
ArborOne, ACA

SECOND QUARTER 2009

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CERTIFICATION

The undersigned certify that we have reviewed the June 30, 2009 quarterly report of **ArborOne, 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.



Jasper W. Shuler
Chief Executive Officer



Tammy G. Smith
Chief Financial Officer



James M. Ward
Chairman of the Board

July 27, 2009

ArborOne, ACA

Report on Internal Control Over Financial Reporting

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

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

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

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



Jasper W. Shuler
Chief Executive Officer



Tammy G. Smith
Chief Financial Officer

July 27, 2009

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

(dollars in thousands)

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

LOAN PORTFOLIO

The Association provides funds to farmers, rural homeowners and farm-related businesses for financing of short and intermediate-term loans and long-term real estate mortgage loans. The Association's loan portfolio is diversified over a range of agricultural commodities in our region, including tobacco, poultry, swine and forestry. Farm size varies and many of the borrowers in the region have diversified farming operations. These factors, along with the numerous opportunities for non-farm income in the area, somewhat impact the level of dependency on a given commodity. Approximately twenty-seven percent of the portfolio has significant outside income to diversify dependence on agriculture, consisting of lifestyle loans and loans to less than full-time farmers with retirement income, salaried income and non-agricultural business income. Further, approximately sixteen percent of the assets carry federal guarantees as a risk management tool.

The gross loan volume of the Association as of June 30, 2009, was \$300,424, a decrease of \$569 as compared to \$300,993 at December 31, 2008. Net loans outstanding at June 30, 2009, were \$299,158 as compared to \$299,082 at December 31, 2008. During the six months ended June 30, 2009, the Association's sold participations to *AgFirst Farm Credit Bank* (the Bank) decreased by \$4,615. As of June 30, 2009, the Association had \$110,259 of such participations outstanding. The Association has investment securities that are classified as available for sale in the amount of \$24,175 at June 30, 2009 compared to \$27,770 at December 31, 2008. The Association entered into commitments to acquire Successor-in-Interest Contracts (SIIC), beginning in the fourth quarter of 2005. As of June 30, 2009, the Association had \$95,637 in other investments for SIIC, compared to \$111,934 at December 31, 2008. Net loans and investments accounted for 93.59 percent of total assets at June 30, 2009, as compared to 93.10 percent of total assets at December 31, 2008.

Net loans and investments decreased by \$19,824 during the reporting period. The decrease in loan volume is primarily due to a decrease in gross loan volume, and partially offset by a decrease in participations sold loan volume. The Association has tightened lending policies as well as strengthened its capital position.

Investment securities available for sale decreased by \$3,595 and investments held to maturity decreased by \$8 due to normal payments. The decrease in investment securities available for sale was due to pay downs of \$4,206 and partially offset by an improvement in fair values of \$611. The other investments for SIIC decreased by \$16,297, which was due to the annual payments on the contracts and partially offset by purchasing additional contracts. The Association continues to review and engage in investment and participation opportunities, while serving customers within the territory.

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 increased from \$6,586 at December 31, 2008, to \$11,845 at June 30, 2009. This was due to four additional large participation loans that were moved to non-accrual plus several core agricultural loans.

Association management maintains an allowance for loan losses in an amount considered sufficient to absorb possible losses in the loan portfolio based on credit quality, current conditions, and expected future conditions. The allowance for loan losses at June 30, 2009, was \$1,266, compared to \$1,911 at December 31, 2008. This decrease was the result of recognizing charge offs of specific reserves on three large participation accounts in the amount of \$1,051. Additional charge offs to two participation accounts in the amount of \$537 and four core agricultural loans in the amount of \$751 were also processed. Additions were made to the allowance in the amount of \$1,654. There were net recoveries of \$39 for the six months ended June 30, 2009. The allowance for loan loss for the period ending June 30, 2009, is considered by management to be adequate to cover any future possible losses.

