2010 ANNUAL REPORT
TEXAS FARM CREDIT DISTRICT

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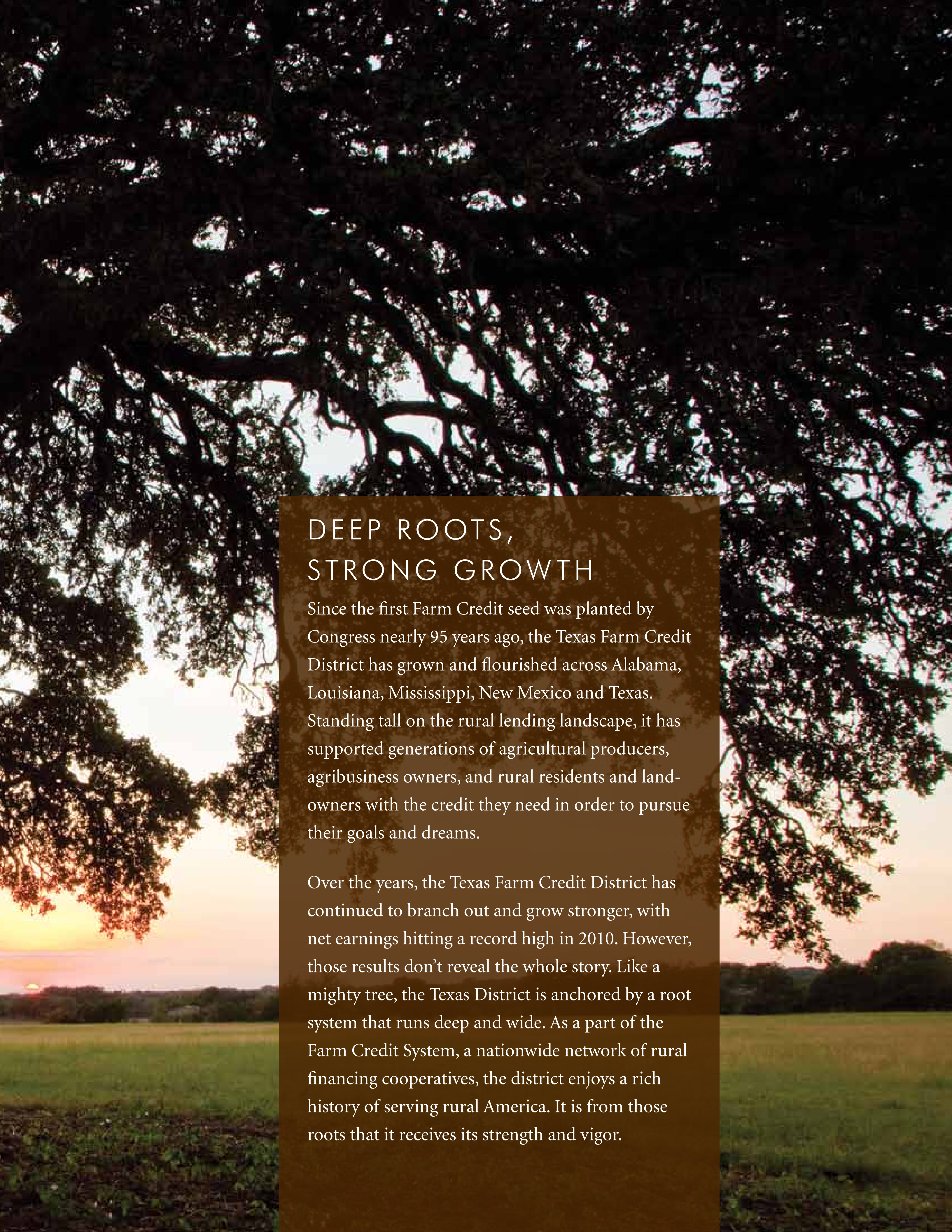


DEEP ROOTS, STRONG GROWTH

Since the first Farm Credit seed was planted by Congress nearly 95 years ago, the Texas Farm Credit District has grown and flourished across Alabama, Louisiana, Mississippi, New Mexico and Texas. Standing tall on the rural lending landscape, it has supported generations of agricultural producers, agribusiness owners, and rural residents and landowners with the credit they need in order to pursue their goals and dreams.

Over the years, the Texas Farm Credit District has continued to branch out and grow stronger, with net earnings hitting a record high in 2010. However, those results don't reveal the whole story. Like a mighty tree, the Texas District is anchored by a root system that runs deep and wide. As a part of the Farm Credit System, a nationwide network of rural financing cooperatives, the district enjoys a rich history of serving rural America. It is from those roots that it receives its strength and vigor.


BOBKAT FARMS

BRANCHING OUT IN RURAL AMERICA

For the Texas Farm Credit District, our MISSION is a lofty one: to enhance the quality of life in rural America by using cooperative principles to provide competitive credit and superior service to our customers.

Every day, we fulfill that mission when we help a young farmer purchase his first farm, extend a revolving line of credit to a livestock producer, or refinance an agribusiness operation for a new corporate customer. Over the years, we have branched out to provide a variety of financial services, as well.

Because we have a dependable source of competitively priced capital, we have continued to fulfill our mission, even during such troubled economic times as the nation has experienced the past three years. Our funding comes from the sale of Farm Credit System bonds and notes in the nation's money markets. These funds flow from Wall Street to the Farm Credit Bank of Texas to the 17 financing cooperatives and four Other Financing Institutions that own the bank. Those local lenders, in turn, make loans to their customer-owners — farmers, ranchers, agribusiness firms, and other rural landowners and homeowners.

OUR LEADERSHIP

If it is true that an organization is only as strong as its leaders, then the Texas Farm Credit District owes a debt of gratitude to the experienced and steady members at its helm. The seven-member Farm Credit Bank of Texas Board of Directors oversees the district's direction and progress, assessing both the challenges and opportunities that potentially impact the long-term success of the bank and its affiliated cooperatives.

These directors bring a depth of experience and a variety of backgrounds to the boardroom table. Together, they possess a wealth of knowledge about the district's business, from both an agricultural and a business perspective, which translates to informed decisions on behalf of the district's stockholders. Five of the board members are farmers or ranchers, who are elected by the customer-stockholders of the cooperatives that own the bank. Two directors come from the business and financing sectors and are appointed by the five elected board members.

With every decision they make, the Farm Credit Bank of Texas directors continue to push for excellence and operate in the best interest of the customers they represent.

BOARD OF DIRECTORS
FARM CREDIT BANK OF TEXAS

(Left to right)
Jon M. "Mike" Garnett
Elizabeth G. "Betty" Flores
Ralph W. "Buddy" Cortese, Chairman
William F. Staats
James F. "Jimmy" Dodson, Vice Chairman
Joe R. Crawford
Lester Little

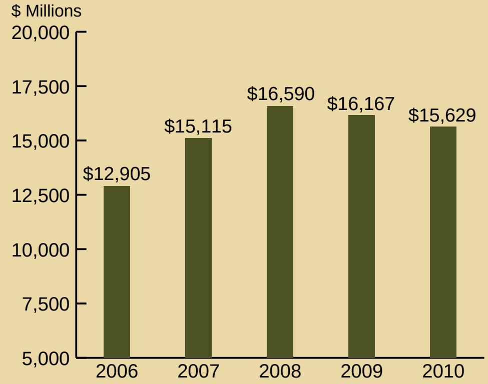
2010 FINANCIAL HIGHLIGHTS

The Texas Farm Credit District reported solid financial results for 2010, highlighted by record net income of $275.3 million for the year. This was an increase of $76.9 million, or 38.8 percent, over 2009 net income. Net interest income for 2010 totaled $580.2 million, compared to $535.8 million for 2009.

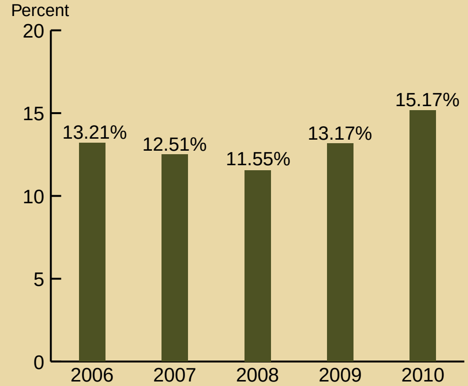
Loan volume remained relatively flat, decreasing 3.3 percent to $15.63 billion at Dec. 31, 2010, from $16.17 billion at Dec. 31, 2009.

District assets totaled $19.6 billion at Dec. 31, 2010, compared with $19.1 billion at Dec. 31, 2009. Credit quality was stable, with 93.2 percent of loan volume considered acceptable and special mention at year-end 2010, compared to 94.1 percent a year earlier.

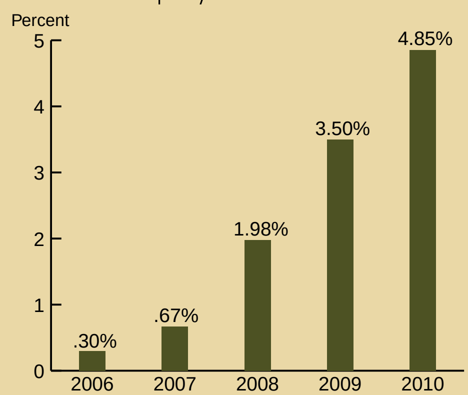
Total Loans Outstanding at Year End



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



2010 KEY FINANCIAL HIGHLIGHTS

(Dollars in Thousands)

Total Loans	$15,628,890
Total Assets	$19,555,584
Net Income	$275,317
Return on Average Assets	1.41%
Return on Average Members' Equity	9.87%

2010
MESSAGE TO STOCKHOLDERS

For the Texas Farm Credit District, 2010 was a significant year of accomplishment and change — a year in which we laid the groundwork for future growth and success. We emerged from the economic downturn of 2008 and 2009 as a more efficient and competitive source of credit and services for rural America.

A number of changes took place across the district in 2010 that strengthened individual associations and, consequently, the district as a whole. Four Federal Land Bank Associations expanded their lending authorities by converting to full-service Agricultural Credit Associations, capable of making operating loans, in addition to real estate loans. Two mergers involving four associations were completed in 2010, which resulted in those associations having more diversity in their loan portfolios.

We also saw a number of association management changes occur, with the retirement of longtime executives. The boards of directors at these associations worked diligently to find replacements who would have the expertise and experience to keep their organizations moving forward.

In the midst of these weighty changes, the district continued to perform well. We are particularly proud to report record net income of $275.3 million for the year, a 39 percent increase in earnings over 2009. This accomplishment can be attributed largely to the Farm Credit Bank of Texas' ability to manage its debt portfolio by calling high-cost debt and replacing it with lower-cost debt. Other contributing factors were careful loan pricing and underwriting practices at the association level and the improvements in certain commodity markets.

While increased earnings were a reassuring sign that the district had rounded the corner on one of the most challenging economic periods this generation of lenders has known, there were other indicators, as well: Return on average assets and return on average members' equity both improved from 2009 to 2010.

At year-end 2010, the district's loan portfolio was down slightly from 2009, a factor of both enhanced credit standards and stronger prices for several commodities, which resulted in some customers paying down existing loans. However, the general outlook for agriculture remains positive, and our district associations stand to benefit from increased lending activity in the near future.

Clearly, the Texas District's solid performance in 2010 can be linked to our cooperative business model. The Farm Credit Bank of Texas shared its success with the district associations and Other Financing Institutions (OFIs) that own the bank through a record patronage payment. The patronage effectively reduced the associations' cost of funds to zero, allowing them to be more competitive in the lending marketplace.

Additionally, the bank's issuance of $300 million of preferred stock and the affirmation of its positive ratings by Moody's Investor Services and Fitch Ratings in 2010 demonstrated the stability of the bank as the Texas District's funding source.

Our success in 2010 and our vision for 2011 reflect our guiding mission, to be a reliable source of competitive credit and superior service for creditworthy borrowers in rural America. We will stay focused on credit quality and work to keep the district strong for the benefit of our customer-stockholders.

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

REPORT OF MANAGEMENT

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

The accompanying combined financial statements of the Farm Credit Bank of Texas (bank) and its affiliated associations, collectively referred to as the district, 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 as well as review of internal controls over financial reporting. 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 associations at December 31, 2010, 2009 and 2008. The independent auditors have direct access to the audit committee, 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, 2010, 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

Amie Pala
Chief Financial Officer

March 1, 2011

REPORT OF AUDIT COMMITTEE

The Farm Credit Bank of Texas and the Texas 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 over financial reporting, 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 2010, seven committee meetings were held. The committee approved the appointment of PricewaterhouseCoopers LLP (PwC) as independent auditors for 2010.

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, 2010 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 2010 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
Lester Little, Vice Chairman
Ralph W. Cortese
Joe R. Crawford
James F. Dodson
Elizabeth G. Flores
Jon M. Garnett

Audit Committee Members

March 1, 2011

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 board 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, 2010. In making the assessment, management used the framework in Internal Control — Integrated Framework, promulgated by the Committee of Sponsoring Organizations of the Treadway Commission, commonly referred to as the "COSO" criteria. This evaluation relies upon the evaluations made by the individual associations and the related certification they provide to the bank.

Based on the assessment performed, the district concluded that as of December 31, 2010, 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, 2010.

Larry R. Doyle
Chief Executive Officer

Amie Pala
Chief Financial Officer

March 1, 2011

Five-Year Summary of Selected Combined Financial Data

FARM CREDIT BANK OF TEXAS AND DISTRICT ASSOCIATIONS

(dollars in thousands)	**2010**	2009	2008	2007	2006
Balance Sheet Data					
Cash and federal funds sold	**$ 473,760**	$ 521,457	$ 233,580	$ 181,205	$ 149,399
Investment securities	**3,231,562**	2,179,312	3,046,397	2,410,999	2,672,242
Loans	**15,628,890**	16,167,170	16,590,071	15,114,537	12,905,321
Less allowance for loan losses	**163,145**	144,731	51,653	24,495	13,969
Net loans	**15,465,745**	16,022,439	16,538,418	15,090,042	12,891,352
Other property owned, net	**78,124**	53,324	6,495	1,817	2,020
Other assets	**306,393**	340,631	341,422	312,434	272,054
Total assets	**$ 19,555,584**	$ 19,117,163	$ 20,166,312	$ 17,996,497	$ 15,987,067
Obligations with maturities of one year or less	**$ 8,812,176**	$ 8,588,063	$ 9,920,558	$ 7,751,462	$ 6,458,754
Obligations with maturities greater than one year	**7,777,077**	8,011,696	7,916,037	7,994,374	7,415,653
Total liabilities	**16,589,253**	16,599,759	17,836,595	15,745,836	13,874,407
Preferred stock	**482,000**	202,754	202,754	202,754	203,565
Capital stock and participation certificates	**61,843**	63,202	63,859	62,489	59,068
Allocated retained earnings	**327,435**	266,991	211,450	133,423	83,705
Unallocated retained earnings	**2,121,822**	2,061,299	1,984,421	1,886,488	1,792,723
Additional paid-in-capital	**22,622**	—	—	—	—
Accumulated other comprehensive loss	**(49,391)**	(76,842)	(132,767)	(34,493)	(26,401)
Total members' equity	**2,966,331**	2,517,404	2,329,717	2,250,661	2,112,660
Total liabilities and members' equity	**$ 19,555,584**	$ 19,117,163	$ 20,166,312	$ 17,996,497	$ 15,987,067
Statement of Income Data					
Net interest income	**$ 580,170**	$ 535,792	$ 470,428	$ 432,381	$ 386,246
Provision for loan losses	**(141,457)**	(172,140)	(53,514)	(43,131)	(9,356)
Noninterest expense, net	**(163,687)**	(167,837)	(148,842)	(146,569)	(137,000)
Benefit from (provision for) income taxes	**291**	2,609	(344)	(141)	228
Net income	**$ 275,317**	$ 198,424	$ 267,728	$ 242,540	$ 240,118
Key Financial Ratios (unaudited)					
Net income to:					
Average assets	**1.41%**	1.01%	1.40%	1.44%	1.66%
Average members' equity	**9.87**	8.02	11.37	10.86	11.69
Net interest income to average earning assets	**3.09**	2.82	2.50	2.61	2.72
Net charge-offs to average loans	**0.75**	0.48	0.16	0.23	0.04
Total members' equity to total assets	**15.17**	13.17	11.55	12.51	13.21
Allowance and reserve for credit losses to total loans	**1.04**	0.90	0.31	0.16	0.11
Regulatory permanent capital ratio (bank only)	**22.00**	15.98	14.03	13.43	13.67
Total surplus ratio (bank only)	**17.83**	12.47	11.25	11.15	11.61
Core surplus ratio (bank only)	**10.67**	7.11	6.40	6.70	6.93
Net collateral ratio (bank only)	**107.91**	105.83	105.40	105.18	105.35
Other (unaudited)					
Net income distributions declared and accrued					
Preferred stock dividends	**$ 45,601**	$ 15,122	$ 15,122	$ 15,122	$ 15,122
Patronage distributions					
Cash	**82,846**	52,303	71,402	76,253	70,479
Allocated earnings	**59,818**	55,648	80,558	57,400	54,328

Combined Average Balances and Net Interest Earnings

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

(dollars in thousands)	**2010** Average Balance	**2010** Interest	**2010** Average Rate	2009 Average Balance	2009 Interest	2009 Average Rate	2008 Average Balance	2008 Interest	2008 Average Rate
Assets									
Investment securities and federal funds sold	**$ 2,993,627**	**$ 77,701**	**2.60%**	$ 2,526,664	$ 88,441	3.50%	$ 2,709,676	$ 111,358	4.11%
Loans	**15,785,538**	**797,608**	**5.05**	16,460,808	873,032	5.30	16,106,806	1,006,081	6.25
Total interest-earning assets	**18,779,165**	**875,309**	**4.66**	18,987,472	961,473	5.06	18,816,482	1,117,439	5.94
Cash	**415,056**			304,910			30,863		
Accrued interest receivable	**176,560**			196,441			228,902		
Allowance for loan losses	**(152,810)**			(90,285)			(36,800)		
Other noninterest-earning assets	**248,680**			197,532			118,792		
Total average assets	**$ 19,466,651**			$ 19,596,070			$ 19,158,239		
Liabilities and Members' Equity									
Bonds, medium-term notes and subordinated debt, net	**$ 11,488,249**	**$ 262,706**	**2.29%**	$ 11,634,484	$ 376,176	3.23%	$ 11,541,763	$ 502,377	4.35%
Discount notes, net, and other	**4,830,875**	**32,433**	**0.67**	5,100,493	49,505	0.97	4,851,341	144,634	2.98
Total interest-bearing liabilities	**16,319,124**	**295,139**	**1.81**	16,734,977	425,681	2.54	16,393,104	647,011	3.95
Noninterest-bearing liabilities	**358,340**			387,598			410,778		
Total liabilities	**16,677,464**			17,122,575			16,803,882		
Members' equity and retained earnings	**2,789,187**			2,473,495			2,354,357		
Total average liabilities and members' equity	**$ 19,466,651**			$ 19,596,070			$ 19,158,239		
Net interest rate spread		**$ 580,170**	**2.85%**		$ 535,792	2.52%		$ 470,428	1.99%
Net interest margin			**3.09%**			2.82%			2.50%

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 Association (FLCA) and the Agricultural Credit Associations (ACAs) for the years ended December 31, 2010, 2009 and 2008. The FLCA and ACAs collectively are referred to as "associations," and the bank and its affiliated associations are collectively referred to as the district. 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, 2010, the district comprised the bank, one FLCA and 16 ACAs. The bank also had funding relationships with four Other Financing Institutions (OFIs). In January 2010, four FLCAs restructured to form ACA structures with operating FLCA and Production Credit Association subsidiaries. Effective July 1, 2010, AgCredit of South Texas, ACA headquartered in Weslaco, Texas, was acquired by Texas AgFinance, FCS headquartered in Robstown, Texas. The continuing association uses the Texas AgFinance name and is headquartered in Robstown, Texas. Effective December 1, 2010, Louisiana Ag Credit, ACA headquartered in Arcadia, Louisiana, was acquired by Southern AgCredit, ACA headquartered in Ridgeland, Mississippi. The continuing association uses the Southern AgCredit, ACA name and is headquartered in Ridgeland, Mississippi.

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 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 identifies loans that may be impaired. Each of these 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. If the present value of expected future cash flows (or, alternatively, the fair value of the collateral) is less than the recorded investment in the loan (including accrued interest, net deferred loan fees or costs, and unamortized premium or discount), an impairment is recognized by making an addition to the allowance for loan losses with a corresponding charge to the provision for loan losses or by similarly adjusting an existing valuation allowance. In addition to these specific allowances, general allowances for loan losses are recorded to reflect expected credit deterioration and inherent losses in that portion of loans that are not individually evaluated.
- 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 Aon Hewitt's Hewitt Top Quartile Curve, actuarial analyses and industry norms. The Hewitt yield curves are determined based on actual corporate bond yields for AA or better rated bonds as of the measurement date.

OVERVIEW

General

The district's loan portfolio totaled $15.6 billion at December 31, 2010, a 3.3 percent decrease from the prior year. The district's net income for 2010 was $275.3 million, an increase of $76.9 million, or 38.8 percent, from the $198.4 million in net income for 2009. The district's $76.9 million increase in net income for 2010 was driven by a $44.4 million increase in net interest income, a $30.7 million decrease in provisions for loan losses, and a $21.3 million increase in noninterest income, offset by a $17.1 million increase in noninterest expense. 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 improvement in the district's net interest income was due in large part to the bank's debt management, and its ability to call debt and replace it with debt with lower interest rates.

Funding

During 2010, the financial markets began to stabilize and the capital markets showed signs of returning to pre-crisis activity levels. As a result of significant government monetary policy actions, short-term interest rates remained low while medium- and long-term interest rates declined for most of 2010. Even in this low interest rate environment, investor demand for Systemwide debt remained strong.

Throughout this period of financial market turbulence, the System has been able to access the debt capital markets to support its mission of providing credit to farmers, ranchers and other eligible borrowers. We expect to be able to continue to issue Systemwide debt securities as the financial crisis dissipates and the economy rebounds. District institutions did respond to the credit issues with appropriate actions, including adjusting loan structures and payment terms, and, in appropriate cases, increasing pricing to customers based on risk.

Agricultural Outlook

General and agricultural economic conditions for farming and for livestock production improved during 2010. Net farm income improved in 2010 and is forecast by the U.S. Department of Agriculture to increase 19.8 percent from the 2010 forecast. The debt to asset ratio in the farm business sector is expected to improve, and cash receipts are expected to increase 9.1 percent, with cotton, soybean, wheat and corn receipts showing the largest gains.

In the beef and cattle sector, which constitutes approximately 38 percent of the district's loan portfolio, profitability improved due to strong export demand and feed prices which declined during the first half of 2010. However, the expectation of higher feed costs resulted in heavy commercial cow slaughter, which implies a reduction in the supply of feeder cattle in the future, despite strong global demand for U.S. beef predicted for 2011. High farm prices for corn in the 2010/2011 season reflect the heavy demand which has reduced its projected ending stocks. Continued demand for corn for export and for the production of ethanol and high-fructose corn syrup could significantly increase input costs and put further pressure on livestock and dairy producers.

Dairy producers also enjoyed improvements in profitability during 2010. Strong domestic use, a good export outlook and a moderate expected increase in production suggest strong prices in 2011, but expected input costs could diminish that profitability.

U.S. cotton exports for the 2010/2011 season are expected to increase to the highest level since the record season of 2005/2006, due to a larger exportable U.S. supply and a rising foreign demand. Prices for the 2010/2011 season are expected to be above that of a year ago.

Although the Texas Farm Credit District's agricultural portfolio benefits from geographical and commodity diversity, as well as continued government support programs, credit quality for the bank and for the district has been impacted by stress in the general economy as well as by the effect of volatility in commodity prices on many sectors. Commodity prices are expected to remain strong and should have a positive impact on producers' overall profitability in 2011/2012.

