

# ALABAMA FARM CREDIT, ACA

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**2011  
Quarterly Report  
Third Quarter**



**For the Quarter Ended September 30, 2011**

## REPORT OF MANAGEMENT

The undersigned certify that we have reviewed this report, that it has been prepared in accordance with all applicable statutory or regulatory requirements, and that the information contained herein is true, accurate and complete to the best of his or her knowledge and belief.



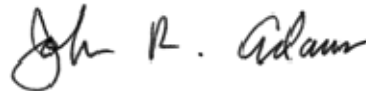
K. Ben Gore, Chief Executive Officer/President  
*November 4, 2011*



Loyd Rutherford, Chairman, Board of Directors  
*November 4, 2011*



Karri H. Sumrall, Chief Financial Officer/Sr. Vice President  
*November 4, 2011*



John R. Adams, CPA, Chairman, Audit Committee  
*November 4, 2011*

**ALABAMA FARM CREDIT, ACA  
MANAGEMENT’S DISCUSSION AND ANALYSIS**

The following commentary reviews the financial performance of the Alabama Farm Credit, ACA (Agricultural Credit Association), referred to as the Association, for the quarter and nine months ended September 30, 2011. These comments should be read in conjunction with the accompanying financial statements and the December 31, 2010 Annual Report to Stockholders.

The Association is a member of the Farm Credit System (System), a nationwide network of cooperatively owned financial institutions established by and subject to the provisions of the Farm Credit Act of 1971, as amended, and the regulations of the Farm Credit Administration (FCA) promulgated thereunder.

The consolidated financial statements comprise the operations of the ACA and its wholly-owned subsidiaries. The consolidated financial statements were prepared under the oversight of the Association’s audit committee.

**Significant Events:**

On April 27, 2011, many of the Association’s twenty-seven counties it serves were affected by the line of storms and tornadoes that passed through the state of Alabama. The Association worked closely with, and continues to work with the borrowers to ensure proper servicing and attention is given to borrowers and their accounts while also protecting the Association’s collateral interest. The Association had approximately seven dwellings totally destroyed and approximately ninety poultry houses that were either damaged or totally destroyed. These type facilities have insurance requirements that include income loss clauses that have helped borrowers maintain their income stream until they could rebuild if they choose to do so. As discussed also below, the large decrease in loan volume during 2011 is primarily the result of large payoffs and pay downs of loan balances from borrowers that have received insurance proceeds as a result of these storms. Due to the downturn in the poultry industry, it is uncertain that the poultry integrators will replace the poultry houses that were destroyed if the operators decide not to rebuild; therefore, this decline may be more than temporary.

**Loan Portfolio:**

The Association makes and services loans to farmer, ranchers, rural homeowners and certain farm-related businesses. The Association’s loan volume consists of long-term farm mortgage loans, production and intermediate term loans, and farm-related business loans. These loans are available to eligible borrowers with competitive fixed, adjustable and indexed-based interest rates and loan maturities ranging up to 40 years. Loans serviced by the Association offer several installment payment cycles, the timing of which usually coincides with seasonal cash-flow capabilities of the borrower.

Total loans outstanding at September 30, 2011, including nonaccrual loans, were \$404,221,972 compared to \$409,962,715 at December 31, 2010, reflecting a decrease of \$5,740,743 or 1.4 percent. Since the April 27, 2011 storms, the Association has received approximately \$10 million from insurance proceeds. Also, the Association’s capital markets portfolio segment has decreased just over \$1.9 million primarily as a result of the Association not being active in the purchase of participation loans during the first nine months of 2011. This decrease is offset by the Association closing \$53.1 million in loans during 2011 as a result of an increased demand for loans and continuing marketing and servicing efforts throughout the Association’s territory.

	<b>September 30, 2011</b>	December 31, 2010
Acceptable	<b>83.0%</b>	83.0%
Special Mention	<b>13.7%</b>	13.7%
Substandard	<b>3.3%</b>	3.3%
Total	<b>100.0%</b>	100.0%

The Association’s credit quality began to deteriorate slightly in late 2008 due primarily to the impact of a poultry integrator in the Association’s territory filing Chapter 11 bankruptcy. This bankruptcy has had a residual effect on Association grower borrowers as a result of the inherent counterparty risk associated with the integrator. In 2009, the integrator emerged from bankruptcy and the Association has not experienced any adverse effects to growers with Association loans to date. At September 30, 2011, Association loans to growers of this integrator consisted of 326 loans representing \$78.8 million in volume, of which \$32.7 million are government guaranteed. The Association anticipates these producer loans will be upgraded after the integrator shows positive earnings trends and once approval from Farm Credit Administration is received. Also, another poultry integrator that operates in the Association’s territory filed Chapter 11 bankruptcy in October. The Association has ten grower loans for \$2.25 million that have contracts with this integrator. The bankruptcy filing should not significantly affect the Association’s overall portfolio and should have only minimal effect to the growers.

The Association's largest commodity concentration in its loan portfolio continues to be poultry, which is approximately 49.9 percent. The industry is presently in a downturn with market prices for poultry being depressed and continued high feed cost. This has resulted in the integrators sustaining an operating loss in the short run. They are reacting to this loss by reducing egg and chick placement and beginning to have longer holdout times between batches sold for the contract growers. This could cause an increase in Association delinquencies due to the delayed payments from growers/integrators as a result of these longer holdout periods in between sales of birds to the integrators. However, this has not materialized as of the end of the 3<sup>rd</sup> quarter 2011. Overall, the industry remains mostly stable. Production for the remainder of 2011 should decrease until markets both in the states and overseas rebound. The effect of the storms that hit the Association's territory in April has not significantly affected the poultry industry as a whole, for areas serviced by the Association.

Commodity prices remain volatile for production agricultural borrowers but are at all time highs compared to the five year average for corn, cotton and soybean growers. These higher prices are partially offset by higher input cost and lower government payments. Crop yield for all three commodities are reported to be above average this growing season coupled with all time high prices should result in record level high profit margin for these row crop producers. Livestock producers have seen higher prices for cattle sold due to the overall low inventory of cattle nationwide and worldwide due to increased demand for beef products abroad and within the US compared to the last few years. Cattle prices are projected to remain high with the liquidation of cattle herds in other parts of the country due to severe droughts experienced this past summer. The majority of Association livestock producers have considerable nonfarm income which should lessen the impact of price volatility. The decline in the general economy has shown minimal effects on the Association's non-agricultural income dependent borrowers and their repayment abilities at this time. Delinquency percentages of total volume continue to be slightly above prior years' percentages.

Timber markets in 2011 continued to be depressed due to the decreased demand from the housing market. Indicators for 2011 show that timber prices will remain relatively stable with no evidence of a strong recovery seen at this time. We will continue to work with our borrowers as all market segments make corrections with minimal restructuring.

Overall land values have remained fairly stable or have seen a slight decline in some areas of the Association territory based on the current economic climate. The agricultural economy, in general for the area, has seen a slight decline. This can be seen in the Association's slight decrease in credit quality volume over the last 12 to 18 months.