RESULTS OF OPERATIONS

For the three months ended June 30, 2009

Net income for the three months ended June 30, 2009, totaled \$384, as compared to \$959 for the same period in 2008. Net interest income decreased \$208, for the three months ended June 30, 2009, as compared to the same period in 2008 due to

decreased loan volume and lower interest rates. This decrease in net interest income is attributed mostly to a decrease of \$1,092 in interest income from loan volume, other investments (SIIC), and investment securities. Interest expense also decreased by \$884. The interest expense decrease was a result of decreased loan volume and lower interest rates which were partially offset by the interest expense for the subordinated debt of \$169.

At June 30, 2009, interest income on accruing loans decreased by \$837 compared to \$4,691 at June 30, 2008. Nonaccrual income was \$69 for the three months ended June 30, 2009, as compared to \$38 for the same period in 2008. Interest income on investment securities was \$157 compared to \$246 for the same period in 2008. Interest income on other investments (SIIC) was \$1,277 for the three months ended June 30, 2009, and \$1,473 for the same period in 2008. Interest expense decreased \$884 for the three months ended June 30, 2009, as compared to the comparable period of 2008. The interest expense decrease was a result of decreased loan volume and lower interest rates as well as a decrease in investment securities volume. This decrease was partially offset by the interest expense from the subordinated debt of \$169. The Association recorded a net provision for loan loss of \$987 for the quarter compared to \$636 for the comparable period of 2008.

Noninterest income for the three months ended June 30, 2009, totaled \$1,899 as compared to \$2,081 for the same period of 2008, a decrease of \$182. The decrease is primarily the result of lower patronage income for loans sold to the Bank, coupled with a decrease in loan fees. Noninterest expense for the three months ended June 30, 2009, decreased \$157 compared to the same period of 2008. Increases in salaries and employee benefits were primarily offset by occupancy and equipment and other operating expenses. The Association did not record a provision for income taxes for the three months ended March 31, 2009 compared to \$9 for the three months ended June 30, 2008.

For the six months ended June 30, 2009

Net income for the six months ended June 30, 2009, totaled \$1,182, as compared to \$3,026 for the same period in 2008. Net interest income decreased \$795 or 21.93 percent compared to June 30, 2008. Interest income on loans and other investments (SIIC) decreased by \$2,940 and investment securities decreased by \$391. Interest expense decreased by \$2,536 to the same period of 2008. This decrease was partially offset by the interest expense from the subordinated debt of \$338. This change in net interest income is the result of both decreased loan volume and lower interest rates.

Nonaccrual income was \$73 for the six months ended June 30, 2009, as compared to \$65 for the same period in 2008. The Association recorded a provision for loan loss of \$1,654 for the six months ended June 30, 2009, as compared to a provision for loan loss of \$636 for the same period in 2008.

Noninterest income for the six months ended June 30, 2009, totaled \$4,008 as compared to \$4,090 for the same period of 2008, a decrease of \$82. The decrease is primarily due to a decrease in patronage income of \$131 and loan fees of \$27. The decrease was partially offset by an increase in fees for financially related services of \$70. Noninterest expense for the six months ended June 30, 2009, decreased \$38 compared to the same period of 2008. This decrease is attributable to a decrease in other operating expenses of \$494 offset by a rise in salaries and employee benefits of \$361, occupancy and equipment expenses of \$66, and Insurance fund premium of \$29. The Association recorded a provision for income taxes of \$6 for the six months ended June 30, 2009, a decrease of \$13 as compared to the same period in 2008.

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, 2009, was \$385,738 as compared to \$406,997 at December 31, 2008. The decrease during the period is primarily attributable to decreased loan volume and lower interest rates.

In September 2008, the Association issued \$7,500 of fixed rate unsecured subordinated debt due in 2018, generating proceeds that were primarily used to increase the permanent capital of the Association pursuant to the Farm Credit Administration regulations, and for general corporate purposes. The debt is payable to another association in the Farm Credit System (System). It is subordinate to all other categories of creditors, including any claims of the Bank and general creditors, and is senior to all classes of shareholders. The subordinated debt is not considered System debt, and thus is not guaranteed by the System and not insured by the Farm Credit System Insurance Corporation.

