

TEXAS AGFINANCE, FARM CREDIT SERVICES

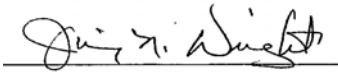
2011 Quarterly Report Third Quarter



For the Quarter Ended September 30, 2011

REPORT OF MANAGEMENT

The undersigned certify that we have reviewed this report, that it has been prepared in accordance with all applicable statutory or regulatory requirements, and that the information contained herein is true, accurate and complete to the best of his or her knowledge and belief.



Jimmy N. Wright, Chief Executive Officer

November 1, 2011



John Prukop, Chairman, Board of Directors

November 1, 2011



Keith A. Ibrom, Chief Financial Officer

November 1, 2011

TEXAS AGFINANCE, FARM CREDIT SERVICES MANAGEMENT'S DISCUSSION AND ANALYSIS

The following commentary reviews the financial performance of the Texas AgFinance, Farm Credit Services (Agricultural Credit Association), referred to as the Association, for the quarter and nine months ended September 30, 2011. These comments should be read in conjunction with the accompanying financial statements and the December 31, 2010 Annual Report to Stockholders.

The Association is a member of the Farm Credit System (System), a nationwide network of cooperatively owned financial institutions established by and subject to the provisions of the Farm Credit Act of 1971, as amended, and the regulations of the Farm Credit Administration (FCA) promulgated thereunder.

The consolidated financial statements comprise the operations of the ACA and its wholly-owned subsidiaries. The consolidated financial statements were prepared under the oversight of the Association's audit committee.

Significant Events:

Effective July 1, 2010, the Association acquired AgCredit of South Texas, ACA, and its subsidiaries. The acquisition package was approved by its regulators, the Farm Credit Administration and the majority of voting stockholders from both Associations. Further discussion and additional information related to the acquisition can be found in the Association's 2010 Annual Report to Stockholders.

On June 25, 2010, the Association entered into a Capitalized Participation Pool agreement with the Farm Credit Bank of Texas (Bank) whereas the Bank purchased a pool of Federal Agricultural Mortgage Corporation (Farmer Mac) mortgage-backed securities (AMBS) from the Association in exchange for the Association agreeing to purchase Bank stock equivalent to 1.6 percentage of the pool's par value. The Association will continue to service the underlying loans in the AMBS. The goal of the program is to better utilize capital between the Association and Bank, while neutralizing the net earnings result at the Association level. The net earnings generated by these loans are paid to the Association in the form of patronage from the Bank. No gain or loss on the AMBS sale to the Bank was recognized.

Loan Portfolio:

Total loans outstanding at September 30, 2011, including nonaccrual loans and sales contracts, were \$371,929,046 compared to \$384,446,939 at December 31, 2010, reflecting a decrease of 3.3 percent. Nonaccrual loans as a percentage of total loans outstanding were 1.8 percent at September 30, 2011, compared to 3.0 percent at December 31, 2010.

The Association recorded \$231,600 in recoveries and \$28,604 in charge-offs for the quarter ending September 30, 2011, and \$464,094 in recoveries and \$37,888 in charge-offs for the same period in 2010. The Association's allowance for loan losses was 0.5 percent and 0.5 percent of total loans outstanding as of September 30, 2011, and December 31, 2010, respectively.

Risk Exposure:

High-risk assets include nonaccrual loans, loans that are past due 90 days or more and still accruing interest, formally restructured loans and other property owned. The following table illustrates the Association's components and trends of high-risk assets.

	September 30, 2011		December 31, 2010	
	Amount	%	Amount	%
Nonaccrual	\$ 8,395,375	73.0%	\$ 11,607,891	69.0%
90 days past due and still accruing interest	-	0.0%	-	0.0%
Formally restructured	-	0.0%	-	0.0%
Other property owned, net	3,105,375	27.0%	4,032,374	31.0%
Total	\$ 11,500,750	100.0%	\$ 15,640,265	100.0%

Results of Operations:

The Association had net income of \$9,377,516 for the nine months ended September 30, 2011, as compared to net income of \$7,302,879 for the same period in 2010 reflecting an increase of 28.4 percent. Net interest income was \$10,045,707 for the nine months ended September 30, 2011, compared to \$9,080,221 for the same period in 2010. Interest income for the nine months of 2011 decreased by \$1,097,690 or 6.5 percent, from the same period of 2010, primarily due to a decrease in average loan volume offset by an increase yields. Interest expense for the months of 2011 decreased by \$2,063,176 or 26.3 percent, from the same period of 2010 due to a decrease in interest rates and a decrease in average debt volume. Average loan volume for the nine months of 2011 was \$391,513,062, compared to \$413,194,974 for the same period of 2010. The average spread on the loan portfolio for the nine months of 2011 was 3.11 percent, compared to 2.66 percent for the same period of 2010.

The Association's return on average assets for the nine months ended September 30, 2011, was 3.05 percent compared to 2.28 percent for the same period in 2010. The Association's return on average equity for the nine months ended September 30, 2011, was 17.92 percent, compared to 18.71 percent for the same period in 2010.

Noninterest income for the nine months ended September 30, 2011, increased \$597,954 compared to the same period in 2010 due to the recognition of net earnings from the AMBS sold to the Farm Credit Bank of Texas. The net earnings generated by these investments during the first six months of 2010 were classified as net interest income. Noninterest expenses for the nine months ended September 30, 2011, decreased \$238,995 compared to the same period in 2010 primarily due to the elimination of billed data processing expenses from the Farm Credit Bank of Texas.

