

2009 Quarterly Report



For the 2nd Quarter Ended June 30, 2009

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.



Charles P. Gant
Chief Executive Officer/President
August 7, 2009



Barnett L. Baker
Chairman, Board of Directors
August 7, 2009



Chief Financial Officer
August 7, 2009

TEXAS LAND BANK, ACA

Management's Discussion and Analysis

The following commentary reviews the financial performance of the Texas Land Bank, ACA (Agricultural 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 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.

RESULTS OF OPERATIONS:

Net Income

The Association had net income of \$315,959 and \$2,428,948 for the three and six months ended June 30, 2009, as compared to net income of \$2,153,917 and \$4,188,890 for the same periods in 2008 reflecting a decrease of 85.3 and 42.0 percent, respectively. The decrease in net income for the three months ended June 30, 2009, consisted of a \$15,798 decrease in net interest income, a \$109,112 decrease in noninterest income, a \$142,475 increase in noninterest expenses, and a \$1,570,573 increase in provision for loan losses expense as compared to the same period in 2008.

Net Interest Income

Net interest income was \$2,956,789 and \$6,003,094, respectively, for the three and six months ended June 30, 2009, compared to \$2,972,587 and \$5,981,879 for the same periods in 2008. Although average loan volume for the second quarter of 2009 was \$416,403,627, compared to \$399,612,810 in the second quarter of 2008, and the average spread on the loan portfolio for the second quarter of both 2009 and 2008 was 2.17 percent, the loan portfolio experienced an increased level of nonaccrual loans in 2009 which negatively impacted interest income, and ultimately, net interest income for the quarter and six months ended June 30, 2009.

Noninterest Income and Expense

Noninterest income for the quarter ended June 30, 2009, decreased by \$109,112 or 20.4 percent from the same period in 2008. This decrease was due primarily to a decline in loan fees collected on loans serviced and originated by the Association in the second quarter of 2009 as compared to the higher than average volume of loan fees collected during the same period in 2008. Noninterest expenses for the quarter ended June 30, 2008, increased by \$142,475 or 10.9 percent from the same period in 2008. The increase is primarily attributable to an increase in Farm Credit Insurance Corporation (FCSIC) expenses as well as increased salary and benefits expenses related to pension plan costs.

Provision for Loan Losses

Provision for loan losses for the three and six months ended June 30, 2009, was \$1,620,573 and \$1,661,914, representing an increase of \$1,570,573 and \$1,561,914 as compared to the same periods in 2008. During the second quarter of 2009, the Association recorded specific provisions on participation loans to two borrowers which were placed into nonaccrual status during the quarter. Following this, the allowance at June 30, 2009, was considered adequate by management to absorb probable losses inherent in its portfolio.

Financial Ratios

The Association's return on average assets for the six months ended June 30, 2009, was 1.15 and 2.07 percent for the same period in 2008. The Association's return on average equity for the six months ended June 30, 2009, was 6.00 and 10.80 percent for the same period in 2008. These decreases are caused by lower net income in 2009 which is largely related to a decrease in earnings on own funds caused by lower interest rates, slightly higher operating costs, and additional provision for loan loss expenses as discussed above.

LOAN PORTFOLIO:

Total loans outstanding at June 30, 2009, including nonaccrual loans and sales contracts, were \$422,759,345 compared to \$408,270,608 at December 31, 2008, reflecting an increase of 3.6 percent that was attributable to growth in both the Federal Land Credit Association (FLCA) and Production Credit Association (PCA) subsidiaries. Nonaccrual loans as a percentage of total loans outstanding were 1.6 percent at June 30, 2009, compared to 1.0 percent at December 31, 2008.

The Association recorded \$0 in recoveries and a \$28,000 charge-off for the quarter ending June 30, 2009, resulting from a specific allowance on a large participation loan that was transferred from nonaccrual status to other property owned pending the sale of the borrowing entity and related assets. There were no recoveries or charge-offs for the same period in 2008. The Association's allowance for loan losses was 0.5 percent and 0.1 percent of total loans outstanding as of June 30, 2009, and December 31, 2008, respectively.

