686, representing a 16.1 percent increase (or an increase of $1,145,734) from the same period the previous year. Program cost for the public mission is approximately 19.2 percent of FCA's total cost because of the emphasis on developing regulations and policy initiatives that encourage FCS institutions, including Farmer Mac, to develop credit and financial products to better serve the public and to facilitate the flow of funds to agriculture and rural areas.

In addition, the Agency maintained its focus in 2006 on improving FCS institution lending to YBS farmers and ranchers. The Agency met or exceeded all of its performance measures for completing rulemaking and corporate activity projects. FCA continues to develop new products and services for identifying and monitoring FCS risk. The Agency also continues to invite the public to identify ways to reduce the regulatory burden on the FCS. As a result of public input, the Board has approved the elimination of some outdated and unnecessary regulations. FCA's initiatives to encourage FCS institutions to use loan participations and similar-entity lending authorities have improved the System's risk management and its funding of agriculture and related businesses loans. Alliances with commercial banks have provided needed services to rural areas. FCA's corporate activity has declined; the FCS has a relatively small number of institutions remaining after the significant number of mergers since 2000.

Safety and Soundness Program

The regulatory examination and supervision of the safety and soundness of the FCS represent the most significant part of FCA program costs. We have maintained an effective examination and oversight program. FCA has exceeded its goal and measures to ensure the safety and soundness of FCS institutions, including Farmer Mac. Program cost for the examination and supervision of the FCS decreased $1,894,875 to $31,687,731, or 73.5 percent of FCA's total costs in 2006. All FCS institutions, including Farmer Mac, remain fundamentally sound, with no institution under any FCA supervisory or enforcement action. In support of our commitment to the examination and oversight of FCS risk, we issued an Agency Regulatory Philosophy Statement (PS-59) for risk-based supervision of FCS institutions.

In addition, the Office of Examination reorganized to better utilize its available resources and employee skill sets, and to enhance risk oversight programs. FCA provides conclusions and makes recommendations where appropriate to institution boards of directors on their institutions' risks and regulatory compliance. Agency examiners provide feedback through written communication and also by meeting directly with senior management and boards of FCS institutions. To maintain its quality of products, services, and operations, FCA continues to incur significant costs in the recruitment and training of staff through its Pre-commissioned Examiner Program; these recruiting and training efforts are necessary to meet human resource needs because a significant number of FCA employees are expected to retire over the next 4 or 5 years. FCA maintains effective early warning and risk identification systems and oversight programs to identify and address emerging risk and related issues in FCS institutions.

Other Activity

Other activity represents the examination and oversight of the National Cooperative Bank (NCB) and the performance of reimbursable services for the Small Business Administration (SBA), USDA, and the Farm Credit System Insurance Corporation. Program cost for other activity increased $876,916 to $2,986,266 in 2006. The increase in cost compares unfavorably with earned revenues and resulted in an increase in the net costs of other activity. Earned revenue for other activity totaled $1,518,981 for 2006, compared with $1,620,522 for 2005.

Reimbursable services provided by FCA primarily include examining the NCB, which we are required by the U.S. Congress to do, and examining institutions affiliated with the SBA and USDA, which we have agreed to do through interagency agreements. The FCA performs an annual examination of the NCB as directed by Congress. FCA has performed examinations under interagency agreements of affiliated institutions for the SBA since 1999 and for the USDA since 2001. The costs for providing reimbursable services represented approximately 6.9 percent of FCA's total costs in 2006, compared with 5.2 percent in both 2005 and 2004.

Limitations of the Financial Statements

The principal financial statements have been prepared to report the financial position and results of operations of FCA, pursuant to the requirements of 31 U.S.C. 3515(b).

While the statements have been prepared from the books and records of the entity in accordance with U.S. generally accepted accounting principles (GAAP) for Federal entities and the formats prescribed by the Office of Management and Budget, the statements are in addition to the financial reports used to monitor and control budgetary resources that are prepared from the same books and records.

The statements should be read with the realization that they are for a component of the U.S. Government, a sovereign entity.

President's Management Agenda

The President's Management Agenda represents the President's goal to reform the Federal Government and make it more citizen centered, results oriented, and market based. Five Government-wide initiatives have been identified to improve performance in the following areas:

1. strategic management of human capital
2. improved financial performance
3. expanded electronic government
4. budget and performance integration
5. competitive sourcing

FCA has responded to these initiatives by incorporating them into a goal within the Agency's Strategic Plan. As part of the FCA Strategic Plan, the Agency has adopted the following approaches to implement the President's Management Agenda.

Strategic Management of Human Capital

FCA will link the Agency's human capital needs and strategies to its organizational mission, vision, core values, goals, and objectives. As part of our Human Capital Plan, we will use strategic workforce planning and flexible tools to recruit, retain, and reward employees and to continue to develop a high-performing workforce. This will give the Agency more flexibility to accomplish its mission efficiently.

Improved Financial Performance

The Agency will continue to invest significant resources in maintaining a financial management system that can produce accurate, reliable, and timely information to support policy, budget, and operating decisions. The system will facilitate consistent and comparable trend analysis over time and produce better performance measurements. For the past 12 years, FCA has received unqualified opinions on its annual financial statements, and that continues to be our goal.

Expanded Electronic Government

FCA continues to support e-regulation, e-signatures, and e-procurement. We will continue to expand our ability to collect information electronically from the FCS over the Internet, and we will expand the information that is available to our constituents on our Web site. We will focus on compliance with Section 508 of the Rehabilitation Act of 1973, as amended, to ensure that our electronic and information technology is accessible to people with disabilities. These and other initiatives will enable the public to have greater access and to participate more fully in the Agency's decision-making process.

Budget and Performance Integration

The Agency will continue to include high-quality outcome measures, to monitor the performance of programs, and to integrate the presentation with associated costs. This information allows program costs and benefits to be clearly identified. This will enable the Agency to enhance its control over resources used and better establish accountability for results.

Competitive Sourcing

FCA recognizes that competition promotes innovation, efficiency, and greater effectiveness. We will continue to determine our "core competencies" and then decide when to build internal capacity and when to contract for services from the private sector. This process will encourage the Agency to focus on continual improvement and to remove roadblocks to greater efficiency.

FCA is striving to become more results oriented through efficiency and accountability. We have set clear goals and implemented action plans, and we are following through on those plans. For more detailed information on FCA's accomplishments under each of the President's Management Agenda initiatives, please review Goal 3 in the FCA Performance Report on page 38.

Systems, Controls, and Legal Compliance

Federal agencies are required to comply with a wide range of laws and regulations, to develop and maintain effective internal controls, and to maintain systems that generate timely, accurate, and useful information with which to make informed decisions. This section provides information on FCA's financial management system and its compliance with the following acts:

- The Inspector General Act
- The Federal Managers' Financial Integrity Act
- The Federal Financial Management Improvement Act
- The Prompt Payment Act
- The Debt Collection Improvement Act

FCA's Financial Management System

In compliance with the Financial Management Line of Business initiative to improve the cost, quality, and performance of financial management systems by using shared services, FCA partnered with the Bureau of the Public Debt's Administrative Resource Center to provide the Agency with several financial management services. As a result of this partnership, FCA uses Oracle Federal Financials as its financial management system of record. Oracle Federal Financials is a commercial, off-the-shelf software package that is certified by the Chief Financial Officers Council to meet Federal Government accounting needs. It is Web-based and interfaces with other systems to provide for the integration of other key activities that are also used by FCA, such as e-payroll, procurement, purchase cards, e-travel, and Federal investments. The transition of these services to the Bureau of the Public Debt also ensures that FCA obtains the best value while maintaining its high standard of financial management practices. FCA's transition of its financial services to the Bureau of the Public Debt was effective on April 1, 2006.

Inspector General Act

The Inspector General Act of 1978, as amended, requires semiannual reporting on Inspector General audits and related activities, as well as agency follow-up. The Inspector General's two semiannual reports covering FY 2006 are available at www.fca.gov/oig. Information about recommendations made in audits and inspections by the Office of the Inspector General (OIG), as well as management's progress in taking corrective action, is summarized below. The OIG continues to report actions required to correct audit or inspection findings as "agreed-upon actions" whenever the OIG and management have agreed on a mutually acceptable way to resolve a problem identified during reviews. The OIG's objective is to recognize management's preferred method of correcting problems whenever the approach is reasonable. A recommendation often includes these agreed-upon actions.

Summary of Audit and Inspection Recommendations

October 1, 2005, to September 30, 2006	
Recommendations uncorrected as of October 1, 2005	18
Recommendations made during FY 2006	4
Recommendations corrected during FY 2006	16
Open recommendations at September 30, 2006	6
Recommendations open more than 1 year	2

Summary of Audit Activities for FY 2006

At the beginning of FY 2006, there were 18 unimplemented recommendations.

- Two were from the audit of Performance Budgeting issued on March 23, 2001.
- Two were from the audit on the Office of the Chief Financial Officer issued on January 24, 2002.
- Four were from the audit of the Loan Account Reporting System issued August 28, 2003.
- One was from the audit of Human Capital: Job Classification issued June 29, 2004.
- Two were from the audit Call Report Data Verification issued on February 3, 2005.
- Two were from the audit Performance Measures and Internal Controls issued on July 1, 2005.
- Three were from the inspection of FCA Board Policies issued on September 15, 2003.
- Two were from the inspection of Project Management issued September 9, 2004.

OIG issued the audit of the Financial Statement for 2005 and the results of a review under the Federal Information Security Management Act. One additional audit, Records Management and Preservation of Institutional Knowledge, was issued on February 21, 2006, and had four agreed-upon actions.

During this reporting period, management worked with OIG to close 16 recommendations. At the end of the FY 2006 reporting period, there were two recommendations and four agreed-upon actions remaining open. Four agreed-upon actions were from the audit of Records Management and Preservation of Institutional Knowledge, issued on February 21, 2006; and two recommendations were from the audit Performance Measures and Internal Controls, issued on July 1, 2005.

Federal Managers' Financial Integrity Act

The Federal Managers' Financial Integrity Act (FMFIA) requires agencies to establish management controls over their programs and financial systems to provide reasonable assurance that the integrity of Federal programs and operations is protected. As a result, FCA holds managers accountable for the performance of their programs through the use of management controls. Annually, managers evaluate the adequacy of the management controls surrounding their activities to determine whether they conform to the principles and standards established by the Office of Management and Budget and the Government Accountability Office. The results of these management control evaluations are used to determine whether there are any problems to be reported as material weaknesses. As reported in the Chairman's statement for FY 2005, the Agency has identified no material weakness or financial system nonconformance that places the overall control system at risk.

Federal Financial Management Improvement Act

The Federal Financial Management Improvement Act (FFMIA) requires certain executive branch departments and agencies to report on their substantial compliance with Federal financial management system requirements, Federal accounting standards, and the U.S. Government Standard General Ledger. Although FCA is not one of the agencies required to report under the FFMIA, FCA was in substantial compliance with these system requirements for FY 2006.

Prompt Payment Act

The Prompt Payment Act generally requires agencies to pay vendors 30 days after receipt of a valid invoice for goods and services ordered and delivered. During FY 2006, FCA and the Bureau of the Public Debt paid most of the bills within the time requirement. However, because of some invoice approval delays, interest penalty payments were made in the amount of $128. Payments are made by electronic funds transfer through the use of the Secure Payment System.

Debt Collection Improvement Act

The Debt Collection Improvement Act (DCIA) prescribes standards for the administrative collection, compromise, suspension, and termination of Federal agency collection actions. It also prescribes policy for referral of agency uncollectible debts to the proper Federal agency for follow-up collection and litigation. Although the DCIA has no material effect on the FCA since it operates with virtually no delinquent debt, the Agency sometimes does transfer debts more than 180 days old to Treasury for cross-servicing.

Statement of Assurance

The Farm Credit Administration management is responsible for establishing and maintaining effective internal control and financial management systems that meet the objectives of the Federal Managers' Financial Integrity Act. The FCA conducted its assessment of the effectiveness of internal control over the effectiveness and efficiency of operations and compliance with applicable laws and regulations in accordance with OMB Circular A-123, Management's Responsibility for Internal Control.

Based on the results of this evaluation, the Agency can provide reasonable assurance that its internal control over the effectiveness and efficiency of operations and compliance with applicable laws and regulations as of September 30, 2006, was operating effectively and that no material weaknesses were found in the design or operation of the internal control.

In addition, the FCA conducted its assessment of the effectiveness of internal control over financial reporting, which includes safeguarding the assets and ensuring compliance with applicable laws and regulations, in accordance with the requirements of Appendix A of OMB Circular A-123. Based on the results of this evaluation, the Agency can provide reasonable assurance that its internal control over financial reporting as of June 30, 2006, was operating effectively and that no material weaknesses were found in the design or operation of the internal control over financial reporting.

Nancy C. Pellett

Nancy C. Pellett
Chairman and Chief Executive Officer
FARM CREDIT ADMINISTRATION

September 30, 2006

Program Performance

Farm Credit Administration Performance Report

The Farm Credit Administration (FCA or Agency) is an independent Federal agency responsible for regulating and examining the Farm Credit System (FCS or System) and the Federal Agricultural Mortgage Corporation (Farmer Mac). Both of these organizations are Government-sponsored enterprises (GSEs) that serve agriculture and rural America.

Our mission is to ensure that a safe, sound, and dependable source of credit and related services is made available through the FCS institutions for agriculture and rural America. Our vision is to maintain a flexible regulatory environment that will ensure the System meets current and future rural credit needs in a safe and sound manner.

We fulfill the Agency's mission by performing two principal program activities: (1) issuing regulations and implementing public policy, and (2) identifying risk and taking corrective action. Consistent with our mission and program activities, the FCA Board has adopted three strategic goals for fiscal years 2004-2009. These goals, which remained the primary focus of the Agency's activities in FY 2006, are as follows:

1. Ensure the Farm Credit System and Farmer Mac fulfill their public mission for agriculture and rural areas.

2. Evaluate risk and provide timely and proactive oversight to ensure the safety and soundness of the Farm Credit System and Farmer Mac.