Liquidity and Funding Sources:

The Association secures the majority of its lendable funds from the Farm Credit Bank of Texas (the Bank), which obtains its funds through the issuance of Systemwide obligations and with lendable equity. The following schedule summarizes the Association's borrowings.

	September 30, 2011	December 31, 2010
Note payable to the bank	\$ 314,731,908	\$ 332,143,938
Accrued interest on note payable	562,152	617,685
Total	\$ 315,294,060	\$ 332,761,623

Capital Resources:

The Association's capital position increased by \$9,277,607 at September 30, 2011, compared to December 31, 2010. The Association's debt as a percentage of members' equity was 4.26:1 as of September 30, 2011, compared to 5.14:1 as of December 31, 2010.

Under regulations governing minimum permanent capital adequacy and other capitalization issues, the Association is required to maintain a minimum adjusted permanent capital of 7.0 percent of risk-adjusted assets as defined by the FCA. The Association's permanent capital ratio at September 30, 2011, was 15.5 percent, which is in compliance with the FCA's minimum permanent capital standard. The Association's core surplus ratio and total surplus ratio at September 30, 2011, were 14.7 and 15.0 percent, respectively, which is in compliance with the FCA's minimum surplus standard.

Significant Recent Accounting Pronouncements:

In June 2011, the Financial Accounting Standards Board (FASB) issued guidance entitled, "Comprehensive Income – Presentation of Comprehensive Income." This guidance is intended to increase the prominence of other comprehensive income in financial statements. The current option that permits the presentation of other comprehensive income in the statement of changes in equity has been eliminated. The main provisions of the guidance provides that an entity that reports items of other comprehensive income has the option to present comprehensive income in either one or two consecutive financial statements:

- A single statement must present the components of net income and total net income, the components of other comprehensive income and total other comprehensive income, and a total for comprehensive income.

- In a two-statement approach, an entity must present the components of net income and total net income in the first statement. That statement must be immediately followed by a financial statement that presents the components of other comprehensive income, a total for other comprehensive income, and a total for comprehensive income.

This guidance is to be applied retrospectively and is effective for fiscal years, and interim periods within those years, beginning after December 15, 2011. The adoption of this guidance will not impact financial condition or results of operations, but will result in changes to the presentation of comprehensive income.

In May 2011, the FASB issued guidance entitled, “Fair Value Measurement – Amendments to Achieve Common Fair Value Measurements and Disclosure Requirements in U.S. GAAP and IFRSs.” The amendments change the wording used to describe the requirements in U.S. GAAP for measuring fair value and for disclosing information about fair value measurements. The amendments include the following:

1. Application of the highest and best use and valuation premise is only relevant when measuring the fair value of nonfinancial assets (does not apply to financial assets and liabilities).
2. Aligning the fair value measurement of instruments classified within an entity’s shareholders’ equity with the guidance for liabilities. As a result, an entity should measure the fair value of its own equity instruments from the perspective of a market participant that holds the instruments as assets.
3. Clarifying that a reporting entity should disclose quantitative information about the unobservable inputs used in a fair value measurement that is categorized within Level 3 of the fair value hierarchy.
4. An exception to the requirement for measuring fair value when a reporting entity manages its financial instruments on the basis of its net exposure, rather than its gross exposure, to those risks.
5. Clarifying that the application of premiums and discounts in a fair value measurement is related to the unit of account for the asset or liability being measured at fair value. Premiums or discounts related to size as a characteristic of the entity’s holding (that is, a blockage factor) instead of as a characteristic of the asset or liability (for example, a control premium), are not permitted. A fair value measurement that is not a Level 1 measurement may include premiums or discounts other than blockage factors when market participants would incorporate the premium or discount into the measurement at the level of the unit of account specified in other guidance.
6. Expansion of the disclosures about fair value measurements. The most significant change will require entities, for their recurring Level 3 fair value measurements, to disclose quantitative information about unobservable inputs used a description of the valuation processes used by the entity, and a qualitative discussion about the sensitivity of the measurements. New disclosures are required about the use of a nonfinancial asset measured or disclosed at fair value if its use differs from its highest and best use. In addition, entities must report the level in the fair value hierarchy of assets and liabilities not recorded at fair value but where fair value is disclosed.

The amendments are to be applied prospectively. The amendments are effective during interim and annual periods beginning after December 15, 2011. Early application is not permitted.

In January 2011, the FASB issued guidance entitled, “Deferral of the Effective Date of Disclosures about Troubled Debt Restructurings.” This guidance temporarily delayed the effective date of the disclosures about troubled debt restructurings required by the guidance previously issued on “Disclosures about the Credit Quality of Financing Receivables and the Allowance for Credit Losses.” The effective date of the new disclosures about troubled debt restructurings (TDR) coincides with the guidance for determining what constitutes a TDR as described below.

In April 2011, the FASB issued its guidance entitled, “A Creditor’s Determination of Whether a Restructuring is a Troubled Debt Restructuring,” which provides for clarification on whether a restructuring constitutes a TDR. In evaluating whether a restructuring is a TDR, a creditor must separately conclude that both of the following exists: (1) the restructuring constitutes a concession, and (2) the debtor is experiencing financial difficulties. For nonpublic entities, the guidance is effective for annual periods ending on or after December 15, 2012, including interim periods within those annual periods. The Association is currently evaluating the impact of adoption of this Standard on the financial condition or results of operations. The adoption will result in additional disclosures.