High-risk assets in the loan portfolio 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:

	June 30, 2009		December 31, 2008	
	Amount	%	Amount	%
Nonaccrual	\$ 6,874,659	89.4%	\$ 4,210,523	100.0%
Other property owned, net	812,914	10.6%	-	0.0%
Total	<u>\$ 7,687,573</u>	<u>100.0%</u>	<u>\$ 4,210,523</u>	<u>100.0%</u>

As of June 30, 2009, the Association's portfolio included nonaccrual loans in the amount of \$6,874,659, which represented a 63.27 percent increase from December 31, 2008. The increase was due in large part to the reclassification of two large participation loans for which it was deemed that it was probable that not all principal and interest would be collected according to the contractual terms.

In addition, during the second quarter of 2009, a participation loan in the amount of \$812,914 that had previously been classified as a nonaccrual loan was moved to other property owned. This transaction served as an asset transition loan pending the sale of the related assets on July 30, 2009.

With the exception of a small number of large participation loans, the overall quality of the portfolio remained strong through the second quarter of 2009, with loans classified under Farm Credit Administration's Uniform Loan Classification System as "acceptable" or "other assets especially mentioned" at 98.11 percent of total loans and accrued interest at June 30, 2009. Cattle prices have been fairly stable with improving pasture conditions and a reduction in feed costs through lower grain prices. However, while export sales are still weak, ongoing demand for meat protein and supply management in meat production have continued to provide support for meat prices. As the United States continues to seek expansion of export sales, markets will likely find ongoing support internationally, depending on the state of the international economy, particularly those in emerging markets, going forward.

The Spring rainfall was beneficial but has since subsided, leaving some portions of the Central Texas market serviced by the Association without enough rainfall during critical points of the growing season. Fuel and fertilizer costs, which are impacted by changes in fuel oil and natural gas prices, continue to be a major consideration in producers' planning processes. While fuel oil and natural gas prices have decreased in the previous year, market volatility could continue to put upward pressure on these prices. Cotton and grain prices have also come under pressure due to weaker export markets and USDA crop reports, and prices in the commodity markets in general have experienced a trend of decline during the overall softening in the financial markets.

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.

	June 30, 2009	December 31, 2008
Note payable to the Bank	\$ 349,797,404	\$ 333,802,614
Accrued interest on note payable	1,109,771	1,293,137
Total	\$ 350,907,175	\$ 335,095,751

The Association experienced a \$15,811,424 increase in notes and accrued interest payable to the Bank through the quarter ended June 30, 2009, due to increased loan volume experienced by the Association since December 31, 2008.

CAPITAL RESOURCES:

The Association's capital position increased by \$2,381,481 at June 30, 2009, compared to December 31, 2008. This increase is the result of net income of \$2,428,948 offset by slight decreases in capital stock and participation certificates as well as accumulated other comprehensive income. As a result of the Association's capital position, the Association's debt as a percentage of members' equity was 430:1 as of June 30, 2009, compared to 426.90:1 as of December 31, 2008.

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 17.7 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 17.1 and 17.1 percent, respectively, which is in compliance with the FCA's minimum surplus standard.

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, 2008 Annual Report of Texas Land Bank, ACA 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 fcf@farmcreditbank.com. The District makes its annual and quarterly stockholder reports available on its web site at www.farmcreditbank.com.

The Association's quarterly stockholder reports are also available free of charge, upon request 45 days after the close of the quarter. These reports can be obtained by writing to Texas Land Bank, ACA, P. O. Box 20997, Waco, Texas 76702 or calling (254) 772-6905. Copies of the Association's quarterly and annual stockholder reports can also be requested by e-mailing sharla.chambers@texaslandbank.com.

TEXAS LAND BANK, ACA

Consolidated Balance Sheet

	June 30, 2009 (unaudited)	December 31, 2008
ASSETS		
Cash	\$ 291,971	\$ 60,000
Loans	422,759,345	408,270,608
Less: allowance for loan losses	2,039,236	368,663
Net loans	420,720,109	407,901,945
Accrued interest receivable	4,390,857	3,928,186
Investment in and receivable from the Bank:		
Capital stock	6,605,955	6,605,955
Other	-	380
Other property owned, net	812,914	-
Premises and equipment	1,408,323	1,364,663
Other assets	572,852	118,987
Total assets	\$ 434,802,981	\$ 419,980,116
LIABILITIES		
Note payable to the Bank	\$ 349,797,404	\$ 333,802,614
Advance conditional payments	-	305
Accrued interest payable	1,110,600	1,293,137
Drafts outstanding	228,531	666,896
Patronage distributions payable	-	2,751,042
Other liabilities	1,570,467	1,751,624
Total liabilities	352,707,002	340,265,618
MEMBERS' EQUITY		
Capital stock and participation certificates	2,609,335	2,620,855
Allocated retained earnings	12,754,258	12,765,444
Unallocated retained earnings	66,500,977	64,072,029
Accumulated other comprehensive income (loss)	231,409	256,170
Total members' equity	82,095,979	79,714,498
Total liabilities and members' equity	\$ 434,802,981	\$ 419,980,116

