

# FEDERAL LAND BANK ASSOCIATION OF SOUTH ALABAMA, FLCA

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**2009**  
**Quarterly Report**  
**2nd Quarter**



**For the Quarter Ended June 30, 2009**



Part of the Farm Credit System

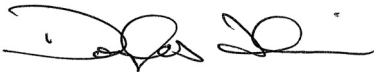
## REPORT OF MANAGEMENT

The financial statements of the Federal Land Bank Association of South Alabama, FLCA (Association) are prepared by management, who are responsible for the statements' integrity and objectivity, including amounts that must necessarily be based on judgments and estimates. The financial statements have been prepared in conformity with generally accepted accounting principles appropriate in the circumstances. Other financial information included in the quarterly report is consistent with that in the financial statements.

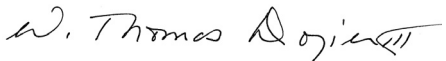
To meet its responsibility for reliable financial information, management depends on the Farm Credit Bank of Texas' (Bank) and the Association's accounting and internal control systems, which have been designed to provide reasonable, but not absolute, assurance that assets are safeguarded and transactions are properly authorized and recorded. The systems have been designed to recognize that the cost of controls must be related to the benefits derived. The annual financial statements are audited by PricewaterhouseCoopers LLP, independent accountants, who conduct a review of internal controls solely for the purpose of establishing a basis for reliance thereon in determining the nature, extent and timing of audit tests applied in the audit of the financial statements in accordance with generally accepted auditing standards. The Association is also examined by the Farm Credit Administration.

The audit committee of the board of directors has oversight responsibility for the Association's system of internal controls and financial reporting. The audit committee consults regularly with management and meets periodically with the independent auditors and the internal auditor to review the scope and results of their work. The independent auditors and internal auditor have direct access to the audit committee.

The undersigned certify that, to the best of our knowledge and belief, the financial statements and other financial information included in this quarterly report reliably present the financial condition of the Federal Land Bank Association of South Alabama, FLCA and the results of its operations for the periods shown.



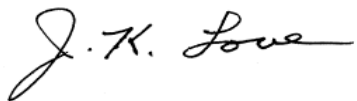
Douglas Thiessen  
President/Chief Executive Officer  
July 29, 2009



W. Thomas Dozier, III  
Chairman, Board of Directors  
July 29, 2009



M. Scott Sellers, CPA  
Sr.VP/Chief Financial Officer  
July 29, 2009



J.K. Love, CPA  
Chairman, Audit Committee  
July 29, 2009

## **FEDERAL LAND BANK ASSOCIATION OF SOUTH ALABAMA, FLCA MANAGEMENT'S DISCUSSION AND ANALYSIS**

The following commentary reviews the financial performance of the Federal Land Bank Association of South Alabama, FLCA (Federal Land Credit Association), referred to as the Association, for the quarter and six months ended June 30, 2009. These comments should be read in conjunction with the accompanying financial statements and the December 31, 2008 Annual Report of the Association.

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 financial statements were prepared under the oversight of the Association's audit committee.

### **Results of Operations:**

The Association had net income of \$866,283 and \$2,529,437 for the three and six months ended June 30, 2009, as compared to net income of \$2,863,434 and \$5,813,789 for the same periods in 2008 reflecting an decrease of 69.8 and 56.5 percent, respectively. Net interest income was \$4,108,502 and \$8,198,741, respectively, for the three and six months ended June 30, 2009, compared to \$3,970,739 and \$7,964,743 for the same periods in 2008. Interest income for the first six months of 2009 decreased by \$1,833,836 or 9.9 percent, from the same period of 2008, primarily due to declines in yields on earning assets, offset partially by an increase in average loan volume. Interest expense for the first six months of 2009 decreased by \$2,067,834, or 19.4 percent, from the same period of 2008 due to a decrease in interest rates, offset partially by an increase in average debt volume. The provision for loan losses for the first six months of 2009 increased by \$2,568,834, or 100.9 percent, over the same period of 2008, due mostly to specific reserves recorded for three large credits in 2009. All three credits were participation loans in the ethanol industry and are discussed further in the "Risk Exposure" section of Management's Discussion and Analysis below. Average loan volume for the second quarter of 2009 was \$610,887,207, compared to \$559,256,117 in the second quarter of 2008.

