

# **FIRST QUARTER 2010**

## **TABLE OF CONTENTS**

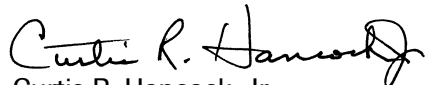
Report on Internal Control Over Financial Reporting.....	2
Management's Discussion and Analysis of Financial Condition and Results of Operations.....	3
Consolidated Financial Statements	
Consolidated Balance Sheets.....	5
Consolidated Statements of Income.....	6
Consolidated Statements of Changes in Members' Equity.....	7
Notes to the Consolidated Financial Statements.....	8

## **CERTIFICATION**

The undersigned certify that we have reviewed the March 31, 2010 quarterly report of Jackson Purchase Agricultural Credit Association, 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.



Stan Brunston  
Chief Executive Officer



Curtis R. Hancock, Jr.  
Chairman of the Board



Barbara Davis  
Chief Financial Officer



Joe F. Campbell  
Member of the Board of Directors  
Chairman of the Audit Committee

May 7, 2010

---

*Jackson Purchase Agricultural Credit Association*

# 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 March 31, 2010. 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 March 31, 2010, 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 March 31, 2010



Stan Brunston  
Chief Executive Officer



Barbara Davis  
Chief Financial Officer

May 7, 2010

# 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 Jackson Purchase, ACA (Association) for the period ended March 31, 2010. These comments should be read in conjunction with the accompanying consolidated financial statements, notes to the consolidated financial statements and the 2009 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 including corn, soybeans, poultry, and tobacco. 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, somewhat reduces the level of dependency on any single commodity.

The gross loan volume of the Association as of March 31, 2010, was \$236,087, a decrease of \$31,987, as compared to \$268,074 at December 31, 2009. Net loans outstanding at March 31, 2010, were \$234,155 as compared to \$265,004 at December 31, 2009. Net loans accounted for 91.18 percent of total assets at March 31, 2010, as compared to 90.22 percent of total assets at December 31, 2009. The decrease in gross and net loan volume during the reporting period is primarily attributable to seasonal paydown on production loans and the reduced need for additional credit due to the bountiful harvest in 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 and credit administration remains satisfactory. Nonaccrual loans decreased from \$5,870 at December 31, 2009, to \$3,073 at March 31, 2010. This decrease is primarily the result of a participation loan pay off and participation loans transferred back to accrual status.

Other property owned (OPO) consists primarily of assets once held as loan collateral that were acquired through foreclosure or deeded to the Association (or a lender group) in satisfaction of secured loans. Traditionally, OPO is primarily in the form of real estate. However, it can also include equipment and equity interests in companies or partnerships. OPO totaled \$77 at March 31, 2010, an increase of \$0, compared to December 31, 2009.

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 March 31, 2010, was \$1,932 compared to \$3,070 at December 31, 2009, and was considered by management to be adequate to cover probable losses. The decrease of \$1,138 in the allowance for loan losses was primarily the result of one participation loan chargeoff.

## **RESULTS OF OPERATIONS**

### ***For the three months ended March 31, 2010***

Net income for the three months ended March 31, 2010, totaled \$1,757, as compared to \$1,080 for the same period in 2009. Net interest income increased \$126 for the three months ended March 31, 2010, as compared to the same period in 2009. This increase in net interest income is attributed primarily to a decrease in interest expense as a result of the Association's concerted effort to effectively manage interest rates.

Noninterest income for the three months ended March 31, 2010, totaled \$1,527 as compared to \$1,052 for the same period of 2009, an increase of \$475. The increase is primarily the result of a refund from the Farm Credit System Insurance Corporation (FCSIC). Noninterest expense for the three months ended March 31, 2010, decreased \$76 compared to the same period of 2009. The primary reason for the decrease in noninterest expense resulted from a decrease in occupancy and equipment, insurance fund premium, and other operating expenses.