In July 2010, the Financial Accounting Standards Board (FASB) issued guidance on “Disclosures about the Credit Quality of Financing Receivables and the Allowance for Loan 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 by class, the 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 on or 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 impact the Association's financial condition or results of operations, but did result in significant 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 will 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 did not impact the Association's financial condition or results of operations but did result in additional disclosures.

Relationship with the Farm Credit Bank of Texas:

The Association's financial condition may be impacted by factors that affect the Bank. The financial condition and results of operations of the Bank may materially affect the stockholder's investment in the Association. The Management's Discussion and Analysis and Notes to Financial Statements contained in the December 31, 2010 Annual Report of Texas AgFinance, Farm Credit Services more fully describe the Association's relationship with the Bank.

The Texas Farm Credit District's (District) annual and quarterly stockholder 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 also can be requested by e-mail at fcb@farmcreditbank.com. The District makes its annual and quarterly stockholder reports available on its website at www.farmcreditbank.com.

The Association's quarterly stockholder reports are also available free of charge, upon request. These reports can be obtained by writing to Texas AgFinance, Farm Credit Services, P.O. Box 711, Robstown, Texas, 78380 or calling (361) 387-8563. Copies of the Association's quarterly stockholder reports can also be requested by e-mailing kibrom@texasagfinance.com. The Association makes its annual and quarterly stockholder reports available on its Web site at www.texasagfinance.com.

TEXAS AGFINANCE, FARM CREDIT SERVICES

CONSOLIDATED BALANCE SHEET

	September 30, 2011 (unaudited)	December 31, 2010
<u>ASSETS</u>		
Cash	\$ 906,582	\$ 1,523,621
Loans	371,929,046	384,446,939
Less: allowance for loan losses	2,000,000	2,000,000
Net loans	369,929,046	382,446,939
Accrued interest receivable	3,004,735	2,506,144
Investment in and receivable from the bank:		
Capital stock	9,741,385	9,741,385
Other	4,000	162,328
Deferred taxes, net	229,274	351,548
Other property owned, net	3,105,375	4,032,374
Premises and equipment	2,794,711	2,183,634
Other assets	3,945,193	112,460
Total assets	\$ 393,660,301	\$ 403,060,433
<u>LIABILITIES</u>		
Note payable to the bank	\$ 315,182,039	\$ 332,197,638
Advance conditional payments	1,267,851	597,427
Accrued interest payable	562,152	611,518
Patronage distributions payable	(1,108)	2,259,675
Other liabilities	1,759,143	1,781,558
Total liabilities	318,770,077	337,447,816
<u>MEMBERS' EQUITY</u>		
Capital stock and participation certificates	1,759,780	1,814,075
Additional paid-in capital	12,498,556	12,498,556
Allocated retained earnings	8,860,022	8,861,079
Unallocated retained earnings	51,605,541	42,223,347
Accumulated other comprehensive income (loss)	166,325	215,560
Total members' equity	74,890,224	65,612,617
Total liabilities and members' equity	\$ 393,660,301	\$ 403,060,433

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

TEXAS AGFINANCE, FARM CREDIT SERVICES

CONSOLIDATED STATEMENT OF INCOME

(unaudited)

	Quarter Ended September 30,		Nine Months Ended September 30,	
	2011	2010	2011	2010
<u>INTEREST INCOME</u>				
Loans	\$ 5,060,985	\$ 5,282,510	\$ 15,823,792	\$ 14,611,140
Investments	-	-	-	2,310,342
Total interest income	<u>5,060,985</u>	<u>5,282,510</u>	<u>15,823,792</u>	<u>16,921,482</u>
<u>INTEREST EXPENSE</u>				
Note payable to the bank	1,780,534	2,083,120	5,381,035	7,839,882
Advance conditional payments	186	622	619	1,379
Other	129,383	-	396,431	-
Total interest expense	<u>1,910,103</u>	<u>2,083,742</u>	<u>5,778,085</u>	<u>7,841,261</u>
Net interest income	<u>3,150,882</u>	<u>3,198,768</u>	<u>10,045,707</u>	<u>9,080,221</u>
<u>PROVISION FOR LOSSES</u>				
Provision (negative provision) for loan losses	(208,340)	(432,683)	(375,635)	(432,683)
Provision for acquired property losses	<u>173,677</u>	<u>420,930</u>	<u>161,056</u>	<u>420,930</u>
Net interest income after provision for loan losses	<u>3,185,545</u>	<u>3,210,521</u>	<u>10,260,286</u>	<u>9,091,974</u>
<u>NONINTEREST INCOME</u>				
Income from the bank:				
Patronage income	1,053,840	1,194,736	3,284,077	1,957,602
Loan fees	172,176	363,173	476,912	732,642
Financially related services income	478,775	484,442	634,875	521,729
Gain (loss) on other property owned, net	-	11,320	(750)	11,320
Gain (loss) on sale of premises and equipment, net	-	2,220	11,283	6,113
Other noninterest income	<u>674</u>	<u>4,535</u>	<u>45,427</u>	<u>624,464</u>
Total noninterest income	<u>1,705,465</u>	<u>2,060,426</u>	<u>4,451,824</u>	<u>3,853,870</u>
<u>NONINTEREST EXPENSES</u>				
Salaries and employee benefits	1,096,696	1,309,780	3,383,855	3,331,342
Directors' expense	35,679	45,594	167,050	130,326
Purchased services	81,414	81,169	230,428	241,610
Travel	71,320	65,568	226,210	179,067
Occupancy and equipment	111,409	192,032	359,664	445,829
Communications	31,450	40,852	112,815	106,522
Advertising	13,589	10,531	39,165	27,148
Public and member relations	60,033	64,821	199,059	160,025
Supervisory and exam expense	40,571	63,745	121,711	119,191
Insurance Fund premiums	50,291	50,376	148,296	144,457
Other noninterest expense	87,170	151,493	224,068	565,799
Total noninterest expenses	<u>1,679,622</u>	<u>2,075,961</u>	<u>5,212,321</u>	<u>5,451,316</u>
Income before income taxes	<u>3,211,388</u>	<u>3,194,986</u>	<u>9,499,789</u>	<u>7,494,528</u>
Provision for (benefit from) income taxes	<u>1,628</u>	<u>80,138</u>	<u>122,273</u>	<u>191,649</u>
Net income	<u>\$ 3,209,760</u>	<u>\$ 3,114,848</u>	<u>\$ 9,377,516</u>	<u>\$ 7,302,879</u>