CAPITAL RESOURCES

Total members' equity at June 30, 2009, increased to \$52,572 from the December 31, 2008, total of \$51,089. The increase is primarily attributable to the increase in retained earnings in excess of the reduction of protected stock and revolved equities, along with a decrease in other comprehensive losses.

Total capital stock and participation certificates were \$1,496 on June 30, 2009, compared to \$1,576 on December 31, 2008. This decrease is attributed to the retirement of protected stock

and participation certificates on loans liquidated in the normal course of business and the annual retirement of B stock.

The Association reports other comprehensive income (loss) (OCI) in its Consolidated Statements of Changes in Members' Equity. The Association recognized OCI loss of \$(176) as of June 30, 2009, as compared to \$(225) in 2008 for FAS 158, *"Employers' Accounting for Defined Benefit Pension and Other Postretirement Plans."* The Association also recognized OCI loss of \$(1,140) as of June 30, 2009, as compared to \$(1,751) in 2008 for unrealized gains (losses) on investments available for sale.

Farm Credit Administration (FCA) regulations require all Farm Credit institutions to maintain minimum permanent capital, total surplus and core surplus ratios. These ratios are calculated by dividing the Association's permanent capital, total surplus and core surplus as defined in FCA regulations, by a risk-adjusted asset base. As of June 30, 2009, the Association's total surplus ratio and core surplus ratio were 15.77 percent and 12.58 percent, respectively, and the permanent capital ratio was 16.22 percent. All three ratios were well above the minimum regulatory ratios of 7.00 percent for permanent capital and total surplus ratios and 3.50 percent for the core surplus ratio.

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 2008 Annual Report to Shareholders for recently issued accounting pronouncements.

NOTE: Shareholder investment in the Association could be affected by the financial condition and results of operations of AgFirst Farm Credit Bank. Copies of AgFirst's Annual and Quarterly reports are available upon request free of charge by calling 1-800-845-1745, ext. 378, or writing Stephen Gilbert, AgFirst Farm Credit Bank, P.O. Box 1499, Columbia, SC 29202. Information concerning AgFirst Farm Credit Bank can also be obtained at their website, www.agfirst.com. Copies of the Association's Annual and Quarterly reports are also available upon request free of charge by calling 1-800-741-7332, writing Casey Sherman, Corporate Secretary, ArborOne, ACA, P.O. Box 3699, Florence, SC 29502, or accessing the website, www.arborone.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.

ArborOne, ACA

Consolidated Balance Sheets

<i>(dollars in thousands)</i>	June 30, 2009 <i>(unaudited)</i>	December 31, 2008 <i>(audited)</i>
Assets		
Cash	\$ 16	\$ 1
Investment securities:		
Available for sale (amortized cost of \$25,315 and \$29,521 respectively)	24,175	27,770
Held to maturity (fair value of \$3,561 and \$3,975 respectively)	4,382	4,390
Total investment securities	28,557	32,160
Loans	300,424	300,993
Less: allowance for loan losses	1,266	1,911
Net loans	299,158	299,082
Other investments	95,637	111,934
Accrued interest receivable	3,378	4,463
Investment in other Farm Credit institutions	17,248	17,679
Premises and equipment, net	744	848
Other property owned, net	1,690	—
Due from AgFirst Farm Credit Bank	3,014	6,397
Other assets	2,909	3,463
Total assets	\$ 452,351	\$ 476,027
Liabilities		
Notes payable to AgFirst Farm Credit Bank	\$ 385,738	\$ 406,997
Subordinated debt payable to other Farm Credit institutions (Note 5)	7,500	7,500
Accrued interest payable	1,271	1,549
Patronage refund payable	404	2,063
Other liabilities	4,866	6,829
Total liabilities	399,779	424,938
Commitments and contingencies		
Members' Equity		
Protected borrower equity	327	371
Capital stock and participation certificates	1,169	1,205
Retained earnings		
Allocated	31,119	30,751
Unallocated	21,273	20,738
Accumulated other comprehensive income (loss)	(1,316)	(1,976)
Total members' equity	52,572	51,089
Total liabilities and members' equity	\$ 452,351	\$ 476,027

