*Puerto Rico Farm Credit, ACA*

# SECOND QUARTER 2012

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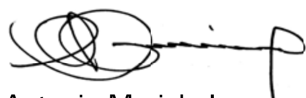
## CERTIFICATION

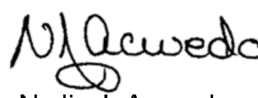
The undersigned certify that we have reviewed the June 30, 2012 quarterly report of Puerto Rico Farm Credit, ACA, that the report has been prepared under the oversight of the Audit Committee of the Board of Directors and in accordance with all applicable statutory or regulatory requirements, and that the information contained herein is true, accurate, and complete to the best of our knowledge and belief.

Robert G. Miller
Chairman of Board of Directors

Ricardo L. Fernández
Chief Executive Officer



Antonio Marichal
Member of Board of Directors
Chairman of the Audit Committee



Nydia J. Acevedo
Controller

August 8, 2012

# Report on Internal Control Over Financial Reporting

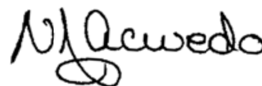
The Association's principal executives and principal financial officers, or persons performing similar functions, are responsible for establishing and maintaining adequate internal control over financial reporting for the Association's Consolidated Financial Statements. For purposes of this report, "internal 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, 2012. 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, 2012, 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, 2012.

Ricardo L. Fernández
Chief Executive Officer



Nydia J. Acevedo
Controller

August 8, 2012

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

*(dollars in thousands)*

The following commentary reviews the consolidated financial condition and results of operations of Puerto Rico Farm Credit, ACA (Association) for the six months ended June 30, 2012. These comments should be read in conjunction with the accompanying consolidated financial statements, notes to the consolidated financial statements, and the 2011 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 short and intermediate-term loans and long-term real estate mortgage loans. The Association also maintains a portfolio of purchased loans, originated by other Farm Credit System entities and non-system entities. The Association's predominant chartered territory agricultural commodities were dairy, livestock, rural home and field crops which totaled approximately $104,625 or 59.36 percent of all outstanding loan volume at June 30, 2012.

The outstanding loan volume of the Association at June 30, 2012 was $166,920 a decrease of $8,462 or 4.82 percent as compared to $175,382 at December 31, 2011. Loans originated within the Association's chartered territory were lower by approximately $3,196, while participation loans purchased decreased by approximately $5,266.

Net loans outstanding at June 30, 2012 totaled $163,730 as compared to $171,900 at December 31, 2011. The decrease in the net loan volume is attributed to scheduled repayments in the loan portfolio and a reduced demand for credit in the market. Net loans made up 89.26 percent of total assets at June 30, 2012, as compared to 89.61 percent at December 31, 2011.

As a percentage of outstanding loans, nonaccrual loans totaled 9.36 percent at June 30, 2012, compared with 9.66 percent at December 31, 2011. The decrease in the percentage of nonaccrual loan volume during the first six months of 2012 was primarily the result of four loans amounting $1,160 being transferred to acquired property (three chartered territory loans and one participation loan); and two nonaccrual chartered territory loans amounting $718 being paid in full, for a total decrease of approximately $1,878. This reduction in the nonaccrual portfolio was partially offset by five loans being transferred from accruing to nonaccrual totaling approximately $1,030. Some borrowers have continued to find it difficult to maintain payments current in a depressed economic environment. However, the overall delinquency rate for the chartered territory accruing loan portfolio has remained stable, as a result of good credit administration practices and a low interest rate environment.

Management continues to monitor and remains cautious about the credit quality of certain chartered territory and participation loans through 2012.

The allowance for loan losses decreased by $292 to $3,190 at June 30, 2012, from $3,482 at December 31, 2011. The decrease was primarily due to small charge offs recorded on various nonaccrual loans transferred to acquired property that reduced the specific reserve for the impaired loans evaluated individually.

The total allowance for loan losses to outstanding loan volume ratio decreased to 1.91 percent at June 30, 2012 from 1.99 percent at December 31, 2011 as a result of a decrease in loan volume. During the first six months of 2012, charge-offs recognized totaled $93 while recoveries totaled $153.

Management anticipates additional provision expense, charge-off activity and loss of sale of acquired property during the remainder of 2012. Some problem loans identified in both, the chartered territory and participation's portfolio may be transferred into non-accrual, thereby, requiring specific reserves. In addition, three industries in the United States, in which the Association participated loans such as, ethanol, forestry and poultry, continue experiencing economic hardship and borrowers in these industries continue to phase difficulties in maintaining repayment capacity. Management is also monitoring the local dairy industry as feed prices may impact the ability of farmers to repay their debt. Enhanced stress-testing of the allowance for loan loss may also lead to additional provision expense in 2012. The ACA is actively marketing acquired properties and may incur in accounting loses as sales are completed.

The Association will continue to search for opportunities to fulfill its public mission. The Board of Directors and management remain cautious of the ACA's ability to quickly grow the portfolio under the prevailing economic environment. Management will focus on targeted marketing

to viable farmers in sectors demonstrating the ability to grow and remain competitive in a changing marketplace.

## RESULTS OF OPERATIONS

### For the three months ended June 30, 2012

For the second quarter of 2012, the Association recognized net income from operations of $1,454 for an increase of $1,743 when compared to a net loss from operations of $289 for the second quarter of 2011. The primary driver of this increase is the review of the allowance for loan losses that resulted in a reversal of $353 for the three months ended June 30, 2012. When compared with the $671 provision expense recognized as of June 30, 2011, the result is an increase of $1,024 between quarters. In addition, during the second quarter of 2012, the Association received a nonrecurring insurance premium refund from the Farm Credit System Insurance Corporation (FCSIC) which totaled $679.

Net interest income for the three months ended June 30, 2012 was $1,145 compared to $985 for the three months ended June 30, 2011. Interest income increased year-over-year even though the accruing loan volume decreased primarily due to various loans transferred to nonaccrual status. This was offset by a reduction in the cost of funds and improved spreads on new and serviced loans, which sustained net interest income.

Noninterest income for the three months ended June 30, 2012, including net gains or losses on other property owned, was $1,177 compared to $531 for the same period of 2011 resulting in an increase of $646. The increase was mostly related with the $679 nonrecurring insurance premium refund from FCSIC partially offset by a decrease of $33 in the patronage refunds from other Farm Credit institutions due to a decrease in the total portfolio average daily balance.

For the second quarter of 2012, noninterest expense increased by $87, from $1,134 to $1,221 as compared to the second quarter of 2011. The increase year-over-year is primarily attributed to purchased services and other operating expenses.

### For the six months ended June 30, 2012

For the six months ended June 30, 2012, the Association recognized net income of $1,639. This was an increase of $1,710 as compared to a net loss of $71 for the first six months of 2011. The increase primarily resulted from an increase of provision expense to record the charge offs.

During the first six months of 2012, interest income, primarily from accruing loans decreased by $155 or 2.03 percent. Interest expense related to the notes payable to AgFirst FCB (the Bank) decreased by $280 or 3.66 percent. Thus, net interest income increased by $125 or 1.63 percent. The increase in net interest income was due primarily to the reduction in the cost of funds and the improvements in the spreads on loans.

Noninterest income for the first half of 2012 was $1,595 or 86.77 percent higher than the $854 recognized during the first half of 2011. The increase was primarily attributable to the non-recurring income of $679 refund distributions received from the FCSIC during the second quarter of 2012.

Noninterest expense for the six months ended June 30, 2012 increased by $179 or 7.79 percent compared to the same six month period of 2011. The increase was primarily related to an increase of salaries and employee benefits of $18 related to one time severance payments and other operating expenses.

Although the Association is subject to federal income tax, the Association does not expect to incur a federal tax liability in 2012 due to the taxable loss carryforward. No provision for income taxes has been recognized in 2012.

***Key Results of Operations Ratios***

| | Annualized for the six months ended 6/30/12 | For the year ended 12/31/11 |
|---|---|---|
| Return on Average Assets | 1.76% | (0.50)% |
| Return on Average Equity | 7.12% | (2.14)% |
| Net Interest Income as a Percentage of Average Earning Assets | 2.40% | 2.34% |

## LIQUIDITY AND FUNDING SOURCES

*Liquidity*

Liquidity management is the process whereby funds are made available to meet all financial commitments including the extension of credit, payment of operating expenses and payment of debt obligations. The Association receives access to funds through its borrowing relationship with the Bank and from income generated by operations. Sufficient liquid funds have been available to meet all financial obligations.