During the first quarter of 2010, the Association recorded \$647 of insurance premium refunds from the Farm Credit System Insurance Corporation (FCSIC), which insures the System's debt obligations. The amount is reflected in Noninterest Income on the Consolidated Statements of Income. These

---

payments are nonrecurring and resulted from the assets of the Farm Credit Insurance Fund exceeding the secure base amount as defined by the Farm Credit Act.

Nonaccrual income was \$73 for the three months ended March 31, 2010, as compared to \$6 for the same period in 2009. This increase is mainly the result of participation loans that were transferred back to accrual status. The Association recorded a provision for loan loss of \$0 for the three months ended March 31, 2010, as compared to \$0 for the same period in 2009.

### **FUNDING SOURCES**

The principal source of funds for the Association is the borrowing relationship established with AgFirst Farm Credit Bank (the Bank) 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 Bank advances funds to the Association in the form of notes payable. The notes payable are 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 and approximately 50% of the Association's own funds. The total notes payable to the Bank at March 31, 2010, was \$205,312 compared to \$241,378 at December 31, 2009.

### **CAPITAL RESOURCES**

Total members' equity at March 31, 2010, increased to \$44,698 from the December 31, 2009, total of \$42,925. The increase is primarily attributed to an increase in unallocated retained earnings.

Total capital stock and participation certificates were \$2,004 on March 31, 2010, compared to \$2,009 on December 31, 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 March 31, 2010, the Association's total surplus ratio and core surplus ratio were 16.55 percent and 14.80 percent, respectively, and the permanent capital ratio was 17.50 percent. The 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.

---

**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 (270) 247-5613, writing Barbara Davis, Chief Financial Officer, Jackson Purchase ACA, P. O. Box 309, Mayfield, KY 42066, or accessing the website, [www.jacksonpurchaseaca.com](http://www.jacksonpurchaseaca.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.

# Jackson Purchase Agricultural Credit Association

## Consolidated Balance Sheets

<i>(dollars in thousands)</i>	<b>March 31, 2010</b> <i>(unaudited)</i>	<b>December 31, 2009</b> <i>(audited)</i>
<b>Assets</b>		
Cash	\$ 615	\$ 2,503
Investment securities:		
Held to maturity (fair value of \$6,396 and \$7,143 respectively)	6,410	7,145
Loans	236,087	268,074
Less: allowance for loan losses	1,932	3,070
Net loans	234,155	265,004
Loans held for sale	481	533
Other investments	2,226	2,821
Accrued interest receivable	2,367	3,067
Investment in other Farm Credit institutions	6,381	6,539
Premises and equipment, net	1,760	1,783
Other property owned	77	77
Due from AgFirst Farm Credit Bank	716	2,941
Other assets	1,609	1,331
Total assets	\$ 256,797	\$ 293,744
<b>Liabilities</b>		
Notes payable to AgFirst Farm Credit Bank	\$ 205,312	\$ 241,378
Accrued interest payable	555	598
Patronage refund payable	30	1,383
Advanced conditional payments	2,879	2,543
Other liabilities	3,323	4,917
Total liabilities	212,099	250,819
Commitments and contingencies		
<b>Members' Equity</b>		
Capital stock and participation certificates	2,004	2,009
Retained earnings		
Allocated	18,192	18,231
Unallocated	24,502	22,685
Total members' equity	44,698	42,925
Total liabilities and members' equity	\$ 256,797	\$ 293,744

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

Jackson Purchase Agricultural Association  
**Consolidated Statements of Income**