The probability of higher input costs, questions about future commodity supplies and prices, uncertainty of the export markets and unfolding world events increase the level of financial risk in the farming sector and, likewise, the level of credit risk to those financial institutions providing credit to that sector. Given the conditions outlined herein, the quality of the loan portfolio is expected to remain constant or slightly deteriorate throughout 2011, as a result of a continued weak economy. The duration of the conditions described is a concern that has the potential to be more problematic for financial results over the longer term for both the lender and the operator. Continued diligence in the areas of credit controls and monitoring is essential.

#### **Risk Exposure:**

High-risk assets include nonaccrual loans, loans that are past due 90 days or more and still accruing interest, formally restructured loans and other property owned. The following table illustrates the Association's components and trends of high-risk assets.

	<b>September 30, 2011</b>		<b>December 31, 2010</b>	
	<b>Amount</b>	<b>%</b>	<b>Amount</b>	<b>%</b>
Nonaccrual	<b>\$ 6,540,370</b>	<b>65.3%</b>	\$ 5,375,102	69.1%
90 days past due and still accruing interest	<b>63,523</b>	<b>0.6%</b>	498,014	6.4%
Formally restructured	<b>1,248,639</b>	<b>12.5%</b>	-	0.0%
Other property owned, net	<b>2,169,654</b>	<b>21.6%</b>	1,900,967	24.5%
<b>Total</b>	<b>\$ 10,022,186</b>	<b>100.0%</b>	<b>\$ 7,774,083</b>	<b>100.0%</b>

At September 30, 2011 and December 31, 2010 loans that were considered impaired were \$7,852,532 and \$5,873,116, representing 1.9 percent and 1.4 percent of loan volume, respectively. Impaired loans consist of all high-risk assets except other property owned, net.

High-risk assets increased by \$2,248,103 or 28.9 percent primarily due to the increase in nonaccrual volume and other property owned as a result of the Association acquiring collateral, through foreclosure proceedings. During the second quarter of 2011, one large restructured participation moved out of nonaccrual status into accrual status and is now therefore reported as formerly

restructured. Since December, the Association has acquired eleven properties within the Association's lending territory and sold eight properties. As of September 30, 2011, the Association held eleven properties on its books. The Association is actively working to ensure properties are accurately valued on the Association's books and that proactive marketing activities are in place.

Nonaccrual loans as a percentage of total loans outstanding were 1.6 percent at September 30, 2011, compared to 1.3 percent at December 31, 2010. The increase in nonaccrual assets from 2010 to 2011 is derived primarily as a result of the receipt of scheduled principal and interest payments becoming questionable due to economic stress surrounding personal income and commodity prices on the Association's core business loans. Loans in the category "90 days past due and still accruing interest" are to customers that have a documented plan that details how and when the amount owed will be paid and management believes the plan will result in the payment of all principal and interest currently due within the near future. Management continues to be alert to portfolio trends and has attempted to identify and report problem loans as quickly as possible. Management strives to implement proactive steps and allocate resources to work with distressed borrowers to either work through temporary repayment problems or to orderly liquidate collateral to repay the loan when the borrower's operation is no longer viable.

The Association, in the normal course of business, has participation loans with other Farm Credit associations and Farm Credit banks. The Association holds interests in loans with geographic or industry related risks that have warranted risk rating reclassifications to nonaccrual status. Performance of these loans remains uncertain even though management constantly monitors these accounts.

Counterparty risk is continually monitored by management of the Association. The Association's primary counterparty risk comes from the poultry integrators to which its borrowers are associated. Because the Association's portfolio has such a high concentration in poultry, it mitigates its inherent risks with poultry and the integrators by heavy utilization of government guarantees. Also, the Association's lending territory has multiple integrators which would minimize the risk of counterparty failure or lack of performance. Management analyzes the financial position and performance of these integrators by regularly gathering updated financials and other reports that are made available to the public.

As disclosed in the Association's 2010 Annual Report, it is management's assertion that the allowance coverage is adequate based on historical losses, portfolio stress testing, risk analysis, mitigation of losses due to having first lien real estate with minimal to no price appreciation and having \$73,489,174 or 18.2 percent of its portfolio government guaranteed. Management continuously monitors high-risk assets in an effort to reduce their impact on the Association and will continue to work with all of the Association's high-risk borrowers to receive full payment on the debt. Except for the relationship between installment due date and seasonal cash-flow capabilities of the borrower, the Association is not affected by any seasonal characteristics. The factors affecting the operations of the Association are the same factors that would affect any agricultural real estate lender.

The Association recorded no recoveries and \$320,944 in charge-offs for the quarter ending September 30, 2011, and \$3,500 in recoveries and \$971,698 in charge-offs for the same period in 2010. The Association's allowance for loan losses was 0.6 percent and 0.4 percent of total loans outstanding as of September 30, 2011, and December 31, 2010, respectively.

### **Results of Operations:**

The Association had net income of \$1,624,105 and \$5,629,728 for the three and nine months ended September 30, 2011, as compared to net income of \$1,958,623 and \$6,039,167 for the same period in 2010 reflecting a decrease of 17 and 6.8 percent, respectively. This decrease is primarily attributable to an increase in provision for loan losses, a decrease in noninterest income, offset by a slight increased net interest income when compared to the same period in 2010. Net interest income was \$3,390,305 and \$10,137,515 for the three and nine months ended September 30, 2011, compared to \$3,148,645 and \$9,414,705 for the same period in 2010. Interest income for the first nine months of 2011 decreased by \$993,469, or 5.4 percent, from the same period of 2010, primarily due to a decrease in yields on earning assets and a decrease in average loan volume. Interest expense for the first nine months of 2011 decreased by \$1,716,279, or 18.9 percent, from the same period of 2010 due to a decrease in average debt interest rates and a decrease in average debt volume. Average loan volume for the third quarter of 2011 was \$401,734,837, compared to \$406,080,673 in the third quarter of 2010.

The Association offers fixed, adjustable and indexed priced loans. These different type loans have different spreads and therefore provide differing net interest margins to the Association. The average spread on the loan portfolio for the third quarter 2011 increase 0.32 basis points compared to third quarter 2010.

Noninterest income for the three and nine months ended September 30, 2011 increased slightly by \$31,067, or 6.7 percent and decreased by \$307,898 or 20.0 percent, respectively when compared to the same period in 2010, offset by a decrease on loan fees. The three month increase compared to the same period in 2010 was due to the Association recording more patronage income from the Bank, an increase in income derived from the sale of premises and equipment, offset by a decrease in loan fees and as result of

implementing authoritative accounting guidance in December 2010 requiring the capitalization and amortization of loan origination fees and costs that was not in effect the during the same period of 2010. The nine month decrease was primarily due to a decrease in loan fees and other income. The loan fee decrease was the result of implementing authoritative accounting guidance in December 2010 requiring the capitalization and amortization of loan origination fees and costs that was not in effect the first nine months of 2010, and receiving an allocated distribution of excess Farm Credit System Insurance Corporation (FCSIC) fund balance above the 2.0 percent secured based which was not received during the same reporting period for 2011.

