


First QUARTER 2010

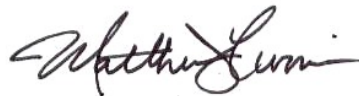
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CERTIFICATION

The undersigned certify that we have reviewed the March 31, 2010 quarterly report of Cape Fear Farm Credit, ACA, that the report has been prepared under the oversight of the Audit Committee of the Board of Directors and in accordance with all applicable statutory or regulatory requirements, and that the information contained herein is true, accurate, and complete to the best of our knowledge and belief.


Richard A. Eason
Chief Executive Officer


Matthew J. Currin
Chief Financial Officer


Ronald J. Allen
Chairman of the Board

May 7, 2010

Report on Internal Control Over Financial Reporting

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

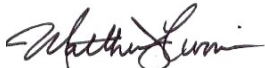
Internal control over financial reporting includes those policies and procedures that: (1) pertain to the maintenance of records that in reasonable detail accurately and fairly reflect the transactions and dispositions of the assets of the Association, (2) provide reasonable assurance that transactions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

The Association's management has completed an assessment of the effectiveness of internal control over financial reporting as of March 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.

Based on the assessment performed, the Association concluded that as of March 31, 2010, the internal control over financial reporting was effective based upon the COSO criteria. Additionally, based on this assessment, the Association determined that there were no material weaknesses in the internal control over financial reporting as of March 31, 2010



Richard A. Eason
Chief Executive Officer



Matthew J. Currin
Chief Financial officer

May 7, 2010

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

(dollars in thousands)

The following commentary reviews the financial condition and results of operations of Cape Fear Farm Credit ACA, (Association) for the period ended March 31, 2010. These comments should be read in conjunction with the accompanying consolidated financial statements, notes to the consolidated financial statements and the 2009 Annual Report of the Association. The accompanying consolidated financial statements were prepared under the oversight of the Audit Committee of the Board of Directors.

LOAN PORTFOLIO

The Association provides funds to farmers, rural homeowners and farm-related businesses for financing of short and intermediate-term loans and long-term real estate mortgage loans. The Association's loan portfolio is diversified over a range of agricultural commodities in our region, including tobacco, swine, poultry, and row-crop operations. Farm size varies and many of the borrowers in the region have diversified farming operations. This factor, along with the numerous opportunities for non-farm income in the area, lessens the level of dependency on any single given commodity. Concentration risk is further mitigated by a portfolio of participation loans purchased or originated and sold.

The gross loan volume of the Association as of March 31, 2010 was \$712,812, an increase of \$30,366 as compared to \$743,178 at December 31, 2009. Net loans outstanding at March 31, 2010, were \$702,736 as compared to \$733,102 at December 31, 2009. Net loans accounted for 92.26 percent of total assets at March 31, 2010, as compared to 91.01 percent of total assets at December 31, 2009.

The decrease in gross and net loan volume during the reporting period is attributed to decreased demand for credit within the general portfolio as well as continued paydown from integrated facility loans. The Association had fewer opportunities for growth in the first quarter due to reduced demand in most of the industries in our portfolio due to uncertainty within these industries and the general economy as a whole. The short-term portfolio, which is heavily influenced by operating-type loans, normally reaches a peak in August and declines in the fall months as farm commodities are marketed and proceeds are applied to the operating loans.

There is an inherent risk in the extension of any type of credit. Portfolio credit quality continues to be maintained at an acceptable level and credit administration remains satisfactory. Nonaccrual loans decreased from \$ 31,548 at December 31, 2009 to \$31,387 at March 31, 2010. This decrease is due to loan reinstatements back into accrual status as well as some pay downs from nonaccrual loans.

Association management maintains an allowance for loan losses in an amount considered sufficient to absorb possible losses in the loan portfolio based on current and expected future conditions. The allowance for loan losses at March 31, 2010 was \$10,076, which is consistent with the December 31, 2009 amount. The overall allowance remained the same in the first quarter but there was a significant movement between the two components of the allowance, the general and specific reserves. The specific reserve portion of the allowance decreased as a result of a reduction in the allowance provision on a loan with a large reserve.. The general allowance was increased to offset anticipated deterioration in credit quality in the overall loan portfolio.

RESULTS OF OPERATIONS

For the three months ended March 31, 2010

Net income for the three months ended March 31, 2010 totaled \$5,480 as compared to \$3,912 for the same period in 2009. The increase of \$1,569 or 40.10 percent is attributed to a decrease in allowance for loan loss provisions of \$1,007 and a decrease in operating expenses of \$275. Also attributing to this increase was a growth in noninterest income in the amount of \$370.