Financial Highlights

- ❖ Net income totaled $275.3 million for the year ended December 31, 2010, compared to $198.4 million for 2009 and $267.7 million for 2008, reflecting an increase of 38.8 percent from 2009 and an increase of 2.8 percent over 2008.
- ❖ Net interest income for the year ended December 31, 2010, was $580.2 million compared to $535.8 million for 2009 and $470.4 million for 2008, reflecting 8.3 and 23.3 percent increases over the years ended December 31, 2009 and 2008, respectively.
- ❖ Return on average assets and return on average members' equity for the year ended December 31, 2010, were 1.41 and 9.87 percent, respectively, compared to 1.01 and 8.02 percent for 2009 and 1.40 and 11.37 percent for 2008, respectively.
- ❖ Patronage distributions declared totaled $142.7 million in 2010, compared to $107.9 million and $152.0 million in 2009 and 2008, respectively.
- ❖ The aggregate principal amount of loans outstanding at December 31, 2010, was $15.63 billion, compared to $16.17 billion at December 31, 2009, reflecting a decrease of 3.3 percent.

- ❖ In August 2010 the bank issued $300.0 million of Class B non-cumulative subordinated perpetual preferred stock, which is treated as equity and is not mandatorily redeemable.
- ❖ In July 2010, Fitch Ratings affirmed the bank's long-term and short-term Issuer Default Ratings at "AA-" and "F1+," respectively, citing solid operating performance, a manageable increase in loan delinquency, and conservative liquidity and capital management.
- ❖ Also in July 2010, Moody's Investor Services affirmed the bank's investment-grade of Aa2 issuer rating, A1 subordinated debt rating and A2 preferred stock rating.

RESULTS OF OPERATIONS

Net Income

The district's net income of $275.3 million for the year ended December 31, 2010, reflected an increase of 38.8 percent from net income of $198.4 million for the year ended December 31, 2009, and an increase of 2.8 percent from net income of $267.7 million for 2008. The return on average assets increased to 1.41 percent for the year ended December 31, 2010, from 1.01 percent reported for the year ended December 31, 2009. This increase was due primarily to an increase of $44.4 million in net interest income, a decrease of $30.6 million in the district's provision for loan losses, discussed more fully in the "Loan Portfolio" section of this discussion, and a $21.3 million increase in noninterest income, partially offset by a $17.1 million increase in noninterest expense and a $2.3 million decrease in benefit from income taxes.

Changes in Components of Net Income

	2010 vs. 2009	2009 vs. 2008
Net income, prior period	$ 198,424	$ 267,728
Increase (decrease) due to:		
Decrease in interest income	(86,164)	(155,966)
Decrease in interest expense	130,542	221,330
Net interest income	44,378	65,364
Provision for loan losses	30,683	(118,626)
Noninterest income	21,273	4,207
Noninterest expense	(17,123)	(23,202)
Benefit from (provision for) income taxes	(2,318)	2,953
Total increase (decrease) in net income	76,893	(69,304)
Net income	$ 275,317	$ 198,424

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, 2010, was $875.3 million, a decrease of $86.2 million, or 9.0 percent, compared to 2009. Total interest income for 2009 was $961.5 million, a decrease of $156.0 million, or 14.0 percent, from 2008. The decrease for 2010 was due to a decrease in yield on earning assets and a decrease in average interest-earning assets. The decrease in 2009 was due to a decrease in the yield on earning assets, slightly offset by an increase in the average balance of earning assets.

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

	Year Ended December 31,	
	2010 vs. 2009	2009 vs. 2008
(Decrease) increase in average earning assets	$ (208,307)	$ 170,990
Average yield, prior year	5.06%	5.94%
Interest income variance attributed to change in volume	(10,540)	10,154
Average earning assets, current year	18,779,165	18,987,472
Decrease in average yield	(0.40)%	(0.88)%
Interest income variance attributed to change in yield	(75,624)	(166,120)
Net change in interest income	$ (86,164)	$ (155,966)

Interest Expense

Total interest expense for the year ended December 31, 2010, was $295.1 million, a decrease of $130.5 million, or 30.7 percent, from the prior year. Total interest expense for the year ended December 31, 2009, was $425.7 million, a decrease of $221.3 million, or 34.2 percent, from 2008. The decrease for 2010 was due primarily to a decrease in the average rate on debt and a decrease in interest-bearing liabilities. During 2010, the bank was able to reduce its interest expense by calling $12.829 billion in debt and replacing it with debt that had lower interest rates and shorter maturities that match earning assets, which resulted in an estimated annualized interest expense savings of approximately $65.8 million, net of related concession expenses. The decrease for 2009 was due primarily to a decrease in the average rate on debt, slightly offset by an increase in the average balance of interest-bearing debt. During 2009 the bank called and replaced $10.326 billion in debt, which resulted in a reduction of interest expense of approximately $42.5 million, net of related concession expenses.

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

	Year Ended December 31,	
	2010 vs. 2009	2009 vs. 2008
(Decrease) increase in average interest-bearing liabilities	$ (415,853)	$ 341,873
Average rate, prior year	2.54%	3.95%
Interest expense variance attributed to change in volume	(10,563)	13,493
Average interest-bearing liabilities, current year	16,319,124	16,734,977
Decrease in average rate	(0.73)%	(1.41)%
Interest expense variance attributed to change in rate	(119,979)	(234,823)
Net change in interest expense	$ (130,542)	$ (221,330)

Analysis of Operating Margin to Average Earning Assets

	For the Years Ended December 31,		
	2010	2009	2008
Net interest margin	**3.09%**	2.82%	2.50%
Operating expense	**1.12**	1.06	0.98
Operating margin	**1.97%**	1.76%	1.52%

Net Interest Income

Net interest income increased by $44.4 million, or 8.3 percent, from 2009 to 2010 and increased by $65.4 million, or 13.9 percent, from 2008 to 2009. Factors responsible for these changes are illustrated in Figure 1.

Net interest income for 2010 increased from 2009 due to a 33-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, offset by a decrease in average-earning assets.

The decrease in average earning assets was due primarily to a decrease in loan growth at the district's associations and slight decreases in the bank's loan participation portfolio. The increase in the interest rate spread was due primarily to the bank's ability to call and replace callable debt with debt with lower interest rates. During 2010, the bank called $12.829 billion in debt, replacing it with debt that had more favorable terms. Moderate increases in loan pricing spreads at the associations also contributed to the increase in the district's net interest rate spread.

Net interest income for 2009 increased from 2008 due to an increase in the district's earning assets, and a 53-basis-point increase in the interest rate spread. The increase in the interest rate spread was due primarily to the bank's ability to call $10.326 billion and replace it with debt with more favorable terms.

Provision for Loan Losses

The provision for loan losses for 2010 was $141.5 million, reflecting a decrease of $30.7 million from the $172.1 million provision recorded in 2009. The provision for loan losses at the bank decreased by $5.1 million, while the associations' provisions decreased by $25.6 million. The decrease is due primarily to specific provisions for loan losses on impaired loans. Specific provisions for 2010 decreased from those of 2009, when efforts to identify risks and loss potential were intensified in 2009. The specific provisions reflect credit deterioration primarily in those agricultural sectors that continue to be impacted by volatility in commodity prices, such as the livestock and dairy industries, as well as those borrowers impacted by the overall downturn in the general economy, primarily land in transition.

Noninterest Income

Noninterest income of $61.7 million reflected an increase of $21.2 million, or 52.6 percent, from 2009 to 2010. The increase was primarily due to a $22.3 million in Farm Credit System Insurance Corporation (FCSIC or Insurance Fund) refund distributions of excess reserves from prior periods recorded during the first quarter of 2010, an $11.7 million increase in fees for loan-related services, and a $3.5 million decrease in impairment losses recognized due to the estimated amount of credit loss related to other-than-temporary impairments on investment securities which is more fully discussed in the "Investments" section of this discussion and in Note 3, "Investment Securities," offset by a $7.1 million decrease in gain on sale of investments, a $7.2 million loss at an association on the sale of loans at fair value to the bank, a $781 decrease in patronage income, and a $1.1 million decrease in all other noninterest items, collectively. During 2009, the bank realized gains of $5.5 million on the sale of six agency mortgage-backed securities that had an amortized cost of $106.0 million. The bank also realized a gain of $2.1 million on the sale of five rural home loan mortgage-backed securities with an amortized cost of $39.4 million, which had comprised the bank's held-to-maturity investment portfolio. These sales were made in order to enhance the bank's liquidity position, which entails the conversion of certain assets into cash. The bank's current liquidity posture is such that it is not likely for the bank to have sales of investment securities in 2011.

Noninterest income for 2009 of $40.5 million reflected an increase of $4.2 million, or 11.6 percent, from 2008 to 2009. The increase was primarily due to a $5.1 million increase in gain on sale of investments, a $952 increase in fees for loan-related services and a $1.4 million increase in all other noninterest items, collectively, offset by a $3.1 million increase in estimated credit losses related to other-than-temporary impairments on investment securities, which is more fully discussed in "Investments," and a $264 decrease in patronage and dividend income.

Figure 1

Analysis of Net Interest Income

	2010		2009		2008	
	Avg. Balance	**Interest**	Avg. Balance	Interest	Avg. Balance	Interest
Loans	**$ 15,785,538**	**$ 797,608**	$ 16,460,808	$ 873,032	$ 16,106,806	$ 1,006,081
Investments	**2,993,627**	**77,701**	2,526,664	88,441	2,709,676	111,358
Total earning assets	**18,779,165**	**875,309**	18,987,472	961,473	18,816,482	1,117,439
Interest-bearing liabilities	**16,319,124**	**295,139**	16,734,977	425,681	16,393,104	647,011
Impact of capital	**$ 2,460,041**		$ 2,252,495		$ 2,423,378	
NET INTEREST INCOME		**$ 580,170**		$ 535,792		$ 470,428

	2010 Average Yield	2009 Average Yield	2008 Average Yield
Yield on loans	**5.05%**	5.30%	6.25%
Yield on investments	**2.60**	3.50	4.11
Yield on earning assets	**4.66**	5.06	5.94
Cost of interest-bearing liabilities	**1.81**	2.54	3.95
Interest rate spread	**2.85**	2.52	1.99
Impact of capital	**0.24**	0.30	0.51
Net interest income/average earning assets	**3.09**	2.82	2.50

Noninterest Expenses

Noninterest expenses for 2010 totaled $225.4 million, increasing $17.1 million, or 8.2 percent, from 2009. The increase was primarily due to an increase of $29.9 million in salaries and employment benefits, an increase of $7.3 million in net losses on other property owned, an increase of $1.3 million in occupancy and equipment expense, and a $2.1 million increase in other operating expenses, offset by a $23.5 million decrease in premiums to the FCSIC. The $29.9 million increase in salaries and employee benefits was due primarily to a $22.7 million decrease in salaries and benefits capitalized for nonrefundable fees and costs associated with originating and acquiring loans and an $8.3 million increase in salaries and related payroll taxes at the district's associations, net of a $2.5 million decrease in district pension and retirement expenses, due mainly to improved performance of the district defined benefit pension plan's assets and reduced amortization of its losses from the previous year. Salaries and benefits capitalized as a part of loan origination costs decreased as loan originations decreased at the district's associations during 2010. Salaries increased due to increases in salaries and bonuses, primarily at the district's associations and to the bank's recognition of $2.9 million in employee annual Success Sharing Plan bonuses in December 2010 in addition to the annual award recognized in January 2010 for 2009 performance, net of a $3.9 million decrease in deferred compensation for the bank's chief executive officer (see CEO compensation discussion in the Disclosure and Information Index section). Pension and retirement benefits decreased due primarily to losses recognized in 2009 in the district's defined benefit pension plan as a result of the effect of economic downturn on the values of plan assets in 2008. The $7.3 million increase in losses on other property owned was primarily due to a $5.8 million increase in provision for losses on property acquired by district associations. The $1.3 million increase in occupancy and equipment expenses included a $714 increase in computer expenses. The $2.1 million increase in other operating expenses was primarily due to a $751 increase in professional and contract services, a $283 increase in director's expenses, a $236 increase in advertising and member relations expenses, and a $1.7 million increase in all other operating expenses, collectively, offset by a $710 decrease in Funding Corporation assessment fees. The $23.5 million decrease in premiums paid to the FCSIC was primarily due to a premium rate reduction from 20 basis points in 2009 to 5 basis points in 2010. Assessments from the Funding Corporation decreased primarily due to a $687 special assessment in January 2009 to provide additional funding for the Funding Corporation's pension plan.

Noninterest expenses for 2009 totaled $208.3 million, increasing $23.2 million, or 12.5 percent, from 2008. The increase was primarily due to an increase of $7.7 million in salaries and employment benefits, an increase of $7.4 million in net losses on other property owned, an increase of $7.0 million in premiums to the FCSIC, an increase of $658 in occupancy and equipment expense, and an increase of $441 in other operating expenses. The $7.7 million increase in salaries and employee benefits was due primarily to a $1.7 million increase in salaries and related payroll taxes, a $11.4 million increase in pension and retirement benefits, and a $61 increase in other benefits, offset by a $4.3 million increase in salaries and benefits capitalized for nonrefundable fees and costs associated with originating and acquiring loans, and a $1.2 million increase in capitalized salaries and benefits related to the bank's development of new lending systems. 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 was due primarily to an increase in losses recognized in the district's defined benefit pension plan during 2008. The increase in compensation included a $3.9 million accrual of deferred compensation for the bank's chief executive officer (see CEO compensation discussion in the Disclosure and Information Index section). The $7.4 million increase in losses on other property owned was primarily due to a $6.9 million increase in provision for losses on property acquired by district associations during the fourth quarter. The $7.0 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 outstanding, as well as an increase in the premium rate which began in January 2009. The $658 increase in occupancy and equipment expenses included a $452 increase in computer expenses. The $441 increase in other operating expenses was primarily due to a $1.3 million increase in professional and contract services, a $1.1 million increase in Funding Corporation assessment fees, and an $866 increase in all other operating expenses, collectively, offset by a $1.9 million decrease in advertising and member relations expenses, a $550 decrease in directors' expenses, and a $394 decrease in travel expenses. Assessments from the Funding Corporation increased primarily due to a $687 special assessment in January 2009 to provide additional funding for the Funding Corporation's pension plan, a $365 increase in the assessment for the Funding Corporation's contingency funding plan, and an increase of $74 in allocated System 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,

	2010	2009	2008
Excess of net interest income over operating expense	**$ 369,909**	$ 335,305	$ 285,714
Operating expense as a percentage of net interest income	**36.24%**	37.42%	39.27%
Operating expense as a percentage of net interest income and noninterest income	**32.76**	34.79	36.46
Operating expense as a percentage of average loans	**1.33**	1.22	1.15
Operating expense as a percentage of average earning assets	**1.12**	1.06	0.98

The district's operating expense statistics for 2010 and 2009 reflect the district's growth in net interest income, which outpaced increases in operating expenses. Net interest income has increased 8.3 percent and 13.8 percent for the years ended December 31, 2010 and 2009, respectively, while operating expenses increased at the rates of 4.9 percent and 8.5 percent, respectively, for the same periods. Average loans decreased 0.4 percent in 2010 and increased 2.2 percent in 2009. Average investments increased 18.5 percent in 2010 and decreased 6.8 percent in 2009. Average earning assets decreased 1.1 percent in 2010 and increased 0.9 percent in 2009.

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, the System utilizes 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.

The ratios in the CIPA model are currently under review, 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, and the bank permanent capital ratio is primarily the bank's common stock, preferred stock 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 December 31, 2010, all banks met the agreed-upon standards for the net collateral and permanent capital ratios required by the MAA. As of December 31, 2010, all banks met the agreed-upon standard of financial condition and performance required by the CIPA. During the three years ended December 31, 2010, the banks met the defined CIPA score required by the MAA, except for the Farm Credit Bank of Texas which fell below a defined CIPA score as of September 30, 2009, and, effective November 9, 2009, was placed in "Category I." As of December 31, 2009, the Farm Credit Bank of Texas met the defined CIPA score required by the MAA and effective February 27, 2010, exited "Category I." The Farm Credit Bank of Texas was able to return to compliance with the defined CIPA score under MAA primarily due to reductions in the district's substandard assets, including high-risk assets, due to improvements in borrowers' repayment capacities. 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 — requirements that govern intended use of 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 objective and subjective criteria. 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 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 $15.63 billion at December 31, 2010, reflected a decrease of $538.3 million, or 3.3 percent, from the $16.17 billion loan portfolio balance at December 31, 2009. Loans, net of the allowance for loan losses, represented 79.1 percent, 83.8 percent and 82.0 percent of total assets as of December 31, 2010, 2009 and 2008, respectively.

Agricultural real estate mortgage loans totaled $10.49 billion at December 31, 2010, a decrease of $552.6 million, or 5.0 percent, from 2009, and currently comprise approximately 67.1 percent of the district's loan portfolio. Commercial loans for agricultural production, processing and marketing totaled $3.14 billion, a decrease of $78.0 million, or 2.4 percent, from 2009, and represented 20.1 percent of the loan portfolio at December 31, 2010. All other loans, including energy loans, communications loans, farm-related business loans, rural home loans and loans to OFIs, increased by $92.3 million. The composition of the district's loan portfolio by category may be found in Note 4, "Loans and Allowance for Loan Losses."

In March 2010, the bank purchased loans which had experienced credit deterioration from a district association. The loans, with contractual balances totaling $40.1 million, were purchased at fair value of $32.8 million. The fair value was estimated by discounting the total estimated cash flows of $36.3 million by appropriate yield curves. The bank recognized additional provisions for loan losses totaling $2.0 million related to these loans during 2010, the effect of which also slightly reduces the resulting accretable discount, which will be accreted into interest income on a level-yield basis over the life of the loans. At December 31, 2010, the balance of these loans, net of the unaccreted discount, was $21.9 million. In addition to these loans, the bank also purchased other property owned related to three other loans from the association at fair value of $2.9 million.

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,

	2010	2009	2008
Acceptable	**87.9%**	89.3%	94.8%
Special mention	**5.3**	4.8	2.3
Substandard	**6.8**	5.9	2.9
Total	**100.0%**	100.0%	100.0%

During 2010, overall credit quality reflected some deterioration from prior years. Volatility in the general economy and in agricultural sectors has resulted in some migration to more adverse classifications. 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 93.2 percent at December 31, 2010, compared to 94.1 percent at December 31, 2009 and 97.1 percent at December 31, 2008.

High-Risk Assets

Nonperforming loan volume is composed of nonaccrual loans, restructured loans, and loans 90 days or more past due and still accruing interest and is referred to as impaired loans. High-risk assets consisted of impaired loans and other property owned. Total high-risk assets have increased by $167.5 million, or 27.7 percent, from $605.1 million at December 31, 2009, to $772.6 million at December 31, 2010. The increase in high-risk assets during 2010 includes a $168.7 million increase in nonaccrual loans and a $24.8 million increase in other property owned. The increases are reflective of the adverse conditions in the agricultural and general economy, and are due to the volatility in the agricultural commodity market which has resulted in higher risk profiles for dairy, livestock, and borrowers who use corn and other grains in their products, primarily ethanol. The growth in nonaccrual loans included significant increases in livestock, dairy, and hunting, trapping and game propagation, as well as loans related to land in transition, whose values are driven primarily by development values near urban areas rather than agricultural value. The $24.8 million increase in other property owned was due mainly to the credit stress induced by the general economy as well as the agricultural sectors previously mentioned.

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

(in millions)	**2010**	2009	2008
Nonaccrual loans	**$ 683.1**	$ 514.4	$ 322.4
Formally restructured loans	**9.0**	3.0	6.1
Loans past due 90 days or more and still accruing interest	**2.4**	34.4	17.9
Other property owned, net	**78.1**	53.3	6.5
Total	**$ 772.6**	$ 605.1	$ 352.9

At December 31, 2010, $282.9 million, or 41.4 percent, of loans classified as nonaccrual were current as to principal and interest, compared to $211.8 million, or 41.2 percent, of nonaccrual loans at December 31, 2009, and $249.9 million, or 77.5 percent, at December 31, 2008.

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, 2010, 2009 and 2008. Due to expected improvements related to these higher risk profiles and in the general economic environment, the district anticipates credit quality of the loan portfolio will stabilize in 2011.

Allowance and Provision for Loan Losses

At December 31, 2010, the allowance for loan losses was $163.1 million, or 1.04 percent of total loans outstanding, compared to $144.7 million (0.90 percent) and $51.7 million (0.31 percent) at December 31, 2009 and 2008, respectively. Net charge-offs of $119.0 million, $78.3 million and $26.2 million were recorded in 2010, 2009 and 2008, respectively. Charge-offs during 2010 included significant charge-offs on loans related to land in transition, beef- and cattle-related loans, ethanol loans, and participations in a loan to an electric service provider. The district's net provision for loan losses of $141.5 million for 2010 reflected a decrease of $30.7 million, or 17.8 percent, from the provision recorded for 2009, 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 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:

	2010	2009	2008
Allowance for loan losses as a percentage of:			
Average loans	**1.0%**	0.9%	0.3%
Loans at year end			
Total loans	**1.0**	0.9	0.3
Nonaccrual loans	**23.9**	28.1	16.0
Total impaired loans	**23.5**	26.2	14.9
Net charge-offs to average loans	**0.8**	0.5	0.2
Provision expense to average loans	**0.9**	1.0	0.3

Figure 2

Nonaccrual Loans as a Percentage of Total Loans at Year End

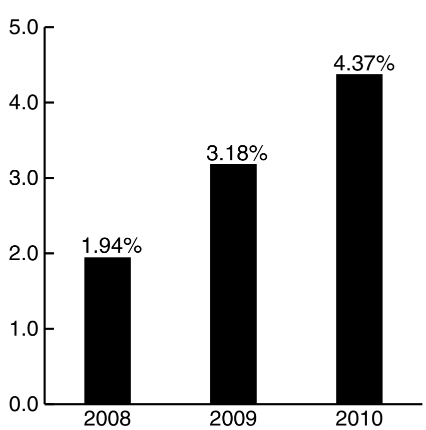


Figure 3

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

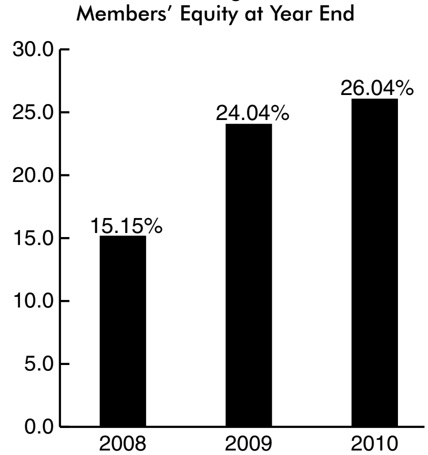


Figure 4

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

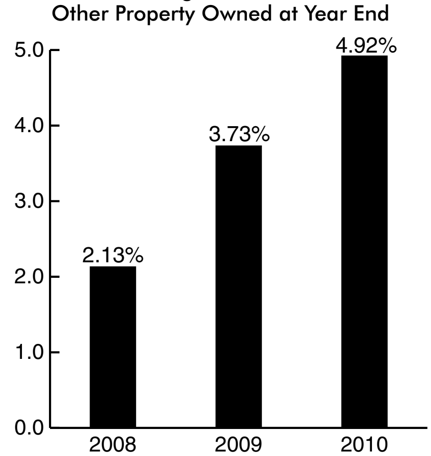


Figure 5

Interest Rate Gap Analysis
as of December 31, 2010

	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	$ 5,686,023	$ 2,023,422	$ 1,497,491	**$ 9,206,936**	$ 4,828,131	$ 1,593,823	**$ 15,628,890**
Total investments	1,470,036	341,979	326,982	**2,138,997**	852,716	260,286	**3,251,999**
Total earning assets	7,156,059	2,365,401	1,824,473	**11,345,933**	5,680,847	1,854,109	**18,880,889**
Interest-Bearing Liabilities							
Total interest-bearing funds*	6,042,405	2,488,173	2,764,720	**11,295,298**	4,111,020	836,819	**16,243,137**
Excess of earning assets over interest-bearing liabilities	—	—	—	**—**	—	2,637,752	**2,637,752**
Total interest-bearing liabilities	6,042,405	2,488,173	2,764,720	**11,295,298**	4,111,020	3,474,571	**$ 18,880,889**
Interest rate sensitivity gap	$ 1,113,654	$ (122,772)	$ (940,247)	**$ 50,635**	$ 1,569,827	$ (1,620,462)	
Cumulative interest rate sensitivity gap	$ 1,113,654	$ 990,882	$ (50,635)	**$ 50,635**	$ 1,620,462		

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

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 bank's and district's interest-rate-sensitive assets and liabilities. The bank is able to manage the balance sheet composition by using various debt issuance strategies and hedging transactions to match its asset structure. 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 its 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, 2010, 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 positive gap position, indicating that the district has an exposure to decreasing interest rates. This occurs when interest income earning assets decrease, due to their maturing or repricing cycle, sooner than maturing or repricing debt.