Noninterest expenses for the three and nine months September 30, 2011 decreased \$159,681 or 10.8 percent, and \$148,434 or 3.4 as compared to the same period in 2010. The decrease for the three months ended September 30, 2011 is due primarily to a decrease in salaries and employee benefits and purchased services expense compared to the same period in 2010. The decrease in salaries and benefits was primarily due to the result of implementing authoritative accounting guidance requiring the capitalization and amortization of loan origination fees and costs was implemented and recorded for the entire year in December 2010, resulting in the capitalization in origination costs (primarily salaries and benefits), which will be amortized over the life of the loans as an adjustment to yield in net interest income. The decrease in purchase services is the direct result of the Association’s funding bank, Farm Credit Bank of Texas (FCBT) no longer charging the associations a monthly technology fee as they did during the same period in 2010.

The increase in noninterest expenses for the nine months ended September 30, 2011 is due primarily to the Association recognizing losses on the sale of other property owned and provisions for losses on other property owned that were not incurred during the same period in 2010. This increase was offset by a decrease in salaries and employee benefits and purchased services compared to the same period in 2010. The decrease in salaries and benefits was primarily due to the result of implementing authoritative accounting guidance requiring the capitalization and amortization of loan origination fees and costs was implemented and recorded for the entire year in December 2010, resulting in the capitalization in origination costs (primarily salaries and benefits), which will be amortized over the life of the loans as an adjustment to yield in net interest income. The decrease in purchase services is the direct result of FCBT no longer charging the associations a monthly technology fee as they did during the same period in 2010.

The Association’s return on average assets for the nine months ended September 30, 2011, was 1.78 percent compared to 1.91 percent for the same period in 2010. The Association’s return on average equity for the nine months ended September 30, 2011, was 9.80 percent, compared to 11.32 percent for the same period in 2010.

**Liquidity and Funding Sources:**

The Association secures the majority of its lendable funds from the Farm Credit Bank of Texas (the bank), which obtains its funds through the issuance of Systemwide obligations and with lendable equity. The following schedule summarizes the Association’s borrowings.

	September 30, 2011	December 31, 2010
Note payable to the Bank	\$ 338,831,549	\$ 344,869,304
Accrued interest on note payable	756,255	889,350
Total	<u>\$ 339,587,804</u>	<u>\$ 345,758,654</u>

The interest rate inherent in the Association’s loan portfolio is substantially mitigated through the funding relationship with the Bank. The Bank manages interest rate risk through its direct loan pricing and asset/liability management process.

The Association will continue to fund its operations through direct borrowings from the Bank, retained earnings, member stock and funds held. It is management’s opinion that funds available to the Association are sufficient to fund its operations for the current year.

**Capital Resources:**

The Association’s capital position increased by \$5,610,229 at September 30, 2011, compared to December 31, 2010. The Association’s debt as a percentage of members’ equity was 4.33:1 as of September 30, 2011, compared to 4.79:1 as of December 31, 2010.

Under regulations governing minimum permanent capital adequacy and other capitalization issues, the Association is required to maintain a minimum adjusted permanent capital of 7.0 percent of risk-adjusted assets as defined by the FCA. The Association’s permanent capital ratio at September 30, 2011, was 20.3 percent, which is in compliance with the FCA’s minimum permanent

capital standard. The Association's core surplus ratio and total surplus ratio at September 30, 2011, were 19.6 and 19.6 percent, respectively, which is in compliance with the FCA's minimum surplus standard.

### **Significant Recent Accounting Pronouncements:**

In June 2011, the Financial Accounting Standards Board (FASB) issued guidance entitled, "Comprehensive Income – Presentation of Comprehensive Income." This guidance is intended to increase the prominence of other comprehensive income in financial statements. The current option that permits the presentation of other comprehensive income in the statement of changes in equity has been eliminated. The main provisions of the guidance provides that an entity that reports items of other comprehensive income has the option to present comprehensive income in either one or two consecutive financial statements:

- A single statement must present the components of net income and total net income, the components of other comprehensive income and total other comprehensive income, and a total for comprehensive income.
- In a two-statement approach, an entity must present the components of net income and total net income in the first statement. That statement must be immediately followed by a financial statement that presents the components of other comprehensive income, a total for other comprehensive income, and a total for comprehensive income.

This guidance is to be applied retrospectively and is effective for fiscal years, and interim periods within those years, beginning after December 15, 2011. The adoption of this guidance will not impact financial condition or results of operations, but will result in changes to the presentation of comprehensive income.

In May 2011, the FASB issued guidance entitled, "Fair Value Measurement – Amendments to Achieve Common Fair Value Measurements and Disclosure Requirements in U.S. GAAP and IFRSs." The amendments change the wording used to describe the requirements in U.S. GAAP for measuring fair value and for disclosing information about fair value measurements. The amendments include the following:

1. Application of the highest and best use and valuation premise is only relevant when measuring the fair value of nonfinancial assets (does not apply to financial assets and liabilities).
2. Aligning the fair value measurement of instruments classified within an entity's shareholders' equity with the guidance for liabilities. As a result, an entity should measure the fair value of its own equity instruments from the perspective of a market participant that holds the instruments as assets.
3. Clarifying that a reporting entity should disclose quantitative information about the unobservable inputs used in a fair value measurement that is categorized within Level 3 of the fair value hierarchy.
4. An exception to the requirement for measuring fair value when a reporting entity manages its financial instruments on the basis of its net exposure, rather than its gross exposure, to those risks.
5. Clarifying that the application of premiums and discounts in a fair value measurement is related to the unit of account for the asset or liability being measured at fair value. Premiums or discounts related to size as a characteristic of the entity's holding (that is, a blockage factor) instead of as a characteristic of the asset or liability (for example, a control premium), are not permitted. A fair value measurement that is not a Level 1 measurement may include premiums or discounts other than blockage factors when market participants would incorporate the premium or discount into the measurement at the level of the unit of account specified in other guidance.
6. Expansion of the disclosures about fair value measurements. The most significant change will require entities, for their recurring Level 3 fair value measurements, to disclose quantitative information about unobservable inputs used, a description of the valuation processes used by the entity, and a qualitative discussion about the sensitivity of the measurements. New disclosures are required about the use of a nonfinancial asset measured or disclosed at fair value if its use differs from its highest and best use. In addition, entities must report the level in the fair value hierarchy of assets and liabilities not recorded at fair value but where fair value is disclosed.

The amendments are to be applied prospectively. The amendments are effective during interim and annual periods beginning after December 15, 2011. Early application is not permitted.

In January 2011, the FASB issued guidance entitled, "Deferral of the Effective Date of Disclosures about Troubled Debt Restructurings." This guidance temporarily delayed the effective date of the disclosures about troubled debt restructurings required by the guidance previously issued on "Disclosures about the Credit Quality of Financing Receivables and the Allowance for Credit Losses." The effective date of the new disclosures about troubled debt restructurings (TDR) coincides with the guidance for determining what constitutes a TDR as described below.

