


# SECOND QUARTER 2009

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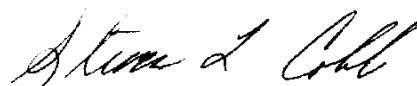
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## CERTIFICATION

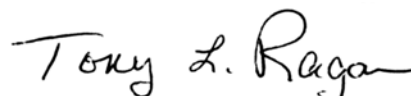
The undersigned certify that we have reviewed the June 30, 2009 quarterly report of Carolina Farm Credit, ACA, that the report has been prepared under the oversight of the Audit Committee of the Board of Directors and in accordance with all applicable statutory or regulatory requirements, and that the information contained herein is true, accurate, and complete to the best of our knowledge and belief.



Michael R. Morton  
Chief Executive Officer



Steven L. Cobb  
Chief Information and Technology Officer



Tony L. Ragan  
Chairman of the Board

July 30, 2009

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*Carolina Farm Credit, ACA*

# Report on Internal Control Over Financial Reporting

The Association's principal executives and principal financial officers, or persons performing similar functions, are responsible for establishing and maintaining adequate internal control over financial reporting for the Association's Consolidated Financial Statements. For purposes of this report, "internal control over financial reporting" is defined as a process designed by, or under the supervision of the Association's principal executives and principal financial officers, or persons performing similar functions, and effected by its Board of Directors, management and other personnel. This process provides reasonable assurance regarding the reliability of financial reporting information and the preparation of the Consolidated Financial Statements for external purposes in accordance with accounting principles generally accepted in the United States of America.

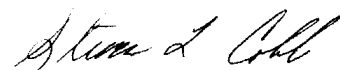
Internal control over financial reporting includes those policies and procedures that: (1) pertain to the maintenance of records that in reasonable detail accurately and fairly reflect the transactions and dispositions of the assets of the Association, (2) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial information in accordance with accounting principles generally accepted in the United States of America, and that receipts and expenditures are being made only in accordance with authorizations of management and directors of the Association, and (3) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use or disposition of the Association's assets that could have a material effect on its Consolidated Financial Statements.

The Association's management has completed an assessment of the effectiveness of internal control over financial reporting as of June 30, 2009. In making the assessment, management used the framework in *Internal Control — Integrated Framework*, promulgated by the Committee of Sponsoring Organizations of the Treadway Commission, commonly referred to as the "COSO" criteria.

Based on the assessment performed, the Association concluded that as of June 30, 2009, the internal control over financial reporting was effective based upon the COSO criteria. Additionally, based on this assessment, the Association determined that there were no material weaknesses in the internal control over financial reporting as of June 30, 2009



Michael Morton  
Chief Executive Officer



Steven L. Cobb  
Chief Information and Technology Officer

July 30, 2009

# Management's Discussion and Analysis of Financial Condition and Results of Operations

*(dollars in thousands)*

The following commentary reviews the financial condition and results of operations of Carolina Farm Credit, ACA (Association) for the period ended June 30, 2009. These comments should be read in conjunction with the accompanying consolidated financial statements, notes to the consolidated financial statements and the 2008 Annual Report of the Association. The accompanying consolidated financial statements were prepared under the oversight of the Audit Committee of the Board of Directors.

## **LOAN PORTFOLIO**

The Association provides funds to farmers, rural homeowners and farm-related businesses for financing of short and intermediate-term loans and long-term real estate mortgage loans. The Association's loan portfolio is diversified over a range of agricultural commodities in our region, including part-time farm, poultry, and rural home loans. Farm size varies and many of the borrowers in the region have diversified farming operations. This factor, along with the numerous opportunities for non-farm income in the area, reduces the dependency on a single agricultural commodity.

The gross loan volume of the Association as of June 30, 2009, was \$1,205,251, a decrease of \$98,527 as compared to \$1,303,778 at December 31, 2008. Net loans outstanding at June 30, 2009, were \$1,193,579 as compared to \$1,293,521 at December 31, 2008. Net loans accounted for 89.40 percent of total assets at June 30, 2009, as compared to 89.29 percent of total assets at December 31, 2008. The decrease in loan volume is the result of significant sales of loans to the AgFirst Farm Credit Bank (AgFirst) during the first quarter of 2009.

There is an inherent risk in the extension of any type of credit. Portfolio credit quality continues to be maintained at an acceptable level, however, and credit administration remains satisfactory.