TEXAS LAND BANK, ACA

Consolidated Statement of Income
(unaudited)

	Quarter Ended		Six Months Ended	
	June 30,		June 30,	
	2009	2008	2009	2008
<u>INTEREST INCOME</u>				
Loans	\$ 6,275,613	\$ 6,832,807	\$ 12,675,519	\$ 13,901,974
Total interest income	6,275,613	6,832,807	12,675,519	13,901,974
<u>INTEREST EXPENSE</u>				
Note payable to the Bank	3,318,824	3,860,094	6,672,424	7,919,868
Advance conditional payments	-	126	1	227
Total interest expense	<u>3,318,824</u>	<u>3,860,220</u>	<u>6,672,425</u>	<u>7,920,095</u>
Net interest income	2,956,789	2,972,587	6,003,094	5,981,879
<u>PROVISION FOR LOSSES</u>				
Provision (negative provision) for loan losses	<u>1,620,573</u>	<u>50,000</u>	<u>1,661,914</u>	<u>100,000</u>
Net interest income after provision for loan losses	1,336,216	2,922,587	4,341,180	5,881,879
<u>NONINTEREST INCOME</u>				
Income from the bank:				
Patronage income	63,721	71,529	130,517	149,684
Loan fees	358,423	424,544	770,684	703,784
Financially related services income	3,587	4,016	8,274	8,739
Gain (loss) on sale of premises and equipment, net	(2,097)	(4,014)	6,662	(4,014)
Other noninterest income	1,656	38,327	25,506	42,391
Total noninterest income	425,290	534,402	941,643	900,584
<u>NONINTEREST EXPENSES</u>				
Salaries and employee benefits	792,929	661,940	1,596,072	1,330,422
Directors' expense	78,786	69,935	139,036	128,302
Purchased services	125,459	120,534	221,683	230,958
Travel	27,170	35,405	46,432	70,337
Occupancy and equipment	54,047	54,278	147,105	144,740
Communications	20,649	18,224	39,267	35,511
Advertising	68,302	90,145	116,528	142,714
Public and member relations	35,138	22,216	59,447	42,621
Supervisory and exam expense	36,317	34,220	72,634	68,440
Insurance Fund premiums	160,883	147,778	320,718	292,067
Other noninterest expense	45,867	48,397	94,953	107,461
Total noninterest expenses	1,445,547	1,303,072	2,853,875	2,593,573
Income before income taxes	315,959	2,153,917	2,428,948	4,188,890
Provision for (benefit from) income taxes	-	-	-	-
Net income	\$ 315,959	\$ 2,153,917	\$ 2,428,948	\$ 4,188,890

TEXAS LAND BANK, ACA

Consolidated Statement of Changes in Members' Equity

(unaudited)