3. Implement the President's Management Agenda.

To further clarify what we expect to accomplish for the public good, the FCA's strategic plan also contains "desired outcomes" for each goal, as well as 24 in-depth descriptions of the "means and strategies" that FCA uses to accomplish the goals and achieve the desired outcomes and results. In addition, 18 performance measures with associated "targets" show the extent of the Agency's success in accomplishing each aspect of its mission to regulate the System and ensure safety and soundness.

FCA's strategic plan provides that it shall be reviewed annually to keep it updated to reflect expectations for the ensuing short- and long-term operating environments. Consequently, the FCA Board updated the means and strategies and several performance measures in January 2005 to better reflect current expectations for Agency operations. Expectations set when the plan was adopted in 2003 have changed as a result of recent changes in the operating environment. However, the substance and direction of the plan remain focused on improving effectiveness and efficiency; minimizing the cost burden on FCS borrowers; and helping ensure a safe, sound, and dependable source of credit and financially related services for agriculture and rural America. Based on the results achieved, we believe the Agency's two program activities and our initiatives were effective in helping to meet each of the three strategic goals described below.

Strategic Goals and Outcomes

Goal 1—Ensure the Farm Credit System and Farmer Mac fulfill their public mission for agriculture and rural areas.

The primary purpose of Goal 1 is to maximize the ability of the FCS and Farmer Mac to fulfill their purposes and meet their public missions, as defined by Congress in the Farm Credit Act of 1971, as amended, (Act). The Agency established

12 means and strategies to accomplish this goal, and it defined six performance measures to evaluate the Agency's progress and success.

The means and strategies refer to initiatives that encourage the FCS to establish outreach programs, as well as credit and other financially related products, to better serve chartered territories, ensure equitable treatment of borrowers and applicants, and encourage cooperation among System and non-System lenders to facilitate the flow of funds to agriculture and rural areas.

The Agency also maintained its focus on activities that it believed would help improve funding to new entrants into agriculture, defined as young, beginning, and small (YBS) farmers and ranchers. The importance of this initiative has its roots in the need for the FCS to help cultivate the next generation of farmers and ranchers who will produce food and fiber, and provide the processing and marketing services needed for the nation's agriculture in the 21st century.

FCA recognized that for agriculture to flourish, it is equally important to ensure that our nation's cooperatives and farm-related businesses have access to a dependable source of credit and financially related services so that they may successfully process and market the products of agriculture. The Agency believes that its regulatory supervision of the FCS must be flexible yet, in accordance with the Act, ensure that the benefits Congress intended the System to provide to America's agricultural and rural areas continue without disruption. The means and strategies embodied in the FCA's strategic plan embrace these concepts so that all of the public can benefit as Congress intended when it established the FCS and Farmer Mac.

The following discussion provides additional information on the activities the Agency undertook to accomplish Goal 1.

Means and Strategy #1—Ensure FCS lenders and Farmer Mac fulfill their public mission by reaching out to all potential customers.

FCA examinations continue to evaluate whether System lenders are fulfilling their public mission by reaching out to all potential customers. The examinations in FY 2006 disclosed that the FCS institutions have maintained effective business and marketing plans and effective credit delivery programs. System lending continues to reflect quality loan growth.

YBS farmer and rancher programs are also routinely evaluated, relative to the demographics of chartered territories, to assess trends in lending to YBS farmers and ranchers and to assess the System's efforts to provide financial or business management assistance and outreach to YBS farmers and ranchers. The results achieved through these initiatives have been fruitful. The System has made steady progress toward meeting the needs of YBS farmers and ranchers, as well as other borrowers.

Through the Office of Secondary Market Oversight (OSMO), FCA evaluates Farmer Mac's mission accomplishments. Farmer Mac's customer base includes financial institutions and other lenders that seek a secondary market for their agriculture loan portfolios. The evaluation of Farmer Mac's performance in reaching out to all potential customers and creating easy access to its services is a component of OSMO's oversight activities. Farmer Mac's annual mission report is submitted to OSMO at the end of each calendar year. The report includes data on Farmer Mac's participation in Federal and State guarantee programs and the geographic distribution of Farmer Mac's book of business. In addition, the report has been expanded to include data on small and family farms, which Farmer Mac is required by statute to promote and encourage.

As a part of the Federal Government, FCA has a principal responsibility to ensure that the System it regulates serves the public good. To fulfill this responsibility, FCA maintains a program of responding to and investigating, as needed, all issues raised by applicants and borrowers of the System and other members of the public regarding the activities of FCS institutions and Farmer Mac. During the reporting period from July 1, 2005, through June 30, 2006, the Agency addressed and responded to 16 borrower inquiries. Our investigations found no violations of law or regulation on the part of the FCS institutions or Farmer Mac. In general, we concluded the investigations by providing additional information to the inquirers and encouraging FCS institutions to follow up with the inquirers to resolve the issues raised. Although no overall conclusions were drawn on mission accomplishment from the relative inactivity of borrower inquiries, this program did not reveal any information or evidence to suggest that the System's direct-lender institutions were not adequately fulfilling their mission.

Means and Strategy #2—Ensure all eligible customers have access and are treated equitably.

In addition to the regulations that govern the rights of applicants and borrowers, FCA's program activities include processes that review borrower inquiries and complaints about the loan-granting process and provide for investigations on any allegations of discrimination. Although FCA examinations have periodically identified issues concerning compliance with borrower-rights regulations, the examiners have not discovered any discriminatory pattern or practice, any overt or deliberate discrimination against any eligible customers, or an unwillingness of FCS institutions to serve their chartered territories. Based on examinations and investigations conducted, we concluded that eligible and creditworthy customers have access to the System and are treated fairly and equitably. We also note continued compliance with equal credit opportunity and equal housing laws. Although we have not found discriminatory patterns or practices or any overt discrimination against any eligible customers, our examinations found some technical violations of applicants' rights. Those violations were promptly corrected or addressed in follow-up plans by System institutions, as required by FCA examiners.

Means and Strategy #3—Enable the FCS and Farmer Mac to serve evolving customer needs by maintaining a flexible regulatory environment.

To the extent permitted by the Farm Credit Act of 1971, as amended, the Agency explores all avenues to be flexible in its interpretive guidance to System institutions. While examining compliance with borrower-eligibility and scope-of-lending rules, examiners work closely with the Office of the General Counsel and the Office of Regulatory Policy to ensure an appropriate and consistent interpretation of statutes and regulations. The interpretations derived are communicated to System institutions to enable them to better understand their lending authorities and therefore to more appropriately market their products and services to prospective eligible customers. FCA also publishes its semiannual Regulatory Performance Plan on its Web site so that the public is notified of upcoming regulatory actions and is provided the opportunity to participate in the regulatory process. In addition, the Agency improved its e-government program so that the public may make comments in electronic format and review comments from others on the FCA Web site.

The following are examples of FCA activities that helped the FCS serve its evolving needs and those of its borrowers within the provisions of the Farm Credit Act of 1971, as amended:

1. FCA circulated an informational memorandum to inform System institutions that the Agency considers all insurance services approved and administered by the Federal Crop Insurance Corporation and the Risk Management Agency to be already approved as multiple-peril-crop-insurance-related services.

2. The Agency circulated an informational memorandum to System institutions that provided clarification regarding the security requirements for long-term loans.

3. FCA initiated the development of a rule that would amend the processing and marketing regulations to change the ownership requirement for the eligibility of processing and marketing entities for FCS funding.

4. FCA approved several mission-related investment pilot programs to evaluate how System partnerships and investments could help increase the availability of funds to agriculture and rural America.

5. The FCA Board approved a final rule to amend the Agency's liquidity reserve requirements for System banks and to change the eligible investment limit from 30 percent to 35 percent of total outstanding loans. The intent of the final rule was to ensure that FCS banks have adequate liquidity and flexibility to provide credit in all economic conditions.

6. The Agency conducted a comprehensive study of the loan syndication market to determine what changes, if any, are needed in FCA's approach toward syndications and assignments.

7. Guidance was provided to Farmer Mac in applying the Risk-Based Capital Stress Test to new products developed to broaden customer service. The guidance enhances Farmer Mac's flexibility to serve customer needs through appropriate capitalization of risks.

8. OSMO provided guidance to Farmer Mac related to its liquidity portfolio. OSMO's guidance allowed a flexible approach to the regulatory requirements on eligible investment types.

Means and Strategy #4—Emphasize regulatory activities related to young, beginning, and small farmers, ranchers, and producers or harvesters of aquatic products.

Since 1998, the Agency has focused considerable resources on improving the implementation and controls of YBS programs and the reporting of YBS lending results. Using a risk-based approach, we continue to evaluate YBS programs and related trends in System lending activities based on the demographics of chartered territories and FCS efforts to provide financial or business management assistance and outreach to YBS farmers. All programs evaluated by examiners for the reporting period were considered satisfactory, with only a few weaknesses related to compliance with the YBS regulations. As a result of the examination and regulatory attention FCA has placed on YBS lending, the System has substantially increased its focus on, and improved its administration of, YBS programs, the quality of board reporting, and public disclosure. Borrowers have directly benefited: YBS loan volume and loan numbers have risen over the past 5 years. YBS initiatives remain a priority of the Agency, and FCA will continue to provide considerable oversight to the System's activities and programs related to YBS farmers, ranchers, and producers and harvesters of aquatic products.

Means and Strategy #5—Emphasize Farmer Mac's obligation to promote and encourage the inclusion of qualified loans for small farms and family farmers in the agricultural mortgage secondary market.

The statute requires Farmer Mac to promote and encourage the inclusion of small and family farms in its programs. New reporting requirements developed by OSMO for Farmer Mac monitor the statutory requirements for nondiscrimination against small borrowers and lenders, and support Farmer Mac's work with lenders to meet the credit needs of small and family farms. OSMO encouraged Farmer Mac to work with lenders to meet the credit needs of small and family farms by providing timely feedback on various issues, including loan eligibility on prospective new lines of business. Farmer Mac responded by providing preferential terms to commercial banks in rural areas through its recently established marketing alliance with the American Bankers Association. In this way, Farmer Mac enhanced the service it provides to the market that serves small and family farms.

Means and Strategy #6—Encourage the System and Farmer Mac to use guarantee programs and work with Federal and State agencies that offer such programs to streamline processes.

As a part of the evaluation of YBS programs, the Agency continues to assess the extent to which FCS institutions use guarantee programs. When needed, FCA encourages the FCS institutions to work with Federal and State agencies that offer such programs, including qualifying for the U.S. Department of Agriculture's Farm Service Agency's "preferred lender" status. System use of Federal and State guarantees has been growing as a percentage of the System's overall portfolio. Agency staff members are mindful of how institutions can and should use guarantees as an effective risk management tool that helps borrowers who need this assistance. Loan guarantees are also encouraged for YBS borrowers with limited financial capacity and existing borrowers who are temporarily experiencing financial difficulties. In addition, Farmer Mac provides secondary market liquidity to Federal and State guarantee programs through its Farmer Mac II program. In 2006, FCA has overseen the implementation of new regulations that provide more flexible treatment of Government-guaranteed loans in Farmer Mac's liquidity portfolio in recognition of the marketability of such loans.

Means and Strategy #7—Encourage all FCS institutions and Farmer Mac to continue to include a discussion in annual reports of how they are meeting their public mission.

FCA's routine examinations of institution business plans and shareholder and public disclosures include a review of how the institutions meet their public mission as GSEs. The manner in which each institution is meeting its public mission is evaluated and, as needed, addressed with institution officials in the examination oversight process.

In its quarterly and annual reports on Forms 10-Q and 10-K, respectively, Farmer Mac discusses its congressional and public mission. It describes how its innovative products are serving the financing needs of rural America.

Means and Strategy #8—Enable the agricultural GSEs to restructure themselves to best serve their customers and rural America.

While the pace of institution mergers and restructures remained slow, Agency staff continue to analyze and approve periodic requests by institutions to restructure to more effectively and efficiently serve their chartered territories in rural America.

In the past, the most significant change in System structure was the creation of a parent-subsidiary structure in which an agricultural credit association (ACA) serves as the parent institution and a production credit association (PCA) and a Federal land credit association (FLCA) serve as subsidiaries. This structure allows ACAs to benefit from the tax-exempt status of the long-term mortgage loan portfolio, as provided for by Congress in the Farm Credit Act of 1971, as amended. During the year, the FCA Board approved requests from two FLCAs to convert to the parent-subsidiary structure; converting to this structure enables the institutions to operate more efficiently while offering their borrowers a broader array of services.

In addition, Farmer Mac opened its first underwriting field office in Ames, Iowa, in 2005. This field office is expected to provide greater responsiveness to customers.

Means and Strategy #9—Ensure regulatory definitions reflect the changes in agriculture, rural areas, and the financial marketplace.

FCA monitors changes in the regulatory community and periodically reviews and updates its regulations to ensure that definitions of terms are relevant. When rules are republished as final rules, these definitions are again reviewed for completeness and accuracy with respect to industry and market parlance. FCA also issues informational memoranda to FCS institutions that provide technical clarification or examination guidance to FCS institutions.

Means and Strategy #10—Identify and eliminate, consistent with law and safety and soundness, all regulations that are unnecessary, unduly burdensome, or not based on law.

In support of section 212(b) of the Farm Credit System Reform Act of 1996 and FCA's policy statement on regulatory philosophy, the Agency solicited comments for the removal or revision of outdated, unnecessary, or burdensome regulations during spring 2003. During the year, Agency staff completed the review and analysis of the initial comments received. Then, in February 2006, the FCA Board approved a proposed rule to eliminate specific regulations that were identified as outdated and unnecessary. Final action is scheduled for Board consideration in early FY 2007.

