FARM CREDIT FOCUS

2008 ANNUAL REPORT

TENTH FARM CREDIT DISTRICT

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Overall, the Tenth District had a successful year in 2008, accomplishing milestones in areas such as investment ratings, patronage paid to customers, corporate giving and director training. However, the district also weathered its share of challenges, including the landfall of three hurricanes in the district's five-state territory and the impacts of a major worldwide economic downturn.

In the midst of these triumphs and tragedies, the Tenth District stayed its course by focusing on the Farm Credit mission, basic lending principles and its long-term objectives. It will strive to keep this unwavering focus as it moves forward in today's challenging economic environment.

Noteworthy accomplishments included:

- Despite a challenging economy, overall credit quality remained strong and the district had positive financial results — increasing year-over-year net income.
- The district's wholesale bank received favorable investment-grade ratings that position it to maintain access to high-quality funding for the district.
- The associations paid a record $152.0 million in patronage to their customer-owners.
- The district's two largest associations merged, creating one of the largest Farm Credit associations in the nation.
- More than 300 directors from the Tenth District and the AgFirst District attended the district's Director Development Program.

FARM CREDIT FOCUS

OUR MISSION is to enhance the quality of life in rural America by using cooperative principles to provide competitive credit and superior service to our customers.

BOARD OF DIRECTORS
FARM CREDIT BANK OF TEXAS

Jimmy Dodson

Jon "Mike" Garnett
Vice Chairman

Betty Flores

Ralph W. "Buddy" Cortese
Chairman

William Staats

Joe Crawford

Kenneth Andrews

The board of directors sets policy for the Farm Credit Bank of Texas, which provides funding and services for the Tenth Farm Credit District. In 2008, the board supported key initiatives that will positively impact the district for years to come.

For example, the Farm Credit Bank of Texas received favorable ratings from both Moody's Investors Service and Fitch Ratings. These investment-grade ratings position the bank to maintain access to high-quality funding for the district.

In addition to pursuing the agency ratings mentioned above, the board approved a project to upgrade the district's lending systems, which will enhance efficiency and greatly expand the ability of the district's lending staff to price and structure loans to the market.

Under the leadership of the board, the bank also continues to provide new products and services to meet the diverse financial needs of the district's customers.

NEW DIRECTOR
Lester Little

In December, Tenth District stockholders elected Lester Little of Hallettsville, Texas, to fill the board position being vacated by retiring board member Kenneth Andrews. His three-year term began Jan. 1, 2009.

Little owns and operates a farm headquartered in Lavaca County, Texas, with operations in Jackson, Harris, Fort Bend and Brazoria counties. He is active both in his community and in Farm Credit. At the time of his election, he was chairman of the Capital Farm Credit Board of Directors. He also previously served on several Farm Credit district committees.

2008 FINANCIAL HIGHLIGHTS

Despite a challenging general economy, the Tenth District ended 2008 with positive financial results. Net income increased once again, totaling $267.7 million at year end, up $25.2 million over the net income reported in 2007. Credit quality remains strong at 97.1 percent acceptable at year end, compared to 98.8 percent at Dec. 31, 2007.

Gross loan volume increased 9.8 percent in 2008, up to $16.59 billion, or $1.48 billion more than the $15.11 billion reported at year-end 2007.

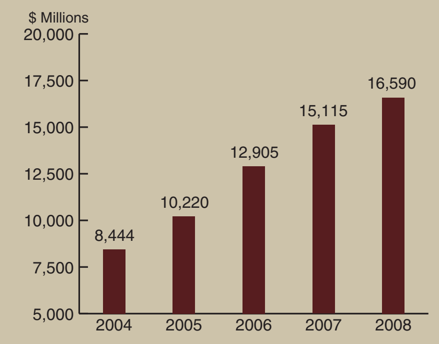
Consistent with cooperative principles, Tenth District associations continued to share earnings with borrowers through patronage programs. Patronage distributions totaled $152.0 million in 2008, compared to $133.7 and $124.8 million in 2007 and 2006, respectively.

2008 KEY FINANCIAL HIGHLIGHTS

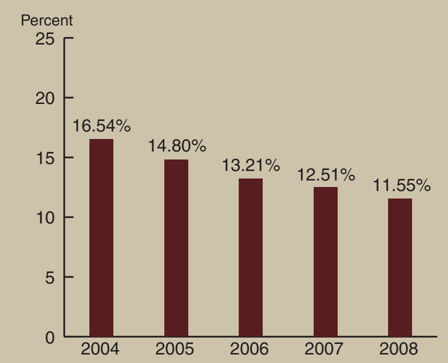
(Dollars in Thousands)

Total Loans	$16,590,071
Total Assets	$20,166,312
Net Income	$267,728
Return on Average Assets	1.40%
Return on Average Members' Equity	11.37%

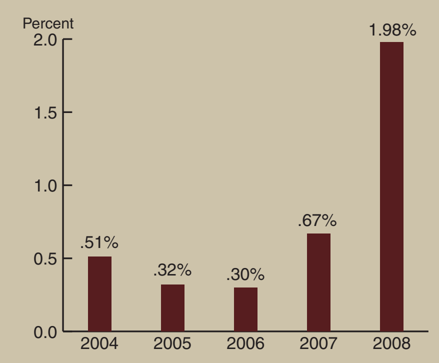
Total Loans Outstanding at Year End



Total Members' Equity to Total Assets at Year End



Nonaccrual Loans and Other Property Owned to Total Loans and Other Property Owned at Year End



2008 MESSAGE TO STOCKHOLDERS

Last year was one for the history books. In the general economy, the news for 2008 could be summed up in one word: recession. Although the first half of the year remained relatively positive, it was followed by two quarters that took a decisively negative downturn. In fact, the conditions in the financial markets at the end of 2008 were some of the worst I've experienced in more than 30 years as an agricultural lender.

Although agriculture fared better than many sectors, the industry witnessed tremendous volatility in commodity prices and input costs. When combined with a global financial crisis, we had a perfect environment to test the mettle of even the best agricultural lenders. Given that context, I am extremely pleased with the positive year-end financial results posted by the Tenth District. Results that would be good in an ordinary year become outstanding in a difficult one.

The district increased its net income, ending the year at $267.7 million, up $25.2 million over the net income reported in 2007. Gross loan volume increased to $16.59 billion, adding another $1.48 billion, or 9.8 percent, to the $15.11 billion reported at year-end 2007.

Even more significant, the associations in the district increased the amount of patronage paid to their customer-owners. Patronage distributions totaled $152.0 million in 2008, compared to $133.7 and $124.8 million in 2007 and 2006, respectively.

Credit quality also remained strong, although deteriorating slightly from year-end 2007. At year end, credit quality was 97.1 percent, compared to 98.8 percent at Dec. 31, 2007.

We continue to be blessed because of where we live. The states in the Tenth District have fared better than many other areas of the nation so far, but a recession of this magnitude will undoubtedly have a ripple effect on our regional economy and on the borrowers we serve in 2009.

In anticipation of a challenging year ahead, we will focus extensively on credit analysis and review, pricing and structuring loans to the market, and closely servicing our existing portfolio. In addition, we will remain focused on fulfilling the Farm Credit mission — to provide access to a competitive and dependable source of credit for qualified borrowers who have well-managed operations. The Farm Credit System was created for such times as these.

Larry R. Doyle
Chief Executive Officer
Farm Credit Bank of Texas

REPORT OF MANAGEMENT

The Farm Credit Bank of Texas and the Tenth Farm Credit District Associations

The accompanying combined financial statements of the Farm Credit Bank of Texas (bank) and Tenth Farm Credit District (district) associations are prepared by management, which is responsible for their integrity and objectivity, including amounts that must necessarily be based on judgments and estimates. The combined financial statements have been prepared in conformity with accounting principles generally accepted in the United States of America appropriate in the circumstances. The combined financial statements, in the opinion of management, present fairly the financial condition of the district. Other financial information included in the annual report is consistent with that in the combined financial statements.

To meet its responsibility for reliable financial information, management depends on the accounting and internal control systems which have been designed to provide reasonable, but not absolute, assurance that assets are safeguarded and transactions are properly authorized and recorded. The systems have been designed to recognize that the cost must be reasonable in relation to the benefits derived. To monitor compliance, financial operations audits are performed. The combined financial statements are audited by PricewaterhouseCoopers LLP (PwC) independent auditors, who also conduct a review of internal controls to the extent necessary to comply with auditing standards generally accepted in the United States of America. The Farm Credit Bank of Texas and district associations are also examined by the Farm Credit Administration.

In the opinion of management, the combined financial statements are true and correct and fairly state the financial position of the bank and district at December 31, 2008, 2007 and 2006. The independent auditors have direct access to the board, which is composed solely of directors who are not officers or employees of the bank or district associations.

The undersigned certify that we have reviewed the December 31, 2008, annual report of the Farm Credit Bank of Texas and district associations, that the report has been prepared in accordance with all applicable statutory or regulatory requirements, and that the information included herein is true, accurate and complete to the best of our knowledge and belief.

Ralph W. Cortese
Chairman of the Board

Larry R. Doyle
Chief Executive Officer

Thomas W. Hill
Senior Vice President, Chief Financial Officer,
Chief Operations Officer

February 27, 2009

REPORT OF AUDIT COMMITTEE

The Farm Credit Bank of Texas and the Tenth Farm Credit District Associations

The Audit Committee (committee) is comprised of the entire board of directors of the Farm Credit Bank of Texas (bank). The committee oversees the scope of the district's system of internal controls and procedures, and the adequacy of management's action with respect to recommendations arising from those internal control activities. The committee's approved responsibilities are described more fully in the Audit Committee Charter, which is available on request or on the bank's Web site at www.farmcreditbank.com. In 2008, six committee meetings were held. The committee approved the appointment of PricewaterhouseCoopers LLP (PwC) as independent auditors for 2008.

Management is responsible for the district's internal controls and the preparation of the financial statements in accordance with accounting principles generally accepted in the United States of America. PwC is responsible for performing an independent audit of the district's financial statements in accordance with auditing standards generally accepted in the United States of America and to issue a report thereon. The committee's responsibilities include monitoring and overseeing these processes.

In this context, the committee reviewed and discussed the district's audited financial statements for the year ended December 31, 2008 with management and PwC. The committee also reviewed with PwC the matters required to be discussed by Statement on Auditing Standards No. 114 (The Auditor's Communications With Those Charged With Governance), and both PwC and the district's internal auditor directly provided reports on significant matters to the committee.

The committee discussed with appropriate representatives of PwC the firm's independence from the district. The committee also reviewed the non-audit services provided by PwC and concluded that these services were not incompatible with maintaining the independent accountant's independence. Furthermore, throughout 2008 the committee has discussed with management and PwC such other matters and received such assurances from them as the committee deemed appropriate.

William F. Staats, Chairman
Joe R. Crawford, Vice Chairman
Ralph W. Cortese
Jon M. Garnett
James F. Dodson
Elizabeth G. Flores
Lester Little

Audit Committee Members

February 27, 2009

REPORT ON *INTERNAL CONTROL OVER FINANCIAL REPORTING*

The Farm Credit Bank of Texas' (bank's) principal executive and principal financial officer are responsible for establishing and maintaining adequate internal control over financial reporting for the district's combined 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 bank's principal executive and principal financial officer, or persons performing similar functions, and effected by its boards of directors, management and other personnel, to provide reasonable assurance regarding the reliability of financial reporting information and the preparation of the combined financial statements for external purposes in accordance with accounting principles generally accepted in the United States of America and 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 district; (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 bank; and (3) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use or disposition of the district's assets that could have a material effect on its combined financial statements.

The bank's management has completed an assessment of the effectiveness of internal control over financial reporting as of December 31, 2008. 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 district concluded that as of December 31, 2008, the internal control over financial reporting was effective based upon the COSO criteria. Additionally, based on this assessment, the bank determined that there were no material weaknesses in the internal control over financial reporting as of December 31, 2008.

Larry R. Doyle
Chief Executive Officer

Thomas W. Hill
Senior Vice President, Chief Financial Officer,
Chief Operations Officer

February 27, 2009

Five-Year Summary of Selected Combined Financial Data

FARM CREDIT BANK OF TEXAS AND DISTRICT ASSOCIATIONS

(dollars in thousands)	**2008**	2007	2006	2005	2004*
Balance Sheet Data					
Cash, federal funds sold and securities purchased under resale agreements	**$ 233,580**	$ 181,205	$ 149,399	$ 94,291	$ 91,669
Investment securities	**3,046,397**	2,410,999	2,672,242	2,697,876	1,787,706
Loans	**16,590,071**	15,114,537	12,905,321	10,219,596	8,444,347
Less allowance for loan losses	**51,653**	24,495	13,969	9,533	10,617
Net loans	**16,538,418**	15,090,042	12,891,352	10,210,063	8,433,730
Other property owned, net	**6,495**	1,817	2,020	3,902	5,184
Other assets	**341,422**	312,434	272,054	206,088	180,650
Total assets	**$ 20,166,312**	$ 17,996,497	$ 15,987,067	$ 13,212,220	$ 10,498,939
Obligations with maturities of one year or less	**$ 9,920,558**	$ 7,751,462	$ 6,458,754	$ 5,968,414	$ 4,521,114
Obligations with maturities greater than one year	**7,916,037**	7,994,374	7,415,653	5,288,711	4,241,696
Total liabilities	**17,836,595**	15,745,836	13,874,407	11,257,125	8,762,810
Preferred stock	**202,754**	202,754	203,565	203,569	103,963
Capital stock and participation certificates	**63,859**	62,489	59,068	73,642	88,962
Allocated retained earnings	**211,450**	133,423	83,705	32,327	32,662
Unallocated retained earnings	**1,984,421**	1,886,488	1,792,723	1,692,534	1,531,503
Accumulated other comprehensive loss	**(132,767)**	(34,493)	(26,401)	(46,977)	(20,961)
Total members' equity	**2,329,717**	2,250,661	2,112,660	1,955,095	1,736,129
Total liabilities and members' equity	**$ 20,166,312**	$ 17,996,497	$ 15,987,067	$ 13,212,220	$ 10,498,939
Statement of Income Data					
Net interest income	**$ 470,428**	$ 432,381	$ 386,246	$ 340,472	$ 304,136
(Provision) negative provision for loan losses	**(53,514)**	(43,131)	(9,356)	(1,084)	157,325
Noninterest expense, net	**(148,842)**	(146,569)	(137,000)	(118,872)	(117,177)
(Provision for) benefit from income taxes	**(344)**	(141)	228	(639)	(1,768)
Net income	**$ 267,728**	$ 242,540	$ 240,118	$ 219,877	$ 342,516
Key Financial Ratios (unaudited)					
Net income to:					
Average assets	**1.40%**	1.44%	1.66%	1.92%	3.66%
Average members' equity	**11.37**	10.86	11.69	11.80	21.89
Net interest income to average earning assets	**2.50**	2.61	2.72	3.04	3.26
Net charge-offs (recoveries) to average loans	**0.16**	0.23	0.04	0.02	0.08
Total members' equity to total assets	**11.55**	12.51	13.21	14.80	16.54
Allowance for loan losses to total loans	**0.31**	0.16	0.11	0.09	0.13
Regulatory permanent capital ratio (bank only)	**14.03**	13.43	13.67	17.36	19.82
Total surplus ratio (bank only)	**11.25**	11.15	11.61	14.97	16.55
Core surplus ratio (bank only)	**6.40**	6.70	6.93	8.82	11.51
Net collateral ratio (bank only)	**105.40**	105.18	105.35	105.90	105.69
Other (unaudited)					
Net income distributions declared					
Preferred stock dividends	**$ 15,122**	$ 15,122	$ 15,122	$ 11,342	$ 7,561
Patronage distributions					
Cash	**71,402**	76,253	70,479	49,964	37,946
Allocated earnings	**80,558**	57,400	54,328	6,435	1,886

*Net income and certain profitability ratios for 2004 were affected by the nonrecurring negative provision for loan losses of $157.7 million due to the refinement of the allowance methodology in 2004.

Combined Average Balances and Net Interest Earnings

FARM CREDIT BANK OF TEXAS AND DISTRICT ASSOCIATIONS
(unaudited)
December 31,

	2008			2007			2006		
(dollars in thousands)	**Average Balance**	**Interest**	**Average Rate**	Average Balance	Interest	Average Rate	Average Balance	Interest	Average Rate
Assets									
Investment securities, federal funds sold and securities purchased under resale agreements	**$ 2,709,676**	**$ 111,358**	**4.11%**	$ 2,598,854	$ 131,768	5.07%	$ 2,929,742	$ 141,260	4.82%
Loans	**16,106,806**	**1,006,081**	**6.25**	13,940,105	1,053,629	7.56	11,272,884	845,135	7.50
Total interest-earning assets	**18,816,482**	**1,117,439**	**5.94**	16,538,959	1,185,397	7.17	14,202,626	986,395	6.95
Cash	**30,863**			33,110			32,709		
Accrued interest receivable	**228,902**			238,632			191,322		
Allowance for loan losses	**(36,800)**			(21,122)			(11,285)		
Other noninterest-earning assets	**118,792**			103,376			90,355		
Total average assets	**$ 19,158,239**			$ 16,892,955			$ 14,505,727		
Liabilities and Members' Equity									
Bonds, medium-term notes and subordinated debt, net	**$ 11,541,763**	**$ 502,377**	**4.35%**	$ 11,718,042	$ 608,067	5.19%	$ 10,343,964	$ 506,346	4.90%
Discount notes, net, and other	**4,851,341**	**144,634**	**2.98**	2,618,740	144,949	5.54	1,788,304	93,803	5.25
Total interest-bearing liabilities	**16,393,104**	**647,011**	**3.95**	14,336,782	753,016	5.25	12,132,268	600,149	4.95
Noninterest-bearing liabilities	**410,778**			323,042			319,585		
Total liabilities	**16,803,882**			14,659,824			12,451,853		
Members' equity and retained earnings	**2,354,357**			2,233,131			2,053,874		
Total average liabilities and members' equity	**$ 19,158,239**			$ 16,892,955			$ 14,505,727		
Net interest rate spread		**$ 470,428**	**1.99%**		$ 432,381	1.92%		$ 386,246	2.00%
Net interest margin			**2.50%**			2.61%			2.72%

Management's Discussion and Analysis

(dollars in thousands, except as noted)

The following commentary provides a discussion and analysis of the combined financial position and results of operations of the Farm Credit Bank of Texas (bank), the Federal Land Credit Associations (FLCAs) and the Agricultural Credit Associations (ACAs) of the Tenth Farm Credit District (district). FLCAs and ACAs collectively are referred to as "associations." The commentary should be read in conjunction with the accompanying combined financial statements, notes to the combined financial statements (notes) and additional sections of this report. The accompanying combined financial statements were prepared under the oversight of the bank's Audit Committee.

The district, which serves Texas, Alabama, Mississippi, Louisiana and portions of New Mexico, is part of the federally chartered Farm Credit System (System). The bank provides funding to the associations, which, in turn, provide credit to their borrower-shareholders. As of December 31, 2008, the district comprised the bank, six FLCAs and 13 ACAs. The bank also had funding relationships with five Other Financing Institutions (OFIs).

Forward-Looking Information

This annual information report contains forward-looking statements. These statements are not guarantees of future performance and involve certain risks, uncertainties and assumptions that are difficult to predict. Words such as "anticipates," "believes," "could," "estimates," "may," "should," "will," or other variations of these terms are intended to identify the forward-looking statements. These statements are based on assumptions and analyses made in light of experience and other historical trends, current conditions and expected future developments. However, actual results and developments may differ materially from our expectations and predictions due to a number of risks and uncertainties, many of which are beyond our control. These risks and uncertainties include, but are not limited to:

- political, legal, regulatory, and economic conditions and developments in the United States and abroad;
- economic fluctuations in the agricultural, rural utility, international and farm-related business sectors;
- weather-related, disease and other adverse climatic or biological conditions that periodically occur that impact agricultural productivity and income;
- changes in United States government support of the agricultural industry; and
- actions taken by the Federal Reserve System in implementing monetary policy.

Critical Accounting Policies

The combined financial statements are reported in conformity with accounting principles generally accepted in the United States of America. Our significant accounting policies are critical to the understanding of our results of operations and financial position because some accounting policies require us to make complex or subjective judgments and estimates that may affect the value of certain assets or liabilities. We consider these policies critical because management has to make judgments about matters that are inherently uncertain. For a complete discussion of significant accounting policies, see Note 2, "Summary of Significant Accounting Policies," of the accompanying combined financial statements. The following is a summary of certain critical policies.

- Allowance for loan losses – The allowance for loan losses is management's best estimate of the amount of probable losses existing in and inherent in our loan portfolio. The allowance for loan losses is increased through provisions for loan losses and loan recoveries and is decreased through loan loss reversals and loan charge-offs. The allowance for loan losses is determined based on a periodic evaluation of the loan portfolio, which generally considers recent historical charge-off experience adjusted for relevant factors. These factors include types of loans, credit quality, specific industry conditions, general economic and political conditions, and changes in the character, composition and performance of the portfolio, among other factors.

  Significant individual loans are evaluated based on the borrower's overall financial condition, resources and payment record; the prospects for support from any financially responsible guarantor; and, if appropriate, the estimated net realizable value of any collateral. The allowance for loan losses attributable to these loans is established by a process that estimates the probable loss inherent in the loans, taking into account various historical and projected factors, internal risk ratings, regulatory oversight, and geographic, industry and other factors.

  Changes in the factors considered by management in the evaluation of losses in the loan portfolios could result in a change in the allowance for loan losses and could have a direct impact on the provision for loan losses and the results of operations.

- Valuation methodologies – Management applies various valuation methodologies to assets and liabilities that often involve a significant degree of judgment, particularly when liquid markets do not exist for the particular items being valued. Quoted market prices are referred to when estimating fair values for certain assets for which an observable liquid market exists, such as most investment securities. Management utilizes significant estimates and assumptions to value items for which an observable liquid market does not exist. Examples of these items include impaired loans, pension and other postretirement benefit obligations, certain mortgage-related securities, and certain derivative and other financial instruments. These valuations require the use of various assumptions, including, among others, discount rates, rates of return on assets, repayment rates, cash flows, default rates, costs of servicing and liquidation values. The use of different assumptions could produce significantly different results, which could have material positive or negative effects on the bank's or district's results of operations.

- Pensions – The bank and its related associations participate in defined benefit retirement plans. These plans are non-contributory, and benefits are based on salary and years of service. In addition, the bank and its related associations also participate in defined contribution retirement savings plans. Pension expense for all plans is recorded as part of salaries and employee benefits. Pension expense is determined by actuarial valuations based on certain assumptions, including expected long-term rate of return on plan assets and discount rate. The expected return on plan assets for the year is calculated based on the composition of assets at the beginning of the year and the expected long-term rate of return on that portfolio of assets. The discount rate is used to determine the present value of our future benefit obligations. We selected the discount rate by reference to Hewitt Associates' median corporate bond index, actuarial analyses and industry norms.

OVERVIEW

General

The district's loan portfolio grew to $16.6 billion in 2008, a 9.8 percent increase over the prior year. The district's $25.2 million increase in net income for 2008 was driven by an 8.8 percent increase in net interest income. The net interest rate spread improved, as well as the district's efficiency ratios, tracking operating expense in relation to income and earning assets. The passage of the Food, Conservation, and Energy Act of 2008 (2008 Farm Bill), continued federal support of agriculture. However, continued growth has put additional pressure on capital ratios and strategies for the management of assets and capital adequacy. Adverse conditions in the general economy have impacted the last six months of 2008, resulting in a $223.2 million increase in impaired loans, and a $10.4 million increase in provisions for loan losses as compared to 2007.

Funding

The Farm Credit System continues to be a reliable source of debt capital for the farmers, ranchers and other rural businesses that we serve. However, the extraordinary instability of the global financial markets in the last six months and the negative economic developments of the last year have increased uncertainty about repayment capacity in the financial markets. The resulting reduction in investor willingness to invest in longer-term debt securities has reduced the System's ability to issue debt with preferred maturities and structures. Responses of the federal government to assist and protect commercial banks and the housing government-sponsored enterprises may have the unintended consequence of increasing our funding costs and further reducing our ability to issue debt with preferred maturities and structures.

Due the System's healthy financial position, it continues to enjoy a high demand for short-term debt securities at desirable rates, though the cost of issuing longer-term debt is expected to remain at higher levels. Although the bank has been able to augment its net interest rate spread with callable debt management, and although district lending practices have adapted to financial market conditions by instituting loan pricing and structuring changes that more appropriately reflect these funding challenges, these current market pressures may compress net interest margins in the near term.

Agricultural Outlook

Although 2008 has been generally projected to be an exceptional year for American crop producers, results in the Tenth District have been significantly impacted by drought as well as by the effect of higher commodity prices and global demands. In the livestock market, which underlies 38 percent of the district's loan portfolio, drought, high feed costs, and reduced feeder cattle prices have resulted in increased cow slaughter, reducing expectations of beef production in the future. As the economic downturn became more prevalent in 2008, beef purchasing has shifted away from restaurant and commercial dining to increased home consumption. In a slowing economy, declining consumer meat demand may soften all protein prices. Poultry, bird slaughter and broiler production decreased in the fourth quarter of 2008, and the trend is expected to continue during most of 2009.

The Southwest region, which includes the western half of the district, was forecast to have its smallest upland cotton crop in five years, due to weather impact and the resulting significant abandonment. The Delta region's production was forecast to be 50 percent less than 2007, and is expected to be the lowest harvest since 1986. The Southeast region's modest increase was expected to be the only regional increase in production over 2007. Corn and feed grain crops, which have enjoyed higher prices in 2008, have started to soften as projections for feed, residual use and food, and ethanol use are being lowered.

While the district's agricultural economy faces these challenges, it does enjoy geographic and commodity diversity. Government support programs also assist agricultural borrowers. Though the district's loan portfolio has also enjoyed the enhancement of loans supported by off-farm income, some borrowers reliant on off-farm income may be adversely affected by the general economic downturn.

