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*Central Kentucky Agricultural Credit Association*

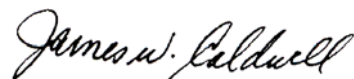
# **SECOND QUARTER 2010**

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## **CERTIFICATION**

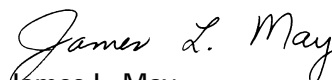
The undersigned certify that we have reviewed the June 30, 2010 quarterly report of Central Kentucky Agricultural Credit Association, that the report has been prepared under the oversight of the Audit Committee of the Board of Directors and in accordance with all applicable statutory or regulatory requirements, and that the information contained herein is true, accurate, and complete to the best of our knowledge and belief.



James W. Caldwell  
Chief Executive Officer



Marcus G. Barnett  
Chief Financial Officer



James L. May  
Chairman of the Board

August 6, 2010

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*Central Kentucky Agricultural Credit Association*

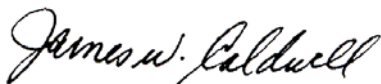
# Report on Internal Control Over Financial Reporting

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.

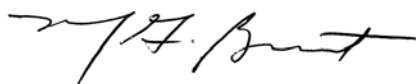
Internal control over financial reporting includes those policies and procedures that: (1) pertain to the maintenance of records that in reasonable detail accurately and fairly reflect the transactions and dispositions of the assets of the Association, (2) provide reasonable assurance that transactions 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 June 30, 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 June 30, 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 June 30, 2010.



James W. Caldwell  
Chief Executive Officer



Marcus G. Barnett  
Chief Financial Officer

August 6, 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 Central Kentucky Agricultural Credit Association (the Association) for the period ended June 30, 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 in our region. The predominate enterprises are beef cattle and thoroughbred horses. Overall, the outlook for the beef cattle industry is cautiously optimistic with better prices in the market but still some concern over the impact of the economic downturn on consumer demand. The thoroughbred horse industry is guarded due to negative effects from the downturn in the general economy. 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 employment in the area, significantly reduces the level of dependency on a given commodity.

The gross loan volume of the Association as of June 30, 2010 was \$263,267, an increase of \$11,519 as compared to \$251,748 at December 31, 2009. Net loans outstanding at June 30, 2010 were \$261,163 as compared to \$249,101 at December 31, 2009. Net loans accounted for 86.73 percent of total assets at June 30, 2010, as compared to 83.64 percent of total assets at December 31, 2009.

The increase in gross and net loan volume during the reporting period is primarily due to growth in real estate loans due to a reduction in agricultural lending activity among other lenders in the region.

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

satisfactory. Nonaccrual loans decreased from \$2,564 at December 31, 2009, to \$447 at June 30, 2010. This decrease is primarily due to the sale of one larger account and a significant paydown on another.

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 \$2,104 allowance for loan losses at June 30, 2010 reflected a \$543 decrease from December 31, 2009, and was considered by management to be adequate to cover possible losses.

## **RESULTS OF OPERATIONS**

### ***For the three months ended June 30, 2010***

Net income for the three months ended June 30, 2010 totaled \$975, as compared to \$191 for the same period in 2009. Net interest income increased \$239 for the three months ended June 30, 2010 as compared to the same period in 2009. The Association recorded a provision for loan losses of \$300 for the three months ended June 30, 2010, as compared to a provision for loan losses of \$600 for the same period in 2009.

At June 30, 2010, interest income on accruing loans increased \$212 compared to June 30, 2009. The Association recorded nonaccrual income of \$0 for the three months ended June 30, 2010, as compared to \$5 for the same period in 2009. Interest income from tobacco successor-in-interest contract (SIIC) investments was \$309 for the three months ended June 30, 2010, as compared to \$380 for the same period in 2009. Interest expense decreased \$98 for the three months ended June 30, 2010 as compared to the comparable period of 2009. Movement in interest income and expense is primarily attributed to increases in loan volume and an early-year reduction in the Association's direct note from receipt of patronage from the AgFirst Farm Credit Bank (Bank). Noninterest income for the three months ended June 30, 2010 totaled \$782, as compared to \$612 for the same period of 2009, an increase of \$170. Increase within this category is primarily attributed to increased income from equity in earnings of the Bank.