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

TEXAS AGFINANCE, FARM CREDIT SERVICES

CONSOLIDATED STATEMENT OF CHANGES IN MEMBERS' EQUITY

(unaudited)

	<u>Capital Stock/ Participation Certificates</u>	<u>Additional Paid-in-Capital</u>	<u>Retained Earnings</u>		<u>Accumulated Other Comprehensive Income (Loss)</u>	<u>Total Members' Equity</u>
			<u>Allocated</u>	<u>Unallocated</u>		
Balance at December 31, 2009	\$ 1,409,735	\$ -	\$ 8,162,321	\$ 34,874,517	\$ 472,079	\$ 44,918,652
Comprehensive income						
Net income	-	-	-	7,302,879	-	7,302,879
Change in postretirement benefit plans	-	-	-	-	(50,486)	(50,486)
Total comprehensive income	-	-	-	7,302,879	(50,486)	7,252,393
Capital stock/participation certificates and allocated retained earnings issued	748,910	-	-	-	-	748,910
Capital stock/participation certificates and allocated retained earnings retired	(323,085)	-	-	-	-	(323,085)
Equity issued or re-characterized upon merger	-	12,498,556	-	-	-	12,498,556
Patronage refunds:						
Cash	-	-	-	783,889	-	783,889
Capital stock/participation certificates and allocated retained earnings	-	-	(1,242)	(783,889)	-	(785,131)
Balance at September 30, 2010	<u>\$ 1,835,560</u>	<u>\$ 12,498,556</u>	<u>\$ 8,161,079</u>	<u>\$ 42,177,396</u>	<u>\$ 421,593</u>	<u>\$ 65,094,184</u>
Balance at December 31, 2010	\$ 1,814,075	\$ 12,498,556	\$ 8,861,079	\$ 42,223,347	\$ 215,560	\$ 65,612,617
Comprehensive income						
Net income	-	-	-	9,377,516	-	9,377,516
Change in postretirement benefit plans	-	-	-	-	(49,235)	(49,235)
Total comprehensive income	-	-	-	9,377,516	(49,235)	9,328,281
Capital stock/participation certificates and allocated retained earnings issued	123,325	-	-	-	-	123,325
Capital stock/participation certificates and allocated retained earnings retired	(177,620)	-	-	-	-	(177,620)
Patronage refunds:						
Cash	-	-	-	-	-	-
Capital stock/participation certificates and allocated retained earnings	-	-	(1,057)	4,678	-	3,621
Balance at September 30, 2011	<u>\$ 1,759,780</u>	<u>\$ 12,498,556</u>	<u>\$ 8,860,022</u>	<u>\$ 51,605,541</u>	<u>\$ 166,325</u>	<u>\$ 74,890,224</u>

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

TEXAS AGFINANCE, FARM CREDIT SERVICES
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
(UNAUDITED)

NOTE 1 — ORGANIZATION AND SIGNIFICANT ACCOUNTING POLICIES:

The Texas AgFinance, Farm Credit Services (Agricultural Credit Association), referred to as the Association, is a member-owned cooperative that provides credit and credit-related services to or for the benefit of eligible borrowers/stockholders for qualified agricultural purposes. The Association serves the counties of Aransas, Atascosa, Austin, Bandera, Bee, Bexar, Brooks, Cameron, DeWitt, Dimmitt, Duval, Edwards, Fayette, Frio, Goliad, Gonzales, Guadalupe, Hidalgo, Jim Hogg, Jim Wells, Karnes, Kenedy, Kerr, Kinney, Kleberg, LaSalle, Lavaca, Live Oak, Maverick, McMullen, Medina, Nueces, Real, San Patricio, Starr, Uvalde, Val Verde, Waller, Washington, Webb, Willacy, Wilson, Zapata, and Zavala, parts of Refugio, and the lower half of Lee in the State of Texas. The Association is a lending institution of the Farm Credit System (the System), which was established by Acts of Congress to meet the needs of American agriculture.

