



FARM CREDIT
of Central Florida

2006 ANNUAL REPORT



FARM CREDIT OF CENTRAL FLORIDA, ACA

2006 ANNUAL REPORT

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Management

Richard W. Joyner	President
Robert W. Teston	Executive Vice President
Gregory D. Ellis	Senior Vice President & Treasurer
Reginald T. Holt.....	Senior Vice President
Wayne R. Montgomery.....	Senior Vice President

Board of Directors

Al Bellotto	Chairman
David J. Stanford.....	Vice Chairman
W. T. Bice, Sr.	Director
C. Dennis Carlton, Sr.	Director
W. Rex Clonts, Jr.	Director
Homer E. Hunnicutt, Jr.	Director
John S. Langford.....	Director
Robert R. Roberson.....	Director
Lewis S. Stidham	Director
Ronald R. Wetherington	Director

Message from the President & Chief Executive Officer

On behalf of the Farm Credit of Central Florida Board and staff, I am pleased to present our 2006 Annual Report.

Farm Credit of Central Florida, ACA is a member-owned cooperative. We provide credit and credit-related services to eligible borrowers/stockholders for qualified purposes in the counties of Brevard, Citrus, Hernando, Hillsborough, Lake, Orange, Osceola, Pasco, Pinellas, Polk, Seminole, Sumter, and Volusia in the State of Florida.

The Association is an institution of the Farm Credit System, which was created by Congress in 1916. We are pleased to have celebrated 90 years of service to American Agriculture and Rural America. We are dedicated to the Congressional Charge of improving the income and well-being of American farmers, ranchers, and producers or harvesters of aquatic products and farm-related businesses.

The central Florida region is very diverse and continually changing. Our mission is: **“To be the lender of choice to the agricultural marketplace and rural communities in our service area.”** To be successful, we must:

- Be consistently available and competitive in all customer segments within the marketplace.
- Balance credit risk, operational risk and growth to insure safety and soundness while providing acceptable returns to members/stockholders.
- Provide loan products and other services that are competitive across a broad spectrum of markets served.

In order to continue to be successful in meeting our mission the Association board and management established the following key business objectives for 2006.

- Assure the continued viability of the Association
- Protect and enhance member equity and returns
- Provide superior service to all market segments
- Maintain a professional and high-performing staff and work environment
- Manage operational risk and controllable costs

Our report card for 2006 will show that we have obtained high marks in meeting these objectives. As a very highly regulated institution, we are proud of our record and results from the many facets of “overseers” that are watching out for your interest. While we believe some of the increased oversight we have experienced in the last few years by statute, regulation, and/or policy have been costly to our stockholders; it should provide you with a very high comfort level of the quality and content of our reports to you. I commit to you that we will always strive to provide you and the Board of Directors with the most accurate and current information available.

I hope you will take time to review the financial performance of the association by reading the following reports and financial statements. Our growth continues to be strong, accompanied by record high credit quality and strong earnings.

Because of the federated cooperative relationship we enjoy with the AgFirst Farm Credit Bank and the system, we are able to manage our Capital in a manner that allows us to meet the needs of our larger borrowers and provide a reliable and stable source of capital to all of our market segments. We are very grateful for the commitment and performance of AgFirst in providing funding and services that allow us to operate in an efficient and competitive manner. These attributes in turn allow us to provide our members market competitive rates. We are then able to continue our tradition of returning our profits to our members and significantly reducing their cost of borrowing. As I like to say: **“Enjoying the Cooperative Advantage”**.

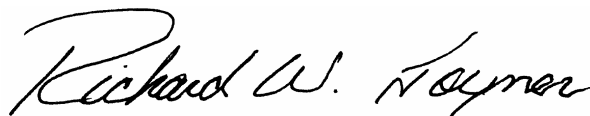
We enter 2007 with optimism. The implementation of the “Customer Relationship Management” and “Imaging” programs we planned for 2006 have been delayed until 2007. We believe these processes will improve efficiency and convenience in providing you the customer support you need and deserve. As the demographics of agriculture and our Central Florida area change, we are committed to being prepared to meet its needs. While we remain committed to our core business of production agriculture and Agribusiness, we are also expanding our commitment to rural communities, young beginning and small farmers, and those that enjoy a rural lifestyle or country home.