*(unaudited)*

<i>(dollars in thousands)</i>	<b>For the three months ended March 31,</b>	
	<b>2010</b>	<b>2009</b>
<b>Interest Income</b>		
Investment securities	\$ 29	\$ 31
Loans	3,196	3,240
Other	29	34
Total interest income	3,254	3,305
<b>Interest Expense</b>		
Notes payable to AgFirst Farm Credit Bank	1,663	1,818
Other	8	30
Total interest expense	1,671	1,848
Net interest income	1,583	1,457
Provision for (reversal of allowance for) loan losses	—	—
Net interest income after provision for (reversal of allowance for) loan losses	1,583	1,457
<b>Noninterest Income</b>		
Loan fees	64	64
Fees for financially related services	57	147
Equity in earnings of other Farm Credit institutions	716	739
Gains (losses) on other property owned, net	(3)	—
Gains (losses) on sale of rural home loans, net	26	82
Insurance Fund refund	647	—
Other noninterest income	20	20
Total noninterest income	1,527	1,052
<b>Noninterest Expense</b>		
Salaries and employee benefits	963	964
Occupancy and equipment	83	93
Insurance Fund premium	43	84
Other operating expenses	264	288
Total noninterest expense	1,353	1,429
Income before income taxes	1,757	1,080
Provision (benefit) for income taxes	—	—
Net income	\$ 1,757	\$ 1,080

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

Jackson Purchase Agricultural Credit Association  
**Consolidated Statements of Changes in  
Members' Equity**

*(unaudited)*

*(dollars in thousands)*

	<b>Capital Stock and Participation Certificates</b>	<b>Retained Earnings</b>		<b>Total Members' Equity</b>
		<b>Allocated</b>	<b>Unallocated</b>	
Balance at December 31, 2008	\$ 2,015	\$ 16,553	\$ 23,804	\$ 42,372
Net income			1,080	1,080
Capital stock/participation certificates issued/(retired), net	(32)			(32)
Patronage distribution adjustment		37	(58)	(21)
Balance at March 31, 2009	<u>\$ 1,983</u>	<u>\$ 16,590</u>	<u>\$ 24,826</u>	<u>\$ 43,399</u>
Balance at December 31, 2009	\$ 2,009	\$ 18,231	\$ 22,685	\$ 42,925
Net income			1,757	1,757
Capital stock/participation certificates issued/(retired), net	(5)			(5)
Patronage distribution adjustment		(39)	60	21
Balance at March 31, 2010	<u>\$ 2,004</u>	<u>\$ 18,192</u>	<u>\$ 24,502</u>	<u>\$ 44,698</u>

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

---

*Jackson Purchase Agricultural Credit Association*

# 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 Jackson Purchase Agricultural Credit Association (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, 2009, are contained in the 2009 Annual Report to Shareholders. These unaudited first quarter 2010 consolidated financial statements should be read in conjunction with the 2009 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 three months ended March 31, 2010, are not necessarily indicative of the results to be expected for the year ending December 31, 2010.

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 March 31, 2010, 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 2009 Annual Report to Shareholders, in June 2009, the Financial Accounting Standards Board (FASB) issued guidance "Accounting for Transfers of Financial Assets," which amended previous guidance by improving the relevance, representational faithfulness, and comparability of the information that a reporting entity provides in its financial statements about a transfer of financial assets; the effects of a transfer on its financial position, financial performance, and cash flows; and a transferor's continuing involvement, if any, in transferred financial assets.

This guidance was effective as of the beginning of each reporting entity's first annual reporting period that begins after November 15, 2009, for interim periods within that first annual reporting period and for interim and annual reporting periods thereafter. Earlier application was prohibited. This guidance must be applied to transfers occurring on or after the effective date. Additionally, on and after the effective date, the concept of a qualifying special purpose entity is no longer relevant for accounting purposes. Therefore, formerly qualifying special-purpose entities (as defined under previous accounting guidance) should be evaluated for consolidation by reporting entities on and after the effective date in accordance with the applicable consolidation guidance. If the evaluation on the effective date results in consolidation, the reporting entity should apply the transition guidance that requires consolidation. The Association evaluated the impact of adoption on its loan participation agreements to ensure that participations would meet the requirements for sales treatment. The impact of adoption on January 1, 2010 was immaterial to the Association's financial condition and results of operations.