Noninterest income for the three and six months ended June 30, 2009 decreased by \$265,312 and \$547,106, or 33.7 percent and 32.9 percent, respectively, over the same periods of 2008. This is due primarily to lower patronage income from Farm Credit Bank of Texas (the Bank) in the first six months of 2009 as compared to the first six months of 2008. This decrease in patronage is due almost entirely to the fact that in 2009, the Association began accruing less Direct Note patronage from the Bank on a monthly basis than in 2008. Accordingly, six months of estimated Direct Note patronage, to be received at year end, have been accrued into income as of June 30, 2009, but at a lesser amount than in the prior year. Also contributing

to the decrease in noninterest income is a decrease in loan fees caused by proportionately lower activity in loan closings in the first two quarters of 2009 compared to the first two quarters of 2008.

Noninterest expenses for the three and six months ended June 30, 2009, increased by \$201,847 and \$379,271, or 10.7 percent and 9.9 percent, respectively, as compared to the same periods in 2008. The increase is due primarily to an increase in salaries and employee benefits costs and Farm Credit System Insurance Corporation (FCSIC) premium expense. The increase in salaries and employee benefits is primarily due to an increase in contributions to the defined benefit retirement plan, as well as the addition of three employees. For more information on the defined benefit plan, refer to the 2008 Annual Report and Note 5, "Employee Benefit Plans," to the financial statements, included in this quarterly report. FCSIC premiums increased on the basis of the Association having higher loan volume in the first two quarters of 2009 than in the first two quarters of 2008.

The Association had charge-offs of \$32,801 and \$754,830 for the three and six months ended June 30, 2009, and charge-offs of \$0 and \$35,004 for the same periods in 2008. The Association did not record any recoveries during these respective time periods. The Association's allowance for loan losses was 0.4 percent and 0.1 percent of total loans outstanding as of June 30, 2009, and 2008, respectively.

The Association's return on average assets for the six months ended June 30, 2009, was 0.81 and 2.03 percent for the same period in 2008. The Association's return on average equity for the six months ended June 30, 2009, was 4.94 and 12.05 percent for the same period in 2008.

### **Loan Portfolio:**

The Association makes and services loans, secured by a first lien on real estate, to farmers, ranchers, rural homeowners and certain farm-related businesses. The majority of the loans serviced by the Association contain provisions for variable interest rates and are long-term. Loans serviced by the Association offer several installment payment cycles, the timing of which usually coincides with the seasonal cash-flow capabilities of the borrower.

Total loans outstanding at June 30, 2009, stated at recorded investment (principle less funds held), were \$618,816,842 compared to \$593,982,063 at December 31, 2008, reflecting an increase of 4.2 percent. The major commodities within the Association's loan portfolio are timber, poultry, cattle, and field crops.

The following table reflects the credit quality of the Association's loan volume as of:

	<b>June 30, 2009</b>	December 31, 2008
Acceptable	<b>94.8 %</b>	96.2 %
Special Mention	<b>1.6 %</b>	1.9 %
Substandard	<b>3.6 %</b>	1.9 %
Total	<b>100.0 %</b>	100.0 %

**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.

	<b>June 30, 2009</b>		December 31, 2008	
	Amount	%	Amount	%
Nonaccrual	\$ 8,216,066	80.8%	\$ 4,231,385	91.5%
90 days past due and still accruing interest	1,190,321	11.7%	129,691	2.8%
Formally restructured	-	0.0%	-	0.0%
Other property owned, net	758,319	7.5%	262,784	5.7%
Total	<b>\$ 10,164,706</b>	<b>100.0%</b>	<b>\$ 4,623,860</b>	<b>100.0%</b>

At June 30, 2009 loans that were considered impaired were \$9,406,387 compared to \$4,361,076 at December 31, 2008. This represents 1.5 percent and 0.7 percent of loan volume, respectively. Impaired loans consist of all high-risk assets except other property owned, net. The increase in impaired assets is primarily due to three large credits related to the ethanol industry, which has experienced significant financial stress as a result of high input costs, among other factors, and a small number of other loans adversely affected by the poor economic conditions over the past year.

