


SECOND QUARTER 2010

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CERTIFICATION

The undersigned certify that we have reviewed the June 30, 2010 quarterly report of MidAtlantic 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.


J. Robert Frazee
Chief Executive Officer


John E. Wheeler, Jr.
Chief Financial Officer


Gary L. Grossnickle
Chairman of the Board

August 6, 2010

MidAtlantic Farm Credit, 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, 2010. In making the assessment, management used the framework in *Internal Control — Integrated Framework*, promulgated by the Committee of Sponsoring Organizations of the Treadway Commission, commonly referred to as the "COSO" criteria.

Based on the assessment performed, the Association concluded that as of June 30, 2010, the internal control over financial reporting was effective based upon the COSO criteria. Additionally, based on this assessment, the Association determined that there were no material weaknesses in the internal control over financial reporting as of June 30, 2010.



J. Robert Frazee
Chief Executive Officer



John E. Wheeler, Jr.
Chief Financial Officer

August 6, 2010

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

(dollars in thousands)

The following commentary reviews the financial condition and results of operations of MidAtlantic Farm Credit, ACA (Association) for the period ended June 30, 2010. On November 25, 2008, the stockholders of Valley Farm Credit, ACA and MidAtlantic Farm Credit, ACA approved a merger (Merger) to merge Valley into MidAtlantic; the FCA granted its final approval of the Merger on December 31, 2008 and the Merger was effective on December 31, 2008. The comments contained in this report should be read in conjunction with the accompanying consolidated financial statements, notes to the consolidated financial statements and the 2009 Annual Report of the Association. The accompanying consolidated financial statements were prepared under the oversight of the Audit Committee of the Board of Directors.

LOAN PORTFOLIO

The Association provides funds to farmers, rural homeowners and farm-related businesses for the financing of short- and intermediate-term loans and long-term real estate mortgage loans. The Association's loan portfolio encompasses a well diversified range of agricultural commodities, with cash grains, poultry and dairy representing the largest segments. In addition, the Association provides a significant amount of loans to lessors of agricultural real estate. Farm size varies and many of the borrowers in the region have diversified farming operations. This factor, along with the opportunities for non-farm income, impacts the level of dependency on any particular commodity.

Gross loans at June 30, 2010 totaled \$2,236,334 compared to \$2,288,344 at December 31, 2009, decreasing \$52,010 (2.27 percent) during the first six months. The Association's allowance for loan losses of \$25,412 increased \$4,392 (20.89 percent) during the first six months of 2010 resulting in net loans (gross loans less allowance for loan losses) of \$2,210,922 and \$2,267,324 at June 30, 2010 and December 31, 2009, respectively. Nonaccrual loans increased \$28,641 (58.83 percent) from \$48,683 at December 31, 2009 to \$77,324 at June 30, 2010 resulting in an increase in the ratio of nonaccrual loans to total loans from 2.13 percent to 3.46 percent. The significant increase in nonaccrual loans is primarily related to an account in the timber industry.

There is an inherent risk in the extension of any type of credit and, accordingly, the Association maintains an allowance for loan losses consistent with the risk measured in the portfolio.

Credit administration remains satisfactory and the overall credit quality of the Association's loan portfolio has remained acceptable. A provision for loan losses of \$3,200 was recorded in the second quarter of 2010, that after giving effect to the net impact of charge-offs in excess of recoveries, increased the Association's allowance \$4,392 as of June 30, 2010. The allowance for loan losses represented 1.14 percent and 0.92 percent of total loans at June 30, 2010 and December 31, 2009, respectively. See also Note 2 of "Notes to the Consolidated Financial Statements".

RESULTS OF OPERATIONS

For the three months ended June 30, 2010

Net income for the three months ended June 30, 2010 totaled \$10,906, an increase of \$3,325 (43.86 percent) compared to the three months ended June 30, 2009. Major changes in the components of net income are identified as follows:

- Net interest income increased \$1,354 (9.67 percent) for the quarter ended June 30, 2010 compared to the same period in 2009. The increase in net interest income is primarily attributable to (a) an increased portfolio margin attributable to the decrease in interest rates which occurred over the past year, and (b) a \$124 increase attributable to the increase in interest income recognized from nonaccrual volume. This was partially offset by a \$20 million decrease in loan volume at June 30, 2010 as compared to June 30, 2009 and a \$34.7 million increase in nonaccruing loans from June 30, 2009.
- The risks identified in the Association's loan portfolio required a provision for loan losses of \$3,200 to be recorded in the second quarter of 2010 as compared to \$2,000 in the second quarter of 2009. The Association's delinquent loans increased from 0.92 percent at December 31, 2009 to 1.14 percent of the portfolio at June 30, 2010. See also Note 2 of "Notes to the Consolidated Financial Statements".