Net interest income for the three months ended March 31, 2010 decreased \$83 or 1.53 percent compared to March 31, 2009. Interest income on loans decreased by \$1,440 and interest income from other sources decreased by \$66, while interest income from investments increased by \$82. Interest expense decreased \$1,340 compared to the same period last year. The decrease in net interest income was a result of decreased earnings on the Association's loanable funds credit with AgFirst Farm Credit Bank. Nonaccrual income was \$160 for the three months ended March 31, 2010, as compared to \$86 for the same period in 2009. Noninterest income for the three months ended March 31, 2010 totaled \$2,925 as compared to \$2,555 for the same period of 2009, an increase of \$370. This increase was a result of a refund from

the Farm Credit System Insurance Corporation (insurance fund) in the amount of \$788. This refund was a result of overpayment of insurance premiums for the years 2001 through 2003 and also 2009. Adding to the increase in noninterest income were Gains/Losses on Rural Home Loans in the amount of \$26. This is a result of our newly reorganized correspondent home lending program. Offsetting these positive variances were decreases in loan fees in the amount of \$262 and a decrease in Equity in earnings of other Farm Credit institutions of \$151. These were a result of reduced loan demand and the resulting decline in loan volume. Other offsetting decreases in noninterest income were a reduction of \$14 in Fees for financially related services, \$7 in Gains/Losses on other property owned and \$10 in other noninterest income.

Noninterest expense for the three months ended March 31, 2010 decreased \$275 compared to the same period of 2009. This decrease resulted from decreases of \$129 in Salaries and benefits and \$151 in Insurance Fund premiums offset by increases of \$4 in Occupancy and equipment and \$1 in other noninterest income.

FUNDING SOURCES

The principal source of funds for the Association is the borrowing relationship established with the Bank through a General Financing Agreement. The General Financing Agreement utilizes the Association's credit and fiscal performance as criteria for establishing a line of credit on which the Association may draw funds. The funds are advanced by the Bank to the Association in the form of notes payable. The notes payable are segmented into variable rate and fixed rate sections. The variable rate note is utilized by the Association to fund variable rate loan advances and operating funds requirements. The fixed rate note is used specifically to fund fixed rate loan advances made by the Association. The total notes payable to the Bank at March 31, 2010, were \$631,107 as compared to \$678,235 at December 31, 2009.

CAPITAL RESOURCES

Total members' equity at March 31, 2010 increased to \$5,499 from the December 31, 2009 total of \$111,162. The increase is primarily due to increased net income due to items mentioned above.

Farm Credit Administration (FCA) regulations require all Farm Credit institutions to maintain minimum permanent capital, total surplus and core surplus ratios. These ratios are calculated by dividing the Association's permanent capital, total surplus and core surplus as defined in FCA regulations, by a risk-adjusted asset base. As of March 31, 2010, the Association's total surplus ratio and core surplus ratio were both 13.71 percent and the permanent capital ratio was 14.07 percent. All three ratios were well above the minimum regulatory ratios of 7.00 percent for permanent capital and total surplus ratios and 3.50 percent for the core surplus ratio.

NOTE: Shareholder investment in the Association could be affected by the financial condition and results of operations of AgFirst Farm Credit Bank. Copies of AgFirst's annual and quarterly reports are available upon request free of charge by calling 1-800-845-1745, ext. 378, or writing Stephen Gilbert, AgFirst Farm Credit Bank, P.O. Box 1499, Columbia, SC 29202. Information concerning AgFirst Farm Credit Bank can also be obtained at their website, www.agfirst.com. Copies of the Association's annual and quarterly reports are also available upon request free of charge by calling 1-800-368-5819 ext. 3243, writing Matthew J. Currin, Cape Fear Farm Credit, P. O. Box 2405, Fayetteville, NC 28302, or accessing the website, www.capefearfarmcredit.com. The Association prepares a quarterly report within 40 days after the end of each fiscal quarter, except that no report need be prepared for the fiscal quarter that coincides with the end of the fiscal year of the institution.