Financial Highlights

- ❖ The aggregate principal amount of loans outstanding at December 31, 2008, was $16.59 billion, compared to $15.11 billion at December 31, 2007, reflecting an increase of 9.8 percent over December 31, 2007.
- ❖ Net income totaled $267.7 million for the year ended December 31, 2008, compared to $242.5 million for 2007 and $240.1 million for 2006, reflecting an increase of 10.4 percent from 2007 and an increase of 11.5 percent over 2006.
- ❖ Net interest income for the year ended December 31, 2008, was $470.4 million compared to $432.4 million for 2007 and $386.2 million for 2006, reflecting 8.8 and 21.8 percent increases over the years ended December 31, 2007 and 2006, respectively.
- ❖ Return on average assets and return on average members' equity for the year ended December 31, 2008, were 1.40 and 11.37 percent, respectively, compared to 1.44 and 10.86 percent for 2007 and 1.66 and 11.69 percent for 2006, respectively.
- ❖ Patronage distributions declared totaled $152.0 million in 2008, compared to $133.7 and $124.8 million in 2007 and 2006, respectively.
- ❖ In 2008, the bank sold $800 million of participations in district direct notes receivable to another System bank. In 2007, the bank sold $1.3 billion of these participations. Cumulative sales of the participations in direct notes totaled $3.5 billion at December 31, 2008. These transactions enhance the composition of the bank's capital and liquidity position in order to facilitate the district's diversification and opportunities for growth.

RESULTS OF OPERATIONS

Net Income

The district's net income of $267.7 million for the year ended December 31, 2008, reflected an increase of 10.4 percent from net income of $242.5 million for the year ended December 31, 2007, and an increase of 11.5 percent from net income of $240.1 million for 2006. The return on average assets decreased to 1.40 percent for the year ended December 31, 2008, from 1.44 percent reported for the year ended December 31, 2007. This decrease was due primarily to an increase of $10.4 million in the district's provision for loan losses, discussed more fully in the "Loan Portfolio" section of this discussion, offset by effects of a 13.8 percent expansion in the district's earning assets and the increase in the interest rate spread on those earning assets, discussed more fully in the following "Net Interest Income" section.

Changes in Components of Net Income

	2008 vs. 2007	2007 vs. 2006
Net income, prior period	$ 242,540	$ 240,118
Interest income	(67,958)	199,002
Interest expense	106,005	(152,867)
Net interest income	38,047	46,135
Provision for loan losses	(10,383)	(33,775)
Noninterest income	11,426	3,498
Noninterest expense	(13,699)	(13,067)
Provision for income taxes	(203)	(369)
Total increase in net income	25,188	2,422
Net income	$ 267,728	$ 242,540

Discussion of the changes in components of net income is included in the following narrative.

Interest Income

Total interest income for the year ended December 31, 2008, was $1.1 billion, a decrease of $68.0 million, or 5.7 percent, compared to 2007. This decrease was due to a decrease in the interest rates on earning assets, offset by an increase in average interest-earning assets.

Total interest income for 2007 was $1.2 billion, an increase of $199.0 million, or 20.2 percent, from 2006. This increase was due to an increase in average interest-earning assets, and to a lesser extent, an increase in the interest rates on earning assets.

The following table illustrates the impact that volume and yield changes had on interest income over these periods.

	Year Ended December 31,	
	2008 vs. 2007	2007 vs. 2006
Increase in average earning assets	$ 2,277,523	$ 2,336,333
Average yield, prior year	7.17%	6.95%
Interest income variance attributed to change in volume	163,298	162,375
Average earning assets, current year	18,816,482	16,538,959
(Decrease) increase in average yield	(1.23)%	0.22%
Interest income variance attributed to change in yield	(231,256)	36,627
Net change in interest income	$ (67,958)	$ 199,002

Analysis of Operating Margin to Average Earning Assets

	For the Years Ended December 31,		
	2008	2007	2006
Net interest margin	**2.50%**	2.61%	2.72%
Operating expense	**0.98**	1.04	1.11
Operating margin	**1.52%**	1.57%	1.61%

Interest Expense

Total interest expense for the year ended December 31, 2008, was $647.0 million, a decrease of $106.0 million, or 14.1 percent, from the prior year. Total interest expense for the year ended December 31, 2007, was $753.0 million, an increase of $152.9 million, or 25.5 percent, from 2006. The decrease for 2008 over 2007 was due primarily to a decrease in the average rate on that debt, offset by an increase in interest-bearing liabilities. The increase from 2007 over 2006 was due mainly to an increase in interest-bearing liabilities, and to a lesser extent, to an increase in the average rate on that debt.

The following table illustrates the impact that volume and rate changes had on interest expense over these periods.

	Year Ended December 31,	
	2008 vs. 2007	2007 vs. 2006
Increase in average interest-bearing liabilities	$ 2,056,322	$ 2,204,514
Average rate, prior year	5.25%	4.95%
Interest expense variance attributed to change in volume	107,957	109,123
Average interest-bearing liabilities, current year	16,393,104	14,336,782
(Decrease) increase in average rate	(1.31)%	0.30%
Interest expense variance attributed to change in rate	(213,962)	43,744
Net change in interest expense	$ (106,005)	$ 152,867

Net Interest Income

Net interest income increased by $38.0 million, or 8.8 percent, from 2007 to 2008 and increased by $46.1 million, or 11.9 percent, from 2006 to 2007. Factors responsible for these changes are illustrated in Figure 1.

Net interest income for 2008 increased from 2007 due to an increase in average-earning assets and a 7-basis-point increase in the interest rate spread, which is the difference between the average rate received on interest-earning assets and the average rate paid on interest-bearing debt.

The increase in earning assets was due primarily to loan growth at the district's associations, and, to a lesser extent, to growth in the bank's loan participation portfolio, and a slight increase in the bank's investment portfolio. The increase in the interest rate spread was due primarily to the result of the bank's ability to call and replace callable debt with debt that had more favorable terms. Loan pricing spreads at the associations have remained narrow due to continued competition with commercial banks and other lenders for a larger market share. Competitive conditions at the time of an association loan's repricing may affect interest rate spreads. Although the interest rate spread on association loans has been compressed, they continue to be the highest yielding of the district's earning assets.

Net interest income for 2007 increased from 2006 due to an increase in the district's earning assets, partially offset by an 8-basis-point decrease in the interest rate spread.

Noninterest Income

Noninterest income of $36.2 million reflected an increase of $11.4 million, or 46.0 percent, from 2007 to 2008. The increase was primarily due to a $10.5 million increase in patronage from another System bank, a $2.5 million increase in fees for loan-related services, and a $2.1 million increase in gains on sales of investment securities, offset by a $2.2 million decrease in other noninterest income which includes a $2.2 million loss recognized due to other-than-temporary impairment on an investment security which is more fully discussed in "Investments."

Noninterest income for 2007 of $24.8 million reflected an increase of $3.5 million, or 16.4 percent, from 2006 to 2007. The increase was due to a $3.7 million increase in patronage from another System bank and the $1.2 million write-off in the fourth quarter of 2006 of patronage receivable from the Funding Corporation, offset by an $825 decrease in loan prepayment fees, a decrease of $364 in gains on sales of investments and a $287 adjustment decreasing the bank's gain recognized on the bank's portion of property sold by the Farm Credit System Building Association during 2006.

Provision for Loan Losses

The provision for loan losses for 2008 was $53.5 million, reflecting an increase of $10.4 million from the $43.1 million provision recorded in 2007. The increase is due primarily to the increase of the bank's provision of $19.5 million which was primarily related to a $20.5 million provision related to participation loans to seven borrowers, offset by a $9.1 million decrease in provisions made by the district's associations. The decrease in the provision recorded by the district's associations is primarily related to provisions made in 2007 on participations in a loan to one borrower.

Noninterest Expenses

Noninterest expenses for 2008 totaled $185.1 million, increasing $13.7 million, or 8.0 percent, from 2007. The increase was primarily due to an increase of $5.6 million in salaries and employment benefits, an increase of $3.1 million in premiums to the Farm Credit System Insurance Corporation (FCSIC or Insurance Fund), an increase of $3.9 million in other operating expenses, an increase of $711 in occupancy and equipment expense, and an increase of $343 in net losses on other property owned. The $5.6 million increase in salaries and employee benefits was due primarily to a $7.9 million increase in salaries and related payroll taxes, a $2.6 million increase in pension and retirement benefits, and an $884 increase in other benefits, offset by a $5.2 million increase in salaries and benefits capitalized in accordance with Statement of Financial Accounting Standards (SFAS) No. 91, "Accounting for Nonrefundable Fees and Costs Associated With Originating and Acquiring Loans and Initial Direct Costs of Leases," and a $652 increase in capitalized salaries and benefits related to the costs of information technology systems obtained for internal use by the bank. Salaries increased due to increases in the number of employees and in pay rates, primarily at the district's associations. The increase in pension and retirement benefits included a $3.1 million benefit expense related to the settlement upon discontinuation of a key bank employee's participation in the Supplemental Pension Plan (see CEO compensation discussion in the Disclosure and Information Index section). The $3.1 million increase in premiums paid to the FCSIC was primarily due to a change in the premium base effective July 1, 2008, from loans to Systemwide debt issued, and to increases during the first six months of 2008 over the same period of 2007 on the loan balances on which premiums were based at that time. The $3.9 million increase in other operating expenses was primarily due to a $2.7 million increase in professional and contract services, an $819 increase in travel expenses, a $552 increase in directors' expenses, and a $345 increase in communications expenses, offset by a $472 decrease in training expenses.

Noninterest expenses for 2007 totaled $171.4 million, increasing $13.1 million, or 8.3 percent, from 2006. The increase was primarily due to an increase of $4.8 million in premiums to the FCSIC, an increase of $3.6 million in salaries and employment benefits, an increase of $3.8 million in other operating expenses, and an increase of $1.0 million in occupancy and equipment expense. The $4.8 million

Figure 1

Analysis of Net Interest Income

	2008		2007		2006	
	Avg. Balance	Interest	Avg. Balance	Interest	Avg. Balance	Interest
Loans	$ 16,106,806	$ 1,006,081	$ 13,940,105	$ 1,053,629	$ 11,272,884	$ 845,135
Investments	2,709,676	111,358	2,598,854	131,768	2,929,742	141,260
Total earning assets	18,816,482	1,117,439	16,538,959	1,185,397	14,202,626	986,395
Interest-bearing liabilities	16,393,104	647,011	14,336,782	753,016	12,132,268	600,149
Impact of capital	$ 2,423,378		$ 2,202,177		$ 2,070,358	
NET INTEREST INCOME		$ 470,428		$ 432,381		$ 386,246

	2008 Average Yield	2007 Average Yield	2006 Average Yield
Yield on loans	6.25%	7.56%	7.50%
Yield on investments	4.11	5.07	4.82
Yield on earning assets	5.94	7.17	6.95
Cost of interest-bearing liabilities	3.95	5.25	4.95
Interest rate spread	1.99	1.92	2.00
Impact of capital	0.51	0.69	0.72
Net interest income/average earning assets	2.50	2.61	2.72

increase in premiums paid to the FCSIC was primarily due to volume increases on the loans on which premiums are assessed. The $3.6 million increase in salaries and employee benefits was due primarily to a $7.9 million increase in compensation and related payroll taxes, a $1.2 million increase in pension and retirement expenses, and an $861 increase in other benefits, substantially offset by a $6.4 million increase in capitalization of salaries and benefits in accordance with FAS 91. Compensation and payroll-related taxes increased due to increases in compensation rates and in the number of employees at district associations and at the bank. The $3.8 million increase in other operating expenses was primarily due to a $2.3 million increase in professional and contract services, a $594 increase in advertising and member relations expenses, a $415 increase in supervisory and examination expenses, a $357 increase in travel expenses, a $322 increase in training expenses, and a $305 increase in directors' expenses.

Operating expense (salaries and employee benefits, occupancy and equipment, Insurance Fund premiums, and other operating expenses) statistics are set forth below for each of the three years ended December 31,

	2008	2007	2006
Excess of net interest income over operating expense	**$ 285,714**	$ 261,023	$ 228,017
Operating expense as a percentage of net interest income	**39.3%**	39.6%	41.0%
Operating expense as a percentage of net interest income and noninterest income	**36.5**	37.5	38.8
Operating expense as a percentage of average loans	**1.15**	1.23	1.40
Operating expense as a percentage of average earning assets	**0.98**	1.04	1.11

The district's operating expense statistics for 2008 and 2007 reflect the district's growth in net interest income, which outpaced increases in operating expenses, and also the growth in the district's earning assets. In 2006, the increase in operating expenses was greater than the growth of net interest income. Net interest income has increased 8.8 percent and 11.9 percent for the years ended December 31, 2008 and 2007, respectively, while operating expenses increased at the rates of 7.8 percent and 8.3 percent, respectively, for the same periods.

CORPORATE RISK PROFILE

Overview

The district is in the business of making agricultural and other loans that requires us to take certain risks in exchange for compensation for the risks undertaken. Management of risks inherent in our business is essential for our current and long-term financial performance. Our goal is to mitigate risk, where appropriate, and to properly and effectively identify, measure, price, monitor and report risks in our business activities.

The major types of risk to which we have exposure are:

- structural risk – risk inherent in our business and related to our structure (an interdependent network of lending institutions);
- credit risk – risk of loss arising from an obligor's failure to meet the terms of its contract or failure to perform as agreed;
- interest rate risk – risk that changes in interest rates may adversely affect our operating results and financial condition;
- liquidity risk – risk of loss arising from the inability to meet obligations when they come due without incurring unacceptable losses;
- operational risk – risk of loss resulting from inadequate or failed internal processes or systems, errors by employees or external events; and
- political risk – risk of loss of support for the System and agriculture by the federal and state governments.

Structural Risk Management

Structural risk results from the fact that the bank and its related associations are part of the Farm Credit System (System), which is comprised of banks and associations that are cooperatively owned, directly or indirectly, by their borrowers. While System institutions are financially and operationally interdependent, this structure at times requires action by consensus or contractual agreement. Further, there is structural risk in that only the banks are jointly and severally liable for the payments of Systemwide debt securities. Although capital at the association level reduces a bank's credit exposure with respect to its direct loans to its affiliated associations, this capital may not be available to support the payment of principal and interest on Systemwide debt securities.

In order to mitigate this risk, we utilize two integrated contractual agreements — the Amended and Restated Contractual Interbank Performance Agreement, or CIPA, and the Amended and Restated Market Access Agreement, or MAA. Under provisions of the CIPA, a score is calculated that measures the financial condition and performance of each district using various ratios that take into account the district's and bank's capital, asset quality, earnings, interest-rate risk and liquidity. Based on these measures, the CIPA establishes an agreed-upon standard of financial condition and performance that each district must achieve and maintain.

Periodically, the ratios in the CIPA model are reviewed, with the assistance of an independent party, to take into consideration current performance standards in the financial services industry. In connection with the most recent review, effective January 1, 2005, certain ratios were revised to better reflect improved financial condition and performance in the financial services industry. In addition, the agreed-upon financial condition and performance standard was revised to conform to the trigger points in the MAA. The CIPA also establishes economic incentives whereby monetary penalties are applied if the performance standard is not met. These penalties will occur at the same point at which a bank would be required to provide additional monitoring information under the MAA.

The MAA establishes criteria and procedures for the banks — which are jointly and severally liable for the payment of Systemwide debt securities — that provide operational oversight and control over a bank's access to System funding if the creditworthiness of the bank declines below certain agreed-upon levels. The MAA promotes the identification and resolution of individual bank financial problems in a timely manner and discharges the Federal Farm Credit Banks Funding Corporation's (Funding Corporation) statutory responsibility for determining conditions of participation for each bank's participation in each issuance of Systemwide debt securities.

Under the MAA, if certain financial criteria are not met, a bank may be placed in one of three categories, each of which imposes certain requirements and/or restrictions on the affected bank. The criteria under the MAA are the CIPA scores, the net collateral ratio and the permanent capital ratio of a bank. The bank net collateral ratio is net collateral (primarily earning assets) divided by total liabilities less subordinated debt, subject to certain limits, and the bank permanent capital ratio is primarily the bank's common stock, preferred stock, subordinated debt, subject to certain limits, and surplus divided by risk-adjusted assets. The criteria for the net collateral ratio and the permanent capital ratio are:

	Net Collateral Ratio	Permanent Capital Ratio
Category I	<104%	<8.0%
Category II	<103%	<7.0%
Category III	<102%	<5.0%

The categories are progressively more restrictive: a "Category I" bank is subject to additional monitoring and reporting requirements; with very limited exceptions, a bank in Category II will be allowed market access only to the extent necessary to roll over principal (net of any original issue discount) on maturing debt obligations; and a "Category III" bank may not be permitted to participate in issuances of Systemwide debt securities.

During the three years ended and as of December 31, 2008, all banks met the agreed-upon standard of financial condition and performance required by the CIPA, and none of the banks were placed in any of the three categories designated for banks failing to meet the MAA's specified financial criteria.

Credit Risk Management

Credit risk arises from the potential inability of an obligor to meet its repayment obligation and exists in our outstanding loans, letters of credit, unfunded loan commitments, investment portfolio and derivative counterparty credit exposures. We manage credit risk associated with our retail lending activities through an assessment of the credit risk profile of an individual borrower. Each institution sets their own underwriting standards and lending policies, approved by the board of directors, that provides direction to loan officers. Underwriting standards include, among other things, an evaluation of:

- character – borrower integrity and credit history;
- capacity – repayment capacity of the borrower based on cash flows from operations or other sources of income;
- collateral – protects the lender in the event of default and represents a potential secondary source of loan repayment;
- capital – ability of the operation to survive unanticipated risks; and
- conditions – intended use of the loan funds.

The retail credit risk management process begins with an analysis of the borrower's credit history, repayment capacity and financial position. Repayment capacity focuses on the borrower's ability to repay the loan based on cash flows from operations or other sources of income, including non-farm income. Real estate loans with terms greater than 10 years must be secured by first liens on the real estate (collateral). As required by Farm Credit Administration regulations, each institution that makes loans on a secured basis must have collateral evaluation policies and procedures. Real estate loans with terms greater than 10 years may be made only in amounts up to 85 percent of the original appraised value of the property taken as security or up to 97 percent of the appraised value if guaranteed by a state, federal or other governmental agency. The actual loan to appraised value when loans are made is generally lower than the statutory maximum percentage. Appraisals are required for loans of more than $250,000. In addition, each loan is assigned a credit risk rating based on the underwriting standards. This credit risk rating process incorporates objective and subjective criteria to identify inherent strengths and weaknesses and risks in a particular relationship.

This credit risk rating process uses a two-dimensional loan rating structure, incorporating a 14-point risk-rating scale to identify and track the probability of borrower default and a separate 4-point scale addressing loss given default. The 14-point risk rating scale provides for nine "acceptable" categories, one "other assets especially mentioned" category, two "substandard" categories, one "doubtful" category and one "loss" category. The loss given default scale establishes four ranges of anticipated economic loss if the loan defaults. The calculation of economic loss includes principal and interest as well as collections costs, legal fees and staff costs.

By buying and selling loans or interests in loans to or from other institutions within the System or outside the System, we limit our exposure to either a borrower or commodity concentration. This also allows us to manage growth and capital, and to improve geographic diversification.

Portfolio credit risk is also evaluated with the goal of managing the concentration of credit risk. Concentration risk is reviewed and measured by industry, product, geography and customer limits.

Loan Portfolio

The loan portfolio consists only of retail loans. Bank loans to its affiliated associations have been eliminated in the combined financial statements. Gross loan volume of $16.59 billion at December 31, 2008, reflected an increase of $1.5 billion, or 9.8 percent, from the $15.11 billion loan portfolio balance at December 31, 2007. Loans, net of the allowance for loan losses, represented 82.0 percent, 83.8 percent and 80.6 percent of total assets as of December 31, 2008, 2007 and 2006, respectively.

Agricultural real estate mortgage loans totaled $11.02 billion at December 31, 2008, an increase of $865.9 million, or 8.5 percent, from 2007, and currently comprise approximately 66.4 percent of the district's loan portfolio. Commercial loans for agricultural production, processing and marketing totaled $3.66 billion, an increase of $325.7 million, or 9.8 percent, from 2007, and represented 22.1 percent of the loan portfolio at December 31, 2008. All other loans, including energy loans, communications loans, farm-related business loans, rural home loans and loans to OFIs, increased by $284.0 million to $1.91 billion. The composition of the district's loan portfolio by category may be found in Note 4, "Loans and Allowance for Loan Losses." The primary factors contributing to the growth in the district's loan volume included an increased focus on market share and loan growth opportunities within the territory; competitive pricing; increased marketing and customer service efforts by the associations; and growth in loan participations.

The bank and district associations review the credit quality of the loan portfolio as a part of their credit risk practices, using the classifications of the Uniform Classification System which is used by all System institutions. The classifications are defined as follows:

- Acceptable – Assets are expected to be fully collectible and represent the highest quality.
- Other Assets Especially Mentioned (Special Mention) – Assets are currently collectible but exhibit some potential weakness.

- Substandard – Assets exhibit some serious weakness in repayment capacity, equity and/or collateral pledged on the loan.
- Doubtful – Assets exhibit similar weaknesses to substandard assets, but have additional weaknesses in existing facts, conditions and values that make collection in full highly questionable.
- Loss – Assets are considered uncollectible.

The following table discloses the credit quality of the district's loan portfolio at December 31,

	2008	2007	2006
Acceptable	**94.8%**	97.2%	97.1%
Special mention	**2.3**	1.6	1.8
Substandard	**2.9**	1.2	1.1
Total	**100.0%**	100.0%	100.0%

During 2008, overall credit quality remained strong. Loans classified (under the Farm Credit Administration's Uniform Loan Classification System) as "acceptable" or "other assets especially mentioned" as a percentage of total loans and accrued interest receivable were 97.1 percent at December 31, 2008, compared to 98.8 percent at December 31, 2007, and 98.9 percent at December 31, 2006.

High-Risk Assets

Total high-risk assets have increased by $227.9 million, or 182.3 percent, from $125.0 million at December 31, 2007, to $352.9 million at December 31, 2008. The increase is primarily attributable to a $222.3 million increase in nonaccrual loans which includes the addition of $114.5 million in loans to one borrower held by the bank and 13 district associations. This large poultry credit filed for bankruptcy protection on December 1, 2008, and due to the uncertainty on the loans, they were moved to nonaccrual status at the recommendation of the originator. Due to the collateralization on the loans, the district determined that there was no probable loss in the event of default; there was therefore no provision for loan losses made on the loan. Also included in the increase in nonaccrual loans was $24.9 million in loans to two subsidiaries of an ethanol-related borrower which declared bankruptcy. In addition, loans to 174 other borrowers totaling $82.9 million were added to nonaccrual status during 2008. The $4.7 million increase in other property owned was due mainly to increases at two of the district's associations.

The following table discloses the components of the district's high-risk assets at December 31,

(in millions)	**2008**	2007	2006
Nonaccrual loans	**$ 322.4**	$ 100.1	$ 36.2
Formally restructured loans	**6.1**	6.2	7.2
Loans past due 90 days or more and still accruing interest	**17.9**	16.9	0.8
Other property owned, net	**6.5**	1.8	2.0
Total	**$ 352.9**	$ 125.0	$ 46.2

At December 31, 2008, $249.9 million, or 77.5 percent, of loans classified as nonaccrual were current as to principal and interest, compared to $79.5 million, or 79.4 percent, of nonaccrual loans at December 31, 2007, and $24.5 million, or 67.8 percent, at December 31, 2006.

Figures 2, 3 and 4 provide analyses of the relationships of nonaccrual loans and high-risk assets to total loans and members' equity at December 31, 2008, 2007 and 2006. Volatility in the agricultural commodity market and increases in farm input costs have resulted in higher risk profiles for livestock, grain producers, and borrowers who use corn and other grains in their products. Due to these higher risk profiles and the impact of volatility in the general economic environment the bank anticipates credit quality of the loan portfolio may continue to decline in 2009.