Means and Strategy #11—Encourage partnerships between System and non- System lenders and Farmer Mac that facilitate the flow of funds to agriculture and rural areas.

FCA encourages prudent use of loan participations and similar-entity lending authorities to manage risk in FCS institutions and better serve rural America. These authorities allow lenders to diversify risk and enable the FCS to continue funding agriculture and related businesses. Participations purchased from outside sources by FCS institutions have increased considerably as a percentage of the System's portfolio in recent years. FCA examiners also reported a number of alliances with commercial banks and investment managers who provide deposit and investment products to System customers.

Farmer Mac recently issued guarantee notes that are collateralized by an obligation of a major insurance company. That collateral is, in turn, secured by Farmer Mac-eligible agricultural real estate mortgage loans. This transaction continues Farmer Mac's initiative to diversify its marketing focus by tailoring its pricing based on asset quality. While Farmer Mac receives lower compensation for securing higher-quality assets, the quality of the assets provides greater protection against adverse credit performance.

Means and Strategy #12—Publish best practices findings or establish guidelines when appropriate on FCA-regulated institutions' efficient and effective use of partnerships and other relationships with non-FCA-regulated entities to facilitate the flow of funds to agriculture and rural areas.

The Agency routinely communicates matters to System institutions that are intended to protect each institution's safety and soundness and facilitate proper management of risk. This guidance facilitates the flow of funds to agriculture and rural areas by providing System institutions with sound practices to follow in developing and implementing lending programs and information technology. Ultimately, this guidance can assist management to originate, close, and manage loan and funding programs more efficiently. Farmer Mac continues to enhance its relationships with its loan sellers and servicers. Farmer Mac's new relationships with non-FCA-regulated entities are examples of such partnerships. They include relationships with the American Bankers Association, commercial banks, and cooperative lenders serving the power generation and distribution needs of rural communities.

Goal 2—Evaluate risk and provide timely and proactive oversight to ensure the safety and soundness of the Farm Credit System and Farmer Mac.

The primary purpose of Goal 2 is to maintain the safety and soundness of the Farm Credit System and Farmer Mac and to ensure compliance with laws and regulations. FCA's examination and regulatory supervision of each institution, as well as Farmer Mac, is the principal avenue by which this goal is achieved. We established seven means and strategies to accomplish this goal and defined seven performance measures to evaluate the progress and success of our oversight of the System. The means and strategies address the critical components of effective supervision and require FCA to maintain an effective training program for examiners, to coordinate regulatory guidance and examination procedures, to focus on risk management and risk-bearing capabilities of institutions, and to identify risk and take corrective actions in a timely manner. The seven performance measures in the FCA strategic plan are designed to measure the overall safety and soundness of the System and FCA's performance in keeping System institutions fundamentally sound in all material respects and in compliance with laws and regulations. The following discussion provides additional details on the activities that contributed to FCA's achievement of Goal 2.

Means and Strategy #1—Maintain an effective examination and oversight program through maintenance of the Pre-commission Training Program and ongoing training of commissioned examiners.

The FCA examiner workforce is seasoned, with a significant number of workers who are nearing retirement age. To maintain a sufficient number of staff members skilled in their professions, the FCA continues to maintain a comprehensive Pre-commission Training Program to replenish our workforce. The Staff Development and Training Team was established as part of the reorganization of the Office of Examination (OE) to improve the quality and consistency in recruiting and developing associate examiners. Significant resources are expended to provide quality training to these employees. A redesign of the Pre-commission Training Program is being evaluated to ensure successful staff development and advancement. Part of the redesign recognizes that today's college recruits want early responsibility and the ability to contribute to the examination program and to progress in their career track at a pace consistent with their abilities. FCA's strategy is designed to maintain a competent core of commissioned examiners.

FCA's examiner training also makes a considerable investment in post-commission staff development. This is accomplished through human capital planning, career path development, and expansion of specialty examiner programs to additional technical areas. The specialty programs are designed to encourage ongoing professional development and ensure that examiners are recognized and compensated for their expertise. Presently, the Agency maintains a cadre of commissioned examiners with specialized skills, including information technology examiners, capital markets specialists, certified public accountants, and quality assurance examiners. The Agency is in the process of building greater expertise and competencies in the technical skills of examiners for the credit and accounting and controls areas. Examiners are also increasing their skills in the testing of an institution's internal control environment and board governance.

Means and Strategy #2—Develop regulatory guidance and examination procedures that keep pace with evolving strategies used by the institutions comprising the two agricultural GSEs in addressing the changing needs of their customers in rural areas.

Agency staff continues to develop regulations to provide timely and proactive oversight of System risk. The goal is to maintain the safety and soundness of the FCS while keeping pace with its changing needs. Examples of Agency regulatory and reporting activity include the following:

- Approving a final rule to amend governance regulations to enhance the oversight of management and operations.
- Approving a final rule on receiverships to provide clarification on the handling of certain transactions when institutions are placed into receivership or conservatorship.
- Approving a final rule on the issuance of preferred stock and regulatory controls to ensure fair and equitable treatment of all shareholders.

- Proposing a rule to update regulations to reflect current disclosure and reporting practices used within the financial services industry, especially those prescribed by Sarbanes-Oxley and the recently amended Securities and Exchange Commission regulations.

- Proposing a rule to revise the Farmer Mac Risk-Based Capital Stress Test regulations. The rule concerns the modeling of low-documentation loans and loans with other refinements and credit enhancements.

- Conducting a review of current regulatory requirements governing eligibility and scope of lending to determine if the current regulatory requirements are reasonable in light of the changing needs of customers in agriculture and rural America.

The FCA Board adopted a revised examination policy (Policy Statement No. 53) to guide a risk-based supervisory approach. To more effectively implement oversight programs in accordance with this directive, the Office of Examination decided to reorganize. Examination teams are now aligned according to the types of institutions that are examined, and institution "types" are defined by certain common characteristics and potential risks. The teams are coordinating closely with two newly constituted divisions, the Risk Supervision Division, which provides oversight of the FCS as a whole, and the Examination Policy Development Division, which provides proactive guidance to System institutions. These divisions respond to the System's immediate need for guidance on technical issues, regulatory changes, and emerging risks. OE made a further change in its structure by centralizing specialists in information technology and capital markets.

The changes in OE have enabled the Agency to increase its national focus and to have greater flexibility in assigning examiners to risks. As a result of its reorganization, OE now provides a more robust training development program and a more consistent approach to risk management. In addition, OE has plans to develop examination programs that identify and highlight best practices, as well as potential weaknesses for management to address proactively.

OE has adopted four national strategic oversight areas for 2006:

1. internal control environment and disclosures

2. governance and related guidance developed from a new regulation to help boards understand new requirements and achieve compliance

3. risk management systems that emphasize counterparty and collateral risk

4. mission accomplishment related to investments in rural America, YBS farmers and ranchers, and diversity

The Agency continues to develop examination procedures and guidance to keep pace with evolving strategies used by the institutions. FCA provides this guidance to FCS institutions by issuing informational memoranda and examination bulletins. Examples of such guidance include the following:

- an informational memo issued on January 25 titled, "Livestock Risk Protection and Other Products Offered by the Federal Crop Insurance Program"

- an informational memo issued May 15 titled, "Clarification of FCA Regulation 614.4200(b)(1)-Security for Long-Term Loans"

- an informational memo issued on June 22 titled, "Guidance on Preparing Your Institution for a Catastrophic Event"

- an examination bulletin issued in June to FCS institutions that provided clarification and guidance regarding qualified residential loans and related risk-weighting treatment for regulatory capital purposes

Also, as part of their operational and strategic planning efforts, examiners stay alert to the need for changes in examination procedures.

With respect to Farmer Mac, the FCA encourages innovations in its product development within the bounds of safety and soundness considerations and provisions of the Farm Credit Act of 1971, as amended. OSMO's ongoing communication, examination reports, and offsite monitoring of Farmer Mac provide timely guidance to management on the risk implications of new products.

Means and Strategy #3—Evaluate whether each FCS institution and Farmer Mac have established and are maintaining proactive risk management practices commensurate with their respective risk-bearing capacities.

Risk management, which involves developing risk parameters, stress testing, and developing loan underwriting standards, is evaluated as a normal and routine aspect of FCA's examinations, with conclusions and recommendations shared with System boards of directors. An integral part of those evaluations is determining whether the FCS institutions have proactive risk management practices commensurate with their respective risk-bearing capacities. In addition, one of OE's national strategic oversight areas is risk management systems that emphasize counterparty and collateral risk.

Means and Strategy #4—Evaluate whether each direct-lender institution maintains systems that allow it to analyze the characteristics of risk and borrower profiles in its loan portfolio.

FCA examiners evaluate whether direct-lender institutions maintain systems that allow them to properly assess the loans in their portfolios for risks. Although the timeliness and accuracy of data maintained by some FCS institutions could be improved, FCS institutions have adequate risk management systems in place and continue to make progress in positioning their balance sheets and management systems for the future. In addition, the FCS implemented a 14-point risk-rating system, which is being tested and validated. This system will allow the development and maintenance of a dynamic loan portfolio information database. Improved technology and databases provide more capabilities to run queries and conduct stress testing of loan portfolios.

Means and Strategy #5—Evaluate whether management and board governance of FCA-regulated institutions is keeping pace with the increasing size and complexity of institutions' operations.

FCA examinations evaluate whether management and board governance of FCA-regulated institutions is keeping pace with the increasing size and complexity of institution operations. Examiners continue to make recommendations, where appropriate, to further strengthen institution governance. In particular, examiners are focusing on the effectiveness of audit and review programs and the scope and depth of activities performed by audit committees.

In addition, the Agency finalized a rule to strengthen the governance of FCS institutions. The intent was to enhance board oversight; improve disclosure of compensation arrangements; provide guidance on director qualifications; and strengthen requirements for audit, nominating, and compensation committees. The FCA Board approved the final rule on January 6, 2006, and the rule became effective on April 5, 2006. FCA examiners are actively discussing the new governance rule with FCS boards and management, and a list of frequently asked questions related to the new governance rule is available to the FCS on FCA's Web site.

Board governance practices at Farmer Mac remain a central focus of the annual FCA examination because of the extent to which these practices resonate throughout Farmer Mac. FCA is actively engaged in the oversight of Farmer Mac's implementation of the Sarbanes-Oxley Act's provisions on board governance, as well as industry self-regulatory standards established by the New York Stock Exchange.

Means and Strategy #6—Maintain early warning systems that allow timely identification of emerging risks and related issues in FCS institutions.

The Agency maintains early warning systems that provide for timely identification of emerging risks and related issues in FCS institutions. The Office of Examination provides many of these systems. First, OE maintains a dynamic Financial Institution Rating System (FIRS) and benchmark ratio program that evaluates changes in the financial condition of FCS institutions each quarter. Second, a detailed quarterly risk analysis report is prepared for the board and the risk management committee that identifies emerging risks within the FCS as a whole, within each Farm Credit district, and within each OE team's portfolio; the report also provides supporting background information from the Federal Farm Credit Banks Funding Corporation. Finally, OE maintains an ongoing oversight program of each institution whereby the assigned examiners review materials and other information provided to them by FCS institutions.

In addition to examination-related activities, the Agency maintains commodity price databases, farm income and trade data, lending data, and other economic databases that are available to examiners and others in the Agency. These databases, as well as periodic presentations on assessing economic risks and changing industry trends, enable examiners and others in FCA to stay current on the changing agricultural and financial sectors.

One of the Agency's major changes was to add a new risk-assessment process that broadens the perspective of risk assessment and allows the Agency to be more proactive and forward-looking. The areas assessed include the following: credit, interest rate exposure, liquidity, operations, compliance, strategy, reputation, and internal controls.

FCA has instituted several periodic reporting requirements of Farmer Mac that collectively serve as an early warning system across all Farmer Mac functional areas. This ongoing monitoring provides significant detail on debt spreads and term structure, derivative contracts, liquidity, and nonprogram investments. It also provides information about the legal structure of Farmer Mac's new products, which is critical to the Agency's oversight of Farmer Mac activities.

Means and Strategy #7—Undertake research and analysis of emerging risks and related issues and incorporate the findings into examination and oversight programs.

Following recommendations in a strategic study, the Agency has established a Risk Committee. The Agency Risk Committee is chaired by the Chief of Staff and consists of senior Agency officials and the FCA Board executive assistants. The committee meets regularly on an agenda managed by the Chief Examiner and provides direction, where appropriate, to staff.

In addition, OE established and staffed a Risk Supervision Division to direct OE's national oversight activities. The OE Risk Committee focuses on emerging risks and brings in industry experts as appropriate to support the Agency Risk Committee. Members of the Risk Committee share ideas and seek input and collaboration from FCS leaders in addressing and managing emerging risks.

Agency staff members routinely research and analyze emerging risks and related issues and incorporate the findings into examination and oversight programs, guidance to System institutions, and regulatory policy development. During the reporting period, staff researched and communicated guidance on the following:

- qualified residential loans and related risk-weighting treatment for regulatory capital purposes
- preparing institutions for a catastrophic event
- clarification of security for long-term loans
- livestock risk protection and other insurance services offered by the Federal Crop Insurance Corporation

Other recent guidance to the FCS included informational memoranda on the prohibition against discrimination in credit transactions, the standard flood determination form, and various compliance issues. The Agency has also conducted research on the potential impact of the avian flu and Hurricanes Katrina and Rita on agriculture, the general economy, and FCS institutions.

Significant resources continue to be employed to analyze and revise the Farmer Mac Risk-Based Capital Stress Test in relation to (1) the carrying costs of nonperforming loans, (2) counterparty risk, and (3) new financial and risk structures within the program business underwritten by Farmer Mac.

Goal 3—Implement the President's Management Agenda.