Cape Fear Farm Credit, ACA

Consolidated Balance Sheets

<i>(dollars in thousands)</i>	March 31, 2010 <i>(unaudited)</i>	December 31, 2009 <i>(audited)</i>
Assets		
Cash	\$ 2,305	\$ 3,972
Investment securities:		
Held to maturity (fair value of \$6,000 and \$6,351 respectively)	6,200	6,200
Loans	712,812	743,178
Less: allowance for loan losses	10,076	10,076
Net loans	702,736	733,102
Other investments	19,508	24,742
Accrued interest receivable	6,781	7,781
Investment in other Farm Credit institutions	12,288	12,288
Premises and equipment, net	3,122	3,148
Other property owned	828	828
Due from AgFirst Farm Credit Bank	1,424	6,196
Other assets	6,533	7,284
Total assets	<u>\$ 761,725</u>	<u>\$ 805,541</u>
Liabilities		
Notes payable to AgFirst Farm Credit Bank	\$ 631,107	\$ 678,235
Accrued interest payable	1,795	1,885
Patronage refund payable	367	5,023
Other liabilities	11,795	9,236
Total liabilities	<u>645,064</u>	<u>694,379</u>
Commitments and contingencies		
Members' Equity		
Protected borrower equity	50	56
Capital stock and participation certificates	2,624	2,645
Retained earnings		
Allocated	21,625	21,739
Unallocated	92,675	87,041
Accumulated other comprehensive income (loss)	(313)	(319)
Total members' equity	<u>116,661</u>	<u>111,162</u>
Total liabilities and members' equity	<u>\$ 761,725</u>	<u>\$ 805,541</u>

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

Cape Fear Farm Credit, ACA
Consolidated Statements of Income

(unaudited)

**For the three months
ended March 31,**

(dollars in thousands)

	2010	2009
Interest Income		
Investment securities	\$ 82	\$ —
Loans	10,267	11,706
Other	288	354
	10,637	12,060
Interest Expense		
Notes payable to AgFirst Farm Credit Bank	5,288	6,628
	5,349	5,432
Provision for (reversal of allowance for) loan losses	—	1,006
	5,349	4,426
Net interest income after provision for (reversal of allowance for) loan losses	5,349	4,426
Noninterest Income		
Loan fees	558	821
Fees for financially related services	42	55
Equity in earnings of other Farm Credit institutions	1,469	1,620
Gains (losses) on other property owned, net	1	7
Insurance Fund refunds	788	—
Other noninterest income	41	52
	2,925	2,555
Total noninterest income	2,925	2,555
Noninterest Expense		
Salaries and employee benefits	1,848	1,977
Occupancy and equipment	214	210
Insurance Fund premium	153	304
Other operating expenses	579	578
	2,794	3,069
Total noninterest expense	2,794	3,069
Income before income taxes	5,480	3,912
Provision (benefit) for income taxes	—	—
	5,480	3,912
Net income	\$ 5,480	\$ 3,912

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

Cape Fear Farm Credit, ACA
**Consolidated Statements of Changes in
Members' Equity**

(unaudited)

(dollars in thousands)

	Protected Borrower Capital	Capital Stock and Participation Certificates	Retained Earnings		Accumulated Other Comprehensive Income (Loss)	Total Members' Equity
			Allocated	Unallocated		
Balance at December 31, 2008	\$ 73	\$ 2,634	\$ 17,699	\$ 85,891	\$ (323)	\$ 105,974
Comprehensive income						
Net income				3,912		3,912
Employee benefit plans adjustments					2	2
Total comprehensive income						3,914
Protected borrower equity retired	(14)					(14)
Capital stock/participation certificates issued/(retired), net		(2)				(2)
Retained earnings retired			(4,234)			(4,234)
Patronage distribution adjustment			(21)	100		79
Balance at March 31, 2009	\$ 59	\$ 2,632	\$ 13,444	\$ 89,903	\$ (321)	\$ 105,717
Balance at December 31, 2009	\$ 56	\$ 2,645	\$ 21,739	\$ 87,041	\$ (319)	\$ 111,162
Comprehensive income		7,284				
Net income				5,480		5,480
Employee benefit plans adjustments					6	6
Total comprehensive income						5,486
Protected borrower equity retired	(6)					(6)
Capital stock/participation certificates issued/(retired), net		(21)				(21)
Patronage distribution adjustment			(114)	154		40
Balance at March 31, 2010	\$ 50	\$ 2,624	\$ 21,625	\$ 92,675	\$ (313)	\$ 116,661

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

Cape Fear Farm Credit, ACA

Notes to the Consolidated Financial Statements

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

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

The accompanying financial statements include the accounts of Cape Fear Farm Credit, ACA (the Association). A description of the organization and operations of the Association, the significant accounting policies followed, and the financial condition and results of operations as of and for the year ended December 31, 2009, are contained in the 2009 Annual Report to Shareholders. These unaudited first quarter 2010 consolidated financial statements should be read in conjunction with the 2009 Annual Report to Shareholders.