Nonaccrual loans increased from \$45,043 at December 31, 2008, to \$50,989 at June 30, 2009. This increase is primarily the result of transfers of loan volume to nonaccrual being more than regular payments made on nonaccrual loans, along with nonaccrual loans liquidated or reinstated to accrual status.

Association management maintains an allowance for loan losses in an amount considered sufficient to absorb possible losses in the loan portfolio based on current and expected future conditions. The allowance for loan losses at June 30, 2009, was \$11,672 compared to \$10,257 at December 31, 2008, and was considered by management to be adequate to cover probable losses.

## **RESULTS OF OPERATIONS**

### ***For the three months ended June 30, 2009***

Net income for the three months ended June 30, 2009, totaled \$2,123, as compared to \$7,547 for the same period in 2008. Net interest income decreased \$1,199, for the three months ended June 30, 2009, as compared to the same period in 2008.

At June 30, 2009, total interest income decreased \$4,853 compared to June 30, 2008. Nonaccrual income was \$100 for the three months ended June 30, 2009, as compared to \$165 for the same period in 2008. Interest expense decreased \$3,654 for the three months ended June 30, 2009, as compared to the comparable period of 2008.

The Association recorded a provision for loan losses of \$4,770 for the three months ended June 30, 2009 as compared to a reversal of \$150 for the same period of 2008.

Noninterest income for the three months ended June 30, 2009, totaled \$4,829, as compared to \$4,121 for the same period of 2008, an increase of \$708. This rise in earnings is attributed to an increase of \$713 in equity in earnings of other Farm Credit institutions, \$97 in loans fees, \$31 in fees for financially related services, and \$23 in other noninterest income when compared to the same period in 2008. These increases were offset by decreases of \$111 in losses on other property owned, and \$45 in gains on sale of rural home loans when compared for the same period of 2008.

Noninterest expense for the three months ended June 30, 2009, decreased \$17 compared to the same period of 2008. This decline in noninterest expense is attributed to a decrease of \$18 in occupancy and equipment, and \$91 in other operating expenses when compared to the same period in 2008. These decreases were offset by increases of \$41 in salaries and employee benefits and \$51 in the insurance fund premium when compared for the same period of 2008.

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The Association recorded a provision for income taxes of \$35 for the three months ended June 30, 2009 as compared to a provision of \$5 for the same period of 2008.

***For the six months ended June 30, 2009***

Net income for the six months ended June 30, 2009, totaled \$6,912, as compared to \$11,430 for the same period in 2008. This decrease of \$4,518, or 39.53 percent, is attributed to a sizable provision to the allowance for loan loss account and a decline in net interest income.

At June 30, 2009, total interest income decreased \$10,260 compared to June 30, 2008. Nonaccrual income was \$152 for the six months ended June 30, 2009, as compared to \$263 for the same period in 2008. Interest expense decreased \$8,384 for the six months ended June 30, 2009, as compared to the same period in 2008. Both interest income and interest expense have decreased due to the lower interest rate environment, but also from the significant sales of loans to AgFirst during the first quarter of 2009.

The Association recorded a provision for loan losses of \$6,440 for the six months ended June 30, 2009 as compared to a provision of \$4,450 for the same period of 2008. This increased provision for loan losses is related to the increase in nonaccrual loans and the weakening of the general economy.

Noninterest income for the six months ended June 30, 2009, totaled \$9,421, as compared to \$8,199 for the same period of 2008, an increase of \$1,222. The rise in earnings is attributed to an increase of \$236 in loan fees, \$1,452 in equity in earnings of other Farm Credit institutions and \$31 in the gains on sale of rural home loans when compared to the same period in 2008. These increases were offset by a decrease of \$2 in fees for financially related services, \$75 in the gains on other property owned, and \$420 in other noninterest income when compared to the same period in 2008.

Noninterest expense for the six months ended June 30, 2009, increased \$1,846 compared to the same period of 2008. This rise in noninterest expense is attributed to an increase of \$1,763 in salaries and employee benefits, \$5 in occupancy and equipment, and \$98 in the insurance fund premium when compared to the same period in 2008. The increases were offset by a decrease of \$20 in other operating expenses when compared for the same period of 2008.

The Association recorded a provision for income taxes of \$34 for the six months ended June 30, 2009 as compared to a provision of \$6 for the same period of 2008.