Allowance and Provision for Loan Losses

At December 31, 2008, the allowance for loan losses was $51.7 million, or 0.31 percent of total loans outstanding, compared to $24.5 million (0.16 percent) and $14.0 million (0.11 percent) at December 31, 2007 and 2006, respectively. Net charge-offs of $26.2 million, $32.6 million and $4.9 million were recorded in 2008, 2007 and 2006, respectively. The district's net provision for loan losses of $53.5 million for 2008 reflected an increase of $10.4 million, or 24.1 percent, from the $43.1 million provision recorded for 2007, due primarily to provision related to the loans described in the "Provision for Loan Losses" section of this discussion. The allowance for loan losses for the district represents the aggregate of each entity's individual evaluation of its allowance for loan losses requirements. Although aggregated in the combined financial statements, the allowance for loan losses of each entity is particular to that institution and is not available to absorb losses realized by other institutions. The allowance for loan losses at each period end

Figure 2

Nonaccrual Loans
as a Percentage of Total Loans at Year End

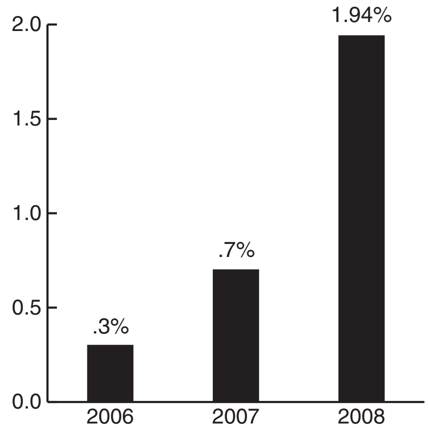


Figure 3

High-Risk Assets
as a Percentage of Total Members' Equity at Year End

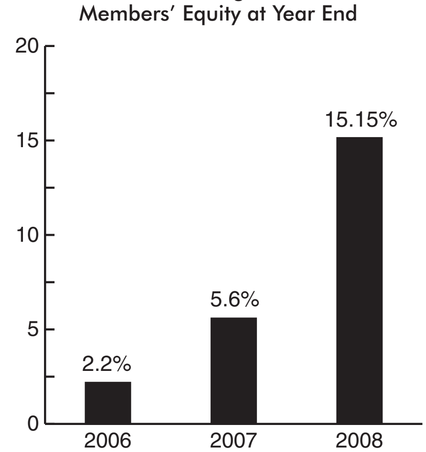


Figure 4

High-Risk Assets
as a Percentage of Total Loans and Other Property Owned at Year End

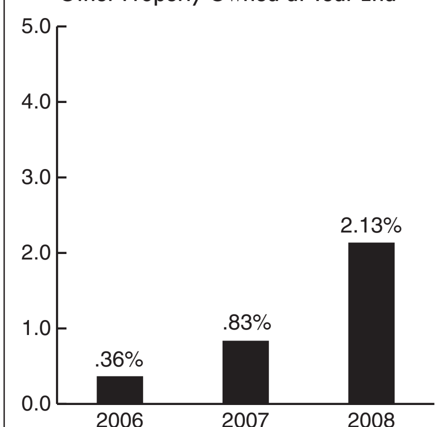


Figure 5

Interest Rate Gap Analysis
as of December 31, 2008

	Interest-Sensitive Period: One Month or Less	Over One Through Six Months	Over Six Through Twelve Months	**Total Twelve Months or Less**	Over One Year but Less Than Five Years	Over Five Years and Non-Rate Sensitive	**Total**
Earning Assets							
Total loans	$ 6,848,453	$ 2,182,309	$ 1,413,622	**$ 10,444,384**	$ 4,797,846	$ 1,347,841	**$ 16,590,071**
Total investments	1,097,304	610,373	500,903	**2,208,580**	957,512	57,003	**3,223,095**
Total earning assets	7,945,757	2,792,682	1,914,525	**12,652,964**	5,755,358	1,404,844	**19,813,166**
Interest-Bearing Liabilities							
Total interest-bearing funds*	7,210,146	3,967,000	2,520,000	**13,697,146**	2,906,000	755,500	**17,358,646**
Excess of earning assets over interest-bearing liabilities	—	—	—	**—**	—	2,454,520	**2,454,520**
Total interest-bearing liabilities	7,210,146	3,967,000	2,520,000	**13,697,146**	2,906,000	3,210,020	**$ 19,813,166**
Interest rate sensitivity gap	$ 735,611	$ (1,174,318)	$ (605,475)	**$ (1,044,182)**	$ 2,849,358	$ (1,805,176)	
Cumulative interest rate sensitivity gap	$ 735,611	$ (438,707)	$ (1,044,182)	**$ (1,044,182)**	$ 1,805,176		

*The impact of interest rate swaps is included with interest-bearing funds.

was considered by management to be adequate to absorb probable losses existing in and inherent to its loan portfolio. Management's evaluations consider factors including loan loss experience, portfolio quality, loan portfolio composition, current agricultural production conditions and economic conditions.

The following table provides an analysis of key statistics related to the allowance for loan losses at December 31:

	2008	2007	2006
Allowance for loan losses as a percentage of:			
Average loans	**0.3%**	0.2%	0.1%
Loans at year end			
Total loans	**0.3**	0.2	0.1
Nonaccrual loans	**16.0**	24.5	38.6
Total impaired loans	**14.9**	19.9	31.6
Net charge-offs to average loans	**0.2**	0.2	<0.1
Provision expense to average loans	**0.3**	0.3	0.1

Interest Rate Risk Management

Asset/liability management is the bank's process for directing and controlling the composition, level and flow of funds related to the district's interest-rate-sensitive assets and liabilities. Management's objective is to generate adequate and stable net interest income in a changing interest rate environment.

The bank uses a variety of techniques to manage the district's financial exposure to changes in market interest rates. These include monitoring the difference in the maturities or repricing cycles of interest-rate-sensitive assets and liabilities; monitoring the change in the market value of interest-rate-sensitive assets and liabilities under various interest rate scenarios; and simulating changes in net interest income under various interest rate scenarios.

The interest rate risk inherent in a district association's loan portfolio is substantially mitigated through its funding relationship with the bank. The bank manages interest rate risk through its direct loan pricing and asset/liability management process. Under the Farm Credit Act of 1971, as amended, a district association is obligated to borrow only from the bank unless the bank approves borrowing from other funding sources. An association's indebtedness to the bank, under a general financing agreement between the bank and the association, represents demand borrowings by the association to fund the majority of its loan advances to association members.

The district's net interest income is determined by the difference between income earned on loans and investments and the interest expense paid on funding sources, typically Systemwide bonds, medium-term notes, discount notes and subordinated debt. The district's level of net interest income is affected by both changes in market interest rates and timing differences in the maturities or repricing cycles of interest-rate-sensitive assets and liabilities. Depending upon the direction and magnitude of changes in market interest rates, the district's net interest income may be affected either positively or negatively by the mismatch in the maturity or the repricing cycle of interest-rate-sensitive assets and liabilities.

The rate sensitivity gap analysis in Figure 5 sets forth a static measurement of the district's volume of interest-rate-sensitive assets and liabilities outstanding as of December 31, 2008, which are projected to mature or reprice in each of the future time periods shown. The "interest rate sensitivity gap" line reflects the mismatch, or gap, in the maturity or repricing of interest-rate-sensitive assets and liabilities. A gap position can be either positive or negative. A positive gap indicates that a greater volume of assets than liabilities reprices or matures in a given time period, and conversely, a negative gap indicates that a greater volume of liabilities than assets reprices or matures in a given time period. On a 12-month cumulative basis, the district has a negative gap position, indicating that the district has an exposure to rising interest rates. This occurs when interest expense on interest-bearing liabilities increases, due to their maturing or repricing cycle, sooner than maturing or repricing assets.

To more appropriately reflect the cash flow and repricing characteristics of the district's balance sheet, an estimate of expected prepayments on loans is reflected in the maturities of the loans in the earning assets section of Figure 5. Changes in market interest rates will affect the volume of prepayments on loans. Correspondingly,

Figure 6

Activity in Derivative Financial Instruments
(Notional Amounts)

(in millions)	
Balance, December 31, 2007	$ 925
Additions	200
Terminations	(325)
Balance, December 31, 2008	**$ 800**

adjustments have been made to reflect the characteristics of callable debt instruments and the effect derivative financial instruments have on the repricing structure of the district's balance sheet.

The bank uses derivative financial instruments to manage the district's interest rate risk and liquidity position. Interest rate swaps for asset/liability management purposes are used to change the repricing characteristics of liabilities to match the repricing characteristics of the assets they support. The bank does not hold, and is restricted by policy from holding, derivative financial instruments for trading purposes and is not a party to leveraged derivative transactions.

At December 31, 2008, the bank had four fair value interest rate swap contracts with a total notional amount of $350 million. The fair value swap contracts had a net fair value of $31.4 million, which is reflected in other assets. In addition, the bank had four cash flow interest rate swaps with a total notional amount of $450 million; these cash flow hedges had a net liability fair value of $3.1 million at December 31, 2008. To the extent that its derivatives have a negative fair value, the bank has a payable on the instrument and the counterparty is exposed to the credit risk of the bank. To the extent that its derivatives have a positive fair value, the bank has a receivable on the instrument and is therefore exposed to credit risk from the counterparty. To manage this credit risk, the bank has bilateral collateral agreements to reduce potential exposure, diversifies counterparties in the swap transactions and monitors the credit ratings of all counterparties with whom it transacts. Figure 6 summarizes the bank's activity in derivative financial instruments for 2008.

Interest rate risk exposure is measured by simulation modeling, which calculates the district's expected net interest income based upon projections of interest-rate-sensitive assets and liabilities, derivative financial instruments and interest rate scenarios. The bank monitors the district's financial exposure to instantaneous and parallel changes in interest rates of 200 basis points up or down over a rolling 12-month period. As of December 31, 2008, projected district net interest income would increase by $9.5 million, or 1.9 percent, if interest rates were to increase by 200 basis points, and would increase by $809, or 0.16 percent, if interest rates were to decrease by 6 basis points. In general, the bank's ability to exercise call options on debt benefit the district in the event of decreasing interest rates. In a rising interest rate scenario, the benefit of rate increases on investments, association loans and the bank's participation loans would outpace the increase in the cost of debt.

Liquidity Risk Management

The district's liquidity risk management practices ensure the district's ability to meet its financial obligations. These obligations include the repayment of Systemwide debt securities as they mature, the ability to fund new and existing loan and other funding commitments, and the ability to fund operations in a cost-effective manner. A primary objective of liquidity risk management is to plan for unanticipated changes in the capital markets.

Funding Sources

Our primary source of liquidity is the ability to issue Systemwide debt securities, which are the general unsecured joint and several obligations of the System banks. We continually raise funds to support our mission to provide credit and related services to the rural and agricultural sectors, repay maturing Systemwide debt securities, and meet other obligations. As a government-sponsored enterprise, we have had access to the nation's and world's capital markets. This access has provided us with a dependable source of competitively priced debt that is critical to support our mission of providing funding to the rural and agricultural sectors. Moody's Investors Service and Standard & Poor's rate the System's long-term debt as Aaa and AAA, and our short-term debt as P-1 and A-1+. These rating agencies base their ratings on many quantitative and qualitative factors, including the System's government-sponsored enterprise status. Material changes to the factors considered could result in a different debt rating. However, as a result of the System's financial performance, credit quality and standing in the capital markets, we anticipate continued access to funding necessary to support System needs. The U.S. government does not guarantee, directly or indirectly, Systemwide debt securities.

In September 2008, the bank issued $50.0 million in subordinated debt in a private placement to one investor. The debt is a 10-year instrument with a coupon rate of 8.406 percent. The bank confirmed its determination that the subordinated debt will receive preferential regulatory ratio treatment, being includible in permanent capital and total surplus and being excludible from total liabilities for purposes of net collateral ratio calculation. These preferential treatments will be ratably removed 20 percent per year during years six to 10 of the debt's term.

During 2008, the bank received ratings from two rating agencies. In August 2008, Moody's Investors Service upgraded the bank's issuer rating to Aa2 from the Aa3 rating it had issued in July 2008. In addition, the bank's A2 preferred stock rating was affirmed and the bank received an A1 subordinated debt rating. In June 2008, Fitch Ratings, Ltd. issued an AA-long-term issuer default rating with a stable rating outlook and assigned an A rating to the bank's preferred stock.

The following table provides a summary of the period-end balances of the debt obligations of the district *(dollars in millions)*:

	December 31,		
	2008	2007	2006
Bonds and term notes outstanding	**$ 11,335**	$ 11,464	$ 11,354
Average effective interest rate	**3.89%**	4.98%	5.04%
Average life (years)	**3.4**	3.2	2.7
Subordinated debt outstanding	**$ 50**	$ —	$ —
Average effective interest rate	**8.50%**	—	—
Average life (years)	**9.8**	—	—
Discount notes outstanding	**$ 2,467**	$ 1,160	$ 767
Average effective interest rate	**1.37%**	4.10%	5.23%
Average life (days)	**107**	39	29
Notes payable to other System banks	**$ 3,500**	$ 2,700	$ 1,400
Average effective interest rate	**3.25%**	5.74%	5.84%
Average life (years)	**1.0 or less**	1.0 or less	1.0 or less

The following table provides a summary of the average balances of the debt obligations of the district *(dollars in millions)*:

	For the years ended December 31,		
	2008	2007	2006
Average interest-bearing liabilities outstanding	**$ 16,393**	$ 14,337	$12,132
Average interest rates on interest-bearing liabilities	**3.95%**	5.25%	4.95%

Liquidity Standard

The System banks have jointly developed and adopted a common minimum liquidity standard (standard). This standard is designed to maintain and assure adequate liquidity to meet the business and financial needs of each bank and the System. The standard requires each bank to maintain a minimum of 90 days of liquidity on a continuous basis, assuming no access to the capital markets. The number of days of liquidity is calculated by comparing maturing Systemwide debt securities and other bonds with the total amount of cash, investments and other liquid assets maintained by that bank. For purposes of calculating liquidity, liquid assets are subject to discounts that reflect potential exposure to adverse market value changes that might be recognized upon liquidation or sale. At December 31, 2008, the bank had 134 days of liquidity coverage, as compared with 121 days at December 31, 2007.

The bank maintains a $150.0 million commercial bank commited line of credit to support possible general short-term credit needs.

Investments

As permitted under FCA regulations, a bank is authorized to hold eligible investments (including federal funds) for the purposes of maintaining a diverse source of liquidity, profitably managing short-term surplus funds, and managing interest rate risk. During 2005, the Farm Credit Administration (FCA) approved a rule that increased the amount of eligible investments a bank is authorized to hold to an amount not to exceed 35 percent of loans outstanding from the previous percentage of 30 percent. Farm Credit Administration regulations also permit an association to hold eligible investments with the approval of its affiliated bank.

Farm Credit Administration regulations also define eligible investments by specifying credit rating criteria, final maturity limit and percentage of investment portfolio limit for each investment type. Generally, the banks' investments must be highly rated by a Nationally Recognized Statistical Rating Organization, such as Moody's Investors (Moody's) Service or Standard & Poor's. A bank must develop and submit to the FCA a divestiture plan that includes disposal of an asset that becomes ineligible.

The following table discloses the district's holdings in federal funds and investment securities at December 31,

	2008	2007	2006
Federal agency mortgage-backed securities	**$ 1,681,033**	$ 1,801,734	$ 1,921,980
Other mortgage-backed securities	**192,581**	—	—
Agency debt	**500,957**	—	—
Corporate debt	**382,061**	178,840	234,878
Money market instruments	**154,255**	219,475	131,349
Asset-backed securities	**84,970**	210,950	384,035
Federal funds	**176,698**	125,502	89,229
Total available-for-sale investments	**$ 3,172,555**	$ 2,536,501	$ 2,761,471
Mission-related investments	**50,540**	—	—
Total	**$ 3,223,095**	$ 2,536,501	$ 2,761,471

At December 31, 2008, the available-for-sale investment portfolio included guaranteed Small Business Administration pooled securities totaling $17.9 million held by a district association. The district's available-for-sale portfolio is reflected at fair value. The mission-related investments are held-to-maturity and are reflected at amortized cost.

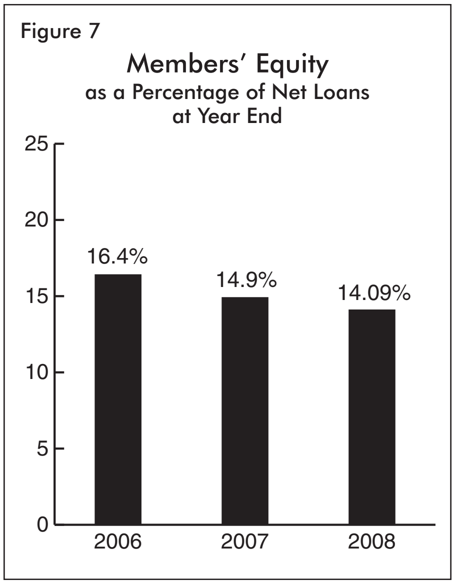
At December 31, 2008, the bank had two investments which were ineligible for liquidity purposes as a result of credit downgradings. One asset-backed investment in sub-prime mortgages had credit ratings at December 31, 2008, of Baa1 and BB by Moody's and Standard and Poor's, respectively. This investment had an amortized cost of $4.1 million and a fair value of $2.2 million, with an unrealized loss of $1.9 million at December 31, 2008. In May 2008, the FCA approved the bank's plan of divestiture for this downgraded investment, which indicated the bank's desire to continue to hold the investment. In addition, one of the bank's whole-loan mortgage-backed investments was downgraded to Baa1 and B by Moody's and Standard and Poor's in December 2008, respectively. Using more detailed cash flow analysis, the bank determined that the investment's impairment was other than temporary, and as a result, the investment's amortized cost of $14.9 million was written down to its fair value of $12.7 million, resulting in a realized loss of $2.2 million for 2008. The downgrading of the whole-loan mortgage-backed security will require a submission of a plan of divestiture to the FCA and their formal approval. The plan of divestiture was submitted on February 10, 2009. While these investments do not meet the FCA's standards for liquidity, they are included in the net collateral calculation, albeit at their lower market value rather than the normal book value for qualifying investments. Due to the continued deterioration in the mortgage markets, the bank may have additional other-than-temporary impairments on non-guaranteed mortgage and asset-backed securities.

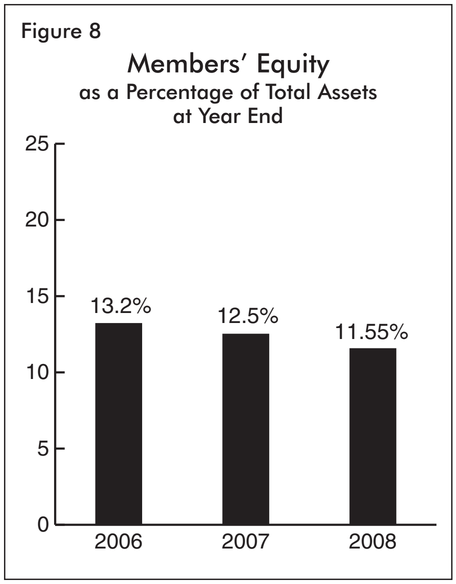
The bank's liquidity investment portfolio included $59.3 million of money market holdings in The Reserve U.S. Government Fund (Government Fund). This fund was composed of short-term senior debt securities issued by Federal National Mortgage Association (Fannie Mae), Federal Home Loan Mortgage Association (Freddie Mac), Federal Home Loan Bank and Farm Credit System. Effective September 18, 2008, the Securities and Exchange Commission (SEC) issued an order, at the request of The Reserve, to suspend all rights of redemption on its Government Fund and other funds. The Reserve was experiencing heavy redemption requests on its funds. The SEC's goal was to ensure an orderly disposition of the securities in the Government Fund to maintain the integrity of the fund's Net Asset Value (NAV) of $1.00 per share. Subsequent to year end, on January 16, 2009, the bank received the remainder of its principal balance, along with accrued interest on the investment security.

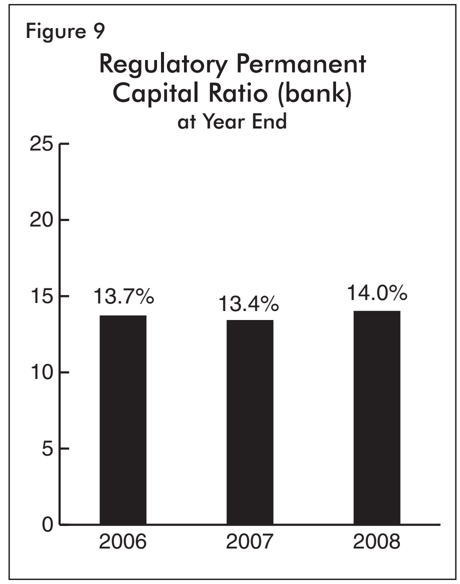
The composition and characteristics of the district's investment securities are described in Note 3, "Investment Securities."

Capital Adequacy

In November 2003, the bank issued 100,000 shares of $1,000 Cumulative Perpetual Preferred Stock for net proceeds of $98.6 million. The preferred stock is treated as equity and is not mandatorily redeemable. The preferred stock was issued for general corporate purposes. In September 2005, an additional 100,000 shares of $1,000 Cumulative Perpetual Preferred Stock was issued for net proceeds of $108.9 million, which included $2.1 million in accrued dividends payable. Net proceeds from the additional issue were used to enhance the composition of the bank's capital and liquidity position; to







support the bank's loan growth; to provide a base for further growth and service opportunities to our members and to rural America; and for general corporate purposes.

Borrower equity purchases required by association capitalization bylaws (see Note 8, "Members' Equity"), combined with a history of growth in retained earnings at district institutions, have resulted in district institutions being able to maintain strong capital positions. The $2.33 billion capital position of the district at December 31, 2008, reflects an increase of 3.6 percent over the December 31, 2007, capital position of $2.25 billion. This increase is attributable to the $267.7 million of net income earned in 2008; issuances of capital stock, participation certificates and allocated retained earnings of $13.6 million; offset by an increase in net unrealized losses on investments of $16.0 million; a decrease of net unrealized gains in cash flow derivatives of $4.1 million; dividend and patronage distributions of $86.5 million; an adjustment to accumulated other comprehensive income of $78.2 million resulting from the application of Statement of Financial Accounting Standards No. 158, "Employers' Accounting for Defined Benefit Pension and Other Postretirement Plans" (SFAS 158); and retirements of capital stock, participation certificates and allocated retained earnings of $14.8 million.

The return on average members' equity for the year ended December 31, 2008, was 11.4 percent, compared to 10.9 percent and 11.7 percent reported for the years ended December 31, 2007 and 2006, respectively.

The district recorded a $2.7 million charge to retained earnings pursuant to a change in the measurement date used for the valuation of pension and other postretirement benefit obligations from September 30 to December 31 in 2008.

FCA regulations require System institutions to compute a total surplus ratio, a core surplus ratio and a net collateral ratio (bank only), and maintain at least the minimum standard for each ratio. In those instances where an entity may not be in compliance, the regulations require the entity to submit a corrective plan to the FCA designed to move the institution into compliance. As of December 31, 2008, the bank and all district associations were in compliance with the regulations. Note 8, "Members' Equity," outlines the ranges of capital ratios for the bank and district associations. The bank's permanent capital ratio of 14.03 percent at December 31, 2008, is considered adequate, in accordance with the capital plan adopted by the bank's board of directors. An analysis of the trend in the district's capital ratios is presented in Figures 7, 8 and 9.

Operational Risk Management

Operational risk is the risk of loss resulting from inadequate or failed processes or systems, human factors or external events, including the execution of unauthorized transactions by employees, errors relating to transaction processing and technology, breaches of the internal control system, and the risk of fraud by employees or persons outside the System. The board of directors is required, by regulation, to adopt an internal control policy that provides adequate direction to the institution in establishing effective control over and accountability for operations, programs and resources. The policy must include, at a minimum, the following items:

- direction to management that assigns responsibility for the internal control function to an officer of the institution;
- adoption of internal audit and control procedures;
- direction for the operation of a program to review and assess its assets;
- adoption of loan, loan-related assets and appraisal review standards, including standards for scope of review selection and standards for work papers and supporting documentation;
- adoption of asset quality classification standards;
- adoption of standards for assessing credit administration, including the appraisal of collateral; and
- adoption of standards for the training required to initiate a program.

In general, we address operational risk through the organization's internal framework under the supervision of the internal auditors. Exposure to operational risk is typically identified with the assistance of senior management, and internal audit plans are developed with higher risk areas receiving more review.

Political Risk Management

We, as part of the System, are an instrumentality of the federal government and are intended to further governmental policy concerning the extension of credit to or for the benefit of agricultural and rural America. The System and its borrowers may be significantly affected by federal legislation that affects the System directly, such as changes to the Farm Credit Act, or indirectly, such as agricultural appropriations bills. Political risk to the System is the risk of loss of support for the System or agriculture by the U.S. government.

We manage political risk by actively supporting The Farm Credit Council (council), which is a full-service, federal trade association representing the System before Congress, the executive branch and others. The council provides the mechanism for "grassroots" involvement in the development of System positions and policies with respect to federal legislation and government actions that impact the System. Additionally, we take an active role in representing the individual interests of System institutions and their borrowers before Congress. In addition to The Farm Credit Council, each district has its own council, which is a member of The Farm Credit Council. The district councils represent the interests of their members on a local and state level, as well as on a federal level.

Recent Accounting Pronouncements

In March 2008, the Financial Accounting Standards Board (FASB) issued Statement of Financial Accounting Standards (SFAS) No. 161, "Disclosures About Derivative Instruments and Hedging Activities," which amends and expands the disclosure requirements for derivative instruments and for hedging activities previously required by SFAS No. 133. It states that an entity with derivative instruments shall disclose information to enable users of the financial statements to understand: (a) how and why an entity uses derivative instruments, (b) how derivative instruments and related hedged items are accounted for under this Statement and related interpretations, and (c) how derivative instruments and related hedged items affect an entity's financial position, financial performance, and cash flows. This Statement is effective for financial statements issued for fiscal years and interim periods beginning after November 15, 2008, with early application encouraged. This Statement encourages, but does not require, comparative disclosures for earlier periods at initial adoption. The bank is currently evaluating the impact of adoption on its financial statement disclosures.

Association Structural Changes

As of December 31, 2008, there were 13 ACAs and six FLCAs, totaling 19 associations within the district. During 2008, two of the district's ACAs merged. In January, 2009, one FLCA restructured to form an ACA structure with operating FLCA and Production Credit Association subsidiaries. As of December 31, 2007 and 2006, there were 14 ACAs and six FLCAs, totaling 20 associations within the district.

Regulatory Matters

During the year ended December 31, 2008, the Farm Credit Administration took no enforcement actions against the bank or its related associations, and there were no enforcement actions in effect for the bank or its related associations at December 31, 2008.

On October 31, 2007, the Farm Credit Administration published an advanced notice of public rule-making in the Federal Register with respect to the consideration of possible modifications to the Farm Credit Administration's risk-based capital rules for Farm Credit System institutions that are similar to the standardized approach delineated in the Basel II Framework. The Farm Credit Administration is seeking comments to facilitate the development of a proposed rule that would enhance their regulatory capital framework and more closely align minimum capital requirements with risks taken by System institutions. Comments on the advanced notice of public rule-making were originally due by March 31, 2008; the comment period was extended to December 31, 2008. The System is in the process of developing a comment letter to provide to the Farm Credit Administration on the advanced notice of public rule-making.