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

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

The Association maintains an allowance for loan losses in accordance with GAAP. The loan portfolio is reviewed quarterly to determine the adequacy of the allowance for losses. As of March 31, 2010, the allowance for losses is adequate in management's opinion to provide for possible losses on existing loans.

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

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

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

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

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

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

disclosures of valuation techniques and inputs to fair value measurement. The new disclosures and clarification of existing disclosures were effective for interim and annual reporting periods beginning after December 15, 2009, except for the disclosures about purchases, sales, issuances and settlements in the rollforward of activity in Level 3 fair value measurements. Those disclosures are effective for fiscal years beginning after December 15, 2010, and for interim periods within those fiscal years. The adoption of this guidance had no impact on the Association's financial condition and results of operations but resulted in additional disclosures (see Note 5).

NOTE 2 – INVESTMENT SECURITIES

A summary of the amortized cost and fair value of investment securities held-to-maturity at March 31, 2010 and December 31, 2009 follows:

	March 31, 2010				
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value	Yield
Mission related investments	\$ 6,200	\$ 48	\$ (248)	\$ 6,000	5.39%

	December 31, 2009				
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value	Yield
Mission related investments	\$ 6,200	\$ 151	\$ -	\$ 6,351	5.39%

A summary of the expected maturity, amortized cost and estimated fair value of investment securities held-to-maturity at March 31, 2010 follows:

	March 31, 2010		
	Amortized Cost	Fair Value	Weighted Average Yield
In one year or less	\$ 500	\$ 500	4.50%
After one year through five years	-	-	-
After five years through ten years	-	-	-
After ten years	5,700	5,500	5.47
Total	\$ 6,200	\$ 6,000	5.39%

The Association's mission related investments consist of private placement securities purchased under the Rural America Bond Program approved by the FCA.

An investment is considered impaired if its fair value is less than its cost. A continuous unrealized loss position for an investment is based on the date the impairment was first identified. The following table shows the fair value and gross unrealized losses for investments that have been in a continuous unrealized loss position aggregated by investment category at March 31, 2010:

	Less than 12 Months		Greater than 12 Months	
	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
Mission related investments	\$ 3,002	\$ (248)	\$ -	\$ -

The Association performs periodic credit reviews, including other-than-temporary impairment analyses, on its investment securities portfolio. The objective is to quantify any future possible loss of principal or interest due on each security identified for additional analysis. Factors considered in determining whether an impairment is other-than-temporary include among others as applicable: 1) the length of time and the extent to which the fair value is less than cost, 2) adverse conditions specifically related to the industry, 3) geographic area and the condition of the underlying collateral, 4) payment structure of the security, 5) ratings by rating agencies, 6) the credit worthiness of bond insurers, and 7) volatility of the fair value changes.

Based on the results of all analyses, the Association has not recognized any other-than-temporary impairment as the unrealized losses resulted primarily from non-credit related factors. The Association has the ability and intent to hold these investments until a recovery of unrealized losses occurs, which may be at maturity, and at this time expects to collect the full principal amount and interest due on these securities. The Association does not intend to sell these investments and it is not more likely than not that the Association would be required to sell these investments before recovering its costs. All securities continue to perform.

NOTE 3 – ALLOWANCE FOR LOAN LOSSES AND IMPAIRED LOANS

An analysis of the allowance for loan losses follows:

	For the three months ended March 31,	
	2010	2009
Balance at beginning of period	\$10,076	\$ 5,986
Provision for (reversal of) loan losses	-	1,006
Charge-offs	-	(85)
Recoveries	-	32
Balance at end of period	\$10,076	\$ 6,939

The following table presents information concerning impaired loans as of March 31,

	<u>2010</u>	<u>2009</u>
Impaired loans with related allowance	\$15,608	\$ 6,653
Impaired loans with no related allowance	15,835	7,197
Total impaired loans	<u>31,443</u>	<u>13,850</u>
Allowance on impaired loans	<u>\$ 5,669</u>	<u>\$ 2,791</u>

The following table summarizes impaired loan information for the three months ended March 31,