## **FUNDING SOURCES**

The principal source of funds for the Association is the borrowing relationship established with AgFirst through a General Financing Agreement. The General Financing Agreement utilizes the Association's credit and fiscal performance as criteria for establishing a line of credit on which the Association may draw funds. The funds are advanced by the Bank to the Association in the form of notes payable. The notes payable is segmented into variable rate and fixed rate sections. The variable rate note is utilized by the Association to fund variable rate loan advances and operating funds requirements. The fixed rate note is used specifically to fund fixed rate loan advances made by the Association. The total notes payable to the Bank at June 30, 2009, was \$1,095,467 as compared to \$1,206,784 at December 31, 2008. The decrease in notes payable is the result of significant sales of loans to AgFirst during the first quarter of 2009.

The Association has no lines of credit outstanding with third parties as of June 30, 2009.

## **CAPITAL RESOURCES**

Total members' equity at June 30, 2009, increased to \$218,425 from the December 31, 2008, total of \$211,894. The change in capital is attributed to net earnings for the six months ending June 30, 2009.

Farm Credit administration (FCA) regulations require all Farm Credit institutions to maintain minimum permanent capital, total surplus and core surplus ratios. These ratios are calculated by dividing the Association's permanent capital, total surplus and core surplus as defined in FCA regulations, by a risk-adjusted asset base. As of June 30, 2009, the Association's total surplus ratio and core surplus ratio were 14.22 percent and 11.46 percent, respectively, and the permanent capital ratio was 14.85 percent. All three ratios were well above the minimum regulatory ratios of 7.00 percent for permanent capital and total surplus ratios and 3.50 percent for the core surplus ratio.

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**NOTE:** Shareholder investment in the Association could be affected by the financial condition and results of operations of AgFirst Farm Credit Bank. Copies of AgFirst's annual and quarterly reports are available upon request free of charge by calling 1-800-845-1745, ext. 378, or writing Stephen Gilbert AgFirst Farm Credit Bank, P.O. Box 1499, Columbia, SC 29202. Information concerning AgFirst Farm Credit Bank can also be obtained at their website, [www.agfirst.com](http://www.agfirst.com). Copies of the Association's annual and quarterly reports are also available upon request free of charge by calling 1-800-521-9952, or writing Michael R. Morton, CEO, Carolina Farm Credit, ACA, P.O. Box 1827, Statesville NC 28687-1827, or accessing the website, [www.carolinafarmcredit.com](http://www.carolinafarmcredit.com). The Association prepares a quarterly report within 40 days after the end of each fiscal quarter, except that no report need be prepared for the fiscal quarter that coincides with the end of the fiscal year of the institution.

Carolina Farm Credit, ACA  
**Consolidated Balance Sheets**

<i>(dollars in thousands)</i>	<b>June 30, 2009</b> <i>(unaudited)</i>	<b>December 31, 2008</b> <i>(audited)</i>
<b>Assets</b>		
Cash	\$ 640	\$ 2,121
Loans	1,205,251	1,303,778
Less: allowance for loan losses	11,672	10,257
Net loans	1,193,579	1,293,521
Other investments	53,239	63,801
Accrued interest receivable	12,705	15,030
Investment in other Farm Credit institutions	36,924	29,463
Premises and equipment, net	16,531	15,925
Other property owned	741	1,032
Due from AgFirst Farm Credit Bank	6,991	11,966
Other assets	13,711	15,816
Total assets	\$ 1,335,061	\$ 1,448,675
<b>Liabilities</b>		
Notes payable to AgFirst Farm Credit Bank	\$ 1,095,467	\$ 1,206,784
Accrued interest payable	3,180	4,248
Patronage refund payable	354	5,249
Other liabilities	17,635	20,500
Total liabilities	1,116,636	1,236,781
Commitments and contingencies		
<b>Members' Equity</b>		
Protected borrower equity	193	234
Capital stock and participation certificates	7,689	7,734
Retained earnings		
Allocated	104,681	104,671
Unallocated	105,991	99,384
Accumulated other comprehensive income (loss)	(129)	(129)
Total members' equity	218,425	211,894
Total liabilities and members' equity	\$ 1,335,061	\$ 1,448,675