In April 2011, the FASB issued its guidance entitled, “A Creditor’s Determination of Whether a Restructuring is a Troubled Debt Restructuring,” which provides for clarification on whether a restructuring constitutes a TDR. In evaluating whether a restructuring is a TDR, a creditor must separately conclude that both of the following exists: (1) the restructuring constitutes a concession, and (2) the debtor is experiencing financial difficulties. For nonpublic entities, the guidance is effective for annual periods ending on or after December 15, 2012, including interim periods within those annual periods. The Association is currently evaluating the impact of adoption of this Standard on the financial condition or results of operations. The adoption will result in additional disclosures.

In July 2010, the Financial Accounting Standards Board (FASB) issued guidance on “Disclosures about the Credit Quality of Financing Receivables and the Allowance for Loan Losses,” which is intended to provide additional information to assist financial statement users in assessing an entity’s credit risk exposures and evaluating the adequacy of the allowance for credit losses. Existing disclosures are amended to include additional disclosures of financing receivables on a disaggregated basis (by portfolio segment and class of financing receivable) including among others, a rollforward schedule of the allowance for credit losses from the beginning of the reporting period to the end of the period on a portfolio segment basis, with the ending balance further disaggregated on the basis of the method of impairment (individually or collectively evaluated). The guidance also calls for new disclosures including but not limited to credit quality indicators at the end of the reporting period by class of financing receivables, the aging of past due financing receivables by class, the nature and extent of financing receivables modified as troubled debt restructurings by class and the effect on the allowance for credit losses. For public entities, the disclosures as of the end of a reporting period are effective for interim and annual reporting periods ending on or after December 15, 2010. The disclosures about activity that occurs during a reporting period are effective for interim and annual reporting periods beginning on or after December 15, 2010. The adoption of this Standard did not impact the Association’s financial condition or results of operations, but did result in significant additional disclosures.

In January 2010, the FASB issued guidance on “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 robust 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 Standard did not impact the Association’s financial condition or results of operations but did result in additional disclosures.

#### **Relationship with the Farm Credit Bank of Texas (Bank):**

The Association’s financial condition may be impacted by factors that affect the Bank. The financial condition and results of operations of the Bank may materially affect the stockholder’s investment in the Association. The Management’s Discussion and Analysis and Notes to Financial Statements contained in the December 31, 2010 Annual Report of Alabama Farm Credit, ACA more fully describe the Association’s relationship with the bank.

The Texas Farm Credit District’s (district) annual and quarterly stockholder reports are available free of charge, upon request. These reports can be obtained by writing to Farm Credit Bank of Texas, The Ag Agency, P.O. Box 202590, Austin, Texas 78720, or by calling (512) 483-9204. Copies of the district’s quarterly and annual stockholder reports also can be requested by e-mail at [fcdb@farmcreditbank.com](mailto:fcdb@farmcreditbank.com). The district makes its annual and quarterly stockholder reports available on its website at [www.farmcreditbank.com](http://www.farmcreditbank.com).

The Association’s quarterly stockholder reports are also available free of charge, upon request. These reports can be obtained by writing to Alabama Farm Credit, ACA, P.O. Box 639, Cullman, Alabama 35056 or calling (256) 737-7128. Copies of the Association’s quarterly stockholder reports can also be requested by e-mailing [karri.sumrall@farmcreditbank.com](mailto:karri.sumrall@farmcreditbank.com) or can be obtain on its web site at [www.alabamalandbank.com](http://www.alabamalandbank.com) 40 days after quarter end. The Association’s annual stockholder report is available on its Web site at [www.alabamalandbank.com](http://www.alabamalandbank.com) 75 days after the fiscal year end. Copies of the Association’s annual stockholder report can also be requested 90 days after the fiscal year end.

**ALABAMA FARM CREDIT, ACA**  
**CONSOLIDATED BALANCE SHEET**

	September 30, 2011 (unaudited)	December 31, 2010
<b><u>ASSETS</u></b>		
Cash	\$ 15,009	\$ 5,842
Loans	404,221,972	409,962,715
Less: allowance for loan losses	2,444,500	1,490,624
Net loans	401,777,472	408,472,091
Accrued interest receivable	6,158,863	5,246,279
Investment in and receivable from the bank:		
Capital stock	6,956,070	6,956,070
Other	1,255,718	1,020
Other property owned, net	2,169,654	1,900,967
Premises and equipment	3,657,090	3,713,047
Other assets	485,156	220,687
Total assets	<u>\$ 422,475,032</u>	<u>\$ 426,516,003</u>
<b><u>LIABILITIES</u></b>		
Note payable to the bank	\$ 338,831,549	\$ 344,869,304
Advance conditional payments	5,636	-
Accrued interest payable	756,255	889,348
Drafts outstanding	1,850,521	1,272,716
Patronage distributions payable	58	3,637,140
Other liabilities	1,760,362	2,187,073
Total liabilities	<u>343,204,381</u>	<u>352,855,581</u>
<b><u>MEMBERS' EQUITY</u></b>		
Capital stock and participation certificates	2,489,565	2,474,920
Unallocated retained earnings	76,771,298	71,141,624
Accumulated other comprehensive income	9,788	43,878
Total members' equity	<u>79,270,651</u>	<u>73,660,422</u>
Total liabilities and members' equity	<u>\$ 422,475,032</u>	<u>\$ 426,516,003</u>

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

ALABAMA FARM CREDIT, ACA

CONSOLIDATED STATEMENT OF INCOME  
(unaudited)

	Quarter Ended September 30,		Nine Months Ended September 30,	
	2011	2010	2011	2010
<b><u>INTEREST INCOME</u></b>				
Loans	\$ 5,768,393	\$ 6,082,659	\$ 17,490,073	\$ 18,483,542
Total interest income	5,768,393	6,082,659	17,490,073	18,483,542
<b><u>INTEREST EXPENSE</u></b>				
Note payable to the bank	2,378,088	2,934,014	7,352,558	9,068,837
Total interest expense	2,378,088	2,934,014	7,352,558	9,068,837
Net interest income	3,390,305	3,148,645	10,137,515	9,414,705
<b><u>PROVISION FOR LOAN LOSSES</u></b>				
	948,991	180,361	1,486,751	513,966
Net interest income after provision for loan losses	2,441,314	2,968,284	8,650,764	8,900,739
<b><u>NONINTEREST INCOME</u></b>				
Income from the bank:				
Patronage income	302,410	144,236	913,138	440,846
Loan fees	132,706	311,479	241,146	669,487
Financially related services income	6,651	7,139	19,464	20,442
Gain (loss) on sale of premises and equipment, net	29,198	1,025	31,134	37,912
Other noninterest income	24,154	173	24,275	368,368
Total noninterest income	495,119	464,052	1,229,157	1,537,055
<b><u>NONINTEREST EXPENSES</u></b>				
Salaries and employee benefits	814,634	886,372	2,483,710	2,827,274
Directors' expense	42,669	46,293	171,547	155,720
Purchased services	55,218	147,083	274,198	431,935
Travel	104,360	96,347	271,150	237,513
Occupancy and equipment	63,386	89,311	188,239	183,888
Communications	21,746	21,675	70,155	54,491
Advertising	27,524	37,776	140,813	173,886
Public and member relations	29,240	26,601	106,306	87,709
Supervisory and exam expense	35,741	35,240	106,222	102,204
Insurance fund premiums	39,638	34,357	120,566	103,580
Business insurance premiums	2,256	2,238	63,919	57,302
Loss (gain) on other property owned, net	1,996	3,298	34,739	(139,432)
Other noninterest expense	75,622	47,122	218,629	122,557
Total noninterest expenses	1,314,030	1,473,713	4,250,193	4,398,627
Income before income taxes	1,622,403	1,958,623	5,629,728	6,039,167
Benefit from income taxes	(1,702)	-	-	-
Net income	\$ 1,624,105	\$ 1,958,623	\$ 5,629,728	\$ 6,039,167