	<u>2010</u>	<u>2009</u>
Average impaired loans	\$ 31,891	\$ 12,378
Interest income recognized on impaired loans	200	97

NOTE 4 – EMPLOYEE BENEFIT PLANS

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

	For the three months ended March 31,	
	<u>2010</u>	<u>2009</u>
Pension	\$ 524	\$ 463
401(k)	34	76
Other postretirement benefits	81	90
Total	<u>\$ 639</u>	<u>\$ 629</u>

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

	Actual YTD Through 3/31/2010	Projected Contributions For Remainder of 2010	Projected Total Contributions 2010
Pension	\$ 7	\$ 1,763	\$ 1,770
Other postretirement benefits	72	171	243
Total	<u>\$ 79</u>	<u>\$ 1,934</u>	<u>\$ 2,013</u>

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

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

NOTE 5 – FAIR VALUE MEASUREMENT

Effective January 1, 2008, the Association adopted FASB guidance on fair value measurements. This guidance defines fair value, establishes a framework for measuring fair value and expands the Association's fair value disclosures for certain assets and liabilities measured at fair value on a recurring and non-recurring basis. These assets and liabilities consist primarily of assets held in trust funds, standby letters of credit, impaired loans, and other property owned.

This guidance defines fair value as the exchange price that would be received for an asset or paid to transfer a liability in an orderly transaction between market participants in the principal or most advantageous market for the asset or liability.

This guidance establishes a fair value hierarchy for disclosure of fair value measurements to maximize the use of observable inputs, that is, inputs that reflect the assumptions market participants would use in pricing an asset or liability based on market data obtained from sources independent of the reporting entity. The valuation hierarchy is based upon the transparency of inputs to the valuation of an asset or liability as of the measurement date. A financial instrument's categorization within the valuation hierarchy is based upon the lowest level of input that is significant to the fair value measurement.

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

Level 1

Level 1 inputs to the valuation methodology are unadjusted quoted prices for identical assets or liabilities in active markets. The Association's Level 1 assets at March 31, 2010 consist of assets held in trust funds related to deferred compensation and supplemental retirement plans. The trust funds include investments in securities that are actively traded and have quoted net asset value prices that are directly observable in the marketplace.

Level 2

Level 2 inputs to the valuation methodology include quoted prices for similar assets and liabilities in active markets; quoted prices in markets that are not active; and inputs that are observable, or can be corroborated, for substantially the full term of the asset or liability. The Association has no Level 2 assets and liabilities measured at fair value on a recurring basis at March 31, 2010.

Level 3

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

Level 3 assets at March 31, 2010 include impaired loans which represent the fair value of certain loans that were evaluated for impairment under FASB guidance. The fair value was based upon the underlying collateral since these were collateral-dependent loans. The fair value measurement process uses independent appraisals and other market-based information, but in many cases it also requires significant input based on management's knowledge of and judgment about current market conditions, specific issues relating to the collateral and other matters. As a result, these fair value measurements fall within Level 3 of the hierarchy. When the value of the collateral, less estimated costs to sell, is less than the principal balance of the loan, a specific reserve is established.

Other property owned is classified as a Level 3 asset at March 31, 2010. The fair value for other property owned is based upon the collateral value. Costs to sell represent transaction costs and are not included as a component of the fair value of other property owned. Level 3 liabilities at March 31, 2010 include standby letters of credit whose market value is internally calculated based on information that is not observable either directly or indirectly in the marketplace.

Assets and Liabilities Measured at Fair Value on a Recurring Basis

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

March 31, 2010				
Level 1	Level 2	Level 3	Total Fair Value	
Assets:				
Assets held in trust funds	\$ 163	\$ -	\$ -	\$ 163
Total Assets	\$ 163	\$ -	\$ -	\$ 163

Liabilities:				
Standby letters of credit	\$ -	\$ -	\$ 70	\$ 70
Total Liabilities	\$ -	\$ -	\$ 70	\$ 70

December 31, 2009				
Level 1	Level 2	Level 3	Total Fair Value	
Assets:				
Assets held in trust funds	\$ 169	\$ -	\$ -	\$ 169
Total Assets	\$ 169	\$ -	\$ -	\$ 169

Liabilities:				
Standby letters of credit	\$ -	\$ -	\$ 97	\$ 97
Total Liabilities	\$ -	\$ -	\$ 97	\$ 97

The following tables present the changes in Level 3 assets and liabilities measured at fair value on a recurring basis for the three months ended March 31, 2010 and 2009. The Association had no transfer of assets or liabilities into or out of Level 1 or Level 2 during the first three months of 2010 and 2009.