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

Carolina Farm Credit, ACA

# Consolidated Statements of Income

*(unaudited)*

<i>(dollars in thousands)</i>	For the three months ended June 30,		For the six months ended June 30,	
	2009	2008	2009	2008
<b>Interest Income</b>				
Loans	\$ 17,442	\$ 22,073	\$ 37,107	\$ 47,159
Other	716	938	1,432	1,640
Total interest income	18,158	23,011	38,539	48,799
<b>Interest Expense</b>				
Notes payable to AgFirst Farm Credit Bank	9,682	13,336	20,767	29,151
Net interest income	8,476	9,675	17,772	19,648
Provision for (reversal of allowance for) loan losses	4,770	(150)	6,440	4,450
Net interest income after provision for (reversal of allowance for) loan losses	3,706	9,825	11,332	15,198
<b>Noninterest Income</b>				
Loan fees	758	661	1,569	1,333
Fees for financially related services	114	83	272	274
Equity in earnings of other Farm Credit institutions	3,789	3,076	7,036	5,584
Gains (losses) on other property owned, net	(113)	(2)	(148)	(73)
Gains (losses) on sale of rural home loans, net	165	210	387	356
Other noninterest income	116	93	305	725
Total noninterest income	4,829	4,121	9,421	8,199
<b>Noninterest Expense</b>				
Salaries and employee benefits	4,076	4,035	9,134	7,371
Occupancy and equipment	618	636	1,277	1,272
Insurance Fund premium	490	439	991	893
Other operating expenses	1,193	1,284	2,405	2,425
Total noninterest expense	6,377	6,394	13,807	11,961
Income before income taxes	2,158	7,552	6,946	11,436
Provision (benefit) for income taxes	35	5	34	6
Net income	\$ 2,123	\$ 7,547	\$ 6,912	\$ 11,430

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

Carolina Farm Credit, ACA

# Consolidated Statements of Changes in Members' Equity

*(unaudited)*

*(dollars in thousands)*

	Protected Borrower Capital	Capital Stock and Participation Certificates	Retained Earnings		Accumulated Other Comprehensive Income	Total Members' Equity
			Allocated	Unallocated		
Balance at December 31, 2007	\$ 327	\$ 7,899	\$ 100,372	\$ 95,087	\$ (314)	\$ 203,371
Comprehensive income						
Net income				11,430		11,430
Employee benefit plans adjustments				(43)	72	29
Total comprehensive income						11,459
Protected borrower equity retired	(90)					(90)
Capital stock/participation						
certificates issued/(retired), net		(64)				(64)
Retained earnings retired			(2)			(2)
Patronage distribution adjustment			602	(671)		(69)
Balance at June 30, 2008	\$ 237	\$ 7,835	\$ 100,972	\$ 105,803	\$ (242)	\$ 214,605
Balance at December 31, 2008	\$ 234	\$ 7,734	\$ 104,671	\$ 99,384	\$ (129)	\$ 211,894
Net income				6,912		6,912
Protected borrower equity retired	(41)					(41)
Capital stock/participation						
certificates issued/(retired), net		(45)				(45)
Patronage distribution adjustment			10	(305)		(295)
Balance at June 30, 2009	\$ 193	\$ 7,689	\$ 104,681	\$ 105,991	\$ (129)	\$ 218,425

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

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Carolina Farm Credit, ACA

# Notes to the Consolidated Financial Statements

(dollars in thousands, except as noted)  
(unaudited)

## NOTE 1 – ORGANIZATION, SIGNIFICANT ACCOUNTING POLICIES, AND RECENTLY ISSUED ACCOUNTING PRONOUNCEMENTS

The accompanying financial statements include the accounts of Carolina Farm Credit, ACA (the Association). A description of the organization and operations of the Association, the significant accounting policies followed, and the financial condition and results of operations as of and for the year ended December 31, 2008, are contained in the 2008 Annual Report to Shareholders. These unaudited second quarter 2009 consolidated financial statements should be read in conjunction with the 2008 Annual Report to Shareholders.

The accompanying consolidated financial statements contain all adjustments necessary for a fair presentation of the interim financial condition and results of operations and conform with generally accepted accounting principles (GAAP) and prevailing practices within the banking industry. The results for the six months ended June 30, 2009, are not necessarily indicative of the results to be expected for the year ending December 31, 2009.

Certain amounts in the prior period's consolidated financial statements may have been reclassified to conform to the current period's consolidated financial statement presentation. Such reclassifications had no effect on the prior period net income or total capital as previously reported.