The Association originated a loan to one borrower through the Capital Markets of the South (CMS) and participated the loan to 13 other Farm Credit associations, with the Association serving as the lead lender. The original funded balance of the loan was \$68,500,000, and the Association retained 5.56 percent of the loan. In 2007, the loan was deemed to be nonaccrual due to its significant under collateralized position and a credit default. Accordingly, the Association began pursuing collection efforts, including liquidating part of the loan's collateral, which was applied to the outstanding balance for all participants. In addition, by the end of 2007 the Association, along with the four other CMS member associations, repurchased, on a pro-rata basis, the portions of the loan held by all other non-CMS participants. As part of loan repurchase transactions noted above, the Association received a general release from the non-CMS

participants for claims related to the loan, and agreed to indemnify the non-CMS participants from any liability arising from legal proceedings related to the loan.

In 2008 collection efforts continued, resulting in legal judgments against the borrowers, allowing the Association to foreclose on portions of the real estate collateral, with sales proceeds being applied against the outstanding balance of the loan. The Association is still in process of foreclosing on the remaining portions of the real estate collateral. In addition, the borrowers have surrendered various other real and personal properties, all of which is to be liquidated and applied against the loan balance. All sales of remaining real estate collateral and other properties are expected to be completed by the end of 2009.

During 2007, charge-offs of \$30,245,000 were recognized; the Association's portion of the 2007 charge-offs was \$4,812,212. No further charge-offs or allowance reserves were required to be recognized in 2008 or year to date in 2009. As of June 30, 2009, the Association's portion of the loan's remaining book balance was \$360,148. For more information on impaired loans and the allowance for loan losses, see Note 2 to the financial statements, "Allowance for Loan Losses," included in this quarterly report.

**Liquidity and Funding Sources:**

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

	<u>June 30, 2009</u>	<u>December 31, 2008</u>
Note payable to the Bank	\$ 530,873,327	\$ 506,309,605
Accrued interest on note payable	1,429,212	1,687,429
Total	<u>\$ 532,302,539</u>	<u>\$ 507,997,034</u>

**Capital Resources:**

The Association's capital position decreased by \$933,749 at June 30, 2009, compared to December 31, 2008. The Association's debt as a ratio to members' equity was 5.26:1 as of June 30, 2009, compared to 4.99:1 as of December 31, 2008.

In February 2009, the board declared a \$3,500,000 cash patronage to be paid to stockholders from the Association's 2008 Earnings. The patronage distribution was completed in April 2009.

Under regulations governing minimum permanent capital adequacy and other capitalization issues, the Association is required to maintain a minimum adjusted permanent capital of seven percent of risk-adjusted assets as defined by the FCA.

The Association's permanent capital ratio at June 30, 2009, was 15.1 percent, which is in compliance with the FCA's minimum permanent capital standard. The Association's core surplus ratio and total surplus ratio at June 30, 2009, were 14.5 and 14.5 percent, respectively, which is in compliance with the FCA's minimum surplus standard.

### **Legal Proceedings:**

In relation to the loan described in the "Risk Exposure" section of Management's Discussion and Analysis, above, the Association is involved in one lawsuit as of the date of this report. The overall character of the lawsuit is for damages incurred by the Association as a result of alleged wrongful acts of the borrower and other third-party defendants. The Association brought this civil lawsuit in the US Federal District Court in Texas, the borrower's domicile state, and the trial was held in early February 2009. On March 19, 2009, the court rendered judgment in favor of the Association against all parties, jointly and severally, on all counts for \$41,549,236 in actual damages. On April 23, 2009 the Court trebled the judgment to \$124,647,710. Two defendants are pursuing an appeal of the judgment. The Association is pursuing the assets of all liable parties in satisfaction of the judgment.

In February 2009, the Association received approval to foreclose the lien of its mortgage on the remaining real estate collateral located in Muhlenberg County, Kentucky and intends to foreclose such lien as soon as possible. However, prior to conducting the foreclosure, the Association is investigating the value of coal reserves on the property in order to properly understand the overall value of the property. The Association has been and will remain vigorous in pursuit of collection of the loan balances outstanding and other potential sources of recovery.

### **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 stockholders' investment in the Association. The Management's Discussion and Analysis and Notes to Financial Statements contained in the December 31, 2008 Annual Report of Federal Land Bank of South Alabama, FLCA more fully describe the Association's relationship with the Bank.

The Tenth 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) 483-9260. Copies of the District's quarterly and annual stockholder reports also can be requested by e-mail at [fcb@farmcreditbank.com](mailto:fcb@farmcreditbank.com). The District makes its annual and quarterly stockholder reports available on its web site at [www.farmcreditbank.com](http://www.farmcreditbank.com).