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

ArborOne, ACA

Consolidated Statements of Income

(unaudited)

<i>(dollars in thousands)</i>	For the three months ended June 30,		For the six months ended June 30,	
	2009	2008	2009	2008
Interest Income				
Investment securities	\$ 157	\$ 246	\$ 301	\$ 692
Loans	3,922	4,729	7,866	10,384
Other	1,277	1,473	2,535	2,957
Total interest income	5,356	6,448	10,702	14,033
Interest Expense				
Notes payable to AgFirst Farm Credit Bank	3,711	4,764	7,533	10,407
Subordinated debt payable to other Farm Credit institutions (Note 5)	169	—	338	—
Total interest expense	3,880	4,764	7,871	10,407
Net interest income	1,476	1,684	2,831	3,626
Provision for (reversal of allowance for) loan losses	987	636	1,654	636
Net interest income after provision for (reversal of allowance for) loan losses	489	1,048	1,177	2,990
Noninterest Income				
Loan fees	247	320	733	760
Fees for financially related services	41	9	97	27
Equity in earnings of other Farm Credit institutions	1,546	1,673	3,023	3,154
Gains (losses) on other property owned, net	—	7	—	(22)
Gains (losses) on sale of rural home loans, net	—	11	1	16
Gains (losses) on sales of premises and equipment, net	14	(1)	17	5
Other noninterest income	51	62	137	150
Total noninterest income	1,899	2,081	4,008	4,090
Noninterest Expense				
Salaries and employee benefits	1,296	1,132	2,557	2,196
Occupancy and equipment	250	326	503	437
Insurance Fund premium	115	96	214	185
Other operating expenses	343	607	723	1,217
Total noninterest expense	2,004	2,161	3,997	4,035
Income before income taxes	384	968	1,188	3,045
Provision (benefit) for income taxes	—	9	6	19
Net income	\$ 384	\$ 959	\$ 1,182	\$ 3,026

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

ArborOne, ACA

Consolidated Statements of Changes in Members' Equity

(unaudited)

(dollars in thousands)

	Protected Borrower Capital	Capital Stock and Participation Certificates	Retained Earnings		Accumulated Other Comprehensive Income	Total Members' Equity
			Allocated	Unallocated		
Balance at December 31, 2007	\$ 412	\$ 1,196	\$ 29,195	\$ 18,105	\$ (494)	\$ 48,414
Comprehensive income						
Net income				3,026		3,026
Unrealized gains (losses) on investments available for sale, net of reclassification adjustments					(648)	(648)
Employee benefit plans adjustments				(45)	67	22
Total comprehensive income						2,400
Protected borrower equity retired	(39)					(39)
Capital stock/participation certificates issued/(retired), net		7				7
Patronage distribution adjustment			(261)	166		(95)
Balance at June 30, 2008	\$ 373	\$ 1,203	\$ 28,934	\$ 21,252	\$ (1,075)	\$ 50,687
Balance at December 31, 2008	\$ 371	\$ 1,205	\$ 30,751	\$ 20,738	\$ (1,976)	\$ 51,089
Comprehensive income						
Net income				1,182		1,182
Unrealized gains (losses) on investments available for sale, net of reclassification adjustments					611	611
Employee benefit plans adjustments					49	49
Total comprehensive income						1,842
Protected borrower equity retired	(44)					(44)
Capital stock/participation certificates issued/(retired), net		(36)				(36)
Patronage distribution adjustment			368	(647)		(279)
Balance at June 30, 2009	\$ 327	\$ 1,169	\$ 31,119	\$ 21,273	\$ (1,316)	\$ 52,572

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

ArborOne, ACA

Notes to the Consolidated Financial Statements

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

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

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

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

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

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

In addition to the recently issued accounting pronouncements discussed in the 2008 Annual Report to Shareholders, effective January 1, 2009, the Association adopted Financial Accounting Standards Board (FASB) Statement of Position (FSP) No. 157-2, "Effective Date of FASB Statement No. 157." This FSP delayed the effective date of Statement No. 157 for nonfinancial assets and nonfinancial liabilities until fiscal years beginning after November 15, 2008. The impact of adoption requires additional fair value disclosures (see Note 6), primarily regarding other property owned, but does not have an impact on the Association's financial condition or results of operations.