To reflect the expected cash flow and repricing characteristics of the district's balance sheet, an estimate of expected prepayments on loans and mortgage-related investments is used to adjust the maturities of the loans and investments in the earning assets section of the gap analysis. Changes in market interest rates will affect the volume of prepayments on loans. Correspondingly, 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, 2010, the bank had three fair value interest rate swap contracts with a total notional amount of $150.0 million. The interest rate swap contracts had a net fair value of $1.8 million. In addition, at December 31, 2010, the bank held interest rate caps with a notional amount of $645.0 million and a fair value of $4.7 million. See Note 16, "Derivative Instruments and Hedging Activity," for further discussion. Unrealized losses on interest rate caps, the difference between the amortized cost and fair value, are recorded as a reduction of accumulated other comprehensive income. 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, diversify counterparties in the swap transactions and monitor the credit ratings of all counterparties with whom it transacts. Figure 6 summarizes the bank's activity in derivative financial instruments for 2010.

Interest rate risk exposure as measured by simulation modeling calculates the district's expected net interest income and market value of equity based upon projections of interest-rate-sensitive assets, 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, 2010, projected district net interest income would increase by $37.4 million, or 6.5 percent, if interest rates were to increase by 200 basis points, and would decrease by $5.9 million, or 1.0 percent, if interest rates were to decrease by 6 basis points. In general, the bank's ability to exercise call options on debt benefits 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.

The bank's 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 as discussed below. As a secondary source of liquidity, the bank maintains an investment portfolio comprised primarily of high-quality liquid securities. The securities provide a stable source of income for the bank, and their high quality ensures the portfolio can quickly be converted to cash should the need arise.

FCA regulations require 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 the 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, 2010, the bank had 177 days of liquidity coverage, as compared with 144 days at December 31, 2009.

The System banks have worked together to enhance liquidity within the Farm Credit System. As of December 31, 2009, the bank implemented new internal liquidity guidelines to maintain a minimum of 120 days of liquidity with the first 15 days of liquidity composed of cash, cash equivalents and Treasury securities, and an additional 30 days composed of high-quality government guaranteed securities, resulting in a total of 45 days of high-quality liquidity. These guidelines were designed to allow the bank to continue normal operations should a market disruption occur that would prevent the bank from accessing the Systemwide debt market. As of December 31, 2010, the bank had 19 days of liquidity coverage from cash and cash equivalents and an additional 105 days of liquidity coverage from government guaranteed securities. In total the bank maintained 177 days of liquidity coverage at December 31, 2010.

In addition, the bank maintains a $150.0 million commercial bank committed line of credit.

Funding Sources

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. Prior to the bank's issuance of its Class B non-cumulative subordinated perpetual preferred stock (Class B) in August 2010, the subordinated debt received preferential regulatory capital and collateral treatment, being includible in portions of permanent capital and total surplus

Figure 6

Activity in Derivative Financial Instruments
(Notional Amounts)

(in millions)	
Balance at December 31, 2009	$ 255
Additions	1,240
Terminations	(700)
Balance at December 31, 2010	**$ 795**

and being excludible from total liabilities for purposes of net collateral ratio calculation. Regulatory conditions related to the issuance of the Class B preferred stock effectively eliminated these preferential ratio treatments, which would previously have been ratably removed 20.0 percent per year during years six to 10 of the debt's term.

The bank receives ratings from two rating agencies. On July 2, 2010, Fitch Ratings affirmed the bank's long-term and short-term Issuer Default Ratings at "AA-" and "F1+," respectively, citing solid operating performance, a manageable increase in loan delinquency, and conservative liquidity and capital management. On July 9, 2010, Moody's Investor Services affirmed the bank's investment-grade of Aa2 issuer rating, A1 subordinated debt rating and A2 preferred stock rating.

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

	December 31,		
	2010	2009	2008
Bonds and term notes outstanding	**$ 10,708**	$ 11,847	$ 11,335
Average effective interest rate	**1.74%**	2.46%	3.89%
Average life (years)	**2.9**	2.8	3.4
Subordinated debt outstanding	**$ 50**	$ 50	$ 50
Average effective interest rate	**8.41%**	8.41%	8.41%
Average life (years)	**7.8**	8.8	9.8
Discount notes outstanding	**$ 2,072**	$ 922	$ 2,467
Average effective interest rate	**0.25%**	0.29%	1.37%
Average life (days)	**122**	76	107
Notes payable to other System banks	**$ 3,400**	$ 3,400	$ 3,500
Average effective interest rate	**0.72%**	0.78%	3.25%
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,		
	2010	2009	2008
Average interest-bearing liabilities outstanding	**$ 16,319**	$ 16,735	$16,393
Average interest rates on interest-bearing liabilities	**1.81%**	2.54%	3.95%

Investments

As permitted under FCA regulations, a bank is authorized to hold eligible investments 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. FCA regulations also permit an association to hold eligible investments with the approval of its affiliated bank.

FCA 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 bank's investments must be highly rated by a Nationally Recognized Statistical Rating Organization, such as Moody's Investors (Moody's) Service, Standard & Poor's and Fitch Ratings. A bank must develop and submit to the FCA a divestiture plan that includes disposal of an asset that becomes ineligible within six months, unless the FCA grants permission to divest the instrument over a longer period of time.

The following table discloses the district's available-for-sale liquidity portfolio at December 31,

	2010		2009	
	Amortized Cost	**Fair Value**	Amortized Cost	Fair Value
Corporate debt	**$ 300,531**	**$ 302,091**	$ 131,815	$ 133,733
Federal agency collateralized mortgage-backed securities	**2,524,022**	**2,559,429**	1,843,894	1,871,339
Other collateralized mortgage-backed securities	**71,192**	**64,918**	123,315	110,106
Asset-backed securities	**11,493**	**10,005**	67,069	64,134
Total liquidity investments	**$ 2,907,238**	**$ 2,936,443**	$ 2,166,093	$ 2,179,312

The district's increases in federal agency collateralized mortgage obligations during 2010 have been in Government National Mortgage Association (GNMA) mortgage-backed securities. Pricing on agency securities remains strong due to the Federal Reserve's mortgage-backed securities purchase program, stabilization in the agency market, and increased demand for quality GNMA structures. The decreases in other collateralized mortgage-backed securities and asset-backed securities are due primarily to repayments on those securities.

The district's other investments, totaling $295.1 million, consisted of Federal Agricultural Mortgage Corporation (Farmer Mac) guaranteed agricultural mortgage-backed securities (AMBS). The bank held AMBS with a fair value of $140.5 million in an available-for-sale other investments portfolio, and associations held AMBS with an amortized cost of $154.6 million in a held-to-maturity portfolio. The Farmer Mac securities are backed by loans originated by the associations and previously held by the associations under the Farmer Mac long-term standby commitments to purchase agreements.

Farmer Mac is a government-sponsored enterprise and is examined and regulated by FCA. It provides secondary market arrangements for agricultural and rural home mortgage loans that meet certain underwriting standards. Farmer Mac is authorized to provide loan guarantees or be a direct pooler of agricultural mortgage loans. Farmer Mac is owned by both System and non-System investors and its board of directors has both System and non-System representation. Farmer Mac is not liable for any debt or obligation of any System institution and no System institution other than Farmer Mac is liable for any debt or obligation of Farmer Mac.

The bank's available-for-sale other investments portfolio consisted of Farmer Mac AMBS at December 31:

	2010		2009	
	Amortized Cost	**Fair Value**	Amortized Cost	Fair Value
Agricultural mortgage-backed securities	**$ 145,122**	**$ 140,503**	$ —	$ —

At December 31, 2009, the available-for-sale investment portfolio included guaranteed Small Business Administration pooled securities totaling $35.8 million held by a district association. The district's available-for-sale portfolio is reflected at fair value. In 2009, the bank sold six federal agency mortgage-backed securities that had an amortized cost of $106.0 million for a gain of $5.5 million. The bank also sold its held-to-maturity portfolio, consisting of five rural home loan mortgage-backed securities with an amortized cost of $39.4 million, for a gain of $2.1 million. These sales were part of the bank's efforts to enhance its liquidity involving the conversion of certain assets into cash. In addition to these sales, maturities on investments in commercial paper, master notes and agency debt instruments were used to increase the district's cash position by $444.1 million during 2009.

At December 31, 2010, the bank had 12 investments which were ineligible for liquidity purposes as a result of credit downgradings. These investments had credit ratings at December 31, 2010 that were below AAA by both Moody's and Standard & Poor's. These investments had an amortized cost of $57.1 million and a fair value of $50.5 million, with an unrealized loss of $6.6 million at December 31, 2010. The downgrading of the investment securities requires a submission of a plan of divestiture to the FCA and their formal approval. The FCA has approved, with conditions, plans submitted by the bank to continue to hold all ineligible investments at this time. To date, the FCA has not required disposition of any of these securities. 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. During 2010, the bank recognized credit losses on six other-than-temporarily impaired investment securities totaling $1.8 million. Noncredit losses on these investments, totaling $5.4 million, are included as a charge against accumulated other comprehensive income at December 31, 2010. Due to the continued deterioration in the mortgage markets, the bank may incur additional other-than-temporary impairments on non-guaranteed mortgage- and asset-backed securities.

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

The following table sets forth investments available-for-sale within the liquidity portfolio at fair value by credit rating:

	Eligible		**Ineligible**								
December 31, 2010	**AAA/Aaa**	**Split Rated**	**AA/Aa**	**AA/BBB Split Rated**	**A-/BB- Split Rated**	**B3/BBB/B Split Rated**	**BBB/Baa**	**BB/Ba**	**B3/CCC/CC**	**CCC/Caa**	**Total**
FDIC-guaranteed corporate debt	**$ 302,091**	**$ —**	**$ —**	**$ —**	**$ —**	**$ —**	**$ —**	**$ —**	**$ —**	**$ —**	**$ 302,091**
Federal agency collateralized mortgage-backed securities	**2,559,429**	**—**	**—**	**—**	**—**	**—**	**—**	**—**	**—**	**—**	**2,559,429**
Other collateralized mortgage-backed securities	**5,918**	**10,896**	**11,745**	**—**	**—**	**—**	**—**	**6,953**	**6,293**	**23,113**	**64,918**
Asset-backed securities	**3,294**	**4,305**	**—**	**—**	**—**	**—**	**418**	**1,668**	**—**	**320**	**10,005**
Total	**$ 2,870,732**	**$ 15,201**	**$ 11,745**	**$ —**	**$ —**	**$ —**	**$ 418**	**$ 8,621**	**$ 6,293**	**$ 23,433**	**$2,936,443**

	Eligible			Ineligible							
December 31, 2009	AAA/Aaa	AA/Aa	Split Rated	AA/BBB Split Rated	A-/BB- Split Rated	B3/BBB/B Split Rated	BBB/Baa	BB/Ba	B3/CCC/CC	CCC/Caa	Total
Corporate debt	$ 103,733	$ 30,000	$ —	$ —	$ —	$ —	$ —	$ —	$ —	$ —	$ 133,733
Federal agency collateralized mortgage-backed securities	1,871,339	—	—	—	—	—	—	—	—	—	1,871,339
Other collateralized mortgage-backed securities	32,753	—	25,698	5,792	2,400	8,203	—	10,909	—	24,351	110,106
Asset-backed securities	55,482	—	4,958	—	—	—	2,014	1,680	—	—	64,134
Total	$ 2,063,307	$ 30,000	$ 30,656	$ 5,792	$ 2,400	$ 8,203	$ 2,014	$ 12,589	—	$ 24,351	$2,179,312

Capital Adequacy

Bank Class A Cumulative Perpetual Preferred Stock (Class A preferred stock) – On November 7, 2003, the bank issued 100,000 shares of $1,000 per share par value Class A preferred stock for net proceeds of $98,644, after expenses of $1,356 associated with the offering. The dividend rate is 7.561 percent, payable semi-annually to December 15, 2013, after which dividends are payable quarterly at a rate equal to the three-month London Interbank Offered Rate (LIBOR) plus 445.75 basis points. On September 26, 2005, the bank issued an additional 100,000 shares of cumulative perpetual preferred stock with the same terms. During 2010, the bank repurchased $18.0 million par value of the Class A preferred stock at net premium and costs of $529. For regulatory purposes, the preferred stock is treated as equity, and is not mandatorily redeemable. The preferred stock ranks, as to dividends and other distributions (including patronage) upon liquidation, dissolution or winding up, prior to all other classes and series of equity securities of the bank. In 2010, Class A preferred stock dividends of $21,851 were declared, of which $14,970 were paid and $6,881 were payable at December 31, 2010, which is an accrual of the amount payable on the next dividend date, June 15, 2011, required by "dividend/patronage stopper" clauses in the preferred stock offerings. The clauses require the payment or declaration of current period dividends on the preferred stock issuances before any other patronage can be declared, and was required before payment of the December 31, 2010, bank investment and direct note patronage to associations and OFIs could be paid.

Bank Class B Non-cumulative Subordinated Perpetual Preferred Stock (Class B preferred stock) – On August 26, 2010, the bank issued $300.0 million of Class B non-cumulative subordinated perpetual preferred stock, representing three hundred thousand shares at $1,000 per share par value for net proceeds of $296.6 million. The net proceeds of the issuance were used to increase the bank's capital and for general corporate purposes. Dividends on the preferred stock, if declared by the board of directors at its sole discretion, are non-cumulative and are payable semi-annually in arrears on the fifteenth day of June and December in each year, commencing December 15, 2010, at an annual fixed rate of 10 percent of par value of $1,000 per share. The Class B preferred stock is not mandatorily redeemable at any time, but may be redeemed in whole or in part at the option of the bank after the dividend payment date in June 2020. The Class B preferred stock ranks junior, both as to dividends and upon liquidation to our Class A preferred stock, and senior to all of our outstanding capital stock. For regulatory purposes, the Class B preferred stock is included in permanent capital, total surplus and core surplus within certain limitations. Due to regulatory limitations on third-party capital, the preferred stock issuance will require that subordinated debt no longer receive favorable treatment in net collateral ratio calculations. In 2010, Class B preferred stock dividends of $23,750 were declared, of which $8,750 were paid and $15,000 were payable at December 31, 2010, which is an accrual of the amount payable on the next dividend date, June 15, 2011, required by "dividend/patronage stopper" clauses in the preferred stock offerings. The clauses require the payment or declaration of current period dividends on the preferred stock issuances before any other patronage can be declared, and was required before payment of the December 31, 2010, bank investment and direct note patronage to associations and OFIs could be paid.

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 $2.97 billion capital position of the district at December 31, 2010, reflects an increase of 17.8 percent over the December 31, 2009, capital position of $2.52 billion. This increase is attributable to net income of $275.3 million earned in 2010, the bank's issuance of $300.0 million of Class B preferred stock net of issuance costs of $3.4 million, an increase in unrealized net gains on investment securities totaling $11.4 million, an $18.1 million amortization related to retirement benefits, and an increase of $54 in net adjustments related to two mergers of four district associations, offset by patronage paid of $82.8 million, dividends accrued on preferred stock totaling $21.9 million, dividends paid on preferred stock totaling $23.7 million, an $18.0 million repurchase of the bank's Class A cumulative perpetual preferred stock net of premium and costs on redemption of $529, retirement of $2.8 million of association preferred stock, a $2.0 million unrealized loss on cash flow derivatives, and a net decrease in capital stock and allocated earnings of $733.

The return on average members' equity for the year ended December 31, 2010, was 9.9 percent, compared to 8.0 percent and 11.4 percent reported for the years ended December 31, 2009 and 2008, respectively.

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, 2010, 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 22.0 percent at December 31, 2010, 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.

Figure 7

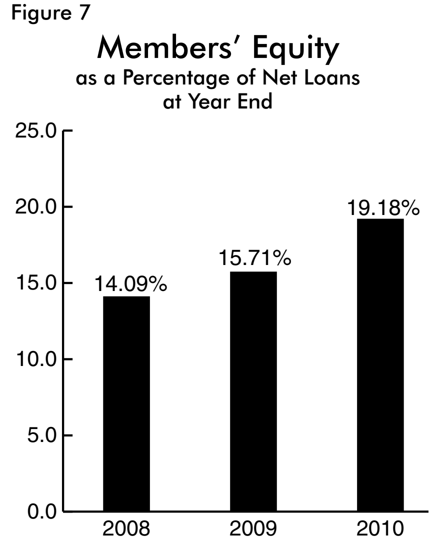


Figure 8

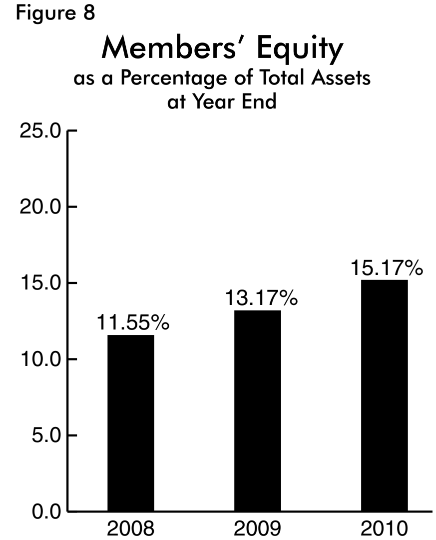
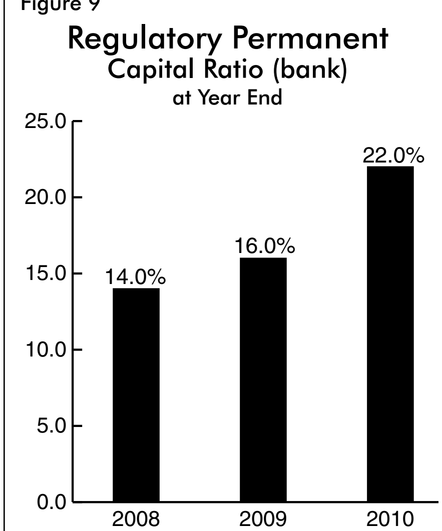


Figure 9



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. The board of directors is responsible for defining the role of the audit committee in providing oversight and review of the institution's internal controls.

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 July 2010, the Financial Accounting Standards Board (FASB) issued guidance on "Disclosures about the Credit Quality of Financing Receivables and the Allowance for Credit Losses," which is intended to provide additional information to assist financial statement users in assessing an entity's credit risk exposures and evaluating the adequacy of the allowance for credit losses. Existing disclosures are amended to include additional disclosures of financing receivables on a disaggregated basis (by portfolio segment and class of financing receivable) including among others, a rollforward schedule of the allowance for credit losses from the beginning of the reporting period to the end of the period on a portfolio segment basis, with the ending balance further disaggregated on the basis of the method of impairment (individually or collectively evaluated). The guidance also calls for new disclosures including but not limited to credit quality indicators at the end of the reporting period by class of financing receivables, the aging of past due financing receivables and the effect on the allowance for credit losses. For public entities, the disclosures as of the end of a reporting period are effective for interim and annual reporting periods ending after December 15, 2010. The disclosures about activity that occurs during a reporting period are effective for interim and annual reporting periods beginning on or after December 15, 2010. The adoption of this Standard did not have an impact on the bank's or associations' financial conditions or results of operations, but did result in additional disclosures.

In January 2010, the FASB issued guidance on "Fair Value Measurements and Disclosures," which is to improve disclosures about fair value measurement by increasing transparency in financial reporting. The changes provide a greater level of disaggregated information and more robust disclosures of valuation techniques and inputs to fair value measurement. The new disclosures and clarification of existing disclosures were effective for interim and annual reporting periods beginning after December 15, 2009, except for the disclosures about purchases, sales, issuances and settlements in the rollforward of activity in Level 3 fair value measurements. Those disclosures are effective for fiscal years beginning after December 15, 2010, and for interim periods within those fiscal years. The adoption of this Standard had no impact on the district's financial condition and results of operations but resulted in additional disclosures.

In June 2009, the FASB issued guidance on "Accounting for Transfers of Financial Assets," which amends previous guidance by improving the relevance, representational faithfulness, and comparability of the information that a reporting entity provides in its financial statements about a transfer of financial assets; the effects of a transfer on its financial position, financial performance, and cash flows; and a transferor's continuing involvement, if any, in transferred financial assets.

This guidance was effective as of the beginning of each reporting entity's first annual reporting period that begins after November 15, 2009, for interim periods within that first annual reporting period and for interim and annual reporting periods thereafter. Earlier application was prohibited. This Statement must be applied to transfers occurring on or after the effective date. Additionally, on and after the effective date, the concept of a qualifying special purpose entity is no longer relevant for accounting purposes. Therefore, formerly qualifying special-purpose entities (as defined under previous accounting standards) should be evaluated for consolidation by reporting entities on and after the effective date in accordance with the applicable consolidation guidance. If the evaluation on the effective date results in consolidation, the reporting entity should apply the transition guidance provided in the pronouncement that requires consolidation. The district reviewed their loan participation agreements to ensure that participations would meet the requirements for sales treatment and not be required to be consolidated. The impact of adoption on January 1, 2010 was immaterial to the district's financial condition and results of operations.

In June 2009, the FASB also issued guidance to improve financial reporting for those enterprises involved with variable interest entities, which amends previous guidance by requiring an enterprise to perform an analysis to determine whether the enterprise's variable interest or interests give it a controlling financial interest in a variable interest entity. Additionally, an enterprise is required to assess whether it has an implicit financial responsibility to ensure that a variable interest entity operates as designed when determining whether it has the power to direct the activities of the variable interest entity that most significantly impact the entity's economic performance.

This guidance was effective as of the beginning of each reporting entity's first annual reporting period that begins after November 15, 2009, for interim periods within that first annual reporting period and for interim and annual reporting periods thereafter. Earlier application was prohibited. The district reviewed its transactions that are included in the scope of this guidance and determined that the impact of adoption on January 1, 2010 was immaterial to the district's financial condition and results of operations.

Association Structural Changes

In January 2010, four FLCAs restructured to form ACA structures with operating FLCA and Production Credit Association subsidiaries.

In 2010 there were two acquisitions affecting four district associations. Effective July 1, 2010, Texas AgFinance, FCS acquired AgCredit of South Texas, ACA, and, effective December 1, 2010, Southern AgCredit, ACA purchased Louisiana Ag Credit, ACA. Both acquisitions were accounted for under the acquisition method of accounting under generally accepted accounting principles. The mergers are more fully discussed in Note 19, "Association Mergers."

As of December 31, 2010, there were 16 ACAs and one FLCA, totaling 17 associations within the district.