*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 notes. The variable rate notes are utilized by the Association to fund variable rate loan advances and operating fund requirements.

The total notes payable to the Bank at June 30, 2012 were $133,189 as compared with $143,364 at December 31, 2011. The decrease of $10,175 or 7.10 percent corresponded closely to the decrease in outstanding loan volume of $8,170.

See Note 6 in the Notes to the Consolidated Financial Statements for additional information on the status of compliance with covenants under the General Financing Agreement.

The Association had no lines of credit outstanding with third parties as of June 30, 2012.

*Funds Management*

Demand for loan types is a driving force in establishing a funds management strategy. The Association offers variable and fixed rate loan products which are competitively priced according to local market rates. Variable rate loans are generally indexed to either the Prime rate or the London Interbank Offered Rate (LIBOR). The majority of the interest rate risk in the Association balance sheet is transferred to the Bank through the notes payable structure. The Bank, in turn, actively utilizes funds management techniques to identify, quantify and control interest rate risk associated with the loan portfolio.

## CAPITAL RESOURCES

Total members' equity at June 30, 2012 increased 3.60 percent to $47,462 from December 31, 2011 when total members' equity was $45,813. The increase of $1,647 was primarily attributable to the year-to-date net income which totaled $1,639 at June 30, 2012.

Total capital stock and participation certificates were $626 on June 30, 2012 compared to $648 on December 31, 2011. The decrease of $22 was the net result of refunding more stock to non-borrowing stockholders than new stockholders purchasing capital stock or participation certificates.

Unallocated retained earnings increased $1,639 or 3.65 percent from December 31, 2011 when unallocated retained earnings totaled $44,886. The increase was due to the net income during the first six months of 2012.

The Association's regulatory permanent capital ratio at June 30, 2012 was 20.37 percent compared to 18.61 percent at December 31, 2011. The Association's total surplus and core surplus ratios were both 19.98 percent at June 30, 2012. 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.

***Key financial condition ratios were as follows:***

| | 6/30/12 | 12/31/11 |
|---|---|---|
| Total Members' Equity to Asset | 25.87% | 23.88% |
| Debt to Total Members' Equity | 2.86:1 | 3.19:1 |

## REGULATORY MATTERS

***<u>FCA Supervisory Agreement</u>***

As previously disclosed, on March 17, 2011 the Farm Credit Administration (FCA) entered into a written Supervisory Agreement (SA) with the Board of Directors of the Association. This agreement supersedes FCA Supervisory Letters dated July 23, 2009, March 2, 2010, and December 10, 2010 and incorporates certain requirements from these letters. The Supervisory Agreement requires the Board of Directors to take certain corrective and precautionary measures with respect to some Association practices, including board governance and operation, director fiduciary duties, nominating committee procedures, board policies, board business planning, Association earnings and liquidity, senior management and human capital development, internal audit and review, asset quality, allowance for loan losses and collateral risk management, and capital markets and participation activities. In addition, the SA prohibits the Association from distributing patronage-sourced income without FCA consent.

Conditions and events that led to the need for this agreement include portfolio credit quality deterioration, high turnover in senior management, perceived weaknesses in board governance, and, reduced earnings and liquidity. The Board of Directors and the Association have worked during the year to reach several milestones. On October 4, 2011, FCA communicated in a letter to the board that efforts had led to an overall rating of "partial compliance" with the agreement and encouraged the board to continue working towards achieving full compliance with the agreement. On February 14, 2012, FCA again communicated in a letter to the Board that it had achieved incremental progress towards complying with the Agreement but that improved business results had not yet materialized. The FCA delivered an in person report of examination to the Board of Directors on June 13, 2012 with updated results. The Association had achieved full compliance in 4 out 17 items, substantial compliance in 8 out of 17 items and partial compliance in 5 out 17 items. Some of the results achieved in compliance with the agreement include the following:

- Hiring a board consultant and continued work with the consultant to assist the Board in fulfilling its fiduciary duties and improving board operations and governance.
- Updating its board committee charters, undergoing several training sessions and changing leadership to improve governance of the Association.

- Revising the director candidate nominating procedures to qualify new candidates, which led to stockholders electing two new directors to the Board.
- Hiring a new CEO beginning on February 1, 2011 to lead the Association after the retirement of the previous CEO on June 30, 2010.
- Overseeing the implementation of updated collateral risk management policies and procedures that are in line with best practices in the industry.
- Improving the methodology used to calculate the Allowance for Loan Losses of the Association.
- Hiring a specialized third party auditor that assessed the capital markets portfolio credit risk and helped, strengthened credit policies and procedures.
- Establishing a Compliance Committee to monitor management's progress in implementing the corrective actions of items identified in the SA.
- Ensuring that FCA's recommendations are incorporated in the various action plans.
- Reviewing the Association's internal audit plan to focus on areas where perceived weaknesses were identified.
- Establishing a risk assessment process to assess risks and controls in the ACA.
- Establishing an asset quality improvement plan to monitor management efforts in managing high risk loans.
- Revising the 2011 business plan to establish strategic priorities and to comply with FCA regulations governing business planning.
- Establishing a human capital plan and succession plan to assist in the long-term success of the Association.
- Revising board policies on a quarterly basis to guide management in conducting day to day operations.
- Enhancing the participation's portfolio credit underwriting and administration controls.

All required measures have not been achieved or completed as of the date of this report and the Board of Directors continues to work with the management team in improving the areas identified in the Supervisory Agreement. Besides the ongoing corrective actions already mentioned, other actions to be taken target the following areas.

- Improving board efficacy in overseeing the Association's business practices by updating board policies. This review of board policies was completed subsequent to the end of the quarter.
- Improving risk management work in the area of stress-testing.
- Building a cohesive senior management team.
- Developing strategies for growing the Association's loan portfolio with high quality loans to improve asset quality and, enhance earnings and liquidity.

The Board of Directors will continue engaging a board consultant to provide advice in understanding and fulfilling its fiduciary responsibilities and to perform other advisory functions as specified in the agreement. Both the Board of Directors and Senior Management are committed to continuing the administration of the Association in a sound manner, compliant with all FCA Regulations.

The Association remained under written supervisory agreement as of the date of this report.

**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 2011 Annual Report to Shareholders for recently issued accounting pronouncements.

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**NOTE**: Shareholder investment in the Association could be affected by the financial condition and results of operations of AgFirst Farm Credit Bank. Copies of AgFirst's annual and quarterly reports are available upon request free of charge by calling 1-800-845-1745, ext. 2832, or writing Susanne Caughman, AgFirst Farm Credit Bank, P.O. Box 1499, Columbia, SC 29202. Information concerning AgFirst Farm Credit Bank can also be obtained at its website, *www.agfirst.com*. Copies of the Association's annual and quarterly reports are also available upon request free of charge by calling 1-800-981-3323, or writing Nydia J. Acevedo, Controller, Puerto Rico Farm Credit, ACA, PO Box 363649, San Juan, PR 00936-3649, or accessing the website, *www.puertoricofarmcredit.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 Association.