In April 2009, the FASB issued FSP No. 157-4, "Determining Fair Value When the Volume and Level of Activity for the Asset or Liability Have Significantly Decreased and Identifying Transactions That Are Not Orderly" (FSP 157-4). FSP 157-4 emphasizes that even if there has been a significant decrease in the volume and level of activity for the asset or liability and regardless of the valuation technique and inputs used, the objective for the fair value measurement is unchanged from what it would be if markets were operating at normal activity levels or transactions were orderly; that is, to determine the current exit price. It sets forth additional factors that should be considered to determine whether there has been a significant decrease in volume and level of activity when compared with normal market activity. The reporting entity shall evaluate the significance and relevance of the factors to determine whether, based on the weight of evidence, there has been a significant decrease in activity and volume. FSP 157-4 indicates that if an entity determines that either the volume or level of activity for an asset or liability has significantly decreased (from normal conditions for that asset or liability) or price quotations or observable inputs are not associated with orderly transactions, increased analysis and management judgment will be required to estimate fair value. It is further noted that a fair value measurement should include a risk adjustment to reflect the amount market participants would demand because of the risk (uncertainty) in the cash flows.

FSP 157-4 also requires a reporting entity to make additional disclosures in interim and annual periods. It is effective for interim periods ending after June 15, 2009 (see Note 2 and Note 6). Revisions resulting from a change in valuation techniques or their application are accounted for as a change in accounting estimate.

In April 2009, the FASB issued FSP No. 115-2, "Recognition and Presentation of Other-Than-Temporary Impairments" (FSP 115-2), which amends the other-than-temporary impairment guidance for debt securities to make the guidance more operational and to improve the presentation and disclosure of other-than-temporary impairments on debt securities in the financial statements. It does not change existing recognition and measurement guidance related to other-than-temporary impairments of equity securities.

FSP 115-2 changes existing impairment guidance under FASB Statement No. 115, Accounting for Certain Investments in Debt and Equity Securities (FAS 115) by eliminating the "ability and intent to hold" provision. In

addition, impairment is now considered to be other than temporary if an entity 1) intends to sell the security, 2) more likely than not will be required to sell the security before recovering its cost, or 3) does not expect to recover the security's entire amortized cost basis (even if the entity does not intend to sell). The "probability" standard relating to the collectability of cash flows is also eliminated, and impairment is now considered to be other-than-temporary if the present value of cash flows expected to be collected from the debt security is less than the amortized cost basis of the security (any such shortfall is referred to in FSP 115-2 as a "credit loss"). If an entity intends to sell an impaired debt security or more likely than not will be required to sell the security before recovery of its amortized cost basis less any current-period credit loss, the impairment is other-than-temporary and should be recognized currently in earnings in an amount equal to the entire difference between fair value and amortized cost. If a credit loss exists, but an entity does not intend to sell the impaired debt security and is not more likely than not to be required to sell before recovery, the impairment is other-than-temporary and should be separated into 1) the estimated amount relating to credit loss, and 2) the amount relating to all other factors. Only the estimated credit loss amount is recognized currently in earnings, with the remainder of the loss amount recognized in other comprehensive income. For held-to-maturity securities, the portion of the other-than-temporary impairment not related to a credit loss will be recognized in a new category of other comprehensive income and amortized over the remaining life of the debt security as an increase in the security's carrying amount. Disclosure requirements for impaired debt and equity securities are expanded and will now be required quarterly (see Note 2), as well as annually.

This FSP is effective for interim and annual periods ending after June 15, 2009. For securities held at the beginning of the interim period of adoption for which an other-than-temporary impairment was previously recognized, if an entity does not intend to sell and it is not more likely than not that it will be required to sell before recovery of its amortized cost basis, the entity shall recognize the cumulative effect of initially applying this FSP adjustment to the opening balance of retained earnings with a corresponding adjustment to accumulated other comprehensive income. There was no initial adjustment to apply this FSP for the Association since no other-than-temporary impairment was previously recognized by the Association.