Other

On September 30, 2008, the bank, in concert with the four other System banks, purchased senior cumulative perpetual preferred stock of the Federal Agricultural Mortgage Corporation (Farmer Mac). The bank's investment is $7.0 million of the $60.0 million total invested by System banks. The investment enabled Farmer Mac to strengthen its capital position and comply with its minimum regulatory capital requirements. The investment is not considered part of the bank's liquidity investment portfolio and is included in other assets at cost.

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Report of Independent Auditors

To the Board of Directors and Shareholders
of the Farm Credit Bank of Texas and the Tenth District Associations:

In our opinion, the accompanying combined balance sheets and the related combined statements of income, of changes in shareholders' equity and of cash flows present fairly, in all material respects, the financial position of the Farm Credit Bank of Texas and Tenth District Associations (district) at December 31, 2008, 2007 and 2006, and the results of their operations and their cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America. These financial statements are the responsibility of the district's management. Our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audits of these statements in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

PricewaterhouseCoopers LLP

February 27, 2009

COMBINED
FINANCIAL STATEMENTS

Combined Balance Sheets

FARM CREDIT BANK OF TEXAS AND DISTRICT ASSOCIATIONS

	December 31,		
(dollars in thousands)	**2008**	2007	2006
Assets			
Cash	**$ 56,882**	$ 55,703	$ 60,170
Federal funds sold and securities purchased under resale agreements	**176,698**	125,502	89,229
Investment securities	**3,046,397**	2,410,999	2,672,242
Loans	**16,590,071**	15,114,537	12,905,321
Less allowance for loan losses	**51,653**	24,495	13,969
Net loans	**16,538,418**	15,090,042	12,891,352
Accrued interest receivable	**202,807**	228,212	204,603
Other property owned, net	**6,495**	1,817	2,020
Premises and equipment, net	**49,499**	42,599	40,635
Other assets	**89,116**	41,623	26,816
Total assets	**$ 20,166,312**	$ 17,996,497	$ 15,987,067
Liabilities and members' equity			
Liabilities			
Bonds and notes, net	**$ 17,302,205**	$ 15,324,015	$ 13,520,784
Subordinated debt	**50,000**	—	—
Accrued interest payable	**103,288**	122,459	102,585
Patronage distributions payable	**55,024**	63,899	60,073
Other liabilities	**326,078**	235,463	190,965
Total liabilities	**17,836,595**	15,745,836	13,874,407
Commitments and contingencies (Note 12)			
Members' equity			
Preferred stock	**202,754**	202,754	203,565
Common stock and participation certificates	**63,859**	62,489	59,068
Allocated retained earnings	**211,450**	133,423	83,705
Unallocated retained earnings	**1,984,421**	1,886,488	1,792,723
Accumulated other comprehensive loss	**(132,767)**	(34,493)	(26,401)
Total members' equity	**2,329,717**	2,250,661	2,112,660
Total liabilities and members' equity	**$ 20,166,312**	$ 17,996,497	$ 15,987,067

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

Combined Statements of Income

FARM CREDIT BANK OF TEXAS AND DISTRICT ASSOCIATIONS

	Year Ended December 31,		
(dollars in thousands)	**2008**	2007	2006
Investment securities and other	**$ 111,358**	$ 131,768	$ 141,260
Loans	**1,006,081**	1,053,629	845,135
Total interest income	**1,117,439**	1,185,397	986,395
Bonds, notes and subordinated debt	**541,316**	653,972	562,211
Notes payable and other	**105,695**	99,044	37,938
Total interest expense	**647,011**	753,016	600,149
Net interest income	**470,428**	432,381	386,246
Provision for loan losses	**53,514**	43,131	9,356
Net interest income after provision for loan losses	**416,914**	389,250	376,890
Patronage income	**17,420**	7,003	1,237
Fees for loan-related services	**16,933**	14,429	15,255
Net gain on investment securities	**318**	503	907
Miscellaneous income, net	**1,575**	4,460	3,923
Total noninterest income	**36,246**	24,820	21,322
Salaries and employee benefits	**94,043**	88,489	84,936
Occupancy and equipment expense	**13,105**	12,394	11,422
Insurance Fund premiums	**24,248**	21,092	16,328
Losses on other property owned, net	**374**	31	93
Other operating expenses	**53,318**	49,383	45,543
Total noninterest expense	**185,088**	171,389	158,322
Income before income taxes	**268,072**	242,681	239,890
Provision for (benefit from) income taxes	**344**	141	(228)
Net income	**$ 267,728**	$ 242,540	$ 240,118

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

Combined Statements of Changes in Members' Equity

FARM CREDIT BANK OF TEXAS AND DISTRICT ASSOCIATIONS

(dollars in thousands)	Preferred Stock	Common Stock and Participation Certificates	Retained Earnings Allocated	Retained Earnings Unallocated	Retained Earnings Total	Accumulated Other Comprehensive Income (Loss)	Total Members' Equity
Balance at December 31, 2005	$ 203,569	$ 73,642	$ 32,327	$ 1,692,534	$ 1,724,861	$ (46,977)	$ 1,955,095
Comprehensive income							
Net income	—	—	—	240,118	240,118	—	240,118
Net change in unrealized losses on investment securities	—	—	—	—	—	5,707	5,707
Net change in unrealized gains on cash flow hedge derivatives	—	—	—	—	—	(1,047)	(1,047)
Minimum pension liability adjustment	—	—	—	—	—	15,916	15,916
Total comprehensive income	—	—	—	240,118	240,118	20,576	260,694
Capital stock/participation certificates issued	—	22,878	—	—	—	—	22,878
Capital stock/participation certificates and allocated retained earnings retired	(4)	(37,452)	(2,950)	—	(2,950)	—	(40,406)
Cash dividends on preferred stock	—	—	—	(15,122)	(15,122)	—	(15,122)
Patronage distributions							
Cash	—	—	—	(70,479)	(70,479)	—	(70,479)
Members' equity	—	—	54,328	(54,328)	—	—	—
Balance at December 31, 2006	203,565	59,068	83,705	1,792,723	1,876,428	(26,401)	2,112,660
Comprehensive income							
Net income	—	—	—	242,540	242,540	—	242,540
Net change in unrealized net losses on investment securities	—	—	—	—	—	16,513	16,513
Net change in unrealized gains on cash flow hedge derivatives	—	—	—	—	—	1,047	1,047
Minimum pension liability adjustment	—	—	—	—	—	4,931	4,931
Total comprehensive income	—	—	—	242,540	242,540	22,491	265,031
Adjustment to initially apply SFAS 158	—	—	—	—	—	(30,583)	(30,583)
Capital stock/participation certificates issued	—	12,926	—	—	—	—	12,926
Capital stock/participation certificates and allocated retained earnings retired	(811)	(9,505)	(7,682)	—	(7,682)	—	(17,998)
Cash dividends on preferred stock	—	—	—	(15,122)	(15,122)	—	(15,122)
Patronage distributions							
Cash	—	—	—	(76,253)	(76,253)	—	(76,253)
Members' equity	—	—	57,400	(57,400)	—	—	—
Balance at December 31, 2007	202,754	62,489	133,423	1,886,488	2,019,911	(34,493)	2,250,661
Adjustment for accounting changes:							
Change in measurement date – SFAS No. 158	—	—	—	(2,713)	(2,713)	—	(2,713)
Balance at January 1, 2008	202,754	62,489	133,423	1,883,775	2,017,198	(34,493)	2,247,948
Comprehensive income							
Net income	—	—	—	267,728	267,728	—	267,728
Change in pension and postretirement benefit plans	—	—	—	—	—	(78,201)	(78,201)
Net change in unrealized net losses on investment securities	—	—	—	—	—	(15,952)	(15,952)
Net change in unrealized gains on cash flow hedge derivatives	—	—	—	—	—	(4,121)	(4,121)
Total comprehensive income	—	—	—	267,728	267,728	(98,274)	169,454
Capital stock/participation certificates issued	—	13,594	—	—	—	—	13,594
Capital stock/participation certificates and allocated retained earnings retired	—	(12,224)	(2,531)	—	(2,531)	—	(14,755)
Cash dividends on preferred stock	—	—	—	(15,122)	(15,122)	—	(15,122)
Patronage distributions							
Cash	—	—	—	(71,402)	(71,402)	—	(71,402)
Members' equity	—	—	80,558	(80,558)	—	—	—
Balance at December 31, 2008	**$ 202,754**	**$ 63,859**	**$ 211,450**	**$1,984,421**	**$2,195,871**	**$(132,767)**	**$ 2,329,717**

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

Combined Statements of Cash Flows

FARM CREDIT BANK OF TEXAS AND DISTRICT ASSOCIATIONS

	Year Ended December 31,		
(dollars in thousands)	**2008**	2007	2006
Operating Activities			
Net income	**$ 267,728**	$ 242,540	$ 240,118
Reconciliation of net income to net cash provided by operating activities			
Provision for loan losses	**53,514**	43,131	9,356
Provision for losses on other property owned	**458**	133	249
Depreciation and amortization on premises and equipment	**5,715**	5,375	5,029
Accretion of net discount on loans	**(1,263)**	(1,876)	(344)
Amortization and accretion on debt instruments	**(2,240)**	(1,759)	(660)
Accretion of net (discount) premium on investments	**(1,405)**	(3,004)	3,626
Gain on sale of investment securities	**(2,556)**	(503)	(907)
Loss on impairment of available-for-sale investment	**2,238**	—	—
(Gain) loss on sales of other property owned, net	**(297)**	34	256
Gain on sales of premises and equipment	**(2,932)**	(1,978)	(6,422)
Decrease (increase) in accrued interest receivable	**25,405**	(23,609)	(57,834)
Increase in other assets, net	**(9,077)**	(7,643)	(2,407)
(Decrease) increase in accrued interest payable	**(19,171)**	19,874	40,867
Increase in other liabilities, net	**8,819**	13,716	16,836
Net cash provided by operating activities	**324,936**	284,431	247,763
Investing Activities			
Net increase in federal funds sold and securities purchased under resale agreements	**(51,196)**	(36,273)	(46,785)
Investment securities available for sale:			
Purchases	**(4,338,753)**	(3,971,804)	(6,666,471)
Proceeds from maturities, calls and prepayments	**3,572,339**	4,159,943	6,587,280
Proceeds from sales	**116,785**	93,123	107,814
Investment in Farmer Mac preferred stock	**(7,000)**	—	—
Allocated equity patronage from System bank	**(6,468)**	(1,972)	(2,361)
Increase in loans, net	**(1,514,401)**	(2,244,329)	(2,693,630)
Proceeds from sale of loans	**800,000**	1,300,000	1,000,000
Proceeds from sales of other property owned, net	**8,935**	4,420	4,706
Proceeds from sales of premises and equipment	**2,872**	4,255	4,033
Expenditures for premises and equipment	**(12,555)**	(9,616)	(5,293)
Net cash used in investing activities	**(1,429,442)**	(702,253)	(1,710,707)
Financing Activities			
Bonds and notes issued	**57,398,132**	31,248,805	28,809,507
Subordinated debt issued, net of costs	**49,458**	—	—
Bonds and notes retired	**(56,243,332)**	(30,751,324)	(27,261,180)
(Decrease) increase in advanced conditional payments	**(2,014)**	8,495	8,440
Capital stock and participation certificates issued	**13,594**	12,926	22,878
Capital stock and participation certificates retired and allocated retained earnings distributed	**(14,755)**	(17,998)	(40,406)
Cash dividends on preferred stock	**(15,122)**	(15,122)	(15,122)
Cash dividends and patronage distributions paid	**(80,276)**	(72,427)	(52,850)
Net cash provided by financing activities	**1,105,685**	413,355	1,471,267
Net increase (decrease) in cash	**1,179**	(4,467)	8,323
Cash at beginning of year	**55,703**	60,170	51,847
Cash at end of year	**$ 56,882**	$ 55,703	$ 60,170
Supplemental Schedule of Noncash Investing and Financing Activities			
Financed sales of other property owned	**$ —**	$ 4,079	$ 2,575
Loans transferred to other property owned	**13,560**	4,043	4,464
Net (increase) decrease in unrealized losses on investment securities	**(15,952)**	21,444	5,708
Patronage distributions payable	**55,024**	63,899	60,073
Supplemental Schedule of Noncash Changes in Fair Value Related to Hedging Activities			
Increase in bonds and notes	**$ 25,630**	$ 7,510	$ 9,837
Supplemental Information			
Cash paid during the year for:			
Interest	**$ 666,182**	$ 733,142	$ 559,282
Income taxes	**826**	315	203

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

Notes to Combined Financial Statements

Farm Credit Bank of Texas and District Associations

(dollars in thousands, except per share amounts and as noted)

Note 1 — Organization and Operations

A. Organization:

The Farm Credit Bank of Texas (bank) is one of the banks of the Farm Credit System (System), a nationwide system of cooperatively owned banks and associations established by acts of Congress. The System is currently subject to the provisions of the Farm Credit Act of 1971, as amended (Farm Credit Act). The System specializes in providing financing and related services to qualified borrowers for agricultural and rural purposes.

The United States is served by four Farm Credit Banks (FCBs), each of which has specific lending authority within its chartered territory, and one Agricultural Credit Bank (ACB), (collectively, the "System banks") which has nationwide lending authority for lending to cooperatives. The ACB also has lending authorities of an FCB within its chartered territories. The bank is chartered to service the states of Alabama, Louisiana, Mississippi, New Mexico and Texas.

Each FCB and the ACB serve one or more Agricultural Credit Associations (ACAs) and/or Federal Land Credit Associations (FLCAs). The bank and its related associations collectively are referred to as the Tenth Farm Credit District (district). The district's six FLCAs, 13 ACA parent associations, each containing two wholly-owned subsidiaries (an FLCA and a Production Credit Association [PCA]), certain Other Financing Institutions (OFIs) and preferred stockholders jointly owned the bank at December 31, 2008. FLCAs and ACAs collectively are referred to as associations.

Each FCB and the ACB provides funding for its district associations and is responsible for supervising certain activities of the associations within their districts. The FCBs and/or associations make loans to or for the benefit of eligible borrower-stockholders for qualified agricultural purposes. District associations borrow the majority of funds from their related bank. The System banks obtain a substantial majority of their funds for lending operations through the sale of consolidated Systemwide bonds and notes to the public, but also obtain a portion of their funds from internally generated earnings and from the issuance of common and preferred stock and, to a lesser extent, from the issuance of subordinated debt.

The Farm Credit Administration (FCA) is delegated authority by Congress to regulate the bank and associations. The activities of the bank and associations are examined by the FCA, and certain actions by these entities are subject to the FCA's prior approval.

B. Operations:

The Farm Credit Act sets forth the types of authorized lending activities and financial services which can be offered by the bank and the associations and defines the eligible borrowers which they may serve. The associations are authorized to provide, or participate with other lenders to provide, credit, credit commitments and related services to eligible borrowers. Eligible borrowers are defined as (a) bona fide farmers and ranchers and producers or harvesters of aquatic products, (b) persons furnishing to farmers and ranchers services directly related to their on-farm operating needs, (c) owners of rural homes, (d) rural residents and (e) farm-related businesses. The bank also may lend to any national bank, state bank, trust company, agricultural credit corporation, incorporated livestock loan company, savings institution, credit union or any association of agricultural producers (aggregately referred to as OFIs) engaged in the making of loans to farmers and ranchers, and any corporation engaged in the making of loans to producers or harvesters of aquatic products.

The associations also serve as intermediaries in offering credit life and multi-peril crop insurance and financial management services to their borrowers.

FCA regulations require borrower information be held in strict confidence by Farm Credit institutions, their directors, officers and employees. Directors and employees of the Farm Credit institutions are prohibited, except under specified circumstances, from disclosing nonpublic personal information about members.

FLCAs borrow funds from the bank and in turn originate and service long-term real estate mortgage loans made to their members. The OFIs borrow from the bank and, in turn, originate and service short- and intermediate-term loans for their members. The ACAs borrow from the bank and in turn may originate and service both long-term real estate mortgage and short- and intermediate-term loans to their members. ACAs may form a parent-subsidiary structure and may operate their long-term mortgage activities through an FLCA subsidiary and their short- and intermediate-term lending activities through a PCA subsidiary. In the states of Alabama and Mississippi, the bank may discount or purchase from FLCAs long-term real estate mortgage loans. In the states of Louisiana, New Mexico and Texas, the bank may discount or purchase from FLCAs and ACAs long-term real estate mortgage loans and, from ACAs, short- and intermediate-term loans.

The bank, in conjunction with other banks in the System, jointly owns several service organizations which were created to provide a variety of services for the System. The bank has ownership interests in the following service organizations:

- Federal Farm Credit Banks Funding Corporation (Funding Corporation) – provides for the issuance, marketing and processing of Systemwide debt securities using a network of investment dealers and dealer banks. The Funding Corporation also provides financial management and reporting services.
- Farm Credit System Building Association – leases premises and equipment to the FCA, as required by the Farm Credit Act.
- Farm Credit System Association Captive Insurance Company – as a reciprocal insurer, provides insurance services to its member organizations.

In addition, The Farm Credit Council acts as a full-service, federated trade association which represents the System before Congress, the executive branch and others, and provides support services to System institutions on a fee basis.

The Farm Credit Act also established the Farm Credit System Insurance Corporation (Insurance Corporation) to administer the Farm Credit Insurance Fund (Insurance Fund). The Insurance Fund is required to be used to (1) insure the timely payment of principal and interest on Systemwide debt obligations (insured debt), (2) ensure the retirement of protected borrower capital at par or stated value, and (3) for other specified purposes. The Insurance Fund is also available for the discretionary uses, by the Insurance Corporation, of providing assistance to certain troubled System institutions and to cover the operating expenses of the Insurance Corporation. Each System bank has been required to pay premiums, which may be passed on to the associations, into the Insurance Fund based on its annual average loan principal outstanding until the assets in the Insurance Fund reach the "secure base amount," which is defined in the Farm Credit Act as 2.0 percent of the aggregate insured obligations (Systemwide debt obligations) or such other percentage of the aggregate obligations as the Insurance Corporation in its sole discretion determines to be actuarially sound. When the amount in the Insurance Fund exceeds the secure base amount, the Insurance Corporation is required to reduce premiums, but it still must ensure that reduced premiums are sufficient to maintain the level of the Insurance Fund at the secure base amount. In June 2008, with the passage of the Food, Conservation, and Energy Act of 2008 (Farm Bill), the basis for assessing premiums was changed, beginning with the second half of 2008, to reflect each System bank's pro rata share of outstanding insured debt. The Farm Bill imposes premiums of 20 basis points on adjusted insured debt obligations, with the Insurance Corporation Board having the ability to reduce the amount, and a risk surcharge of 10 basis points on nonaccrual loans and other-than-temporarily impaired investments.

Note 2 — Summary of Significant Accounting Policies

The accounting and reporting policies of the combined bank and associations conform to accounting principles generally accepted in the United States of America (GAAP) and prevailing practices within the banking industry. The preparation of combined financial statements in conformity with GAAP requires the managements of the bank and associations to make estimates and assumptions that affect the amounts reported in the combined financial statements and accompanying notes. Significant estimates are discussed in these notes as applicable. Certain amounts in prior years' combined financial statements have been reclassified to conform to the current year's presentation.

The accompanying combined financial statements include the accounts of the bank and associations, and reflect the investments in and allocated earnings of the service organizations in which the bank has partial ownership interests. All significant transactions and balances between the bank and associations have been eliminated in combination. The multi-employer structure of the district's defined benefit retirement plan results in the recording of the plan upon combination only.

A. Cash:

Cash, as included in the financial statements, represents cash on hand and on deposit at banks.

B. Investment Securities:

The bank and associations, as permitted under FCA regulations, hold eligible investments for the purposes of maintaining a liquidity reserve, managing short-term surplus funds and managing interest rate risk.

Most of the district's investments are to be held for an indefinite time period and, accordingly, have been classified as available for sale at December 31, 2008, 2007 and 2006. These investments are reported at fair value, and unrealized holding gains and losses are netted and reported as a separate component of members' equity in the combined balance sheets. Changes in the fair value of investments are reflected as direct charges or credits to other comprehensive income, unless the investment is deemed to be other-than-temporarily impaired. If an investment is deemed to be other-than-temporarily impaired, the cost basis of the investment is written down to its fair value and an impairment loss is recorded in earnings in the period of impairment. Purchased premiums and discounts are amortized or accreted using the effective interest method over the term of the respective issues. Realized gains and losses are determined using the specific identification method and are recognized in current operations.

During May 2008 the bank purchased mission-related rural housing mortgage-backed securities which constitute the bank's held-to-maturity investment portfolio. These securities are not marked to market and have an amortized cost basis of $50.5 million and a fair market value of $51.6 million; they are not included in the bank's liquidity calculations.

The bank reviews all investments that are in a loss position in order to determine whether the unrealized loss, which is considered an impairment, is temporary or other than temporary. In the event of other-than-temporary impairment, the cost basis of the investment would be written down to its fair value, and the loss would be included in current earnings. The bank and associations may also hold additional investments in accordance with mission-related investment programs, approved by the FCA.

C. Loans and Allowance for Loan Losses:

Long-term real estate mortgage loans can have maturities ranging from five to 30 years. Substantially all short-term and intermediate-term loans are made for agricultural production or operating purposes and have maturities of 10 years or less.

Loans are carried at their principal amount outstanding less any unearned income or unamortized discount. Interest on loans is accrued and credited to interest income based on the daily principal amount outstanding. Funds which are held by the district on behalf of the borrowers, where legal right of setoff exists, and which can be used to reduce outstanding loan balances at the district's discretion, are netted against loans in the combined balance sheets.

Loan origination fee income and direct loan origination costs are capitalized and the net fee or cost is amortized over the life of the related loans as an adjustment to yield.

Impaired loans are loans for which it is probable that not all principal and interest will be collected according to the contractual terms of the loan. Impaired loans include nonaccrual loans, restructured loans, and loans past due 90 days or more and still accruing interest. A loan is considered contractually past due when any principal repayment or interest payment required by the loan instrument is not received on or before the due date. A loan shall remain contractually past due until it is formally restructured or until the entire amount past due, including principal, accrued interest, and penalty interest incurred as the result of past due status, is collected or otherwise discharged in full.

Loans are generally placed in nonaccrual status when principal or interest is delinquent for 90 days (unless adequately secured and in the process of collection) or circumstances indicate that full collection of principal and interest is in doubt. In accordance with FCA regulations, all loans 180 days or more past due are considered nonaccrual. When a loan is placed in nonaccrual status, accrued interest deemed uncollectible is either reversed (if current year interest) or charged against the allowance for loan losses (if prior year interest).

Payments received on nonaccrual loans are generally applied to the recorded investment in the loan asset. If collection of the recorded investment in the loan is fully expected and the loan does not have a remaining unrecovered prior charge-off associated with it, payments are recognized as interest income. Nonaccrual loans may be returned to accrual status when contractual principal and interest are current, prior charge-offs have been recovered, the ability of the borrower to fulfill the contractual repayment terms is fully expected and the loan is not classified "doubtful" or "loss." If previously unrecognized interest income exists upon reinstatement of a nonaccrual loan to accrual status, interest income will only be recognized upon receipt of cash payments applied to the loan.

In cases where a borrower experiences financial difficulties and the bank or association makes certain monetary concessions to the borrower through modifications to the contractual terms of the loan, the loan is classified as a restructured loan. If the borrower's ability to meet the revised payment schedule is uncertain, the loan is classified as a nonaccrual loan.

The allowance for loan losses is maintained at a level considered adequate by management to provide for probable and estimable losses inherent in the loan portfolio. The allowance is based on a periodic evaluation of the loan portfolio by management in which numerous factors are considered, including economic conditions, loan portfolio composition and prior loan loss experience. The allowance for loan losses encompasses various judgments, evaluations and appraisals with respect to the loans and their underlying security that, by their nature, contain elements of uncertainty and imprecision. Changes in the agricultural economy and their impact on borrower repayment capacity will cause these various judgments, evaluations and appraisals to change over time. Accordingly, actual circumstances could vary significantly from the institutions' expectations and predictions of those circumstances. Management considers the following factors in determining and supporting the levels of allowances for loan losses: the concentration of lending in agriculture, combined with uncertainties associated with farmland values, commodity prices, exports, government assistance programs, regional economic effects and weather-related influences. The allowance is increased through provisions for loan losses and loan recoveries and is decreased through reversals of provisions for loan losses and loan charge-offs. The level of allowance for loan losses is generally based on recent charge-off experience adjusted for relevant environmental factors.

The allowance for loan losses is a valuation account used to reasonably estimate loan and lease losses as of the financial statement date. Determining the appropriate allowance for loan losses balance involves significant judgment about when a loss has been incurred and the amount of that loss. The determination of the allowance for loan losses is based on management's current judgments about the credit quality of its loan portfolio. A specific allowance may be established for impaired loans under SFAS No. 114, "Accounting by Creditors for Impairment of a Loan." Impairment of these loans is measured based on the present value of expected future cash flows discounted at the loan's effective interest rate or, as practically expedient, at the loan's observable market price or fair value of the collateral if the loan is collateral-dependent.

D. Other Property Owned:

Other property owned, consisting of real and personal property acquired through foreclosure or other collection action, is recorded at fair value, based on appraisal, less estimated selling costs upon acquisition. Revised estimates to the fair value less cost to sell are reported as adjustments to the carrying amount of the asset, provided that such adjusted value is not in excess of the carrying amount at acquisition. Income and expenses from operations and carrying value adjustments are included in losses (gains) on other property owned, net.

E. Premises and Equipment:

Premises and equipment are carried at cost less accumulated depreciation. Land is carried at cost. Depreciation expense is calculated using the straight-line method over the estimated useful lives of 40 years for buildings and improvements, three to 10 years for furniture, equipment and certain leasehold improvements, and three to four years for automobiles. Computer software and hardware are amortized over three years. Gains and losses on dispositions are reflected currently. Maintenance and repairs are charged to operating expense, and improvements are capitalized and amortized over the remaining useful life of the asset.