Puerto Rico Farm Credit, ACA

# Consolidated Balance Sheets

| (dollars in thousands) | | June 30, 2012 | | December 31, 2011 |
|---|---|---|---|---|
| | | (unaudited) | | (audited) |
| **Assets** | | | | |
| Cash | $ | 255 | $ | 164 |
| Loans | | 166,920 | | 175,382 |
| Less: allowance for loan losses | | 3,190 | | 3,482 |
| Net loans | | 163,730 | | 171,900 |
| Notes receivable from other Farm Credit institutions (Note 5) | | 10,000 | | 10,000 |
| Accrued interest receivable | | 676 | | 568 |
| Investments in other Farm Credit institutions | | 2,706 | | 2,706 |
| Premises and equipment, net | | 870 | | 916 |
| Other property owned | | 3,515 | | 2,489 |
| Deferred tax asset, net | | 16 | | — |
| Due from AgFirst Farm Credit Bank | | 550 | | 1,479 |
| Other assets | | 1,116 | | 1,610 |
| Total assets | $ | 183,434 | $ | 191,832 |
| **Liabilities** | | | | |
| Notes payable to AgFirst Farm Credit Bank | $ | 133,189 | $ | 143,364 |
| Accrued interest payable | | 247 | | 274 |
| Other liabilities | | 2,536 | | 2,381 |
| Total liabilities | | 135,972 | | 146,019 |
| Commitments and contingencies | | | | |
| **Members' Equity** | | | | |
| Capital stock and participation certificates | | 626 | | 648 |
| Unallocated retained earnings | | 46,525 | | 44,886 |
| Accumulated other comprehensive income (loss) | | 311 | | 279 |
| Total members' equity | | 47,462 | | 45,813 |
| Total liabilities and members' equity | $ | 183,434 | $ | 191,832 |

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

Puerto Rico Farm Credit, ACA

# Consolidated Statements of Operations

*(unaudited)*

| *(dollars in thousands)* | For the three months ended June 30, 2012 | For the three months ended June 30, 2011 | For the six months ended June 30, 2012 | For the six months ended June 30, 2011 |
|---|---|---|---|---|
| **Interest Income** | | | | |
| Loans | $ 1,669 | $ 1,650 | $ 3,240 | $ 3,395 |
| Notes receivable from other Farm Credit institutions (Note 5) | 225 | 225 | 450 | 450 |
| Total interest income | 1,894 | 1,875 | 3,690 | 3,845 |
| **Interest Expense** | | | | |
| Notes payable to AgFirst Farm Credit Bank | 749 | 890 | 1,521 | 1,801 |
| Net interest income | 1,145 | 985 | 2,169 | 2,044 |
| Provision for (reversal of allowance for) loan losses | (353) | 671 | (352) | 671 |
| Net interest income after provision for (reversal of allowance for) loan losses | 1,498 | 314 | 2,521 | 1,373 |
| **Noninterest Income** | | | | |
| Loan fees | 57 | 68 | 78 | 123 |
| Patronage rebate fees | 56 | 59 | 115 | 117 |
| Patronage refunds from other Farm Credit institutions | 364 | 397 | 643 | 696 |
| Gains (losses) on other property owned, net | 14 | 5 | 31 | (97) |
| Insurance Fund refunds | 679 | — | 679 | — |
| Other noninterest income | 7 | 2 | 49 | 15 |
| Total noninterest income | 1,177 | 531 | 1,595 | 854 |
| **Noninterest Expense** | | | | |
| Salaries and employee benefits | 735 | 760 | 1,551 | 1,533 |
| Occupancy and equipment | 77 | 72 | 144 | 140 |
| Insurance Fund premiums | 20 | 24 | 41 | 50 |
| Other operating expenses | 389 | 278 | 741 | 575 |
| Total noninterest expense | 1,221 | 1,134 | 2,477 | 2,298 |
| Net income (loss) | $ 1,454 | $ (289) | $ 1,639 | $ (71) |

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

Puerto Rico Farm Credit, ACA

# Consolidated Statements of Comprehensive Income (Loss)

*(unaudited)*

| *(dollars in thousands)* | For the three months ended June 30, 2012 | For the three months ended June 30, 2011 | For the six months ended June 30, 2012 | For the six months ended June 30, 2011 |
|---|---|---|---|---|
| Net income (loss) | $ 1,454 | $ (289) | $ 1,639 | $ (71) |
| **Other comprehensive income net of tax** | | | | |
| Employee benefit plans adjustments | 16 | 21 | 32 | 42 |
| Comprehensive income (loss) | $ 1,470 | $ (268) | $ 1,671 | $ (29) |

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

Puerto Rico Farm Credit, ACA

# Consolidated Statements of Changes in Members' Equity

*(unaudited)*

| *(dollars in thousands)* | Capital Stock and Participation Certificates | Unallocated Retained Earnings | Accumulated Other Comprehensive Income (Loss) | Total Members' Equity |
|---|---|---|---|---|
| Balance at December 31, 2010 | $ 679 | $ 45,878 | $ (208) | $ 46,349 |
| Comprehensive income (loss) | | (71) | 42 | (29) |
| Capital stock/participation certificates issued/(retired), net | (15) | | | (15) |
| Balance at June 30, 2011 | $ 664 | $ 45,807 | $ (166) | $ 46,305 |
| | | | | |
| Balance at December 31, 2011 | $ 648 | $ 44,886 | $ 279 | $ 45,813 |
| Comprehensive income | | 1,639 | 32 | 1,671 |
| Capital stock/participation certificates issued/(retired), net | (22) | | | (22) |
| Balance at June 30, 2012 | $ 626 | $ 46,525 | $ 311 | $ 47,462 |

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

# 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 Puerto Rico Farm Credit, ACA (the Association). A description of the organization and operations of the Association, the significant accounting policies followed, and the financial condition and results of operations as of and for the year ended December 31, 2011, are contained in the 2011 Annual Report of the Association. These unaudited second quarter 2012 consolidated financial statements should be read in conjunction with the 2011 Annual Report of the Association.

The accompanying consolidated financial statements contain all necessary adjustments 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, 2012 are not indicative of the results to be expected for the year ending December 31, 2012.

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, 2012, the allowance for losses is adequate in management's opinion to provide for possible losses on existing loans.

**Recently Issued Accounting Pronouncements**

In June 2011, the Financial Accounting Standards Board (FASB) issued ASU 2011-05, "Comprehensive Income (Topic 220): Presentation of Comprehensive Income." This amendment 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 was 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: (1) 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; (2) 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. With either approach, an entity is required to present reclassification adjustments for items reclassified from other comprehensive income to net income in the statement(s). This guidance is to be applied retrospectively. For public entities, it is effective for fiscal years, and interim periods within those years, beginning after December 15, 2011. The adoption of this guidance did not impact the Association's financial condition or results of operations, but resulted in changes to the presentation of comprehensive income. In December 2011, the FASB issued guidance (ASU 2011-12; Topic 220) to defer the new requirement to present components of accumulated other comprehensive income reclassified as components of net income on the face of the financial statements. All other requirements in the guidance for comprehensive income were required to be adopted as set forth in the June 2011 guidance. The deferral is effective at the same time the new standard on comprehensive income is adopted.

In May 2011, the FASB issued ASU 2011-04, "Fair Value Measurement (Topic 820): 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) Aligns 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) Clarifies 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) Clarifies 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. The adoption of this guidance did not impact the Association's financial condition or results of operations, but resulted in additional disclosures.

In April 2011, the FASB issued ASU 2011-02, "Receivables (Topic 310): A Creditor's Determination of Whether a Restructuring is a Troubled Debt Restructuring," which provides for clarification on whether a restructuring constitutes a troubled debt restructuring (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. The guidance is effective for nonpublic entities, for annual periods ending on or after December 15, 2012, including interim periods within those annual periods. The guidance should be applied retrospectively to the beginning of the annual period of adoption. The new disclosures about TDR activity required by the guidance on "Disclosures about the Credit Quality of Financing Receivables and the Allowance for Credit Losses," as discussed below, are effective for annual reporting periods ending after December 15, 2011.

In January 2011, the FASB issued ASU 2011-01, "Receivables (Topic 310): Deferral of the Effective Date of Disclosures about Troubled Debt Restructurings." This amendment temporarily delayed the effective date of the disclosures about TDRs 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 TDRs coincides with the guidance for determining what constitutes a TDR as described above. The adoption of this guidance had no material impact on the Association's financial condition and results of operations but resulted in significant additional disclosures.

Other recently issued accounting pronouncements are discussed in the 2011 Annual Report to Shareholders.