The primary purpose of Goal 3 is to implement the President's Management Agenda effectively and efficiently. This internally focused goal supports the five Government-wide initiatives to make the Government more results-oriented and focused on achievement and accountability. These initiatives are as follows:

1. Strategic Management of Human Capital-to maximize the value of FCA's most important resource, its workforce.

2. Improved Financial Performance-to produce accurate, reliable, and timely information to support policy, budget, and operating decisions.

3. Expanded Electronic Government-to strengthen our management of information technology resources and use the Internet to simplify and enhance service delivery.

4. Budget and Performance Integration-to enhance FCA's control over resources used and better establish accountability for results.

5. Competitive Sourcing-to encourage continuous improvement and remove roadblocks to greater efficiency.

The Agency's Strategic Plan includes five means and strategies and five performance measures that evaluate accomplishment of Goal 3. The following discussion provides additional information on the Agency's activities that led to the overall accomplishment of Goal 3.

Means and Strategy #1—Strategically manage human capital.

Sound human resource management is crucial to FCA's mission and goals. The Agency has a performance-based compensation system that rewards employees for individual job accomplishments that support the Agency's performance objectives. FCA is dedicated to effective human resource strategic planning, recruiting and hiring a diverse and competent workforce, establishing competitive compensation and benefits programs, training and developing highly qualified employees, developing policies to reward and recognize employees, and administering a performance management system that effectively measures an employee's contributions to the Agency's mission and goals.

The Agency's key human capital challenge is the large number of employees who are eligible to retire over the next 5 years. To address this issue, FCA has developed a 5-year Human Capital Plan. The plan contains numerous initiatives to help the FCA integrate workforce planning and deployment, employee development, and recruitment and retention strategies with its strategic planning process to ensure that the Agency will continue to meet its statutory mandates.

One component of the plan is the Knowledge Management Initiative. This initiative involves developing strategies for knowledge sharing, knowledge retention, training, and supervisory development to ensure that corporate knowledge and specialized experience are passed on to new employees before seasoned, more experienced employees retire. In addition, throughout the Human Capital Plan, there are initiatives designed to increase diversity within the Agency. One initiative involves implementing an overall strategy to address diversity issues at the Agency; this strategy also includes a means to measure the success of these efforts to support diversity.

Recruiting efforts to create a more diverse workforce continue to include individuals in underrepresented groups. FCA also maintains a supportive, yet challenging, workplace environment that encourages employees to excel in their job responsibilities and prepares them for future duties. FCA has various programs and policies to recruit qualified employees and retain them by rewarding accomplishments and helping employees balance work and family needs. The following are efforts that have recently been initiated; work is still underway to fully develop these programs.

- Paying for student loans as a recruiting tool to attract highly qualified employees.

- Identifying job competencies and developing career tracks within the Agency, then placing these competencies and career tracks into an Individual Development Plan database to assist employees and managers in enhancing their knowledge, skills, and abilities.

- Identifying and developing e-learning training opportunities as a cost-effective means to expand employee competencies.

- Creating a two-year career internship program to assist with succession planning needs.

- Linking strategic Agency goals to individual development plans and to the budget process to help prepare Agency staff for future endeavors.

- Expanding telework opportunities and reimbursing essential employees for broadband costs; this helps ensure the continuity of operations in cases of natural disasters or emergencies.

- Maintaining a variety of policies to help retain employees and assist them in balancing work and family needs, including flexible hours of duty, business casual dress, transit subsidies, voluntary 401(k) savings opportunities, reimbursements up to $150 for annual physical exams and preventive health screenings, donations of $750 to flexible spending accounts, and contributions up to $400 toward health and fitness programs and equipment.

FCA's programs and policies have enabled us to maintain a cohesive group of employees with the skills to accomplish current responsibilities and to expand their levels of expertise to address future issues.

Means and Strategy #2—Upgrade the Agency's financial management system.

FCA continues to emphasize strong fiscal management. The Agency's management system produces accurate, reliable, and timely information to support policy, budget, and operating decisions. Since FY 2001, FCA maintained this capability through the use of American Management System's mainframe financial management system, the Federal Financial System (FFS). Developed in the early 1980s, FFS remained reliable until it was phased out by its developer; in 2003, FFS was not recertified as compliant with the Joint Financial Management Improvement Program. After conducting a thorough cost-benefit analysis, FCA entered into a shared-services agreement with the Bureau of the Public Debt's (BPD's) Administrative Service Center to ensure that the Agency's financial management system remains secure, effective, and dependable. FCA's partnership with BPD will enable the Agency to track and manage expenditures, compile scheduled and on-demand reports for management, and to produce the required reports for the Office of Management and Budget and Congress. Full implementation was accomplished on April 1, 2006.

Means and Strategy #3—Continue the expansion of electronic government.

FCA is constantly striving to improve its e-government operations by adding more content to its Web site, enhancing its usability, and making it easier for FCS institutions to submit more kinds of reports and other information to the Agency. E-government initiatives during FY 2006 included the following:

- providing FCA staff with access to their e-mail through the Internet

- expanding the Agency's partnership program with System institutions to safely exchange information over the Internet using secured accounts

- improving the ability of Agency employees to work from remote sites through enhanced broadband virtual-private-network and wireless technology

- partnering with other agencies to participate in the Government-wide Enterprise Human Resources Integration program, which provides electronic official personnel files and analytical tools

- enhancing FCA's Web site through redesign to make information easier to identify and access

- implementing encrypted e-mail to facilitate the exchange of sensitive information with external parties securely over the Internet

Means and Strategy #4—Continue the evolution of budget and performance integration.

The Agency continues the evolution of its performance budgeting program by aligning resource requirements for continuing programs and new initiatives with outputs and performance goals identified in the FCA strategic plan. FCA has continued to refine, through the automation of its budget formulation system, the integration of budget resources with both Agency-wide and individual office performance goals.

Means and Strategy #5—Give due consideration to competitive sourcing.

FCA commits to improving internal operations by using resources more effectively to solve workload challenges. To carry out this commitment, the Agency conducts an annual inventory of commercial activities that are not inherently Government but are performed by Federal employees. FCA conducts the inventory according to the Federal Activities Inventory Reform Act of 1998 and the Office of Management and Budget Circular A-76, Performance of Commercial Activities. Through self-examination, FCA evaluates areas for potential improvements and identifies ways to enhance products and services. Open competition results in improvements and helps the Agency perform its mission and meet its goals and objectives.

It is the Agency's goal to provide the best products and services to customers. Therefore, FCA continually reevaluates the effective use of Agency human capital to best carry out its mission within budget.

Table 6a
Goal 1—Mission
Performance Measures and Results

Measure	Results	FY 2003 Target[2]	FY 2003 Results	FY 2004 Target	FY 2004 Results	FY 2005 Target	FY 2005 Results	FY 2006[1] Target	FY 2006[1] Results	FY 2006 Results vs. Target
1. Percentage of FCS institutions[3] with satisfactory strategic business plans as rated by FCA examiners for providing constructive credit and related services to all potential customers, including those operating under corrective action plans acceptable to the FCA.[4]	FCA examiners reviewed the strategic business plans of 101 FCS institutions. All were found to be satisfactory or were operating under acceptable corrective action plans.	NA	NA	100%	98%	>90%	99%	>90%	100%	▲
2. Farmer Mac has developed and implemented a marketing program to appropriately grow program assets consistent with its mission and received a satisfactory rating from the Office of Secondary Market Oversight (OSMO) or is operating under a corrective action plan acceptable to OSMO.	Farmer Mac has a marketing program that accomplishes this measure.	NA	NA	NA	NA	Yes	Yes	Yes	Yes	✓
3. Percentage of direct-lender institutions with satisfactory internal controls over consumer compliance and borrower-rights compliance, including those operating under corrective action plans acceptable to FCA. FCA examiner reviews of consumer compliance and borrower rights are absent any material deficiencies or weaknesses in internal controls.[4]	FCA examiners performed compliance reviews at 39 direct-lender institutions. All were absent any material deficiencies or weaknesses in internal controls or were operating under acceptable corrective action plans.	NA	NA	100%	97%	≥90%	100%	≥90%	100%	▲

1. Because of the accelerated due date for the Performance and Accountability Report, the reportable performance period runs from July 1, 2005, to June 30, 2006.
2. The following defines the symbols and abbreviations used to describe targets in the Performance Measures and Results table: < is less than; > is greater than; ≤ is less than or equal to; ≥ is greater than or equal to; NA indicates either that the measure is not applicable or that FCA's performance could not be measured; ▲ indicates FCA's performance exceeded the FY 2006 target; ✓ indicates FCA achieved the target; ★ indicates FCA substantially accomplished the target in all material respects; and ▼ indicates FCA did not achieve its target.
3. For purposes of performance measurement, the term "institutions" does not include the FCS service corporations, the National Cooperative Bank, Farmer Mac (unless specifically noted), or institutions that FCA examines on behalf of the Small Business Administration and the U.S. Department of Agriculture on a contract basis.
4. Performance measure has been restated for clarity.

Table 6a
Goal 1—Mission
Performance Measures and Results

Measure	Results	FY 2003 Target[2]	FY 2003 Results	FY 2004 Target	FY 2004 Results	FY 2005 Target	FY 2005 Results	FY 2006[1] Target	FY 2006[1] Results	FY 2006 Results vs. Target
4. Percentage of instances in which FCA solicits public comment and input on applicable regulatory initiatives using supplemental approaches[5] to the notice and comment rulemaking process.	Supplemental approaches were used on 7 of 10 regulatory initiatives.	NA	NA	≥40%	72.3%	≥40%	30%	≥40%	70%	▲
5. Percentage of direct-lender institutions that have satisfactory programs as rated by FCA examiners to furnish sound and constructive credit and related services to young, beginning, and small (YBS) farmers, ranchers, and producers and harvesters of aquatic products, or that have acceptable corrective action plans in place.[4]	FCA examiners reviewed the YBS programs at 51 direct- lender institutions. All were found to be satisfactory or were operating under an acceptable corrective action plan.	100%	92%	100%	100%	≥90%	99%	≥90%	100%	▲
6. The aggregate annual change in the level of System participation in Federal and State guarantee programs in relation to the aggregate annual change in total Federal and State guarantee programs to further accomplish the System's public mission.[4]	This performance measure cannot be calculated for the State guarantee program activity because of a lack of reporting from State agencies. For the Federal guarantee program, the System achieved the target.[6]	NA	NA	≥1.00	NA	≥1.00	1.12	≥1.00	1.00	✓

5. Supplemental approaches include advance notice of proposed rulemaking, comment period reopenings and extensions, constituent/congressional committee meetings, public meetings, focus groups, town meetings, and other unique approaches to gathering a broad range of public input. To ensure technical accuracy, the results reported were calculated by dividing the number of regulatory initiatives that used supplemental approaches by the total number of regulatory projects published in the Regulatory Performance Plan. The process for reporting performance results for supplemental approaches was addressed in a recent report by the Office of the Inspector General (IG). The results reported herein are in accordance with the IG's recommendations.
6. Because of the accelerated due date for the Performance and Accountability Report, the Federal guarantee program results are based on data from September 30 of the previous year.

Table 6b
Goal 2—Safety and Soundness
Performance Measures and Results

Measure	Results	FY 2003 Target[2]	FY 2003 Results	FY 2004 Target	FY 2004 Results	FY 2005 Target	FY 2005 Results	FY 2006[1] Target	FY 2006[1] Results	FY 2006 Results vs. Target
7. Number of institutions that FCA placed in receivership because of financial failure during the previous 12 months.[4]	During the past 12 months, no FCS institutions were placed in receivership.	NA	NA	0	0	0	0	0	0	✓
8. The total assets of FCS institutions that FCA has determined are fundamentally sound in all material respects.[4]	All FCS institutions were fundamentally sound in all material respects, as reflected by their composite Financial Institution Rating System (FIRS) ratings of 1 and 2.	NA	NA	≥90%	100%	≥90%	100%	≥90%	100%	▲
9. Percentage of FCS institutions with composite FIRS ratings of 3, 4, or 5 with acceptable corrective action plans in place to address the underlying problems as determined by FCA examiners.[4]	No FCS institution had composite FIRS ratings of 3 or worse. Consequently, no corrective action plans were required.	NA	NA	100%	100%	100%	100%	100%	100%	✓
10. Percentage of System assets in institutions with adverse assets-to-risk funds less than 100 percent.[4]	All FCS institutions maintained adversely classified assets at levels that were within their risk-bearing capacity as adverse assets-to-risk funds were less than 100 percent.	100%	100%	100%	100%	≥90%	100%	≥90%	100%	▲
11. Percentage of institutions complying with all regulatory capital ratio requirements (permanent capital ratio, total capital ratio, core surplus ratio, net collateral, risk-based capital), including those operating under corrective action plans acceptable to FCA.[4]	All FCS institutions complied with the regulatory capital requirements.	100%	100%	100%	100%	100%	100%	100%	100%	✓

Table 6b
Goal 2—Safety and Soundness
Performance Measures and Results

Measure	Results	FY 2003 Target[2]	FY 2003 Results	FY 2004 Target	FY 2004 Results	FY 2005 Target	FY 2005 Results	FY 2006[1] Target	FY 2006[1] Results	FY 2006 Results vs. Target
12. Percentage of FCS institutions with acceptable action plans to correct violations of laws and regulations identified by FCA examinations.[4]	FCA examiners identified 28 FCS institutions that had violations of laws and regulations. All had acceptable corrective action plans.	NA	NA	100%	93%	100%	100%	100%	100%	✓
13. Percentage of FCA-regulated institutions that have satisfactory audit and review programs as determined by FCA examiners, including those with corrective action plans acceptable to FCA.[4]	FCA examiners reviewed the audit and review programs of 56 FCA-regulated institutions. All were found to be satisfactory or were operating under acceptable corrective action plans.	NA	NA	100%	97%	100%	100%	100%	100%	✓