The Association's annual and quarterly stockholder reports are also available free of charge, upon request. These reports can be obtained by writing to Federal Land

Bank Association of South Alabama, FLCA, P.O. Box 241687, Montgomery, Alabama, 36124-1687, or by calling (334) 270-8687. Copies of the reports can also be requested by e-mailing [awolf@farmcreditbank.com](mailto:awolf@farmcreditbank.com). The Association's quarterly stockholder reports are available on its website at [www.alabamalandloan.com](http://www.alabamalandloan.com) approximately 40 days after each quarter end, and the annual stockholder report is available on its website 75 days after the fiscal year end. Copies of the annual stockholder report can also be requested 90 days after fiscal year end

**FEDERAL LAND BANK ASSOCIATION OF SOUTH ALABAMA, FLCA**

**BALANCE SHEET**

	<b>June 30, 2009 (unaudited)</b>	<b>December 31, 2008</b>
	<hr/>	<hr/>
<b><u>ASSETS</u></b>		
Cash	\$ 247,226	\$ 2,115,315
Loans	618,816,842	593,982,063
Less: allowance for loan losses	<u>2,750,842</u>	<u>959,718</u>
Net loans	616,066,000	593,022,345
Accrued interest receivable	8,279,015	8,069,442
Investment in and receivable from the Bank:		
Capital stock	9,567,900	9,567,900
Accrued patronage receivable	255,000	365,891
Other property owned, net	758,319	262,784
Premises and equipment	1,839,460	1,794,341
Other assets	<u>742,974</u>	<u>205,034</u>
Total assets	<u><u>\$ 637,755,894</u></u>	<u><u>\$ 615,403,052</u></u>
 <b><u>LIABILITIES</u></b>		
Note payable to the Bank	\$ 530,873,327	\$ 506,309,605
Accrued interest payable	1,429,212	1,687,429
Drafts outstanding	1,309,650	1,172,178
Other liabilities	<u>2,265,553</u>	<u>3,421,940</u>
Total liabilities	<u><u>535,877,743</u></u>	<u><u>512,591,152</u></u>
 <b><u>MEMBERS' EQUITY</u></b>		
Capital stock and participation certificates	3,550,505	3,494,180
Unallocated retained earnings	98,163,104	99,133,667
Accumulated other comprehensive income	<u>164,542</u>	<u>184,053</u>
Total members' equity	<u>101,878,151</u>	<u>102,811,900</u>
Total liabilities and members' equity	<u><u>\$ 637,755,894</u></u>	<u><u>\$ 615,403,052</u></u>

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

FEDERAL LAND BANK ASSOCIATION OF SOUTH ALABAMA, FLCA

STATEMENT OF INCOME

(unaudited)

	Quarter Ended		Six Months Ended	
	June 30,		June 30,	
	2009	2008	2009	2008
<b><u>INTEREST INCOME</u></b>				
Loans	\$ 8,394,426	\$ 9,051,747	\$ 16,767,212	\$ 18,601,048
<b><u>INTEREST EXPENSE</u></b>				
Note payable to the Bank	4,285,924	5,081,008	8,568,471	10,636,305
Net interest income	4,108,502	3,970,739	8,198,741	7,964,743
<b><u>PROVISION FOR LOSSES</u></b>				
Provision for loan losses	1,711,226	18,847	2,545,953	(22,881)
Provision for acquired property losses	(24,264)	-	43,614	20,475
Net interest income after provision for loan losses	2,421,540	3,951,892	5,609,174	7,967,149
<b><u>NONINTEREST INCOME</u></b>				
Patronage income from the Bank	204,378	440,421	410,352	891,060
Loan fees	302,959	343,080	650,902	710,475
Financially related services income	960	1,031	2,667	2,534
Gain on sale of other property owned, net	7,159	-	7,092	-
Gain (Loss) on sale of premises and equipment, net	6,571	784	(5,893)	2,272
Other noninterest income	-	2,023	47,369	53,254
Total noninterest income	522,027	787,339	1,112,489	1,659,595
<b><u>NONINTEREST EXPENSES</u></b>				
Salaries and employee benefits	1,273,088	1,086,652	2,574,944	2,157,667
Directors' expense	56,996	65,648	149,537	126,817
Purchased services	368,199	574,698	906,669	1,365,593
Travel	80,513	98,620	137,093	164,833
Occupancy and equipment	78,609	62,988	156,623	123,240
Communications	24,573	24,503	50,766	47,380
Advertising	28,293	46,782	46,481	75,356
Public and member relations	34,104	35,564	70,692	66,766
Supervisory and exam expense	55,568	54,384	111,137	108,770
FCSIC insurance expense	263,249	225,894	545,109	463,087
Other noninterest expense	30,923	26,186	46,540	47,504
CMS expense reimbursements	(216,831)	(426,122)	(603,365)	(934,058)
Total noninterest expenses	2,077,284	1,875,797	4,192,226	3,812,955
Net income	\$ 866,283	\$ 2,863,434	\$ 2,529,437	\$ 5,813,789