Regulatory Matters

As of December 31, 2010, the Farm Credit Administration had enforcement actions in place against three associations in the district, which have not had, and are not expected to have, a significant impact on the bank.

On April 12, 2010, FCA published a final rule that consolidates general election procedures, clarifies the role of nominating committees, enhances the eligibility and disclosure requirements for director candidates, improves annual meeting information statement instructions and adds new regulations on floor nominations and meetings of stockholders. This regulation became effective May 24, 2010.

On May 18, 2010, FCA published a proposed rule that would amend its rules on loan policies to permit System institutions with direct lending authority to purchase from the Federal Deposit Insurance Corporation (FDIC) loans to farmers, ranchers, producers or harvesters of aquatic products and cooperatives that meet eligibility and scope of financing requirements in order to provide liquidity and a stable source of funding and credit for borrowers in rural areas affected by the failure of lending institutions insured by the FDIC. The comment period for this proposed rule expired on July 19, 2010 and was re-opened on September 16, 2010. This second comment period expired on October 18, 2010.

On July 8, 2010, the FCA published an advance notice of proposed rulemaking to facilitate the development of capital adequacy regulations that would more closely align the minimum capital requirements for the System with the Tier 1/Tier 2 capital structure delineated in the new Basel Accord and the capital requirements of the other federal banking regulators. FCA has extended the deadline for comments until May 4, 2011.

On July 28, 2010, FCA, together with the Office of the Comptroller of the Currency, the Federal Reserve Board, the Federal Deposit Insurance Corporation, the Office of Thrift Supervision, and the National Credit Union Administration, published a joint final rule to implement the requirement of the Secure and Fair Enforcement for Mortgage Licensing Act to develop and maintain a system for registering mortgage loan originators employed by institutions regulated by these agencies. The rule became effective October 1, 2010, and compliance becomes mandatory on July 29, 2011.

On August 18, 2010, the FCA published a proposed rule that would lower the current limit on extensions of credit to a single borrower for each System institution operating under title I or II, and would require each System institution to adopt written policies that effectively identify, limit, measure and monitor their exposures to loan and lease concentration risks. The comment period for this proposed rule expired on October 18, 2010.

On November 18, 2010, FCA published an advance notice of proposed rulemaking requesting comments on ways to clarify and enhance FCA's regulations related to System institutions' disclosures to shareholders and investors on compensation, retirement programs and related benefits for senior officers, highly compensated individuals, and certain individual employees or other groups of employees. Comments on this proposed rule are due March 18, 2011.

In addition to the above regulations, FCA issued three bookletters in 2010: BL-062, dated May 13, 2010, providing guidance for the pricing and structure of loans to ensure earnings performance; BL-063, dated July 8, 2010, communicating FCA's expectations for the submission of proposals to merge System banks; and BL-064, dated December 9, 2010, providing clarification and guidance regarding FCA's regulations and expectations with respect to the key elements of an investment asset management framework that each System institution should establish to prudently manage its investments.

Also, on August 18, 2010, FCA published for comment a Joint and Several Liability Reallocation Agreement ("Reallocation Agreement") to be entered into by all of the System banks that would establish a procedure for non-defaulting banks to pay maturing Systemwide debt obligations on behalf of defaulting banks based upon a bank's pro-rata share of outstanding System-wide indebtedness prior to a statutory joint and several liability call by FCA based on a bank's share of available collateral. On October 20, 2010, FCA published notice of its approval of the Reallocation Agreement. On December 9, 2010, FCA published notice of its approval of an amendment to the Amended and Restated Market Access Agreement to be entered into by all System banks that conforms that agreement to the amended Reallocation Agreement.

The Dodd-Frank Wall Street Reform and Consumer Protection Act (the Dodd-Frank Act) was signed into law on July 21, 2010. While the Dodd-Frank Act represents a significant overhaul of many aspects of the regulation of the financial services industry, many of the statutory provisions of the act are not applicable to the System. While the act creates new regulators and expands the authority of the Federal Reserve Board over non-bank financial companies previously not subject to regulatory jurisdiction, it largely preserves the authority of the Farm Credit Administration as the System's independent federal regulator by excluding System institutions from consideration as non-bank financial companies. The act also provides other exemptions and exclusions from certain of the law's provisions. The Dodd-Frank Act's provisions pertaining to the regulation of over-the-counter derivatives, requiring more of these transactions to utilize third-party clearinghouses and cash collateral, may make these transactions more costly and less attractive as risk management tools for System institutions. Certain provisions within the act call for studies and recommendations related to the future of other housing government-sponsored enterprises (GSEs), and while they do not specifically include or relate to the System, a potential risk exists that the System, as a GSE, may directly or indirectly be impacted by decisions yet to be made by Congress.

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Report of Independent Auditors

To the Board of Directors and Shareholders
of the Farm Credit Bank of Texas and the Texas 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 Texas District Associations (District) at December 31, 2010, 2009 and 2008, 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

March 1, 2011

COMBINED FINANCIAL STATEMENTS

Combined Balance Sheets

FARM CREDIT BANK OF TEXAS AND DISTRICT ASSOCIATIONS

(dollars in thousands)	December 31, 2010	2009	2008
Assets			
Cash	**$ 453,322**	$ 500,967	$ 56,882
Federal funds sold	**20,438**	20,490	176,698
Investment securities	**3,231,562**	2,179,312	3,046,397
Loans	**15,628,890**	16,167,170	16,590,071
Less allowance for loan losses	**163,145**	144,731	51,653
Net loans	**15,465,745**	16,022,439	16,538,418
Accrued interest receivable	**154,023**	177,094	202,807
Other property owned, net	**78,124**	53,324	6,495
Premises and equipment, net	**62,539**	55,525	49,499
Other assets	**89,831**	108,012	89,116
Total assets	**$ 19,555,584**	$ 19,117,163	$ 20,166,312
Liabilities and members' equity			
Liabilities			
Bonds and notes, net	**$ 16,179,932**	$ 16,169,479	$ 17,302,205
Subordinated debt	**50,000**	50,000	50,000
Accrued interest payable	**45,881**	70,074	103,288
Patronage distributions payable	**66,011**	42,974	55,024
Preferred stock dividends payable	**21,881**	—	—
Other liabilities	**225,548**	267,232	326,078
Total liabilities	**16,589,253**	16,599,759	17,836,595
Commitments and contingencies (Note 12)			
Members' equity			
Preferred stock	**482,000**	202,754	202,754
Common stock and participation certificates	**61,843**	63,202	63,859
Allocated retained earnings	**327,435**	266,991	211,450
Unallocated retained earnings	**2,121,822**	2,061,299	1,984,421
Additional paid-in-capital	**22,622**	—	—
Accumulated other comprehensive loss	**(49,391)**	(76,842)	(132,767)
Total members' equity	**2,966,331**	2,517,404	2,329,717
Total liabilities and members' equity	**$ 19,555,584**	$ 19,117,163	$ 20,166,312

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)	**2010**	2009	2008
Investment securities and other	**$ 77,701**	$ 88,441	$ 111,358
Loans	**797,608**	873,032	1,006,081
Total interest income	**875,309**	961,473	1,117,439
Bonds, notes and subordinated debt	**270,945**	396,467	541,316
Notes payable and other	**24,194**	29,214	105,695
Total interest expense	**295,139**	425,681	647,011
Net interest income	**580,170**	535,792	470,428
Provision for loan losses	**141,457**	172,140	53,514
Net interest income after provision for loan losses	**438,713**	363,652	416,914
Patronage income	**16,845**	17,626	17,420
Fees for loan-related services	**29,577**	17,885	16,933
Gain from sale of investment securities	**529**	7,650	2,556
Refunds from Farm Credit System Insurance Corporation	**22,268**	—	—
Other (losses) gains, net	**(6,347)**	1,462	482
Miscellaneous income, net	**684**	1,123	1,093
Impairment losses on investments			
Total other-than-temporary impairment losses	**(2,743)**	(11,804)	(2,238)
Less: portion of loss recognized in other comprehensive income	**913**	6,511	—
Net impairment loss recognized in earnings	**(1,830)**	(5,293)	(2,238)
Total noninterest income	**61,726**	40,453	36,246
Salaries and employee benefits	**131,661**	101,700	94,043
Occupancy and equipment expense	**15,071**	13,763	13,105
Insurance Fund premiums	**7,720**	31,265	24,248
Losses on other property owned, net	**15,152**	7,803	374
Other operating expenses	**55,809**	53,759	53,318
Total noninterest expense	**225,413**	208,290	185,088
Income before income taxes	**275,026**	195,815	268,072
(Benefit from) provision for income taxes	**(291)**	(2,609)	344
Net income	**$ 275,317**	$ 198,424	$ 267,728

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	Additional Paid-in-Capital	Accumulated Other Comprehensive (Loss) Income	Total Members' Equity
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 benefits measurement date	—	—	—	(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
Noncredit portion of previous other-than-temporary impairment losses	—	—	—	1,527	1,527	—	(1,527)	—
Balance at January 1, 2009	202,754	63,859	211,450	1,985,948	2,197,398	—	(134,294)	2,329,717
Comprehensive income								
Net Income	—	—	—	198,424	198,424	—	—	198,424
Change in pension and postretirement benefit plans	—	—	—	—	—	—	19,028	19,028
Net change in unrealized net gains on investment securities	—	—	—	—	—	—	42,166	42,166
Noncredit portion of current other-than-temporary impairment losses	—	—	—	—	—	—	(6,511)	(6,511)
Net change in unrealized gains on cash flow hedge derivatives	—	—	—	—	—	—	2,769	2,769
Total comprehensive income	—	—	—	198,424	198,424	—	57,452	255,876
Capital stock/participation certificates issued	—	7,601	—	—	—	—	—	7,601
Capital stock/participation certificates and allocated retained earnings retired	—	(8,258)	(107)	—	(107)	—	—	(8,365)
Cash dividends on preferred stock	—	—	—	(15,122)	(15,122)	—	—	(15,122)
Patronage distributions								
Cash	—	—	—	(52,303)	(52,303)	—	—	(52,303)
Members' equity	—	—	55,648	(55,648)	—	—	—	—
Balance at December 31, 2009	202,754	63,202	266,991	2,061,299	2,328,290	—	(76,842)	2,517,404
Comprehensive income								
Net Income	—	—	—	275,317	275,317	—	—	275,317
Change in pension and postretirement benefit plans	—	—	—	—	—	—	18,085	18,085
Net change in unrealized net gains on investment securities	—	—	—	—	—	—	12,280	12,280
Noncredit portion of current other-than-temporary impairment losses	—	—	—	—	—	—	(913)	(913)
Net change in unrealized losses on cash flow hedge derivatives	—	—	—	—	—	—	(2,001)	(2,001)
Total comprehensive income	—	—	—	275,317	275,317	—	27,451	302,768
Capital stock/participation certificates and allocated retained earnings issued	—	4,606	626	—	626	—	—	5,232
Capital stock/participation certificates retired	—	(5,965)	—	—	—	—	—	(5,965)
Preferred stock issued	300,000	—	—	—	—	—	—	300,000
Issuance costs on preferred stock	—	—	—	(3,432)	(3,432)	—	—	(3,432)
Preferred stock repurchased	(20,754)	—	—	—	—	—	—	(20,754)
Net premium and costs on repurchase of preferred stock	—	—	—	(529)	(529)	—	—	(529)
Impact of association merger:								
Equity issued upon association merger	—	3,688	—	—	—	22,622	—	26,310
Equity retired upon association merger	—	(3,688)	—	(22,568)	(22,568)	—	—	(26,256)
Preferred stock dividends accrued	—	—	—	(21,881)	(21,881)	—	—	(21,881)
Cash dividends on preferred stock	—	—	—	(23,720)	(23,720)	—	—	(23,720)
Patronage distributions								
Cash	—	—	—	(82,846)	(82,846)	—	—	(82,846)
Members' equity	—	—	59,818	(59,818)	—	—	—	—
Balance at December 31, 2010	**$ 482,000**	**$ 61,843**	**$ 327,435**	**$ 2,121,822**	**$ 2,449,257**	**$ 22,622**	**$ (49,391)**	**$ 2,966,331**

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

(dollars in thousands)	Year Ended December 31, 2010	2009	2008
Operating Activities			
Net income	**$ 275,317**	$ 198,424	$ 267,728
Reconciliation of net income to net cash provided by operating activities			
Provision for loan losses	**141,457**	172,140	53,514
Provision for losses on other property owned	**13,167**	7,349	458
Depreciation and amortization on premises and equipment	**6,275**	6,075	5,715
Accretion of net discount on loans	**(736)**	(1,005)	(1,263)
Amortization and accretion on debt instruments	**(4,821)**	(4,045)	(2,240)
Accretion of net (discount) premium on investments	**(5,773)**	4,062	(1,405)
Gain on sale of investment securities	**(529)**	(7,650)	(2,556)
Loss on impairment of available-for-sale investments	**1,830**	5,293	2,238
Allocated equity patronage from System bank	**(12,487)**	(11,780)	(6,468)
Gain on sales of other property owned, net	**(1,292)**	(686)	(297)
Gain on sales of premises and equipment	**(5,696)**	(4,501)	(2,932)
Decrease in accrued interest receivable	**23,071**	25,713	25,405
Decrease (increase) in other assets, net	**22,598**	(8,760)	(9,077)
Decrease in accrued interest payable	**(24,193)**	(33,214)	(19,171)
(Decrease) increase in other liabilities, net	**(20,080)**	(1,752)	8,819
Net cash provided by operating activities	**408,108**	345,663	318,468
Investing Activities			
Net decrease (increase) in federal funds sold	**52**	156,208	(51,196)
Investment securities:			
Purchases	**(2,075,085)**	(1,419,563)	(4,338,753)
Proceeds from maturities, calls and prepayments	**971,512**	2,147,272	3,572,339
Proceeds from sales	**66,635**	165,512	116,785
Redemption of (investment in) Farmer Mac preferred stock	**7,000**	—	(7,000)
Decrease (increase) in loans, net	**384,652**	243,832	(1,514,401)
(Expenditures) proceeds from (purchase) sale of loans	**(32,822)**	(100,000)	800,000
Proceeds from sales of other property owned, net	**27,468**	18,341	8,935
Proceeds from sales of premises and equipment	**4,119**	3,944	2,872
Expenditures for premises and equipment	**(11,712)**	(11,544)	(12,555)
Net cash (used in) provided by investing activities	**(658,181)**	1,204,002	(1,422,974)
Financing Activities			
Bonds and notes issued	**19,497,527**	42,684,817	57,398,132
Subordinated debt issued, net of costs	—	—	49,458
Bonds and notes retired	**(19,483,209)**	(43,682,950)	(56,243,332)
Decrease in advanced conditional payments	**(2,967)**	(27,208)	(2,014)
Equity issued upon merger	**54**	—	—
Bank Class B preferred stock issued	**300,000**	—	—
Issuance costs on preferred stock	**(3,432)**	—	—
Bank Class A preferred stock repurchased	**(18,000)**	—	—
Association preferred stock retired	**(2,754)**	—	—
Net premium and costs on repurchase of Class A preferred stock	**(529)**	—	—
Capital stock and participation certificates issued	**5,232**	7,601	13,594
Capital stock and participation certificates retired and allocated retained earnings distributed	**(5,965)**	(8,365)	(14,755)
Cash dividends on preferred stock	**(23,720)**	(15,122)	(15,122)
Cash dividends and patronage distributions paid	**(59,809)**	(64,353)	(80,276)
Net cash provided by (used in) financing activities	**202,428**	(1,105,580)	1,105,685
Net (decrease) increase in cash	**(47,645)**	444,085	1,179
Cash at beginning of year	**500,967**	56,882	55,703
Cash at end of year	**$ 453,322**	$ 500,967	$ 56,882
Supplemental Schedule of Noncash Investing and Financing Activities			
Financed sales of other property owned	**$ 11,835**	$ 24,884	$ —
Loans transferred to other property owned	**75,978**	96,717	13,560
Net increase (decrease) in unrealized gains on investment securities	**11,367**	34,128	(15,952)
Patronage distributions payable	**66,011**	42,974	55,024
Traded but not settled participation loan sales	—	29,178	—
Transfer of surplus to additional paid-in-capital related to association merger	**22,568**	—	—
Supplemental Schedule of Noncash Changes in Fair Value Related to Hedging Activities			
Increase (decrease) in bonds and notes	**$ 956**	$ (30,548)	$ 25,630
Supplemental Information			
Cash paid during the year for:			
Interest	**$ 319,332**	$ 458,895	$ 666,182
Income taxes	**291**	345	826

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 Farm Credit Bank of Texas and affiliated associations (district). The district's one FLCA, 16 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, 2010. The FLCA 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 FCA examines the activities of System institutions to ensure their compliance with the Farm Credit Act, FCA regulations, and safe and sound banking practices.

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.

The FLCA borrows funds from the bank and in turn originates and services 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, Louisiana, Mississippi, New Mexico and Texas, the bank may discount or purchase from the FLCA 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 adjusted outstanding insured debt 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 (adjusted to reflect the reduced risk on loans or investments guaranteed by federal or state governments) 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 and may return excess funds above the secure base amount to System institutions.

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 bank's investments are to be held for an indefinite time period and, accordingly, have been classified as available for sale at December 31, 2010, 2009 and 2008, respectively. These investments are reported at fair value, and unrealized holding gains and losses on investments are netted and reported as a separate component of members' equity in the balance sheet. Changes in the fair value of these investments are reflected as direct charges or credits to other comprehensive income, unless the investment is deemed to be other-than-temporarily impaired. 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. Impairment is considered to be other-than-temporary if the present value of cash flows expected to be collected from the debt security is less than the amortized cost basis of the security (any such shortfall is referred to as a "credit loss"). If an entity intends to sell an impaired debt security or is more likely than not to be required to sell the security before recovery of its amortized cost basis less any current-period credit loss, the impairment is other-than-temporary and should be recognized currently in earnings in an amount equal to the entire difference between fair value and amortized cost. If a credit loss exists, but an entity does not intend to sell the impaired debt security and is not more likely than not to be required to sell before recovery, the impairment is other-than-temporary and should be separated into (i) the estimated amount relating to credit loss, and (ii) the amount relating to all other factors. Only the estimated credit loss amount is recognized currently in earnings, with the remainder of the loss amount recognized in other comprehensive income. In subsequent periods, if the present value of cash flows expected to be collected is less than the amortized cost basis, the bank would record an additional other-than-temporary impairment and adjust the yield of the security prospectively. The amount of total other-than-temporary impairment for an available-for-sale security that previously was impaired is determined as the difference between its carrying amount prior to the determination of other-than-temporary impairment and its fair value. Gains and losses on the sales of investments available-for-sale are determined using the specific identification method. Neither the bank nor the associations hold investments for trading purposes. Premiums and discounts are amortized or accreted into interest income over the term of the respective issues.

The bank and associations may also hold additional investments in accordance with mission-related investment programs, approved by the Farm Credit Administration. These programs allow the bank to make investments that further the System's mission to serve rural America. Mission-related investments are not included in the bank's liquidity calculations and are not covered by the eligible investment limitations specified by the FCA regulations. Mission-related investments for which the bank has the intent and ability to hold to maturity are classified as held-to-maturity and carried at cost, adjusted for the amortization of premiums and accretion of discounts. In May 2008, the bank purchased mission-related rural housing mortgage-backed securities which constituted the bank's held-to-maturity investment portfolio. These securities had an amortized cost basis of $50.5 million and a fair market value of $51.6 million at December 31, 2008. In December 2009, these securities, which had an amortized cost basis of $39.4 million, were sold for a gain of $2.1 million to enhance the bank's liquidity position.

At December 31, 2010, the district held other investments, totaling $295.1 million, which consisted of Federal Agricultural Mortgage Corporation (Farmer Mac) guaranteed agricultural mortgage-backed securities (AMBS). The bank held AMBS with a fair value of $140.5 million in an available-for-sale other investments portfolio, and associations held AMBS with an amortized cost of $154.6 million in a held-to-maturity portfolio. The Farmer Mac securities are backed by loans originated by the associations and previously held by the associations under the Farmer Mac long-term standby commitments to purchase agreements.

Farmer Mac is a government-sponsored enterprise and is examined and regulated by FCA. It provides secondary market arrangements for agricultural and rural home mortgage loans that meet certain underwriting standards. Farmer Mac is authorized to provide loan guarantees or be a direct pooler of agricultural mortgage loans. Farmer Mac is owned by both System and non-System investors and its board of directors has both System and non-System representation. Farmer Mac is not liable for any debt or obligation of any System institution and no System institution other than Farmer Mac is liable for any debt or obligation of Farmer Mac.

The district's holdings in investment securities are more fully described in Note 3, "Investment Securities."

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 and are generally considered substandard or doubtful, which is in accordance with the loan rating model, as described below. 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 bank and related associations use a two-dimensional loan rating model based on an internally generated combined system risk rating guidance that incorporates a 14-point risk-rating scale to identify and track the probability of borrower default and a separate scale addressing loss given default over a period of time. Probability of default is the probability that a borrower will experience a default within 12 months from the date of the determination of the risk rating. A default is considered to have occurred if the lender believes the borrower will not be able to pay its obligation in full or the borrower is past due more than 90 days. The loss given default is management's estimate as to the anticipated economic loss on a specific loan assuming default has occurred or is expected to occur within the next 12 months.

Each of the probability of default categories carries a distinct percentage of default probability. The 14-point risk-rating scale provides for granularity of the probability of default, especially in the acceptable ratings. There are nine acceptable categories that range from a borrower of the highest quality to a borrower of minimally acceptable quality. The probability of default between 1 and 9 is very narrow and would reflect almost no default to a minimal default percentage. The probability of default grows more rapidly as a loan moves from a "9" to other assets especially mentioned and grows significantly as a loan moves to a substandard (viable) level. A substandard (non-viable) rating indicates that the probability of default is almost certain.

The credit risk rating methodology is a key component of the bank's and associations' allowance for loan losses evaluation, and is generally incorporated into the institution's loan underwriting standards and internal lending limit. 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 authoritative accounting guidance. 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 deed in lieu of foreclosure, is recorded at fair value, based on appraisal, less estimated selling costs upon acquisition. Any initial reduction in the carrying amount of a loan to the fair value of the collateral received is charged to the allowance for loan losses. On at least an annual basis, 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 years for automobiles. Computer software and hardware are amortized over three to 10 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, 2010, 2009 and 2008 were $88.7 million, $109.8 million and $271.5 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:

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. 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 authoritative accounting guidance. The bank and all associations provide certain health care 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. Participating employers are jointly and severally liable for their plan obligations. Upon withdrawal or termination of their participation in the plan, a participating employer must pay all associated costs of its withdrawal from the plan, including its unfunded liability (the difference between replacement annuities and the withdrawing employer's share of allocated plan assets) and associated costs of withdrawal. 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.

Certain qualified individuals in the bank also participated in a nonqualified supplemental defined benefit pension plan, which was terminated effective January 16, 2011, with no further vesting or benefit accrual after that date. All remaining vested benefits will be distributed to the participating bank employees in lump sums after a one-year deferral period.

Authoritative accounting guidance requires the accrual of the expected cost of providing postretirement benefits other than pensions (primarily health care benefits) to an employee and an employee's beneficiaries and covered dependents during the years that the employee renders service necessary to become eligible for these benefits.

H. Income Taxes:

The bank, the FLCA 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, 2010, deferred income taxes have not been provided by the ACAs and their PCA subsidiaries on $35.3 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 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:

In the normal course of business, we enter into derivative financial instruments, including interest rate swaps and caps, 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 authoritative accounting guidance, 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:

The Financial Accounting Standards Board (FASB) guidance 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. Included in Level 1 are assets held in trust funds, which 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. The market value of collateral assets and liabilities is their face value, plus accrued interest, as these instruments are cash balances; therefore, fair value approximates face value. Pension plan assets that are derived from observable inputs, including corporate bonds and mortgage-backed securities, are reported in Level 2.