In June 2009, the FASB also issued guidance, to improve financial reporting for those enterprises involved with variable interest entities, which amends previous guidance by requiring an enterprise to perform an analysis to determine whether the enterprise's variable interest or interests give it a controlling financial interest in a variable interest entity.

Additionally, an enterprise is required to assess whether it has an implicit financial responsibility to ensure that a variable interest entity operates as designed when determining whether it has the power to direct the activities of the variable interest entity that most significantly impact the entity's economic performance.

This guidance was effective as of the beginning of each reporting entity's first annual reporting period that begins after November 15, 2009, for interim periods within that first annual reporting period and for interim and annual reporting periods thereafter. Earlier application was prohibited. The Association does not have any variable interest or controlling interest in a variable entity. Therefore, there was no impact of adoption of the guidance for the Association.

In January 2010, the FASB issued guidance "Fair Value Measurements and Disclosures," which is to improve disclosures about fair value measurement by increasing transparency in financial reporting. The changes will provide a greater level of disaggregated information and more detail

disclosures of valuation techniques and inputs to fair value measurement. The new disclosures and clarification of existing disclosures were effective for interim and annual reporting periods beginning after December 15, 2009, except for the disclosures about purchases, sales, issuances and settlements in the rollforward of activity in Level 3 fair value measurements. Those disclosures are effective for fiscal years beginning after December 15, 2010, and for interim periods within those fiscal years. The adoption of this guidance had no impact on the Association's financial condition and results of operations but resulted in additional disclosures (see Note 5).

## NOTE 2 — INVESTMENT SECURITIES

A summary of the amortized cost and fair value of investment securities held-to-maturity at March 31, 2010 and December 31, 2009 follows:

	March 31, 2010				
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value	Yield
Asset backed securities	\$ 6,410	\$ 6	\$ (20)	\$ 6,396	1.88%

	December 31, 2009				
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value	Yield
Asset backed securities	\$ 7,145	\$ 9	\$ (11)	\$ 7,143	2.00%

A summary of the expected maturity, amortized cost and estimated fair value of investment securities held-to-maturity at March 31, 2010 follows:

	Amortized Cost	Fair Value	Weighted Average Yield
In one year or less	\$ 2,070	\$ 2,064	1.60%
After one year through five years	4,207	4,201	2.02
After five years through ten years	133	131	1.48
After ten years	-	-	-
Total	\$ 6,410	\$ 6,396	1.88%

The Association's investments consist primarily of asset-backed securities (ABSs). These ABSs are rated AAA and they are guaranteed by the full faith and credit of the United States government. ABSs are held for maintaining a liquidity reserve, managing short-term surplus funds and managing interest rate risk. These securities must meet the applicable Farm Credit Administration (FCA) regulatory guidelines, which require these securities to be high quality, senior class, and rated AAA at the time of purchase. To achieve the ratings, these securities have a guarantee of timely payment of principal and interest or credit enhancement achieved through over collateralization and the priority of payments of senior classes over junior classes. The FCA considers an asset-backed security investment ineligible if it falls below

the AAA credit rating criteria and requires System institutions to divest of such an investment unless approval is granted to continue to hold by the FCA. All of the Association's asset-backed securities at March 31, 2010 are considered eligible under FCA regulatory guidelines.

An investment is considered impaired if its fair value is less than its cost. A continuous unrealized loss position for an investment is based on the date the impairment was first identified. The following table shows the fair value and gross unrealized losses for investments that have been in a continuous unrealized loss position aggregated by investment category at March 31, 2010:

	March 31, 2010			
	Less than 12 Months		Greater than 12 Months	
	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
Asset backed securities	\$ 3,049	\$ (7)	\$ 1,271	\$ (13)

The Association performs periodic credit reviews, including other-than-temporary impairment analyses, on its investment securities portfolio. The objective is to quantify any future possible loss of principal or interest due on each security identified for additional analysis. Factors considered in determining whether an impairment is other-than-temporary include among others as applicable: 1) the length of time and the extent to which the fair value is less than cost, 2) adverse conditions specifically related to the industry, 3) geographic area and the condition of the underlying collateral, 4) payment structure of the security, 5) ratings by rating agencies, 6) the credit worthiness of bond insurers, and 7) volatility of the fair value changes.