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

ALABAMA FARM CREDIT, ACA

CONSOLIDATED STATEMENT OF CHANGES IN MEMBERS' EQUITY

(unaudited)

	<u>Capital Stock/ Participation Certificates</u>	<u>Retained Earnings Unallocated</u>	<u>Accumulated Other Comprehensive Income</u>	<u>Total Members' Equity</u>
Balance at December 31, 2009	\$ 2,432,380	\$ 65,533,125	\$ 277,186	\$ 68,242,691
Comprehensive income				
Net income	-	6,039,167	-	6,039,167
Change in postretirement benefit plans	-	-	(41,901)	(41,901)
Total comprehensive income	-	6,039,167	(41,901)	5,997,266
Capital stock/participation certificates issued	204,710	-	-	204,710
Capital stock/participation certificates retired	(175,020)	-	-	(175,020)
<b>Balance at September 30, 2010</b>	<u>\$ 2,462,070</u>	<u>\$ 71,572,292</u>	<u>\$ 235,285</u>	<u>\$ 74,269,647</u>
Balance at December 31, 2010	\$ 2,474,920	\$ 71,141,624	\$ 43,878	\$ 73,660,422
Comprehensive income				
Net income	-	5,629,728	-	5,629,728
Change in postretirement benefit plans	-	-	(34,090)	(34,090)
Total comprehensive income	-	5,629,728	(34,090)	5,595,638
Capital stock/participation certificates issued	244,180	-	-	244,180
Capital stock/participation certificates retired	(229,535)	-	-	(229,535)
Patronage refunds:				
Cash	-	(54)	-	(54)
<b>Balance at September 30, 2011</b>	<u>\$ 2,489,565</u>	<u>\$ 76,771,298</u>	<u>\$ 9,788</u>	<u>\$ 79,270,651</u>

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

**ALABAMA FARM CREDIT, ACA**  
**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS**  
(UNAUDITED)

**NOTE 1 — ORGANIZATION AND SIGNIFICANT ACCOUNTING POLICIES:**

The Alabama Farm Credit, ACA (Agricultural Credit Association), referred to as the Association, is a member-owned cooperative that provides credit and credit-related services to or for the benefit of eligible borrowers/stockholders for qualified agricultural purposes. The Association serves the counties of Blount, Calhoun, Cherokee, Clay, Cleburne, Colbert, Cullman, DeKalb, Etowah, Fayette, Franklin, Jackson, Jefferson, Lamar, Lauderdale, Lawrence, Limestone, Madison, Marion, Marshall, Morgan, Randolph, Shelby, St. Clair, Talladega, Walker and Winston in the state of Alabama.

The Association is a lending institution of the Farm Credit System (the System), which was established by Acts of Congress to meet the needs of American agriculture.

The significant accounting policies followed and the financial condition and results of operations of the Association as of and for the year ended December 31, 2010 are contained in the 2010 Annual Report to Stockholders. These unaudited third quarter 2011 financial statements should be read in conjunction with the 2010 Annual Report to Stockholders.

The Farm Credit Bank of Texas (FCBT) and its related associations are collectively referred to as the “District.” The Association’s financial condition may be affected by factors that affect the FCBT. The financial condition and results of operations of the FCBT may materially affect stockholders’ investment in the Association. Upon request, stockholders of the Association will be provided the Tenth Farm Credit District’s Annual Report to Stockholders, which includes the combined financial statements of the FCBT and all of the District associations. The District’s annual report discusses the material aspects of the financial condition, changes in financial condition, and results of operations for the FCBT and the District. In addition, the District’s annual report identifies favorable and unfavorable trends, significant events, uncertainties and the impact of activities of the Farm Credit System Insurance Corporation.

In September 2011, the Financial Accounting Standards Board (FASB) issued guidance entitled, “Compensation – Retirement Benefits – Multiemployer Plans.” The guidance is intended to provide more information about an employer’s financial obligations to a multiemployer pension plan, which should help financial statement users better understand the financial health of significant plans that the employer participates. The additional disclosures include: a) a description of the nature of plan benefits, b) a qualitative description of the extent to which the employer could be responsible for the obligations of the plan, including benefits earned by employees during employment with another employer, and c) other quantitative information to help users understand the financial information about the plan. The amendments are effective for annual periods for fiscal years ending after December 15, 2011 for public entities or for annual periods for fiscal years ending after December 15, 2012 for non-public entities. The amendments should be applied retrospectively for all prior periods presented

In June 2011, the Financial Accounting Standards Board (FASB) issued guidance entitled, “Comprehensive Income – Presentation of Comprehensive Income.” This guidance is intended to increase the prominence of other comprehensive income in financial statements. The current option that permits the presentation of other comprehensive income in the statement of changes in equity has been eliminated. The main provisions of the guidance provides that an entity that reports items of other comprehensive income has the option to present comprehensive income in either one or two consecutive financial statements:

- A single statement must present the components of net income and total net income, the components of other comprehensive income and total other comprehensive income, and a total for comprehensive income.
- In a two-statement approach, an entity must present the components of net income and total net income in the first statement. That statement must be immediately followed by a financial statement that presents the components of other comprehensive income, a total for other comprehensive income, and a total for comprehensive income.

This guidance is to be applied retrospectively and is effective for fiscal years, and interim periods within those years, beginning after December 15, 2011. The adoption of this guidance will not impact financial condition or results of operations, but will result in changes to the presentation of comprehensive income.

In May 2011, the FASB issued guidance entitled, “Fair Value Measurement – Amendments to Achieve Common Fair Value Measurements and Disclosure Requirements in U.S. GAAP and IFRSs.” The amendments change the wording used to describe the requirements in U.S. GAAP for measuring fair value and for disclosing information about fair value measurements. The amendments include the following:

1. Application of the highest and best use and valuation premise is only relevant when measuring the fair value of nonfinancial assets (does not apply to financial assets and liabilities).
2. Aligning the fair value measurement of instruments classified within an entity’s shareholders’ equity with the guidance for liabilities. As a result, an entity should measure the fair value of its own equity instruments from the perspective of a market participant that holds the instruments as assets.
3. Clarifying that a reporting entity should disclose quantitative information about the unobservable inputs used in a fair value measurement that is categorized within Level 3 of the fair value hierarchy.
4. An exception to the requirement for measuring fair value when a reporting entity manages its financial instruments on the basis of its net exposure, rather than its gross exposure, to those risks.
5. Clarifying that the application of premiums and discounts in a fair value measurement is related to the unit of account for the asset or liability being measured at fair value. Premiums or discounts related to size as a characteristic of the entity’s holding (that is, a blockage factor) instead of as a characteristic of the asset or liability (for example, a control premium), are not permitted. A fair value measurement that is not a Level 1 measurement may include premiums or discounts other than blockage factors when market participants would incorporate the premium or discount into the measurement at the level of the unit of account specified in other guidance.
6. Expansion of the disclosures about fair value measurements. The most significant change will require entities, for their recurring Level 3 fair value measurements, to disclose quantitative information about unobservable inputs used, a description of the valuation processes used by the entity, and a qualitative discussion about the sensitivity of the measurements. New disclosures are required about the use of a nonfinancial asset measured or disclosed at fair value if its use differs from its highest and best use. In addition, entities must report the level in the fair value hierarchy of assets and liabilities not recorded at fair value but where fair value is disclosed.