**Note 2 — Loans and Allowance for Loan Losses**

A summary of loans outstanding at period end were as follows:

| | June 30, 2012 | December 31, 2011 |
|---|---|---|
| Real estate mortgage | $ 107,374 | $ 113,241 |
| Production and intermediate-term | 35,171 | 32,628 |
| Agribusiness | | |
| Processing and marketing | 4,026 | 6,559 |
| Farm-related business | 708 | 732 |
| Total agribusiness | 4,734 | 7,291 |
| Communication | – | 1,261 |
| Energy | 2,020 | 2,480 |
| Rural residential real estate | 17,621 | 18,481 |
| Total Loans | $ 166,920 | $ 175,382 |

The Association may purchase or sell participation interests with other parties in order to diversify risk, manage loan volume, and comply with Farm Credit Administration regulations. Participations purchased and sold balances at period end were as follows:

| | June 30, 2012 | | | | | | | |
|---|---|---|---|---|---|---|---|---|
| | Within AgFirst District | | Within Farm Credit System | | Outside Farm Credit System | | Total | |
| | Participations Purchased | Participations Sold | Participations Purchased | Participations Sold | Participations Purchased | Participations Sold | Participations Purchased | Participations Sold |
| Real estate mortgage | $ 1,787 | $ 11,780 | $ – | $ – | $ 1,043 | $ – | $ 2,830 | $ 11,780 |
| Production and intermediate term | 21,592 | 589 | – | – | 848 | – | 22,440 | 589 |
| Agribusiness | | | | | | | | |
| Processing and marketing | 3,235 | – | – | – | 729 | – | 3,964 | – |
| Farm-related business | – | – | – | – | 685 | – | 685 | – |
| Total agribusiness | 3,235 | – | – | – | 1,414 | – | 4,649 | – |
| Energy | 2,021 | – | – | – | – | – | 2,021 | – |
| Total | $ 28,635 | $ 12,369 | $ – | $ – | $ 3,305 | $ – | $ 31,940 | $ 12,369 |

| | December 31, 2011 | | | | | | | |
|---|---|---|---|---|---|---|---|---|
| | Within AgFirst District | | Within Farm Credit System | | Outside Farm Credit System | | Total | |
| | Participations Purchased | Participations Sold | Participations Purchased | Participations Sold | Participations Purchased | Participations Sold | Participations Purchased | Participations Sold |
| Real estate mortgage | $ 2,044 | $ 10,403 | $ – | $ – | $ 1,260 | $ – | $ 3,304 | $ 10,403 |
| Production and intermediate term | 22,874 | – | – | – | 939 | – | 23,813 | – |
| Agribusiness | | | | | | | | |
| Processing and marketing | 6,371 | – | – | – | 791 | – | 7,162 | – |
| Farm-related business | – | – | – | – | 702 | – | 702 | – |
| Total agribusiness | 6,371 | – | – | – | 1,493 | – | 7,864 | – |
| Communication | 1,267 | – | – | – | – | – | 1,267 | – |
| Energy | 2,485 | – | – | – | – | – | 2,485 | – |
| Total | $ 35,041 | $ 10,403 | $ – | $ – | $ 3,692 | $ – | $ 38,733 | $ 10,403 |

A significant source of liquidity for the Association is the repayments and maturities of loans. The following table presents the contractual maturity distribution of loans by loan type at June 30, 2012 and indicates that approximately 34.90 percent of loans had maturities of less than one year:

| | Due less than 1 year | Due 1 Through 5 years | Due after 5 years | Total |
|---|---|---|---|---|
| Real estate mortgage | $ 29,998 | $ 43,510 | $ 33,866 | $ 107,374 |
| Production and intermediate-term | 24,303 | 9,409 | 1,459 | 35,171 |
| Agribusiness | | | | |
| Processing and marketing | 1,622 | 1,302 | 1,102 | 4,026 |
| Farm-related business | – | – | 708 | 708 |
| Total agribusiness | 1,622 | 1,302 | 1,810 | 4,734 |
| Energy | 2,020 | – | – | 2,020 |
| Rural residential real estate | 308 | 314 | 16,999 | 17,621 |
| Total Loans | $ 58,251 | $ 54,535 | $ 54,134 | $ 166,920 |

The following table shows loans and related accrued interest classified under the Farm Credit Administration Uniform Loan Classification System as a percentage of total loans and related accrued interest receivable by loan type.

| | June 30, 2012 | December 31, 2011 |
|---|---|---|
| **Real estate mortgage:** | | |
| Acceptable | 80.26% | 82.64% |
| OAEM | 3.80 | 2.69 |
| Substandard/doubtful/loss | 15.94 | 14.67 |
| | 100.00% | 100.00% |
| **Production and intermediate-term:** | | |
| Acceptable | 72.66% | 69.54% |
| OAEM | 10.47 | 13.07 |
| Substandard/doubtful/loss | 16.87 | 17.39 |
| | 100.00% | 100.00% |
| **Agribusiness:** | | |
| **Processing and marketing:** | | |
| Acceptable | 38.53% | 57.24% |
| OAEM | 26.16 | 18.94 |
| Substandard/doubtful/loss | 35.31 | 23.82 |
| | 100.00% | 100.00% |
| **Farm-related business:** | | |
| Acceptable | 100.00% | 100.00% |
| OAEM | – | – |
| Substandard/doubtful/loss | – | – |
| | 100.00% | 100.00% |

| | June 30, 2012 | December 31, 2011 |
|---|---|---|
| **Total agribusiness:** | | |
| Acceptable | 47.69% | 61.52% |
| OAEM | 22.26 | 17.05 |
| Substandard/doubtful/loss | 30.05 | 21.43 |
| | 100.00% | 100.00% |
| **Communication:** | | |
| Acceptable | –% | 100.00% |
| OAEM | – | – |
| Substandard/doubtful/loss | – | – |
| | –% | 100.00% |
| **Energy and water/waste disposal:** | | |
| Acceptable | 100.00% | 100.00% |
| OAEM | – | – |
| Substandard/doubtful/loss | – | – |
| | 100.00% | 100.00% |
| **Rural residential real estate:** | | |
| Acceptable | 91.72% | 91.11% |
| OAEM | 2.50 | 3.67 |
| Substandard/doubtful/loss | 5.78 | 5.22 |
| | 100.00% | 100.00% |
| **Total Loans:** | | |
| Acceptable | 79.18% | 80.59% |
| OAEM | 5.55 | 5.26 |
| Substandard/doubtful/loss | 15.27 | 14.15 |
| | 100.00% | 100.00% |

The following tables provide an aging analysis of past due loans and related accrued interest.

| | June 30, 2012 | | | | | |
|---|---|---|---|---|---|---|
| | 30 Through 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 or More Past Due and Accruing Interest |
| Real estate mortgage | $ 1,400 | $ 9,735 | $ 11,135 | $ 96,628 | $ 107,763 | $ – |
| Production and intermediate-term | 1,298 | 3,402 | 4,700 | 30,602 | 35,302 | – |
| Agribusiness | | | | | | |
| Processing and marketing | – | – | – | 4,051 | 4,051 | – |
| Farm-related business | – | – | – | 710 | 710 | – |
| Total agribusiness | – | – | – | 4,761 | 4,761 | – |
| Energy and water/waste disposal | – | – | – | 2,020 | 2,020 | – |
| Rural residential real estate | 252 | 134 | 386 | 17,289 | 17,675 | – |
| Total | $ 2,950 | $ 13,271 | $ 16,221 | $ 151,300 | $ 167,521 | $ – |

| | December 31, 2011 | | | | | |
|---|---|---|---|---|---|---|
| | 30 Through 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 or More Past Due and Accruing Interest |
| Real estate mortgage | $ 2,787 | $ 11,099 | $ 13,886 | $ 99,675 | $ 113,561 | $ – |
| Production and intermediate-term | 1,203 | 3,722 | 4,925 | 27,785 | 32,710 | – |
| Agribusiness | | | | | | |
| Processing and marketing | – | (2) | (2) | 6,596 | 6,594 | – |
| Farm-related business | – | – | – | 734 | 734 | – |
| Total agribusiness | – | (2) | (2) | 7,330 | 7,328 | – |
| Communication | – | – | – | 1,261 | 1,261 | – |
| Energy and water/waste disposal | – | – | – | 2,481 | 2,481 | – |
| Rural residential real estate | 1,092 | 263 | 1,355 | 17,179 | 18,534 | – |
| Total | $ 5,082 | $ 15,082 | $ 20,164 | $ 155,711 | $ 175,875 | $ – |

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.