The Association maintains an allowance for loan losses in accordance with GAAP. The loan portfolio is reviewed quarterly to determine the adequacy of the allowance for losses. As of June 30, 2009, the allowance for losses is adequate in management's opinion to provide for possible losses on existing loans.

In addition to the recently issued accounting pronouncements discussed in the 2008 Annual Report to Shareholders, effective January 1, 2009, the Association adopted Financial Accounting Standards Board (FASB) Statement of Position (FSP) No. 157-2, "Effective Date of FASB Statement No. 157." This FSP delayed the effective date of Statement No. 157 for nonfinancial assets and nonfinancial liabilities until fiscal years beginning after November 15, 2008. The impact of adoption requires additional fair value disclosures (see Note 4), primarily

regarding other property owned, but does not have an impact on the Association's financial condition or results of operations.

In April 2009, the FASB issued FSP No. 107-1 and Accounting Principles Board (APB) No. 28-1, "Interim Disclosures about Fair Value of Financial Instruments." This FSP requires disclosures about fair value of financial instruments for interim reporting periods of publicly traded companies as well as in annual financial statements. The FSP is effective for interim periods ending after June 15, 2009 (see Note 5).

In May 2009, the FASB issued SFAS No. 165, "Subsequent Events," which sets forth general standards of accounting for and disclosure of events that occur after the balance sheet date but before financial statements are issued or are available to be issued. Recognized subsequent events should be recognized in the financial statements since the conditions existed at the date of the balance sheet. Nonrecognized subsequent events are not recognized in the financial statements since the conditions arose after the balance sheet date but before the financial statements are issued or are available to be issued. This Standard, which includes a required disclosure of the date through which an entity has evaluated subsequent events, is effective for interim or annual periods ending after June 15, 2009 (see Note 6).

## NOTE 2 – ALLOWANCE FOR LOAN LOSSES AND IMPAIRED LOANS

An analysis of the allowance for loan losses follows:

	For the six months ended June 30,	
	2009	2008
Balance at beginning of period	\$ 10,257	\$ 4,287
Provision for (reversal of) loan losses	6,440	4,450
Charge-offs	(5,049)	(130)
Recoveries	24	40
Balance at end of period	<u>\$ 11,672</u>	<u>\$ 8,647</u>

The following table presents information concerning impaired loans as of June 30,

	<u>2009</u>	<u>2008</u>
Impaired loans with related allowance	\$ 26,755	\$ 16,084
Impaired loans with no related allowance	24,234	16,842
Total impaired loans	<u>50,989</u>	<u>32,926</u>
Allowance on impaired loans	<u>\$ 8,034</u>	<u>\$ 5,846</u>

The following table summarizes impaired loan information for the six months ended June 30,

	<u>2009</u>	<u>2008</u>
Average impaired loans	\$ 48,504	\$ 24,616
Interest income recognized on impaired loans	159	275

### NOTE 3 – EMPLOYEE BENEFIT PLANS

The following is a table of retirement and other postretirement benefit expenses for the Association:

	<b>For the six months ended June 30,</b>	
	<u>2009</u>	<u>2008</u>
Pension	\$ 2,438	\$ 517
401(k)	189	193
Other postretirement benefits	478	419
Total	<u>\$ 3,105</u>	<u>\$1,129</u>

The following is a table of retirement and other postretirement benefit contributions for the Association:

	<b>Actual YTD Through 6/30/09</b>	<b>Projected Contributions For Remainder of 2009</b>	<b>Projected Total Contributions 2009</b>
Pension	\$ 18	\$ 18	\$ 36
Other postretirement benefits	308	358	666
Total	<u>\$ 326</u>	<u>\$ 376</u>	<u>\$ 702</u>

Actuarial calculations as of the last plan measurement date (December 31, 2008) projected contributions of \$36 to the pension plan for 2009. However, market conditions could impact discount rates and return on plan assets which could make additional contributions necessary before the next plan measurement date of December 31, 2009.

Further details regarding employee benefit plans are contained in the 2008 Annual Report to Shareholders.