The amendments are to be applied prospectively. The amendments are effective during interim and annual periods beginning after December 15, 2011. Early application is not permitted.

In January 2011, the FASB issued guidance entitled, “Deferral of the Effective Date of Disclosures about Troubled Debt Restructurings.” This guidance temporarily delayed the effective date of the disclosures about troubled debt restructurings required by the guidance previously issued on “Disclosures about the Credit Quality of Financing Receivables and the Allowance for Credit Losses.” The effective date of the new disclosures about troubled debt restructurings (TDR) coincides with the guidance for determining what constitutes a TDR as described below.

In April 2011, the FASB issued its guidance entitled, “A Creditor’s Determination of Whether a Restructuring is a Troubled Debt Restructuring,” which provides for clarification on whether a restructuring constitutes a TDR. In evaluating whether a restructuring is a TDR, a creditor must separately conclude that both of the following exists: (1) the restructuring constitutes a concession, and (2) the debtor is experiencing financial difficulties. For nonpublic entities, the guidance is effective for annual periods ending on or after December 15, 2012, including interim periods within those annual periods. The Association is currently evaluating the impact of adoption of this Standard on the financial condition or results of operations. The adoption will result in additional disclosures.

In July 2010, the FASB issued guidance on “Disclosures about the Credit Quality of Financing Receivables and the Allowance for Loan Losses,” which is intended to provide additional information to assist financial statement users in assessing an entity’s credit risk exposures and evaluating the adequacy of the allowance for credit losses. Existing disclosures are amended to include additional disclosures of financing receivables on a disaggregated basis (by portfolio segment and class of financing receivable) including among others, a rollforward schedule of the allowance for credit losses from the beginning of the reporting period to the end of the period on a portfolio segment basis, with the ending balance further disaggregated on the basis of the method of impairment (individually or collectively evaluated). The guidance also calls for new disclosures including but not limited to credit quality indicators at the end of the reporting period by class of financing receivables, the aging of past due financing receivables by class, the nature and extent of financing receivables modified as troubled debt restructurings by class and the effect on the allowance for credit losses. For public entities, the disclosures as of the end of a reporting period are effective for interim and annual reporting periods ending on or after December 15, 2010. The disclosures about activity that occurs during a reporting period are effective for interim and annual reporting periods beginning on or after December 15, 2010. The adoption of this Standard did not impact the Association’s financial condition or results of operations, but did result in additional disclosures.

In January 2010, the FASB issued guidance on “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 robust 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 Standard did not impact the Association’s financial condition and results of operations but did result in additional disclosures.

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, except for the inclusion of a statement of cash flows. Generally accepted accounting principles require a business enterprise that provides a set of financial statements reporting both financial position and results of operations to also provide a statement of cash flows for each period for which results of operations are provided. In regulations issued by FCA, associations have the option to exclude statements of cash flows in interim financial statements. Therefore, the Association has elected not to include a statement of cash flows in these consolidated financial statements.

The consolidated financial statements comprise the operations of the ACA and its wholly-owned subsidiaries. The preparation of these consolidated financial statements requires the use of management’s estimates. The results for the quarter ended September 30, 2011, are not necessarily indicative of the results to be expected for the year ended December 31, 2011. Certain amounts in the prior period’s financial statements have been reclassified to conform to current financial statement presentation.

## NOTE 2 — LOANS AND ALLOWANCE FOR LOAN LOSSES:

A summary of loans follows:

Loan Type	September 30, 2011 Amount	December 31, 2010 Amount
Real estate mortgage	\$ 392,955,111	\$ 400,066,360
Rural residential real estate	5,197,633	5,306,828
Production and intermediate term	4,404,806	2,977,675
Agribusiness:		
Processing and marketing	1,517,776	1,597,382
Farm-related business	146,646	14,470
Total	\$ 404,221,972	\$ 409,962,715

The Association had no purchases or sales of participation interests with other parties during the quarter ended June 30, 2011. The following table presents information regarding the balances of participations purchased and sold at September 30, 2011:

	Other Farm Credit Institutions		Non-Farm Credit Institutions		Total	
	Participations Purchased	Participations Sold	Participations Purchased	Participations Sold	Participations Purchased	Participations Sold
Real estate mortgage	\$ 7,815,612	\$ -	\$ -	\$ -	\$ 7,815,612	\$ -
Agribusiness	1,530,872	-	-	-	1,530,872	-
Production and intermediate term	758,449	-	-	-	758,449	-
Total	\$ 10,104,933	\$ -	\$ -	\$ -	\$ 10,104,933	\$ -

The allowance for loan losses is maintained at a level considered adequate by management to provide for estimated losses inherent in the loan portfolio. The allowance is based on a periodic evaluation of the loan portfolio by management in which numerous factors are considered, including economic conditions, loan portfolio composition and prior loan loss experience. An analysis of the allowance for loan losses follows:

	<b>September 30, 2011</b>	<b>December 31, 2011</b>
Balance at beginning of quarter	\$ 1,816,453	\$ 1,304,301
Provision for loan losses	948,991	170,105
Charge-offs	(320,944)	(439)
Recoveries	-	16,657
Balance at end of quarter	<u>\$ 2,444,500</u>	<u>\$ 1,490,624</u>

Nonperforming assets (including related accrued interest) and related credit quality statistics are as follows:

	<b>September 30, 2011</b>	<b>December 31, 2010</b>
<b>Nonaccrual loans:</b>		
Real estate mortgage	\$ 6,527,274	\$ 5,360,632
Production and intermediate term	13,096	14,470
Total nonaccrual loans	<u>\$ 6,540,370</u>	<u>\$ 5,375,102</u>
<b>Accruing restructured loans:</b>		
Real estate mortgage	1,248,639	-
Total accruing restructured loans	<u>\$ 1,248,639</u>	<u>\$ -</u>
<b>Accruing loans 90 days or more past due:</b>		
Real estate mortgage	63,523	498,014
Total accruing loans 90 days or more	<u>\$ 63,523</u>	<u>\$ 498,014</u>
Total nonperforming loans	<u>7,852,532</u>	<u>5,873,116</u>
Other property owned	2,169,654	1,900,967
Total nonperforming assets	<u>\$ 10,022,186</u>	<u>\$ 7,774,083</u>

One credit quality indicator utilized by the Association is the Farm Credit Administration Uniform Loan Classification System that categorizes loans into five categories. The categories are defined as follows:

- Acceptable – assets are expected to be fully collectible and represent the highest quality,
- Other assets especially mentioned (OAEM) – assets are currently collectible but exhibit some potential weakness,
- Substandard – assets exhibit some serious weakness in repayment capacity, equity and/or collateral pledged on the loan,
- Doubtful – assets exhibit similar weaknesses to substandard assets; however, doubtful assets have additional weaknesses in existing factors, conditions and values that make collection in full highly questionable, and
- Loss – assets are considered uncollectible.