Table 6c
Goal 3—President's Management Agenda
Performance Measures and Results

Measure	Results	FY 2003 Target[2]	FY 2003 Results	FY 2004 Target	FY 2004 Results	FY 2005 Target	FY 2005 Results	FY 2006[1] Target	FY 2006[1] Results	FY 2006 Results vs. Target
14. Structure of Agency is assessed at least once every 5 years[7] to determine whether changes are needed to better meet mission goals.	As many in the FCA workforce draw closer to retirement age, management continues to evaluate human capital needs. During 2005, staffing studies were conducted throughout the Agency to help identify workforce requirements to meet future needs. Organizational structural changes were made to improve operations and efficiency.	NA	NA	Yes	Not Available	Yes	Yes	Yes	Yes	✓
15. Audit opinion on the Agency's annual financial statements, as reported by the Agency's external auditors.	Performance measure goal was achieved for FY 2006. On October 28, 2005, the Agency received an unqualified audit opinion from its external auditors on the FY 2005 annual financial statements.	NA	NA	Unqualified	Unqualified	Unqualified	Unqualified	Unqualified	Unqualified	✓
16. Number of material internal control weaknesses reported by the Agency's financial auditors.	Performance measure goal was achieved for FY 2006. No material internal control weaknesses were identified by the Agency's external auditors during the 2005 year-end audit.	NA	NA	0	0	0	0	0	0	✓
17. Percentage of the Agency's Web pages and electronic devices that are Section 508 accessibility compliant.[8]	Performance measure goal was again exceeded for FY 2006. As of June 30, 2006, 97.9 percent of the Agency's Web pages and electronic devices were Section 508 accessibility compliant.	NA	NA	≥95%	95.5%	≥95%	95.4%	≥95%	97.9%	▲

7. The frequency for the assessment of the Agency's structure was revised from once every 3 years to once every 5 years to better reflect when staffing studies are actually conducted.
8. The goal of Section 508 of the Rehabilitation Act of 1973, as amended by the Workforce Investment Act of 1998, is to provide Federal employees with disabilities access to office systems and information equal to their nondisabled colleagues. It also ensures that people in the general public who have disabilities have equal access to government information.

Table 6c
Goal 3—President's Management Agenda
Performance Measures and Results

Measure	Results	FY 2003		FY 2004		FY 2005		FY 2006[1]		FY 2006
		Target[2]	Results	Target	Results	Target	Results	Target	Results	Results vs. Target
18. FCA information and technology services are available on a 24-hour basis to provide appropriate users access to Agency information, communications, and data collection services.[4]	Performance measure goal was again exceeded for FY 2006. FCA's network and Web components were available 99.5 percent of the time.[9]	NA	NA	≥97%	98.2%	≥97%	98.3%	≥97%	99.5%	▲

9. In calculating the availability of information resources, FCA does not include the minutes of scheduled downtime for routine network maintenance.

Auditor's Reports and Financial Statements

Letter from the Chief Financial Officer

Fiscal year (FY) 2006 has been an exciting and challenging year for the Farm Credit Administration (Agency or FCA), both in the administration of the Agency's programs and in its financial operations. In 2005, FCA began implementing various organizational and functional changes within the examination and regulatory policy processes. These changes were the result of strategic studies performed to help the Agency position itself to better meet the needs of a changing Farm Credit System, including the Federal Agricultural Mortgage Corporation. During 2006, FCA saw these changes come to fruition, which has resulted in systemic improvements in the way the Agency is now able to fulfill its mission.

Equally as important as the programmatic changes are the significant accomplishments that FCA has made in improving its support functions. FCA's support functions responded to the programmatic changes with required human resource needs, financial structural changes, budgetary realignments, and improved electronic and information technology initiatives. These have helped to ensure that FCA continues to operate in a more effective and efficient manner.

With regard to financial management, I share the overall vision of the Financial Management Line of Business, which is to improve the cost, quality, and performance of financial management systems by leveraging shared-service solutions and implementing other Government-wide reforms that foster efficiencies in Federal financial operations. To this end, on April 1, 2006, the FCA partnered with the Bureau of the Public Debt (BPD), Administrative Resource Center, to ensure that the Agency's financial management system remains secure, effective, and dependable. In addition to its financial system, FCA transitioned its accounting, procurement, credit card, travel management, and relocation services to BPD. FCA's intent was to ensure that the Agency obtains the best value through the grouping of services while also maintaining its high standard of financial management practices. As with any major change, there have been some challenges that the Agency has had to overcome. But with the use of best practices, revised mindsets, and the use of innovative techniques, the partnership is succeeding.

In summary, I am pleased with the vast improvements FCA has made during FY 2006. As we embark on the new fiscal year, I am fully committed to the work of making FCA the best it can be. With the help of a dedicated staff and our financial management partner, I am confident that this goal can be achieved.

Stephen G. Smith
Director and Chief Financial Officer
Office of Management Services

Farm Credit Administration

Office of Inspector General
1501 Farm Credit Drive
McLean, Virginia 22102-5090
(703) 883-4000

November 9, 2006

The Honorable Nancy C. Pellett
Chairman of the Board
Farm Credit Administration
1501 Farm Credit Drive
McLean, Virginia 22102-5090

Dear Chairman Pellett:

This letter transmits the report on the audit of the Farm Credit Administration's (FCA or Agency) financial statements for the fiscal year ended September 30, 2006. The Office of Inspector General (OIG) contracted with Harper, Rains, Knight, & Company, P.A. (HRK), an independent accounting firm, to perform the audit. This letter also incorporates a summary of what I believe are significant management and performance challenges facing the Agency. I also described these challenges in the OIG Semiannual Report to the Congress for the period ended September 30, 2006 (Semiannual Report).

HRK issued an unqualified opinion. HRK opined that FCA's principal financial statements present fairly, in all material respects, the financial position of the Agency as of September 30, 2006 and 2005, in conformity with generally accepted accounting principles. HRK issued two other reports. Its report on internal control noted no matters considered to be material weaknesses. The HRK report on compliance with laws and regulations does not note any instances of noncompliance. In the OIG's opinion, HRK's work provides a reasonable basis on which to render its opinion and we concur with their reports.

The contract with HRK required they perform the audit in accordance with "Government Auditing Standards" issued by the Comptroller General of the United States and Office of Management and Budget Bulletin No. 01-02, "Audit Requirements for Federal Financial Statements." To ensure the quality of the work performed, the OIG:

- reviewed HRK's approach and planning of the audit;
- evaluated the qualifications and independence of the auditors;
- monitored progress of the audit;
- examined work papers; and
- reviewed the audit reports.

As part of the Agency's annual Performance and Accountability Report, the Inspector General is required to provide an opinion on the most serious management and performance challenges facing the Agency. In the Semiannual Report, I outlined substantive challenges confronting the Agency. These challenges fall into two general categories. First are the challenges related to the FCA's mission of ensuring a safe, sound, and dependable Farm Credit System (FCS or System) as a source of credit and related services to agriculture. Some of these challenges may be influenced by events that are outside the control of the Agency. Second, but no less important, are the challenges related to the Agency's operations.

Management and Performance Challenges

FCS - The System is a lender to a single industry, agriculture, and is therefore vulnerable to economic swings in that industry. Nevertheless, the FCS remains sound in all material respects. Earnings and capital levels have continued to strengthen and asset quality remains high. However, there are many aspects of agriculture and rural America today that raise the question of whether there should be modifications to the Farm Credit Act of 1971, as amended (Act), in order to enable the System to better serve agricultural and rural economies of the future.

The FCA and the System have a responsibility to inform Congress when there is a need to update the Act in order to ensure the FCS is able to provide constructive and sufficient credit and related services to agriculture into the future. Ensuring that Congress is so informed will require a consistency in approach and strategic thinking on the part of the Agency and the System to assist Congress in maintaining the Act as a dynamic and empowering vehicle for the ultimate benefit of America's farmers, ranchers, and other rural citizens.

FCA - The FCA must balance the often competing demands of ensuring the FCS fulfills its public policy purpose, proactively examining risk in the regulated institutions both individually and systemically, and controlling the cost of the regulator. FCA's challenge is complex because it has become increasingly difficult to reconcile significant provisions of the Act with the realities of the agricultural industry, the economic environment, and financial markets in the 21ST Century.

The Agency should anticipate that the System will seek broader powers through regulatory interpretations of the Act. At the same time, FCA should expect that the System's competitors will press for the Agency to be a strict interpreter of the Act. As a financial regulator, FCA must maintain a flexible and responsive, yet independent and objective, regulatory environment for the System.

Strategic Planning - The FCA Board adopted its 2004-2009 Strategic Plan in December 2003. Since adoption, the Agency has a new Chairman and a new Board member. The changes in top leadership provide an opportunity to revise the plan to ensure the Board's vision is accomplished. The challenge is to establish a strategic plan that is ongoing in nature and in pace with the Agency's environment. In 2005, the Board established a Strategic Planning Committee, one of three committees established to facilitate the Board's oversight responsibilities and communication between the Board and Agency staff. This committee has the potential to catalyze the strategic planning function and address this challenge.

The Board refined Agency performance measures in January 2005. FCA should evaluate its performance measures on an ongoing basis to ensure they challenge and stretch the organization. Performance measures can be a powerful tool to continue the push into a results-oriented organization. An effective performance management system fosters performance and accountability at the individual, organizational, and ultimately overall Agency levels.

Agency Governance - The Act provides for a full-time three-member Board. Board members are appointed by the President and confirmed by the Senate. This small full-time Board presents a challenge in terms of defining the roles and responsibilities of Board members relative to the governance of the Agency. The Board must be able to engage in professional policy debate and set a sound course for the Agency. The Board's rules of operation are a foundation for trust and shared expectations among Board members. A collegial Board, founded on mutual trust and respect, is essential to FCA's ultimate effectiveness.

The Chairman has taken action to address this challenge by sharing authority and creating an environment at the Board level that promotes a constructive working relationship between Board members. Board members have made significant and obvious strides to remain current and knowledgeable in the dynamic agriculture, financial, and regulatory environments.

Human Capital - In March 2001, the OIG recommended FCA develop a human capital plan and FCA management agreed. Under Chairman Pellett's leadership, senior managers have focused on the challenge of marshalling, managing, and maintaining human capital to assure accountability and maximize FCA performance. The Agency also made a significant investment in strategic studies in 2004 and 2005. The objective of the strategic studies was to create a picture of the System and the credit needs of rural America in 5 to 7 years and identify organizational and human capital opportunities to help FCA adapt.

Chairman Pellett's leadership in initiating the strategic studies, in reorganizing the Agency, and in emphasizing the importance of human capital has resulted in the completion of a comprehensive 5-year strategic human capital plan. The plan identifies five human capital goals and six human capital initiatives, including leadership continuity of which succession planning is an integral part.

A critical component in implementing the human capital plan is providing for management succession. Individuals with the potential to become managers should be identified, provided developmental opportunities, and, when appropriate, promoted to higher positions. This, as part of a human capital plan, should be linked to the Agency's Strategic Plan for long-term achievement of the Agency's mission.

FCA's challenge will be to implement the human capital plan to ensure organizational approaches that enable FCA to adapt to evolving technology, a changing workforce, and other environmental forces. In addition to achieving full transformation of the Agency's organization and processes, the way in which FCA meets its mission will be heavily dependent on quality of its human capital, having the appropriate skill sets, and how it organizes to meet its mission. A significant step in this direction was the completion of the 5-year strategic human capital plan.

Financial Management - Timely, accurate, and useful financial information is essential for:

- making day-to-day decisions;
- managing the Agency's operations more effectively;
- supporting results-oriented management approaches; and
- ensuring accountability on an ongoing basis.

In April 2006, FCA outsourced accounting, financial reporting, contracting and procurement, and e-Travel functions to the Bureau of the Public Debt, Department of the Treasury. While the transition is still underway, its ultimate success will still need to be measured by whether the Agency and its managers are receiving timely service, useful financial reporting, and improved efficiencies. To measure this, the Agency will need to develop performance measures to assess the achievement of goals related to this outsourcing.

Leveraging Technology - Information technology (IT) is a key element of management reform efforts that can help dramatically reshape government to improve performance and reduce costs. The Agency has recognized that in order to meet the constraints of its budget, it must be able to maximize its return on investment in technology. Internally, there is an opportunity to further strengthen how IT complements human capital initiatives to reformulate the work processes of FCA. There is also an opportunity to capture knowledge of employees who are approaching retirement. In this regard, the Office of Management Services has undertaken an initiative entitled Electronic Recordkeeping-Knowledge Management. The objective of this project is to develop an electronic system to manage the Agency's official records and to retain its critical institutional, technical, and operational knowledge.

Externally, E-Government offers many opportunities to better serve the public, make FCA more efficient and effective, and reduce costs. FCA has begun to implement some E-Government applications, including the use of the Internet to collect and disseminate information. FCA's ongoing challenge is to establish effective mechanisms to ensure that current and future members of staff have the skills to use technology to operate in an efficient, effective, and secure manner.

Respectfully,

Carl A. Clinefelter

Carl A. Clinefelter
Inspector General

HARPER, RAINS, KNIGHT
& COMPANY
Certified Public Accountants
A Professional Association

INDEPENDENT AUDITORS' REPORT ON THE FINANCIAL STATEMENTS

FARM CREDIT ADMINISTRATION
The Board and Office of Inspector General

We have audited the balance sheets of the Farm Credit Administration (FCA) as of September 30, 2006 and 2005, and the related statements of net cost, changes in net position, budgetary resources, and financing for the fiscal years then ended. These financial statements are the responsibility of the FCA's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial statement audits contained in Government Auditing Standards, issued by the Comptroller General of the United States; and Office of Management and Budget (OMB) Bulletin 01-02, "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 of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the assets, liabilities, and net position of the FCA as of September 30, 2006 and 2005, and the net cost, changes in net position, budgetary resources, and reconciliation of net cost to budgetary resources for the years then ended in conformity with accounting principles generally accepted in the United States of America. Our audits were conducted for the purpose of forming an opinion on the fiscal year 2006 and 2005 principal financial statements of the FCA. The accompanying financial information, discussed below, is not a required part of the principal financial statements.