- At June 30, 2010 and 2009, the Association accrued an estimated patronage receipt (reported as "Equity in earnings of other Farm Credit institutions" on the Consolidated Statements of Income) of \$3,797 and \$3,810, respectively, which is based on second quarter operations only; management anticipates additional income for each successive quarter in 2010. Since this income from AgFirst Farm Credit Bank (the Bank) is reasonably estimable and because there is a history of these earnings, management is of the opinion that including this income in quarterly operations provides shareholders with a more accurate forecast of annualized net income. In addition, the Association received \$1,202 for a Special Patronage which was declared and paid by the Bank in June 2010.
- Noninterest income in the second quarter of 2010 included a net decrease in Other noninterest income and Net Gains (losses) on other property owned and sale of rural home loans aggregating \$191.
- Noninterest expense for the second quarter of 2010 was \$7,381 as compared to \$9,177 for the second quarter of 2009 or a decrease of \$1,786 (19.57 percent). The decrease of \$812 for Salaries and employee benefits is primarily the result of decreased staffing which occurred during 2009 with the successful merger with the former Valley Association. Pension expenses related to the defined benefit plan have also declined for 2010 as compared to 2009. See also Note 3 of "Notes to the Consolidated Financial Statements".

Insurance fund premium expense decreased \$923 (97.98 percent) resulting from a .9 percent increase in the average daily balance loan portfolio which was offset by the Farm Credit System Insurance Corporation (FCSIC) announcement in June 2010 to decrease the insurance premium for 2010 effective January 1, 2010. The effect of this announcement also decreased the insurance premium previously recorded in the first quarter results. The lower rate is anticipated to prevail for the remainder of 2010.

Occupancy and equipment and Other operating expenses decreased \$61 from \$2,056 to \$1,995 primarily due to a decrease in Director expenses.

For the six months ended June 30, 2010

Net income for the six months ended June 30, 2010 totaled \$24,663 or \$10,429 (73.27 percent) greater than the six months ended June 30, 2009. Major changes in the components of net income are identified as follows:

- The increase in net interest income of \$3,257 (11.92 percent) is primarily attributable to a \$2.8 million favorable increase in net margin, a \$.4 million increase in interest income recognition on non-accrual volume, and a \$.1 million increase in earnings credit on the Association's equity due to the increase in the Association's Total members' equity.
- Charge-offs and risks identified in the Association's loan portfolio required a provision for loan losses of \$5,200 to be recorded in the first six months of 2010 as compared to a \$4,500 provision in the first half of 2009.
- At the period ended June 30, 2010, the Association accrued an estimated patronage receipt of \$7,559 as compared to \$6,970 at June 30, 2009. This accrual is based on first half operations only; management anticipates additional income for each successive quarter in 2010. Since this income from the Bank is reasonably estimable and because there is a history of these earnings, management is of the opinion that including this income in quarterly operations provides shareholders with a more accurate forecast of annualized net income. In addition, the Association received \$1,202 for a Special Patronage which was declared and paid by the Bank in June 2010.
- Noninterest income included decrease in fee income of \$166 as new loan activity and secondary market origination have slowed considerably this year. As fees are common practice in a marketplace, the Association utilizes this vehicle to help achieve an acceptable return on its capital. The Association also received additional income from its crop insurance program in 2010 based on claims experience.
- During the first quarter of 2010, the Farm Credit System Insurance Corporation (FCSIC), which insures the System's debt obligations, had assets exceeding the secure base amount as defined by the Farm Credit Act. As a result of the excess assets, FCSIC made certain distributions to Farm Credit System Banks and certain Associations, MidAtlantic's share of the distribution, which is nonrecurring, was \$3,753 and is recorded as Insurance Fund refund within the Noninterest Income section of the Consolidated Statements of Income.
- Noninterest expense decreased \$2,701 (15.00 percent) for the first six months of 2010 as compared to 2009. The year-to-date decrease for Salaries and employee benefits of \$1,107 (9.21 percent) includes a \$523 retirement and other

postretirement benefits favorable variance. The magnitude of this difference as compared to 2009 is expected to continue throughout 2010. The remaining Salaries and employee benefits favorable variance of \$584 is primarily attributable to staff reductions attributable to the Merger, net of 2010 salary adjustments.