The following table shows loans and related accrued interest as a percentage of total loans and related accrued interest receivable by loan type as of:

	<b>September 30, 2011</b>	December 31, 2010
Real estate mortgage		
Acceptable	80.8 %	81.1 %
OAEM	13.6	13.6
Substandard/doubtful	2.9	2.9
	<u>97.3 %</u>	<u>97.6 %</u>
Production and intermediate term		
Acceptable	1.0	0.7
OAEM	0.1	0.1
Substandard/doubtful	-	-
	<u>1.1 %</u>	<u>0.8 %</u>
Processing and marketing		
Acceptable	-	-
OAEM	-	-
Substandard/doubtful	0.4	0.4
	<u>0.4 %</u>	<u>0.4 %</u>
Rural residential real estate		
Acceptable	1.2	1.2
OAEM	-	-
Substandard/doubtful	-	-
	<u>1.2 %</u>	<u>1.2 %</u>
Total Loans		
Acceptable	83.0	83.0
OAEM	13.7	13.7
Substandard/doubtful	3.3	3.3
	<u>100.0 %</u>	<u>100.0 %</u>

The following table provides an age analysis of past due loans (including accrued interest) as of September 30, 2011:

	30-89 Days Past Due	90 Days or More Past Due	Total Past Due	Not Past Due or Less Than 30 Days Past Due	Total Loans	Recorded Investment >90 Days and Accruing
Real estate mortgage	\$ 4,760,361	\$ 4,577,143	\$ 9,337,504	\$ 389,685,875	\$ 399,023,379	\$ 63,523
Production and intermediate term	-	-	-	4,471,887	4,471,887	-
Agribusiness:						
Processing and marketing	-	-	-	1,517,912	1,517,912	-
Farm-related business	-	-	-	146,646	146,646	-
Rural residential real estate	-	125,663	125,663	5,095,348	5,221,011	-
Total	<u>\$ 4,760,361</u>	<u>\$ 4,702,806</u>	<u>\$ 9,463,167</u>	<u>\$ 400,917,668</u>	<u>\$ 410,380,835</u>	<u>\$ 63,523</u>

Note: The recorded investment in the receivable is the face amount increased or decreased by applicable accrued interest and unamortized premium, discount, finance charges, or acquisition costs and may also reflect a previous direct write-down of the investment.

Additional impaired loan information is as follows:

	At September 30, 2011			For the Three Months Ended September 30, 2011		For the Nine Months Ended September 30, 2011	
	Recorded	Unpaid	Related	Average	Interest	Average	Interest
	Investment	Principal Balance <sup>a</sup>	Allowance	Impaired Loans	Income Recognized	Impaired Loans	Income Recognized
Impaired loans with a related allowance for credit losses:							
Real estate mortgage	\$ 3,315,038	\$ 4,396,617	\$ 637,990	\$ 3,259,262	\$ -	\$ 4,010,211	\$ -
Impaired loans with no related allowance for credit losses:							
Real estate mortgage	\$ 3,275,759	\$ 3,911,787	\$ -	\$ 3,259,563	\$ 33,315	\$ 2,385,924	\$ 83,868
Farm-related business	13,096	13,096	-	13,345	-	14,032	-
Total	<u>\$ 3,288,855</u>	<u>\$ 3,924,883</u>	<u>\$ -</u>	<u>\$ 3,272,908</u>	<u>\$ 33,315</u>	<u>\$ 2,399,956</u>	<u>\$ 83,868</u>
Total impaired loans:							
Real estate mortgage	\$ 6,590,797	\$ 8,308,404	\$ 637,990	\$ 6,518,825	\$ 33,315	\$ 6,396,135	\$ 83,868
Farm-related business	13,096	13,096	-	13,345	-	14,032	-
Total	<u>\$ 6,603,893</u>	<u>\$ 8,321,500</u>	<u>\$ 637,990</u>	<u>\$ 6,532,170</u>	<u>\$ 33,315</u>	<u>\$ 6,410,167</u>	<u>\$ 83,868</u>

	At December 31, 2010			For the Year Ended December 31, 2010	
	Recorded	Unpaid	Related	Average	Interest
	Investment	Principal Balance <sup>a</sup>	Allowance	Impaired Loans	Income Recognized
Impaired loans with a related allowance for credit losses:					
Real estate mortgage	\$ 1,203,874	\$ 1,203,873	\$ 142,000	\$ 2,978,708	\$ -
Impaired loans with no related allowance for credit losses:					
Real estate mortgage	\$ 4,654,772	\$ 4,654,840	\$ -	\$ 3,155,093	\$ 106,808
Farm-related business	14,470	14,470	-	4,674	-
Total	<u>\$ 4,669,242</u>	<u>\$ 4,669,310</u>	<u>\$ -</u>	<u>\$ 3,159,767</u>	<u>\$ 106,808</u>
Total impaired loans:					
Real estate mortgage	\$ 5,858,646	\$ 5,858,713	\$ 142,000	\$ 6,133,801	\$ 106,808
Farm-related business	14,470	14,470	-	4,674	-
Total	<u>\$ 5,873,116</u>	<u>\$ 5,873,183</u>	<u>\$ 142,000</u>	<u>\$ 6,138,475</u>	<u>\$ 106,808</u>

<sup>a</sup> Unpaid principal balance represents the recorded principal balance of the loan.

A summary of changes in the allowance for loan losses and period end recorded investment in loans is as follows:

	Real Estate Mortgage	Production and Intermediate Term	Agribusiness	Rural Residential Real Estate	Total
<b>Allowance for Credit Losses:</b>					
Balance at					
December 31, 2010	\$ 1,363,462	\$ 2,281	\$ 121,002	\$ 3,879	\$ 1,490,624
Charge-offs	(532,875)	-	-	-	(532,875)
Recoveries	-	-	-	-	-
Provision for loan losses	1,494,001	1,877	(9,597)	470	1,486,751
Adjustment due to merger	-	-	-	-	-
Other	-	-	-	-	-
Balance at					
September 30, 2011	<u>\$ 2,324,588</u>	<u>\$ 4,158</u>	<u>\$ 111,405</u>	<u>\$ 4,349</u>	<u>\$ 2,444,500</u>
Ending Balance:					
individually evaluated for impairment	\$ 646,640	\$ -	\$ -	\$ -	\$ 646,640
Ending Balance:					
collectively evaluated for impairment	<u>\$ 1,677,948</u>	<u>\$ 4,158</u>	<u>\$ 111,405</u>	<u>\$ 4,349</u>	<u>\$ 1,797,860</u>
<b>Recorded Investments in Loans Outstanding:</b>					
Ending Balance at					
September 30, 2011	\$ 399,782,554	\$ 3,712,848	\$ 1,664,422	\$ 5,221,011	\$ 410,380,835
Ending Balance for loans individually evaluated for impairment	<u>\$ 6,527,274</u>	<u>\$ -</u>	<u>\$ 13,096</u>	<u>\$ -</u>	<u>\$ 6,540,370</u>
Ending Balance for loans collectively evaluated for impairment	<u>\$ 393,255,280</u>	<u>\$ 3,712,848</u>	<u>\$ 1,651,326</u>	<u>\$ 5,221,011</u>	<u>\$ 403,840,465</u>