Based on the results of all analyses, the Association has not recognized any other-than-temporary impairment as the unrealized losses resulted primarily from non-credit related factors. The Association has the ability and intent to hold these investments until a recovery of unrealized losses occurs, which may be at maturity, and at this time expects to collect the full principal amount and interest due on these securities, especially after considering credit enhancements. The Association does not intend to sell these investments and it is not more likely than not that the Association would be required to sell these investments before recovering its costs. Substantially all of these investments were in U. S. government agency securities and the Association expects these securities would not be settled at a price less than their amortized costs. All securities continue to perform.

### NOTE 3 – ALLOWANCE FOR LOAN LOSSES AND IMPAIRED LOANS

An analysis of the allowance for loan losses follows:

	For the three months ended March 31,	
	2010	2009
Balance at beginning of period	\$ 3,070	\$ 1,771
Provision for (reversal of) loan losses	-	-
Charge-offs	(1,139)	(333)
Recoveries	1	-
Balance at end of period	\$ 1,932	\$ 1,438

The following table presents information concerning impaired loans as of March 31,

	2010	2009
Impaired loans with related allowance	\$ 1,048	\$ 181
Impaired loans with no related allowance	2,029	3,077
Total impaired loans	3,077	3,258
Allowance on impaired loans	\$ 213	\$ 56

The following table summarizes impaired loan information for the three months ended March 31,

	2010	2009
Average impaired loans	\$ 4,971	\$ 2,669
Interest income recognized on impaired loans	73	9

### NOTE 4 – EMPLOYEE BENEFIT PLANS

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

	For the three months ended March 31,	
	2010	2009
Pension	\$ 151	\$ 142
401(k)	35	34
Other postretirement benefits	-	(3)
Total	\$ 186	\$ 173

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

	Actual YTD Through 3/31/10	Projected Contributions For Remainder of 2010	Projected Total Contributions 2010
Pension	\$ -	\$ 683	\$ 683
Other postretirement benefits	-	-	-
Total	\$ -	\$ 683	\$ 683

Contributions in the above table include allocated estimates of funding for multi-employer plans in which the Association participates. These amounts may change when a total funding amount and allocation is determined by the respective Plan's Sponsor Committee. Also, market conditions could impact discount rates and return on plan assets which could change contributions necessary before the next plan measurement date of December 31, 2010.

Further details regarding employee benefit plans are contained in the 2009 Annual Report to Shareholders.

### NOTE 5 – FAIR VALUE MEASUREMENT

Effective January 1, 2008, the Association adopted FASB guidance on fair value measurements. This guidance defines fair value, establishes a framework for measuring fair value and expands the Association's fair value disclosures for certain assets and liabilities measured at fair value on a recurring and non-recurring basis. These assets and liabilities consist primarily of standby letters of credit, impaired loans and other property owned.

This guidance 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.

This guidance 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 has no Level 1 assets or liabilities measured at fair value on a recurring basis at March 31, 2010.

## 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 March 31, 2010.

## 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 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 March 31, 2010 include impaired loans which represent the fair value of certain loans that were evaluated for impairment under FASB guidance. 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 March 31, 2010. The fair value for other property owned is based upon the collateral value. Costs to sell represent transaction costs and are not included as a component of the fair value of other property owned. Level 3 liabilities at March 31, 2010 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 March 31, 2010 and December 31, 2009 for each of the fair value hierarchy levels:

March 31, 2010				
	Level 1	Level 2	Level 3	Total Fair Value
<b>Liabilities:</b>				
Standby letters of credit	\$ -	\$ -	\$ 22	\$ 22
Total Liabilities	\$ -	\$ -	\$ 22	\$ 22
December 31, 2009				
	Level 1	Level 2	Level 3	Total Fair Value
<b>Liabilities:</b>				
Standby letters of credit	\$ -	\$ -	\$ 28	\$ 28
Total Liabilities	\$ -	\$ -	\$ 28	\$ 28

The following tables present the changes in Level 3 assets and liabilities measured at fair value on a recurring basis for the three months ended March 31, 2010 and 2009. The Association had no transfers of assets or liabilities into or out of Level 1 or Level 2 during the first three months of 2010 and 2009.