Noninterest expense for the three months ended June 30, 2010 decreased \$75 compared to the same period of 2009. The decrease is due primarily to a decrease in FCSIC premiums. The Association recorded no provision for income taxes for the

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three months ended June 30, 2010, and recorded no provision for income taxes for the same period in 2009.

***For the six months ended June 30, 2010***

Net income for the six months ended June 30, 2010 totaled \$2,479, as compared to \$874 for the same period in 2009. Net interest income increased \$426 for the six months ended June 30, 2010 as compared to the same period in 2009. The Association recorded a provision for loan losses of \$350 for the six months ended June 30, 2010, as compared to a provision for loan losses of \$600 for the same period in 2009.

At June 30, 2010, interest income on accruing loans increased \$398 compared to June 30, 2009. The Association recorded nonaccrual income of \$0 for the six months ended June 30, 2010, as compared to \$5 for the same period in 2009. Interest income from tobacco successor-in-interest contract (SIIC) investments was \$622 for the six months ended June 30, 2010, as compared to \$751 for the same period in 2009. Interest expense decreased \$157 for the six months ended June 30, 2010 as compared to the comparable period of 2009. Movement in interest income and expense is primarily attributed to increases in loan volume and an early-year reduction in the Association's direct note from receipt of Bank patronage. Noninterest income for the six months ended June 30, 2010 totaled \$2,038, as compared to \$1,178 for the same period of 2009, an increase of \$860. During the first quarter of 2010, the Association recorded \$605 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. 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. Increase within the Noninterest income category was also attributed to increased income from equity in earnings of the Bank.

Noninterest expense for the six months ended June 30, 2010 decreased \$69 compared to the same period of 2009. The decrease is due primarily to a decrease in FCSIC premiums. The Association recorded no provision for income taxes for the six months ended June 30, 2010, and recorded no provision for income taxes for the same period in 2009.

The financial results of this interim report are not necessarily indicative of the results expected for the year.

**FUNDING SOURCES**

The principal source of funds for the Association is the borrowing relationship established with 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 funds are advanced by the Bank 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. The total notes payable to the Bank at June 30, 2010 was \$260,183 as compared to \$258,279 at December 31, 2009. The increase during the period is primarily attributed to an increase in loan volume partially offset by a decrease in tobacco successor-in-interest contract (SIIC) investments and the receipt at the beginning of the year of AgFirst patronage receivable.

**CAPITAL RESOURCES**

Total members' equity at June 30, 2010 increased to \$38,110 from the December 31, 2009 total of \$35,506. The increase is primarily attributed to the Association's increase in retained earnings as a result of income recorded for the six months ended June 30, 2010. Total capital stock and participation certificates were \$6,304 on June 30, 2010, compared to \$6,185 on December 31, 2009. This increase is attributed to member purchases of equities in relation to increases in loan volume.

Farm Credit Administration (FCA) regulations require all Farm Credit institutions to maintain minimum permanent capital, total surplus and core surplus ratios. These ratios are calculated by dividing the Association's permanent capital, total surplus and core surplus as defined in FCA regulations, by a risk-adjusted asset base. As of June 30, 2010, the Association's permanent capital ratio was 12.75 percent and the total surplus ratio and core surplus ratio were 11.51 percent and 10.83 percent, respectively. All three ratios were well above the minimum regulatory ratios of 7.00 percent for permanent capital and total surplus ratios and 3.50 percent for the core surplus ratio.