To expand our service to our traditional agricultural markets we implemented a crop insurance sales program during 2006. The program was very successful and we look forward to expanding the service in 2007. We hope you will call us when considering your crop insurance needs. In addition to our traditional markets to the agricultural commodities of Florida, we are also pleased to offer products to those who enjoy living in the rural communities of Florida with home loans, lot loans, and Lifestyle loans. Help us spread the word; we are not only for farmers. If you are looking for financing on recreational tracks (hunting, fishing, etc.), give us a call.

Our services to agribusiness also go beyond traditional real estate, equipment, or crop loans. We specialize in “letters of credit”, facility, and capital improvement loans.

As always, agriculture faces the perils of weather, disease, and other forces of Mother Nature. In addition there are the ever present challenges of regulation and competition for resources (land, water, labor, etc.) Nobody said it would be easy, but with the dedication of American farmers, ranchers, and growers, we are committed to being a dependable financial partner to agriculture and rural America.

We appreciate your business and look forward to meeting your financial needs in 2007 and beyond. Tell your friends and neighbors about the advantages of your cooperative.



Richard W. Joyner
President & Chief Executive Officer

February 28, 2007

Report of Management

The accompanying consolidated financial statements and related financial information appearing throughout this annual report have been prepared by management of Farm Credit of Central Florida, ACA (Association) in accordance with generally accepted accounting principles appropriate in the circumstances. Amounts which must be based on estimates represent the best estimates and judgments of management. Management is responsible for the integrity, objectivity, consistency, and fair presentation of the consolidated financial statements and financial information contained in this report.

Management maintains and depends upon an internal accounting control system designed to provide reasonable assurance that transactions are properly authorized and recorded, that the financial records are reliable as the basis for the preparation of all financial statements, and that the assets of the Association are safeguarded. The design and implementation of all systems of internal control are based on judgments required to evaluate the costs of controls in relation to the expected benefits and to determine the appropriate balance between these costs and benefits. The Association maintains an internal audit program to monitor compliance with the systems of internal accounting control. Audits of the accounting records, accounting systems and internal controls are performed and internal audit reports, including appropriate recommendations for improvement, are submitted to the Board of Directors.

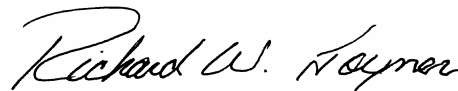
The consolidated financial statements have been examined by independent public auditors, whose report appears elsewhere in this annual report. The Association is also subject to examination by the Farm Credit Administration.

The consolidated financial statements, in the opinion of management, fairly present the financial condition of the Association. The undersigned certify that the 2006 Annual Report 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 our knowledge and belief.

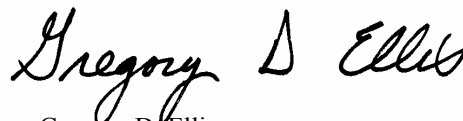
The accompanying consolidated financial statements were prepared under the oversight of the Audit Committee of the Board of Directors.