Insurance fund premium expense decreased \$1,347 (73.21 percent) resulting from the FCSIC announcement in June 2010 to decrease the insurance premium for 2010 effective January 1, 2010.

Occupancy and equipment and Other operating expenses decreased \$247 from \$4,154 to \$3,907 which includes \$190 reduction in Director's related expenses and expense reductions attributable to the previously mentioned staff reduction resulting from the Merger.

- The Provision for income taxes in 2009 includes the impact of a deferred tax asset valuation allowance.

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 Bank advances the funds to the Association in the form of notes payable. The notes payable are segmented into variable rate and fixed rate sectors. The Association utilizes the variable rate note to fund variable rate loan advances and operating funds requirements. The fixed rate note is used specifically to fund fixed rate loan advances made by the Association. The total Notes payable to the Bank at June 30, 2010 was \$1,874,840 compared to \$1,944,081 at December 31, 2009. This decrease during the period of \$69,241 (3.56 percent) corresponds to the decrease in the Association's loan volume, receipt of prior year Bank patronage, current year net cash generated from operating activities and offset by patronage payments to stockholders.

CAPITAL RESOURCES

Members' equity at June 30, 2010 totaled \$387,732 an increase of \$17,331 (4.68 percent) compared to total members' equity of \$370,401 at December 31, 2009. Net income of \$24,663 for the six months ended June 30, 2010 and net member capital stock/participation certificates issued of \$70, an estimated cash patronage distribution accrual for the first six months of 2010 totaling \$7,000, and patronage distribution adjustment and retained earnings retired of \$430 account for the change.

FCA regulations require that all Farm Credit institutions maintain a minimum permanent capital ratio of 7.0 percent and total surplus and core surplus ratios equal to 3.5 percent. 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. At June 30, 2010, the Association's permanent capital, total surplus and core surplus ratios equaled 15.00 percent, 14.54 percent and 14.15 percent, respectively.

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. 2378, 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 1-800-333-7950, or writing John E. Wheeler, Jr., Chief Financial Officer, MidAtlantic Farm Credit, ACA, P.O. Box 770, Westminster, MD 21158-0770, or accessing the website, www.mafc.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.

MidAtlantic Farm Credit, ACA

Consolidated Balance Sheets

<i>(dollars in thousands)</i>	June 30, 2010	December 31, 2009
	<i>(unaudited)</i>	<i>(audited)</i>
Assets		
Cash	\$ 321	\$ 1,651
Loans	2,236,334	2,288,344
Less: allowance for loan losses	25,412	21,020
Net loans	2,210,922	2,267,324
Loans held for sale	1,266	—
Accrued interest receivable	16,183	13,725
Investment in other Farm Credit institutions	30,851	30,673
Premises and equipment, net	14,057	14,345
Other property owned	2,488	1,008
Due from AgFirst Farm Credit Bank	7,617	17,442
Other assets	8,888	11,847
Total assets	\$ 2,292,593	\$ 2,358,015
Liabilities		
Notes payable to AgFirst Farm Credit Bank	\$ 1,874,840	\$ 1,944,081
Accrued interest payable	5,289	5,491
Patronage refund payable	7,069	8,116
Allocated surplus payable	34	6,915
Other liabilities	17,629	23,011
Total liabilities	1,904,861	1,987,614
Commitments and contingencies		
Members' Equity		
Capital stock and participation certificates	11,302	11,232
Retained earnings		
Allocated	167,921	167,428
Unallocated	208,904	192,164
Accumulated other comprehensive income (loss)	(395)	(423)
Total members' equity	387,732	370,401
Total liabilities and members' equity	\$ 2,292,593	\$ 2,358,015