Level 3 — Unobservable inputs are those that are supported by little or no market activity and that are significant to the determination of 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. This category generally includes the bank's Federal Agricultural Mortgage Corporation (Farmer Mac) guaranteed agricultural mortgage-backed securities (AMBS), non-agency securities, certain loans and other property owned.

The fair value disclosures are presented in Note 14, "Fair Value Measurements."

K. Recently Issued or Adopted Accounting Pronouncements:

In July 2010, the Financial Accounting Standards Board (FASB) issued guidance on "Disclosures about the Credit Quality of Financing Receivables and the Allowance for Credit Losses," which is intended to provide additional information to assist financial statement users in assessing an entity's credit risk exposures and evaluating the adequacy of the allowance for credit losses. Existing disclosures are amended to include additional disclosures of financing receivables on a disaggregated basis (by portfolio segment and class of financing receivable) including among others, a rollforward schedule of the allowance for credit losses from the beginning of the reporting period to the end of the period on a portfolio segment basis, with the ending balance further disaggregated on the basis of the method of impairment (individually or collectively evaluated). The guidance also calls for new disclosures including but not limited to credit quality indicators at the end of the reporting period by class of financing receivables, the aging of past due financing receivables, nature and extent of financing receivables modified as troubled debt restructurings by class, and the effect on the allowance for credit losses. For public entities, the disclosures as of the end of a reporting period are effective for interim and annual reporting periods ending after December 15, 2010. The disclosures about activity that occurs during a reporting period are effective for interim and annual reporting periods beginning on or after December 15, 2010. The adoption of this Standard did not have an impact on the district's financial condition or results of operations, but did result in additional disclosures.

In January 2010, the FASB issued guidance on "Fair Value Measurements and Disclosures," which is to improve disclosures about fair value measurement by increasing transparency in financial reporting. The changes provide a greater level of disaggregated information and more robust disclosures of valuation techniques and inputs to fair value measurement. The new disclosures and clarification of existing disclosures were effective for interim and annual reporting periods beginning after December 15, 2009, except for the disclosures about purchases, sales, issuances and settlements in the rollforward of activity in Level 3 fair value measurements. Those disclosures are effective for fiscal years beginning after December 15, 2010, and for interim periods within those fiscal years. The adoption of this Standard had no impact on the district's financial condition and results of operations but resulted in additional disclosures.

In June 2009, the FASB issued guidance on "Accounting for Transfers of Financial Assets," which amends previous guidance by improving the relevance, representational faithfulness, and comparability of the information that a reporting entity provides in its financial statements about a transfer of financial assets; the effects of a transfer on its financial position, financial performance and cash flows; and a transferor's continuing involvement, if any, in transferred financial assets.

This guidance was effective as of the beginning of each reporting entity's first annual reporting period that begins after November 15, 2009, for interim periods within that first annual reporting period and for interim and annual reporting periods thereafter. Earlier application was prohibited. This Statement must be applied to transfers occurring on or after the effective date. Additionally, on and after the effective date, the concept of a qualifying special purpose entity is no longer relevant for accounting purposes. Therefore, formerly qualifying special-purpose entities (as defined under previous accounting standards) should be evaluated for consolidation by reporting entities on and after the effective date in accordance with the applicable consolidation guidance. If the evaluation on the effective date results in consolidation, the reporting entity should apply the transition guidance provided in the pronouncement that requires consolidation. The district reviewed its loan participation agreements to ensure that participations would meet the requirements for sales treatment and not be required to be consolidated. The impact of adoption on January 1, 2010 was immaterial to the district's financial condition and results of operations.

In June 2009, the FASB also issued guidance to improve financial reporting for those enterprises involved with variable interest entities, which amends previous guidance by requiring an enterprise to perform an analysis to determine whether the enterprise's variable interest or interests give it a controlling financial interest in a variable interest entity. Additionally, an enterprise is required to assess whether it has an implicit financial responsibility to ensure that a variable interest entity operates as designed when determining whether it has the power to direct the activities of the variable interest entity that most significantly impact the entity's economic performance.

This guidance was effective as of the beginning of each reporting entity's first annual reporting period that begins after November 15, 2009, for interim periods within that first annual reporting period, and for interim and annual reporting periods thereafter. Earlier application was prohibited. The district reviewed transactions that are included in the scope of this guidance and determined that the impact of adoption on January 1, 2010 was immaterial to the district's financial condition and results of operations.

L. Off-Balance-Sheet Credit Exposures:

Commitments to extend credit are agreements to lend to customers, generally having fixed expiration dates or other termination clauses that may require payment of a fee. Commercial letters of credit are conditional commitments issued to guarantee the performance of a customer to a third party. These letters of credit are issued to facilitate commerce and typically result in the commitment being funded when the underlying transaction is consummated between the customer and third party. The credit risk associated with commitments to extend credit and commercial letters of credit is essentially the same as that involved with extending loans to customers and is subject to normal credit policies. Collateral may be obtained based on management's assessment of the customer's creditworthiness.

Note 3 — Investment Securities

The district's available-for-sale investments include a liquidity portfolio and a portfolio of other investments. The liquidity portfolio consists primarily of FDIC-guaranteed corporate debt instruments, mortgage-backed investments and asset-backed investments. At December 31, 2010, the district's other investments portfolio consisted of Farmer Mac AMBS purchased during the second quarter of 2010, including AMBS held by district associations in a held-to-maturity portfolio with an amortized cost of $154.6 million and AMBS held by the bank in an available-for-sale portfolio with a fair value of $140.5 million. The bank's AMBS were purchased from district associations as a part of the bank's Capitalized Participation Pool (CPP) program. In accordance with this program, any positive impact to the net interest income of the bank can be returned as patronage to the association if declared by the bank's board of directors. The declared patronage approximates the net earnings of the respective pool.

Investments in the available-for-sale liquidity portfolio follow:

	December 31, 2010				
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value	Weighted Average Yield
FDIC-guaranteed corporate debt	**$ 300,531**	**$ 1,724**	**$ (164)**	**$ 302,091**	**0.84%**
Federal agency collateralized mortgage-backed securities	**2,524,022**	**36,453**	**(1,046)**	**2,559,429**	**2.00**
Other collateralized mortgage-backed securities	**71,192**	**68**	**(6,342)**	**64,918**	**5.97**
Asset-backed securities	**11,493**	**1**	**(1,489)**	**10,005**	**3.13**
Total liquidity investments	**$2,907,238**	**$38,246**	**$ (9,041)**	**$2,936,443**	**1.97%**
Held-to-maturity investments:					
Agricultural mortgage-backed securities	**$ 154,616**	**$ 543**	**$ (1,283)**	**$ 153,876**	**5.17%**

	December 31, 2009				
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value	Weighted Average Yield
Corporate debt	$ 131,815	$ 1,918	$ —	$ 133,733	1.56%
Federal agency collateralized mortgage-backed securities	1,843,894	32,866	(5,421)	1,871,339	3.16
Other collateralized mortgage-backed securities	123,315	12	(13,221)	110,106	6.87
Asset-backed securities	67,069	416	(3,351)	64,134	2.66
Total liquidity investments	$ 2,166,093	$35,212	$(21,993)	$ 2,179,312	2.61%

There were no investments in the held-to-maturity portfolio at December 31, 2009.

	December 31, 2008				
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value	Weighted Average Yield
Agency debt	$ 500,000	$ 957	$ —	$ 500,957	3.54%
Commercial paper and other	536,970	1,490	(2,144)	536,316	0.84
Federal agency collateralized mortgage-backed securities	1,660,429	22,313	(1,709)	1,681,033	4.58
Other collateralized mortgage-backed securities	228,059	—	(35,478)	192,581	4.80
Asset-backed securities	91,310	118	(6,458)	84,970	4.17
Total liquidity investments	$ 3,016,768	$24,878	$(45,789)	$ 2,995,857	3.74%
Held-to-maturity investments:					
Mission-related	$ 50,540	$ 1,103	$ —	$ 51,643	4.98%

Investments in the available-for-sale other investments portfolio follow:

	December 31, 2010				
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value	Weighted Average Yield
Agricultural mortgage-backed securities	**$ 145,122**	**$ —**	**$(4,619)**	**$ 140,503**	**5.07%**

There were no investments in the available-for-sale other investments portfolio at December 31, 2009 or December 31, 2008.

A summary of contractual maturity, amortized cost, estimated fair value and weighted average yield of the available-for-sale liquidity portfolio at December 31, 2010, follows:

	Due In One Year Or Less	Due After One Year Through Five Years	Due After Five Years Through 10 Years	Due After 10 Years	Total
FDIC-guaranteed corporate debt	$131,785	$ 170,306	$ —	$ —	$ 302,091
Federal agency collateralized mortgage-backed securities	—	51,257	197,872	2,310,300	2,559,429
Other collateralized mortgage-backed securities	—	—	3,891	61,027	64,918
Asset-backed securities	—	3,245	—	6,760	10,005
Total fair value	$131,785	$ 224,808	$ 201,763	$2,378,087	$ 2,936,443
Total amortized cost	$130,081	$ 223,153	$ 198,437	$2,355,567	$ 2,907,238
Weighted average yield	1.57%	1.25%	2.68%	2.01%	1.97%

Collateralized mortgage obligations (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, 2010, the CMO portfolio had a weighted average remaining life of approximately two years.

Investments in the available-for-sale other investments portfolio are as follows:

	Due in One Year or Less	Due After One Year Through Five Years	Total
Fair value of agricultural mortgage-backed securities	$ 124,715	$ 15,788	$ 140,503
Total amortized cost	128,930	16,192	145,122
Weighted average yield	4.99%	5.70%	5.07%

Investments in the district's held-to-maturity investment portfolio follow:

	Due After One Year Through Five Years	Due After Five Years Through 10 Years	Total
Fair value	$ 124,453	$ 29,423	$ 153,876
Amortized cost	124,589	30,027	154,616
Weighted average yield	5.28%	4.71%	5.17%

At December 31, 2009, the available-for-sale investment portfolio included guaranteed Small Business Administration pooled securities totaling $35.8 million held by a district association. During the quarter ended March 31, 2010, the district association received $34.2 million in its sale of these pooled securities, realizing a gain of $529. Available-for-sale investments are recorded on the balance sheet at fair value; held-to-maturity investments are recorded at amortized cost.

The ratings of the eligible investments held for maintaining a liquidity reserve, managing short-term surplus funds and managing interest rate risk must meet the applicable regulatory guidelines, which require these securities to be high quality, senior class and rated triple-A at the time of purchase. To achieve the ratings, these securities have a guarantee of timely payment of principal and interest or credit enhancement achieved through over collateralization and the priority of payments of senior classes over junior classes. The bank performs analysis based on expected behavior of the loans, whereby these loan performance scenarios are applied against each security's credit-support structure to monitor credit-enhancement sufficiency to protect the investment. The model output includes projected cash flows, including any shortfalls in the capacity of the underlying collateral to fully return the original investment, plus accrued interest.

If an investment no longer meets the credit rating criteria, the investment becomes ineligible. The bank must dispose of an investment that becomes ineligible within six months, unless the Farm Credit Administration approves, in writing, a plan that authorizes the bank to divest over a longer period of time. At December 31, 2010, the bank held 12 investments that were ineligible for liquidity purposes by FCA standards. Those ineligible securities had an amortized cost basis of $57.1 million and a fair value of $50.5 million at December 31, 2010. The bank has received approval from the FCA to continue to hold these investments.

Proceeds and related gains and losses on investment securities follow:

	Year Ended December 31,		
	2010	2009	2008
Proceeds on sales	**$ 66,635**	$ 165,512	$ 114,424
Realized gains on sales	**529**	7,650	2,556
Realized losses due to impairment	**1,830**	5,293	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, 2010, the district had 46 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. 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.

	December 31, 2010					
	Less Than 12 Months		**Greater Than 12 Months**		**Total**	
	Fair Value	**Unrealized Losses**	**Fair Value**	**Unrealized Losses**	**Fair Value**	**Unrealized Losses**
FDIC-guaranteed corporate debt	**$ 199,490**	**$ (164)**	**$ —**	**$ —**	**$ 199,490**	**$ (164)**
Federal agency collateralized mortgage-backed securities	**514,760**	**(1,046)**	**—**	**—**	**514,760**	**(1,046)**
Other collateralized mortgage-backed securities	**9,647**	**(626)**	**50,691**	**(5,716)**	**60,338**	**(6,342)**
Asset-backed securities	**—**	**—**	**6,342**	**(1,489)**	**6,342**	**(1,489)**
Total	**$ 723,897**	**$ (1,836)**	**$ 57,033**	**$ (7,205)**	**$ 780,930**	**$ (9,041)**

	December 31, 2009					
	Less Than 12 Months		Greater Than 12 Months		Total	
	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
Federal agency collateralized mortgage-backed securities	$ 506,742	$ (5,240)	$ 33,840	$ (182)	$ 540,582	$ (5,422)
Other collateralized mortgage-backed securities	2,233	(4)	103,708	(13,216)	105,941	(13,220)
Asset-backed securities	—	—	28,307	(3,351)	28,307	(3,351)
Total	$ 508,975	$ (5,244)	$ 165,855	$ (16,749)	$ 674,830	$ (21,993)

	December 31, 2008					
	Less Than 12 Months		Greater Than 12 Months		Total	
	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
Collateralized mortgage securities	$ 404,984	$ (23,836)	$ 60,853	$ (13,351)	$ 465,837	$ (37,187)
Commercial paper	99,988	(12)	77,867	(2,133)	177,855	(2,145)
Asset-backed securities	—	—	67,041	(6,458)	67,041	(6,458)
Total	$ 504,972	$ (23,848)	$ 205,761	$ (21,942)	$ 710,733	$ (45,790)

Although net unrealized gain on investment securities has increased by $11.4 million during 2010, the fair value of some investments in the portfolios has been impacted as a result of turmoil in the credit markets. As more fully discussed in Note 2, the guidance for other-than-temporary impairment contemplates numerous factors in determining whether an impairment is other-than-temporary including: (i) whether or not an entity intends to sell the security; (ii) whether it is more likely than not that an entity would be required to sell the security before recovering its costs; or (iii) whether an entity does not expect to recover the security's entire amortized cost basis (even if it does not intend to sell).

The bank and associations perform an evaluation quarterly on a security-by-security basis considering all available information. If the bank or association intends to sell the security or it is more likely than not that it would be required to sell the security, the impairment loss equals the full difference between amortized cost and fair value of the security. When the bank or an association does not intend to sell securities in an unrealized loss position, other-than-temporary impairment is considered using various factors, including the length of time and the extent to which the fair value is less than cost, adverse conditions specifically related to the industry, geographic area and the condition of the underlying collateral, payment structure of the security, ratings by rating agencies, the creditworthiness of bond insurers and volatility of the fair value changes. A bank or association uses estimated cash flows over the remaining lives of the underlying collateral to assess whether credit losses exist. In estimating cash flows, the bank and associations consider factors such as expectations of relevant market and economic data, including underlying loan level data for mortgage-backed and asset-backed securities and credit enhancements.

The bank recognized other-than-temporary impairment losses on four mortgage-backed investments and two asset-backed investments during 2010. The credit portion of the impairment losses, totaling $1.8 million for 2010, was recognized as a loss in earnings of $1.3 million in the first quarter, $474 in the second quarter, and $14 in the fourth quarter. The non-credit-related impairment losses on the six investments, totaling $913, are included as a charge against other comprehensive income. Also, in accordance with guidance issued in 2009, $1.5 million in non-credit-related impairment losses taken as a charge against earnings during 2008 was added back to retained earnings and charged against accumulated other comprehensive income during the first quarter of 2009.

As the bank has no intent of selling the securities deemed other-than-temporarily impaired and will not more likely than not be required to sell the securities before recovery, the credit loss portion of impairment was recognized through earnings for 2010. To measure the amount related to credit loss in the determination of other-than-temporary impairment, the bank utilizes an independent third party's services for cash flow modeling and projection of credit losses for specific non-agency residential mortgage-backed securities and subprime asset-backed securities. Applicable securities are identified through prior analysis based on the deterioration of price and credit ratings. Significant inputs utilized in the methodology of the modeling include assumptions surrounding market data (interest rates and home prices) and the applicable securities' loan level data. Loan level data evaluated includes loan status, coupon and resets, FICO scores, loan-to-value, geography, property type, etc. Loan level data is then combined with assumptions surrounding future behavior of home prices, prepayment rates, default rates and loss severity to arrive at cash flow projections for the underlying collateral. Default rate assumptions are generally estimated using historical loss and performance information to estimate future defaults. The default rates used at December 31, 2010, ranged from 3.2 percent to 10.5 percent for non-agency mortgage-backed securities and ranged from 7.3 percent to 13.3 percent for the asset-backed securities. Prepayment rate assumptions are based on historical prepayment rates and ranged from 3.5 percent to 16.0 percent for non-agency mortgage-backed securities and ranged from 2.3 percent to 2.9 percent for the asset-backed securities at December 31, 2010. At December 31, 2010, the loss severity assumptions ranged from 33.6 percent to 52.1 percent for non-agency mortgage-backed securities and ranged from 57.9 percent to 68.4 percent for the asset-backed securities. The present value of these cash flow projections is then evaluated against the specific security's structure and credit enhancement to determine if the bond will absorb losses.

The following table details the activity related to the credit loss component of the amortized cost of debt securities that have been written down for other-than-temporary impairment and the credit component of the loss that is recognized in earnings for the past two years:

Credit losses for which a portion of an other-than-temporary impairment was recognized in OCI at December 31, 2009	$ 6,005
Additions for the amount related to credit loss for which other-than-temporary impairment was not previously recognized	300
Increase to amount related to credit loss for which other-than-temporary impairment was previously recognized when it did not intend to sell and it is not more likely than not that it will be required to sell	1,529
Credit losses for which a portion of an other-than-temporary impairment was recognized in OCI at December 31, 2010	$ 7,834

Credit losses for which a portion of an other-than-temporary impairment was recognized in OCI at December 31, 2008	$ 712
Additions for the amount related to credit loss for which other-than-temporary impairment was not previously recognized	3,594
Increase to amount related to credit loss for which other-than-temporary impairment was previously recognized when it did not intend to sell and it is not more likely than not that it will be required to sell	1,699
Credit losses for which a portion of an other-than-temporary impairment was recognized in OCI at December 31, 2009	$ 6,005

Note 4 — Loans and Allowance for Loan Losses

Loans comprised the following categories at December 31:

	2010	2009	2008
Real estate mortgage	**$ 10,487,949**	$ 11,040,592	$ 11,015,550
Production and intermediate term	**1,792,513**	1,965,720	2,268,893
Agribusiness			
Loans to cooperatives	**274,621**	151,580	188,105
Processing and marketing	**1,346,887**	1,251,631	1,392,895
Farm-related business	**172,501**	229,261	262,007
Communication	**264,634**	253,914	409,341
Energy	**881,227**	869,292	644,236
Water and waste disposal	**50,261**	50,000	50,172
Rural home	**209,708**	212,817	205,949
Mission-related	**64,096**	43,982	41,841
International	**245**	504	1,349
Loans to other financial institutions	**75,737**	93,878	106,126
Lease receivables	**8,511**	3,999	3,607
Total	**$ 15,628,890**	$ 16,167,170	$ 16,590,071

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*):

	2010		2009		2008	
Commodity	**Amount**	**%**	Amount	%	Amount	%
Livestock	**$ 5,975**	**38%**	$ 6,198	38%	$ 6,310	38%
Crops	**2,027**	**13**	2,292	14	2,255	14
Timber	**1,636**	**11**	1,712	11	1,855	11
Cotton	**757**	**5**	750	5	758	5
Poultry	**522**	**3**	625	4	681	4
Dairy	**479**	**3**	449	3	508	3
Rural home	**210**	**1**	213	1	206	1
Other	**4,023**	**26**	3,928	24	4,017	24
Total	**$ 15,629**	**100%**	$ 16,167	100%	$ 16,590	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.

In March 2010, the bank purchased loans which had experienced credit deterioration and other property owned from a district association. The purchase of the loan assets and other property owned by the bank was completed to ensure the district association remained a viable stand-alone institution. This purchase activity avoided a nonaccrual classification of a district association direct note receivable and protected the bank's charter in the state where the district association was located and has lending authorities. The loans, which had book balances at the association totaling $40,069, were purchased at fair value of $32,822. The fair value was derived by discounting the total estimated cash flows of $36,341 using appropriate yield curves, resulting in an accretable discount of $3,519. The bank recognized additional provisions for loan losses totaling $2,001 related to these loans during 2010, the effect of which reduces the resulting accretable discount, which will be accreted into interest income on a level-yield basis over the life of the loans. At December 31, 2010, after the pay-off of one of the loans in December 2010 and the transfer of loans to two borrowers to other property owned (OPO) in November 2010, the balance of these loans, net of the unaccreted discount of $1,814, was $21,911. In addition to these loans, the bank also purchased other property owned related to three other loans from the association at fair value of $2,917. In December 2010, one of the acquired properties was disposed of, leaving a balance of $2,838 in other property owned at December 31, 2010. The financial impact of the purchases to the bank is negligible due to the size of the bank's balance sheet and its financial strength. Because the assets were purchased at fair value, the transaction should not adversely impact future earnings as the assets are liquidated or refinanced over the next two to three years.

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 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,		
	2010	2009	2008
Nonaccrual loans			
Current as to principal and interest	**$ 282,850**	$ 211,756	$ 249,851
Past due	**400,217**	302,611	72,562
Total nonaccrual loans	**683,067**	514,367	322,413
Accrual loans			
Restructured	**8,983**	2,974	6,072
90 days or more past due	**2,396**	34,446	17,896
Total impaired accrual loans	**11,379**	37,420	23,968
Total impaired loans	**$ 694,446**	$ 551,787	$ 346,381

There were $22.5 million in commitments to lend additional funds to borrowers whose loans were classified as nonaccrual or restructured at December 31, 2010.