In April 2009, the FASB issued FSP No. 107-1 and Accounting Principles Board (APB) No. 28-1, "Interim Disclosures about Fair Value of Financial Instruments." This FSP requires disclosures about fair value of financial instruments for interim reporting periods of publicly traded companies as well as in annual financial statements. The FSP is effective for interim periods ending after June 15, 2009 (see Note 7).

In May 2009, the FASB issued SFAS No. 165, "Subsequent Events," which sets forth general standards of accounting for and disclosure of events that occur after the balance sheet date but before financial statements are issued or are available to be issued. Recognized subsequent events should be recognized in the financial statements since the conditions existed at the date of the balance sheet. Nonrecognized subsequent events are not recognized in the financial statements since the conditions arose after the balance sheet date but before the financial statements are issued or are available to be issued. This Standard, which includes a required disclosure of the date through which an entity has evaluated subsequent events, is effective for interim or annual periods ending after June 15, 2009 (see Note 8).

NOTE 2 – INVESTMENT SECURITIES

A summary of the amortized cost and fair value of investment securities held as available-for-sale at June 30, 2009 follows:

	June 30, 2009				
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value	Yield
Commercial MBS	\$11,819	\$ –	\$ (929)	\$10,890	1.56%
Asset-backed Securities	13,496	–	(211)	13,285	1.16
Total investment securities	\$25,315	\$ –	\$ (1,140)	\$24,175	2.72%

A summary of the amortized cost and fair value of investment securities held-to-maturity at June 30, 2009 follows:

	June 30, 2009				
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value	Yield
Other Investments	\$ 4,382	\$ –	\$ (821)	\$ 3,561	6.23%

The Association's investments consist primarily of mortgage-backed securities (MBSs) and asset backed securities (ABSs). MBSs are collateralized by U.S. government or U.S. agency guaranteed residential mortgages and all have a AAA credit rating. One MBS, however, is split rated AAA. ABSs are also all rated AAA due to the senior/subordinate structure and/or a credit wrap by a bond insurer. All unrealized losses referenced above are primarily due to reduced liquidity in the securities markets stemming from general adversity in the financial markets and are not credit related.

The following table shows the fair value and gross unrealized losses for investments in a loss position aggregated by investment category and the length of time the securities have been in a continuous unrealized loss position at June 30, 2009. The continuous loss position is based on the date the impairment occurred. The Association performs periodic credit reviews, including an other-than-temporary impairment analysis, on its investment securities portfolio. The objective is to quantify any future possible loss of principal or interest

due on each security identified for additional analysis. Based on the results of all analyses, the Association has not recognized any other-than-temporary impairment in connection with these investments. The unrealized losses on these investments resulted primarily from reduced liquidity in the securities markets stemming from general adversity in the financial markets and are not credit related. The Association has the ability and intent to hold these investments until a recovery of unrealized losses occurs, which may be at maturity, and at this time expects to collect the full principal amount and interest due on these securities, especially after considering credit enhancements. All securities continue to perform. Substantially all of these investments were in U. S. government securities and the Association expects that these securities would not be settled at a price less than their amortized cost.

	Less than 12 Months		Greater than 12 Months	
	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
Other investments	\$ 3,560	\$ (821)	\$ -	\$ -
Commercial MBS	-	-	10,890	(929)
Asset-backed securities	8,201	(126)	5,084	(85)
Total	\$ 11,761	\$ (947)	\$ 15,974	\$ (1,014)

A summary of the expected maturity, amortized cost and estimated fair value of investment securities at June 30, 2009 follows:

Available-for-Sale:

	June 30, 2009		
	Amortized Cost	Fair Value	Weighted Average Yield
In one year or less	\$ -	\$ -	-%
After one year through five years	1,060	1,046	1.22
After five years through ten years	12,436	12,239	1.16
After ten years	11,819	10,890	1.56
Total	\$ 25,315	\$ 24,175	1.35%

Held-to-Maturity:

	June 30, 2009		
	Amortized Cost	Fair Value	Weighted Average Yield
In one year or less	\$ -	\$ -	-%
After one year through five years	-	-	-
After five years through ten years	989	1,008	7.75
After ten years	3,393	2,553	5.78
Total	\$ 4,382	\$ 3,561	6.23%

Expected maturities for collateralized mortgage obligations will differ from contractual maturities because borrowers may have the right to call or prepay obligations with or without call or prepayment penalties.