Al Bellotto
Chairman of the Board



Richard W. Joyner
Chief Executive Officer



Gregory D. Ellis
Chief Financial Officer

February 28, 2007

Consolidated Five - Year Summary of Selected Financial Data

(UNAUDITED)

<i>(dollars in thousands)</i>	2006	2005	December 31, 2004	2003	2002
Balance Sheet Data					
Cash	\$ 63	\$ 799	\$ 203	\$ 84	\$ 476
Investment securities, held to maturity	38,704	34,682	—	—	—
Loans	349,172	400,399	348,753	329,792	318,796
Less: allowance for loan losses	1,639	2,133	1,954	10,642	11,007
Net loans	347,533	398,266	346,799	319,150	307,789
Investment in other Farm Credit institutions	15,822	4,034	3,951	4,106	5,159
Other property owned	—	—	—	—	2,500
Other assets	14,322	13,494	11,273	6,037	6,063
Total assets	\$ 416,444	\$ 451,275	\$ 362,226	\$ 329,377	\$ 321,987
Notes payable to AgFirst Farm Credit Bank*	\$ 334,575	\$ 374,294	\$ 288,746	\$ 266,932	\$ 258,486
Accrued interest payable and other liabilities with maturities of less than one year	12,769	10,524	9,143	9,711	10,785
Total liabilities	347,344	384,818	297,889	276,643	269,271
Protected borrower stock	97	146	275	399	551
Capital stock and participation certificates	1,209	1,169	1,229	1,190	1,195
Retained earnings					
Allocated	28,995	27,008	26,153	27,842	27,365
Unallocated	38,799	38,134	36,680	26,228	26,801
Accumulated other comprehensive income (loss)	—	—	—	(2,925)	(3,196)
Total members' equity	69,100	66,457	64,337	52,734	52,716
Total liabilities and members' equity	\$ 416,444	\$ 451,275	\$ 362,226	\$ 329,377	\$ 321,987
Statement of Income Data					
Net interest income	\$ 11,871	\$ 10,614	\$ 8,797	\$ 8,245	\$ 8,358
Provision for (reversal of allowance for) loan losses	(612)	68	(8,815)	(550)	—
Noninterest income (expense), net	(1,019)	(829)	(1,551)	(2,026)	(2,369)
Net income	\$ 11,464	\$ 9,717	\$ 16,061	\$ 6,769	\$ 5,989
Key Financial Ratios					
Rate of return on average:					
Total assets	2.63%	2.56%	4.96%	2.13%	1.87%
Total members' equity	16.71%	14.73%	30.06%	12.61%	10.25%
Net interest income as a percentage of					
average earning assets	2.84%	2.89%	2.71%	2.60%	2.66%
Net chargeoffs (recoveries) to average loans	(0.03)%	(0.03)%	(0.04)%	(0.06)%	0.01%
Total members' equity to total assets	16.59%	14.73%	17.76%	16.01%	16.37%
Debt to members' equity (:1)	5.03	5.79	4.63	5.25	5.11
Allowance for loan losses to loans	0.47%	0.53%	0.56%	3.23%	3.45%
Permanent capital ratio	16.55%	15.36%	15.40%	15.76%	16.21%
Total surplus ratio	15.88%	15.06%	15.15%	15.73%	16.13%
Core surplus ratio	13.46%	12.70%	12.13%	12.85%	13.20%
Net Income Distribution					
Cash dividends declared/paid	\$ —	\$ —	\$ 1,000	\$ —	\$ —
Estimated patronage refunds:					
Cash	\$ 3,554	\$ 2,808	\$ 1,727	\$ 2,523	\$ 2,989
Qualified allocated retained earnings	59	—	3,208	4,685	4,483
Nonqualified allocated retained earnings	6,541	4,658	—	—	—
Nonqualified retained earnings	—	558	—	—	—

* General financing agreement is renewable on three-year cycles. The next renewal date is December 31, 2007.

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

(dollars in thousands, except as noted)

GENERAL OVERVIEW

The following commentary summarizes the financial condition and results of operations of Farm Credit of Central Florida, ACA, (Association) for the year ended December 31, 2006 with comparisons to the years ended December 31, 2005 and December 31, 2004. This information should be read in conjunction with the Consolidated Financial Statements, Notes to the Consolidated Financial Statements and other sections in this Annual Report. The accompanying consolidated financial statements were prepared under the oversight of the Audit Committee of the Board of Directors. For a list of the Audit Committee members, refer to the "Report of the Audit Committee" reflected in this Annual Report. Information in any part of this Annual Report may be incorporated by reference in answer or partial answer to any other item of the Annual Report.