F. Other Assets and Other Liabilities:

Direct expenses incurred in issuing debt are deferred and amortized using the prospective level yield method over the term of related indebtedness.

The bank and associations are authorized under the Farm Credit Act to accept "advance conditional payments" (ACPs) from borrowers. To the extent the borrower's access to such ACPs is restricted and the legal right of setoff exists, the ACPs are netted against the borrower's related loan balance. ACPs which are held by the district but cannot be used to reduce outstanding loan balances, except at the direction of the borrower, are classified as other liabilities in the combined balance sheets. ACPs are not insured, and interest is generally paid by the associations on such balances. The total outstanding gross balances of advance conditional payments, both netted against loans and classified as other liabilities, at December 31, 2008, 2007 and 2006 were $271.5 million, $309.0 million and $286.4 million, respectively.

Derivative financial instruments are included on the balance sheet at fair value, as either other assets or other liabilities.

G. Employee Benefit Plans:

Substantially all employees of the bank and associations participate in one of two districtwide retirement plans and are eligible to participate in the 401(k) plan of the district. Additionally, certain qualified individuals in the bank may participate in a separate, supplemental pension plan. Within the 401(k) plan, a certain percentage of employee contributions is matched by the bank and associations. The 401(k) plan costs are expensed as incurred. Additionally, certain qualified individuals in the bank and associations may participate in a separate, nonqualified supplemental 401(k) plan.

As more fully described in Note 10, "Employee Benefit Plans," these plans are accounted for and reported in accordance with

SFAS No. 87, "Employers' Accounting for Pensions," SFAS No. 88, "Employers' Accounting for Settlements and Curtailments of Defined Benefit Pension Plans and for Termination Benefits," SFAS No. 106, "Employers' Accounting for Postretirement Benefits Other Than Pensions," SFAS No. 132, "Employers' Disclosures About Pensions and Other Postretirement Benefits," and SFAS No. 158, "Employers' Accounting for Defined Benefit Pension Plans and Other Postretirement Benefits." The bank and all but one association provide certain health care and life insurance benefits to eligible retired employees and directors. District employees' eligibility for these benefits upon retirement is dependent on conditions set by each district employer.

The structure of the district's defined benefit plan is characterized as multi-employer, since neither the assets, liabilities nor cost of any plan is segregated or separately accounted for by participating employers (bank and associations). No portion of any surplus assets is available to any participating employer, nor is any participating employer required to pay for plan liabilities upon withdrawal from the plans. As a result, participating employers of the plans only recognize as cost the required contributions for the period and a liability for any unpaid contributions required for the period of their financial statements. The majority of plan obligations, assets and the components of annual benefit expenses are recorded and reported upon combination only.

H. Income Taxes:

The bank, FLCAs and FLCA subsidiaries of ACA parent companies are exempt from federal and certain other income taxes as provided in the Farm Credit Act. The ACAs and their PCA subsidiaries provide for federal and certain other income taxes.

Certain ACAs operate as cooperatives which qualify for tax treatment under Subchapter T of the Internal Revenue Code. These ACAs and their PCA subsidiaries can exclude from taxable income amounts distributed as qualified patronage distributions to borrowers in the form of cash, stock or allocated retained earnings. Provisions for income taxes for these ACAs are made only on the earnings not distributed as qualified patronage distributions. Certain ACAs distribute patronage on the basis of taxable income. In this method, deferred income taxes are provided on the taxable income of ACAs on the basis of a proportionate share of the tax effect of temporary differences not allocated in patronage form. Other ACAs distribute patronage on the basis of book income. In this method, deferred taxes are recorded on the tax effect of all temporary differences based on the assumption that such temporary differences are retained by the institution and will therefore impact future tax payments. For all ACAs, a valuation allowance is provided for the deferred tax assets to the extent that it is more likely than not (over 50 percent probability), based on management's estimate, that they will not be realized. The consideration of valuation allowances involves various estimates and assumptions as to future taxable earnings, including the effects of our expected patronage program, which reduce taxable earnings.

As of December 31, 2008, deferred income taxes have not been provided by the ACAs and their PCA subsidiaries on $35.2 million of pre-1993 patronage distributions from the bank because management's intent is to (1) permanently invest these and other undistributed earnings in the bank, thereby indefinitely postponing their conversion to cash, or (2) pass through any distributions related to pre-1993 earnings to borrowers through qualified patronage allocations. No deferred taxes have been provided on the bank's post-1994 unallocated earnings. The bank currently has no plans to distribute unallocated bank earnings and does not contemplate circumstances which, if distributions were made, would result in income taxes being paid at the association level.

I. Derivative Instruments and Hedging Activity:

The bank is party to derivative financial instruments and cash flow hedges, consisting of interest rate swaps, which are principally used to manage interest rate risk on assets, liabilities and firm commitments. Derivatives are recorded on the balance sheet as assets and liabilities at fair value.

For fair-value hedge transactions which hedge changes in the fair value of assets, liabilities or firm commitments, changes in the fair value of the derivative will generally be offset by changes in the hedged item's fair value. For cash flow hedges, which hedge the exposure to variability in expected future cash flows, changes in the fair value of the derivative are reflected in accumulated other comprehensive income. The bank formally documents all relationships between hedging instruments and hedged items, as well as its risk-management objective and strategy for undertaking various hedge transactions. This process includes linking all derivatives to specific liabilities on the balance sheet. The bank uses interest rate swaps whose critical terms match the corresponding hedged item, thereby qualifying for short-cut treatment under the provisions of SFAS No. 133, "Accounting for Derivative Instruments and Hedging Activities," and are presumed to be highly effective in offsetting changes in the fair value. The bank would discontinue hedge accounting prospectively when the bank determines that a derivative has not been or is not expected to be effective as a hedge. In the event that hedge accounting were discontinued and the derivative remained outstanding, the bank would carry the derivative at its fair value on the balance sheet, recognizing changes in fair value in current period earnings.

J. Fair Value Measurements:

Effective January 1, 2008, the System adopted SFAS No. 157, "Fair Value Measurements." This Statement defines fair value, establishes a framework for measuring fair value and expands disclosures about fair value measurements. It describes three levels of inputs that may be used to measure fair value:

Level 1 — Quoted prices in active markets for identical assets or liabilities that the reporting entity has the ability to access at the measurement date. Assets held in trust funds relate to deferred compensation and our supplemental retirement plans. The trust funds include investments that are actively traded and have quoted net asset values that are observable in the marketplace.

Level 2 — Observable inputs other than quoted prices included within Level 1 that are observable for the asset or liability either directly or indirectly. Level 2 inputs include the following: (a) quoted prices for similar assets or liabilities in active markets; (b) quoted prices for identical or similar assets or liabilities in markets that are not active so that they are traded less frequently than exchange-traded instruments, the prices are not current or principal market information is not released publicly; (c) inputs other than quoted prices that are observable such as interest rates and yield curves, prepayment speeds, credit risks and default rates; and (d) inputs derived principally from or corroborated by observable market data by correlation or other means. This category generally includes certain U.S.

government and agency mortgage-backed debt securities, corporate debt securities, and derivative contracts.

Level 3 — Unobservable inputs that are supported by little or no market activity and that are significant to the fair value of the assets or liabilities. These unobservable inputs reflect the reporting entity's own assumptions about assumptions that market participants would use in pricing the asset or liability. Level 3 assets and liabilities include financial instruments whose value is determined using pricing models, discounted cash flow methodologies, or similar techniques, as well as instruments for which the determination of fair value requires significant management judgment or estimation.

The fair value disclosures have been expanded in accordance with SFAS No. 157, as disclosed in Note 14, "Fair Value Measurements."

K. Recently Issued Accounting Pronouncements:

In March 2008, the Financial Accounting Standards Board (FASB) issued Statement of Financial Accounting Standards (SFAS) No. 161, "Disclosures About Derivative Instruments and Hedging Activities," which amends and expands the disclosure requirements for derivative instruments and for hedging activities previously required by SFAS No. 133. It states that an entity with derivative instruments shall disclose information to enable users of the financial statements to understand: (a) how and why an entity uses derivative instruments; (b) how derivative instruments and related hedged items are accounted for under this Statement and related interpretations; and (c) how derivative instruments and related hedged items affect an entity's financial position, financial performance, and cash flows. This Statement is effective for financial statements issued for fiscal years and interim periods beginning after November 15, 2008, with early application encouraged. This Statement encourages, but does not require, comparative disclosures for earlier periods at initial adoption. The bank is currently evaluating the impact of adoption on its financial statement disclosures.

Note 3 — Investment Securities

A summary of the amortized cost and estimated fair value of investment securities at December 31, 2008, 2007 and 2006, follows:

	December 31, 2008				
	Amortized Cost	**Gross Unrealized Gains**	**Gross Unrealized Losses**	**Fair Value**	**Weighted Average Yield**
Agency debt	**$ 500,000**	**$ 957**	**$ 0**	**$ 500,957**	**3.54%**
Commercial paper and other	**536,970**	**1,490**	**(2,144)**	**536,316**	**0.84**
Federal agency collateralized mortgage obligations	**1,661,323**	**22,313**	**(1,709)**	**1,681,033**	**4.58**
Other collateralized mortgage obligations	**227,165**	**—**	**(35,478)**	**192,581**	**4.80**
Asset-backed securities	**91,310**	**118**	**(6,458)**	**84,970**	**4.17**
Total available-for-sale investments	**$3,016,768**	**$24,878**	**$(45,789)**	**$2,995,857**	**3.74%**
Held-to-Maturity Investments:					
Mission related	$ 50,540	$ 1,103	$ 0	$ 51,643	4.98%

	December 31, 2007				
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value	Weighted Average Yield
Commercial paper and other	$ 399,265	$ 14	$ (964)	$ 398,315	4.60%
Federal agency collateralized mortgage obligations	1,502,436	10,899	(5,284)	1,508,051	4.98
Other collateralized mortgage obligations	296,552	22	(2,891)	293,683	5.06
Asset-backed securities	217,703	—	(6,753)	210,950	5.13
Total	$ 2,415,956	$10,935	$(15,892)	$ 2,410,999	4.93%

	December 31, 2006				
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value	Weighted Average Yield
Commercial paper and other	$ 366,173	$ 83	$ (29)	$ 366,227	5.36%
Federal agency collateralized mortgage obligations	1,556,467	1,142	(19,307)	1,538,302	4.80
Other collateralized mortgage obligations	387,375	199	(3,896)	383,678	5.09
Asset-backed securities	383,697	406	(68)	384,035	5.60
Total	$2,693,712	$ 1,830	$(23,300)	$ 2,672,242	5.04%

A summary of contractual maturity, amortized cost, estimated fair value and weighted average yield of investment securities at December 31, 2008, follows:

	Amortized Cost	**Fair Value**	**Weighted Average Yield**
Due in one year or less	$ 904,238	$ 904,278	1.97%
Due after one year through five years	294,197	296,896	3.50
Due after five years through 10 years	297,928	298,082	3.85
Due after 10 years	1,520,405	1,496,601	4.71
Total	$ 3,016,768	$ 2,995,857	3.74%
Mission related:			
Due in one year or less	$ 50,540	$ 51,643	4.98%

At December 31, 2008, the available-for-sale investment portfolio included guaranteed Small Business Administration pooled securities totaling $17.9 million held by a district association. Available-for-sale investments are recorded on the balance sheet at fair value; held-to-maturity investments are recorded at amortized cost.

CMOs have stated contractual maturities in excess of 15 years. However, the security structure of the CMOs is designed to produce a relatively short-term life. At December 31, 2008, the CMO portfolio had a weighted average remaining life of approximately two years.

Proceeds and related gains and losses on investment securities follow:

	Year Ended December 31,		
	2008	2007	2006
Proceeds on sales	**$ 114,424**	$ 93,123	$ 107,814
Realized gains on sales	**2,556**	503	907
Realized losses due to impairment	**2,238**	—	—

The net realized gain and loss is included on the combined statements of income as part of total noninterest income.

At December 31, 2008, the district had 83 investments that were in a loss position. 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 December 31, 2008. The continuous loss position is based on the date the impairment occurred. An investment is considered impaired if its fair value is less than its cost.

	Less Than 12 Months		Greater Than 12 Months	
	Fair Value	**Unrealized Losses**	**Fair Value**	**Unrealized Losses**
Collateralized mortgage obligations	$ 404,984	$ (23,836)	$ 60,853	$ (13,351)
Commercial paper	99,988	(12)	77,867	(2,133)
Asset-backed securities	0	0	67,041	(6,458)
Total	$ 504,972	$ (23,848)	$ 205,761	$ (21,942)

The bank evaluates investment securities for other-than-temporary impairment on a quarterly basis. Factors considered in determining whether an impairment is other than temporary include: 1) the length of time and the extent to which the fair value is less than cost; 2) the credit ratings, financial condition and near-term prospects of the issuer; 3) the estimated cash flow projections compared to contractual cash flows; and 4) our ability and intent to hold these investments for a period of time sufficient to collect all amounts due according to the contractual terms of the investments. Analysis in the fourth quarter of 2008 resulted in a determination that one of the bank's whole-loan mortgage-backed investments had an impairment that was considered other than temporary. The whole-loan mortgage-backed investment was downgraded to Baa1 and B by Moody's and Standard and Poor's, respectively, during 2008. Using more detailed cash flow analysis, the bank determined that the investment's impairment was other than temporary, and as a result, the investment's amortized cost of $14.9 million was written down to its fair value of $12.6 million, resulting in a realized loss of $2.2 million for 2008.

Other investments in loss positions consisted predominantly of mortgage-backed securities and asset-backed securities classified as available-for-sale. The current unrealized loss positions principally resulted from changes in market interest rates and a decrease in liquidity in the marketplace, and not primarily from deterioration in credit quality. The bank has the ability and intent to hold these securities for a period of time sufficient to recover all gross unrealized losses, and thus the securities are not considered to be other-than-temporarily impaired at December 31, 2008.

Note 4 — Loans and Allowance for Loan Losses

Loans comprised the following categories at December 31:

	2008	2007	2006
Real estate mortgage	**$ 11,015,550**	$ 10,149,685	$ 9,005,408
Production and intermediate term	**2,268,893**	2,115,224	1,685,374
Agribusiness			
Loans to cooperatives	**188,105**	184,229	53,988
Processing and marketing	**1,392,895**	1,220,876	944,258
Farm-related business	**262,007**	277,912	226,473
Communication	**409,341**	306,351	378,728
Energy	**644,236**	524,175	348,020
Water and waste disposal	**50,172**	50,098	28,372
Rural home	**205,949**	151,583	130,091
Mission-related	**41,841**	28,055	5,391
International	**1,349**	979	1,056
Loans to other financial institutions	**106,126**	100,328	90,059
Lease receivables	**3,607**	5,042	8,103
Total	**$ 16,590,071**	$ 15,114,537	$ 12,905,321

The FCA approved a program that allows the bank and its associations to purchase investments in debt instruments called "Rural America Bonds." This program is intended to help meet the growing financing needs of agriculture and rural America, improve the income and economic well-being of American farmers and ranchers, and enhance the economic vibrancy of rural areas that support agriculture. Loans related to this initiative are included in "mission-related" loans in the above table.

The district's concentration of credit risk in various agricultural commodities is shown in the following table at December 31 (*dollars in millions*):

	2008		2007		2006	
Commodity	**Amount**	**%**	Amount	%	Amount	%
Livestock	**$ 6,310**	**38%**	$ 6,000	40%	$ 4,966	38%
Crops	**2,255**	**14**	2,095	14	1,692	13
Timber	**1,855**	**11**	1,819	12	1,597	12
Cotton	**758**	**5**	774	5	662	5
Poultry	**681**	**4**	575	4	467	4
Dairy	**508**	**3**	476	3	453	4
Rural home	**206**	**1**	152	1	130	1
Other	**4,017**	**24**	3,224	21	2,938	23
Total	**$ 16,590**	**100%**	$ 15,115	100%	$ 12,905	100%

The amount of collateral obtained, if deemed necessary upon extension of credit, is based on management's credit evaluation of the borrower. Collateral held varies, but typically includes farmland and income-producing property, such as crops and livestock, as well as receivables. Long-term real estate loans are secured by the first liens on the underlying real property. Federal regulations state that long-term real estate loans are not to exceed 85 percent (97 percent if guaranteed by a government agency) of the property's appraised value. However, a decline in a property's market value subsequent to loan origination or advances, or other actions necessary to protect the financial interest of the association in the collateral, may result in the loan to value ratios in excess of the regulatory maximum.

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 loans. Interest income recognized and cash payments received on nonaccrual impaired loans are applied in a similar manner as for nonaccrual loans, as described in Note 2, "Summary of Significant Accounting Policies."

The following table presents information concerning nonaccrual loans, accruing restructured loans and accruing loans 90 days or more past due. Restructured loans are loans whose terms have been modified and on which concessions have been granted because of borrower financial difficulties.

	December 31, 2008	2007	2006
Nonaccrual loans			
Current as to principal and interest	**$ 249,851**	$ 79,501	$ 24,529
Past due	**72,562**	20,618	11,665
Total nonaccrual loans	**322,413**	100,119	36,194
Accrual loans			
Restructured	**6,072**	6,191	7,218
90 days or more past due	**17,896**	16,852	750
Total impaired accrual loans	**23,968**	23,043	7,968
Total impaired loans	**$ 346,381**	$ 123,162	$ 44,162
Average impaired loans	**$ 165,941**	$ 73,680	$ 45,541

There were $16.6 million in commitments to lend additional funds to borrowers whose loans were classified as nonaccrual or restructured at December 31, 2008.

Interest income is recognized and cash payments are applied on nonaccrual impaired loans as described in Note 2, "Summary of Significant Accounting Policies." The following table presents interest income recognized on impaired loans for the years ended December 31:

	2008	2007	2006
Interest income recognized on nonaccrual loans	**$ 577**	$ 1,515	$ 1,976
Interest income on impaired accrual loans	**1,500**	1,353	984
Interest income recognized on impaired loans	**$ 2,077**	$ 2,868	$ 2,960

The following table presents information concerning impaired loans as of December 31:

	2008	2007	2006
With related specific allowance	**$ 116,627**	$ 51,588	$ 12,544
With no related specific allowance	**229,754**	71,574	31,618
Total impaired loans	**$ 346,381**	$ 123,162	$ 44,162
Allowance on impaired loans	**$ 31,379**	$ 10,376	$ 4,047

Interest income on nonaccrual and accruing restructured loans that would have been recognized under the original terms of the loans during 2008 were as follows:

	2008	2007	2006
Interest income which would have been recognized under the original loan terms	**$ 20,727**	$ 15,086	$ 7,238
Less: Interest income recognized	**2,077**	2,868	2,960
Foregone interest income	**$ 18,650**	$ 12,218	$ 4,278

A summary of changes in the allowance for loan losses follows:

	December 31, 2008	2007	2006
Balance at beginning of year	**$ 24,495**	$ 13,969	$ 9,533
Charge-offs:			
Real estate mortgage	**160**	30,017	873
Production and intermediate term	**3,163**	2,868	732
Agribusiness	**—**	—	4,285
Farm-related business	**4,766**	127	—
Energy	**18,958**	—	—
Rural home	**11**	22	—
Total charge-offs	**27,058**	33,034	5,890
Recoveries:			
Production and intermediate term	**473**	142	393
Agribusiness	**—**	—	577
Farm-related business	**322**	287	—
Energy	**27**	—	—
Total recoveries	**822**	429	970
Net charge-offs	**(26,236)**	(32,605)	(4,920)
Provision for loan losses	**53,515**	43,131	9,356
Other	**(121)**	—	—
Balance at end of year	**$ 51,653**	$ 24,495	$ 13,969
Ratio of net charge-offs during the period to average loans outstanding during the period	0.16%	0.23%	0.04%

The $18.9 million energy charge-off consists primarily of charge-offs in 2008 that were related to participation loans to an ethanol borrower. The $121 "other" deduction is the provision for loan losses on unused commitments to that borrower, which are recorded as an other liability.

The following table presents a breakdown of the allowance for loan losses at December 31 (*dollars in thousands*):

	2008		2007		2006	
	Amount	**%**	Amount	%	Amount	%
Real estate mortgage	**$ 36,225**	**70%**	$ 18,847	77%	$ 10,748	77%
Production and intermediate term	**6,610**	**13**	3,315	13	1,843	13
Agribusiness	**6,792**	**13**	1,689	7	943	7
Communication	**1,013**	**2**	153	1	158	1
Energy	**405**	**1**	196	1	101	1
Water and waste disposal	**1**	**—**	—	—	—	—
Rural home	**593**	**1**	285	1	169	1
International	**4**	**—**	2	—	1	—
Lease receivables	**10**	**—**	8	—	6	—
Total	**$ 51,653**	**100%**	$ 24,495	100%	$ 13,969	100%

To mitigate risk of loan losses, district associations have entered into long-term standby commitments to purchase agreements with the Federal Agricultural Mortgage Corporation (Farmer Mac) through an arrangement with the bank. The agreements, which are effectively credit guarantees that will remain in place until the loans are paid in full, give the associations the right to sell the loans identified in the agreements to Farmer Mac in the event of default, subject to certain conditions. The balance of loans under long-term standby commitments to purchase was $512.2 million at December 31, 2008.

Fees paid to Farmer Mac for such commitments totaled $1.8 million for the year ended December 31, 2008, and are classified as noninterest expense.

In 2008, the bank sold an additional $800 million of participations in eight of its direct notes receivable from district associations to another System bank for a total of $3.5 billion. The purpose of these sales was to diversify the credit exposure of the bank and to satisfy the bank's capital management goals.

Note 5 — Premises and Equipment

Premises and equipment comprised the following at:

	December 31,		
	2008	2007	2006
Land	**$ 10,875**	$ 9,798	$ 9,050
Buildings and improvements	**36,678**	33,942	32,687
Furniture and equipment	**36,254**	30,650	28,724
	83,807	74,390	70,461
Accumulated depreciation	**(34,308)**	(31,791)	(29,826)
Total	**$ 49,499**	$ 42,599	$ 40,635

On September 30, 2003, the bank entered into a lease for approximately 102,500 square feet of office space to house its headquarters facility. The lease was effective September 30, 2003, and its term is from September 1, 2003, to August 31, 2013. Under the terms of the lease, the bank was obligated to pay base rental or its share of basic costs during the first 12 months of the lease. Thereafter, the bank will pay annual base rental ranging from $11 per square foot in the second year to $19 per square foot in the tenth year. The bank moved to the new facilities during the second quarter of 2004. Annual lease expenses for the new facility were $2.7 million, $2.9 million, and $2.5 million for 2008, 2007 and 2006, respectively.

Following is a schedule of the minimum lease payments on the lease:

	Minimum Lease Payments
2009	$ 1,674
2010	1,776
2011	1,879
2012	1,947
2013	1,297
Total minimum lease payments	$ 8,573

Note 6 — Other Assets and Other Liabilities

Other assets comprised the following at December 31:

	2008	2007	2006
Fair value of derivatives	**$ 31,439**	**$** 7,034	**$** 1,758
Accounts receivable	**23,866**	16,505	9,948
Investment in another System bank	**10,742**	4,333	2,362
Unamortized debt issue costs	**10,680**	9,628	7,318
Farmer Mac preferred stock	**7,000**	—	—
Deferred tax assets	**2,233**	2,079	2,299
Intangible assets related to pensions	**—**	—	1,278
Land investment	**—**	—	141
Other, net	**3,156**	2,044	1,712
Total	**$ 89,116**	$ 41,623	$ 26,816

Other liabilities comprised the following at December 31:

	2008	2007	2006
Pension liability	**$ 139,783**	$ 72,052	$ 23,536
Advance conditional payments	**49,489**	51,503	43,008
Postretirement benefits	**40,199**	36,547	49,950
Accounts payable	**34,163**	24,785	18,302
Bank draft payable	**32,382**	25,615	26,624
FCSIC premium payable	**21,978**	20,691	16,240
Additional minimum pension liability	**—**	—	6,209
Fair value of derivatives	**3,074**	178	3,459
Income taxes payable	**644**	602	248
Deferred tax liabilities	**411**	611	958
Other, net	**3,955**	2,879	2,431
Total	**$ 326,078**	$ 235,463	$ 190,965

Note 7 — Bonds and Notes

Systemwide Debt Securities:

The System, unlike commercial banks and other depository institutions, obtains funds for its lending operations primarily from the sale of Systemwide debt securities issued by the banks through the Funding Corporation. Certain conditions must be met before the bank can participate in the issuance of Systemwide debt securities. The bank is required by the Farm Credit Act and FCA regulations to maintain specified eligible assets at least equal in value to the total amount of debt obligations outstanding for which it is primarily liable as a condition for participation in the issuance of Systemwide debt. This requirement does not provide holders of Systemwide debt securities, or bank and other bonds, with a security interest in any assets of the banks. In general, each bank determines its participation in each issue of Systemwide debt securities based on its funding and operating requirements, subject to the availability of eligible assets as described above and subject to Funding Corporation determinations and FCA approval. At December 31, 2008, the bank had such specified eligible assets totaling $14.6 billion and obligations and accrued interest payable totaling $13.9 billion, resulting in excess eligible assets of $770.6 million.

In 1994, the System banks and the Funding Corporation entered into the Market Access Agreement (MAA), which established criteria and procedures for the banks to provide certain information to the Funding Corporation and, under certain circumstances, for restricting or prohibiting an individual bank's participation in Systemwide debt issuances, thereby reducing other System banks' exposure to statutory joint and several liability. At December 31, 2008, the bank was, and currently remains, in compliance with the conditions and requirements of the MAA.

Each issuance of Systemwide debt securities ranks equally, in accordance with the FCA regulations, with other unsecured Systemwide debt securities. Systemwide debt securities are not issued under an indenture, and no trustee is provided with respect to these securities. Systemwide debt securities are not subject to acceleration prior to maturity upon the occurrence of any default or similar event.