	Capital Stock/ Participation Certificates	Retained Earnings		Accumulated Other Comprehensive Income (Loss)	Total Members' Equity
		Allocated	Unallocated		
Balance at December 31, 2007	\$ 2,660,520	\$ 8,645,124	\$ 64,088,861	\$ 284,093	\$ 75,678,598
Comprehensive income					
Net income	-	-	4,188,892	-	4,188,892
Other comprehensive income					
Prior service credits (costs)	-	-	-	(25,912)	(25,912)
Actuarial gains (losses)	-	-	-	408	408
Other comprehensive income	-	-	-	(25,504)	(25,504)
Comprehensive income	-	-	4,188,892	(25,504)	4,163,388
Effects of accounting change regarding measurement date of postretirement benefits plans pursuant to FASB Statement No. 158					
Service and interest costs for October 1 - December 31, net of tax	-	-	(21,417)	-	(21,417)
Amortization of prior service credits for October 1 - December 31, net of tax	-	-	12,956	-	12,956
Additional loss, October 1 - December 31, net of tax	-	-	(204)	-	(204)
Statement No. 158	-	-	(8,665)	-	(8,665)
Capital stock/participation certificates issued	201,200	-	-	-	201,200
Capital stock/participation certificates and allocated retained earnings retired	(184,825)	-	-	-	(184,825)
Patronage refunds:					
Change in estimated patronage declared in 2006 and paid in 2007	-	(6,243)	-	-	(6,243)
Balance at June 30, 2008	<u>\$ 2,676,895</u>	<u>\$ 8,638,881</u>	<u>\$ 68,269,088</u>	<u>\$ 258,589</u>	<u>\$ 79,843,453</u>
Balance at December 31, 2008	\$ 2,620,855	\$ 12,765,444	\$ 64,072,029	\$ 256,170	\$ 79,714,498
Comprehensive income					
Net income	-	-	2,428,948	-	2,428,948
Amortization of costs included in periodic retirement benefit costs	-	-	-	(24,761)	(24,761)
Total comprehensive income	-	-	2,428,948	(24,761)	2,404,187
Capital stock/participation certificates issued	149,740	-	-	-	149,740
Capital stock/participation certificates and allocated retained earnings retired	(161,260)	-	-	-	(161,260)
Stock equalization	-	-	-	-	-
Patronage refunds:					
Change in estimated patronage declared in 2008 and paid in 2009	-	(11,186)	-	-	(11,186)
Balance at June 30, 2009	<u>\$ 2,609,335</u>	<u>\$ 12,754,258</u>	<u>\$ 66,500,977</u>	<u>\$ 231,409</u>	<u>\$ 82,095,979</u>

TEXAS LAND BANK, ACA

Notes to the Consolidated Financial Statements

(Unaudited)

NOTE 1 — ORGANIZATION AND SIGNIFICANT ACCOUNTING POLICIES:

The Texas Land Bank, ACA (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 in the counties of Bell, Bosque, Burnet, Coryell, Dallas, Ellis, Falls, Freestone, Hamilton, Hill, Lampasas, Limestone, McLennan, Milam, Navarro and Williamson 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.

Effective January 1, 2009, the Association adopted Financial Accounting Standards Board (FASB) Staff Position No. 157-2, "Effective Date of FASB Statement No. 157" (FSP 157-2). This FSP delayed the effective date of Statement of Financial Accounting Standard (SFAS) No. 157, "Fair Value Measurements" (SFAS 157) for nonfinancial assets and nonfinancial liabilities. The impact of adoption resulted in additional fair value disclosures but did not have an impact on our financial condition or results of operations.

In April 2009, the FASB issued FSP No. 157-4, "Determining Fair Value When the Volume and Level of Activity for the Asset or Liability Have Significantly Decreased and Identifying Transactions That Are Not Orderly" (FSP 157-4). FSP 157-4 emphasizes that even if there has been a significant decrease in the volume and level of activity for the asset or liability and regardless of the valuation technique and inputs used, the objective for fair value measurement is unchanged from what it would be if markets were operating at normal activity levels or transactions were orderly; that is, to determine the current exit price. It sets forth additional factors that should be considered to determine whether there has been a significant decrease in volume and level of activity when compared with normal market activity. The reporting entity shall evaluate the significance and relevance of the factors to determine whether, based on the weight of evidence, there has been a significant decrease in activity and volume. FSP 157-4 indicates that if an entity determines that either the volume or level of activity for an asset or liability has significantly decreased (from normal conditions for that asset or liability) or price quotations or observable inputs are not associated with orderly transactions, increased analysis and management judgment will be required to estimate fair value. It is further noted that a fair value measurement should include a risk adjustment to reflect the amount market participants would demand because of the risk (uncertainty) in the cash flows.

FSP 157-4 also requires a reporting entity to make additional disclosures in interim and annual periods. It is effective for interim periods ending after June 15, 2009, with early application permitted for periods ending after March 15, 2009. Revisions resulting from a change in valuation techniques or their application are accounted for as a change in accounting estimate. The Association adopted the FSP in second quarter 2009. The adoption did not have a material impact on the financial condition or results of operations of the Association.

In April 2009, the FASB issued FSP No. 115-2, "Recognition and Presentation of Other-Than-Temporary Impairments" (FSP 115-2), which amends the other-than-temporary impairment guidance for debt securities to make the guidance more operational and to improve the presentation and disclosure of other-than-temporary impairments on debt securities in the financial statements. It does not change existing recognition and measurement guidance related to other-than-temporary impairments of equity securities.