The Management Discussion and Analysis on pages 2-25 and the Required Supplemental Information on pages 73-76 is supplementary information required by the Federal Accounting Standards Advisory Board. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the information. However, we did not audit the information and express no opinion on it.

Harper, Rains, Knight & Company, P.A.

Harper, Rains, Knight & Company, P.A.
November 3, 2006

Harper, Rains, Knight & Company, P.A. Certified Public Accountants Consultants
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A Professional Association

INDEPENDENT AUDITORS' REPORT ON INTERNAL CONTROL

FARM CREDIT ADMINISTRATION
The Board and Office of Inspector General

We have audited the Principal Statements (hereinafter referred to as "financial statements") of the Farm Credit Administration (FCA) as of and for the fiscal years ended September 30, 2006 and 2005, and have issued our report thereon dated November 3, 2006. We conducted our audits 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. 01-02, "Audit Requirements for Federal Financial Statements."

In planning and performing our audits, we considered FCA's internal control over financial reporting byobtaining an understanding of the agency's internal control, determined whether internal controls had been placed in operation, assessed control risk, and performed tests of controls in order to determine our auditing procedures for the purpose of expressing our opinion on the financial statements. We limited our internal control testing to those controls necessary to achieve the objectives described in OMB Bulletin No. 01-02. We did not test all internal controls relevant to operating objectives as broadly defined by the Federal Managers' Financial Integrity Act of 1982, such as those controls relevant to ensuring efficient operations. The objective of our audits was not to provide assurance on internal control. Consequently, we do not provide an opinion on internal control.

Our consideration of the internal control over financial reporting would not necessarily disclose all matters in the internal control over financial reporting that might be reportable conditions. Under standards issued by the American Institute of Certified Public Accountants, reportable conditions are matters coming to our attention relating to significant deficiencies in the design or operation of the internal control that, in our judgment, could adversely affect the agency's ability to record, process, summarize, and report financial data consistent with the assertions by management in the financial statements. Material weaknesses are reportable conditions in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that misstatements in amounts that would be material in relation to the financial statements being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. Because of inherent limitations in internal controls, misstatements, losses, or noncompliance may nevertheless occur and not be detected. However, we noted no matters involving the internal control and its operation that we considered to be material weaknesses as defined above.

With respect to internal control related to performance measures reported in the Performance Report, we obtained an understanding of the design of significant internal controls relating to the existence and completeness assertions, as required by OMB Bulletin No. 01-02. Our procedures were not designed to provide assurance on internal control over reported performance measures, and, accordingly, we do not provide an opinion on such controls. This report is intended solely for the information and use of the management of FCA, OMB, and Congress, and is not intended to be and should not be used by anyone other than these specified parties.

Harper, Rains, Knight & Company, P.A.

Harper, Rains, Knight & Company, P.A.
November 3, 2006

HRK
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Certified Public Accountants
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INDEPENDENT AUDITORS' REPORT
ON COMPLIANCE WITH LAWS AND REGULATIONS

FARM CREDIT ADMINISTRATION
The Board and Office of Inspector General

We have audited the Principal Statements (hereinafter referred to as "financial statements") of the Farm Credit Administration (FCA) as of and for the fiscal years ended September 30, 2006 and 2005, and have issued our report thereon dated November 3, 2006. We conducted our audits 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. 01-02, "Audit Requirements for Federal Financial Statements."

The management of FCA is responsible for complying with laws and regulations applicable to the agency. As part of obtaining reasonable assurance about whether the agency's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws and regulations, noncompliance with which could have a direct and material effect on the determination of financial statement amounts, and certain other laws and regulations specified in OMB Bulletin No. 01-02, including the requirements referred to in the Federal Financial Management Improvement Act (FFMIA) of 1996. We limited our tests of compliance to these provisions and we did not test compliance with all laws and regulations applicable to FCA.

The results of our tests of compliance with the laws and regulations described in the preceding paragraph exclusive of FFMIA disclosed no instances of noncompliance with laws and regulations that are required to be reported under Government Auditing Standards and OMB Bulletin No. 01-02. Under FFMIA, we are required to report whether the agency's financial management systems substantially comply with the Federal financial management systems requirements, applicable Federal accounting standards, and the United States Government Standard General Ledger at the transaction level. To meet this requirement, we performed tests of compliance with FFMIA section 803(a) requirements. The results of our tests disclosed no instances in which the agency's financial management systems did not substantially comply with the three requirements discussed in the preceding paragraph. Providing an opinion on compliance with certain provisions of laws and regulations was not an objective of our audits and, accordingly, we do not express such an opinion.

This report is intended solely for the information and use of the management of FCA, OMB, and Congress, and is not intended to be and should not be used by anyone other than these specified parties.

Harper, Rains, Knight & Company, P.A.

Harper, Rains, Knight & Company, P.A.
November 3, 2006

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FINANCIAL STATEMENTS AND RELATED NOTES

FARM CREDIT ADMINISTRATION
BALANCE SHEET
As of September 30, 2006 and 2005

	2006	2005
ASSETS		
Intragovernmental		
Fund Balance with Treasury (Note 2)	$ 1,782,919	$ 1,195,445
Investments (Note 3)	22,518,887	18,980,498
Accounts Receivable (Note 4)	301,481	143,296
Prepaid Expenses	7,830	14,167
Total Intragovernmental	24,611,117	20,333,406
Accounts Receivable (Note 4)	226,277	202,265
General Property, Equipment, and Software, Net (Note 5)	386,381	950,965
Prepaid Expenses	66,346	104,400
Total Assets	**$25,290,121**	**$21,591,036**
LIABILITIES		
Intragovernmental		
Accounts Payable	$ -	$ 129,282
Accrued Post-Employment Compensation (Note 6)	34,041	30,870
Advances from Others	3,363	3,363
Accrued Taxes Payable	-	1,490
Employer Contributions and Payroll Taxes Payable	205,262	196,077
Total Intragovernmental	242,666	361,082
Accounts Payable	473,739	487,264
Actuarial Workers' Compensation Liability (Note 7)	1,171,851	1,152,559
Accrued Payroll and Benefits	3,911,313	3,834,720
Accrued Taxes Payable	21,812	-
Employer Contributions and Payroll Taxes Payable	42,271	31,607
Liability for Miscellaneous Funds Received	-	328
Deferred Revenue	2,445,402	2,285,697
Total Liabilities	**8,309,054**	**8,153,257**
NET POSITION		
Cumulative Results of Operations	16,981,067	13,437,779
Total Net Position	16,981,067	13,437,779
Total Liabilities and Net Position	**$25,290,121**	**$21,591,036**

The accompanying notes are an integral part of these statements.

FARM CREDIT ADMINISTRATION
STATEMENT OF NET COST
For the Years Ended September 30, 2006 and 2005

	2006	2005 Reclassified
PROGRAM COSTS		
Safety and Soundness		
Gross Costs	$31,687,731	$33,582,606
Less: Earned Revenues	(32,970,873)	(31,675,445)
Total Net Costs—Safety and Soundness	(1,283,142)	1,907,161
Public Mission		
Gross Costs	8,274,686	7,128,952
Less: Earned Revenues	(8,605,263)	(6,701,990)
Total Net Costs—Public Mission	(330,577)	426,962
Other Activities		
Gross Costs	2,986,266	2,109,350
Less: Earned Revenues	(1,518,981)	(1,620,522)
Total Net Costs—Other Activities	1,467,285	488,828
Net Cost of Operations (+/-) (Notes 8 and 9)	**$ (146,434)**	**$ 2,822,951**

The accompanying notes are an integral part of these statements.

FARM CREDIT ADMINISTRATION
STATEMENT OF CHANGES IN NET POSITION
As of September 30, 2006 and 2005

	2006	2005
CUMULATIVE RESULTS OF OPERATIONS		
Beginning Balances	$13,437,779	$12,502,440
Prior Period Adjustments—Correction of Error (Note 10)	-	10,676
Beginning Balances, as Adjusted	13,437,779	12,513,116
Other Financing Sources		
Imputed Financing from Costs Absorbed by Others		
Federal Employee Benefits (Note 11)	2,101,259	2,226,905
Rent (Note 12)	1,295,595	1,520,709
Total Financing Sources	3,396,854	3,747,614
Net Cost of Operations (+/-)	(146,434)	2,822,951
Net Position—Ending Balances	**$16,981,067**	**$13,437,779**

The accompanying notes are an integral part of these statements.

FARM CREDIT ADMINISTRATION
STATEMENT OF BUDGETARY RESOURCES
For the Years Ended September 30, 2006 and 2005

	2006	2005 Reclassified
BUDGETARY RESOURCES		
Unobligated Balances—Beginning of Period	$13,994,718	$11,847,551
Spending Authority from Offsetting Collections		
Earned		
Collected	$42,997,075	41,029,705
Receivable from Federal Sources	142,664	18,695
Change in Unfilled Customer Orders		
Without Advance from Federal Sources	485,680	(147,728)
Subtotal—Spending Authority from Offsetting Collections	43,625,419	40,900,672
Total Budgetary Resources (Note 13)	**$57,620,137**	**$52,748,223**
STATUS OF BUDGETARY RESOURCES		
Obligations Incurred—Exempt from Apportionment	$38,914,074	$38,753,505
Unobligated Balance Available—Exempt from Apportionment	16,260,661	11,708,693
Unobligated Balance Not Available	2,445,402	2,286,025
Total Status of Budgetary Resources	**$57,620,137**	**$52,748,223**
CHANGE IN OBLIGATED BALANCE		
Obligated Balance, Net		
Unpaid Obligations, Brought Forward, October 1	$ 6,596,801	$ 7,877,822
Less: Uncollected Customer Payments from Federal Sources, Brought Forward, October 1	(539,475)	(668,509)
Total Unpaid Obligated Balance, Net	6,057,326	7,209,313
Obligations Incurred, Net	38,914,075	38,753,505
Gross Outlays	(38,882,266)	(40,034,525)
Change in Uncollected Customer Payments from Federal Sources	(628,344)	(129,033)
Obligated Balance, Net, End of Period		
Unpaid Obligations (Note 14)	6,628,611	6,596,801
Less: Uncollected Customer Payments from Federal Sources	(1,167,820)	(539,475)
Total Unpaid Obligated Balance, Net, End of Period	**$ 5,460,791**	**$ 6,057,326**
NET OUTLAYS		
Gross Outlays	$38,882,266	$40,034,525
Less: Offsetting Collections	(42,997,075)	(41,029,705)
Net Outlays	**$ (4,114,809)**	**$ (995,180)**

The accompanying notes are an integral part of these statements.

FARM CREDIT ADMINISTRATION
STATEMENT OF FINANCING
For the Years Ended September 30, 2006 and 2005

	2006	2005
RESOURCES USED TO FINANCE ACTIVITIES		
Budgetary Resources Obligated		
Obligations Incurred	$38,914,075	$38,753,505
Less: Spending Authority from Offsetting Collections	(43,625,420)	(40,900,672)
Net Obligations	(4,711,345)	(2,147,167)
Other Resources		
Imputed Financing from Costs Absorbed by Others (Notes 11 and 12)	3,396,854	3,747,614
Deferred Revenue Not in the Budget	159,705	590,259
Net Other Resources Used to Finance Activities	3,556,559	4,337,873
Total Resources Used to Finance Activities	(1,154,786)	2,190,706
RESOURCES USED TO FINANCE ITEMS NOT PART OF THE NET COST OF OPERATIONS		
Change in Budgetary Resources Obligated for Goods, Services, and Benefits Ordered but Not Yet Provided	475,391	174,134
Resources That Fund Expenses Recognized in Prior Periods	2,759	(680)
Actuarial FECA Liability Increase/(Decrease)	19,292	(227,732)
Resources That Finance the Acquisition of Assets	(77,065)	(346,308)
Total Resources Used to Finance Items Not Part of the Net Cost of Operations	420,377	(400,586)
Total Resources Used to Finance the Net Cost of Operations	(734,409)	1,790,120
COMPONENTS OF THE NET COST OF OPERATIONS THAT WILL NOT REQUIRE OR GENERATE RESOURCES IN THE CURRENT PERIOD		
Components Requiring or Generating Resources in Future Periods:		
(Increase)/Decrease in Exchange Revenue Receivable from the Public	(24,012)	434,995
Total Components of Net Cost of Operations That Will Require or Generate Resources in Future Periods	(24,012)	434,995
Components Not Requiring or Generating Resources:		
Depreciation and Amortization	611,987	586,752
Gain on Asset Disposition	-	11,084
Total Components of Net Cost of Operations That Will Not Require or Generate Resources	611,987	597,836
Total Components of Net Cost of Operations That Will Not Require or Generate Resources in the Current Period	587,975	1,032,831
Net Cost of Operations (+/-)	**$ (146,434)**	**$ 2,822,951**

The accompanying notes are an integral part of these statements.

NOTES TO THE FINANCIAL STATEMENTS

Note 1. Significant Accounting Policies

A. Reporting Entity—The Farm Credit Administration (FCA or Agency) is an independent agency in the executive branch of the U.S. Government. FCA is responsible for the regulation and examination of the banks, associations, and related entities that compose the Farm Credit System (FCS or System), including the Federal Agricultural Mortgage Corporation (Farmer Mac). Specifically, FCA is empowered to ensure safe and sound operations of all System institutions. Initially created by an Executive order of the President in 1933, FCA now derives its power and authority from the Farm Credit Act of 1971, as amended (Act). The Act requires System institutions to be examined periodically by FCA. Policy making for FCA is vested in a full-time, three-person board whose members are appointed by the President with the advice and consent of the Senate.