	Standby Letters Of Credit
Balance at January 1, 2010	\$ 97
Total gains or (losses) realized/unrealized:	
Included in earnings	-
Included in other comprehensive loss	-
Purchases, sales, issuances and settlements, net	(27)
Transfers in and/or out of level 3	-
Balance at March 31, 2010	<u>\$ 70</u>

	Standby Letters Of Credit
Balance at January 1, 2009	\$ 127
Total gains or (losses) realized/unrealized:	
Included in earnings	-
Included in other comprehensive loss	-
Purchases, sales, issuances and settlements, net	(17)
Transfers in and/or out of level 3	-
Balance at March 31, 2009	<u>\$ 110</u>

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

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

	March 31, 2010				YTD Total Gains (Losses)
	Level 1	Level 2	Level 3	Total Fair Value	
Assets:					
Impaired loans	\$ -	\$ -	\$ 2,098	\$ 2,098	\$ 1,010
Other property owned	\$ -	\$ -	\$ -	\$ -	\$ 1
	December 31, 2009				YTD Total Gains (Losses)
	Level 1	Level 2	Level 3	Total Fair Value	
Assets:					
Impaired loans	\$ -	\$ -	\$ 12,992	\$ 12,992	\$ (6,656)
Other property owned	\$ -	\$ -	\$ 637	\$ 637	\$ 12

NOTE 6 — DISCLOSURES ABOUT FAIR VALUE OF FINANCIAL INSTRUMENTS

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

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

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

	March 31, 2010		December 31, 2009	
	Carrying Amount	Estimated Fair Value	Carrying Amount	Estimated Fair Value
Financial assets:				
Cash	\$ 2,305	\$ 2,305	\$ 3,972	\$ 3,972
Loans, net of allowance	\$ 702,736	\$ 720,558	\$ 733,102	\$ 756,627
Investment securities	\$ 6,200	\$ 6,000	\$ 6,200	\$ 6,351
Tobacco Buyout SIIIC	\$ 19,508	\$ 21,267	\$ 24,742	\$ 26,552
Assets held in trust funds	\$ 163	\$ 163	\$ 169	\$ 169
Financial liabilities:				
Notes payable to AgFirst Farm Credit Bank	\$ 631,107	\$ 639,924	\$ 678,235	\$ 690,319

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

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

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

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

The carrying value of accrued interest approximates its fair value.

- C. **Investment in AgFirst Farm Credit Bank:** Estimating the fair value of the Association's investment in the Bank is not practicable because the stock is not traded. The net investment is a requirement of borrowing from the Bank and is carried at cost plus allocated equities in the accompanying Consolidated Balance Sheets. The Association owns 3.24 percent of the issued stock of the Bank as of March 31, 2010 net of any reciprocal investment. As of that date, the Bank's assets totaled \$30.1 billion and shareholders' equity totaled \$1.7 billion. The Bank's earnings were \$117 million during the first three months of 2010.
- D. **Notes Payable to AgFirst Farm Credit Bank:** The notes payable are segregated into pricing pools according to the types and terms of the loans (or other assets) which they fund. Fair value of the notes payable is estimated by discounting the anticipated cash flows of each pricing pool using the current rate that would be charged for additional borrowings. For purposes of this estimate it is assumed the cash flow on the notes is equal to the principal payments on the Association's loan receivables plus accrued interest on the notes payable. This assumption implies that earnings on the Association's interest margin are used to fund operating expenses and capital expenditures.
- E. **Commitments to Extend Credit:** The estimated market value of off-balance-sheet commitments is minimal since the committed rate approximates current rates offered for commitments with similar rate and maturity characteristics and since the related credit risk is not significant.
- F. **Tobacco Buyout SIIC:** Fair value is determined by discounting the expected future cash flows using current interest rates for similar assets.
- G. **Assets Held in Trust Funds:** See Note 5 for discussion of estimation of fair value for this instrument.
- H. **Investment Securities:** Fair value is determined by discounting the expected future cash flows using appropriate interest rates for similar assets.

NOTE 7 – SUBSEQUENT EVENTS

The Association has evaluated subsequent events and has determined there are none requiring disclosure through May 7, 2010, which is the date the financial statements were issued.