Nonperforming assets (including related accrued interest) and related credit quality statistics at period end were as follows:

| | June 30, 2012 | December 31, 2011 |
|---|---|---|
| **Nonaccrual loans:** | | |
| Real estate mortgage | $ 10,337 | $ 11,239 |
| Production and intermediate-term | 4,591 | 4,964 |
| Agribusiness | | |
| Processing and marketing | – | (2) |
| Rural residential real estate | 697 | 734 |
| Total nonaccrual loans | $ 15,625 | $ 16,935 |
| **Accruing restructured loans:** | | |
| Real estate mortgage | $ 4,014 | $ 4,021 |
| Total accruing restructured loans | $ 4,014 | $ 4,021 |
| **Accruing loans 90 days or more past due:** | $ – | $ – |
| Total nonperforming loans | $ 19,639 | $ 20,956 |
| Other property owned | 3,515 | 2,489 |
| Total nonperforming assets | $ 23,154 | $ 23,445 |
| Nonaccrual loans as a percentage of total loans | 9.36% | 9.66% |
| Nonperforming assets as a percentage of total loans and other property owned | 13.59% | 13.18% |
| Nonperforming assets as a percentage of capital | 48.78% | 51.18% |

The following table presents information relating to impaired loans (including accrued interest) at period end. Impaired loans are loans for which it is probable that all principal and interest will not be collected according to the contractual terms of the loan.

| | June 30, 2012 | December 31, 2011 |
|---|---|---|
| Impaired nonaccrual loans: | | |
| Current as to principal and interest | $ 2,157 | $ 1,379 |
| Past due | 13,468 | 15,556 |
| Total impaired nonaccrual loans | 15,625 | 16,935 |
| Impaired accrual loans: | | |
| Restructured | 4,014 | 4,021 |
| 90 days or more past due | – | – |
| Total impaired accrual loans | 4,014 | 4,021 |
| Total impaired loans | $ 19,639 | $ 20,956 |

The following tables present additional information concerning impaired loans and related allowance by loan type at period end.

| | June 30, 2012 | | | Quarter Ended June 30, 2012 | | Six Months Ended June 30, 2012 | |
|---|---|---|---|---|---|---|---|
| | Recorded Investment | Unpaid Principal Balance | Related Allowance | Average Impaired Loans | Interest Income Recognized on Impaired Loans | Average Impaired Loans | Interest Income Recognized on Impaired Loans |
| **Impaired loans with a related allowance for credit losses:** | | | | | | | |
| Real estate mortgage | $ 3,076 | $ 3,031 | $ 605 | $ 3,218 | $ 14 | $ 3,248 | $ 14 |
| Production and intermediate-term | 2,825 | 8,522 | 253 | 2,955 | 12 | 2,982 | 13 |
| Agribusiness | | | | | | | |
| Processing and marketing | – | – | – | – | – | – | – |
| Rural residential real estate | 260 | 281 | 41 | 272 | 1 | 275 | 1 |
| Total | $ 6,161 | $ 11,834 | $ 899 | $ 6,445 | $ 27 | $ 6,505 | $ 28 |
| **Impaired loans with no related allowance for credit losses:** | | | | | | | |
| Real estate mortgage | $ 11,275 | $ 13,466 | $ – | $ 11,793 | $ 48 | $ 11,903 | $ 50 |
| Production and intermediate-term | 1,766 | 1,904 | – | 1,847 | 8 | 1,864 | 8 |
| Agribusiness | | | | | | | |
| Processing and marketing | – | – | – | – | – | – | – |
| Rural residential real estate | 437 | 497 | – | 457 | 2 | 461 | 2 |
| Total | $ 13,478 | $ 15,867 | $ – | $ 14,097 | $ 58 | $ 14,228 | $ 60 |
| **Total impaired loans:** | | | | | | | |
| Real estate mortgage | $ 14,351 | $ 16,497 | $ 605 | $ 15,011 | $ 62 | $ 15,151 | $ 64 |
| Production and intermediate-term | 4,591 | 10,426 | 253 | 4,802 | 20 | 4,846 | 21 |
| Agribusiness | | | | | | | |
| Processing and marketing | – | – | – | – | – | – | – |
| Rural residential real estate | 697 | 778 | 41 | 729 | 3 | 736 | 3 |
| Total | $ 19,639 | $ 27,701 | $ 899 | $ 20,542 | $ 85 | $ 20,733 | $ 88 |

| | December 31, 2011 | | | Year Ended December 31, 2011 | |
|---|---|---|---|---|---|
| | Recorded Investment | Unpaid Principal Balance | Related Allowance | Average Impaired Loans | Interest Income Recognized on Impaired Loans |
| **Impaired loans with a related allowance for credit losses:** | | | | | |
| Real estate mortgage | $ 2,851 | $ 2,913 | $ 677 | $ 2,138 | $ 42 |
| Production and intermediate-term | 3,748 | 9,525 | 461 | 2,811 | 56 |
| Agribusiness | | | | | |
| Processing and marketing | – | – | – | – | – |
| Rural residential real estate | 277 | 284 | 56 | 208 | 4 |
| Total | $ 6,876 | $ 12,722 | $ 1,194 | $ 5,157 | $ 102 |
| **Impaired loans with no related allowance for credit losses:** | | | | | |
| Real estate mortgage | $ 12,409 | $ 14,882 | $ – | $ 9,305 | $ 185 |
| Production and intermediate-term | 1,216 | 1,324 | – | 912 | 18 |
| Agribusiness | | | | | |
| Processing and marketing | (2) | 655 | – | (1) | – |
| Rural residential real estate | 457 | 509 | – | 342 | 7 |
| Total | $ 14,080 | $ 17,370 | $ – | $ 10,558 | $ 210 |
| **Total impaired loans:** | | | | | |
| Real estate mortgage | $ 15,260 | $ 17,795 | $ 677 | $ 11,443 | $ 227 |
| Production and intermediate-term | 4,964 | 10,849 | 461 | 3,723 | 74 |
| Agribusiness | | | | | |
| Processing and marketing | (2) | 655 | – | (1) | – |
| Rural residential real estate | 734 | 793 | 56 | 550 | 11 |
| Total | $ 20,956 | $ 30,092 | $ 1,194 | $ 15,715 | $ 312 |

Unpaid principal balance represents the contractual principal balance of the loan.

There were no material commitments to lend additional funds to debtors whose loans were classified as impaired at June 30, 2012.

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

| | Real Estate Mortgage | Production and Intermediate-term | Agribusiness | Communication | Energy and Water/Waste Disposal | Rural Residential Real Estate | Total |
|---|---|---|---|---|---|---|---|
| **Allowance for credit losses:** | | | | | | | |
| Balance at March 31, 2012 | $ 1,740 | $ 789 | $ 719 | $ 8 | $ 3 | $ 187 | $ 3,446 |
| Charge-offs | (8) | (46) | – | – | – | – | (54) |
| Recoveries | 151 | – | – | – | – | – | 151 |
| Provision for loan losses | (174) | (128) | (49) | 2 | 9 | (13) | (353) |
| Balance at June 30, 2012 | $ 1,709 | $ 615 | $ 670 | $ 10 | $ 12 | $ 174 | $ 3,190 |
| | | | | | | | |
| Balance at December 31, 2011 | $ 1,359 | $ 657 | $ 1,273 | $ 7 | $ 2 | $ 184 | $ 3,482 |
| Charge-offs | (47) | (46) | – | – | – | – | (93) |
| Recoveries | 153 | – | – | – | – | – | 153 |
| Provision for loan losses | 244 | 4 | (603) | 3 | 10 | (10) | (352) |
| Balance at June 30, 2012 | $ 1,709 | $ 615 | $ 670 | $ 10 | $ 12 | $ 174 | $ 3,190 |
| | | | | | | | |
| Balance at March 31, 2011 | $ 1,165 | $ 109 | $ 2,562 | $ 12 | $ 6 | $ 130 | $ 3,984 |
| Charge-offs | (4) | (7) | (1,645) | – | – | – | (1,656) |
| Recoveries | 1 | – | – | – | – | – | 1 |
| Provision for loan losses | 17 | 729 | (71) | (4) | – | – | 671 |
| Balance at June 30, 2011 | $ 1,179 | $ 831 | $ 846 | $ 8 | $ 6 | $ 130 | $ 3,000 |
| | | | | | | | |
| Balance at December 31, 2010 | $ 1,107 | $ 153 | $ 2,580 | $ 17 | $ 6 | $ 140 | $ 4,003 |
| Charge-offs | (23) | (7) | (1,645) | – | – | – | (1,675) |
| Recoveries | 1 | – | – | – | – | – | 1 |
| Provision for loan losses | 94 | 685 | (89) | (9) | – | (10) | 671 |
| Balance at June 30, 2011 | $ 1,179 | $ 831 | $ 846 | $ 8 | $ 6 | $ 130 | $ 3,000 |
| | | | | | | | |
| Loans individually evaluated for impairment | $ 605 | $ 253 | $ – | $ – | $ – | $ 41 | $ 899 |
| Loans collectively evaluated for impairment | 1,104 | 362 | 670 | 10 | 12 | 133 | 2,291 |
| Balance at June 30, 2012 | $ 1,709 | $ 615 | $ 670 | $ 10 | $ 12 | $ 174 | $ 3,190 |
| | | | | | | | |
| Loans individually evaluated for impairment | $ 677 | $ 461 | $ – | $ – | $ – | $ 56 | $ 1,194 |
| Loans collectively evaluated for impairment | 682 | 196 | 1,273 | 7 | 2 | 128 | 2,288 |
| Balance at December 31, 2011 | $ 1,359 | $ 657 | $ 1,273 | $ 7 | $ 2 | $ 184 | $ 3,482 |
| | | | | | | | |
| **Recorded investment in loans outstanding:** | | | | | | | |
| Loans individually evaluated for impairment | $ 9,999 | $ 4,617 | $ – | $ – | $ – | $ 261 | $ 14,877 |
| Loans collectively evaluated for impairment | 97,764 | 30,684 | 4,761 | – | 2,021 | 17,414 | 152,644 |
| Ending balance at June 30, 2012 | $ 107,763 | $ 35,301 | $ 4,761 | $ – | $ 2,021 | $ 17,675 | $ 167,521 |
| | | | | | | | |
| Loans individually evaluated for impairment | $ 10,464 | $ 4,991 | $ – | $ – | $ – | $ 277 | $ 15,732 |
| Loans collectively evaluated for impairment | 103,097 | 27,719 | 7,328 | 1,261 | 2,481 | 18,257 | 160,143 |
| Ending balance at December 31, 2011 | $ 113,561 | $ 32,710 | $ 7,328 | $ 1,261 | $ 2,481 | $ 18,534 | $ 175,875 |