Nonperforming assets (including related accrued interest) and related credit quality statistics are as follows:

	December 31,		
	2010	2009	2008
Nonaccrual loans			
Real estate mortgage	**$ 440,836**	$ 259,301	$ 107,244
Production and intermediate term	**102,027**	87,976	132,579
Agribusiness	**129,220**	153,746	75,053
Communication	**6,129**	9,198	3,441
Rural residential real estate	**2,019**	1,829	1,306
Energy and water/waste disposal	**—**	2,317	60
Lease receivables	**2,836**	—	376
Mission-related loans	**—**	—	2,354
Total nonaccrual loans	**683,067**	514,367	322,413
Accruing restructured loans			
Real estate mortgage	**1,491**	1,304	4,524
Production and intermediate term	**2,510**	1,670	1,060
Agribusiness	**4,982**	—	488
Total accruing restructured loans	**8,983**	2,974	6,072
Accruing loans 90 days or more past due			
Real estate mortgage	**2,198**	23,393	2,147
Production and intermediate term	**93**	11,049	5,147
Agribusiness	**—**	—	10,355
Rural residential real estate	**105**	4	247
Total accruing loans 90 days or more past due	**2,396**	34,446	17,896
Total nonperforming loans	**694,446**	551,787	346,381
Other property owned	**78,124**	53,324	6,495
Total nonperforming assets	**$ 772,570**	$ 605,111	$ 352,876

The following table shows loans and related accrued interest classified under the Farm Credit Administration Uniform Loan Classification System as a percentage of total loans and related accrued interest receivable by loan type as of December 31:

	2010	2009	2008
Real estate mortgage			
Acceptable	**89.2%**	91.7%	96.4%
OAEM	**4.3**	3.5	2.1
Substandard/Doubtful	**6.5**	4.8	1.5
	100.0%	100.0%	100.0%
Production and intermediate term			
Acceptable	**83.0%**	83.1%	90.1%
OAEM	**8.1**	8.5	2.7
Substandard/Doubtful	**8.9**	8.4	7.2
	100.0%	100.0%	100.0%
Agribusiness			
Acceptable	**76.4%**	71.6%	87.7%
OAEM	**12.7**	13.8	4.9
Substandard/Doubtful	**10.9**	14.6	7.4
	100.0%	100.0%	100.0%
Energy and water/waste disposal			
Acceptable	**99.0%**	99.7%	100.0%
OAEM	**—**	—	—
Substandard/Doubtful	**1.0**	0.3	—
	100.0%	100.0%	100.0%
Communication			
Acceptable	**97.7%**	96.4%	98.9%
OAEM	**—**	—	0.3
Substandard/Doubtful	**2.3**	3.6	0.8
	100.0%	100.0%	100.0%

	2010	2009	2008
Rural residential real estate			
Acceptable	**95.2%**	96.7%	97.5%
OAEM	**2.7**	1.4	1.4
Substandard/Doubtful	**2.1**	1.9	1.1
	100.0%	100.0%	100.0%
International			
Acceptable	**100.0%**	100.0%	100.0%
OAEM	**—**	—	—
Substandard/Doubtful	**—**	—	—
	100.0%	100.0%	100.0%
Lease receivables			
Acceptable	**63.5%**	96.2%	87.0%
OAEM	**2.6**	3.8	2.7
Substandard/Doubtful	**33.9**	—	10.3
	100.0%	100.0%	100.0%
Loans to other financing institutions			
Acceptable	**100.0%**	100.0%	100.0%
OAEM	**—**	—	—
Substandard/Doubtful	**—**	—	—
	100.0%	100.0%	100.0%
Mission related			
Acceptable	**89.5%**	100.0%	100.0%
OAEM	**0.6%**	—	—
Substandard/Doubtful	**9.9%**	—	—
	100.0%	100.0%	100.0%
Total loans			
Acceptable	**87.9%**	89.3%	94.8%
OAEM	**5.3**	4.8	2.3
Substandard/Doubtful	**6.8**	5.9	2.9
	100.0%	100.0%	100.0%

The following table provides an age analysis of past due loans (including accrued interest) as of December 31, 2010:

	30-89 Days Past Due	90 Days or More Past Due	Total Past Due	Not Past Due or Less Than 30 Days Past Due	Total Loans	Greater Than 90 Days Past Due and Accruing
Real estate mortgage	$ 79,990	$ 238,037	$ 318,027	$ 10,279,673	$ 10,597,700	$ 2,198
Production and intermediate term	25,785	56,637	82,422	1,728,152	1,810,574	93
Agribusiness	15,708	53,973	69,681	1,732,337	1,802,018	—
Energy and water/waste disposal	—	—	—	937,912	937,912	—
Communication	—	—	—	265,495	265,495	—
Rural residential real estate	1,919	418	2,337	208,637	210,974	105
International	—	—	—	245	245	—
Lease receivables	2,809	—	2,809	5,813	8,622	—
Loans to OFIs	—	—	—	75,892	75,892	—
Mission related	—	—	—	64,501	64,501	—
Total	$ 126,211	$ 349,065	$ 475,276	$ 15,298,657	$ 15,773,933	$ 2,396

Note: The recorded investment in the receivable is the face amount increased or decreased by applicable accrued interest and unamortized premium, discount, finance charges, or acquisition costs and may also reflect a previous direct write-down of the investment.

Additional impaired loan information is as follows:

	Recorded Investment at 12/31/2010	Unpaid Principal Balance*	Related Allowance	Average Impaired Loans	Interest Income Recognized
Impaired loans with a related allowance for credit losses					
Real estate mortgage	$ 170,333	$ 209,522	$ 48,136	$ 151,736	$ 1,597
Production and intermediate term	45,839	57,932	24,336	45,242	492
Processing and marketing	52,836	60,998	12,205	37,319	381
Farm-related business	23,882	24,947	10,081	17,499	172
Energy and water/waste disposal	—	—	—	5	—
Communication	4,596	2,953	3,236	3,501	22
Rural residential real estate	617	659	121	698	9
Lease receivables	21	24	10	501	6
Total	$ 298,124	$ 357,035	$ 98,125	$ 256,501	$ 2,679
Impaired loans with no related allowance for credit losses					
Real estate mortgage	$ 274,192	$ 294,903	$ —	$ 244,233	$ 3,322
Production and intermediate term	58,791	87,771	—	62,293	723
Processing and marketing	34,776	59,385	—	49,471	551
Farm-related business	22,709	37,861	—	22,673	246
Energy and water/waste disposal	—	14,131	—	7	—
Communication	1,533	3,280	—	3,528	25
Rural residential real estate	1,507	1,732	—	1,067	14
Lease receivables	2,814	2,807	—	767	10
Total	$ 396,322	$ 501,870	$ —	$ 384,039	$ 4,891
Total impaired loans					
Real estate mortgage	$ 444,525	$ 504,425	$ 48,136	$ 395,969	$ 4,919
Production and intermediate term	104,630	145,703	24,336	107,535	1,215
Processing and marketing	87,612	120,383	12,205	86,790	932
Farm-related business	46,591	62,808	10,081	40,172	418
Energy and water/waste disposal	—	14,131	—	12	—
Communication	6,129	6,233	3,236	7,029	47
Rural residential real estate	2,124	2,391	121	1,765	23
Lease receivables	2,835	2,831	10	1,268	16
Total	$ 694,446	$ 858,905	$ 98,125	$ 640,540	$ 7,570

*Unpaid principal balance represents the contractual obligations of the loans

Interest income on nonaccrual and accruing restructured loans that would have been recognized under the original terms of the loans during 2010 were as follows:

	2010	2009	2008
Interest income which would have been recognized under the original loan terms	**$ 45,935**	$ 40,496	$ 20,727
Less: Interest income recognized	**7,570**	13,885	2,077
Foregone interest income	**$ 38,365**	$ 26,611	$ 18,650

A summary of changes in the allowance for loan losses and period end recorded investment (including accrued interest) in loans follows:

	Real Estate Mortgage	Production and Intermediate Term	Agribusiness	Communications	Energy and Water/Waste Disposal	Rural Residential Real Estate	International	Lease Receivables	Loans to OFIs	Mission Related	Total
Allowance for Credit Losses											
Balance at December 31, 2009	$ 97,132	$ 14,759	$ 23,054	$ 6,533	$ 3,134	$ 119	$ —	$ —	$ —	$ —	$ 144,731
Charge-offs	(66,492)	(16,722)	(25,743)	(2,272)	(17,745)	(127)	—	—	—	—	(129,101)
Recoveries	4,188	2,967	1,501	417	1,025	1	—	—	—	—	10,099
Provision for loan losses	65,345	30,286	29,844	(753)	15,687	1,002	1	45	—	—	141,457
Adjustment due to merger	(4,418)	—	—	—	—	—	—	—	—	—	(4,418)
Other	377	—	—	—	—	—	—	—	—	—	377
Balance at December 31, 2010	$ 96,132	$ 31,290	$ 28,656	$ 3,925	$ 2,101	$ 995	$ 1	$ 45	$ —	$ —	$ 163,145
Ending Balance: individually evaluated for impairment	$ 52,058	$ 24,509	$ 23,451	$ 3,236	$ —	$ 137	$ —	$ 10	$ —	$ —	$ 103,401
Ending Balance: collectively evaluated for impairment	$ 42,323	$ 6,666	$ 5,205	$ 689	$ 2,101	$ 858	$ 1	$ 35	$ —	$ —	$ 57,878
Ending Balance: loans acquired with deteriorated credit quality	$ 1,751	$ 115	$ —	$ —	$ —	$ —	$ —	$ —	$ —	$ —	$ 1,866
Recorded Investments in Loans Outstanding											
Balance at December 31, 2010	$ 10,597,700	$ 1,810,574	$ 1,802,018	$ 265,495	$ 937,912	$ 210,974	$ 245	$ 8,622	$ 75,892	$ 64,501	$15,773,933
Ending Balance: loans individually evaluated for impairment	$ 431,343	$ 102,896	$ 134,202	$ 6,129	$ —	$ 2,124	$ —	$ 2,836	$ —	$ —	$ 679,530
Ending Balance: loans collectively evaluated for impairment	$ 10,147,553	$ 1,702,004	$ 1,667,816	$ 259,366	$ 937,912	$ 208,850	$ 245	$ 5,786	$ 75,892	$ 64,501	$15,069,925
Ending Balance: loans acquired with deteriorated credit quality	$ 18,804	$ 5,674	$ —	$ —	$ —	$ —	$ —	$ —	$ —	$ —	$ 24,478

At December 31, 2010, the bank had a total of $3.4 billion of direct notes sold to another System bank. The sales included participations of eight of its direct notes receivable from district associations. The purpose of these sales was to diversify the credit exposure of the bank by providing capital for liquidity and expansion of the capital markets loan participations portfolio.

Note 5 — Premises and Equipment

Premises and equipment comprised the following at:

	December 31, 2010	2009	2008
Land	**$ 12,071**	$ 10,938	$ 10,875
Buildings and improvements	**41,940**	39,011	36,678
Furniture and equipment	**47,506**	42,586	36,254
	101,517	92,535	83,807
Accumulated depreciation	**(38,978)**	(37,010)	(34,308)
Total	**$ 62,539**	$ 55,525	$ 49,499

Included in the district's property and equipment at December 31, 2010, is $12.6 million in capitalized costs related to the bank's development of new lending systems, reflecting an increase of $3.5 million from the $9.1 million included in 2009. The first phase of the lending systems, designed for participation loans and direct notes, was implemented effective July 2010. Depreciation on that system began upon implementation. Depreciation on the second phase of the lending systems, designed for association retail loans, will begin when it is implemented. The new systems are designed to enhance the accounting and informational capabilities related to district association lending as well as the bank's capital markets loan portfolios.

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 was from September 1, 2003, to August 31, 2013. On November 16, 2010, the bank entered into a lease amendment which extended the term of the lease to August 31, 2024. In addition, the lease amendment included expansion of the leased space to approximately 111,500 square feet of office space. Under the terms of the lease amendment, the bank will pay annual base rental ranging from $18 per square foot in the first year to $26 per square foot in the last year. Annual lease expenses for the facility, including certain operating expenses passed through from the landlord, were $2.6 million, $2.8 million and $2.7 million for 2010, 2009 and 2008, respectively.

Following is a schedule of the minimum lease payments for the bank and district associations on leases:

	Minimum Lease Payments
2011	$ 6,348
2012	6,429
2013	5,897
2014	5,366
2015	5,960
Total minimum lease payments	$ 30,000

Note 6 — Other Assets and Other Liabilities

Other assets comprised the following at December 31:

	2010	2009	2008
Investment in another System bank	**$ 34,979**	$ 22,504	$ 10,742
Other accounts receivable	**21,914**	20,807	23,866
Unamortized debt issue costs	**9,242**	10,017	10,680
Fair value of derivatives	**6,512**	2,526	31,439
Deferred tax assets, net	**5,225**	5,013	2,231
Receivable on participation loan sales	**—**	29,178	—
Farmer Mac preferred stock	**—**	7,000	7,000
Other, net	**11,959**	10,967	3,158
Total	**$ 89,831**	$ 108,012	$ 89,116

Other liabilities comprised the following at December 31:

	2010	2009	2008
Pension liability	**$ 81,415**	$ 111,296	$ 139,783
Postretirement benefits	**49,442**	41,607	40,199
Accounts payable	**43,872**	37,645	34,163
Bank draft payable	**24,001**	17,218	32,382
Advance conditional payments	**19,314**	22,281	49,489
FCSIC premium payable	**6,049**	24,386	21,978
Income taxes payable	**392**	334	644
Deferred tax liabilities	**161**	371	410
Fair value of derivatives	**5**	30	3,074
Other, net	**897**	12,064	3,956
Total	**$ 225,548**	$ 267,232	$ 326,078

Note 7 — Bonds and Notes

Systemwide Debt Securities and Notes Payable:

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, 2010, the bank had such specified eligible assets totaling $14.0 billion, and obligations and accrued interest payable totaling $12.8 billion, resulting in excess eligible assets of $1.2 billion.

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, 2010, 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 district's participation in Systemwide debt securities and notes payable to other System bank at December 31, 2010 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
2011	$ 2,930.5	1.13%	$ —	—%	$ 2,072.3	0.25%	$ 3,400.0	0.72%	$ 8,402.8	0.75%
2012	2,162.6	1.09	—	—	—	—	—	—	2,162.6	1.09
2013	1,616.4	1.40	—	—	—	—	—	—	1,616.4	1.40
2014	1,293.8	1.81	—	—	—	—	—	—	1,293.8	1.81
2015	1,042.2	2.33	—	—	—	—	—	—	1,042.2	2.33
Subsequent years	1,662.1	3.55	—	—	—	—	—	—	1,662.1	3.55
Total	$ 10,707.6	1.74%	$ —	—%	$ 2,072.3	0.25%	$ 3,400.0	0.72%	$ 16,179.9	1.33%

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, 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, 2010, was 122 days.

The bank's Systemwide debt includes callable debt, consisting of the following at December 31, 2010:

Year of Maturity	Amount	Range of First Call Dates
2011	$ 200,000	1/6/2011 – 1/28/2011
2012	1,135,000	1/4/2011 – 6/14/2011
2013	1,160,000	1/3/2011 – 12/16/2011
2014	1,005,000	1/2/2011 – 9/2/2011
2015	870,000	1/16/2011 – 7/27/2012
Subsequent years	948,000	1/1/2011 – 6/22/2015
Total	$ 5,318,000	1/1/2011 – 6/22/2015

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 $50.0 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:

At December 31, 2010, the bank had a total of $3.4 billion of direct notes sold to another System bank. The sales included participations of eight of its direct notes receivable from district associations. The purpose of these sales was to diversify the credit exposure of the bank by providing capital for liquidity and expansion of the capital markets loan participations portfolio.

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, 2010, was 22.00 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, 2010:

	Permanent Capital Ratio Ranges %	Core Surplus Ratio Ranges %	Total Surplus Ratio Ranges %
Bank	22.00	10.67	17.83
FLCA	16.76	16.31	16.31
ACAs	11.27 – 19.08	11.06 – 18.49	11.06 – 18.49
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, 2010, the bank's net collateral ratio was 107.91 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, 2010	2009	2008
Stock				
Common – voting (eligible for dividends, convertible)	$ 5.00	**11,534,470**	11,759,905	11,899,534
Common – nonvoting (eligible for dividends, convertible)	$ 5.00	**41,429**	55,802	76,595
Preferred – nonvoting (eligible for dividends, nonconvertible)	$ 5.00	**—**	550,840	550,840
Participation certificates – nonvoting (eligible for dividends, convertible)	$ 5.00	**439,183**	430,705	396,849

The preferred stock noted above for prior years was nonvoting stock. It was issued by one association as evidence of borrowers' claims to allocated retained earnings of a specific year. The preferred stock was 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 FLCA 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 OFIs' 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, 2010, the bank had $1.77 million of common stock outstanding to OFIs at a par value of $5.00 per share.

Class A Cumulative Perpetual Preferred Stock (Class A preferred stock) – On November 7, 2003, the bank issued 100,000 shares at $1,000 per share par value of Class A preferred stock for net proceeds of $98,644, after expenses of $1,356 associated with the offering. The dividend rate is 7.561 percent, payable semi-annually to December 15, 2013, after which dividends are payable quarterly at a rate equal to the three-month London Interbank Offered Rate (LIBOR) plus 445.75 basis points. On September 26, 2005, the bank issued an additional 100,000 shares of cumulative perpetual preferred stock with the same terms. During 2010, the bank repurchased $18.0 million par value of the Class A preferred stock at a net premium and costs of $529. For regulatory purposes, the preferred stock is treated as equity, and is not mandatorily redeemable. Dividends on preferred stock are recorded as declared. The preferred stock ranks, as to dividends and other distributions (including patronage) upon liquidation, dissolution or winding up, prior to all other classes and series of equity securities of the bank. In 2010, Class A preferred stock dividends of $21,851 were declared, of which $14,970 were paid and $6,881 were payable at December 31, 2010, which is an accrual of the amount payable on the next dividend date, June 15, 2011, required by "dividend/patronage stopper" clauses in the preferred stock offerings. The clauses require the payment or declaration of current period dividends on the preferred stock issuances before any other patronage can be declared, and was required before payment of the December 31, 2010, bank investment and direct note patronage to associations and OFIs could be paid.

Class B Non-cumulative Subordinated Perpetual Preferred Stock (Class B preferred stock) – On August 26, 2010, the bank issued $300.0 million of Class B non-cumulative subordinated perpetual preferred stock, representing three hundred thousand shares at $1,000 per share par value for net proceeds of $296.6 million. The net proceeds of the issuance were used to increase the bank's capital and for general corporate purposes. Dividends on the preferred stock, if declared by the board of directors at its sole discretion, are non-cumulative and are payable semi-annually in arrears on the fifteenth day of June and December in each year, commencing December 15, 2010, at an annual fixed rate of 10 percent of par value of $1,000 per share. The Class B preferred stock is not mandatorily redeemable at any time, but may be redeemed in whole or in part at the option of the bank after the dividend payment date in June 2020. The Class B preferred stock ranks junior, both as to dividends and upon liquidation to our Class A preferred stock, and senior to all of our outstanding capital stock. For regulatory purposes, the Class B preferred stock is included in permanent capital, total surplus and core surplus within certain limitations. Due to regulatory limitations on third-party capital, the preferred stock issuance will require that subordinated debt no longer receive favorable treatment in net collateral ratio calculations. In 2010, Class B preferred stock dividends of $23,750 were declared, of which $8,750 were paid and $15,000 were payable at December 31, 2010, which is an accrual of the amount payable on the next dividend date, June 15, 2011, required by "dividend/patronage stopper" clauses in the preferred stock offerings. The clauses require the payment or declaration of current period dividends on the preferred stock issuances before any other patronage can be declared, and was required before payment of the December 31, 2010, bank investment and direct note patronage to associations and OFIs could be paid.

Class A Voting Common Stock – According to the bank's bylaws, the minimum and maximum stock investments that the bank may require of the ACAs and FLCA 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 (with a par value of $5 per share) and allocated retained earnings. The current investment required of the associations is 2 percent of their average borrowings from the bank. There were 45,326 shares, 47,078 shares and 45,044 shares of Class A voting common stock issued and outstanding at December 31, 2010, 2009 and 2008, respectively. Class A voting common stock includes 489 shares purchased by district associations as a condition of the bank's Capitalized Participation Pool (CPP) program. Under the CPP program, the stock investment that the bank requires is 8 percent of each pool.

Class A Nonvoting Common Stock – The bank requires OFIs to make cash purchases of Class A nonvoting common stock (with a par value of $5 per share) in the bank based on a minimum and maximum of 2 percent (or one thousand dollars, whichever is greater) and 5 percent, respectively, of the OFIs' average borrowings from the bank. The bank has a first lien on these equities for the repayment of any indebtedness to the bank. There were 354 shares, 395 shares and 399 shares of Class A nonvoting common stock issued and outstanding at December 31, 2010, 2009 and 2008, respectively.

E. Additional Paid-in-Capital

The $22,622 in additional paid-in-capital represents the excess value received by acquiring associations from acquired associations over the par value of capital stock issued in association mergers. Additional paid-in-capital is considered unallocated surplus for purposes of shareholder distributions. Generally, patronage is paid out of current year earnings and as such, this would not be paid out in the form of patronage. In the case of liquidation, additional paid-in-capital would be treated as unallocated surplus and distributed to shareholders after other obligations of the association had been satisfied.

F. Accumulated Other Comprehensive Loss:

Accumulated other comprehensive loss was comprised of the following components at December 31:

	2010	2009	2008
Unrealized losses on other-than-temporarily impaired investments	**$ 5,428**	$ 8,038	$ —
Unrealized (gains) losses on investments available-for-sale, net	**(30,014)**	(21,256)	20,910
Pension and other benefit plans	**71,671**	89,756	108,783
Unrealized losses on cash flow interest rate caps	**2,306**	304	—
Unrealized losses (gains) on cash flow interest rate swaps, net	**—**	—	(3,074)
Total	**$ 49,391**	$ 76,842	$ 132,767

Note 9 — Income Taxes

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

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

	2010	2009	2008
Current			
Federal	**$ 131**	$ 167	$ 694
State	**—**	44	3
Total current	**131**	211	697
Deferred			
Federal	**(336)**	(2,625)	(357)
State	**(86)**	(195)	4
Total deferred	**(422)**	(2,820)	(353)
Total (benefit from) provision for income taxes	**$ (291)**	$ (2,609)	$ 344

The (benefit from) provision for 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:

	2010	2009	2008
Federal tax at statutory rate	**$ 57,128**	$ 35,107	$ 60,322
State tax, net	**(86)**	(150)	7
Effect of nontaxable entities	**(70,912)**	(44,869)	(59,080)
Valuation allowance	**10,689**	4,400	1,934
Patronage distributions	**(3,229)**	(1,684)	(3,739)
Capital download to associations	**(273)**	(40)	(195)
Other, net	**6,392**	4,627	1,095
Total (benefit from) provision for income taxes	**$ (291)**	$ (2,609)	$ 344

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

	2010	2009	2008
Allowance for loan losses	**$ 13,416**	$ 11,519	$ 5,392
Allowance for acquired property	**63**	19	32
Postretirement benefits	**1,933**	2,073	3,632
Net operating loss carryforward	**14,670**	6,043	2,659
Other	**525**	51	808
Gross deferred tax assets	**30,607**	19,705	12,523
Less valuation allowance	**(25,382)**	(14,692)	(10,292)
Adjusted gross deferred tax assets	**5,225**	5,013	2,231
FCBT stock redemption	**—**	(273)	(313)
Other	**(161)**	(98)	(97)
Gross deferred tax liabilities	**(161)**	(371)	(410)
Net deferred tax assets	**$ 5,064**	$ 4,642	$ 1,821

There were no uncertain tax positions and related liabilities for unrecognized tax benefits recorded at December 31, 2010. 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 district 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 authoritative accounting guidance, 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, 2010, 2009 and 2008.

Additionally, certain qualified individuals in the bank participated in a separate, nonqualified defined benefit supplemental pension plan. Effective January 16, 2011, the bank's board of directors approved the termination of the bank's nonqualified defined benefit supplemental pension plan. As a result, no further vesting or benefit accrual shall occur under the plan following January 16, 2011, and all remaining unpaid vested benefits shall be distributed in a cash lump sum payment to the participating bank employees after a one year deferral period.

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 $3.1 million, $2.9 million and $4.7 million for the years ended December 31, 2010, 2009 and 2008, 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 $3.3 million, $3.2 million and $3.1 million for the years ended December 31, 2010, 2009 and 2008, 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).