The significant accounting policies followed and the financial condition and results of operations of the Association as of and for the year ended December 31, 2010 are contained in the 2010 Annual Report to Stockholders. These unaudited third quarter 2011 financial statements should be read in conjunction with the 2010 Annual Report to Stockholders.

In June 2011, the Financial Accounting Standards Board (FASB) issued guidance entitled, “Comprehensive Income – Presentation of Comprehensive Income.” This guidance is intended to increase the prominence of other comprehensive income in financial statements. The current option that permits the presentation of other comprehensive income in the statement of changes in equity has been eliminated. The main provisions of the guidance provides that an entity that reports items of other comprehensive income has the option to present comprehensive income in either one or two consecutive financial statements:

- A single statement must present the components of net income and total net income, the components of other comprehensive income and total other comprehensive income, and a total for comprehensive income.
- In a two-statement approach, an entity must present the components of net income and total net income in the first statement. That statement must be immediately followed by a financial statement that presents the components of other comprehensive income, a total for other comprehensive income, and a total for comprehensive income.

This guidance is to be applied retrospectively and is effective for fiscal years, and interim periods within those years, beginning after December 15, 2011. The adoption of this guidance will not impact financial condition or results of operations, but will result in changes to the presentation of comprehensive income.

In May 2011, the FASB issued guidance entitled, “Fair Value Measurement – Amendments to Achieve Common Fair Value Measurements and Disclosure Requirements in U.S. GAAP and IFRSs.” The amendments change the wording used to describe the requirements in U.S. GAAP for measuring fair value and for disclosing information about fair value measurements. The amendments include the following:

1. Application of the highest and best use and valuation premise is only relevant when measuring the fair value of nonfinancial assets (does not apply to financial assets and liabilities).
2. Aligning the fair value measurement of instruments classified within an entity’s shareholders’ equity with the guidance for liabilities. As a result, an entity should measure the fair value of its own equity instruments from the perspective of a market participant that holds the instruments as assets.
3. Clarifying that a reporting entity should disclose quantitative information about the unobservable inputs used in a fair value measurement that is categorized within Level 3 of the fair value hierarchy.
4. An exception to the requirement for measuring fair value when a reporting entity manages its financial instruments on the basis of its net exposure, rather than its gross exposure, to those risks.
5. Clarifying that the application of premiums and discounts in a fair value measurement is related to the unit of account for the asset or liability being measured at fair value. Premiums or discounts related to size as a characteristic of the entity’s holding (that is, a blockage factor) instead of as a characteristic of the asset or liability (for example, a control premium), are not permitted. A fair value measurement that is not a Level 1 measurement may include premiums or discounts other than blockage factors when market participants would incorporate the premium or discount into the measurement at the level of the unit of account specified in other guidance.

6. Expansion of the disclosures about fair value measurements. The most significant change will require entities, for their recurring Level 3 fair value measurements, to disclose quantitative information about unobservable inputs used, a description of the valuation processes used by the entity, and a qualitative discussion about the sensitivity of the measurements. New disclosures are required about the use of a nonfinancial asset measured or disclosed at fair value if its use differs from its highest and best use. In addition, entities must report the level in the fair value hierarchy of assets and liabilities not recorded at fair value but where fair value is disclosed.

The amendments are to be applied prospectively. The amendments are effective during interim and annual periods beginning after December 15, 2011. Early application is not permitted.

In January 2011, the FASB issued guidance entitled, “Deferral of the Effective Date of Disclosures about Troubled Debt Restructurings.” This guidance temporarily delayed the effective date of the disclosures about troubled debt restructurings required by the guidance previously issued on “Disclosures about the Credit Quality of Financing Receivables and the Allowance for Credit Losses.” The effective date of the new disclosures about troubled debt restructurings (TDR) coincides with the guidance for determining what constitutes a TDR as described below.

In April 2011, the FASB issued its guidance entitled, “A Creditor’s Determination of Whether a Restructuring is a Troubled Debt Restructuring,” which provides for clarification on whether a restructuring constitutes a TDR. In evaluating whether a restructuring is a TDR, a creditor must separately conclude that both of the following exists: (1) the restructuring constitutes a concession, and (2) the debtor is experiencing financial difficulties. For nonpublic entities, the guidance is effective for annual periods ending on or after December 15, 2012, including interim periods within those annual periods. The Association is currently evaluating the impact of adoption of this Standard on the financial condition or results of operations. The adoption will result in additional disclosures.

In July 2010, the FASB issued guidance on “Disclosures about the Credit Quality of Financing Receivables and the Allowance for Loan 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 by class, the 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 on or 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 impact the Association’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 will 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 did not impact the Association’s financial condition and results of operations but did result in additional disclosures.

The accompanying consolidated financial statements contain all adjustments necessary for a fair presentation of the interim financial condition and results of operations and conform with generally accepted accounting principles, except for the inclusion of a statement of cash flows. Generally accepted accounting principles require a business enterprise that provides a set of financial statements reporting both financial position and results of operations to also provide a statement of cash flows for each period for which results of operations are provided. In regulations issued by FCA, associations have the option to exclude statements of cash flows in interim financial statements. Therefore, the Association has elected not to include a statement of cash flows in these consolidated financial statements.