### **NOTE 3 — CAPITAL:**

The Association's board of directors has established a Capital Adequacy Plan (Plan) that includes the capital targets that are necessary to achieve the institution's capital adequacy goals as well as the minimum permanent capital standards. The Plan monitors projected patronage payments, equity retirements and other actions that may decrease the Association's permanent capital. In addition to factors that must be considered in meeting the minimum standards, the board of directors also monitors the following factors: capability of management; quality of operating policies, procedures, and internal controls; quality and quantity of earnings; asset quality and the adequacy of the allowance for losses to absorb potential loss within the loan and lease portfolios; sufficiency of liquid funds; needs of an institution's customer base; and any other risk-oriented activities, such as funding and interest rate risk, potential obligations under joint and several liability, contingent and off-balance-sheet liabilities or other conditions warranting additional capital. At least quarterly, management reviews the Association's goals and objectives with the board.

### **NOTE 4 – CAPITAL MARKETS**

Until the second quarter of 2007, the Association participated in the Capital Markets of the South (CMS), a joint venture created in 2003 for the purpose of expanding the participants' lending opportunities. The CMS group was comprised of the Association, Alabama Ag Credit, ACA, Mississippi Land Bank, ACA, Southern Ag Credit, ACA, and Louisiana Land Bank, ACA. During the second quarter of 2007, the CMS members decided to discontinue and dissolve the joint venture. The associations will continue to service the existing CMS loan portfolio, with revenue and expenses continuing to be shared accordingly as noted below, until such time as all of the loans are fully matured or paid off.

Pursuant to the terms of the alliance, each of the five CMS participating associations generally shares equally in the costs of operating the venture. The Association's pro-rata share of income from CMS operations is recorded in the statement of income in their respective line items. The Association's pro-rata share of expenses from CMS operations is recorded in the statement of income in the line item "Purchased services."

As of September 30, 2011 and December 31, 2010, the Association had CMS related loan volume outstanding in the amount of \$8,888,355 and \$10,693,555 respectively. In addition, the Association had unfunded commitments on CMS loans of \$945,969 as of September 30, 2011.

### **NOTE 5 — INCOME TAXES:**

Alabama Farm Credit, ACA and its subsidiary are subject to federal and certain other income taxes. The associations are eligible to operate as cooperatives that qualify for tax treatment under Subchapter T of the Internal Revenue code. Under specified conditions, the associations can exclude from taxable income amounts distributed as qualified patronage refunds in the form of cash, stock or allocated surplus. Provisions for income taxes are made only on those earnings that will not be distributed as qualified patronage refunds. During the nine months ended September 30, 2011, the Association did participate in a patronage program. Deferred taxes are recorded at the tax effect of all temporary differences based on the assumption that such temporary differences are retained by the institution and will therefore impact future tax payments. A valuation allowance is provided against deferred tax assets to the extent that it is more likely than not (more than 50 percent probability), based on management's estimate, that they will not be realized. For the nine months ended September 30, 2011, and 2010 the Association had no taxable income and tax deferments.

The subsidiary, FLBA of North Alabama, FLCA, is exempt from federal and other income taxes as provided in the Farm Credit Act of 1971.

### **NOTE 6 — FAIR VALUE MEASUREMENTS:**

FASB guidance defines fair value as the exchange price that would be received for an asset or paid to transfer a liability in the principal or most advantageous market for the asset or liability. See Note 12 to the 2010 Annual Report to Stockholders for a more complete description.

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

<u>September 30, 2011</u>	Fair Value Measurement Using			Total Fair Value	Total Gains (Losses)
	Level 1	Level 2	Level 3		
Assets:					
Loans *	\$ -	\$ -	\$ 5,994,678	\$ 5,994,678	\$ 24,180
Other property owned	\$ -	\$ -	\$ 2,169,654	\$ 2,169,654	\$ (137,162)
<u>December 31, 2010</u>	Fair Value Measurement Using			Total Fair Value	Total Gains (Losses)
	Level 1	Level 2	Level 3		
Assets:					
Loans *	\$ -	\$ -	\$ 6,412,615	\$ 6,412,615	\$ (1,936,894)
Other property owned	\$ -	\$ -	\$ 1,900,967	\$ 1,900,967	\$ -

\*Represents the fair value of certain loans that were evaluated for impairment under authoritative guidance, "Accounting by Creditors for Impairment of a Loan." The fair value was based upon the underlying collateral since these were collateral-dependent loans for which real estate is the collateral.

### Valuation Techniques

As more fully discussed in Note 12 to the 2010 Annual Report to Stockholders, authoritative guidance establishes a fair value hierarchy, which requires an entity to maximize the use of observable inputs and minimize the use of unobservable inputs when measuring fair value. The following represent a brief summary of the valuation techniques used for the Associations' assets and liabilities. For a more complete description, see Notes to the 2010 Annual Report to Stockholders

#### Loans

For certain loans evaluated for impairment under authoritative guidance, the fair value is based upon the underlying collateral since the loans were collateral-dependent loans for which real estate is the collateral. 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 real estate, less estimated costs to sell, is less than the principal balance of the loan, a specific reserve is established.

#### Other Property Owned

Other property owned is generally classified as Level 3. The fair value is based upon the collateral value, which is generally determined using appraisals or other indications based on comparable sales of similar properties. Costs to sell represent transaction costs and are not included as a component of the asset's fair value.

### NOTE 7 — EMPLOYEE BENEFIT PLANS:

The following table summarizes the components of net periodic benefit costs of non-pension other postretirement employee benefits for the months ended September 30,:

	Other Benefits	
	2011	2010
Service cost	\$ 19,225	\$ 16,026
Interest cost	54,245	47,031
Expected return on plan assets	-	-
Amortization of prior service costs	(40,908)	(41,901)
Amortizations of net loss	6,817	-
Net periodic benefit cost	<u>\$ 39,379</u>	<u>\$ 21,156</u>

The Association previously disclosed in its financial statements for the year ended December 31, 2010, that it expected to contribute \$30,594 to its other postretirement plan in 2011. As of September 30, 2011, \$24,457 of contributions have been made. The Association presently anticipates contributing an additional \$7,649 to fund its other postretirement plan in 2011 for a total of \$32,106.

**NOTE 8 — COMMITMENTS AND CONTINGENT LIABILITIES:**

The Association is involved in various legal proceedings in the normal course of business. In the opinion of legal counsel and management, there are no legal proceedings at this time that are likely to materially affect the Association.

**NOTE 9 — SUBSEQUENT EVENTS:**

The Association has evaluated subsequent events through November 4, 2011, which is the date the financial statements were issued.