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		
	2010	2009	2008	**2010**	2009	2008
Accumulated benefit obligation, end of year	**$ 256,263**	$ 231,745	$ 205,854			
Change in projected benefit obligation						
Benefit obligation, beginning of year	**$ 278,678**	$ 253,946	$ 242,007	**$ 41,607**	$ 40,291	$ 36,811
Service cost	**5,967**	5,516	6,987	**1,226**	1,239	1,331
Interest cost	**16,145**	15,681	19,304	**2,478**	2,497	2,937
Plan participants' contributions	**—**	—	—	**476**	419	497
Plan amendments	**—**	—	—	**—**	—	(658)
Settlements	**—**	—	(458)	**—**	—	—
Actuarial (gain) loss	**(2,375)**	13,198	12,993	**5,642**	(1,001)	1,367
Benefits paid	**(16,408)**	(9,663)	(26,887)	**(1,987)**	(1,838)	(1,994)
Projected benefit obligation, end of year	**$ 282,007**	$ 278,678	$ 253,946	**$ 49,442**	$ 41,607	$ 40,291
Change in plan assets						
Plan assets at fair value, beginning of year	**$ 167,382**	$ 114,163	$ 169,954	**$ —**	$ —	$ —
Actual return on plan assets	**24,472**	30,897	(52,254)	**—**	—	—
Company contributions	**25,146**	31,985	23,350	**1,511**	1,419	1,497
Plan participants' contributions	**—**	—	—	**476**	419	497
Benefits paid	**(16,408)**	(9,663)	(26,887)	**(1,987)**	(1,838)	(1,994)
Plan assets at fair value, end of year	**$ 200,592**	$ 167,382	$ 114,163	**$ —**	$ —	$ —
Reconciliation of funded status						
Unfunded status	**$ (81,415)**	$ (111,296)	$ (139,783)	**$ (49,442)**	$ (41,607)	$ (40,291)
Contributions between measurement date and fiscal year end	**N/A**	N/A	N/A	**N/A**	N/A	N/A
Net benefit liability at end of year	**$ (81,415)**	$ (111,296)	$ (139,783)	**$ (49,442)**	$ (41,607)	$ (40,291)

	Pension Benefits			Other Postretirement Benefits		
	2010	2009	2008	**2010**	2009	2008
Amounts recognized consist of:						
Deferred income tax assets	**$ —**	$ —	$ —	**$ —**	$ —	$ (128)
Net benefit liability at end of year	**(81,415)**	(111,296)	(139,783)	**(49,442)**	(41,607)	(40,291)
Accumulated other comprehensive loss (income)	**74,919**	100,164	119,775	**(3,278)**	(10,408)	(10,992)
Amounts recognized in accumulated other comprehensive income						
Additional minimum pension liability adjustment	**$ —**	$ —	$ —	**$ —**	$ —	$ —
Net actuarial loss (gain)	**73,269**	98,124	117,345	**6,405**	878	2,003
Prior service cost (credit)	**1,650**	2,040	2,430	**(9,683)**	(11,286)	(12,995)
Total	**$ 74,919**	$ 100,164	$ 119,775	**$ (3,278)**	$ (10,408)	$ (10,992)

The funding policy 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 increase the funded status by five percent. In accordance with this policy, contributions of $22,867, $20,000 and $31,985 were made to the plan in January 2011, January 2010 and January 2009, respectively. The supplemental (nonqualified) pension plan is not funded.

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

	Pension Benefits 2010	2009	2008	Other Postretirement Benefits 2010	2009	2008
District DB plan projected benefit obligation	**$ 280,102**	$ 272,661	$ 248,726			
District DB plan assets at fair value	**200,592**	167,382	114,163			
Accumulated benefit obligation of district DB plan	**254,653**	227,866	203,053			
Funding shortfall	**(54,061)**	(60,484)	(88,890)			
Supplemental (nonqualified) projected benefit obligation	**$ 1,905**	$ 6,017	$ 5,220			
Supplemental (nonqualified) accumulated benefit obligation	**1,610**	3,879	2,801			
Supplemental (nonqualified) fair value of plan assets	**—**	—	—			
Net periodic benefit cost						
Service cost	**$ 5,967**	$ 5,516	$ 5,590	**$ 1,226**	$ 1,239	$ 1,235
Interest cost	**16,144**	15,681	15,443	**2,478**	2,497	2,271
Expected return on plan assets	**(13,638)**	(10,598)	(14,143)	**—**	—	—
Amortization of:						
Prior service cost	**390**	390	814	**(1,732)**	(1,732)	(1,844)
Net actuarial loss	**9,775**	12,120	2,051	**125**	138	71
Net periodic benefit cost	**$ 18,638**	$ 23,109	$ 9,755	**$ 2,097**	$ 2,142	$ 1,733
Settlement expense	**1,871**	—	3,168	**—**	—	—
Special termination benefits	**—**	—	—	**—**	—	—
Total benefit cost	**$ 20,509**	$ 23,109	$ 12,923	**$ 2,097**	$ 2,142	$ 1,733
Adjustment to retained earnings for 2008 due to change in measurement date	**N/A**	N/A	$ 2,439	**N/A**	N/A	$ 272
Other changes to plan assets and projected benefit obligations recognized in other comprehensive income						
Net actuarial (gain) loss	**$ (13,209)**	$ (7,101)	82,469	**$ 5,642**	$ (986)	1,218
Amortization of net actuarial (gain) loss	**(11,645)**	(12,120)	(2,564)	**—**	(136)	(20)
Settlement expense	**—**	—	(3,168)	**—**	—	(5)
Prior service costs	**—**	—	—	**—**	—	(586)
Amortization of prior service costs	**(390)**	(390)	(1,018)	**1,732**	1,706	1,872
Termination recognition of prior service costs	**—**	—	—	**(125)**	—	4
Net change	**$ (25,244)**	$ (19,611)	75,719	**$ 7,249**	$ 584	2,483
AOCI amounts expected to be amortized in 2011						
Prior service cost (credit)	**$ 36**			**$ (1,682)**		
Net actuarial loss (gain)	**6,970**			**288**		
Total	**$ 7,006**			**$ (1,394)**		
Weighted-average assumptions used to determine benefit obligation as of December 31						
Measurement date	**12/31/2010**	12/31/2009	12/31/2008	**12/31/2010**	12/31/2009	12/31/2008
Discount rate	**5.50%**	5.95%	6.30%	**5.70%**	6.05%	6.30%
Rate of compensation increase	**3% in 2010 up to 3.5% in 2011**	6% in 2010 down to 4% in 2012	7% in 2009 down to 4% in 2012			
Health care cost trend rate assumed for next year (pre/post-65) — medical				**7.5%/6.5%**	8.0%/7.0%	8.5%/6.5%
Health care cost trend rate assumed for next year (pre/post-65) — prescriptions				**10.50%**	10.50%	11.00%
Ultimate health care cost trend rate				**5.00%**	5.00%	5.00%
Year that the rate reaches the ultimate trend rate				**2017**	2017	2015

	Pension Benefits			Other Postretirement Benefits		
	2010	2009	2008	**2010**	2009	2008
Weighted-average assumptions used to determine net periodic cost for year ended December 31						
Measurement date	**12/31/2009**	12/31/2008	9/30/2007	**12/31/2009**	12/31/2008	9/30/2007
Discount rate	**5.95%**	6.30%	6.50%	**6.05%**	6.30%	6.50%
Expected return on plan assets	**7.50%**	7.50%	8.00%	**N/A**	N/A	N/A
Rate of compensation increase	**6% in 2010 down to 4% in 2012**	7% in 2009 down to 4% in 2012	8% in 2008 down to 4% in 2012			
Health care cost trend rate assumed for next year (pre/post-65) — medical				**8.0%/7.0%**	8.5%/6.5%	8.5%/6.5%
Health care cost trend rate assumed for next year (pre/post-65) — prescriptions				**10.00%**	11.00%	12.00%
Ultimate health care cost trend rate				**5.00%**	5.00%	4.75%
Year that the rate reaches the ultimate trend rate				**2017**	2015	2016

Effect of Change in Assumed Health Care Cost Trend Rates

Effect on total service cost and interest cost components	
One-percentage point increase	**$ 797**
One-percentage point decrease	**(632)**
Effect on year-end postretirement benefit obligation	
One-percentage point increase	**$ 8,221**
One-percentage point decrease	**(6,653)**

Plan Assets

The trustees of the district DB plan set investment policies and strategies for the plan, including target allocation percentages for each category of plan asset. Generally, the funding objectives of the DB plan is to achieve and maintain plan assets in accordance with the funding policy mentioned above and to provide competitive investment returns and reasonable risk levels when measured against appropriate benchmarks. Plan trustees develop asset allocation policies based on plan objectives, characteristics of pension liabilities, capital market expectations and asset-liability projections. District postretirement health care plans have no plan assets and are funded on a current basis by employer contributions and retiree premium payments.

	Fair Value Measurement at December 31, 2010			
	Total	**Quoted Prices in Active Markets for Identical Assets (Level 1)**	**Significant Other Observable Inputs (Level 2)**	**Significant Unobservable Inputs (Level 3)**
Asset Category:				
Commingled trust funds:				
Russell Multi-Manager Bond Fund	**$ 78,085**	$ —	$ 78,085	$ —
Russell All International Markets Fund	**41,659**	—	41,659	—
Russell World Equity Fund	**24,579**	—	24,579	—
Russell Commingled Enhanced Fund	**22,520**	—	22,520	—
Russell Small Cap Fund	**10,301**	—	10,301	—
Russell U.S. Value Fund	**8,270**	—	8,270	—
Russell Growth Fund	**8,065**	—	8,065	—
Russell Emerging Markets Fund	**7,113**	—	7,113	—
Total assets	**$ 200,592**	$ —	$ 200,592	$ —

Expected Future Cash Flow Information

	Pension Benefits	Other Postretirement Benefits
Expected Benefit Payments		
Fiscal 2011	**$ 12,083**	**$ 1,773**
Fiscal 2012	**15,196**	**1,950**
Fiscal 2013	**14,541**	**2,169**
Fiscal 2014	**15,771**	**2,381**
Fiscal 2015	**17,020**	**2,551**
Fiscal 2016 - 2020	**100,980**	**15,560**
Expected Contributions		
Fiscal 2011	**$ 22,867**	**$ 1,773**

Plan Assets

	Pension Benefits				Other Postretirement Benefits			
Asset Category	Target	**2010**	2009	2008	Target	**2010**	2009	2008
Equity securities	60%	**60%**	60%	60%	—%	**—%**	—%	—%
Debt securities	40	**40**	40	40	—	**—**	—	—
Cash/other	—	**—**	—	—	100	**100**	100	100
Total	100%	**100%**	100%	100%	100%	**100%**	100%	100%

As disclosed in the preceding table, the expected total contribution for 2011 is $22.9 million. The significant decline in the plan's actual return on plan assets for 2008 reflected the adverse effects of the global financial markets during that year, necessitating the increase in contributions for 2009. The plan's subsequent improved investment results, and general economic trends and their effects on the plan's investment portfolio affected the level of subsequent contributions required to fund the plan.

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 associations have entered into loan transactions with directors, officers and other employees of associations and other organizations with which such persons may be associated. Total loans to such persons at December 31, 2010, amounted to $158.6 million. In the opinion of management, such loans outstanding to directors, officers and other employees at December 31, 2010, did not involve more than a normal risk of collectibility, 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, 2010, were approximately $188.8 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 $3.067 billion, $3.057 billion and $3.320 billion at December 31, 2010, 2009 and 2008, respectively. At December 31, 2010, the district had $141.7 million in outstanding standby letters of credit, issued primarily in conjunction with participation loans. Outstanding standby letters of credit generally have expiration dates ranging from 2011 to 2015.

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

Authoritative accounting guidance defines fair value as the exchange price that would be received for an asset or paid to transfer a liability in an orderly transaction between market participants in the principal or most advantageous market for the asset or liability. 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, 2010 for each of the fair value hierarchy values are summarized below:

	Fair Value Measurement at December 31, 2010			
	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	**$ 20,439**	$ —	$ 20,439	$ —
Investments available-for-sale	**3,076,946**	—	2,829,298	247,648
Derivative assets	**6,512**	—	6,512	—
Assets held in nonqualified benefit trusts	**2,247**	2,247	—	—
Total assets	**$ 3,106,144**	$ 2,247	$ 2,856,249	$ 247,648
Liabilities:				
Derivative liabilities	**$ 5**	$ —	$ 5	$ —
Standby letters of credit	**2,843**	—	2,843	—
Total liabilities	**$ 2,848**	$ —	$ 2,848	$ —

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, 2010:

	Level 3 Assets and Liabilities Investment Securities
Balance at January 1, 2010	$ —
Purchases, issuances and settlements	145,122
Total realized and unrealized losses, net	(4,619)
Transfers into Level 3	107,145
Balance at December 31, 2010	$ 247,648

In December 2010, the bank transferred certain non-agency mortgage-backed and asset-backed securities totaling $107,145 from Level 2 to Level 3. The decision to move these investments to Level 3 was based on the relatively illiquid current market for these investments, which were valued by independent third-party valuation services which used Level 2 and Level 3 criteria in their valuations. The significant inputs included volatility, prepayment rates, market spreads and dealer quotes.

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, 2010	$ 1,830

Assets and liabilities measured at fair value on a nonrecurring basis at December 31, 2010 for each of the fair value hierarchy values are summarized below:

	Fair Value Measurement at December 31, 2010				
	Total	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Total Gains (Losses)
Assets:					
Loans	$ 199,999	$ —	$ —	$ 199,999	$ (129,101)
Other property owned	86,490			86,490	(15,151)
Total assets	$ 286,489	$ —	$ —	$ 286,489	(144,252)

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

	Fair Value Measurement at December 31, 2009			
	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	**$ 20,490**	$ —	$ 20,490	$ —
Investments available-for-sale	**2,179,312**	—	2,179,312	—
Derivative assets	**2,526**	—	2,526	—
Assets held in nonqualified benefit trusts	**1,822**	1,822	—	—
Total assets	**$ 2,204,150**	$ 1,822	$ 2,202,328	$ —
Liabilities:				
Derivative liabilities	**$ 30**	$ —	$ 30	$ —
Standby letters of credit	**4,537**	—	4,537	—
Total liabilities	**$ 4,567**	$ —	$ 4,567	$ —

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, 2009:

	Level 3 Assets and Liabilities Investment Securities
Balance at January 1, 2009	$ 99,992
Net losses included in other comprehensive income	(376)
Net losses included in other earnings	(5,293)
Purchases, issuances and settlements	(104,208)
Net transfers out of Level 3	9,885
Balance at December 31, 2009	$ —
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, 2009	$ 5,293

Assets and liabilities measured at fair value on a nonrecurring basis at December 31, 2009 for each of the fair value hierarchy values are summarized below:

	Fair Value Measurement at December 31, 2009				
	Total	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Total Gains (Losses)
Assets:					
Loans	$ 205,031	$ —	$ —	$ 205,031	$ (78,313)
Other property owned	59,248			59,248	687
Total assets	$ 264,279	$ —	$ —	$ 264,279	$ (77,626)

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 nonqualified 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)	Total Gains (Losses)
Assets:					
Loans	$ 85,248	$ —	$ —	$ 85,248	$ (27,058)
Other property owned	6,495			6,495	298
Total assets	$ 91,743	$ —	$ —	$ 91,743	$ (26,760)

Valuation Techniques

As more fully discussed in Note 2, "Summary of Significant Accounting Policies," authoritative accounting guidance 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. At December 31, 2010, Level 3 securities included primarily the bank's AMBS portfolio which is valued by the bank using a model which incorporates underlying rates and current yield curves. Level 3 assets at December 31, 2010, also include certain non-agency mortgage-backed and asset-backed securities valued using independent third-party valuation services.

As permitted under Farm Credit Administration regulations, the banks are authorized to hold eligible investments. The regulations define eligible investments by specifying credit rating criteria, final maturity limit, and percentage of portfolio limit for each investment type. At the time of purchase, mortgage-backed and asset-backed securities must be triple-A rated by at least one Nationally Recognized Statistical Rating Organization. The triple-A rating requirement puts the banks in a position to hold the senior tranches of securitizations. The underlying loans for mortgage-backed securities are residential mortgages, while the underlying loans for asset-backed securities are home equity lines of credit, small business loans, equipment loans or student loans.

To estimate the fair value of the majority of the investments held, the bank obtains prices from third-party pricing services, including certain non-agency securities.

Assets Held in Nonqualified 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 that are actively traded and have quoted net asset values that are observable in the marketplace.

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.

The models used to determine the fair value of derivative assets and liabilities use an income approach based on observable market inputs, primarily the LIBOR swap curve and volatility assumptions about future interest rate movements.

Standby Letters of Credit

The fair value of letters of credit approximate the fees currently charged for similar agreements or the estimated cost to terminate or otherwise settle similar obligations.

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, 2010, impaired loans with a fair value of $199,999 were included in loans.

Other Property Owned

Other property owned is generally classified as Level 3. The process for measuring the fair value of other property owned involves the use of appraisals or other market-based information. Costs to sell represent transaction costs and are not included as a component of the asset's fair value. As a result, these fair value measurements fall within Level 3 of the hierarchy.

In accordance with authoritative accounting guidance, assets acquired in loan foreclosures are recorded at fair value, less estimated costs of sale. At December 31, 2010, foreclosed assets with a fair value of $86,490 are included in other property owned.

Note 15 — 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, 2010, 2009 and 2008.

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

	December 31, 2010		December 31, 2009		December 31, 2008	
	Carrying Amount	**Fair Value**	Carrying Amount	Fair Value	Carrying Amount	Fair Value
Financial assets						
Cash and federal funds sold and investment securities	**$ 3,705,322**	**$ 3,705,322**	$ 2,700,769	$ 2,700,769	$ 3,279,977	$ 3,281,080
Loans	**15,628,890**	**15,454,918**	16,167,170	16,204,014	16,590,071	17,122,656
Allowance for loan losses	**(163,145)**	**—**	(144,731)	—	(51,653)	—
Loans, net	**15,465,745**	**15,454,918**	16,022,439	16,204,014	16,538,418	17,122,656
Derivative assets	**6,512**	**6,512**	2,526	2,526	31,439	31,439
Financial liabilities						
Bonds and notes	**16,179,932**	**16,273,642**	16,169,479	16,262,844	17,302,205	17,584,236
Subordinated debt	**50,000**	**52,851**	50,000	50,696	50,000	56,168
Derivative liabilities	**5**	**5**	30	30	3,074	3,074

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 and Federal Funds Sold:

The carrying value is a reasonable estimate of fair value.

B. Investment Securities:

Valuation methods for available-for-sale investments for liquidity, mission-related and other purposes are described in Note 14, "Fair Value Measurements." Held-to-maturity investments are valued by the bank using a model which incorporates underlying rates and current yield curves.

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 estimated based upon the Treasury yield curve.

F. Derivative Assets and Liabilities:

Exchange-traded derivatives are valued using quoted prices. However, the majority of the derivative positions are valued using internally developed models that use as their basis readily observable market parameters. See Note 14, "Fair Value Measurements."

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. The bank substantially offsets this risk by concurrently entering into offsetting agreements with non-System counterparties. 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, 2010, the bank had three fair value hedges with a total notional amount of $150.0 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. Because the size of swap positions needed to reduce the impact of market fluctuations varies over time, the bank also enters into swaps in which it receives the floating rate and pays the fixed rate (pay fixed swaps) when necessary to reduce its net position.

The bank has interest rate caps to reduce the impact of rising interest rates on their floating-rate assets. At December 31, 2010, the bank held interest rate caps with a notional amount of $645.0 million and a fair value of $4.7 million. The primary types of derivative instruments used and the amount of activity (notional amount of derivatives) during the year ended December 31, 2010 is summarized in the following table:

	Receive Fixed Swaps	Pay Fixed Swaps	Interest Rate Caps	Total
Balance at January 1, 2010	$ 125,000	$ —	$ 130,000	$ 255,000
Additions	—	725,000	515,000	1,240,000
Terminations	—	(700,000)	—	(700,000)
Balance at December 31, 2010	$ 125,000	$ 25,000	$ 645,000	$ 795,000

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. However, derivative contracts must be reflected in the financial statements on a gross basis regardless of the netting agreement. At December 31, 2010, the bank had credit exposure to counterparties, net of collateral of $6.5 million, as compared with $2.5 million at December 31, 2009.

The table below presents the credit ratings of counterparties to whom the bank has credit exposure at December 31, 2010:

	Remaining Years to Maturity						
(dollars in millions)	Less Than One Year	More Than One to Five Years	Total	Maturity Distribution Netting	Exposure	Collateral Held	Exposure Net of Collateral
Moody's Credit Rating							
Aa1	$ —	$ 1.8	$ 1.8	$ —	$ 1.8	$ —	$ 1.8
Aa3	—	4.7	4.7	—	4.7	—	4.7

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.

Fair-Value Hedges:

For derivative instruments that are designated and qualify as a fair value hedge, the gain or loss on the derivative as well as the offsetting loss or gain on the hedge item (principally, debt securities) attributable to the hedged risk are recognized in current earnings. The bank includes the gain or loss on the hedged items in the same line item (interest expense) as the offsetting loss or gain on the related interest rate swaps. Accordingly, no gain or loss is recognized in earnings.

Cash Flow Hedges:

For derivative instruments that are designated and qualify as a cash flow hedge, the effective portion of the gain or loss on the derivative is reported as a component of other comprehensive income and reclassified into earnings in the same period or periods during which the hedged transaction affects earnings. Gains and losses on the derivative representing either hedge ineffectiveness or hedge components excluded from the assessment of effectiveness are recognized in current earnings.

Derivatives not Designated as Hedges:

For derivatives not designated as a hedging instrument, the related change in fair value is recorded in current period earnings in "gains (losses) on derivative transactions" in the statement of income. The bank does not possess any derivatives not classified as hedges.

Fair Value of Derivative Instruments:

The following table represents the fair value of derivative instruments as of:

	Balance Sheet Location	Fair Value 12/31/2010	Fair Value 12/31/2009	Balance Sheet Location	Fair Value 12/31/2010	Fair Value 12/31/2009
Receive fixed	Other assets	$ 1,848	$ 921	Other liabilities	$ —	$ 30
Pay fixed	Other assets	—	—	Other liabilities	5	—
Interest rate caps	Other assets	4,664	1,605			

The following table sets forth the amount of gain (loss) recognized in the Other Comprehensive Income for the year ended December 31, 2010:

	Change in OCI on Derivative (Effective Portion)
Interest rate caps	$ (1,996)
Cash flow derivatives	(5)

The following table 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 in the table presents the principal cash flows and related weighted average interest rates by expected maturity dates. The derivative information in the table represents the notional amounts and weighted average interest rates by expected maturity dates.