**RECENTLY ISSUED ACCOUNTING PRONOUNCEMENTS**

Please refer to Note 1, "Organization, Significant Accounting Policies, and Recently Issued Accounting Pronouncements", in the Notes to the Financial Statements, and the 2009 Annual Report to Shareholders for recently issued accounting pronouncements.

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**NOTE:** Shareholder investment in the Association could be materially 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. 2378, or by writing Stephen Gilbert, AgFirst Farm Credit Bank, P.O. Box 1499, Columbia, SC 29202. Information concerning AgFirst Farm Credit Bank can also be obtained at their website, [www.agfirst.com](http://www.agfirst.com). Copies of the Association's annual and quarterly reports are also available upon request free of charge by calling 1-859-253-3249, or writing Marcus Barnett, Chief Financial Officer, Central Kentucky Agricultural Credit Association, P.O. Box 1290, Lexington, KY 40588-1290, or accessing the website [www.agcreditonline.com](http://www.agcreditonline.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.

# Central Kentucky Agricultural Credit Association

## Consolidated Balance Sheets

<i>(dollars in thousands)</i>	<b>June 30, 2010</b>	<b>December 31, 2009</b>
	<i>(unaudited)</i>	<i>(audited)</i>
<b>Assets</b>		
Cash	\$ 264	\$ 1,710
Loans	263,267	251,748
Less: allowance for loan losses	2,104	2,647
Net loans	261,163	249,101
Other investments	23,864	29,274
Accrued interest receivable	2,755	3,106
Investment in other Farm Credit institutions	7,559	7,559
Premises and equipment, net	3,466	3,516
Other property owned	102	102
Due from AgFirst Farm Credit Bank	1,107	2,313
Other assets	828	1,138
Total assets	\$ 301,108	\$ 297,819
<b>Liabilities</b>		
Notes payable to AgFirst Farm Credit Bank	\$ 260,183	\$ 258,279
Accrued interest payable	759	849
Patronage refund payable	60	614
Other liabilities	1,996	2,571
Total liabilities	262,998	262,313
Commitments and contingencies		
<b>Members' Equity</b>		
Capital stock and participation certificates	6,304	6,185
Retained earnings		
Allocated	13,673	13,717
Unallocated	18,133	15,604
Total members' equity	38,110	35,506
Total liabilities and members' equity	\$ 301,108	\$ 297,819

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

# Central Kentucky Agricultural Credit Association

## Consolidated Statements of Income

*(unaudited)*

<i>(dollars in thousands)</i>	<b>For the three months ended June 30,</b>		<b>For the six months ended June 30,</b>	
	<b>2010</b>	<b>2009</b>	<b>2010</b>	<b>2009</b>
<b>Interest Income</b>				
Loans	\$ 3,687	\$ 3,475	\$ 7,275	\$ 6,877
Other	309	380	622	751
Total interest income	3,996	3,855	7,897	7,628
<b>Interest Expense</b>				
Notes payable to AgFirst Farm Credit Bank	2,344	2,442	4,729	4,886
Net interest income	1,652	1,413	3,168	2,742
Provision for (reversal of allowance for) loan losses	300	600	350	600
Net interest income after provision for (reversal of allowance for) loan losses	1,352	813	2,818	2,142
<b>Noninterest Income</b>				
Loan fees	59	111	146	179
Equity in earnings of other Farm Credit institutions	719	492	1,277	961
Gains (losses) on sale of rural home loans, net	(1)	8	2	16
Insurance Fund refund	—	—	605	—
Other noninterest income	5	1	8	22
Total noninterest income	782	612	2,038	1,178
<b>Noninterest Expense</b>				
Salaries and employee benefits	868	838	1,705	1,671
Occupancy and equipment	79	93	161	188
Insurance Fund premium	1	97	52	183
Other operating expenses	211	206	459	404
Total noninterest expense	1,159	1,234	2,377	2,446
Income before income taxes	975	191	2,479	874
Provision (benefit) for income taxes	—	—	—	—
Net income	\$ 975	\$ 191	\$ 2,479	\$ 874