The bank's participation in Systemwide debt securities follows (*dollars in millions*):

	Systemwide						Notes Payable to Other System Bank		Total	
	Bonds		Medium-Term Notes		Discount Notes					
Year of Maturity	Amount	Weighted Average Interest Rate	Amount	Weighted Average Interest Rate	Amount	Weighted Average Interest Rate	Amount	Weighted Average Interest Rate	Amount	Weighted Average Interest Rate
2009	$ 3,444.4	2.71%	$ —	—%	$ 2,466.7	1.37%	$ 3,500.0	3.25%	$ 9,411.1	2.56%
2010	1,713.6	3.85	—	—	—	—	—	—	1,713.6	3.85
2011	1,391.3	3.73	—	—	—	—	—	—	1,391.3	3.73
2012	714.9	4.29	—	—	—	—	—	—	714.9	4.29
2013	1,393.5	4.28	—	—	—	—	—	—	1,393.5	4.28
Subsequent years	2,677.8	5.22	—	—	—	—	—	—	2,677.8	5.22
Total	$ 11,335.5	3.89%	$ —	—%	$ 2,466.7	1.37%	$ 3,500.0	3.25%	$ 17,302.2	3.40%

In the preceding table, the weighted average effective rate reflects the effects of interest rate swaps used to manage the interest rate risk on the bonds and notes issued by the bank. The bank's interest rate swap strategy is discussed more fully in Note 2, "Summary of Significant Accounting Policies" and Note 16, "Derivative Instruments and Hedging Activity."

Systemwide bonds, medium-term notes, master notes, discount notes (Systemwide debt securities) and bank bonds are the joint and several obligations of all System banks. Discount notes are issued with maturities ranging from one to 365 days. The average maturity of discount notes at December 31, 2008, was 107 days.

The bank's Systemwide debt includes callable debt, consisting of the following at December 31, 2008:

Year of Maturity	Amount	Range of First Call Dates
2009	$ 290,000	1/1/2009 – 2/17/2009
2010	397,000	1/22/2009 – 10/6/2009
2011	855,000	1/1/2009 – 11/10/2009
2012	495,000	1/12/2009 – 12/27/2010
2013	1,228,000	1/1/2009 – 11/4/2010
Subsequent years	1,840,000	1/1/2009 – 11/7/2011
Total	$ 5,105,000	1/1/2009 – 11/7/2011

Callable debt may be called on the first call date and, generally, every day thereafter with seven business days' notice. Expenses associated with the exercise of call options on debt issuances are included in interest expense.

As described in Note 1, "Organization and Operations," the Insurance Fund is available to ensure the timely payment of principal and interest on bank bonds and Systemwide debt securities (insured debt) of insured System banks to the extent net assets are available in the Insurance Fund. All other liabilities in the combined financial statements are uninsured.

Subordinated Debt:

In September 2008, the bank issued $50 million of 8.406 percent unsecured subordinated notes due in 2018, generating proceeds of $49.4 million. The proceeds were used to increase regulatory permanent capital and total surplus pursuant to Farm Credit Administration regulations and for general corporate purposes. This debt is unsecured and subordinate to all other categories of creditors, including general creditors, and senior to all classes of shareholders. Interest is payable semi-annually on March 15 and September 15. 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 bank may not declare or pay any dividends or patronage refunds, among certain other restrictions, until interest payments are resumed and all deferred interest has been paid. The subordinated debt is not considered Systemwide debt and is not guaranteed by the Farm Credit System or any banks in the System. Payments on the subordinated notes are not insured by the Farm Credit Insurance Fund. In accordance with FCA's approval of the bank's subordinated debt offering, the bank's minimum net collateral ratio for all regulatory purposes while any subordinated debt is outstanding will be 104 percent, instead of the 103 percent stated by regulation.

Other:

In 2008, the bank sold an additional $800 million of participations in eight of its direct notes receivable from district associations to another System bank for a total of $3.5 billion. Accordingly, this $3.5 billion is included as a liability in "bonds and notes, net" on the district's balance sheet.

The bank maintains a $150.0 million commercial bank committed line of credit to support possible general short-term credit needs.

Note 8 — Members' Equity

Descriptions of the bank's and associations' capitalization requirements, regulatory capitalization requirements, and restrictions and equities are provided below.

A. Capitalization Requirements:

As a condition of borrowing, in accordance with the Farm Credit Act, each borrower is required to invest in common stock (in the case of mortgage or agricultural loans) or participation certificates (in the case of rural residence or farm-related business loans) of their respective association. Capitalization bylaws of the associations establish minimum and maximum stock purchase requirements for borrowers. The initial investment requirement of the associations ranges from the statutory minimum of $1,000 to 2 percent of the loan amount. The capitalization bylaws also limit the capital contributions that an institution can require from its borrowers to 10 percent of defined borrowings for associations. If necessary, each association's board of directors may modify, within the range defined in their bylaws, the capitalization requirements to meet the association's capital needs.

A borrower obtaining a mortgage or agricultural loan purchases voting common stock which entitles the holder to a single vote, regardless of the number of shares held in the respective association. Within two years after a borrower's loan is repaid in full, any voting common stock held by the borrower will be converted to nonvoting common stock. A borrower obtaining a rural residence or farm-related business loan purchases participation certificates which provide no voting rights to their owner.

Each class of nonvoting stock must approve, as a class, the adoption of future revisions of capitalization bylaws if the class of stock is affected by a change in the preference provided for in the proposed capitalization bylaws.

Capitalization bylaws for each association provide for the amount of voting common stock or participation certificates that are required to be purchased by a borrower as a percentage of the loan obtained. The borrower acquires ownership of the common stock or participation certificates at the time the loan is made, but usually does not make a cash investment; the aggregate par value is added to the principal amount of the related loan obligation. The bank and the associations have a first lien on the stock or participation certificates owned by borrowers. Retirement of such equities will be at the lower of par or book value, and repayment of a loan does not automatically result in retirement of the corresponding stock or participation certificates.

B. Regulatory Capitalization Requirements and Restrictions:

FCA's capital adequacy regulations require the bank and associations to achieve and maintain, at minimum, permanent capital of 7 percent of risk-adjusted assets and off-balance-sheet commitments. The Farm Credit Act has defined permanent capital to include all capital except stock and other equities that may be retired upon the repayment of the holder's loan or otherwise at the option of the holder, or is otherwise not at risk. Risk-adjusted assets have been defined by regulations as the balance sheet assets and off-balance-sheet commitments adjusted by various percentages ranging from 0 to 100 percent, depending on the level of risk inherent in the various types of assets. The bank and associations are prohibited from reducing permanent capital by retiring stock or by making certain other distributions to stockholders unless the minimum permanent capital standard is met.

The bank's permanent capital ratio at December 31, 2008, was 14.03 percent and exceeded FCA standards. All associations currently meet the minimum capital standard established by FCA regulations. All associations are able to retire stock or distribute earnings in accordance with the Farm Credit Act and FCA regulatory restrictions. Management knows of no reasons why the bank and associations would be prohibited from retiring stock.

The following table sets forth the ranges of capital standards for the district at December 31, 2008:

	Permanent Capital Ratio Ranges %	Core Surplus Ratio Ranges %	Total Surplus Ratio Ranges %
Bank	14.03	6.40	11.25
FLCAs	13.21 – 16.49	12.76 – 15.81	12.76 – 15.81
ACAs	10.12 – 16.02	9.29 – 17.34	9.56 – 17.34
Regulatory minimum standard	7.00	3.50	7.00

The bank is required by FCA regulations to achieve and maintain net collateral of 103 percent of total liabilities. However, the issuance of subordinated debt resulted in FCA requiring the net collateral to be 104 percent to total liabilities while any subordinated debt is outstanding. Net collateral consists of loans, real or personal property acquired in connection with loans, marketable investments, and cash and cash equivalents. At December 31, 2008, the bank's net collateral ratio was 105.40 percent.

C. Description of Associations' Equities:

The following is a summary of the associations' stock and participation certificates outstanding:

Stock and Participation Certificates	Par Value	Number of Shares at December 31, 2008	2007	2006
Stock				
Common – voting (eligible for dividends, convertible)	$ 5.00	**11,899,534**	11,647,412	11,016,476
Common – nonvoting (eligible for dividends, convertible)	$ 5.00	**76,595**	93,083	88,565
Preferred – nonvoting (eligible for dividends, nonconvertible)	$ 5.00	**550,840**	550,840	713,056
Participation certificates – nonvoting (eligible for dividends, convertible)	$ 5.00	**396,849**	370,682	344,044

The preferred stock noted above is nonvoting stock. It is issued by one association as evidence of borrowers' claims to allocated retained earnings of a specific year. The preferred stock may be retired at the sole discretion of the association's board of directors.

In the event of the liquidation or dissolution of an association, any assets of the association remaining after payment or retirement of all liabilities shall be distributed to stockholders in the following order:

First, holders of preferred stock at par value, if any;

Second, ratably to holders of all classes of common stock and participation certificates at par value or face amount;

Third, ratably to the holders of allocated retained earnings on the basis of oldest allocations first;

Fourth, ratably to the holders of nonqualified written notices of allocation on the basis of the oldest allocations first;

Then, the remainder of assets ratably to all holders of common stock and participation certificates, in proportion to the aggregate patronage of each such holder to the total patronage of all holders.

ACA bylaws provide for operation as cooperatives which qualify for tax treatment under Subchapter T of the Internal Revenue Code. Under cooperative operations, earnings of the ACA may be distributed to borrowers. Patronage distributions are generally in the form of allocated retained earnings and cash. At least 20 percent of the total patronage distribution must be paid in cash. Amounts not distributed are retained as unallocated retained earnings.

D. Description of Bank Equities:

According to the bank's bylaws, the minimum and maximum stock investments required of the ACAs and FLCAs are 2 percent (or one thousand dollars, whichever is greater) and 5 percent, respectively, of each association's average borrowings from the bank. The investments in the bank are required to be in the form of Class A voting common stock. These intercompany balances and transactions are eliminated in combination.

The bank requires OFIs to make cash purchases of common nonvoting stock in the bank based on the OFI's average borrowings from the bank. The bank has a first lien on these equities for the repayment of any indebtedness to the bank. At December 31, 2008, the bank had $1.99 million of common stock outstanding to OFIs at a par value of $5.00 per share.

On November 7, 2003, the bank issued 100,000 shares of $1,000 cumulative perpetual preferred stock for net proceeds of $98,644, after expenses of $1,356 associated with the offering. The preferred stock was issued to provide capital for general corporate purposes. On September 26, 2005, an additional 100,000 shares was issued for net proceeds of $108,894, including $2,121 of accrued dividends payable and after expenses of $1,687 associated with the offering. Net proceeds from the additional issue were to enhance the composition of the bank's capital and liquidity, to support the bank's loan growth, to provide a base for further growth and service opportunities to our members and to rural America, and for general corporate purposes. The dividend rate on the cumulative perpetual preferred stock is 7.561 percent, payable semi-annually to December 31, 2013, after which dividends are payable quarterly at a rate equal to 3-month London Interbank Offered Rate (LIBOR) plus 445.75 basis points. For regulatory purposes, the preferred stock is treated as equity, and is not mandatorily redeemable. Dividends on the stock are reported as declared. Preferred stock dividends totaling $15,122 were declared and paid during 2008.

During 2008, the bank received ratings from two rating agencies. In August 2008, Moody's Investors Service upgraded the bank's issuer rating to Aa2 from the Aa3 rating it had issued in July 2008. In addition, the bank's A2 preferred stock rating was affirmed and the bank received an A1 subordinated debt rating. In June 2008, Fitch Ratings, Ltd. issued an AA-long-term issuer default rating with a stable rating outlook and assigned an A rating to the bank's preferred stock.

E. Accumulated Other Comprehensive Loss:

Accumulated Other Comprehensive Loss was comprised of the following components at December 31:

	2008	2007	2006
Unrealized losses on investments available-for-sale, net	$ 21,910	$ 4,957	$ 26,401
Pension and other benefit plans	108,783	30,583	—
Unrealized losses (gains) on cash flow hedge derivatives, net	3,074	(1,047)	—
Total	$ 132,767	$ 34,493	$ 26,401

Note 9 — Income Taxes

The information that follows relates only to the district's ACAs, as the bank and FLCAs are exempt from federal and other income taxes.

The provision for (benefit from) income taxes follows for years ended December 31:

	2008	2007	2006
Current			
Federal	$ 694	$ 262	$ 209
State	3	6	18
Total current	697	268	227
Deferred			
Federal	(357)	(75)	(415)
State	4	(52)	(40)
Total deferred	(353)	(127)	(455)
Total provision for (benefit from) income taxes	$ 344	$ 141	$ (228)

The provision for (benefit from) income tax differs from the amount of income tax determined by applying the statutory federal income tax rate to pretax income as a result of the following differences for years ended December 31:

	2008	2007	2006
Federal tax at statutory rate	$ 60,322	$ 60,407	$ 54,371
State tax, net	7	—	20
Effect of nontaxable entities	(59,080)	(56,265)	(50,244)
Valuation allowance	1,934	814	4,944
Patronage distributions	(3,739)	(4,302)	(6,830)
Capital download to associations	(195)	(351)	(727)
Other, net	1,095	(162)	(1,762)
Total provision for (benefit from) income taxes	$ 344	$ 141	$ (228)

Deferred tax assets and liabilities comprised the following elements at December 31:

	2008	2007	2006
Allowance for loan losses	$ 5,392	$ 3,685	$ 2,912
Allowance for acquired property	32	—	—
Postretirement benefits	3,632	3,490	4,334
Net operating loss carryforward	2,659	2,982	2,429
Other	808	274	167
Gross deferred tax assets	12,523	10,431	9,842
Less valuation allowance	(10,292)	(8,357)	(7,543)
Adjusted gross deferred tax assets	2,231	2,074	2,299
FCBT stock redemption	(313)	(508)	(859)
Other	(97)	(98)	(99)
Gross deferred tax liabilities	(410)	(606)	(958)
Net deferred tax assets	$ 1,821	$ 1,468	$ 1,341

The bank and its related associations adopted the provisions of the Financial Accounting Standards Board Interpretation No. 48, "Accounting for Uncertainty in Income Taxes," on January 1, 2007. There were no uncertain tax positions and related liabilities for unrecognized tax benefits recorded at December 31, 2008. Any penalties and interest related to income taxes would be accounted for as an adjustment to income tax expense.

Note 10 — Employee Benefit Plans

Employees of the bank participate in either the district's defined benefit retirement plan (DB plan) or in a non-elective defined contribution feature (DC plan) within the Farm Credit Benefits Alliance 401(k) plan. In addition, all employees are eligible to participate in the Farm Credit Benefits Alliance 401(k) plan.

The DB plan is noncontributory, and benefits are based on salary and years of service. The "projected unit credit" actuarial method is used for both financial reporting and funding purposes. District employers have the option of providing enhanced retirement benefits, under certain conditions, within the DB plan in 1998 and beyond, to facilitate reorganization and/or restructuring. Under SFAS No. 88, there were no pension plan termination benefits recognized resulting from employees who qualified for an early retirement option under a retention plan at December 31, 2008 as compared to $320 and $103 during the years ended December 31, 2007 and 2006, respectively. Additionally, certain qualified individuals in the bank may participate in a separate, nonqualified defined benefit supplemental pension plan.

Participants in the DC plan generally include employees who elected to transfer from the DB plan prior to January 1, 1996, and employees hired on or after January 1, 1996. Participants in the non-elective pension feature of the DC plan direct the placement of their employers' contributions made on their behalf into various investment alternatives. Employer contributions to the DC plan were $4.7 million, $3.4 million and $3.1 million for the years ended December 31, 2008, 2007 and 2006, respectively.

The district also participates in the Farm Credit Benefits Alliance 401(k) plan, which offers a pre-tax and after-tax compensation deferral feature. Employers match 100 percent of employee contributions for the first 3 percent of eligible compensation and then match 50 percent of employee contributions on the next 2 percent of eligible compensation, for a maximum employer contribution of 4 percent of eligible compensation. Employer contributions were $3.1 million, $2.8 million and $2.5 million for the years ended December 31, 2008, 2007 and 2006, respectively. Additionally, certain qualified individuals may participate in separate nonqualified supplemental 401(k) plans managed by their employer.

The bank and associations also provide certain health care benefits to eligible retired employees, beneficiaries and directors (retiree medical plan).

In September 2006, the FASB issued SFAS No. 158, "Employers' Accounting for Defined Benefit Pension and Other Postretirement Plans," which required the recognition of the overfunded or underfunded status of pension and other postretirement benefit plans on the balance sheet. The balance sheet recognition provisions of SFAS 158 were adopted at December 31, 2007. SFAS 158 also requires that employers measure the benefit obligation and plan assets as of the fiscal year end for fiscal years ending after December 15, 2008. In fiscal 2007 and earlier, the System used a September 30 measurement date for pension and other postretirement benefit plans. The Standard provides two approaches for an employer to transition to a fiscal year-end measurement date. The System has applied the second approach, which allows for the use of the measurements determined for the prior year end.

Under this alternative, pension and postretirement benefit income measured for the three-month period October 1, 2007 to December 31, 2007 (determined using the September 2007 measurement date) was recorded as an adjustment to beginning 2008 retained earnings. As a result, the bank and related associations decreased retained earnings $2.7 million, net of taxes, and increased the pension and other postretirement benefit liabilities by $2.7 million.

The following table reflects the benefit obligation, cost and actuarial assumptions for the district's pension and other postretirement benefit plans:

	Pension Benefits			Other Postretirement Benefits		
	2008	2007	2006	**2008**	2007	2006
Accumulated benefit obligation, end of year	**$ 205,854**	$ 190,594	$ 182,784			
Change in projected benefit obligation						
Benefit obligation, beginning of year	**$ 242,007**	$ 230,244	$ 221,954	**$ 36,811**	$ 38,489	$ 38,730
Service cost	**6,987**	5,209	5,304	**1,331**	1,235	1,404
Interest cost	**19,304**	13,549	11,441	**2,937**	2,271	2,004
Plan participants' contributions	**0**	0	0	**497**	365	346
Plan amendments	**0**	0	3,337	**(658)**	0	411
Settlements	**(458)**	0	0	**0**	0	0
Special termination benefits	**0**	320	103	**0**	0	0
Actuarial loss (gain)	**12,993**	1,424	(4,148)	**1,367**	(3,969)	(3,047)
Benefits paid	**(26,887)**	(8,740)	(7,747)	**(1,994)**	(1,580)	(1,359)
Projected benefit obligation, end of year	**$ 253,946**	$ 242,006	$ 230,244	$ **40,291**	$ 36,811	$ 38,489
Change in plan assets						
Plan assets at fair value, beginning of year	**$ 169,954**	$ 152,936	$ 141,851	$ **0**	$ 0	$ 0
Actual return on plan assets	**(52,254)**	19,206	11,745	**0**	0	0
Company contributions	**23,350**	6,552	7,087	**1,497**	1,215	1,013
Plan participants' contributions	**0**	0	0	**497**	365	346
Benefits paid	**(26,887)**	(8,740)	(7,747)	**(1,994)**	(1,580)	(1,359)
Plan assets at fair value, end of year	**$ 114,163**	$ 169,954	$ 152,936	$ **0**	$ 0	$ 0
Reconciliation of funded status						
Unfunded status	**$ (139,783)**	$ (72,052)	$ (77,308)	$ **(40,291)**	$ (36,811)	$ (38,489)
Unrecognized prior service cost	**N/A**	N/A	4,593	**N/A**	N/A	(16,438)
Unrecognized net loss (gain)	**N/A**	N/A	49,313	**N/A**	N/A	4,729
Contributions between measurement date and fiscal year end	**N/A**	0	103	**N/A**	264	248
Net benefit liability at end of year	**$ (139,783)**	$ (72,052)	$ (23,299)	**$ (40,291)**	$ (36,547)	$ (49,950)
Amounts recognized consist of:						
Accrued liability	**$ 0**	$ 0	$ (23,299)	**$ 0**	$ 0	$ (49,950)
Minimum pension liability adjustment	**0**	0	(6,446)	**0**	0	0
Intangible asset	**0**	0	1,515	**0**	0	0
Deferred income tax assets	**0**	0	0	**(128)**	(431)	0
Net benefit liability at end of year	**(139,783)**	(72,052)	0	**(40,291)**	(36,547)	0
Accumulated other comprehensive loss (income)	**119,775**	44,056	4,931	**(10,992)**	(13,473)	0

	Pension Benefits			Other Postretirement Benefits		
	2008	2007	2006	**2008**	2007	2006
Amounts recognized in accumulated other comprehensive income						
Additional minimum pension liability adjustment	**$ 0**	$ 0	$ 1,853	**$ 0**	$ 0	$ 0
Net actuarial loss (gain)	**117,345**	40,608	N/A	**2,003**	668	N/A
Prior service cost (credit)	**2,430**	3,448	N/A	**(12,995)**	(14,141)	N/A
Total	**$ 119,775**	$ 44,056	$ 1,853	**$ (10,992)**	$ (13,473)	$ 0

A funding policy adopted in 2007 establishes contribution requirements for the district's DB plan if plan assets are less than the accumulated benefit obligation at year end. The policy calls for contributions equal to the value of the additional benefits expected to be earned by employees during the year plus a payment on the shortfall between the accumulated benefit obligation and the plan assets. The additional payments for any shortfall are intended to fund the shortfall over the next five years.

The following table discloses the excess of the DB plan's accumulated benefit obligation over its plan assets at December 31,

	2008	2007	2006
District DB plan assets at fair value	**$ 114,163**	$ 169,954	$ 152,936
Accumulated benefit obligation of district DB plan	**203,053**	185,918	179,083
Funding shortfall	**$ (88,890)**	$ (15,964)	$ (26,147)

In accordance with this policy, a contribution of $31,985 was made to the plan in January 2009. The supplemental (nonqualified) pension plan is not funded. The projected benefit obligation and accumulated benefit obligation for the supplemental pension plan at December 31, 2008, were $5,219 and $2,801, respectively.

	Pension Benefits			Other Postretirement Benefits		
	2008	2007	2006	**2008**	2007	2006
Net periodic benefit cost						
Service cost	**$ 5,590**	$ 5,209	$ 5,304	**$ 1,235**	$ 1,235	$ 1,404
Interest cost	**15,443**	13,549	11,441	**2,271**	2,271	2,004
Expected return on plan assets	**(14,143)**	(12,249)	(11,443)	**0**	0	0
Amortization of:						
Prior service cost	**814**	1,144	1,050	**(1,844)**	(1,844)	(1,919)
Net actuarial loss	**2,051**	3,171	4,286	**71**	71	262
Net periodic benefit cost	**$ 9,755**	$ 10,824	$ 10,638	$ **1,733**	$ 1,733	$ 1,751
Settlement expense	**3,168**	0	0	**0**	0	0
Special termination benefits	**0**	320	103	**0**	0	0
Total benefit cost	**$ 12,923**	$ 11,144	$ 10,741	$ **1,733**	$ 1,733	$ 1,751
Adjustment to retained earnings for 2008 due to change in measurement date	**$ 2,439**			$ **272**		
Other changes to plan assets and projected benefit obligations recognized in other comprehensive income						
Net actuarial loss (gain)	**$ 82,469**	N/A	N/A	$ **1,218**	N/A	N/A
Amortization of net actuarial loss (gain)	**(2,564)**	N/A	N/A	**(20)**	N/A	N/A
Settlement expense	**(3,168)**	N/A	N/A	**(5)**	N/A	N/A
Prior service costs	**0**	N/A	N/A	**(586)**	N/A	N/A
Amortization of prior service costs	**(1,018)**			**1,872**		
Termination recognition of prior service costs	**0**	N/A	N/A	**4**	N/A	N/A
Net change	**$ 75,719**	N/A	N/A	**$ 2,483**	N/A	N/A
AOCI amounts expected to be amortized in 2009						
Prior service cost (credit)	**$ 390**			**$ (1,681)**		
Net actuarial loss (gain)	**12,120**			**18**		
Total	**$ 12,510**			**$ (1,663)**		
Weighted-average assumptions used to determine benefit obligation as of December 31						
Measurement date	**12/31/2008**	9/30/2007	9/30/2006	**12/31/2008**	9/30/2007	9/30/2006
Discount rate	**6.30%**	6.50%	6.00%	**6.30%**	6.50%	6.00%
Rate of compensation increase	**7% in 2009 down to 4% in 2012**	8% in 2008 down to 4% in 2012	9% in 2007 down to 4% in 2012			
Health care cost trend rate assumed for next year (pre/post-65)-medical				**8.5%/6.25%**	8.5%/6.5%	9.0%/6.75%
Health care cost trend rate assumed for next year (pre/post-65)-prescriptions				**11.00%**	12.00%	13.00%
Ultimate health care cost trend rate				**5.00%**	4.75%	4.75%
Year that the rate reaches the ultimate trend rate				**2015**	2016	2016

	Pension Benefits			Other Postretirement Benefits		
	2008	2007	2006	**2008**	2007	2006
Weighted-average assumptions used to determine net periodic cost for year ended December 31						
Measurement date	**9/30/2007**	9/30/2006	9/30/2005	**9/30/2007**	9/30/2006	9/30/2005
Discount rate	**6.50%**	6.00%	5.25%	**6.50%**	6.00%	5.25%
Expected return on plan assets	**8.00%**	8.00%	8.00%	**N/A**	N/A	N/A
Rate of compensation increase	**8% in 2008 down to 4% in 2012**	9% in 2007 down to 4% in 2012	4.50%			
Health care cost trend rate assumed for next year (pre/post-65)-medical				**8.5%/6.5%**	9.0%/6.75%	9.5%/7.0%
Health care cost trend rate assumed for next year (pre/post-65)-prescriptions				**12.00%**	13.00%	13.50%
Ultimate health care cost trend rate				**4.75%**	4.75%	4.75%
Year that the rate reaches the ultimate trend rate				**2016**	2016	2016
Effect of Change in Assumed Heath Care Cost Trend Rates						
Effect on total service cost and interest cost components						
One-percentage point increase				**$ 690**		
One-percentage point decrease				**(551)**		
Effect on year-end postretirement benefit obligation						
One-percentage point increase				**$ 6,440**		
One-percentage point decrease				**(5,242)**		
Expected Future Cash Flow Information						
Expected Benefit Payments						
Fiscal 2009	**$ 10,316**			**$ 1,293**		
Fiscal 2010	**11,606**			**1,453**		
Fiscal 2011	**12,658**			**1,590**		
Fiscal 2012	**14,991**			**1,713**		
Fiscal 2013	**15,122**			**1,881**		
Fiscal 2014 - 2018	**95,904**			**11,460**		
Expected Contributions						
Fiscal 2009	**$ 32,448**			**$ 1,293**		

Plan Assets	Pension Benefits				Other Postretirement Benefits			
Asset Category	Target	**2008**	2007	2006	Target	**2008**	2007	2006
Equity securities	60%	**60%**	60%	60%	0%	**0%**	0%	0%
Debt securities	40	**40**	40	40	0	**0**	0	0
Cash/other	0	**0**	0	0	100	**100**	100	100
Total	100%	**100%**	100%	100%	100%	**100%**	100%	100%

As disclosed above, the expected total contributions for 2009 was $32.4 million, which is $9.1 million greater than contributions for 2008. The significant decline in the plan's actual return on plan assets for 2008 reflects the adverse effects of the global financial markets during the year, necessitating the increase in expected contributions. The plan's investment results in 2008, and general economic trends and their effects on the plan's investment portfolio in 2009 will affect the level of contributions required to fund the plan. Investment results have also resulted in a significant increase in expected defined benefit pension costs for 2009 and beyond.