A restructuring of a debt constitutes a troubled debt restructuring (TDR) if the creditor for economic or legal reasons related to the debtor's financial difficulties grants a concession to the debtor that it would not otherwise consider. The following tables present additional information about activity that occurred during the period presented, related to TDRs. The tables do not include purchased credit impaired loans.

| | Three months ended June 30, 2012 | | | |
|---|---|---|---|---|
| | Pre-modification Outstanding Recorded Investment | | | |
| | Interest Concessions | Principal Concessions | Other Concessions | Total |
| **Troubled debt restructurings:** | | | | |
| Real estate mortgage | $ – | $ – | $ – | $ – |
| Total | $ – | $ – | $ – | $ – |

| | Three months ended June 30, 2012 | | | | | |
|---|---|---|---|---|---|---|
| | Post-modification Outstanding Recorded Investment | | | | Effects of Modification | |
| | Interest Concessions | Principal Concessions | Other Concessions | Total | Provisions | Charge-offs |
| **Troubled debt restructurings:** | | | | | | |
| Real estate mortgage | $ – | $ – | $ – | $ – | $ – | $ – |
| Total | $ – | $ – | $ – | $ – | $ – | $ – |

| | Six months ended June 30, 2012 | | | |
|---|---|---|---|---|
| | Pre-modification Outstanding Recorded Investment | | | |
| | Interest Concessions | Principal Concessions | Other Concessions | Total |
| **Troubled debt restructurings:** | | | | |
| Real estate mortgage | $ – | $ – | $ 34 | $ 34 |
| Total | $ – | $ – | $ 34 | $ 34 |

| | Six months ended June 30, 2012 | | | | | |
|---|---|---|---|---|---|---|
| | Post-modification Outstanding Recorded Investment | | | | Effects of Modification | |
| | Interest Concessions | Principal Concessions | Other Concessions | Total | Provisions | Charge-offs |
| **Troubled debt restructurings:** | | | | | | |
| Real estate mortgage | $ – | $ – | $ 19 | $ 19 | $ (12) | $ – |
| Total | $ – | $ – | $ 19 | $ 19 | $ (12) | $ – |

| | Three months ended June 30, 2011 | | | |
|---|---|---|---|---|
| | Pre-modification Outstanding Recorded Investment | | | |
| | Interest Concessions | Principal Concessions | Other Concessions | Total |
| **Troubled debt restructurings:** | | | | |
| Real estate mortgage | $ – | $ 2,188 | $ – | $ 2,188 |
| Production and intermediate-term | – | 2,589 | – | 2,589 |
| Total | $ – | $ 4,777 | $ – | $ 4,777 |

| | Three months ended June 30, 2011 | | | | | |
|---|---|---|---|---|---|---|
| | Post-modification Outstanding Recorded Investment | | | | Effects of Modification | |
| | Interest Concessions | Principal Concessions | Other Concessions | Total | Provisions | Charge-offs |
| **Troubled debt restructurings:** | | | | | | |
| Real estate mortgage | $ – | $ 2,156 | $ – | $ 2,156 | $ 214 | $ (196) |
| Production and intermediate-term | – | 2,589 | – | 2,589 | 546 | (499) |
| Total | $ – | $ 4,745 | $ – | $ 4,745 | $ 760 | $ (695) |

| | Six months ended June 30, 2011 | | | |
|---|---|---|---|---|
| | Pre-modification Outstanding Recorded Investment | | | |
| | Interest Concessions | Principal Concessions | Other Concessions | Total |
| **Troubled debt restructurings:** | | | | |
| Real estate mortgage | $ – | $ 2,188 | $ – | $ 2,188 |
| Production and intermediate-term | – | 2,589 | – | 2,589 |
| Total | $ – | $ 4,777 | $ – | $ 4,777 |

| | Six months ended June 30, 2011 | | | | | |
|---|---|---|---|---|---|---|
| | Post-modification Outstanding Recorded Investment | | | | Effects of Modification | |
| | Interest Concessions | Principal Concessions | Other Concessions | Total | Provisions | Charge-offs |
| **Troubled debt restructurings:** | | | | | | |
| Real estate mortgage | $ – | $ 2,156 | $ – | $ 2,156 | $ 214 | $ (196) |
| Production and intermediate-term | – | 2,589 | – | 2,589 | 546 | (499) |
| Total | $ – | $ 4,745 | $ – | $ 4,745 | $ 760 | $ (695) |

Interest concessions include interest forgiveness and interest deferment. Principal concessions include principal forgiveness, principal deferment, and maturity extension.

Other concessions include additional compensation received which might be in the form of cash or other assets.

There were no TDRs that occurred during the previous twelve months and for which there was a subsequent payment default during 2012. Payment default is defined as a payment that was thirty days or more past due.

TDRs outstanding at period end totaled $12,209, of which $8,195 were in nonaccrual status.

## NOTE 3 – COMMITMENTS AND CONTINGENT LIABILITIES

Actions are pending against the Association in which money damages are sought. However, on the basis of information now at hand, management and legal counsel are of the opinion that the ultimate liability, if any, resulting therefrom, would not be material in relation to the overall financial position of the Association.

## NOTE 4 – EMPLOYEE BENEFIT PLANS

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

| | For the six months ended June 30, | |
|---|---|---|
| | 2012 | 2011 |
| Pension | $ 525 | $ 586 |
| 401(k)/1165(e) | 26 | 28 |
| Other postretirement benefits | 91 | 118 |
| Total | $ 642 | $ 732 |

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

| | Actual YTD Through 6/30/12 | Projected Contributions For Remainder of 2012 | Projected Total Contributions 2012 |
|---|---|---|---|
| Pension | $ – | $ 815 | $ 815 |
| Other postretirement benefits | 61 | 47 | 108 |
| Total | $ 61 | $ 862 | $ 923 |

Contributions in the above table include an allocated estimate of funding for the multi-employer pension plan in which the Association participates. The projected amount may change when a total funding amount and allocation is determined by the pension Plan's Sponsor Committee. Also, market conditions could impact discount rates and return on plan assets which could change the contribution necessary before the next plan measurement date of December 31, 2012.

Further details regarding employee benefit plans are contained in the 2011 Annual Report to Shareholders.