December 31, 2010 *(dollars in millions)*	Maturities of 2010 Derivative Products and Other Financial Instruments 2011	2012	2013	2014	2015	Subsequent Years	Total	Fair Value
Total debt obligations:								
Fixed rate	$ 3,303	$ 1,673	$ 1,541	$ 1,294	$ 1,042	$ 1,662	$ 10,515	$ 10,613
Weighted average interest rate	1.03%	1.34%	1.45%	1.81%	2.33%	3.55%	1.76%	
Variable rate	$ 5,100	$ 490	$ 75	$ —	$ —	$ —	$ 5,665	$ 5,661
Weighted average interest rate	0.57%	0.26%	0.33%	—	—	—	0.54%	
Total debt obligations	$ 8,403	$ 2,163	$ 1,616	$ 1,294	$ 1,042	$ 1,662	$ 16,180	$ 16,274
Weighted average interest rate	0.75%	1.09%	1.40%	1.81%	2.33%	3.55%	1.33%	
Derivative instruments:								
Receive fixed swaps								
Notional value	$ 50	$ 75	$ —	$ —	$ —	$ —	$ 125	$ 2
Weighted average receive rate	1.23%	2.23%	—	—	—	—	1.83%	
Weighted average pay rate	0.21%	0.26%	—	—	—	—	0.24%	
Pay fixed swaps								
Notional value	$ 25	$ —	$ —	$ —	$ —	$ —	$ 25	$ —
Weighted average receive rate	0.26%	—	—	—	—	—	0.26%	
Weighted average pay rate	0.62%	—	—	—	—	—	0.62%	
Interest rate caps								
Notional value	$ —	$ —	$ —	$ 130	$ 325	$ 190	$ 645	$ 5
Weighted average receive rate	—	—	—	—	—	—	—	
Weighted average pay rate	—	—	—	—	—	—	—	

Note 17 — Selected Quarterly Financial Information (Unaudited)

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

2010	First	Second	Third	Fourth	Total
Net interest income	**$ 138,246**	**$ 142,137**	**$ 144,350**	**$ 155,437**	**$ 580,170**
Provision for loan losses	**22,883**	**25,585**	**60,781**	**32,208**	**141,457**
Noninterest expense, net	**27,283**	**41,788**	**34,298**	**60,027**	**163,396**
Net income	**$ 88,080**	**$ 74,764**	**$ 49,271**	**$ 63,202**	**$ 275,317**

2009	First	Second	Third	Fourth	Total
Net interest income	$ 124,987	$ 128,882	$ 136,141	$ 145,782	$ 535,792
Provision for loan losses	31,560	43,496	61,809	35,275	172,140
Noninterest expense, net	43,551	39,433	34,198	48,046	165,228
Net income	$ 49,876	$ 45,953	$ 40,134	$ 62,461	$ 198,424

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

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	Year Ended December 31, 2010	2009	2008
Cash and federal funds sold	**$ 457,304**	$ 490,915	$ 189,791
Investment securities	**3,076,946**	2,143,485	3,028,468
Loans			
To associations	**7,530,019**	8,304,420	8,402,595
To others	**2,934,015**	2,728,694	3,000,518
Less allowance for loan losses	**28,678**	31,602	12,549
Net loans	**10,435,356**	11,001,512	11,390,564
Accrued interest receivable	**45,298**	48,709	63,632
Other property owned, net	**2,838**	639	—
Other assets	**90,461**	91,242	88,046
Total assets	**$ 14,108,203**	$ 13,776,502	$ 14,760,501
Bonds and notes	**$ 12,779,932**	$ 12,769,479	$ 13,802,205
Subordinated debt	**50,000**	50,000	50,000
Other liabilities	**127,413**	135,731	163,754
Total liabilities	**12,957,345**	12,955,210	14,015,959
Preferred stock	**482,000**	200,000	200,000
Capital stock	**228,399**	237,361	227,212
Retained earnings	**418,965**	373,060	343,113
Accumulated other comprehensive income (loss)	**21,494**	10,871	(25,783)
Total members' equity	**1,150,858**	821,292	744,542
Total liabilities and members' equity	**$ 14,108,203**	$ 13,776,502	$ 14,760,501

Income Statement	Year Ended December 31, 2010	2009	2008
Interest income	**$ 483,257**	$ 565,384	$ 660,690
Interest expense	**270,737**	396,172	541,294
Net interest income	**212,520**	169,212	119,396
Provision for credit losses	**28,523**	33,648	20,529
Net interest income after provision for credit losses	**183,997**	135,564	98,867
Noninterest income	**44,746**	38,312	33,900
Other expense	**60,293**	67,268	56,034
Net income	**$ 168,450**	$ 106,608	$ 76,733

Note 19 — Association Mergers

Effective July 1, 2010, AgCredit of South Texas, ACA headquartered in Weslaco, Texas, was acquired by Texas AgFinance, FCS headquartered in Robstown, Texas. The continuing association uses the Texas AgFinance, FCS name and is headquartered in Robstown, Texas. Effective December 1, 2010, Louisiana Ag Credit, ACA headquartered in Arcadia, Louisiana, was acquired by Southern AgCredit, ACA headquartered in Ridgeland, Mississippi. The continuing association uses the Southern AgCredit, ACA name and is headquartered in Ridgeland, Mississippi. The primary reason to merge was based on a determination that the combined organization should be financially and operationally stronger than either association on a stand-alone basis.

According to recent accounting guidance, the acquisition method of accounting is required for mergers of cooperatives occurring after January 1, 2009. As the accounting acquirers, Texas AgFinance and Southern AgCredit accounted for the transaction by using their historical information and accounting policies and recording the identifiable assets and liabilities of AgCredit of South Texas and Louisiana Ag Credit as of the acquisition date of July 1, 2010, and December 1, 2010, at their respective fair values. The associations operate for the mutual benefit of their borrowers and other customers and not for the benefit of any other equity investors. As such, their capital stock provides no significant interest in corporate earnings or growth. Specifically, due to restrictions in applicable regulations and their bylaws, the associations can issue stock only at its par value of $5 per share, the stock is not tradable, and the stock can be retired only for the lesser of par value or book value. In these and other respects, the shares of AgCredit of South Texas that were converted into shares of Texas AgFinance and the shares of Louisiana Ag Credit that were converted into shares of Southern AgCredit had identical rights and attributes. For this reason, the conversion of stock pursuant to the merger occurred at a one-for-one exchange ratio. Management believes that because the stock in each association is fixed in value, the stock issued pursuant to the merger provides no basis for estimating the fair value of the consideration transferred pursuant to the merger. In the absence of a purchase price determination, Texas AgFinance and Southern AgCredit identified and estimated the acquisition date fair value of the equity interest of AgCredit of South Texas and Louisiana Ag Credit instead of the acquisition date fair value of the equity interests transferred as consideration. The fair value of the assets acquired, including specific intangible assets and liabilities assumed from AgCredit of South Texas and Louisiana Ag Credit, were measured based on various estimates using assumptions that Texas AgFinance management and Southern AgCredit management believe are reasonable utilizing information available at the merger date. Use of different estimates and judgments could yield materially different results. This evaluation produced a fair value of identifiable assets acquired and liabilities assumed that was substantially equal to the fair value of the member interests transferred in the merger. As a result, Texas AgFinance management and Southern AgCredit management determined goodwill was immaterial and therefore recorded no goodwill. The excess value received by Texas AgFinance from AgCredit of South Texas and the excess value received by Southern AgCredit from Louisiana Ag Credit over par value of capital stock and participation certificates issued in the merger is considered to be additional paid-in-capital.

The following table summarizes the fair values of the identifiable assets acquired and liabilities Texas AgFinance assumed from AgCredit of South Texas and Southern AgCredit assumed from Louisiana Ag Credit upon acquisition:

	Fair Value	Contractual Amount	Contractual Amounts not Expected to be Collected
Loans	$ 172,293	$ 177,797	$ 2,726
Total assets	181,357	—	—
Notes payable	153,011	153,065	—
Total liabilities	156,905	—	—
Net assets acquired	24,452	—	—

As AgCredit of South Texas (the acquired entity) and Louisiana Ag Credit (the acquired entity) were affiliated associations of the district prior to the business combination with Texas AgFinance, and Southern AgCredit, AgCredit of South Texas's and Louisiana Ag Credit's financial position and results of operations are included in the combined district financial statements for 2010 through the merger date, as well as for the years ending December 31, 2009 and 2008. AgCredit of South Texas's and Louisiana Ag Credit's results of operations for the pre-merger periods were as follows:

	2010	2009	2008
Net interest income	**$ 3,635**	$ 6,141	$ 6,597
Provision for loan losses	**979**	2,750	6,209
Noninterest income	**823**	1,635	1,571
Noninterest expense	**3,251**	5,930	5,120
(Benefit from) provision for income taxes	**(216)**	(52)	11
Net income (loss)	**$ 444**	$ (852)	$ (3,172)

Note 20 — Subsequent Events

The district has evaluated subsequent events through March 1, 2011, which is the date the financial statements were issued. There are no other significant subsequent events requiring disclosure as of March 1, 2011.

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 a Federal Land Credit Association (FLCA), collectively referred to as the 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 the FLCA 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 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 bank included in this annual report to shareholders.

Board of Directors and Senior Officers

FCBT is governed by a seven-member board of directors. Five directors are farmers or ranchers, who are elected by the customers of the 17 associations that own the bank. Two directors, who are not stockholders of any of the associations, are appointed by the elected board members. The board of directors is responsible for directing the operations of the bank. The bank's senior officers are accountable to the board of directors and work with the board of directors to set the bank's direction, goals and strategies.

The following represents certain information regarding the board of directors and senior officers of the bank as of March 1, 2011, including business experience during the past five years:

Directors

Ralph W. Cortese, 64, joined the board of directors in 1995, and his current term expires December 31, 2013. 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 president of Cortese Farm and Ranch Inc. and is from Fort Sumner, New Mexico. He operates a cow/calf and yearling operation on grass and in the feedlot, and raises irrigated alfalfa. Cortese is a member of the bank's audit and compensation committees. He also is a member of the Texas Agricultural Cooperative Council board of directors and serves as chief financial officer for his local church. Cortese served on the Farmer Mac board from 2003 to 2008 and is a former board member of the American Land Foundation.

James F. Dodson, 57, joined the board of directors in 2003, and his current term expires December 31, 2011. He has served as vice chairman of the board of directors since 2009. He is a past chairman of the Texas AgFinance, FCS Board of Directors and a former member of the Texas Farm Credit District Stockholders' Advisory Committee. He is chairman of both the bank's compensation committee and the Tenth District Farm Credit Council board and serves on the bank's audit committee. Dodson grows cotton, corn 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 Legacy Farms, Weber Greene, Ltd., and Dodson Family Farms; 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.

Joe R. Crawford, 73, began his first term on the board of directors in 1998, and his current term expires December 31, 2012. 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. Crawford is a member of the bank's audit and compensation committees. 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.

Elizabeth G. Flores, 66, joined the board of directors in August 2006 as an outside director, and her current term expires December 31, 2012. She was mayor of Laredo, Texas, where she resides, from 1998 to 2006. Previously, she was senior vice president of Laredo National Bank. Flores is a member of the bank's audit and compensation committees. She also 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. In 2010, Flores was appointed to serve as a member of the Farm Credit System Diversity Workgroup. She is a partner in a family ranching and real estate business. She is a former member of the Federal Reserve Board Consumer Advisory Council.

Jon M. Garnett, 66, began his first term on the board of directors in 1999, and his current term expires December 31, 2013. 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 (FCC) Board of Directors as a district representative and in 2009 he became vice chairman of the FCC board of directors. In January of 2011, Garnett was elected chairman of the FCC board of directors. In addition, he is a member of the FCC Board of Directors' legislative committee, executive committee, compensation committee and chairs the budget committee. He is also a member of the bank's audit committee and is the vice chairman of the bank's compensation committee. Garnett is a member of the State Technical Committee for the Natural Resources Conservation Service. Garnett raises grain and forage crops and runs stocker cattle near Spearman, Texas, and is President of Garnett Farms, Inc.

Lester Little, 60, joined the board of directors in 2009 and his term will expire December 31, 2011. Prior to joining the bank board, Little was chairman of Capital Farm Credit Board of Directors and previously served as vice chairman of the Texas Farm Credit District Stockholders' Advisory Committee. He also was a member of the district's Association Business Advisory Committee. Little is vice chairman of the bank's audit committee and a member of the bank's compensation committee. He is from Hallettsville, Texas, and owns and operates a farm, and offers custom-farming services. He is a Farm Bureau member and serves on the Lavaca Regional Water Planning Group.

William F. Staats, 73, joined the board of directors in 1997 as an outside director, and his current term expires 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 Lakeside Bank. 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.

Committees

The board of directors has established an audit committee and compensation committee. All members of the board serve on both the audit committee and compensation committee. The responsibilities of each committee are set forth in its respective approved charter.

Compensation of Directors

Directors of the bank are compensated in cash for service on the bank's board. Compensation for 2010 was paid at the rate of $52,133 per year, payable at $4,344 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. The board approved additional compensation in the amount of $2,000 during 2010 as noted below. No director received non-cash compensation exceeding $5,000 in 2010. Total cash compensation paid to all directors as a group during 2010 was $366,931. Information for each director for the year ended December 31, 2010, is provided below:

Board Member	Days Served at Board Meetings*	Days Served on Other Official Assignments**	Total Compensation Paid
Ralph W. Cortese	31.0	39.75	$ 52,133
James F. Dodson	31.25	34.0	52,133
Joe R. Crawford	25.25	23.25	52,133
Elizabeth G. Flores***	31.25	29.25	54,133
Jon M. Garnett	30.0	24.75	52,133
Lester Little	31.0	28.0	52,133
William F. Staats	31.25	26.25	52,133
			$ 366,931

* 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.

*** During 2010, additional compensation of $2,000 was paid to Ms. Flores for attendance at an FCA Board of Directors meeting in her capacity as a member of the Farm Credit System Diversity Workgroup.

Directors are reimbursed for reasonable travel, subsistence and other related expenses while conducting bank business. The aggregate amount of expenses reimbursed to directors in 2010, 2009 and 2008 totaled $120,413, $131,507 and $162,118, respectively. The decrease in expenses in 2010 and 2009 as compared to 2008 was primarily due to less travel costs incurred during 2010 and 2009. The expenses in 2008 include 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. A copy of the bank's travel policy is available to shareholders upon request.

Senior Officers of the Bank

Name and Title	Time in Position	Experience — Past Five Years	Other Business Interests — Past Five Years
Larry R. Doyle, *Chief Executive Officer*	7.5 years	Chief Executive Officer, FCBT	He serves as a member of the board of directors for the Federal Farm Credit Banks Funding Corporation.
Kurt Thomas, *Chief Credit Officer*	Appointed May 2010	Vice President and Unit Manager Association Direct Lending Group	He serves as a member of the Board of Governors for the Farm Credit System Captive Insurance Corporation.
Amie Pala, *Chief Financial Officer*	Appointed July 2010	Vice President of Financial Management	
Allen Buckner, *Chief Operations Officer*	Appointed June 2010	Vice President of Lending Systems 2007 – 2010; Vice President, Credit Operations and Risk Management 2006 – 2007; Chief Executive Officer, Heritage Land Bank, ACA, January 2006 – December 2006	
Stan Ray, *Chief Administrative Officer*	Appointed July 2010	Vice President of Marketing and Corporate Relations	He serves on the AgFirst/FCBT Plan Fiduciary Committee and as a member of the board of directors for the following organizations: Texas Agriculture Finance Authority, Texas FFA Foundation, Grow Texas Foundation, Texas Agriculture Cooperative Council and Emanuel Agriculture Development.
Kyle Pankonien, *Vice President, Corporate Affairs, General Counsel and Corporate Secretary*	3 years	Vice President, Corporate Affairs, Deputy General Counsel, FCBT	

Thomas W. Hill served as chief financial officer and chief operations officer until his retirement on November 15, 2010.

Steven H. Fowlkes ended his tenure with the bank as senior vice president and chief credit officer on May 1, 2010, when he assumed the duties of chief executive officer of Lone Star, ACA, a district association.

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.

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. Additionally, the compensation committee reviews the compensation policies and plans for the other senior officers of the bank and other employees, and approves the overall compensation program for the senior officers. 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, subsidized health insurance and bank-provided vehicles.

Chief Executive Officer (CEO) Compensation Table and Policy

The base salary amount of the CEO was $750,029 for 2010. 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 entered into in November 2008. Pursuant to the terms and conditions of the Compensation Agreement between the bank and CEO, the CEO would not earn any bonuses for performance during 2009 or 2010.

The following table summarizes the compensation paid to the CEO of the bank during 2010, 2009 and 2008.

Summary Compensation Table for the CEO

		Annual					
Name of Chief Executive Officer	Year	Salary (a)	Bonus (b)	Change in Pension Value (c)	Deferred/Perquisites (d)	Other (e)	Total
Larry R. Doyle	2010	$ 750,029	$ —	$ 82,331	$ 20,486	$ —	$ 852,846
Larry R. Doyle	2009	750,029	—	167,901	20,627	4,178,570	5,117,127
Larry R. Doyle	2008	500,019	600,000	<5,810,710>	19,229	8,821,430	4,129,968

(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. For 2010 and 2009, no bonus for performance was paid to the CEO in accordance with the Compensation Agreement.

(c) For 2010 and 2009, disclosure of the change in pension value represents the change in the actuarial present value of the accumulated benefit under the defined benefit pension plan, the Farm Credit Bank of Texas 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. For 2008, disclosure of the change in the pension value represents 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). 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) For 2009, Other reflects the remaining proration of the $4,500,000 payment paid in January 2010 pursuant to the Compensation Agreement between the bank and the CEO. For 2008, 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 was also eligible for a $4,500,000 payment in January 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.

In December of 2010, a memorandum of understanding between the bank and the CEO was executed with an effective date of January 2, 2011. The memorandum of understanding is effective for a term of three years, until December 31, 2013. The base salary for each year of the three-year term for the CEO will be $1,250,000. Bonus payments, if any, are at the sole discretion of the compensation committee. With the execution and effective date of the memorandum of understanding, the CEO received a signing bonus of $500,000 paid in January 2011, with certain claw-back provisions should the CEO resign without good reason or employment is terminated by the bank for cause. The employment relationship between the bank and CEO remains at-will, meaning the bank may terminate the CEO's employment at any time, and the CEO may choose to leave at any time but may be subject to the claw-back provision discussed above.

Pension Benefits Table for the CEO

The following table presents the total annual benefit provided from the defined benefit pension plan applicable to the CEO for the year ended December 31, 2010:

Name	Plan Name	Number of Years Credited Service	Present Value of Accumulated Benefit	Payments During 2010
Larry R. Doyle	Farm Credit Bank of Texas Pension Plan	36.838	$ 1,130,508	$ 0

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 and bonus 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 benefit is calculated assuming retirement had occurred at the measurement date used for financial statement reporting purposes with retirement at age 58. 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, (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, or (d) by a service period of greater than 35 years. 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 paid to the CEO in January 2010 and, (iii) annual base salary of $750,000 for 2009 and 2010. In exchange for those benefits, the Compensation Agreement provided that the CEO would not (1) participate in the Supplemental Pension Plan after 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. The Compensation Agreement was 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 of the Bank

The following table summarizes the compensation paid to the aggregate number of senior officers of the bank during 2010 and the five highest paid officers of the bank during 2009 and 2008. Amounts reflected in the table are presented in the year the compensation is earned.

Summary Compensation Table

		Annual				
Name of Individual or Group	Year	Salary (a)	Bonus (b)	Deferred/Perquisites (c)	Other (d)	Total
Aggregate number of senior officers: (excludes Chief Executive Officer)						
7	2010	$ 2,379,479	$ 409,876	$ 5,223,633	$ 28,512	$ 8,041,500
5	2009	1,317,567	417,510	143,369	—	1,878,446
5	2008	1,249,615	396,360	126,827	—	1,772,802

(a) Gross salary, including retention plan compensation for certain senior officers.

(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, supplemental 401(k) discretionary contributions, automobile benefits and premiums paid for life insurance. For 2010, Deferred/Perquisites also includes payments of $5,078,396 to certain senior officers that withdrew from the Supplemental Pension Plan in 2010.

(d) Other for 2010 reflects an amount paid to one senior officer for their remaining annual leave hours at retirement. No such amounts were paid or earned in 2009 or 2008.

For 2010, the aggregate number of senior officers includes two senior officers that ended their employment with the bank during 2010.

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 2010, 2009 and 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 2010.

Disclosure of the compensation paid during 2010 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, other than the CEO, can earn compensation above base salary through an annual Success Sharing Plan, which the bank adopted in 2001. The Success Sharing Plan is based upon the achievement of bank performance, which is approved by the bank board's compensation committee, annually, and payment is determined by the compensation committee in its discretion. 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 (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 Retention 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 Retention Plan. Certain senior officers and other bank employees, other than the CEO, in the Retention 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.

Effective January 16, 2011, the bank's board of directors approved the termination and liquidation of the Farm Credit Bank of Texas Supplemental Pension Plan (the "Supplemental Pension Plan"), a nonqualified deferred compensation plan. As previously noted, 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, (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, or (d) by a service period of greater than 35 years. By terminating the Supplemental Pension Plan, no further vesting or benefit accrual shall occur under the Supplemental Pension Plan following January 16, 2011 for the respective participants. All remaining unpaid vested benefits shall be distributed in a cash lump sum payment to the participating bank employees after the one year deferral period as required by Section 409A of the Internal Revenue Code. The impact of the termination and liquidation of the Supplemental Pension Plan is not expected to be material to the bank's financial results and will be reflected in the December 31, 2011 financial results of the bank.

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 its term was from September 1, 2003, to August 31, 2013. On November 16, 2010, the bank entered into a lease amendment which extended the term of the lease to August 31, 2024. In addition, the lease amendment included expansion of the leased space to approximately 111,500 square feet of office space. The district associations own 15 headquarter locations and lease two. There are 125 owned and 65 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.

There are no legal proceedings pending against the bank and associations, the outcome of which, in the opinion of legal counsel and management, would materially affect the financial position of the bank and associations. 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, 2010.

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, 2010, 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 are 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 2010, district entities incurred fees of $1.2 million for financial statement audit services and $104 thousand for tax service provided by their independent accountants. During 2010, the district entities incurred fees of $176 thousand for other audit-related services and $152 thousand for non-audit services provided by the independent public accountants. The other audit-related services for the bank and combined district included comfort letter procedures for preferred stock issuance, required FCA accounting letters in conjunction with merger applications, Farmer Mac securitization, transfer of financial assets implementation and an independent tally service for director elections. The non-audit services for the bank and combined district included Information Technology (IT) system implementation audit procedures and best practices, IT-related effectiveness guidance, IT environment and governance recommendations, and Phase II lending system package selection.

Financial Statements

The combined financial statements, together with the report thereon of PricewaterhouseCoopers LLP dated March 1, 2011, and the report of management in this annual report to stockholders, are incorporated herein by reference.

The Farm Credit Bank of Texas and its affiliated associations' (district) 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, 2010	
(dollars in thousands)	Number of Loans	Volume
Total loans and commitments	69,239	$ 18,439,917
Loans and commitments to young farmers and ranchers	12,685	$ 1,818,319
Percent of loans and commitments to young farmers and ranchers	18.3%	9.9%
Loans and commitments to beginning farmers and ranchers	34,816	$ 7,037,128
Percent of loans and commitments to beginning farmers and ranchers	50.3%	38.2%

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

	For the Year Ended December 31, 2010	
(dollars in thousands)	Number of Loans	Volume
Total new loans and commitments	12,531	$ 4,212,655
New loans and commitments to young farmers and ranchers	2,040	$ 460,756
Percent of new loans and commitments to young farmers and ranchers	16.3%	10.9%
New loans and commitments to beginning farmers and ranchers	5,033	$ 1,434,066
Percent of new loans and commitments to beginning farmers and ranchers	40.2%	34.0%

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

	At December 31, 2010				
	Annual Gross Sales				
(dollars in thousands)	$50 Thousand or Less	$50 to $100 Thousand	$100 to $250 Thousand	More Than $250 Thousand	Total
Total number of loans and commitments	17,374	17,662	19,884	14,319	69,239
Number of loans and commitments to small farmers and ranchers	13,288	13,813	15,087	8,186	50,374
Percent of loans and commitments to small farmers and ranchers	76.5%	78.2%	75.9%	57.2%	72.8%
Total loans and commitments volume	$ 1,353,201	$ 1,001,354	$ 2,673,147	$ 13,412,215	$ 18,439,917
Total loans and commitments to small farmers and ranchers volume	$ 279,097	$ 776,656	$ 1,982,891	$ 5,056,775	$ 8,095,419
Percent of loans and commitments volume to small farmers and ranchers	20.6%	77.6%	74.2%	37.7%	43.9%

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

(dollars in thousands)	For the Year Ended December 31, 2010 — Annual Gross Sales — $50 Thousand or Less	$50 to $100 Thousand	$100 to $250 Thousand	More Than $250 Thousand	Total
Total number of new loans and commitments	3,374	2,540	3,287	3,330	12,531
Number of new loans and commitments to small farmers and ranchers	2,652	1,979	2,257	1,356	8,244
Percent of new loans and commitments to small farmers and ranchers	78.6%	77.9%	68.7%	40.7%	65.8%
Total new loans and commitments volume	$ 88,432	$ 191,202	$ 539,462	$ 3,393,559	$ 4,212,655
Total new loans and commitments to small farmers and ranchers volume	$ 72,053	$ 147,663	$ 362,993	$ 950,426	$ 1,533,135
Percent of loan and commitment volume to small farmers and ranchers	81.5%	77.2%	67.3%	28.0%	36.4%