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

Central Kentucky Agricultural Credit Association  
**Consolidated Statements of Changes in  
Members' Equity**

*(unaudited)*

<i>(dollars in thousands)</i>	<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	\$ 6,453	\$ 11,975	\$ 16,073	\$ 34,501
Net income			874	874
Capital stock/participation certificates issued/(retired), net	126			126
Retained earnings retired		(1)		(1)
Patronage distribution adjustment		(45)	61	16
Balance at June 30, 2009	\$ 6,579	\$ 11,929	\$ 17,008	\$ 35,516
Balance at December 31, 2009	\$ 6,185	\$ 13,717	\$ 15,604	\$ 35,506
Net income			2,479	2,479
Capital stock/participation certificates issued/(retired), net	119			119
Patronage distribution adjustment		(44)	50	6
Balance at June 30, 2010	\$ 6,304	\$ 13,673	\$ 18,133	\$ 38,110

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

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*Central Kentucky 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 Central Kentucky 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 second 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 six months ended June 30, 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 June 30, 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 4).

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

An analysis of the allowance for loan losses follows:

	<b>For the six months ended June 30,</b>	
	<b>2010</b>	<b>2009</b>
Balance at beginning of period	\$ 2,647	\$ 1,469
Provision for (reversal of) loan losses	350	600
Charge-offs	(893)	-
Recoveries	-	2
Balance at end of period	<u>\$ 2,104</u>	<u>\$ 2,071</u>

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

	<b>2010</b>	<b>2009</b>
Impaired loans with related allowance	\$ 204	\$ 1,982
Impaired loans with no related allowance	251	2,231
Total impaired loans	<u>455</u>	<u>4,213</u>
Allowance on impaired loans	<u>\$ 175</u>	<u>\$ 787</u>

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

	<b>2010</b>	<b>2009</b>
Average impaired loans	\$ 1,553	\$ 2,118
Interest income recognized on impaired loans	6	17

## NOTE 3 – EMPLOYEE BENEFIT PLANS

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

	<b>For the six months ended June 30,</b>	
	<b>2010</b>	<b>2009</b>
Pension	\$ 320	\$ 312
401(k)	60	59
Other postretirement benefits	46	56
Total	<u>\$ 426</u>	<u>\$ 427</u>

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

	<b>Actual YTD Through 6/30/10</b>	<b>Projected Contributions For Remainder of 2010</b>	<b>Projected Total Contributions 2010</b>
Pension	\$ -	\$ 579	\$ 579
Other postretirement benefits	20	49	69
Total	<u>\$ 20</u>	<u>\$ 628</u>	<u>\$ 648</u>

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 4 – 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 June 30, 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 or liabilities measured at fair value on a recurring basis at June 30, 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 also could include instruments whose price has been adjusted based on dealer quoted pricing that is different than the third-party valuation or internal model pricing.

Level 3 assets at June 30, 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 June 30, 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 June 30, 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 June 30, 2010 and December 31, 2009 for each of the fair value hierarchy levels:

June 30, 2010				
	Level 1	Level 2	Level 3	Total Fair Value
<b>Liabilities:</b>				
Standby letters of credit	\$ -	\$ -	\$ 19	\$ 19
Total Liabilities	\$ -	\$ -	\$ 19	\$ 19
December 31, 2009				
	Level 1	Level 2	Level 3	Total Fair Value
<b>Liabilities:</b>				
Standby letters of credit	\$ -	\$ -	\$ 21	\$ 21
Total Liabilities	\$ -	\$ -	\$ 21	\$ 21

The following table presents the changes in Level 3 assets and liabilities measured at fair value on a recurring basis for the six months ended June 30, 2010 and 2009. The Association had no transfers of assets or liabilities into or out of Level 1 or Level 2 during the first six months of 2010 and 2009.