## NOTE 5 – NOTES RECEIVABLE FROM OTHER FARM CREDT INSTITUTIONS

In September 2008, the Association used capital reserves to purchase $10,000 total of fixed rate unsecured subordinated notes issued by two other associations in the District, both notes due in 2018. The notes receivable are subordinate to all other categories of creditors of the issuing associations, including any claims of the Bank and general creditors, but are senior to all classes of shareholders of the issuing associations. The notes receivable are not considered System debt, and thus are not guaranteed by the System and not insured by the Insurance Corporation. Since the notes receivable are only guaranteed by the issuing associations, repayment could be negatively impacted by funding, credit, and/or counterparty risks encountered by the two issuing associations in their business operations. As of July 1, 2012, one of the two associations carrying higher risk in its credit portfolio, merged with another association within the district, improving its risk profile to acceptable. This investment is no longer considered to carry higher risk than when it was purchased. The second association's loan portfolio maintains an acceptable credit risk profile as of the end of March 2012. Management does not consider that it carries higher risk than average. Management still expects to collect all interest and principal as contracted from both associations. It will also continue to inform the Board of Directors on the financial performance of the Associations on a quarterly basis.

The notes receivable bear interest at an annual fixed rate of 9.00 percent, payable on the fifteenth day of each month, beginning on October 15, 2008. Interest will be deferred if, as of the fifth business day prior to an interest payment date, any applicable minimum regulatory capital ratios are not satisfied by the issuing association(s). A deferral period may not last for more than five consecutive years or beyond the maturity date of the note(s). During such a period, the issuing association(s) may not declare or pay any dividends or patronage refunds, among other certain restrictions, until interest payments are resumed and all deferred interest has been paid. The note(s) may be redeemed, at the issuing Association's option, on October 15, 2013, or upon the occurrence of certain defined regulatory events, at a redemption price of 100 percent of the principal amount, plus any accrued but unpaid interest to the date of redemption, provided the issuing association(s) have made payment in full of all amounts then due in respect of their senior indebtedness.

## NOTE 6 – NOTES PAYABLE TO AGFIRST FARM CREDIT BANK

The Association's indebtedness to the Bank represents borrowings by the Association primarily to fund its loan portfolio. This indebtedness is collateralized by a pledge of substantially all of the Association's assets and the terms of the revolving line of credit are governed by the General Financing Agreement (GFA). The GFA defines Association performance criteria for borrowing from the Bank, which

includes borrowing base margin, earnings and capital covenants. The Association failed to meet its earnings covenant under the GFA at December 31, 2011. The default allows the Bank, in conjunction with the FCA, to accelerate repayment of all indebtedness. The Bank approved a waiver of the default and has allowed the Association to continue to operate under a special credit agreement (SCA). At June 30, 2012, the Association was in compliance with the earnings covenant under the SCA, which expires December 31, 2012.

## NOTE 7 – FAIR VALUE MEASUREMENT

FASB guidance defines fair value, establishes a framework for measuring fair value and requires fair value disclosures for certain assets and liabilities measured at fair value on a recurring and nonrecurring basis. These assets and liabilities consist primarily of assets held in trust funds, 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.

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 0.79 percent of the issued stock of the Bank as of June 30, 2012 net of any reciprocal investment. As of that date, the Bank's assets totaled $28.9 billion and shareholders' equity totaled $2.3 billion. The Bank's earnings were $253 million for the first six months of 2012. In addition, the Association has no investment related to other Farm Credit institutions. Management determines the Association's valuation policies and procedures. The Bank performs the majority of the Association's valuations, and its valuation processes are calibrated annually by an independent consultant. The fair value measurements are analyzed on a quarterly basis. For other valuations, documentation is obtained for third party information, such as pricing, and periodically evaluated alongside internal information and pricing that is available.

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 had no Level 1 assets or liabilities at June 30, 2012. For cash, the carrying value is primarily utilized as a reasonable estimate of fair value.

### 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 had no Level 2 assets or liabilities measured at fair value on a recurring basis at June 30, 2012.

The carrying value of accrued interest approximates its fair value.

### 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, 2012 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. .

Because no active market exists for the Association's accruing loans, fair value is estimated by discounting the expected future cash flows using the Association's current interest rates at which similar loans currently would be made to borrowers with similar credit risk. 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 values of loans in a nonaccrual status are estimated to be the carrying amount of the loan less specific reserves (see Level 3 below).

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. This assumption implies that earnings on the Association's interest margin are used to fund operating expenses and capital expenditures.

Other property owned is classified as a level 3 asset at June 30, 2012. The fair value 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. Other property owned consists of real and personal property acquired through foreclosure or deed in lieu of foreclosure and is carried as an asset held for sale, which is generally not its highest and best use. These properties are part of the Association's credit risk mitigation efforts, not its ongoing business. In addition, FCA regulations require that these types of property be disposed of within a reasonable period of time.

For 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; therefore, the related credit risk is not significant.

For notes receivable from other Farm Credit institutions, fair value is determined by discounting the expected future cash flows using appropriate interest rates for similar assets.

**Information about Sensitivity to Changes in Significant Unobservable Inputs**

For certain recurring fair value measurements categorized within Level 3 of the fair value hierarchy, the significant unobservable inputs used in the fair value measurement are prepayment rates, probability of default, and loss severity in the event of default. Significant increases (decreases) in any of those inputs in isolation would result in a significantly lower (higher) fair value measurement. Generally, a change in the assumption used for the probability of default is accompanied by a directionally similar change in the assumption used for the loss severity and a directionally opposite change in the assumption used for prepayment rates.

Other fair value measurements may use contractual payments and a risk adjusted discount rate, which is generated using the Association's 14-point risk rating scale. An increase in risk rating will generally produce a lower fair value measurement.

The following tables present the changes in Level 3 assets and liabilities measured at fair value on a recurring basis for the six months ended June 30, 2012 and 2011. The Association had no transfers of assets or liabilities into or out of Level 1 or Level 2 during the first six months of 2012 and 2011.

| | Standby Letters Of Credit |
|---|---|
| Balance at January 1, 2012 | $ 22 |
| **Total gains or (losses) realized/unrealized:** | |
| Included in earnings | – |
| Included in other comprehensive income (loss) | – |
| Purchases | – |
| Sales | – |
| Issuances | – |
| Settlements | (2) |
| Transfers in and/or out of level 3 | – |
| Balance at June 30, 2012 | $ 20 |

| | Standby Letters Of Credit |
|---|---|
| Balance at January 1, 2011 | $ 31 |
| **Total gains or (losses) realized/unrealized:** | |
| Included in earnings | – |
| Included in other comprehensive income (loss) | – |
| Purchases | – |
| Sales | – |
| Issuances | 5 |
| Settlements | – |
| Transfers in and/or out of level 3 | – |
| Balance at June 30, 2011 | $ 36 |

**Quantitative Information about Recurring and Nonrecurring Level 3 Fair Value Measurements**

| | Valuation Technique(s) | Unobservable Input | Range |
|---|---|---|---|
| Impaired loans and other property owned | Appraisal | Income and expense | * |
| | | Comparable sales | * |
| | | Replacement costs | * |
| | | Comparability adjustments | * |

** Ranges for this type of input are not useful because each collateral property is unique.*

**Information about Other Financial Instrument Fair Value Measurements**

| | Valuation Technique(s) | Input |
|---|---|---|
| Cash | Carrying Value | Par/Principal and appropriate interest yield |
| Loans | Discounted cash flow | Prepayment rates |
| | | Probability of default |
| | | Loss severity |
| | | Annualized volatility |
| Notes receivable from other Farm Credit institutions | Discounted cash flow | Probability of default |
| | | Risk adjusted discount rate |
| Accrued interest | Carrying value | Coupon interest rates |
| Notes payable to AgFirst Farm Credit Bank | Discounted cash flow | Prepayment rates |
| | | Probability of default |
| | | Loss severity |
| | | Annualized volatility |