Notwithstanding current investment market conditions, the expected long-term rate of return assumption is determined independently for each defined benefit pension plan and for each other postretirement benefit plan. Generally, plan trustees use historical return information to establish a best-estimate range for each asset class in which the plans are invested. Plan trustees select the most appropriate rate for each plan from the best-estimate range, taking into consideration the duration of plan benefit liabilities and plan sponsor investment policies.

Note 11 — Related Party Transactions

In the ordinary course of business, the bank and associations have entered into loan transactions with directors, officers and other employees of the bank or associations and other organizations with which such persons may be associated. Total loans to such persons at December 31, 2008, amounted to $179.2 million. In the opinion of management, such loans outstanding to directors, officers and other employees at December 31, 2008, did not involve more than a normal risk of collectibility and were subject to approval requirements contained in FCA regulations and were made on the same terms, including interest rates, amortization schedules and collateral, as those prevailing at the time for comparable transactions with unrelated borrowers. Disclosures on individual associations' officers and directors are found in the associations' individual annual reports.

Note 12 — Commitments and Contingencies

In the normal course of business, the bank and associations have various outstanding commitments and contingent liabilities as discussed elsewhere in these notes. For a discussion of commitments to extend credit and standby letters of credit issued, see Note 13, "Financial Instruments With Off-Balance-Sheet Risk."

The bank is primarily liable for its portion of Systemwide debt obligations. Additionally, the bank is jointly and severally liable for the consolidated Systemwide bonds and notes of other System banks. The total bank and consolidated Systemwide debt obligations of the System at December 31, 2008, were approximately $178.4 billion.

Other actions are pending against the bank and associations in which claims for monetary damages are asserted. Upon the basis of current information, management and legal counsel are of the opinion that the ultimate liability, if any resulting therefrom, will not be material in relation to the combined financial position or results of operations of the bank and associations.

Note 13 — Financial Instruments With Off-Balance-Sheet Risk

The bank and associations may participate in financial instruments with off-balance-sheet risk to satisfy the financing needs of their borrowers and to manage their exposure to interest rate risk. In the normal course of business, various commitments are made to customers, including commitments to extend credit and standby letters of credit, which represent credit-related financial instruments with off-balance-sheet risk.

At any time, the bank and associations have outstanding a significant number of commitments to extend credit. The bank and associations also provide standby letters of credit to guarantee the performance of customers to third parties. Commitments to extend credit are agreements to lend to a borrower as long as there is not a violation of any condition established in the contract. Commitments and letters of credit generally have fixed expiration dates or other termination clauses and may require payment of a fee. Credit-related financial instruments have off-balance-sheet credit risk, because only origination fees (if any) are recognized in the combined balance sheets (as other liabilities) for these instruments until the commitments are fulfilled or expire. Since many of the commitments are expected to expire without being drawn upon, the total commitments do not necessarily represent future cash requirements. The district's commitments to extend credit totaled $3.320 billion, $3.076 billion and $2.871 billion at December 31, 2008, 2007 and 2006, respectively. At December 31, 2008, the district had $194.0 million in outstanding standby letters of credit, issued primarily in conjunction with participation loans. The letters of credit are generally issued for terms up to one year or are annually renewable. The fair value of these obligations is $1.9 million, based on the fees for the unexpired period remaining.

The credit risk involved in issuing commitments and letters of credit is essentially the same as that involved in extending loans to customers, and the same credit policies are applied by management. In the event of funding, the credit risk amounts are equal to the contract amounts, assuming that counterparties fail completely to meet their obligations and the collateral or other security is of no value. The amount of collateral obtained, if deemed necessary upon extension of credit, is based on management's credit evaluation of the counterparty.

Note 14 — Fair Value Measurements

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. See Note 2, "Summary of Significant Accounting Policies," for additional information.

Assets and liabilities measured at fair value on a recurring basis at December 31, 2008 for each of the fair value hierarchy values are summarized below:

	Fair Value Measurement at December 31, 2008			
	Total	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Assets:				
Federal funds and securities purchased under resale agreements	**$ 176,698**	$ —	$ 176,698	$ —
Investments available-for-sale	**2,995,857**	—	2,895,865	99,992
Derivative assets	**31,439**	—	31,439	—
Assets held in non-qualified benefit trusts	**746**	746	—	—
Total assets	**$ 3,204,740**	$ 746	$ 3,104,002	$ 99,992
Liabilities:				
Derivative liabilities	**$ 3,074**	$ —	$ 3,074	$ —
Standby letters of credit	**1,901**	—	1,901	—
Collateral liabilities	**1,080**	—	1,080	—
Total liabilities	**$ 6,055**	$ —	$ 6,055	$ —

The table below represents a reconciliation of all Level 3 assets and liabilities measured at fair value on a recurring basis for the year ended December 31, 2008:

	Level 3 Assets and Liabilities
	Investment Securities
Balance at January 1, 2008	$ 273,231
Net gains included in other comprehensive income	864
Purchases, issuances and settlements	(112,973)
Net transfers from Level 3	(61,130)
Balance at December 31, 2008	$ 99,992
The amount of gains or losses for the period included in earnings attributable to the change in unrealized gains or losses relating to assets or liabilities still held at December 31, 2008	$ 2,238

Assets and liabilities measured at fair value on a nonrecurring basis at December 31, 2008 for each of the fair value hierarchy values are summarized below:

	Fair Value Measurement at December 31, 2008			
	Total	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Assets:				
Loans	$ 85,248	$ —	$ —	$ 85,248
Other property owned	6,495			6,495
Total assets	$ 91,743	$ —	$ —	$ 91,743

Valuation Techniques

As more fully discussed in Note 2, "Summary of Significant Accounting Policies," SFAS No. 157 establishes a fair value hierarchy, which requires an entity to maximize the use of observable inputs and minimize the use of unobservable inputs when measuring fair value. The following represent a brief summary of the valuation techniques used by the bank and associations for assets and liabilities:

Investment Securities

Where quoted prices are available in an active market, available-for-sale securities would be classified as Level 1. If quoted prices are not available in an active market, the fair value of securities is estimated using pricing models that utilize observable inputs, quoted prices for similar securities received from pricing services or discounted cash flows. Generally, these securities would be classified as Level 2. Among other securities, this would include certain mortgage-backed securities and asset-backed securities. Where there is limited activity or less transparency around inputs to the valuation, the securities are classified as Level 3. Securities classified within Level 3 include commercial paper at December 31, 2008. At January 1, 2008, Level 3 securities included commercial paper and certain asset-backed securities.

Assets Held in Non-Qualified Benefits Trusts

Assets held in trust funds related to deferred compensation and supplemental retirement plans are classified within Level 1. The trust funds include investments in mutual funds.

Derivatives

Exchange-traded derivatives valued using quoted prices would be classified within Level 1 of the valuation hierarchy. However, few classes of derivative contracts are listed on an exchange; thus, the majority of the derivative positions are valued using internally developed models that use as their basis readily observable market parameters and are classified within Level 2 of the valuation hierarchy. Such derivatives include basic interest rate swaps and cash flow derivatives.

Loans

On a nonrecurring basis, specific allowances for loan losses on certain collateral-dependent impaired loans have been recorded to effectively measure the loans, net of their specific allowances, at the fair value of the collateral on which repayment is deemed to be dependent. At December 31, 2008, impaired loans with a fair value of $85,248 were included in loans.

In accordance with SFAS No. 15, "Accounting by Debtors and Creditors for Troubled Debt Restructurings," assets acquired in loan foreclosures are recorded at fair value, less estimated costs of sale. At December 31, 2008, foreclosed assets with a fair value of $6,495 are included in other property owned.

Note 15 — Disclosure About the Fair Value of Financial Instruments

The following table presents the carrying amounts and estimated fair values of the district's financial instruments at December 31, 2008, 2007 and 2006.

The estimated fair values of the district's financial instruments follow:

	December 31, 2008		December 31, 2007		December 31, 2006	
	Carrying Amount	**Fair Value**	Carrying Amount	Fair Value	Carrying Amount	Fair Value
Financial assets						
Cash, federal funds sold, securities purchased under resale agreements and investment securities	**$ 3,279,977**	**$ 3,281,080**	$ 2,592,204	$ 2,592,204	$ 2,821,641	$ 2,821,641
Loans	**16,590,071**	**17,122,656**	15,114,537	15,041,574	12,905,321	12,706,284
Allowance for loan losses	**(51,653)**	**—**	(24,495)	—	(13,969)	—
Loans, net	**16,538,418**	**17,122,656**	15,090,042	15,041,574	12,891,352	12,706,284
Derivative assets	**31,439**	**31,439**	7,034	7,034	1,758	1,758
Financial liabilities						
Bonds and notes	**17,305,279**	**17,587,310**	15,324,193	15,439,340	13,524,243	13,521,813
Fair value adjustment of derivatives	**(3,074)**	**(3,074)**	(178)	(178)	(3,459)	(3,459)
Total bonds and notes, net	**17,302,205**	**17,584,236**	15,324,015	15,439,162	13,520,784	13,518,354
Subordinated debt	**50,000**	**56,168**	—	—	—	—
Derivative liabilities	**3,074**	**3,074**	178	178	3,459	3,459

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

A. Cash, Federal Funds Sold, and Securities Purchased Under Resale Agreements:

The carrying value is a reasonable estimate of fair value.

B. Investment Securities:

Investment securities: If an active market exists, the fair value is based on currently quoted market prices. For those securities for which an active market does not exist, the fair value is determined as described in Note 14, "Fair Value Measurements."

C. Loans:

Because no active market exists for the district's loans, fair value is estimated by discounting the expected future cash flows using the bank's and/or the associations' current interest rates at which similar loans would be made to borrowers with similar credit risk. As the discount rates are based on the district's loan rates as well as on management estimates, management has no basis to determine whether the fair values presented would be indicative of the value negotiated in an actual sale.

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

Fair value of loans in a nonaccrual status which are current as to principal and interest is estimated as described above, with appropriately higher discount rates to reflect the uncertainty of continued cash flows. For noncurrent nonaccrual loans, it is assumed that collection will result only from the disposition of the underlying collateral. Fair value of these loans is estimated to equal the aggregate net realizable value of the underlying collateral, discounted at an interest rate which appropriately reflects the uncertainty of the expected future cash flows over the average disposal period. Where the net realizable value of the collateral exceeds the legal obligation for a particular loan, the legal obligation is generally used in place of net realizable value.

D. Bonds and Notes:

Systemwide bonds and notes are not regularly traded; thus, quoted market prices are not available. Fair value of these instruments is estimated by discounting expected future cash flows based on the quoted market price of new issues of Systemwide bonds with similar-maturity terms.

E. Subordinated Debt:

As discussed in Note 7, "Bonds and Notes," the bank issued subordinated debt in 2008. The fair value of these obligations is determined by discounting expected future cash flows based on the Treasury yield curve.

F. Derivative Assets and Liabilities:

The fair value of derivative financial instruments is the estimated amount that a bank would receive or pay to replace the instruments at the reporting date, considering the current interest rate environment and the current creditworthiness of the counterparties. Where such quoted market prices do not exist, these values are generally provided by sources outside the respective bank or by internal market valuation models.

G. Commitments to Extend Credit:

Fees on commitments to extend credit are not normally assessed; hence, there is no fair value to be assigned to these commitments until they are funded.

Note 16 — Derivative Instruments and Hedging Activity

The bank maintains an overall interest rate risk management strategy that incorporates the use of derivative instruments to minimize significant unplanned fluctuations in earnings that are caused by interest rate volatility. The bank's goal is to manage interest rate sensitivity by modifying the repricing or maturity characteristics of certain balance sheet liabilities so that the net interest margin is not adversely affected by movements in interest rates. As a result of interest rate fluctuations, hedged fixed-rate liabilities will appreciate or depreciate in market value. The effect of this unrealized appreciation or depreciation is expected to be substantially offset by the district's gains or losses on the derivative instruments that are linked to these hedged liabilities. Another result of interest rate fluctuations is that the interest expense of hedged variable-rate liabilities will increase or decrease. The effect of this variability in earnings is expected to be substantially offset by the bank's gains and losses on the derivative instruments that are linked to these hedged liabilities. The bank considers its strategic use of derivatives to be a prudent method of managing interest rate sensitivity, as it prevents earnings from being exposed to undue risk posed by changes in interest rates.

The bank enters into derivatives, particularly fair value and cash flow interest rate swaps, primarily to lower interest rate risk. Fair value hedges allow the bank to raise long-term borrowings at fixed rates and swap them into floating rates that are lower than those available to the bank if floating-rate borrowings were made directly. Under fair value hedge arrangements, the bank agrees with other parties to exchange, at specified intervals, payment streams calculated on a specified notional principal amount, with at least one stream based on a specified floating-rate index. At December 31, 2008, the bank had four fair value hedges with a total notional amount of $350 million.

The bank's interest-earning assets (principally loans and investments) tend to be medium-term floating-rate instruments, while the related interest-bearing liabilities tend to be short- or medium-term fixed-rate obligations. Given this asset-liability mismatch, fair value hedges in which the bank pays the floating rate and receives the fixed rate (receive fixed swaps) are used to reduce the impact of market fluctuations on the bank's net interest income.

At December 31, 2008, the bank had four cash flow hedges, with a total notional amount of $450 million, which hedge the exposure to variability in expected future cash flows.

By using derivative instruments, the bank exposes itself to credit and market risk. If a counterparty fails to fulfill its performance obligations under a derivative contract, the bank's credit risk will equal the fair value gain of the derivative. Generally, when the fair value of a derivative contract is positive, this indicates that the counterparty owes the bank, thus creating a repayment risk for the bank. When the fair value of the derivative contract is negative, the bank owes the counterparty and, therefore, assumes no repayment risk.

To minimize the risk of credit losses, the bank maintains collateral agreements to limit exposure to agreed upon thresholds; the bank deals with counterparties that have an investment grade or better credit rating from a major rating agency; and the bank also monitors the credit standing of, and levels of exposure to, individual counterparties. The bank typically enters into master agreements that contain netting provisions. These provisions allow the bank to require the net settlement of covered contracts with the same counterparty in the event of default by the counterparty on one or more contracts. At December 31, 2008, the bank had credit exposure totaling $32.1 million, net of $1.1 million in collateral held, with three counterparties. The bank does not anticipate nonperformance by these counterparties.

The table below presents the credit ratings of counterparties to whom the bank has credit exposure:

	Remaining Years to Maturity						
(dollars in millions)	Less Than One Year	Over Five Years	Total	Maturity Distribution Netting	Exposure	Collateral Held	Exposure Net of Collateral
Moody's Credit Rating							
Aaa	(1.4)	16.7	15.3	—	15.3	—	15.3
Aaa	0.6	16.7	17.3	—	17.3	1.1	16.2
Aa2	0.6	—	0.6	—	0.6	—	0.6

The bank's derivative activities are monitored by its Asset-Liability Management Committee (ALCO) as part of the ALCO's oversight of the bank's asset/liability and treasury functions. The ALCO is responsible for approving hedging strategies that are developed through its analysis of data derived from financial simulation models and other internal and industry sources. The resulting hedging strategies are then incorporated into the district's overall interest rate risk-management strategies. The bank enters into interest rate swaps classified as fair value hedges primarily to convert a portion of its non-prepayable fixed-rate long-term debt to floating-rate debt.

The table below provides information about derivative financial instruments and other financial instruments that are sensitive to changes in interest rates, including debt obligations and interest rate swaps. The debt information below presents the principal cash flows and related weighted average interest rates by expected maturity dates. The derivative information below represents the notional amounts and weighted average interest rates by expected maturity dates.

December 31, 2008 (dollars in millions)	Maturities of 2008 Derivative Products and Other Financial Instruments 2009	2010	2011	2012	2013	Subsequent Years	Total	Fair Value
Total debt obligations:								
Fixed rate	$ 4,436	$ 1,614	$ 1,391	$ 715	$ 1,393	$ 2,678	$ 12,227	$ 12,509
Weighted average interest rate	2.60%	3.98%	3.73%	4.29%	4.28%	5.22%	3.77%	
Variable rate	$ 4,975	$ 100	$ —	$ —	$ —	$ —	$ 5,075	$ 5,075
Weighted average interest rate	2.52%	1.83%	—	—	—	—	2.51%	
Total debt obligations	$ 9,411	$ 1,714	$ 1,391	$ 715	$ 1,393	$ 2,678	$ 17,302	$ 17,584
Weighted average interest rate	2.56%	3.85%	3.73%	4.29%	4.28%	5.22%	3.40%	
Derivative instruments:								
Receive fixed swaps								
Notional value	$ 200	$ —	$ —	$ —	$ —	$ 150	$ 350	$ 31
Weighted average receive rate	2.60%	—	—	—	—	4.95%	3.61%	
Weighted average pay rate	0.92%	—	—	—	—	0.83%	0.88%	
Pay fixed swaps								
Notional value	$ 450	$ —	$ —	$ —	$ —	$ —	$ 450	$ (3)
Weighted average receive rate	1.90%	—	—	—	—	—	1.90%	
Weighted average pay rate	3.91%	—	—	—	—	—	3.91%	

Note 17 — Selected Quarterly Financial Information (Unaudited)

Quarterly results of operations are shown below for the years ended December 31:

	2008 First	Second	Third	Fourth	Total
Net interest income	**$ 114,007**	**$ 116,240**	**$ 120,642**	**$ 119,539**	**$ 470,428**
Provision for loan losses	**8,410**	**6,663**	**12,431**	**26,010**	**53,514**
Noninterest expense, net	**35,844**	**34,318**	**34,866**	**44,158**	**149,186**
Net income	**$ 69,753**	**$ 75,259**	**$ 73,345**	**$ 49,371**	**$ 267,728**

	2007 First	Second	Third	Fourth	Total
Net interest income	$ 105,570	$ 106,186	$ 110,290	$ 110,335	$ 432,381
Provision for loan losses	1,242	25,778	8,333	7,778	43,131
Noninterest expense, net	37,275	36,107	35,794	37,534	146,710
Net income	$ 67,053	$ 44,301	$ 66,163	$ 65,023	$ 242,540

	2006 First	Second	Third	Fourth	Total
Net interest income	$ 92,571	$ 93,777	$ 97,464	$ 102,434	$ 386,246
Provision for loan losses	973	3,931	1,677	2,775	9,356
Noninterest expense, net	35,029	31,302	32,050	38,391	136,772
Net income	$ 56,569	$ 58,544	$ 63,737	$ 61,268	$ 240,118

Note 18 — Bank-Only Financial Data

Condensed financial information for the bank follows. All significant transactions and balances between the bank and associations are eliminated in combination. The multi-employer structure of the district's defined benefit plan results in the recording of this plan only upon combination.

Balance Sheet Data	December 31, **2008**	2007	2006
Cash, federal funds sold and securities purchased under resale agreements	**$ 189,791**	$ 142,102	$ 103,394
Investment securities	**3,028,468**	2,410,999	2,672,242
Loans			
To associations	**8,402,595**	8,058,130	7,815,233
To others	**3,000,518**	2,807,861	2,240,195
Less allowance for loan losses	**12,549**	1,065	142
Net loans	**11,390,564**	10,864,926	10,055,286
Accrued interest receivable	**63,632**	66,789	63,967
Other assets	**88,046**	35,962	20,871
Total assets	**$ 14,760,501**	$ 13,520,778	$ 12,915,760
Bonds and notes	**$ 13,852,205**	$ 12,624,015	$ 12,120,783
Other liabilities	**163,754**	168,162	130,756
Total liabilities	**14,015,959**	12,792,177	12,251,539
Preferred stock	**200,000**	200,000	200,000
Capital stock	**227,212**	198,864	161,421
Retained earnings	**343,113**	334,394	324,270
Accumulated other comprehensive loss	**(25,783)**	(4,657)	(21,470)
Total members' equity	**744,542**	728,601	664,221
Total liabilities and members' equity	**$ 14,760,501**	$ 13,520,778	$ 12,915,760

Statement of Income Data	Year Ended December 31, **2008**	2007	2006
Interest income	**$ 660,690**	$ 753,541	$ 652,557
Interest expense	**541,294**	653,976	562,216
Net interest income	**119,396**	99,565	90,341
Provision for loan losses	**20,529**	1,043	2,578
Net interest income after provision for loan losses	**98,867**	98,522	87,763
Noninterest income	**33,900**	22,116	17,847
Other expense	**56,034**	46,634	40,616
Net income	**$ 76,733**	$ 74,004	$ 64,994

Disclosure Information and Index

Disclosures Required by Farm Credit Administration Regulations

Description of Business

The Farm Credit Bank of Texas (FCBT or bank), Agricultural Credit Associations (ACAs) and the Federal Land Credit Associations (FLCAs) of the Tenth Farm Credit District (district) are member-owned cooperatives which provide credit and credit-related services to or for the benefit of eligible borrower-shareholders for qualified agricultural purposes in the states of Alabama, Louisiana, Mississippi, New Mexico and Texas. The district's ACA parent associations, which each contain wholly-owned FLCA and Production Credit Association (PCA) subsidiaries, and FLCAs are collectively referred to as associations. A further description of territory served, persons eligible to borrow, types of lending activities engaged in, financial services offered and related Farm Credit organizations required to be disclosed in this section are incorporated herein by reference to Note 1, "Organization and Operations," to the accompanying combined financial statements.

The description of significant developments that had or could have a material impact on results of operations or interest rates to borrowers, acquisitions or dispositions of material assets, material changes in the manner of conducting business, seasonal characteristics and concentrations of assets, if any, required to be disclosed in this section are incorporated herein by reference to "Management's Discussion and Analysis" of the district included in this annual report to stockholders.

Directors and Senior Officers

The following represents certain information regarding the district directors and senior officers of the bank as of February 27, 2009:

DIRECTORS

Ralph W. Cortese joined the board in 1995, and his current term expires December 31, 2010. Cortese has served as chairman since 2000. Prior to joining the bank board, Cortese was chairman of the PCA of Eastern New Mexico Board of Directors. Early in his career, he was vice president of Roswell PCA. He is a farmer and rancher from Fort Sumner, New Mexico. In 2001, he joined the American Land Foundation Board. He is a member of the bank's Audit and Compensation committees. In June 2003, he was appointed to the Farmer Mac Board with an appointment which expired in 2008. He is also a member of the Texas Agricultural Cooperative Council board of directors.

Jon M. Garnett began his first term on the board in 1999, and his current term expires December 31, 2010. He served as board vice chairman from 2000 through 2008. Prior to joining the bank board, he was chairman of Panhandle-Plains Land Bank, FLCA Board of Directors. In January 2003, he joined the national Farm Credit Council Board of Directors as a Tenth District representative and is a member of the Farm Credit Council Board of Directors' legislative committee. He is also a member of the bank's Audit Committee and the State Technical Committee for the Natural Resources Conservation Service, and is the chairman of the bank's Compensation Committee. Garnett raises grain and forage crops and runs stocker cattle near Spearman, Texas.

C. Kenneth Andrews began service on the board in 1994, and his current term expired December 31, 2008. He was manager of the former FLBA of Madisonville for 17 years and later served on the board of directors of the FLBA of Bryan. The Madisonville, Texas, rancher was a member of the Tenth District Farm Credit Council and represented the district on the national Farm Credit Council Board of Directors from 1996 to 2005. He also served on the bank's Audit and Compensation committees. Andrews retired from the bank's board upon the expiration of his term.

Joe R. Crawford began his first term on the board in 1998, and his current term expires December 31, 2009. Previously, he was a member of the FLBA of North Alabama Board of Directors. He also served on the Tenth District FLBA Legislative Advisory Committee. Vice chairman of the bank's Audit Committee, Crawford also serves on the bank's Compensation Committee. He is a director on the board and an audit committee member of the Federal Farm Credit Banks Funding Corporation. He is also a member and past president of the Alabama Cattlemen's Association and a member of the National Cattlemen's Beef Association, the Alabama Farm Bureau and the Alabama Farmers Federation. Crawford, who lives near Baileyton, Alabama, has owned and operated a cattle business since 1968.