B. Basis of Accounting and Presentation—As required by Public Law 107-289, the Accountability of Tax Dollars Act of 2002, the accompanying financial statements have been prepared in accordance with the Office of Management and Budget's (OMB's) Circular No. A-136, Financial Reporting Requirements. Also, the financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America (GAAP) and the Statements of Federal Financial Accounting Standards (SFFAS) prescribed by the Federal Accounting Standards Advisory Board, which has been designated the official body for setting standards for the Federal Government. The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates. FCA's transactions are recorded on the accrual basis of accounting. Under this method, revenues are recognized when earned, and expenses are recognized when goods or services are received, without regard to receipt of funds or payment of cash. Budgetary accounting has also been applied to facilitate compliance with legal constraints and control over the use of funds.

Please note that the Statement of Custodial Activity contained in OMB Circular No. A-136 is not applicable to FCA and is not included as a part of the financial statements. All amounts reported in the accompanying statements and related notes are presented in dollars.

C. Fund Balance with Treasury—FCA maintains a revolving, no-year account with the U.S. Treasury through which cash receipts and disbursements are processed. The funds that are available are obtained from assessments and reimbursable activities. FCA does not receive appropriated funds.

D. Investments—The Act gives FCA the authority to invest in public debt securities with maturities suitable to FCA's needs. FCA invests solely in U.S. Treasury securities, which are normally held to maturity and carried at cost. Investments are adjusted for unamortized premiums or discounts. Premiums and discounts are amortized and interest is accrued using the level-yield, scientific method of effective interest amortization over the term of the respective issues.

E. Accounts Receivable—Accounts receivable are composed of (1) reimbursements for administrative expenses incurred by FCA according to agreements with other Federal entities, (2) assessments from institutions in accordance with the Act and FCA regulations, and (3) amounts owed FCA that are generated through the normal course of business with employees and vendors. The Office of Management Services (OMS)—in conjunction with the Agency's accounting service provider, the Bureau of the Public Debt—reviews the Agency's accounts receivable on an ongoing basis. The OMS has determined that all accounts receivable are fully collectible as of September 30, 2006.

F. Advances and Prepaid Charges—Advance payments are generally prohibited by law. There are some exceptions, such as reimbursable agreements, subscriptions, and payments to contractors and employees. Payments made in advance of the receipt of goods and services are recorded as advances or prepaid charges at the time of prepayment and recognized as expenses when the related goods and services are received.

G. General Property, Equipment, and Software—Property (including vehicles), equipment, and software are recorded at cost, net of an allowance for accumulated depreciation. Repairs and maintenance costs are expensed as incurred. In FY 2006, FCA revised its capitalization threshold policy and adopted the policy of its financial service provider. FCA operates under a policy that property, equipment, and software with itemized costs of $50,000 or more and a useful life of 2 years or more are capitalized. Individual items that are less than $50,000 but meet the bulk purchase criteria of $500,000 or more are also capitalized. The straight-line method of depreciation with half-year convention is used to allocate the cost of capitalized property, equipment, and software over their estimated useful lives.

H. Accounts Payable—Accounts payable consist of amounts owed to other Federal agencies and the public.

I. Liabilities—Liabilities may be covered or not covered by budgetary or other resources. Liabilities covered by budgetary resources are those liabilities for which funding is available to pay amounts due. Liabilities not covered by budgetary resources on the Balance Sheet are equivalent to amounts reported as components not requiring or generating resources on the Statement of Financing. Intragovernmental liabilities are claims against FCA by other Federal agencies.

J. Rent—The Act provides for FCA to occupy buildings and use land owned and leased by the FCS Building Association (FCSBA), an entity owned by the System banks. The FCA Board oversees the FCSBA activities on behalf of its owners. FCA is not charged for the use of the buildings or land, nor does it pay for maintenance and repair of buildings and land improvements. Rent is reflected on FCA's books as an imputed cost and an imputed financing source.

K. Federal Employee Benefits—Federal employee benefits include benefits earned by employees for pension, post-retirement health insurance, and life insurance. For reporting purposes, each employing Federal agency is required to recognize its share of the Federal government's cost and imputed financing for these benefits. To meet this requirement, the Office of Personnel Management (OPM) provides to each agency the cost factors used in the calculation of these Federal employee benefit expenses.

L. Annual, Sick, and Other Leave—Annual leave, compensatory leave, credit hours, and some other types of leave are accrued as a funded liability when earned, with an offsetting reduction for leave taken. The accrued leave liability for each of these types of leave is calculated using current pay rates. Sick leave and other types of nonvested leave are expensed as the leave is taken.

M. Assessments—A substantial portion of FCA's revenues is based upon direct assessments billed to System institutions that are regulated or examined by FCA. FCA also recognizes revenues based on examination services provided by the Office of Examination. Direct assessments are derived using a formula established in FCA regulations and are based, in part, upon the average risk-adjusted assets and the overall financial health of the institution being assessed.

N. Deferred Revenue—Prior to the beginning of each fiscal year, in accordance with the Act, the FCA determines the amount of funding required from assessments for the subsequent fiscal year and the amount of the assessment to be apportioned to each System institution, including Farmer Mac. Each year, these estimates are provided to the System institutions during September. The unearned funds received prior to the beginning of the new fiscal year are established as deferred revenue and are reported as such on the Balance Sheet. These amounts are also reported as Unobligated Funds—Not Available (for commitment/obligation)—on the Statement of Budgetary Resources.

O. Use of Estimates—Management has made certain estimates and assumptions when reporting assets, liabilities, revenue, and expenses; it has also made estimates and assumptions in the note disclosures. Actual results could differ from these estimates. Some estimates include year-end accruals of accounts and accrued workers' compensation.

P. Reclassification—The presentations used for the Statement of Net Cost and the Statement of Budgetary Resources prior to FY 2006 have been revised to reflect new formats required by the OMB Circular A-136. The circular requires agencies to present both FYs 2006 and 2005 reports in the same format. Accordingly, certain reclassifications were made to the previously issued FY 2005 reports to conform to the formats presented for FY 2006. Also, certain FY 2005 balances have been reclassified, retitled, or combined with other financial statement line items for consistency with current year presentation.

Note 2. Fund Balance with Treasury

	2006	2005
Fund Balance with Treasury		
Revolving Fund	$ 1,782,919	$ 1,195,445
Total Fund Balance with Treasury	$ 1,782,919	$ 1,195,445
Status of Fund Balance with Treasury		
Unobligated Balance		
Available	$16,260,661	$11,708,693
Unavailable	2,445,402	2,286,025
Obligated Balance Not Yet Disbursed	5,460,791	6,057,326
Subtotal—Status of Fund Balance	24,166,854	20,052,044
Funds Invested with Treasury		
Net of Unamortized Discount	(22,383,935)	(18,856,599)
Total Fund Balance with Treasury	**$ 1,782,919**	**$ 1,195,445**

Note 3. Investments

Intragovernmental Securities

Amounts for 2006 Balance Sheet Reporting

	Cost	Unamortized (Premium) Discount	Investments Net	Interest Receivable	09/30/06 Investment Balance	Market Value (Including Interest)
Nonmarketable Market-Based	$22,383,935	$ 53,752	$ 22,437,687	$ 81,200	$ 22,518,887	$ 22,430,822

Amounts for 2005 Balance Sheet Reporting (Reclassified)

	Cost	Unamortized (Premium) Discount	Investments Net	Interest Receivable	09/30/05 Investment Balance	Market Value (Including Interest)
Nonmarketable Market-Based	$18,896,095	($12,319)	$ 18,883,776	$ 96,722	$ 18,980,498	$ 18,816,421

Premiums and discounts are amortized and interest is accrued using the level yield, scientific method of effective interest amortization over the term of the respective issues. Interest earned on investments was $1,023,897 and $634,148 for FYs 2006 and 2005, respectively.

Note 4. Accounts Receivable

	2006	2005
Intragovernmental		
Reimbursements for Services Provided	$ 300,061	$ 133,658
Expenditure Refunds	1,420	9,638
Subtotal	301,481	143,296
With the Public		
Assessments	226,277	199,506
Vendor Overpayments	-	2,759
Subtotal	226,277	202,265
Total Accounts Receivable	**$527,758**	**$ 345,561**

Note 5. General Property, Equipment, and Software

As of September 30, 2006

	Estimated Useful Life	Depreciation Method	Acquisition Value	Accumulated Amortization/ Depreciation	Book Value
Equipment	3 years	Straight Line	$ 1,490,766	($ 1,139,796)	$ 350,970
Software	3 years	Straight Line	128,019	(102,704)	25,315
Vehicles	5 years	Straight Line	33,656	(23,560)	10,096
Total			**$ 1,652,441**	**($1,266,060)**	**$ 386,381**

As of September 30, 2005

	Estimated Useful Life	Depreciation Method	Acquisition Value	Accumulated Amortization/ Depreciation	Book Value
Equipment	3 years	Straight Line	$ 1,643,658	($1,628,726)	$ 14,932
IT Equipment	3 years	Straight Line	1,490,766	(642,874)	847,892
Software	3 years	Straight Line	220,013	(148,700)	71,313
Vehicles	5 years	Straight Line	33,656	(16,828)	16,828
Total			**$ 3,388,093**	**($2,437,128)**	**$ 950,965**

During FY 2006, FCA revised its capitalization policy and increased the capitalization threshold to $50,000 for individual item purchases and $500,000 for bulk purchases. Property items that had been fully depreciated and did not meet the revised criteria were removed as capitalized property items.

Note 6. Accrued Post-Employment Compensation

Intragovernmental—Covered by Budgetary Resources

	Current Liabilities
FECA and Unemployment Compensation Accrual—2006	$34,041
FECA and Unemployment Compensation Accrual—2005	$30,870

The Federal Employees' Compensation Act (FECA) provides income and medical cost protection to cover Federal civilian employees injured on the job, employees who have contracted a work-related occupational disease, and beneficiaries of employees whose deaths are attributable to job-related injury or occupational disease. Claims for benefits under the FECA for eligible FCA employees are administered by the Department of Labor (DOL) and ultimately paid by the FCA. FCA annually reimburses the DOL for the actual benefit payments paid to its employees upon receiving notification of claims incurred. As of September 30, 2006, FCA had an outstanding claim of $34,041, which will be paid with the July 2006 through June 2007 billing.

For the fiscal year-end of 2005, the FECA liability amount was $24,965. An accrual of $5,905 was established to cover the estimated charge for unemployment compensation, which brought the total owed the DOL to $30,870. The Unemployment Compensation for Federal Employees program provides benefits for eligible unemployed former civilian employees. It is administered by State Governments as agents of the Federal Government and is operated under the same terms and conditions that apply to regular State Unemployment Insurance. The law of the State under which the claim is filed determines the benefit amount, the number of weeks benefits can be paid, and other eligibility conditions.

Note 7. Actuarial Workers Compensation Liability

The DOL estimates future workers' compensation liability for specified entities that are preparing statements under the Chief Financial Officers' Act and the Government Management Reform Act. The actuarial liability estimates for FECA benefits include the expected liability for death, disability, medical, and miscellaneous costs for approved compensation cases, plus a component for incurred but unreported claims. Because FCA is not one of the specified entities for which the DOL provides individual agency estimates on a routine basis, FCA calculated its actuarial liability amount by using the DOL model for the estimation of FECA actuarial liability.

The FECA actuarial liability amounts for FYs 2006 and 2005 are $1,171,851 and $1,152,559, respectively. The increase in the actuarial liability amount may be attributed to the increase in the average compensation payments covered during FY 2006. The FCA records the FECA actuarial liability as a liability that is "Not Covered by Budgetary Resources."

Note 8. Intragovernmental Costs and Exchange Revenues

Farm Credit Administration
For the Year Ended September 30, 2006

Office

	Examination	Regulatory Policy	Secondary Market Oversight	Other Organizations	Total
Safety and Soundness (S&S)					
Intragovernmental Costs	$ 2,343,194	$ 107,439	$ 52,576	$ 2,519,066	$ 5,022,275
Public Costs	15,947,940	832,111	513,093	9,372,312	26,665,456
Total Costs—S&S	18,291,134	939,550	565,669	11,891,378	31,687,731
Intragovernmental Earned Revenue	(435,726)	(22,382)	(13,475)	(283,272)	(754,855)
Public Earned Revenue	(18,713,004)	(950,725)	(461,522)	(12,090,767)	(32,216,018)
Total Revenue—S&S	(19,148,730)	(973,107)	(474,997)	(12,374,039)	(32,970,873)
Net Program Costs—S&S	(857,596)	(33,557)	90,672	(482,661)	(1,283,142)
Public Mission					
Intragovernmental Costs	78,694	413,534	46,274	858,708	1,397,210
Public Costs	448,381	2,862,211	280,042	3,286,842	6,877,476
Total Costs—Public Mission	527,075	3,275,745	326,316	4,145,550	8,274,686
Intragovernmental Earned Revenue	(12,678)	(78,794)	(7,849)	(99,716)	(199,037)
Public Earned Revenue	(543,127)	(3,376,883)	(266,237)	(4,219,979)	(8,406,226)
Total Revenue—Public Mission	(555,805)	(3,455,677)	(274,086)	(4,319,695)	(8,605,263)
Net Program Costs—Public Mission	(28,730)	(179,932)	52,230	(174,145)	(330,577)
Other Activity					
Intragovernmental Costs	267,031	839	35	93,792	361,697
Public Costs	1,829,494	9,502	1,018	784,555	2,624,569
Total Costs—Other Activity	2,096,525	10,341	1,053	878,347	2,986,266
Intragovernmental Earned Revenue	(929,366)	(4,584)	(467)	(389,360)	(1,323,777)
Public Earned Revenue	(137,044)	(676)	(69)	(57,415)	(195,204)
Total Revenue—Other Activity	(1,066,410)	(5,260)	(536)	(446,775)	(1,518,981)
Net Program Costs—Other Activity	1,030,115	5,081	517	431,572	1,467,285
Net Cost of Operations (+/-)	**$ 143,789**	**$ (208,408)**	**$ 143,419**	**$ (225,234)**	**$ (146,434)**