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

MidAtlantic Farm Credit, 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,	
	2010	2009	2010	2009
Interest Income				
Loans	\$ 31,608	\$ 32,365	\$ 63,613	\$ 64,978
Interest Expense				
Notes payable to AgFirst Farm Credit Bank	16,252	18,363	33,021	37,643
Net interest income	15,356	14,002	30,592	27,335
Provision for (reversal of allowance for) loan losses	3,200	2,500	5,200	4,500
Net interest income after provision for (reversal of allowance for) loan losses	12,156	11,502	25,392	22,835
Noninterest Income				
Loan fees	432	597	863	1,215
Fees for financially related services	564	397	617	431
Equity in earnings of other Farm Credit institutions	4,999	3,863	8,809	7,559
Gains (losses) on other property owned, net	(83)	(1)	(70)	—
Gains (losses) on sale of rural home loans, net	212	285	428	579
Insurance Fund refund	—	—	3,753	—
Other noninterest income	79	115	253	288
Total noninterest income	6,203	5,256	14,653	10,072
Noninterest Expense				
Salaries and employee benefits	5,367	6,179	10,910	12,017
Occupancy and equipment	609	637	1,227	1,287
Insurance Fund premium	19	942	493	1,840
Other operating expenses	1,386	1,419	2,680	2,867
Total noninterest expense	7,381	9,177	15,310	18,011
Income before income taxes	10,978	7,581	24,735	14,896
Provision (benefit) for income taxes	72	—	72	662
Net income	\$ 10,906	\$ 7,581	\$ 24,663	\$ 14,234

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

MidAtlantic Farm Credit, ACA

Consolidated Statements of Changes in Members' Equity

(unaudited)

	Capital Stock and Participation Certificates	Retained Earnings	Accumulated Other Comprehensive Income	Total Members' Equity
<i>(dollars in thousands)</i>	Allocated	Unallocated		
Balance at December 31, 2008	\$ 11,576	\$ 156,869	\$ 185,520	\$ (405) \$ 353,560
Comprehensive income				
Net income		14,234		14,234
Employee benefit plans adjustments			17	17
Total comprehensive income				14,251
Capital stock/participation certificates issued/(retired), net	(428)			(428)
Patronage distribution				
Cash		(4,066)		(4,066)
Patronage distribution adjustment		406	(405)	1
Balance at June 30, 2009	\$ 11,148	\$ 157,275	\$ 195,283	\$ (388) \$ 363,318
Balance at December 31, 2009	\$ 11,232	\$ 167,428	\$ 192,164	\$ (423) \$ 370,401
Comprehensive income				
Net income		24,663		24,663
Employee benefit plans adjustments			28	28
Total comprehensive income				24,691
Capital stock/participation certificates issued/(retired), net	70			70
Patronage distribution				
Cash		(7,000)		(7,000)
Retained earnings retired		(145)		(145)
Patronage distribution adjustment		638	(923)	(285)
Balance at June 30, 2010	\$ 11,302	\$ 167,921	\$ 208,904	\$ (395) \$ 387,732

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 MidAtlantic 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, 2009, are contained in the 2009 Annual Report to Shareholders. These unaudited second quarter 2010 consolidated financial statements should be read in conjunction with the 2009 Annual Report to Shareholders.

The accompanying consolidated financial statements contain all adjustments necessary for a fair presentation of the interim financial condition and results of operations and conform with accounting principles generally accepted in the United States (GAAP) and prevailing practices within the banking industry. The results for the six months ended June 30, 2010, are not necessarily indicative of the results to be expected for the year ending December 31, 2010.

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

The Association maintains an allowance for loan losses in accordance with GAAP. The loan portfolio is reviewed quarterly to determine the adequacy of the allowance for losses. As of June 30, 2010, the allowance for losses is adequate in management's opinion to provide for possible losses on existing loans.

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

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

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

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

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

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

disclosures of valuation techniques and inputs to fair value measurement. The new disclosures and clarification of existing disclosures were effective for interim and annual reporting periods beginning after December 15, 2009, except for the disclosures about purchases, sales, issuances and settlements in the rollforward of activity in Level 3 fair value measurements. Those disclosures are effective for fiscal years beginning after December 15, 2010, and for interim periods within those fiscal years. The adoption of this guidance had no impact on the Association's financial condition and results of operations but resulted in additional disclosures (see Note 4).