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

**FEDERAL LAND BANK ASSOCIATION OF SOUTH ALABAMA, FLCA**

**STATEMENT OF CHANGES IN MEMBERS' EQUITY**

(unaudited)

	<u>Capital Stock/ Participation Certificates</u>	<u>Unallocated Retained Earnings</u>	<u>Accumulated Other Comprehensive Income (Loss)</u>	<u>Total Members' Equity</u>
Balance at December 31, 2007	\$ 3,326,230	\$ 91,538,558	\$ 282,547	\$ 95,147,335
Adjustment to beginning balance due to FAS No. 158 accounting change	-	(18,492)	-	(18,492)
Balance at January 1, 2008	3,326,230	91,520,066	282,547	95,128,843
Comprehensive income				
Net income	-	5,813,789	-	5,813,789
Amortization of costs included in periodic retirement benefit costs	-	-	(19,523)	(19,523)
Total comprehensive income	-	5,813,789	(19,523)	5,794,266
Capital stock/participation certificates issued	344,800			344,800
Capital stock/participation certificates retired	(266,370)			(266,370)
Patronage refunds:				-
Cash	-	(3,200,000)	-	(3,200,000)
Change in patronage declared and paid		294		294
Balance at June 30, 2008	<u>\$ 3,404,660</u>	<u>\$ 94,134,149</u>	<u>\$ 263,024</u>	<u>\$ 97,801,833</u>
Balance at December 31, 2008	\$ 3,494,180	\$ 99,133,667	\$ 184,053	\$ 102,811,900
Comprehensive income				
Net income	-	2,529,437	-	2,529,437
Amortization of costs included in periodic retirement benefit costs	-	-	(19,511)	(19,511)
Total comprehensive income	-	2,529,437	(19,511)	2,509,926
Capital stock/participation certificates issued	253,980			253,980
Capital stock/participation certificates retired	(197,655)			(197,655)
Patronage refunds:				-
Cash	-	(3,500,000)	-	(3,500,000)
<b>Balance at June 30, 2009</b>	<u><b>\$ 3,550,505</b></u>	<u><b>\$ 98,163,104</b></u>	<u><b>\$ 164,542</b></u>	<u><b>\$ 101,878,151</b></u>

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

**FEDERAL LAND BANK ASSOCIATION OF SOUTH ALABAMA, FLCA**  
**NOTES TO THE FINANCIAL STATEMENTS**  
(UNAUDITED)

**NOTE 1 — ORGANIZATION AND SIGNIFICANT ACCOUNTING POLICIES:**

The Federal Land Bank Association of South Alabama, FLCA (Federal Land 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 Autauga, Baldwin, Barbour, Bibb, Bullock, Butler, Chambers, Chilton, Choctaw, Clarke, Coffee, Conecuh, Coosa, Covington, Crenshaw, Dale, Dallas, Elmore, Escambia, Geneva, Greene, Hale, Henry, Houston, Lee, Lowndes, Macon, Marengo, Mobile, Monroe, Montgomery, Perry, Pickens, Pike, Russell, Sumter, Tallapoosa, Tuscaloosa, Washington and Wilcox in the state of Alabama. 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.

A description of the Association's significant accounting policies and the financial condition and results of operations as of December 31, 2008 are contained in the 2008 Annual Report to the stockholders. These unaudited second quarter 2009 financial statements should be read in conjunction with the 2008 Annual Report to the stockholders.

The accompanying 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. However, 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 financial statements.

The preparation of these financial statements requires the use of management's estimates. The results for the quarter ended June 30, 2009 are not necessarily indicative of the results to be expected for the year ended December 31, 2009. Certain amounts in the prior period's financial statements have been reclassified to conform to current financial statement presentation.