	Standby Letters Of Credit
Balance at January 1, 2010	\$ 28
<b>Total gains or (losses) realized/unrealized:</b>	
Included in earnings	-
Included in other comprehensive loss	-
Purchases, sales, issuances and settlements, net	(6)
Transfers in and/or out of level 3	-
Balance at March 31, 2010	\$ 22
	Standby Letters Of Credit
Balance at January 1, 2009	\$ 46
<b>Total gains or (losses) realized/unrealized:</b>	
Included in earnings	-
Included in other comprehensive loss	-
Purchases, sales, issuances and settlements, net	(5)
Transfers in and/or out of level 3	-
Balance at March 31, 2009	\$ 41

## 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 March 31, 2010 and December 31, 2009 for each of the fair value hierarchy values are summarized below:

March 31, 2010					
	Level 1	Level 2	Level 3	Total Fair Value	YTD Total Gains (Losses)
<b>Assets:</b>					
Impaired loans	\$ -	\$ -	\$ 622	\$ 622	\$ 476
Other property owned	\$ -	\$ -	\$ -	\$ -	\$ -
<b>December 31, 2009</b>					
	Level 1	Level 2	Level 3	Total Fair Value	YTD Total Gains (Losses)
<b>Assets:</b>					
Impaired loans	\$ -	\$ -	\$ 2,345	\$ 2,345	\$ (2,200)
Other property owned	\$ -	\$ -	\$ 77	\$ 77	\$ -

## NOTE 6 — DISCLOSURES ABOUT FAIR VALUE OF FINANCIAL INSTRUMENTS

The following table presents the carrying amounts and fair values of the Association's financial instruments at March 31, 2010 and December 31, 2009.

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:

	March 31, 2010		December 31, 2009	
	Carrying Amount	Estimated Fair Value	Carrying Amount	Estimated Fair Value
<b>Financial assets:</b>				
Cash	\$ 615	\$ 615	\$ 2,503	\$ 2,503
Loans, net of allowance	\$ 234,155	\$ 236,315	\$ 265,004	\$ 269,404
Investment securities	\$ 6,410	\$ 6,396	\$ 7,145	\$ 7,143
Tobacco Buyout SIIC	\$ 2,226	\$ 2,401	\$ 2,821	\$ 2,997
<b>Financial liabilities:</b>				
Notes payable to AgFirst Farm Credit Bank	\$ 205,312	\$ 206,902	\$ 241,378	\$ 243,773

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 primarily 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. Discount rates are based on the Bank's loan rates as well as management estimates.

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 of the loan less specific reserves.

The carrying value of accrued interest approximates its fair value.

- C. **Investment Securities:** Fair value is primarily based upon prices obtained from a third party valuation service.
- D. **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 1.66 percent of the issued stock of the Bank as of March 31, 2010 net of any reciprocal investment. As of that date, the Bank's assets totaled \$30.1 billion and shareholders' equity totaled \$1.7 billion. The Bank's earnings were \$117 million during the first three months of 2010.

In addition, the Association has an investment of \$79 related to other Farm Credit institutions.

- E. **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.

F. **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.

G. **Tobacco Buyout SIIC:** Fair value is determined by discounting the expected future cash flows using current interest rates for similar assets.

#### **NOTE 7 – SUBSEQUENT EVENTS**

The Association has evaluated subsequent events and has determined there are none requiring disclosure through May 7, 2010, which is the date the financial statements were issued.