### NOTE 4 – FAIR VALUE MEASUREMENT

Effective January 1, 2008, the Association adopted Statement of Financial Accounting Standards No. 157, "Fair Value Measurements" (SFAS No. 157). This Statement defines fair value, establishes a framework for measuring fair value and expands disclosures about fair value measurements for certain assets and liabilities measured at fair value on a recurring and non-recurring basis. These assets and liabilities primarily consist of assets held in trust funds, standby letters of credit, impaired loans, and other property owned.

SFAS No. 157 defines fair value as the exchange price that would be received for an asset or paid to transfer a liability in an orderly transaction between market participants in the principal or most advantageous market for the asset or liability.

SFAS No. 157 establishes a fair value hierarchy for disclosure of fair value measurements to maximize the use of observable inputs, that is, inputs that reflect the assumptions market participants would use in pricing an asset or liability based on market data obtained from sources independent of the reporting entity. The valuation hierarchy is based upon the transparency of inputs to the valuation of an asset or liability as of the measurement date. A financial instrument's categorization within the valuation hierarchy is based upon the lowest level of input that is significant to the fair value measurement.

The three levels of inputs and the classification of the Association's financial instruments within the fair value hierarchy are as follows:

#### Level 1

Level 1 inputs to the valuation methodology are unadjusted quoted prices for identical assets or liabilities in active markets. The Association's Level 1 assets at June 30, 2009 consist of assets held in trust funds related to deferred compensation and supplemental retirement plans. The trust funds include investments in securities that are actively traded and have quoted net asset value prices that are directly observable in the marketplace.

#### Level 2

Level 2 inputs to the valuation methodology include quoted prices for similar assets and liabilities in active markets; quoted prices in markets that are not active; and inputs that are observable, or can be corroborated, for substantially the full term of the asset or liability. The Association has no Level 2 assets and liabilities measured at fair value on a recurring basis at June 30, 2009.

### Level 3

Level 3 inputs to the valuation methodology are unobservable and supported by little or no market activity. Valuation is determined using pricing models, discounted cash flow methodologies, or similar techniques, and could include significant management judgment or estimation. Level 3 assets and liabilities also could include instruments whose price has been adjusted based on dealer quoted pricing that is different than the third-party valuation or internal model pricing.

Level 3 assets at June 30, 2009 include impaired loans which represent the fair value of certain loans that were evaluated for impairment under SFAS No. 114. The fair value was based upon the underlying collateral since these were collateral-dependent loans. The fair value measurement process uses independent appraisals and other market-based information, but in many cases it also requires significant input based on management's knowledge of and judgment about current market conditions, specific issues relating to the collateral and other matters. As a result, these fair value measurements fall within Level 3 of the hierarchy. When the value of the collateral, less estimated costs to sell, is less than the principal balance of the loan, a specific reserve is established. Other property owned is classified as a level 3 asset at June 30, 2009. The fair value for other property owned is based upon the collateral less estimated costs to sell. Level 3 liabilities at June 30, 2009 include standby letters of credit whose market value is internally calculated based on information that is not observable either directly or indirectly in the marketplace.

### Assets and Liabilities Measured at Fair Value on a Recurring Basis

The following table presents the assets and liabilities that are measured at fair value on a recurring basis at June 30, 2009 for each of the fair value hierarchy levels:

	June 30, 2009			
	Level 1	Level 2	Level 3	Total Fair Value
<b>Assets:</b>				
Assets held in trust funds	\$ 137	\$ -	\$ -	\$ 137
Total Assets	\$ 137	\$ -	\$ -	\$ 137
<b>Liabilities:</b>				
Standby letters of credit	\$ -	\$ -	\$ 239	\$ 239
Total Liabilities	\$ -	\$ -	\$ 239	\$ 239

The following table presents the changes in Level 3 assets and liabilities measured at fair value on a recurring basis:

	Standby Letters Of Credit
Balance at January 1, 2009	\$ 267
<b>Total gains or (losses) realized/unrealized:</b>	
Included in earnings	-
Included in other comprehensive loss	-
Purchases, sales, issuances and settlements, net	(28)
Transfers in and/or out of level 3	-
Balance at June 30, 2009	\$ 239

### Assets and Liabilities Measured at Fair Value on a Non-recurring Basis

Assets and liabilities measured at fair value on a non-recurring basis at June 30, 2009 for each of the fair value hierarchy values are summarized below:

	June 30, 2009				
	Level 1	Level 2	Level 3	Total Fair Value	YTD Total Gains (Losses)
<b>Assets:</b>					
Impaired loans	\$ -	\$ -	\$ 18,721	\$ 18,721	\$ (6,492)
Other property owned	\$ -	\$ -	\$ 741	\$ 741	\$ (160)

### NOTE 5 — DISCLOSURES ABOUT FAIR VALUE OF FINANCIAL INSTRUMENTS AND FAIR VALUE MEASUREMENTS

The following table presents the carrying amounts and fair values of the Association's financial instruments at June 30, 2009. The fair value of a financial instrument is generally defined as the amount at which the instrument could be exchanged in a current transaction between willing parties, other than in a forced or liquidation sale.