The consolidated financial statements comprise the operations of the ACA and its wholly-owned subsidiaries. The preparation of these consolidated financial statements requires the use of management’s estimates. The results for the quarter ended September 30, 2011, are not necessarily indicative of the results to be expected for the year ended December 31, 2011. Certain amounts in the prior period’s financial statements have been reclassified to conform to current financial statement presentation.

NOTE 2 — INVESTMENTS:

The Association held no investments as of September 30, 2011.

NOTE 3 — LOANS AND ALLOWANCE FOR LOAN LOSSES:

A summary of loans follows:

<u>Loan Type</u>	<u>September 30, 2011 Amount</u>	<u>December 31, 2010 Amount</u>
Production agriculture:		
Real estate mortgage	\$ 254,270,114	\$ 236,196,610
Production and intermediate term	93,215,359	120,799,652
Agribusiness:		
Loans to cooperatives	1,729,916	3,143,938
Processing and marketing	10,904,171	10,693,270
Farm-related business	5,080,298	6,074,503
Communication	1,950,814	1,965,814
Energy	3,090,847	3,427,375
Rural residential real estate	2,361,329	3,394,484
Lease receivables	29,503	35,345
Total	<u>\$ 372,632,351</u>	<u>\$ 385,730,991</u>

The Association purchases or sells participation interests with other parties in order to diversify risk, manage loan volume and comply with Farm Credit Administration regulations. The following table presents information regarding the balances of participations purchased and sold at September 30, 2011:

	<u>Other Farm Credit Institutions</u>		<u>Non-Farm Credit Institutions</u>		<u>Total</u>	
	<u>Participations Purchased</u>	<u>Participations Sold</u>	<u>Participations Purchased</u>	<u>Participations Sold</u>	<u>Participations Purchased</u>	<u>Participations Sold</u>
	Real estate mortgage	\$ 9,021,297	\$ 38,259,553	\$ -	\$ 3,909,215	\$ 9,021,297
Production and intermediate term	15,017,934	9,846,260	4,690,076	-	19,708,010	9,846,260
Agribusiness	7,893,497	-	6,755,995	-	14,649,492	-
Communication	1,930,000	-	-	-	1,930,000	-
Energy	3,090,847	-	-	-	3,090,847	-
Total	<u>\$ 36,953,575</u>	<u>\$ 48,105,813</u>	<u>\$ 11,446,071</u>	<u>\$ 3,909,215</u>	<u>\$ 48,399,646</u>	<u>\$ 52,015,028</u>

Nonperforming assets and related credit quality statistics are as follows:

	<u>September 30, 2011</u>	<u>December 31, 2010</u>
Nonaccrual loans:		
Real estate mortgage	\$ 5,618,147	\$ 6,781,655
Production and intermediate term	1,891,318	3,940,246
Agribusiness	885,910	885,990
Total nonaccrual loans	<u>8,395,375</u>	<u>11,607,891</u>
Accruing restructured loans:		
Total accruing restructured loans	-	-
Accruing loans 90 days or more past due:		
Total accruing loans 90 days or more	-	-
Total nonperforming loans	<u>8,395,375</u>	<u>11,607,891</u>
Other property owned	3,105,375	4,032,374
Total nonperforming assets	<u>\$ 11,500,750</u>	<u>\$ 15,640,265</u>

One credit quality indicator utilized by the Association is the Farm Credit Administration Uniform Loan Classification System that categorizes loans into five categories. The categories are defined as follows:

- Acceptable – assets are expected to be fully collectible and represent the highest quality,
- Other assets especially mentioned (OAEM) – 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; however, doubtful assets have additional weaknesses in existing factors, conditions and values that make collection in full highly questionable, and
- Loss – assets are considered uncollectible.

The following table shows loans as a percentage of total loans by loan type as of:

	September 30, 2011	December 31, 2010
Real estate mortgage		
Acceptable	95.9 %	92.1 %
OAEM	1.1	3.1
Substandard/doubtful	3.0	4.8
	<u>100.0</u>	<u>100.0</u>
Production and intermediate term		
Acceptable	94.2	91.8
OAEM	3.5	4.7
Substandard/doubtful	2.3	3.5
	<u>100.0</u>	<u>100.0</u>
Agribusiness		
Acceptable	80.7	84.5
OAEM	14.3	9.0
Substandard/doubtful	5.0	6.5
	<u>100.0</u>	<u>100.0</u>
Energy and water/waste disposal		
Acceptable	43.3	100.0
OAEM	56.7	-
Substandard/doubtful	-	-
	<u>100.0</u>	<u>100.0</u>
Communication		
Acceptable	100.0	100.0
OAEM	-	-
Substandard/doubtful	-	-
	<u>100.0</u>	<u>100.0</u>
Rural residential real estate		
Acceptable	100.0	95.7
OAEM	-	4.3
Substandard/doubtful	-	-
	<u>100.0</u>	<u>100.0</u>
Lease receivables		
Acceptable	100.0	100.0
OAEM	-	-
Substandard/doubtful	-	-
	<u>100.0</u>	<u>100.0</u>
Total Loans		
Acceptable	94.4	91.8
OAEM	2.7	3.8
Substandard/doubtful	2.9	4.4
	<u>100.0 %</u>	<u>100.0 %</u>

The following table provides an age analysis of past due loans (including accrued interest) as of September 30, 2011:

	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	Recorded Investment >90 Days and Accruing
Real estate mortgage	\$ 1,071,516	\$ 3,995,891	\$ 5,067,407	\$ 251,185,274	\$ 256,252,681	\$ -
Production and intermediate term	415,260	257,425	672,685	93,462,442	94,135,127	-
Loans to cooperatives	-	-	-	1,756,250	1,756,250	-
Processing and marketing	-	885,910	885,910	10,041,404	10,927,314	-
Farm-related business	-	-	-	5,104,479	5,104,479	-
Communication	-	-	-	1,951,636	1,951,636	-
Energy and water/waste disposal	-	-	-	3,091,200	3,091,200	-
Rural residential real estate	-	-	-	2,396,087	2,396,087	-
Lease receivables	-	-	-	30,616	30,616	-
Total	\$ 1,486,776	\$ 5,139,226	\$ 6,626,002	\$ 369,019,388	\$ 375,645,390	\$ -

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:

	At September 30, 2011			For the Three Months Ended September 30, 2011		For the Nine Months Ended September 30, 2011	
	Recorded Investment	Unpaid Principal Balance ^a	Related Allowance	Average Impaired Loans	Interest Income Recognized	Average Impaired Loans	Interest Income Recognized
Impaired loans with a related allowance for credit losses:							
Real estate mortgage	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -
Production and intermediate term	-	-	-	-	-	-	-
Loans to cooperatives	-	-	-	-	-	-	-
Processing and marketing	885,910	885,910	47,547	885,910	-	885,910	-
Farm-related business	-	-	-	-	-	-	-
Total	\$ 885,910	\$ 885,910	\$ 47,547	\$ 885,910	\$ -	\$ 885,910	\$ -
Impaired loans with no related allowance for credit losses:							
Real estate mortgage	\$ 5,618,147	\$ 5,863,010	\$ -	\$ 5,240,417	\$ 31,201	\$ 5,173,736	\$ 50,524
Production and intermediate term	1,891,318	5,563,754	-	2,571,582	6,551	3,093,114	9,352
Loans to cooperatives	-	-	-	-	-	-	-
Processing and marketing	-	-	-	-	-	-	-
Farm-related business	-	638,072	-	826	-	551	-
Total	\$ 7,509,465	\$ 12,064,836	\$ -	\$ 7,812,825	\$ 37,752	\$ 8,267,401	\$ 59,876
Total impaired loans:							
Real estate mortgage	\$ 5,618,147	\$ 5,863,010	\$ -	\$ 5,240,417	\$ 31,201	\$ 5,173,736	\$ 50,524
Production and intermediate term	1,891,318	5,563,754	-	2,571,582	6,551	3,093,114	9,352
Loans to cooperatives	-	-	-	-	-	-	-
Processing and marketing	885,910	885,910	47,547	885,910	-	885,910	-
Farm-related business	-	638,072	-	826	-	551	-
Total	\$ 8,395,375	\$ 12,950,746	\$ 47,547	\$ 8,698,735	\$ 37,752	\$ 9,153,311	\$ 59,876

^a Unpaid principal balance represents the recorded principal balance of the loan.

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

	Real Estate Mortgage	Production and Intermediate Term	Agribusiness	Communications	Energy and Water/Waste Disposal	Rural Residential Real Estate	Lease Receivable	Total
Allowance for Credit Losses:								
Balance at								
December 31, 2010	\$ 1,198,126	\$ 609,637	\$ 147,983	\$ 9,860	\$ 17,192	\$ 17,202	\$ -	\$ 2,000,000
Charge-offs	(41,589)	(191)	-	-	-	-	-	-
Recoveries	-	417,415	-	-	-	-	-	-
Provision for loan losses	-	(375,635)	-	-	-	-	-	-
Balance at								
September 30, 2011	\$ 1,156,537	\$ 651,226	\$ 147,983	\$ 9,860	\$ 17,192	\$ 17,202	\$ -	\$ 2,000,000
Ending Balance:								
individually evaluated for impairment	\$ -	\$ 12,975	\$ 95,678	\$ -	\$ -	\$ -	\$ -	\$ 108,653
Ending Balance:								
collectively evaluated for impairment	\$ 1,290,213	\$ 473,963	\$ 89,562	\$ 9,826	\$ 15,564	\$ 12,064	\$ 154	\$ 1,891,346
Recorded Investments in Loans Outstanding:								
Ending Balance at								
September 30, 2011	\$256,252,680	\$ 94,135,127	\$17,788,045	\$ 1,951,636	\$3,091,200	\$ 2,396,087	\$ 30,616	\$375,645,391
Ending Balance for loans individually evaluated for impairment	\$ 38,789	\$ 36,800	\$ 885,910	\$ -	\$ -	\$ -	\$ -	\$ 961,499
Ending Balance for loans collectively evaluated for impairment	\$250,951,218	\$ 91,763,330	\$16,902,135	\$ 1,951,636	\$3,091,200	\$ 2,396,087	\$ 30,616	\$367,086,222
Ending Balance for loans acquired with deteriorated credit quality	\$ 5,262,673	\$ 2,334,997	\$ -	\$ -	\$ -	\$ -	\$ -	\$ 7,597,670

NOTE 4 — CAPITAL:

The Association's Board of Directors has established a Capital Adequacy Plan (Plan) that includes the capital targets that are necessary to achieve the institution's capital adequacy goals as well as the minimum permanent capital standards. The Plan monitors projected dividends, equity retirements and other actions that may decrease the Association's permanent capital. In addition to factors that must be considered in meeting the minimum standards, the Board of Directors also monitors the following factors: capability of management; quality of operating policies, procedures, and internal controls; quality and quantity of earnings; asset quality and the adequacy of the allowance for losses to absorb potential loss within the loan and lease portfolios; sufficiency of liquid funds; needs of an institution's customer base; and any other risk-oriented activities, such as funding and interest rate risk, potential obligations under joint and several liability, contingent and off-balance-sheet liabilities or other conditions warranting additional capital. At least quarterly, management reviews the Association's goals and objectives with the Board of Directors.