James F. Dodson joined the board of directors in January 2003, and his current term expired December 31, 2008. Dodson was reelected to the board with his new term expiring December 31, 2011. He is a past chairman of the Texas AgFinance, FCS Board of Directors and a former member of the Tenth Farm Credit District Stockholders' Advisory Committee. He is chairman of the Tenth District Farm Credit Council board and serves on the bank's Audit and Compensation committees. Dodson grows cotton and milo and operates a seed sales business with his family in Robstown, Texas. He is the president of Dodson Farms, Inc. and Dodson Ag, Inc.; the owner of Jimmy Dodson Farms; a partner in Weber Greene, Ltd.; and managing partner in Weber Station LLC. In addition, Dodson serves on the boards of Gulf Coast Cooperative and South Texas Cotton and Grain Association, and holds leadership positions in the National Cotton Council of America and American Cotton Producers.

Elizabeth G. Flores joined the board in August 2006, and her current term expires December 31, 2009. She was mayor of Laredo, Texas, where she resides, from 1998 to June 2006. Previously, she was senior vice president of Laredo National Bank. Flores serves on the boards of the Texas Agricultural Cooperative Council and the TMF Health Quality Institute, and is a graduate of Leadership Texas 1995 and Leadership America 2008. She is a partner with a ranching and real estate limited partnership, E.G. Ranch, Ltd. She is a former member of the Federal Reserve Board Consumer Advisory Council. Flores also is a member of the bank's Audit and Compensation committees.

William F. Staats joined the board in 1997, and his current term expired December 31, 2008. Staats was reappointed by the board to a new term expiring December 31, 2011. Staats is Louisiana Bankers Association Chair Emeritus of Banking and Professor Emeritus, Department of Finance, at Louisiana State University, where he held the Hermann Moyse Jr. Distinguished Professorship. Previously, he was vice president and corporate secretary of the Federal Reserve Bank of Philadelphia. Staats also serves on the boards of the Money Management International Education Foundation, Money Management International, SevenOaks Capital Associates, LLC and Platinum Healthcare Staffing, Inc. He is a member of the Farm Credit System Audit Committee, is chairman of the bank's Audit Committee, serves on the bank's Compensation Committee, and is the bank's designated financial expert. He is also a member of the Texas Lutheran University board of regents.

Lester Little joined the board in 2009 and his term will expire December 31, 2011. Little fills the director position previously held by C. Kenneth Andrews. Prior to joining the bank board, Little was chairman of Capital Farm Credit Board of Directors and previously served as vice chairman of the Tenth Farm Credit District Stockholders' Advisory Committee. He also was a member of the district's Association Business Advisory Committee. Little is a member of the bank's Audit and Compensation committees. He is from Hallettsville, Texas, and owns and operates a farm, and offers custom-farming services. He is a Farm Bureau member, chairman of the Lavaca Exposition Association and board chairman of the Hallettsville Junior Livestock Show.

Compensation of Directors

Directors of the bank are compensated in cash for service on the bank's board. Compensation for 2008 was paid at the rate of $50,205 per year, payable at $4,183 per month. In addition to days served at board meetings, directors may serve additional days on other official assignments, and under exceptional circumstances where extraordinary time and effort are involved, the board may approve additional compensation, not to exceed 30 percent of the annual maximum allowable by FCA regulations. No additional compensation was approved or paid during 2008. No director received non-cash compensation exceeding $5,000 in 2008. Total cash compensation paid to all directors as a group during 2008 was $351,435. Information for each director for the year ended December 31, 2008, is provided below:

Board Member	Days Served at Board Meetings*	Days Served on Other Official Assignments**	Total Compensation Paid
Ralph W. Cortese	32.0	40.5	$ 50,205
Jon M. Garnett	32.0	33.5	50,205
C. Kenneth Andrews	32.0	12.5	50,205
Joe R. Crawford	29.0	39.0	50,205
James F. Dodson	32.0	37.0	50,205
Elizabeth G. Flores	32.0	22.5	50,205
William F. Staats	32.0	19.5	50,205
			$ 351,435

* Includes travel time, but does not include time required to prepare for board meetings.

** Includes Audit Committee meetings, Compensation Committee meetings, special assignments, training and travel time.

Directors are reimbursed for reasonable travel, subsistence and other related expenses while conducting bank business. The aggregate amount of expenses reimbursed to directors in 2008, 2007 and 2006 totaled $162,118, $149,254 and $123,258, respectively. The increase in expenses in 2008 as compared to the previous year was primarily due to an overall increase in costs for travel related to airlines and fuel as well as an increase in travel expenses associated with the participation by members of the board in meetings held by other System entities. The increase in expenses for 2007 as compared to 2006 was primarily due to the addition of a board member in late 2006. A copy of the bank's travel policy is available to shareholders upon request.

SENIOR OFFICERS

Name and Title	Time in Position	Experience — Past Five Years
Larry R. Doyle, *Chief Executive Officer*	5.5 years	Chief Executive Officer, FCBT. Prior to joining FCBT, Executive Vice President and Chief Operating Officer, AgFirst Farm Credit Bank.
Thomas W. Hill, *Senior Vice President, Chief Financial Officer, Chief Operations Officer*	14 years 5 years	Senior Vice President, Chief Financial Officer, FCBT
Steven H. Fowlkes, *Senior Vice President, Chief Credit Officer*	11 years 5 years	Senior management and management positions, FCBT
Kyle Pankonien, *Vice President, Corporate Affairs, General Counsel and Corporate Secretary*	1 year	Vice President, Corporate Affairs, Deputy General Counsel, FCBT
William E. Zimmerman, *Senior Vice President, Corporate Affairs, General Counsel and Corporate Secretary*	20 years Retired January 2008	Senior Vice President, Corporate Affairs, General Counsel and Corporate Secretary, FCBT

Compensation Discussion and Analysis – Senior Officers

Overview

The board of directors of the Farm Credit Bank of Texas, through its Compensation Committee, has pursued a compensation philosophy for the bank that promotes leadership in the adoption and administration of a comprehensive compensation program so that:

- Competent senior officers can be attracted, developed and retained for the delivery of performance that will result in the attainment of the bank's strategic business plan;
- Operational activities that produce bank efficiencies and produce financial results that maximize the principles of a cooperative organization will be rewarded;
- Consistent application of compensation programs will link compensation to bank performance and levels of accountability for the achievement of the bank's strategies and programs; and,
- Market-based base salaries, benefits and bonus compensation will position the bank to be a competitive employer in the financial services marketplace.

The Compensation Committee annually reviews the appropriate mix of salaries, benefits and bonus arrangements and approves these programs for senior officers of the bank. With data derived from an independent third-party compensation consultant, the Compensation Committee considers market salary data of competition in the financial services sector to ensure that base salaries and bonus plan structures are in line with market-comparable positions with similarly situated financial institutions. This study provides the basis for actions by the Compensation Committee to approve the compensation level and bonus plan structure of the bank's chief executive officer (CEO) annually, plus review and approve other compensation programs for the other senior officers of the bank. The bank's compensation program encompasses four primary elements: (1) base salary, (2) discretionary bonus compensation, (3) bank-paid retirement benefits and (4) secondary benefits such as an executive physical program, annual leave, bank-paid life insurance and bank-provided vehicles.

Chief Executive Officer (CEO) Compensation Table and Policy

The base salary amount of the CEO was $500,019 for 2008. The amount of the CEO's non-equity discretionary bonus compensation was higher than his base salary amount for 2008, which in essence put more of the CEO's total compensation "at risk" based on the performance of the bank. The Compensation Committee considered the year-end 2008 results of certain financial key performance indicators, such as return on assets, return on equity, collateral ratio, credit quality ratios, growth in total and net assets, net income and level of patronage dividends to shareholders, along with accomplishments of the bank in attaining strategic plan operational objectives as the bases for determining the discretionary bonus for the CEO for 2008. Included in the process for awarding base and bonus compensation for the CEO was the committee's annual appraisal assessment of the CEO's performance in areas such as Farm Credit System and Farm Credit Administration relationships; alliances with other financial institutions; and coordination of bank board, stockholder and association relations.

As discussed in detail below, the Compensation Committee settled the bank's obligations to the CEO with respect to the Farm Credit Bank of Texas Supplemental Pension Plan pursuant to a Compensation Agreement between the bank and the CEO.

The following table summarizes the compensation paid to the CEO of the bank during 2008, 2007 and 2006.

Summary Compensation Table

		Annual					
Name of Chief Executive Officer	Year	Salary (a)	Bonus (b)	Change in Pension Value and Nonqualified Deferred Compensation Earnings (c)	Deferred/Perquisites (d)	Other (e)	Total
Larry R. Doyle	**2008**	**$ 500,019**	**$ 600,000**	**<$ 5,810,710>**	**$ 19,229**	**$ 8,821,430**	**$ 4,129,968**
Larry R. Doyle	2007	$ 440,017	$ 560,000	$ 1,884,534	$ 22,017	—	$ 2,906,568
Larry R. Doyle	2006	440,017	440,000	N/A	20,362	—	900,379

(a) Gross salary for year presented.

(b) Bonus compensation is presented in the year earned, and bonuses are paid within the first 30 days of the subsequent calendar year.

(c) Disclosure of change in pension value reflected only for years 2007 and 2008. "N/A" represents information not available for year 2006. The amounts in column (c) represent the change in the actuarial present value of the accumulated benefit under both defined benefit pension plans (i.e., the Farm Credit Bank of Texas Pension Plan and the Farm Credit Bank of Texas Supplemental Pension Plan) from the pension measurement date used for financial statement reporting purposes with respect to the audited financial statements for the prior completed fiscal year to the pension measurement date used for financial statement reporting purposes with respect to the audited financial statements for the covered fiscal year. The decrease in pension value for 2008 is because the CEO no longer participates in the Farm Credit Bank of Texas Supplemental Pension Plan, under the terms of the Compensation Agreement entered into between the bank and the CEO in November 2008. See the Pension Benefits Table Narrative Disclosure for a more detailed explanation regarding the Compensation Agreement.

(d) Deferred/Perquisites include contributions to a 401(k) plan, automobile benefits, and premiums paid for life insurance.

(e) Other reflects the payment of $8,500,000 made in January 2009 pursuant to the Compensation Agreement between the bank and the CEO. In part, this payment was in exchange for the CEO's agreement to no longer participate in the Farm Credit Bank of Texas Supplemental Pension Plan. The CEO is also eligible for a $4,500,000 payment in January 2010, although that payment will be prorated if his employment terminates prior to January 4, 2010. The prorated amount of $4,500,000 as of December 31, 2008 was $321,430, which was earned in 2008 and is also reflected in Other. See the Pension Benefits Table Narrative Disclosure for a more detailed explanation of the Compensation Agreement and the payments provided thereunder.

Pension Benefits Table for the CEO

The following table presents a summary of the total annual benefit provided from both defined benefit pension plans applicable to the CEO for the year ended December 31, 2008:

Name	Plan Name	Number of Years Credited Service	Present Value of Accumulated Benefit	Payments During 2008
Larry R. Doyle	Farm Credit Bank of Texas Pension Plan	34.780	$ 880,276	$ —
	Farm Credit Bank of Texas Supplemental Pension Plan	34.780	$ —	$ —

Pension Benefits Table Narrative Disclosure for the CEO

The CEO participates in the Farm Credit Bank of Texas Pension Plan (the “Pension Plan”), which is a qualified defined benefit retirement plan. Through the end of 2008, the CEO also participated in the Farm Credit Bank of Texas Supplemental Pension Plan (the “Supplemental Pension Plan”), which is a nonqualified deferred compensation plan. Compensation, as defined in the Pension Plan, includes wages, incentive compensation and deferrals to the 401(k) and flexible spending account plans, but excludes annual leave or sick leave that may be paid in cash at the time of termination, retirement, or transfer of employment, severance payments, retention bonuses, taxable fringe benefits, and any other payments. Pension Plan benefits are based on the average of monthly eligible compensation over the 60 consecutive months that produce the highest average after 1996 (“FAC60”). The Pension Plan’s benefit formula for a Normal Retirement Pension is the sum of (a) 1.65 percent of FAC60 times “Years of Benefit Service” and (b) 0.50 percent of (i) FAC60 in excess of Social Security covered compensation times (ii) “Years of Benefit Service” (not to exceed 35). The CEO’s Pension Plan benefit is offset by the CEO’s pension benefits from another Farm Credit System institution. The present value of the CEO’s accumulated Pension Plan and Supplemental Pension Plan benefits are calculated assuming retirement had occurred at the measurement date used for financial statement reporting purposes with retirement at age 56. The Pension Plan’s benefit formula for the Normal Retirement Pension assumes that the CEO is married on the date the annuity begins, that the spouse is exactly 2 years younger than the CEO, and that the benefit is payable in the form of a 50 percent joint and survivor annuity. If any of those assumptions are incorrect, the benefit is recalculated to be the actuarial equivalent benefit. The Supplemental Pension Plan restores benefits under the Pension Plan that are limited or reduced (a) by the imposition of Internal Revenue Code limits, (b) by the exclusion of deferrals to a nonqualified deferred compensation plan from the definition of “Compensation” in the Pension Plan, and (c) by the commencement of benefits prior to “Normal Retirement Age” for a participant who has satisfied the rule of 85 and is at least age 55. After calculating the amount of Pension Plan benefits that are restored in the Supplemental Pension Plan, that amount is grossed-up for income taxes at a fixed rate. Supplemental Pension Plan benefits are payable 30 days after separation from service as a lump sum amount.

The CEO’s earned benefit under the Supplemental Pension Plan was $8,537,622 as of December 2008 and was projected to increase significantly in the coming years based upon his “Years of Benefit Service” and anticipated total compensation during 2009, 2010, 2011 and 2012. Therefore, under a Compensation Agreement between the bank and the CEO that was executed in November 2008, the board approved the settlement of the bank’s obligations to the CEO under the Supplemental Pension Plan in order (a) to limit the bank’s potential future liability under the Supplemental Pension Plan; (b) to decrease the impact upon the bank and the Supplemental Pension Plan of changes in compensation paid to the CEO, changes in interest rates, and changes in law; (c) to remove uncertainty for the bank and the CEO with respect to the amount of the Supplemental Pension Plan benefit; (d) to agree upon a fixed amount of compensation for the CEO during 2009 and 2010; and (e) to provide incentives for the CEO to remain employed at least through the period involving the development of an important lending systems project. Pursuant to the terms and conditions of the Compensation Agreement, the CEO received the following benefits: (i) a payment of $8,500,000 in January 2009; (ii) deferred compensation in the amount of $4,500,000 which will be paid to the CEO (or his beneficiary in the event of his death) in January 2010, unless the CEO’s employment with the bank terminates prior to January 4, 2010, in which case the $4,500,000 payment will be prorated according to a schedule in the Compensation Agreement and paid within 60 days of such termination; (iii) annual base salary of $750,000 for 2009 and 2010. In exchange for those benefits, the Compensation Agreement provides that the CEO will not (1) participate in the Supplemental Pension Plan as of January 1, 2009; (2) actively participate in another nonqualified plan the bank has established; (3) earn any bonuses for performance during 2009 or 2010; and (4) receive the set severance payment of $1,000,000 which was provided under Mr. Doyle’s “employment at will” agreement dated February 26, 2003. Although the Compensation Agreement only covers the CEO’s compensation through 2010, the board of the bank hopes to retain the CEO for a longer period, due to the current economic conditions. Therefore, the Compensation Agreement further provides that if the CEO remains employed past 2010, he shall be eligible for bonuses for years after 2010 and that base salary for years after 2010 shall be negotiated in late 2010.

The Compensation Agreement is not an employment contract. The deferred compensation provisions of the Compensation Agreement are intended to be an unfunded nonqualified deferred compensation plan for tax purposes, are not intended to meet the qualification requirements of Section 401(a) of the Internal Revenue Code, and are intended to be exempt from ERISA as a governmental plan exempted under ERISA § 4(b)(1). The Compensation Agreement was drafted to comply with the provisions of Section 409A of the Internal Revenue Code.

Compensation of Other Senior Officers

The following table summarizes the compensation paid to the five highest paid officers of the bank during 2008, 2007 and 2006. Amounts reflected in the table are presented in the year the compensation is earned.

Summary Compensation Table

Name of Individual or Group	Year	Annual Salary (a)	Annual Bonus (b)	Annual Deferred/Perquisites (c)	Annual Other (d)	Total
Aggregate of five highest paid officers: (excludes Chief Executive Officer)						
5	**2008**	**$ 1,249,615**	**$ 396,360**	**$ 126,827**	**-**	**$ 1,772,802**
5	2007	1,118,743	404,825	115,711	-	1,639,279
5	2006	1,072,241	371,960	105,873	-	1,550,074

(a) Gross salary.

(b) Bonuses paid within the first 30 days of the subsequent calendar year.

(c) Deferred/Perquisites include contributions to 401(k) and defined contribution plans, automobile benefits and premiums paid for life insurance.

(d) Other - no amounts paid in years presented.

Other senior officers of the bank are eligible for deferred compensation plans and can participate in a retention plan, at the discretion and approval of the bank board's Compensation Committee. Amounts paid in 2008 to any senior officer associated with the retention plan are reflected in the salary column in the above table. Senior officers, other than the CEO, participate in a bank discretionary bonus program, whose terms and conditions are detailed in writing as a Success Sharing Plan, with awards annually approved by the board's Compensation Committee. Neither the CEO nor any other senior officer received non-cash compensation exceeding $5,000 in 2008.

Disclosure of the compensation paid during 2008 to any senior officer or officer included in the table is available and will be disclosed to shareholders of the institution and stockholders of the district's associations upon written request.

Senior officers, including the CEO, are reimbursed for reasonable travel, subsistence and other related expenses while conducting bank business. A copy of the bank's travel policy is available to shareholders upon request.

Bank employees can earn compensation above base salary through an annual Success Sharing Plan, which the bank adopted in 2001. The plan is based upon the achievement of bank performance standards, which are approved by the bank board's Compensation Committee, annually. In addition, certain select bank employees participate in a retention plan which was determined at the discretion and approval of the bank board's Compensation Committee. The Farm Credit Bank of Texas Employee Retention Plan is an unfunded nonqualified deferred compensation plan that was created and approved by the bank's board of directors in 2007 as a means to induce specific employees to accomplish certain activities and remain with the bank for a defined period of time. Participants are nominated by the CEO and approved by the bank board's Compensation Committee. The Plan is constructed to be flexible as to the length of the retention period and the amounts paid for each year of successful participation in the Plan. Senior officers and other bank employees in the Plan are currently participating in individual three-year plans that pay a fixed percentage of their salary as long as they are still employed on the anniversary or ending date coincident with the effective date of each participant's Plan year.

Description of Property

On September 30, 2003, the bank entered into a lease for approximately 102,500 square feet of office space to house its headquarters facility. The lease was effective September 30, 2003, and the term is from September 1, 2003 to August 31, 2013. The bank moved into the new facilities during May of 2004. The district associations own 18 headquarter locations and lease one. There are 122 owned and 73 leased association branch locations. The bank's and associations' investment in property is further detailed in Note 5, "Premises and Equipment," to the accompanying combined financial statements.

Legal Proceedings

There were no matters that came to the attention of the board of directors or management regarding the involvement of current directors or senior officers in specified legal proceedings which are required to be disclosed.

Note 12, "Commitments and Contingencies," to the accompanying combined financial statements outlines the bank and association's position with regard to possible contingencies at December 31, 2008.

Description of Capital Structure

The bank and associations are authorized to issue and retire certain classes of capital stock and retained earnings in the management of their capital structures. Details of the capital structures are described in Note 8, "Members' Equity," to the accompanying combined financial statements, and in the "Management's Discussion and Analysis" of the district included in this annual report to stockholders.

Description of Liabilities

The bank's debt outstanding is described in Note 7, "Bonds and Notes," to the accompanying financial statements. The bank's contingent liabilities are described in Note 12, "Commitments and Contingencies," to the accompanying financial statements.

Selected Financial Data

The selected financial data for the five years ended December 31, 2008, required to be disclosed, is incorporated herein by reference to the "Five-Year Summary of Selected Combined Financial Data" included in this annual report to stockholders.

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

"Management's Discussion and Analysis," which precedes the combined financial statements in this annual report, is incorporated herein by reference.

Transactions With Senior Officers and Directors

The district's policies on loans to and transactions with its officers and directors, required to be disclosed in this section, are incorporated herein by reference to Note 11, "Related Party Transactions," to the accompanying combined financial statements.

Relationship With Public Accountants

The district's auditors were PricewaterhouseCoopers LLP. There were no changes in independent public accountants since the prior annual report to stockholders, and there were no material disagreements with our independent public accountants on any matter of accounting principles or financial statement disclosure during this period.

During 2008, district entities paid their independent public accountants $1.2 million for audit services and $85,958 for tax services. During 2008, the bank's non-audit services provided by the independent public accountants were approved by the bank's audit committee prior to commencement of these services. The non-audit services provided by PricewaterhouseCoopers consisted of an independent tally service for director elections. The billing for this service had not been received as of the date of this annual report.

Financial Statements

The combined financial statements, together with the report thereon of PricewaterhouseCoopers LLP dated February 27, 2009, and the report of management in this annual report to stockholders, are incorporated herein by reference.

The Tenth Farm Credit District's annual and quarterly reports are available free of charge, upon request. These reports can be obtained by writing to Farm Credit Bank of Texas, The Ag Agency, P.O. Box 202590, Austin, Texas 78720 or by calling (512) 483-9204. Copies of the district's quarterly and annual stockholder reports can be requested by e-mailing fcb@farmcreditbank.com. The district's quarterly reports are available approximately 40 days after the end of each fiscal quarter. The district's annual report will be posted on the bank's Web site (at www.farmcreditbank.com), within 75 calendar days of the end of the district fiscal year. This posting coincides with an electronic version of the report being provided to its regulator, the Farm Credit Administration. Within 90 calendar days of the end of the district fiscal year, a copy of the district's annual report will be provided to its stockholders.

Credit and Services to Young, Beginning and Small Farmers and Ranchers and Producers or Harvesters of Aquatic Products (YBS)

In line with our mission, we have policies and programs for making credit available to young, beginning and small farmers and ranchers.

The definitions for YBS, as prescribed by FCA regulations, are provided below.

Young Farmer or Rancher – A farmer, rancher or producer or harvester of aquatic products who was age 35 or younger as of the date the loan was originally made.

Beginning Farmer or Rancher – A farmer, rancher or producer or harvester of aquatic products who had 10 years or less of experience at farming, ranching or producing or harvesting aquatic products as of the date the loan was originally made.

Small Farmer or Rancher – A farmer, rancher or producer or harvester of aquatic products who normally generated less than $250,000 in annual gross sales of agricultural or aquatic products at the date the loan was originally made.

For the purposes of YBS, the term "loan" means an extension of, or a commitment to extend, credit authorized under the Farm Credit Act, whether it results from direct negotiations between a lender and a borrower or is purchased from, or discounted for, another lender, including participation interests. A farmer/rancher may be included in multiple categories as they are included in each category in which the definition is met.

The bank and associations' efforts to respond to the credit and related needs of YBS borrowers are evidenced by the following table:

	At December 31, 2008	
(dollars in thousands)	Number of Loans	Volume
Total loans and commitments	78,153	$ 19,421,687
Loans and commitments to young farmers and ranchers	14,198	$ 2,049,505
Percent of loans and commitments to young farmers and ranchers	18.2%	10.6%
Loans and commitments to beginning farmers and ranchers	36,670	$ 7,435,725
Percent of loans and commitments to beginning farmers and ranchers	46.9%	38.3%

The following table summarizes information regarding new loans to young and beginning farmers and ranchers:

	For the Year Ended December 31, 2008	
(dollars in thousands)	Number of Loans	Volume
Total new loans and commitments	18,361	$ 6,534,125
New loans and commitments to young farmers and ranchers	3,215	$ 730,023
Percent of new loans and commitments to young farmers and ranchers	17.5%	11.2%
New loans and commitments to beginning farmers and ranchers	7,803	$ 2,258,746
Percent of new loans and commitments to beginning farmers and ranchers	42.5%	34.6%

The following table summarizes information regarding loans to small farmers and ranchers:

(dollars in thousands)	At December 31, 2008 — Annual Gross Sales: $50 Thousand or Less	$50 to $100 Thousand	$100 to $250 Thousand	Over $250 Thousand	Total
Total number of loans and commitments	23,255	19,126	20,674	15,098	78,153
Number of loans and commitments to small farmers and ranchers	15,802	14,658	15,275	8,133	53,868
Percent of loans and commitments to small farmers and ranchers	68.0%	76.6%	73.9%	53.9%	68.9%
Total loans and commitments volume	$ 471,342	$ 1,091,689	$ 2,759,620	$ 15,099,036	$ 19,421,687
Total loans and commitments to small farmers and ranchers volume	$ 333,667	$ 854,047	$ 2,065,410	$ 5,298,646	$ 8,551,770
Percent of loans and commitments volume to small farmers and ranchers	70.8%	78.2%	74.8%	35.1%	44.0%

The following table summarizes information regarding new loans made to small farmers and ranchers:

(dollars in thousands)	For the Year Ended December 31, 2008 — Annual Gross Sales: $50 Thousand or Less	$50 to $100 Thousand	$100 to $250 Thousand	Over $250 Thousand	Total
Total number of new loans and commitments	5,671	3,442	4,598	4,650	18,361
Number of new loans and commitments to small farmers and ranchers	3,790	2,615	3,228	2,031	11,664
Percent of new loans and commitments to small farmers and ranchers	66.8%	76.0%	70.2%	43.7%	63.5%
Total new loans and commitments volume	$ 124,808	$ 256,046	$ 760,749	$ 5,392,522	$ 6,534,125
Total new loans and commitments to small farmers and ranchers volume	$ 96,320	$ 194,141	$ 527,441	$ 1,511,705	$ 2,329,607
Percent of loan and commitment volume to small farmers and ranchers	77.2%	75.8%	69.3%	28.0%	35.7%