	<b>Standby Letters Of Credit</b>
Balance at January 1, 2010	\$ 21
<b>Total gains or (losses) realized/unrealized:</b>	
Included in earnings	-
Included in other comprehensive loss	-
Purchases, sales, issuances and settlements, net	(2)
Transfers in and/or out of level 3	-
Balance at June 30, 2010	<u>\$ 19</u>

	<b>Standby Letters Of Credit</b>
Balance at January 1, 2009	\$ 20
<b>Total gains or (losses) realized/unrealized:</b>	
Included in earnings	-
Included in other comprehensive loss	-
Purchases, sales, issuances and settlements, net	3
Transfers in and/or out of level 3	-
Balance at June 30, 2009	<u>\$ 23</u>

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

Assets and liabilities measured at fair value on a non-recurring basis at June 30, 2010 and December 31, 2009 for each of the fair value hierarchy values are summarized below:

	June 30, 2010				
	Level	Level	Level	Total	YTD
	1	2	3	Fair	Total
<b>Assets:</b>				Value	Gains (Losses)
Impaired loans	\$ -	\$ -	\$ 30	\$ 30	\$ 32
Other property owned	\$ -	\$ -	\$ -	\$ -	\$ -
	<b>December 31, 2009</b>				
	Level	Level	Level	Total	YTD
	1	2	3	Fair	Total
<b>Assets:</b>				Value	Gains (Losses)
Impaired loans	\$ -	\$ -	\$ 1,143	\$ 1,143	\$ (1,069)
Other property owned	\$ -	\$ -	\$ 102	\$ 102	\$ (2)

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

The following table presents the carrying amounts and fair values of the Association's financial instruments at June 30, 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:

	June 30, 2010		December 31, 2009	
	Carrying Amount	Estimated Fair Value	Carrying Amount	Estimated Fair Value
<b>Financial assets:</b>				
Cash	\$ 264	\$ 264	\$ 1,710	\$ 1,710
Loans, net of allowance	\$ 261,163	\$ 265,133	\$ 249,101	\$ 254,323
Tobacco Buyout SIIC	\$ 23,864	\$ 25,857	\$ 29,274	\$ 31,170
<b>Financial liabilities:</b>				
Notes payable to AgFirst Farm Credit Bank	\$ 260,183	\$ 265,509	\$ 258,279	\$ 263,876

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.

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The carrying value of accrued interest approximates its fair value.

**C. Investment in AgFirst Farm Credit Bank and Other Farm Credit Institutions:** Estimating the fair value of the Association's investment in the Bank and Other Farm Credit Institutions is not practicable because the stock is not traded. The net investment is a requirement of borrowing from the Bank and is carried at cost plus allocated equities in the accompanying Consolidated Balance Sheets. The Association owns 1.09 percent of the issued stock of the Bank as of June 30, 2010 net of any reciprocal investment. As of that date, the Bank's assets totaled \$30.7 billion and shareholders' equity totaled \$1.9 billion. The Bank's earnings were \$206.7 million during the first six months of 2010.

**D. Notes Payable to AgFirst Farm Credit Bank:** The notes payable are segregated into pricing pools according to the types and terms of the loans (or other assets) which they fund. Fair value of the notes payable is estimated by discounting the anticipated cash flows of each pricing pool using the current rate that would be charged for additional borrowings. For purposes of this estimate it is assumed the cash flow on the notes is equal to the principal payments on the Association's loan receivables plus accrued interest on the notes payable. This assumption implies that earnings on the Association's interest margin are used to fund operating expenses and capital expenditures.

**E. Commitments to Extend Credit:** The estimated market value of off-balance-sheet commitments is minimal since the committed rate approximates current rates offered for commitments with similar rate and maturity characteristics and since the related credit risk is not significant.

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

#### **NOTE 6 – SUBSEQUENT EVENTS**

The Association has evaluated subsequent events and has determined there are none requiring disclosure through August 6, 2010, which is the date the financial statements were issued.