**NOTE 2 — ALLOWANCE FOR LOAN LOSSES:**

The allowance for loan losses is maintained at a level considered adequate by management to provide for estimated 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. An analysis of the allowance for loan losses follows:

	<b>June 30, 2009</b>	June 30, 2008
Balance at beginning of quarter	<u>\$ 1,072,417</u>	<u>\$ 475,832</u>
Provision for loan losses	1,711,226	18,847
Charge-offs	(32,801)	-
Recoveries	-	-
Balance at end of quarter	<u><u>\$ 2,750,842</u></u>	<u><u>\$ 494,679</u></u>

The following table presents information concerning impaired loans:

	<b>June 30, 2009</b>	June 30, 2008
Impaired loans with related allowance	<u>\$ 5,859,420</u>	<u>\$ 2,129,416</u>
Impaired loans with no related allowance	3,546,967	841,382
Total impaired loans	<u><u>\$ 9,406,387</u></u>	<u><u>\$ 2,970,798</u></u>
Allowance on impaired loans	\$ 2,133,201	\$ 291,555
Average impaired loans	\$ 5,959,492	\$ 2,937,698
Interest income on impaired loans for the quarter	\$ 8,625	\$ 19,638

**NOTE 3 — 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 inherent losses within the loan portfolio; 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.

In February 2009, the board declared a \$3,500,000 cash patronage to be paid to stockholders from the Association's 2008 Earnings. The patronage distribution was completed in April 2009.

**NOTE 4 — CAPITAL MARKETS:**

Until the second quarter of 2007, the Association participated in the Capital Markets of the South (CMS), a joint venture created in 2003 for the purpose of expanding the participants' lending opportunities. The CMS group was comprised of the Association, the Federal Land Bank Association of North Alabama, FLCA, the Land Bank of North Mississippi, FLCA, Southern AgCredit, ACA (formerly Land Bank South, FLCA), and the Louisiana Federal Land Bank Association, FLCA. During the second quarter of 2007, the CMS members decided to discontinue the joint venture. The Association will continue to service the existing CMS loan portfolio, with revenue and expenses continuing to be shared accordingly as noted below, until such time as all of the loans are fully matured or paid off.

Pursuant to the terms of the alliance, each of the five CMS participating associations generally share equally in the costs of operating the venture. All CMS noninterest expenses are recorded gross on the Association's books and then reimbursed 80% by the other four associations. The total amount of reimbursements is included on the statement of income in the line item entitled "CMS expense reimbursements." The Association's pro-rata share of income from CMS operations are recorded in the statement of income in their respective line items.

**NOTE 5 — EMPLOYEE BENEFIT PLANS:**

The following table summarizes the components of net periodic benefit costs for the six months ended June 30, :

	Other Benefits	
	2009	2008
Service cost	\$ 24,312	\$ 21,536
Interest cost	39,202	34,972
Expected return on plan assets	-	-
Amortization of prior service costs	(19,511)	(19,828)
Amortizations of net (gain) loss	-	305
Net periodic benefit cost	<u>\$ 44,003</u>	<u>\$ 36,985</u>

In September 2006, the Financial Accounting Standards Board issued Statement of Financial Accounting Standards No. 158 "Employers' Accounting for Defined Benefit Pension and Other Postretirement Plans" (SFAS 158), which required the recognition of the overfunded or underfunded status of pension and other postretirement benefit plans on the balance sheet. The balance sheet recognition provisions of SFAS 158 were adopted at December 31, 2007. SFAS 158 also requires that employers measure the benefit obligation and plan assets as of the fiscal year end for fiscal years ending after December 15, 2008. In fiscal 2007 and earlier, we used a September 30 measurement date for other postretirement benefit plans. The Standard provides two approaches for an employer to

transition to a fiscal year end measurement date. The Association has applied the second approach, which allows for the use of the measurements determined for the prior year end.

Under this alternative, postretirement benefit expense measured for the three-month period October 1, 2007 to December 31, 2007 (determined using the September 2007 measurement date) was recorded as an adjustment to beginning 2008 retained earnings. As result, the Association decreased retained earnings by \$18,492 and increased the postretirement benefit liability by \$18,492.

The Association previously disclosed in its Annual Report to the stockholders for the year ended December 31, 2008, that it expected to contribute \$27,959 to its postretirement health and welfare benefits plan in 2009. As of June 30, 2009, \$10,784 of contributions have been made. The Association's liability for the plan's unfunded accumulated benefit obligation at June 30, 2009 was \$1,308,608 and is included in "Other liabilities" in the balance sheet.

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