NOTE 3 – ALLOWANCE FOR LOAN LOSSES AND IMPAIRED LOANS

An analysis of the allowance for loan losses follows:

	For the six months ended June 30,	
	2009	2008
Balance at beginning of period	\$ 1,911	\$ 53
Provision for (reversal of) loan losses	1,654	636
Charge-offs	(2,339)	(20)
Recoveries	40	15
Balance at end of period	\$ 1,266	\$ 684

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

	2009	2008
Impaired loans with related allowance	\$ -	\$ -
Impaired loans with no related allowance	12,319	5,910
Total impaired loans	\$ 12,319	\$ 5,910
Allowance on impaired loans	\$ -	\$ -

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

	2009	2008
Average impaired loans	\$ 9,286	\$ 2,749
Interest income recognized on impaired loans	78	71

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,	
	2009	2008
Pension	\$ 584	\$ 203
401(k)	57	56
Other postretirement benefits	119	114
Total	\$ 760	\$ 373

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

	Actual YTD Through 6/30/09	Projected Contributions For Remainder of 2009	Projected Total Contributions 2009
Pension	\$ -	\$ -	\$ -
Other postretirement benefits	92	130	222
Total	\$ 92	\$ 130	\$ 222

Actuarial calculations as of the last plan measurement date (December 31, 2008) projected no contributions to the pension plan for 2009. However, market conditions could impact discount rates and return on plan assets which could make additional contributions necessary before the next plan measurement date of December 31, 2009.

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

NOTE 5 – SUBORDINATED DEBT

In September 2008, the Association issued \$7,500 of fixed rate unsecured subordinated debt due in 2018, generating proceeds that were primarily used to increase the permanent capital of the Association pursuant to the Farm Credit Administration regulations, and for general corporate purposes. The debt is payable to another association in the District. It is subordinate to all other categories of creditors, including any claims of the Bank and general creditors, and is senior to all classes of shareholders. The subordinated debt is not considered Farm Credit System (System) debt, and thus is not guaranteed by the System and not insured by the Farm Credit System Insurance Corporation.

The subordinated debt bears interest at an annual fixed rate of 9 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 of the debt, any applicable minimum regulatory capital ratios are not satisfied. A deferral period may not last for more than five consecutive years or beyond the maturity date of the subordinated debt. During such a period, the Association 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 subordinated debt may be redeemed, at the 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 Association has made payment in full of all amounts then due in respect of its senior indebtedness.

NOTE 6 – FAIR VALUE MEASUREMENT

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

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

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

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

Level 1

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

Level 2

Level 2 inputs to the valuation methodology include quoted prices for similar assets and liabilities in active markets; quoted prices in markets that are not active; and inputs that are observable, or can be corroborated, for substantially the full term of the asset or liability. The Association has Level 2 assets and no Level 2 liabilities measured at fair value on a recurring basis. Level 2 assets include available-for-sale investment securities that are traded in active, non-exchange markets. These securities are U.S. government and agency mortgage-backed securities, non-agency mortgage-backed securities, and U.S. agency debt securities, all of which have unadjusted values from third-party or internal pricing models. The fair value of substantially all of the Association's available-for-sale investment securities is determined from third-party valuation services that estimate current market prices. Inputs and assumptions related to third-party market valuation services are typically observable in the marketplace. Such services incorporate prepayment assumptions and underlying mortgage- or asset-backed collateral information to generate cash flows that are discounted using appropriate benchmark interest rate curves and volatilities. Third-party valuations also incorporate information regarding broker/dealer quotes, available trade information, historical cash flows, credit ratings, and other market information. Such valuations represent an estimated exit price, or price to