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 following table presents the carrying amounts and fair values of assets and liabilities that are measured at fair value on a recurring and nonrecurring basis, as well as, those financial instruments not measured at fair value, for each of the hierarchy levels at the period ended:

| | June 30, 2012 | | | | | |
|---|---|---|---|---|---|---|
| | Total Carrying Amount | Level 1 | Level 2 | Level 3 | Total Fair Value | Fair Value Effects On Comprehensive Income |
| **Recurring Measurements** | | | | | | |
| **Assets:** | | | | | | |
| Recurring Assets | $ – | $ – | $ – | $ – | $ – | $ – |
| **Liabilities:** | | | | | | |
| Standby letters of credit | $ 20 | $ – | $ – | $ 20 | $ 20 | $ – |
| Recurring Liabilities | $ 20 | $ – | $ – | $ 20 | $ 20 | $ – |
| **Nonrecurring Measurements** | | | | | | |
| **Assets:** | | | | | | |
| Loans | $ 18,740 | $ – | $ – | $ 18,740 | $ 18,740 | $ 355 |
| Other property owned | 3,515 | – | – | 3,829 | 3,829 | 33 |
| Nonrecurring Assets | $ 22,255 | $ – | $ – | $ 22,569 | $ 22,569 | $ 388 |
| **Other Financial Instruments** | | | | | | |
| **Assets:** | | | | | | |
| Cash | $ 255 | $ 255 | $ – | $ – | $ 255 | |
| Loans | 144,990 | – | – | 144,654 | 144,654 | |
| Accrued interest receivable | 676 | – | 676 | – | 676 | |
| Notes receivable from other Farm Credit institutions | 10,000 | – | – | 10,560 | 10,560 | |
| Other Assets | $ 155,921 | $ 255 | $ 676 | $ 155,214 | $ 156,145 | |
| **Liabilities:** | | | | | | |
| Notes payable to AgFirst Farm Credit Bank | $ 133,189 | $ – | $ – | $ 133,734 | $ 133,734 | |
| Accrued interest payable | 247 | – | 247 | – | 247 | |
| Other Liabilities | $ 133,436 | $ – | $ 247 | $ 133,734 | $ 133,981 | |

The following tables present the assets and liabilities that are measured at fair value on a recurring basis at December 31, 2011 for each of the fair value hierarchy levels:

| | December 31, 2011 | | | |
|---|---|---|---|---|
| | Level 1 | Level 2 | Level 3 | Total Fair Value |
| **Liabilities:** | | | | |
| Standby letters of credit | $ – | $ – | $ 22 | $ 22 |
| Total Liabilities | $ – | $ – | $ 22 | $ 22 |

Assets and liabilities measured at fair value on a nonrecurring basis at December 31, 2011 for each of the fair value hierarchy values are summarized below.

| | December 31, 2011 | | | | |
|---|---|---|---|---|---|
| | Level 1 | Level 2 | Level 3 | Total Fair Value | YTD Total Gains (Losses) |
| **Assets:** | | | | | |
| Impaired loans | $ – | $ – | $ 4,779 | $ 4,779 | $ (2,732) |
| Other property owned | $ – | $ – | $ 1,376 | $ 1,376 | $ (205) |

The estimated fair values of the Association's financial instruments at December 31, 2011 are as follows:

| | December 31, 2011 | |
|---|---|---|
| | Carrying Amount | Estimated Fair Value |
| **Financial assets:** | | |
| Cash | $ 164 | $ 164 |
| Loans, net of allowance | $ 171,900 | $ 171,206 |
| Accrued interest receivable | $ 568 | $ 568 |
| Notes receivable from other Farm Credit Institutions | $ 10,000 | $ 10,735 |
| **Financial liabilities**: | | |
| Notes payable to AgFirst Farm Credit Bank | $ 143,638 | $ 144,810 |

## NOTE 8 – ACCUMULATED OTHER COMPREHENSIVE INCOME

Changes in components of Accumulated Other Comprehensive Income are as follows:

| | Employee Benefit Plans |
|---|---|
| Balance at December 31, 2011 | $ 279 |
| Other comprehensive income | 32 |
| Balance at June 30, 2012 | $ 311 |
| | |
| Balance at December 31, 2010 | $ (208) |
| Other comprehensive income | 42 |
| Balance at June 30, 2011 | $ (166) |

| | For the three months ended June 30, | | For the six months ended June 30, | |
|---|---|---|---|---|
| | 2012 | 2011 | 2012 | 2011 |
| **Other Comprehensive Income and Reclassification Amounts:** | | | | |
| Amounts reclassified to net periodic pension costs | $ 16 | $ 21 | $ 32 | $ 42 |
| Net gain (loss) during period | – | – | – | – |
| Defined benefit post retirement plans, net | $ 16 | $ 21 | $ 32 | $ 42 |

## NOTE 9 – REGULATORY ENFORCEMENT MATTERS

As previously disclosed, on March 17, 2011 the Farm Credit Administration (FCA) entered into a written Supervisory Agreement (SA) with the Board of Directors of the Association. This agreement supersedes FCA Supervisory Letters dated July 23, 2009, March 2, 2010, and December 10, 2010 and incorporates certain requirements from these letters. The Supervisory Agreement requires the Board of Directors to take certain corrective and precautionary measures with respect to some Association practices, including board governance and operation, director fiduciary duties, nominating committee procedures, board policies, board business planning, Association earnings and liquidity, senior management and human capital development, internal audit and review, asset quality, allowance for loan losses and collateral risk management, and capital markets and participation activities. In addition, the SA prohibits the Association from distributing patronage-sourced income without FCA consent.

Conditions and events that led to the need for this agreement include portfolio credit quality deterioration, high turnover in senior management, perceived weaknesses in board governance, and, reduced earnings and liquidity. The Board of Directors and the Association have worked during the year to reach several milestones. On October 4, 2011, FCA communicated in a letter to the board that efforts had led to an overall rating of “partial compliance” with the agreement and encouraged the board to continue working towards achieving full compliance with the agreement. On February 14, 2012, FCA again communicated in a letter to the Board that it had achieved incremental progress towards complying with the Agreement but that improved business results had not yet materialized. The FCA delivered an in person report of examination to the Board of Directors on June 13, 2012 with updated results. The Association had achieved full compliance in 4 out 17 items, substantial compliance in 8 out of 17 items and partial compliance in 5 out 17 items. Some of the results achieved in compliance with the agreement include the following:

- Hiring a board consultant and continued work with the consultant to assist the Board in fulfilling its fiduciary duties and improving board operations and governance.
- Updating its board committee charters, undergoing several training sessions and changing leadership to improve governance of the Association.
- Revising the director candidate nominating procedures to qualify new candidates, which led to stockholders electing two new directors to the Board.
- Hiring a new CEO beginning on February 1, 2011 to lead the Association after the retirement of the previous CEO on June 30, 2010.
- Overseeing the implementation of updated collateral risk management policies and procedures that are in line with best practices in the industry.
- Improving the methodology used to calculate the Allowance for Loan Losses of the Association.
- Hiring a specialized third party auditor that assessed the capital markets portfolio credit risk and helped, strengthened credit policies and procedures.
- Establishing a Compliance Committee to monitor management’s progress in implementing the corrective actions of items identified in the SA.
- Ensuring that FCA’s recommendations are incorporated in the various action plans.
- Reviewing the Association’s internal audit plan to focus on areas where perceived weaknesses were identified.
- Establishing a risk assessment process to assess risks and controls in the ACA.
- Establishing an asset quality improvement plan to monitor management efforts in managing high risk loans.
- Revising the 2011 business plan to establish strategic priorities and to comply with FCA regulations governing business planning.
- Establishing a human capital plan and succession plan to assist in the long-term success of the Association.
- Revising board policies on a quarterly basis to guide management in conducting day to day operations.
- Enhancing the participation’s portfolio credit underwriting and administration controls.

All required measures have not been achieved or completed as of the date of this report and the Board of Directors continues to work with the management team in improving the areas identified in the Supervisory Agreement. Besides the ongoing corrective actions already mentioned, other actions to be taken target the following areas.

- Improving board efficacy in overseeing the Association’s business practices by updating board policies. This review of board policies was completed subsequent to the end of the quarter.
- Improving risk management work in the area of stress-testing.
- Building a cohesive senior management team.
- Developing strategies for growing the Association’s loan portfolio with high quality loans to improve asset quality and, enhance earnings and liquidity.

The Board of Directors will continue engaging a board consultant to provide advice in understanding and fulfilling its fiduciary responsibilities and to perform other advisory functions as specified in the agreement. Both the Board of Directors and Senior Management are committed to continuing the administration of the Association in a sound manner, compliant with all FCA Regulations.

The Association remained under written supervisory agreement as of the date of this report.

## NOTE 10 – SUBSEQUENT EVENTS

The Association has evaluated subsequent events and has determined there are none requiring disclosure through August 8, 2012, which is the date the financial statements were issued.