Quoted market prices are generally not available for certain System financial instruments, as described below. Accordingly fair values are based on judgments regarding anticipated cash flows, future expected loss experience, current economic conditions, risk characteristics of various financial instruments, and other factors. These estimates involve uncertainties and matters of judgment, and therefore cannot be determined with precision. Changes in assumptions could significantly affect the estimates.

The estimated fair values of the Association's financial instruments are as follows:

	<b>June 30, 2009</b>	
	<b>Carrying Amount</b>	<b>Estimated Fair Value</b>
<b>Financial assets:</b>		
Cash	\$ 640	\$ 640
Loans, net of allowance	\$ 1,193,579	\$ 1,222,902
Tobacco Buyout SIIC	\$ 53,239	\$ 55,621
Assets held in trust funds	\$ 137	\$ 137
<b>Financial liabilities:</b>		
Notes payable to AgFirst Farm Credit Bank	\$ 1,095,467	\$ 1,116,116

A description of the methods and assumptions used to estimate the fair value of each class of the Association's financial instruments for which it is practicable to estimate that value follows:

- A. **Cash:** The carrying value is a reasonable estimate of fair value.
- B. **Loans:** Because no active market exists for the Association's loans, fair value is estimated by discounting the expected future cash flows using the Association's current interest rates at which similar loans would be made to borrowers with similar credit risk. As the discount rates are based on the Bank's loan rates, as well as management estimates, management has no basis to determine whether the fair values presented would be indicative of the value negotiated in an actual sale. For purposes of determining fair value of accruing loans, the loan portfolio is segregated into pools of loans with homogeneous characteristics based upon repricing and credit risk. Expected future cash flows and interest rates reflecting appropriate credit risk are separately determined for each individual pool.

Fair value of loans in a nonaccrual status is estimated to be the carrying amount less specific reserves.

The carrying value of accrued interest approximates its fair value.

- C. **Investment in AgFirst Farm Credit Bank and Other Farm Credit Institutions:** Estimating the fair value of the Association's investment in the Bank and Other Farm Credit Institutions is not practicable because the stock is not traded. The net investment is a requirement of borrowing from the Bank and is carried at cost plus allocated equities in the accompanying Consolidated Balance Sheets. The Association owns 9.48 percent of the issued stock of the Bank as of June 30, 2008 net of any reciprocal investment. As of that date, the Bank's

assets totaled \$30.0 billion and shareholders' equity totaled \$1.5 billion. The Bank's earnings were \$116 million during the first six months of 2009.

In addition, the Association has an investment of \$435 related to other Farm Credit institutions.

- D. **Notes Payable to AgFirst Farm Credit Bank:** The notes payable are segregated into pricing pools according to the types and terms of the loans (or other assets) which they fund. Fair value of the notes payable is estimated by discounting the anticipated cash flows of each pricing pool using the current rate that would be charged for additional borrowings. For purposes of this estimate it is assumed the cash flow on the notes is equal to the principal payments on the Association's loan receivables plus accrued interest on the notes payable. This assumption implies that earnings on the Association's interest margin are used to fund operating expenses and capital expenditures.
- E. **Commitments to Extend Credit:** The estimated market value of off-balance-sheet commitments is minimal since the committed rate approximates current rates offered for commitments with similar rate and maturity characteristics and since the related credit risk is not significant.
- F. **Tobacco Buyout SIIC:** Fair value is determined by discounting the expected future cash flows using current interest rates for similar assets.
- G. **Assets Held in Trust Funds:** See Note 4 for discussion of estimation of fair value for this instrument.

#### **NOTE 6 – SUBSEQUENT EVENTS**

The Association has evaluated subsequent events through July 30, 2009, which is the date the financial statements were available to be issued.