FSP 115-2 changes existing impairment guidance under FASB Statement No. 115, Accounting for Certain Investments in Debt and Equity Securities (FSP 115) by eliminating the "ability and intent to hold" provision. In addition, impairment is now considered to be other than temporary if an entity (i) intends to sell the security, (ii) more likely than not will be required to sell the security before recovering its cost, or (iii) does not expect to recover the security's entire amortized cost basis (even if the entity does not intend to sell). The "probability" standard relating to the collectability of cash flows is also eliminated, and impairment is now considered to be other-than-temporary if the present value of cash flows expected to be collected from the debt security is less than the amortized cost basis of the security (any such shortfall is referred to in FSP 115-2 as a "credit loss"). If an entity intends to sell an impaired debt security or more likely than not will be required to sell the security before recovery of its amortized cost basis less any current-period credit loss, the impairment is other-than-temporary and should be recognized currently in earnings in an amount equal to the entire difference between fair value and amortized cost. If a credit loss exists, but an entity does not intend to sell the impaired debt security and is not more likely than not to be required to sell before recovery, the impairment is other-than-temporary and should be separated into (i) the estimated amount relating to credit loss, and (ii) the amount relating to all other factors. Only the estimated credit loss amount is recognized currently in earnings, with the remainder of the loss amount recognized in other comprehensive income. For held-to-maturity securities, the portion of the other-than-temporary impairment not related to a credit loss will be recognized in a new category of other comprehensive income and amortized over the remaining life of the debt security as an

increase in the security's carrying amount. Disclosure requirements for impaired debt and equity securities are expanded and will now be required quarterly, as well as annually.

FSP 115-2 is effective for interim and annual periods ending after June 15, 2009, with early application permitted for periods ending after March 15, 2009. For securities held at the beginning of the interim period of adoption for which an other-than-temporary impairment was previously recognized, if an entity does not intend to sell and it is more likely than not that it will be required to sell before recovery of its amortized cost basis, the entity shall recognize the cumulative effect of initially applying this FSP adjustment to the opening balance of retained earnings with a corresponding adjustment to accumulated other comprehensive income. The Association held no investments in debt securities during the first six months of 2009. The Association adopted the FSP in the second quarter of 2009 and did not recognize an adjustment to beginning retained earnings or accumulated other comprehensive income since no impairment losses were previously recognized.

In May 2009, the FASB issued SFAS No. 165, "Subsequent Events" (SFAS 165), which sets forth general standards of accounting for and disclosure of events that occur after the balance sheet date but before financial statements are issued or are available to be issued. Recognized subsequent events should be recognized in the financial statements since the conditions existed at the date of the balance sheet. Nonrecognized subsequent events are not recognized in the financial statements since the conditions arose after the balance sheet date but before the financial statements are issued or are available to be issued. This Standard, which includes a required disclosure of the date through which an entity has evaluated subsequent events, is effective for interim or annual periods ending after June 15, 2009.

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 and the six months 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:

Impaired loans are loans for which it is probable that not all principal and interest will be collected according to the contractual terms. The following table presents information concerning impaired loans:

	June 30, 2009	June 30, 2008
Impaired loans with related allowance	\$ 3,934,829	\$ -
Impaired loans with no related allowance	2,939,830	272,407
Total impaired loans	\$ 6,874,659	\$ 272,407
Allowance on impaired loans	\$ 1,600,573	\$ -
Average impaired loans	\$ 4,235,637	\$ 278,070
Interest income on impaired loans for the quarter	\$ 103	\$ 371

The Association portfolio included \$6,874,659 in loans classified as impaired as of June 30, 2009. This represented an increase of \$6,602,252 from the same period in 2008. All of the loans classified as impaired at June 30, 2009, were also classified as nonaccrual, with 100 percent current as to principal and interest. Total nonaccrual loan volume was primarily driven by four participation loans. Using data provided to the Association it was determined that while there was enough concern regarding the viability of one of the borrowers going forward to prevent the loan from being upgraded to nonaccrual cash basis, the loan continued to be well secured and did not warrant a specific allowance as of June 30, 2009. Based on guidance from FCA in the second quarter of 2009, the Association recorded specific allowances in the amounts of \$656,683 and \$885,890 in relation to two impaired participation loans in the same industry due to their undercollateralized position and potential for loss in the event the assets should be acquired and sold in addition to economic conditions that recently negatively impacted the related industry. The fourth and

smallest loan was deemed to be undercollateralized, and a specific loan loss allowance in the amount of \$86,000 was previously recorded for it as of December 31, 2008.