NOTE 5 — INCOME TAXES:

Texas AgFinance, Farm Credit Services and its subsidiary are subject to federal and certain other income taxes. The Associations are eligible to operate as cooperatives that qualify for tax treatment under Subchapter T of the Internal Revenue code. Under specified conditions, the Associations can exclude from taxable income amounts distributed as qualified patronage refunds in the form of cash, stock or allocated surplus. Provisions for income taxes are made only on those earnings that will not be distributed as qualified patronage refunds. The Association plans on distributing a patronage for the fiscal year. Deferred taxes are recorded at 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. A valuation allowance is provided against deferred tax assets to the extent that it is more likely than not (more than 50 percent probability), based on management's estimate, that they will not be realized. For the nine

months ended September 30, 2011 and 2010, the Association recorded federal income taxes of \$122,273 and \$191,649, respectively.

Subsidiary, Texas AgFinance, FLCA, is exempt from federal and other income taxes as provided in the Farm Credit Act of 1971.

The Association is unaware of any material changes in uncertain tax positions or changes in classification of interest and/or penalties.

NOTE 6 — FAIR VALUE MEASUREMENTS:

FASB guidance defines fair value as the exchange price that would be received for an asset or paid to transfer a liability in the principal or most advantageous market for the asset or liability. See Note 11 to the 2010 Annual Report to Stockholders for a more complete description.

Assets and liabilities measured at fair value on a non-recurring basis for each of the fair value hierarchy values are summarized below:

<u>September 30, 2011</u>	<u>Fair Value Measurement Using</u>		
	<u>Level 1</u>	<u>Level 2</u>	<u>Level 3</u>
Assets:			
Loans *	\$ -	\$ -	\$ 7,093,757
Other property owned	-	-	3,105,375
<u>December 31, 2010</u>	<u>Fair Value Measurement Using</u>		
	<u>Level 1</u>	<u>Level 2</u>	<u>Level 3</u>
Assets:			
Loans *	\$ -	\$ -	\$ 9,808,203
Other property owned	-	-	4,032,374

*Represents the fair value of certain loans that were evaluated for impairment under authoritative guidance, “Accounting by Creditors for Impairment of a Loan.” The fair value was based upon the underlying collateral since these were collateral-dependent loans for which real estate is the collateral.

Valuation Techniques

As more fully discussed in Note 2 to the 2010 Annual Report to Stockholders, authoritative 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 for the Associations’ assets and liabilities. For a more complete description, see Notes to the 2010 Annual Report to Stockholders

Loans

For certain loans evaluated for impairment under authoritative guidance, the fair value is based upon the underlying collateral since the loans were collateral-dependent loans for which real estate is the collateral. The fair value measurement process uses independent appraisals and other market-based information, but in many cases it also requires significant input based on management’s knowledge of and judgment about current market conditions, specific issues relating to the collateral and other matters. As a result, these fair value measurements fall within Level 3 of the hierarchy. When the value of the real estate, less estimated costs to sell, is less than the principal balance of the loan, a specific reserve is established.

Other Property Owned

Other property owned is generally classified as Level 3. The fair value is based upon the collateral value, which is generally determined using appraisals or other indications based on comparable sales of similar properties. Costs to sell represent transaction costs and are not included as a component of the asset’s fair value.

NOTE 7 — EMPLOYEE BENEFITS PLANS:

The following table summarizes the components of net periodic benefit costs of non-pension other postretirement employee benefits for the nine months ended September 30,:

	Other Benefits	
	2011	2010
Service cost	\$ 25,611	\$ 23,886
Interest cost	57,171	49,842
Amortization of prior service costs	(49,236)	(50,487)
Net periodic benefit cost	<u>\$ 33,546</u>	<u>\$ 23,241</u>

The structure of the District's defined benefit pension plan is characterized as multi-employer since the assets, liabilities and cost of the plan are not segregated or separately accounted for by participating employers (Bank and Associations). The Association recognizes its amortized annual contributions to the plan as an expense. The Association previously disclosed in its financial statements for the year ended December 31, 2010, that it expected to contribute \$61,070 to its defined pension plan in 2011. As of September 30, 2011, \$45,803 of contributions has been made. The Association presently does not anticipate contributing any additional funds to its defined pension plan in 2011.

NOTE 8 — COMMITMENTS AND CONTINGENT LIABILITIES:

The Association is involved in various legal proceedings in the normal course of business. In the opinion of legal counsel and management, there are no legal proceedings at this time that are likely to materially affect the Association.

NOTE 9 — SUBSEQUENT EVENTS:

The Association has evaluated subsequent events through November 1, 2011, which is the date the financial statements were issued. There are no events requiring disclosure.