NOTE 2 – ALLOWANCE FOR LOAN LOSSES AND IMPAIRED LOANS

An analysis of the allowance for loan losses follows:

	For the six months ended June 30,	
	2010	2009
Balance at beginning of period	\$21,020	\$16,983
Provision for (reversal of) loan losses	5,200	4,500
Charge-offs	(1,022)	(5,867)
Recoveries	214	36
Balance at end of period	<u>\$25,412</u>	<u>\$15,652</u>

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

	2010	2009
Impaired loans with related allowance	\$57,988	\$18,260
Impaired loans with no related allowance	27,616	25,837
Total impaired loans	<u>85,604</u>	<u>44,097</u>
Allowance on impaired loans	<u>\$17,277</u>	<u>\$ 4,283</u>

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

	2010	2009
Average impaired loans	\$ 68,070	\$ 49,252
Interest income recognized on impaired loans	669	213

NOTE 3 – 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,	
	2010	2009
Pension	\$ 2,545	\$3,040
401(k)	234	232
Other postretirement benefits	382	402
Total	<u>\$ 3,161</u>	<u>\$3,674</u>

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

	Actual YTD Through 6/30/10	Projected Contributions For Remainder of 2010	Projected Total Contributions 2010
Pension	\$ 6	\$ 4,212	\$ 4,218
Other postretirement benefits	221	348	569
Total	<u>\$ 227</u>	<u>\$ 4,560</u>	<u>\$ 4,787</u>

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

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

NOTE 4 – FAIR VALUE MEASUREMENT

Effective January 1, 2008, the Association adopted FASB guidance on fair value measurements. This guidance defines fair value, establishes a framework for measuring fair value and expands the Association's disclosures about fair values for certain assets and liabilities measured at fair value on a recurring and non-recurring 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.

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, 2010 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 no Level 2 assets or liabilities measured at fair value on a recurring basis at June 30, 2010.

Level 3

Level 3 inputs to the valuation methodology are unobservable and supported by little or no market activity. Valuation is determined using pricing models, discounted cash flow methodologies, or similar techniques, and could include significant management judgment or estimation. Level 3 assets and liabilities also could include instruments whose price has been adjusted based on dealer quoted pricing that is different than the third-party valuation or internal model pricing.

Level 3 assets at June 30, 2010 include impaired loans which represent the fair value of certain loans that were evaluated for impairment under FASB guidance. The fair value was based upon the underlying collateral since these were collateral-dependent loans. The fair value measurement process uses independent appraisals and other market-based information, but in many cases it also requires significant input based on management's knowledge of and

judgment about current market conditions, specific issues relating to the collateral and other matters. As a result, these fair value measurements fall within Level 3 of the hierarchy. When the value of the collateral, less estimated costs to sell, is less than the principal balance of the loan, a specific reserve is established.

Other property owned is classified as a Level 3 asset at June 30, 2010. The fair value for other property owned is based upon the collateral value. Costs to sell represent transaction costs and are not included as a component of the fair value of other property owned. Level 3 liabilities at June 30, 2010 include standby letters of credit whose market value is internally calculated based on information that is not observable either directly or indirectly in the marketplace.

Assets and Liabilities Measured at Fair Value on a Recurring Basis

The following tables present the assets and liabilities that are measured at fair value on a recurring basis at June 30, 2010 and December 31, 2009 for each of the fair value hierarchy levels:

June 30, 2010						
	Level 1	Level 2	Level 3	Total Fair Value		
Assets:						
Assets held in trust funds	\$ 523	\$ –	\$ –	\$		523
Total Assets	\$ 523	\$ –	\$ –	\$		523
Liabilities:						
Standby letters of credit	\$ –	\$ –	\$ 324	\$		324
Total Liabilities	\$ –	\$ –	\$ 324	\$		324
December 31, 2009						
	Level 1	Level 2	Level 3	Total Fair Value		
Assets:						
Assets held in trust funds	\$ 519	\$ –	\$ –	\$		519
Total Assets	\$ 519	\$ –	\$ –	\$		519
Liabilities:						
Standby letters of credit	\$ –	\$ –	\$ 322	\$		322
Total Liabilities	\$ –	\$ –	\$ 322	\$		322

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, 2010 and 2009. The Association had no transfers of assets or liabilities into or out of Level 1 or Level 2 during the first six months of 2010 and 2009.