Note 8. Intragovernmental Costs and Exchange Revenues (continued)

Farm Credit Administration
For the Year Ended September 30, 2005

	Office				
	Examination	Regulatory Policy	Secondary Market Oversight	Other Organizations	Total
Safety and Soundness (S&S)					
Intragovernmental Costs	$ 2,507,090	$ 379,541	$ 69,492	$ 5,148,157	$ 8,104,280
Public Costs	17,695,348	1,416,285	549,401	5,817,292	25,478,326
Total Costs—S&S	20,202,438	1,795,826	618,893	10,965,449	33,582,606
Intragovernmental Earned Revenue	(299,184)	(26,595)	(9,166)	(162,390)	(497,335)
Public Earned Revenue	(18,755,955)	(1,667,246)	(574,580)	(10,180,329)	(31,178,110)
Total Revenue—S&S	(19,055,139)	(1,693,841)	(583,746)	(10,342,719)	(31,675,445)
Net Program Costs—S&S	1,147,299	101,985	35,147	622,730	1,907,161
Public Mission					
Intragovernmental Costs	28,397	198,848	38,954	1,241,031	1,507,230
Public Costs	184,258	2,535,188	280,804	2,621,472	5,621,722
Total Costs—Public Mission	212,655	2,734,036	319,758	3,862,503	7,128,952
Intragovernmental Earned Revenue	(3,150)	(40,489)	(4,735)	(57,201)	(105,575)
Public Earned Revenue	(196,770)	(2,529,802)	(295,872)	(3,573,971)	(6,596,415)
Total Revenue—Public Mission	(199,920)	(2,570,291)	(300,607)	(3,631,172)	(6,701,990)
Net Program Costs—Public Mission	12,735	163,745	19,151	231,331	426,962
Other Activity					
Intragovernmental Costs	195,111	24,206	-	270,947	490,264
Public Costs	1,586,075	1,878	-	31,133	1,619,086
Total Costs—Other Activity	1,781,186	26,084	-	302,080	2,109,350
Intragovernmental Earned Revenue	(1,225,978)	(17,953)	-	(207,920)	(1,451,851)
Public Earned Revenue	(142,431)	(2,086)	-	(24,154)	(168,671)
Total Revenue—Other Activity	(1,368,409)	(20,039)	-	(232,074)	(1,620,522)
Net Program Costs—Other Activity	412,777	6,045	-	70,006	488,828
Net Cost of Operations (+/-)	**$ 1,572,811**	**$ 271,775**	**$ 54,298**	**$ 924,067**	**$ 2,822,951**

The purpose of this classification of FCA's revenue and cost is to enable the Federal Government to provide consolidated financial statements, and not to match public and intragovernmental revenue with costs that are incurred to produce public and intragovernmental revenue. Please note that the intragovernmental costs relate to the source of goods and services purchased by FCA, and not to the classification of related revenue.

Note 9. Sub-Organization Program Costs/Program Costs by Segment

Farm Credit Administration
For the Year Ended September 30, 2006

	Office				
	Examination	Regulatory Policy	Secondary Market Oversight	Other Organizations	Total
Safety and Soundness					
Gross Costs	$ 18,291,134	$ 939,550	$ 565,669	$ 11,891,378	$ 31,687,731
Less: Earned Revenue	(19,148,730)	(973,107)	(474,997)	(12,374,039)	(32,970,873)
Net Program Cost	(857,596)	(33,557)	90,672	(482,661)	(1,283,142)
Public Mission					
Gross Costs	527,075	3,275,745	326,316	4,145,550	8,274,686
Less: Earned Revenue	(555,805)	(3,455,677)	(274,086)	(4,319,695)	(8,605,263)
Net Program Cost	(28,730)	(179,932)	52,230	(174,145)	(330,577)
Other Activity					
Gross Costs	2,096,525	10,341	1,053	878,347	2,986,266
Less: Earned Revenue	(1,066,410)	(5,260)	(536)	(446,775)	(1,518,981)
Net Program Cost	1,030,115	5,081	517	431,572	1,467,285
Net Cost of Operations (+/-)	**$ 143,789**	**$ (208,408)**	**$ 143,419**	**$ (225,234)**	**$ (146,434)**

Note 9. Sub-Organization Program Costs/Program Costs by Segment (continued)

Farm Credit Administration
For the Year Ended September 30, 2005

	Office				
	Examination	Regulatory Policy	Secondary Market Oversight	Other Organizations	Total
Safety and Soundness					
Gross Costs	$ 20,202,438	$ 1,795,826	$ 618,893	$ 10,965,449	$ 33,582,606
Less: Earned Revenue	(19,055,139)	(1,693,841)	(583,746)	(10,342,719)	(31,675,445)
Net Program Cost	1,147,299	101,985	35,147	622,730	1,907,161
Public Mission					
Gross Costs	212,655	2,734,036	319,758	3,862,503	7,128,952
Less: Earned Revenue	(199,920)	(2,570,291)	(300,607)	(3,631,172)	(6,701,990)
Net Program Cost	12,735	163,745	19,151	231,331	426,962
Other Activity					
Gross Costs	1,781,186	26,084	-	302,080	2,109,350
Less: Earned Revenue	(1,368,409)	(20,039)	-	(232,074)	(1,620,522)
Net Program Cost	412,777	6,045	-	70,006	488,828
Net Cost of Operations (+/-)	**$ 1,572,811**	**$ 271,775**	**$ 54,298**	**$ 924,067**	**$ 2,822,951**

Note 10. Prior Period Adjustments

FY 2006

There were no prior period adjustments during FY 2006.

FY 2005

In FY 2005, prior period adjustments were made for the following:

Represents an expenditure refund adjustment against a prior year write-off of an accounts receivable	$ 9
Represents depreciation expense adjustments for the net excess amounts recorded in FY 2004	9,667
Represents the prior year gain realized for the trade-in of a capitalized property item	1,000
Total	**$ 10,676**

Note 11. Federal Employee Benefits

	2006	2005
Imputed Pension Cost	$ 885,762	$ 982,912
Other Imputed Retirement Benefits	1,215,497	1,243,993
Total	**$ 2,101,259**	**$ 2,226,905**

Retirement—FCA employees are covered under the Civil Service Retirement System (CSRS) and the Federal Employees Retirement System (FERS) to which FCA makes contributions according to plan requirements. CSRS and FERS are multiemployer plans. FCA does not maintain or report information about the assets of the plan, nor does it report actuarial data for accumulated plan benefits. The reporting of such amounts is the responsibility of the Office of Personnel Management (OPM). FCA reports the amount of its pension expense for employees in accordance with SFFAS No. 5 (see Note 1). When the amount of the payment expense remitted to OPM is less than the full cost to the Government, an imputed cost is recognized. The above imputed costs represent the amounts recognized by FCA for FYs 2006 and 2005. Corresponding amounts of imputed revenue are recorded to offset the imputed cost.

Other Retirement Benefit Expenses—SFFAS No. 5 (see Note 1) requires employing Federal agencies to recognize an expense for the cost of providing health benefits and life insurance to its employees after they retire. Factors used to calculate these costs were provided by OPM to meet this requirement. As with pension payments, imputed costs are recognized when amounts remitted for health benefits and life insurance are less than the full cost to the Government. Corresponding amounts of imputed revenue are recorded to offset the imputed cost.

Note 12. Rent

	2006	2005
Leased Field Offices	$ 658,928	$ 690,009
FCA Headquarters	636,667	830,700
Total	**$ 1,295,595**	**$ 1,520,709**

In accordance with the Act, FCA occupies buildings owned and leased by the FCSBA. The FCA administrative headquarters building and land are located in McLean, Virginia. In addition, the FCSBA leases office space for field offices on behalf of FCA at various locations throughout the United States. Rent is provided at no cost to FCA. The above imputed rent expense is an estimate based on the FCSBA actual results of operations for the 12 months ended December 31, 2005.

In accordance with SFFAS No. 4 (see Note 1), the rent expense and the associated imputed revenue are recorded as a nonmonetary transaction. The full cost of the rent expense is calculated by subtracting the amount of rental income received from commercial tenants renting office space from the gross operating expenses of the FCSBA. The lease expenses for the field offices are included in FCSBA's gross operating expenses.

Note 13. Budgetary Resources

FY 2006

The 2008 Budget of the United States Government, with the Actual Column completed for FY 2006, has not yet been published as of the date of these financial statements. The Budget is expected to be published and delivered to Congress in early February 2007.

FY 2005

The 2007 Budget of the U.S. Government, with the Actual Column completed for 2005, has been reconciled, and there are no significant differences.

Note 14. Undelivered Orders at the End of the Period

Beginning with FY 2006, the format of the Statement of Budgetary Resources has changed and the amount of undelivered orders at the end of the period is no longer required to be reported on the face of the statement. The SFFAS No. 7, Accounting for Revenue and Other Financing Sources and Concepts for Reconciling Budgetary and Financial Accounting, states that the amount of budgetary resources obligated for undelivered orders at the end of the period should be disclosed. For the years ended September 30, 2006 and 2005, undelivered orders amounted to $1,940,172 and $1,885,491, respectively.

REQUIRED SUPPLEMENTAL INFORMATION

Intragovernmental Assets

As of September 30, 2006

Agency	Fund Balance with Treasury	Investments	Accounts Receivable	Prepaid Expenses
U.S. Department of the Treasury	$1,782,919	$22,518,887	$ -	$ -
Consumer Product Safety Commission	-	-	17	-
FCS Insurance Corporation	-	-	7,560	-
Federal Trade Commission	-	-	35	-
Library of Congress	-	-	-	7,830
National Archives and Records Administration	-	-	121	-
National Credit Union Administration	-	-	69	-
National Endowment for the Arts	-	-	35	-
Small Business Administration	-	-	98,870	-
U.S. Department of Agriculture	-	-	194,191	-
U.S. Government Printing Office	-	-	17	-
U.S. International Trade Commission	-	-	35	-
U.S. Postal Service	-	-	531	-
Total	**$1,782,919**	**$22,518,887**	**$301,481**	**$7,830**

REQUIRED SUPPLEMENTAL INFORMATION (continued)

Intragovernmental Assets

As of September 30, 2005

Agency	Fund Balance with Treasury	Investments	Accounts Receivable	Prepaid Expenses
U.S. Department of the Treasury	$1,195,445	$18,980,498	$ 8,470	$ –
Small Business Administration	–	–	72,729	–
U.S. Department of Agriculture	–	–	55,241	–
Library of Congress	–	–	–	14,167
FCS Insurance Corporation	–	–	6,325	–
U.S. Postal Service	–	–	531	–
Total	**$1,195,445**	**$18,980,498**	**$ 143,296**	**$14,167**

REQUIRED SUPPLEMENTAL INFORMATION (continued)

Intragovernmental Liabilities

As of September 30, 2006

Agency	Accrued Post-Employment Compensation	Advances from Others	Employer Contributions and Payroll Taxes Payable
U.S. Department of Agriculture	$ -	$ 3,363	$ -
Office of Personnel Management	-	-	154,887
Social Security Administration (Treasury General Fund)	-	-	50,375
U.S. Department of Labor	34,041	-	-
Total	**$ 34,041**	**$ 3,363**	**$ 205,262**

REQUIRED SUPPLEMENTAL INFORMATION (continued)

Intragovernmental Liabilities

As of September 30, 2005

Agency	Accounts Payable	Accrued Post-Employment Compensation	Advances from Others	Accrued Taxes Payable	Employer Contributions and Payroll Taxes Payable
U.S. Department of Agriculture	$ 1,500	$ –	$ 3,363	$ –	$ –
Office of Personnel Management	–	–	–	–	151,024
Social Security Administration (Treasury General Fund)	–	–	–	–	45,053
U.S. Department of Labor	–	30,870	–	–	–
U.S. Department of the Interior	126,037	–	–	–	–
Federal Deposit Insurance Corporation	1,320	–	–	–	–
Treasury—Internal Revenue Service	–	–	–	1,490	–
U.S. Department of the Treasury	425	–	–	–	–
Total	**$ 129,282**	**$ 30,870**	**$ 3,363**	**$ 1,490**	**$ 196,077**

Additional Information

The *Farm Credit Administration Performance and Accountability Report Fiscal Year 2006* is now available on FCA's Web site at *www.fca.gov.* While supplies last, printed copies of this publication and earlier editions may be obtained without charge from

Office of Congressional and Public Affairs
Farm Credit Administration
1501 Farm Credit Drive
McLean, VA 22102-5090
Telephone: 703-883-4056
Fax: 703-790-3260
E-mail: *info-line@fca.gov*

The Federal Farm Credit Banks Funding Corporation prepares the financial press releases, the System's Annual and Quarterly Information Statements, and the System's combined financial statements contained therein, with the support of the System banks. Copies are available on the Funding Corporation's Web site at *www.farmcredit-ffcb.com* or from

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

The Farm Credit System Insurance Corporation publishes an annual report. Copies are available on FCSIC's Web site at *www.fcsic.gov* or from

Farm Credit System Insurance Corporation
1501 Farm Credit Drive
McLean, VA 22102
Telephone: 703-883-4380

In addition, FCS banks and associations are required by regulation to prepare annual and quarterly financial reports. Copies of these documents are available for public inspection at FCA headquarters in McLean, Virginia.

Copies Are Available From:
Office of Congressional and Public Affairs
Farm Credit Administration
1501 Farm Credit Drive
McLean, VA 22102-5090
703-883-4056
www.fca.gov