The allowance for loan losses is maintained based on estimates that consider the general financial strength of both the overall general and agricultural economies, loan portfolio composition, credit administration and the portfolio's prior loan loss experience. Using these factors, the Association maintains an allowance for loan loss level that is considered adequate by management to provide for estimated losses inherent in the loan portfolio. An analysis of the allowance for loan losses follows:

	June 30, 2009	June 30, 2008
Balance at beginning of quarter	\$ 446,663	\$ 132,663
Provision for loan losses	1,620,573	50,000
Charge-offs	(28,000)	-
Recoveries	-	-
Balance at end of quarter	<u>\$ 2,039,236</u>	<u>\$ 182,663</u>

The allowance for loan losses was \$1,856,573 higher for the quarter ended June 30, 2009, as compared to the same period in 2008. In addition to a \$200,000 increase in the general allowance since June 30, 2008, this increase was also attributable to an increase in the specific allowance for loan loss provision that was warranted by two large participation loans in which it was deemed that there was a weak collateral position and negative economic conditions impacting the related industry as of June 30, 2009.

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 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.

NOTE 4 — INCOME TAXES:

Texas Land Bank, ACA 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. During 2008, the Association participated in a patronage program and intends to do so again in 2009. 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 (over 50 percent probability), based on management's estimate, that they will not be realized. The Association has recorded a full valuation allowance against its deferred tax asset as of June 30, 2009, based on management's estimate that it is more likely than not that the deferred tax asset will not be realized. For the six months ended June 30, 2009, net income for tax purposes did not warrant the recognition of tax expense due to the patronage program implemented.

The subsidiary, Texas Land Bank, FLCA, is exempt from federal and other income taxes as provided in the Farm Credit Act of 1971.

Upon adoption of FIN 48 on January 1, 2007, the Association did not recognize a tax liability for any unrecognized tax benefits.

NOTE 5 — FAIR VALUE MEASUREMENTS:

SFAS No. 157 defines fair value as the exchange price that would be received for an asset or paid to transfer a liability in the principal or most advantageous market for the asset or liability. See Note 11 to the 2008 Annual Report to Stockholders for a more complete description.

Assets and liabilities measured at fair value on a non-recurring basis at June 30, 2009 for each of the fair value hierarchy values are summarized below:

	Fair Value Measurement Using			Total Fair Value	Total Gains (losses)
	Level 1	Level 2	Level 3		
Assets:					
Loans	\$ -	\$ -	\$ 2,306,256	\$ 2,306,256	\$ -
Other property owned	-	-	812,914	812,914	-

* Represents the fair value of certain loans that were evaluated for impairment under SFAS No. 114, "Accounting by Creditors for Impairment of a Loan," (SFAS 114). 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 11 to the 2008 Annual Report to Stockholders, SFAS No. 157 establishes a fair value hierarchy, which requires an entity to maximize the use of observable inputs and minimize the use of unobservable inputs when measuring fair value. The following represent a brief summary of the valuation techniques used for the Bank and its related associations' assets and liabilities. For a more complete description, see Notes to the 2008 Annual Report.

Loans

For certain loans evaluated for impairment under SFAS No. 114, 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 less estimated costs to sell.

NOTE 7 — EMPLOYEE BENEFIT PLANS:

The following table summarizes the components of net periodic benefit costs for the six months ended June 30, 2009:

	Other Benefits	
	2009	2008
Service cost	\$ 14,242	\$ 12,732
Interest cost	30,468	30,102
Amortization of prior service costs	(25,586)	(25,912)
Amortizations of net (gain) loss	826	408
Net periodic benefit cost	\$ 19,950	\$ 17,330

The Association previously disclosed in its financial statements for the year ended December 31, 2008, that it expected to contribute \$864,643 to its defined pension plan in 2009. The Association has now funded the full amount for 2009, and it does not anticipate contributing any additional amounts in 2009. The amount will be recognized as an expense for the Association on a pro rata basis throughout the year.

NOTE 8 — SUBSEQUENT EVENTS:

The Association has evaluated subsequent events through August 7, 2009, which is the date the financial statements were issued. On July 30, 2009, the participation loan included in other property owned at a value of \$812,914 was sold in a seller-financed transaction for \$843,993 and was moved back into nonaccrual status. The effects of this subsequent transaction have no impact on the second quarter 2009 financial statements and are expected to have minimal impact on future financial statements. As of August 7, 2009, there are no other significant subsequent events requiring disclosure in the second quarter 2009 quarterly stockholder report.