	Standby Letters Of Credit
Balance at January 1, 2010	\$ 322
Total gains or (losses) realized/unrealized:	
Included in earnings	-
Included in other comprehensive loss	-
Purchases, sales, issuances and settlements, net	2
Transfers in and/or out of Level 3	-
Balance at June 30, 2010	\$ 324

	Standby Letters Of Credit
Balance at January 1, 2009	\$ 298
Total gains or (losses) realized/unrealized:	
Included in earnings	-
Included in other comprehensive loss	-
Purchases, sales, issuances and settlements, net	164
Transfers in and/or out of Level 3	-
Balance at June 30, 2009	\$ 462

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

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

June 30, 2010						
	Level 1	Level 2	Level 3	Total Fair Value	YTD Total Gains (Losses)	
Assets:						
Impaired loans	\$ -	\$ -	\$ 40,118	\$ 40,118	\$ (9,054)	
Other						
property owned	\$ -	\$ -	\$ 2,321	\$ 2,321	\$ (44)	
December 31, 2009						
	Level 1	Level 2	Level 3	Total Fair Value	YTD Total Gains (Losses)	
Assets:						
Impaired loans	\$ -	\$ -	\$ 19,027	\$ 19,027	\$ (8,217)	
Other						
property owned	\$ -	\$ -	\$ 1,008	\$ 1,008	\$ (12)	

NOTE 5 — DISCLOSURES ABOUT FAIR VALUE OF FINANCIAL INSTRUMENTS

The following table presents the carrying amounts and fair values of the Association's financial instruments at June 30, 2010 and December 31, 2009.

Quoted market prices are generally not available for certain System financial instruments, as described below. Accordingly fair values are based on judgments regarding anticipated cash flows, future expected loss experience, current economic conditions, risk characteristics of various financial instruments, and other factors. These estimates involve uncertainties and matters of judgment, and therefore cannot be determined with precision. Changes in assumptions could significantly affect the estimates.

The estimated fair values of the Association's financial instruments are as follows:

	June 30, 2010		December 31, 2009	
	Carrying Amount	Estimated Fair Value	Carrying Amount	Estimated Fair Value
Financial assets:				
Cash	\$ 321	\$ 321	\$ 1,651	\$ 1,651
Loans, net of allowance	\$2,210,922	\$ 2,248,322	\$ 2,267,324	\$ 2,309,965
Assets held in trust funds	\$ 523	\$ 523	\$ 519	\$ 519
Financial liabilities:				
Notes payable to AgFirst Farm Credit Bank	\$ 1,874,840	\$ 1,911,722	\$ 1,944,081	\$ 1,972,595

A description of the methods and assumptions used to estimate the fair value of each class of the Association's financial instruments for which it is practicable to estimate that value follows:

- Cash:** The carrying value is primarily a reasonable estimate of fair value.
- Loans:** Because no active market exists for the Association's loans, fair value is estimated by discounting the expected future cash flows using the Association's current interest rates at which similar loans would be made to borrowers with similar credit risk. Discount rates are based on the Bank's loan rates as well as management estimates.

For purposes of determining fair value of accruing loans, the loan portfolio is segregated into pools of loans with homogeneous characteristics based upon repricing and credit risk. Expected future cash flows and interest rates reflecting appropriate credit risk are separately determined for each individual pool.

Fair value of loans in a nonaccrual status is estimated to be the carrying amount of the loan less specific reserves.

The carrying value of accrued interest approximates its fair value.

- C. **Investment in AgFirst Farm Credit Bank:** Estimating the fair value of the Association's investment in the Bank 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 7.97 percent of the issued stock of the Bank as of June 30, 2010 net of any reciprocal investment. As of that date, the Bank's assets totaled \$30.7 billion and shareholders' equity totaled \$1.9 billion. The Bank's earnings were \$206.7 million during the first six months of 2010.
- D. **Notes Payable to AgFirst Farm Credit Bank:** The notes payable are segregated into pricing pools according to the types and terms of the loans (or other assets) which they fund. Fair value of the notes payable is estimated by discounting the anticipated cash flows of each pricing pool using the current rate that would be charged for additional borrowings. For purposes of this estimate it is assumed the cash flow on the notes is equal to the principal payments on the Association's loan receivables plus accrued interest on the notes payable. This assumption implies that earnings on the Association's interest margin are used to fund operating expenses and capital expenditures.
- E. **Commitments to Extend Credit:** The estimated market value of off-balance-sheet commitments is minimal since the committed rate approximates current rates offered for commitments with similar rate and maturity characteristics and since the related credit risk is not significant.
- F. **Assets Held in Trust Funds:** See Note 4 for discussion of estimation of fair value for this instrument.

NOTE 6 – SUBSEQUENT EVENTS

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