The Association is an institution of the Farm Credit System (System), which was created by Congress in 1916 and has served agricultural producers for almost 90 years. The System's mission is to maintain and improve the income and well-being of American farmers, ranchers, and producers or harvesters of aquatic products and farm-related businesses. The System is the largest agricultural lending organization in the United States. The System is regulated by the Farm Credit Administration, (FCA), which is an independent safety and soundness regulator.

The Association is a cooperative, which is owned by the members (also referred to throughout this Annual Report as stockholders or shareholders) served. The territory of the Association extends across a diverse agricultural region of Central Florida. Refer to Note 1, "Organization and Operations," of the Notes to the Consolidated Financial Statements for counties in the Association's territory. The Association provides credit to farmers, ranchers, rural residents, and agribusinesses. Our success begins with our extensive agricultural experience and knowledge of the market.

The Association obtains funding from AgFirst Farm Credit Bank (AgFirst or Bank). The Association is materially affected and shareholder investment in the Association could be affected by the financial condition and results of operations of the Bank. Copies of the Bank's Annual and Quarterly Reports are on the AgFirst website, www.agfirst.com, or may be obtained at no charge by calling 1-800-845-1745, extension 316, or writing Wanda Martin, AgFirst Farm Credit Bank, P. O. Box 1499, Columbia, SC 29202.

Copies of the Association's Annual and Quarterly reports are also on the Association's website, www.FarmCreditCFL.com, or may be obtained upon request free of charge by calling 1-800-533-2773 or writing Greg Ellis, Chief Financial Officer, Farm Credit of Central Florida, ACA, Post Office Box 8009, Lakeland, FL 33802-8009. The Association prepares a quarterly report within 45 days after the end of each fiscal quarter, except that no report needs to be prepared for the fiscal quarter that coincides with the end of the fiscal year of the Association.

CRITICAL ACCOUNTING POLICIES

The financial statements are reported in conformity with accounting principles generally accepted in the United States of America. Our significant accounting policies are critical to the understanding of our results of operations and financial position because some accounting policies require us to make complex or subjective judgments and estimates that may affect the value of certain assets or liabilities. We consider these policies critical because management must make judgments about matters that are inherently uncertain. For a complete discussion of significant accounting policies, see Note 2, "Summary of Significant Accounting Policies," of the Notes to the Consolidated Financial Statements. The following is a summary of certain critical policies.

- *Allowance for loan losses* — The allowance for loan losses is management's best estimate of the amount of probable losses existing in and inherent in our loan portfolio. The allowance for loan losses is increased through provisions for loan losses and loan recoveries and is decreased through allowance reversals and loan charge-offs. The allowance for loan losses is determined based on a periodic evaluation of the loan portfolio, which generally considers relevant historical charge-off experience adjusted for relevant factors. These factors include types of loans, credit quality, specific industry conditions, general economic and political conditions, and changes in the character, composition, and performance of the portfolio, among other factors.

Significant individual loans are evaluated based on the borrower's overall financial condition, resources, and payment record, the prospects for support from any financially responsible guarantor, and, if appropriate, the estimated net realizable value of any collateral. The allowance for loan losses attributable to these loans is established by a process that estimates the probable loss inherent in the loans, taking into account various historical and projected factors, internal risk ratings, regulatory oversight, and geographic, industry and other factors.

Changes in the factors considered by management in the evaluation of losses in the loan portfolios could result in a change in the allowance for loan losses and could have a direct impact on the provision for loan losses and the results of operations.

- *Valuation methodologies* — Management applies various valuation methodologies to assets and liabilities that often involve a significant degree of judgment, particularly when liquid markets do not exist for the particular items being valued. Quoted market prices are referred to when estimating fair values for certain assets for which an observable liquid market exists, such as most investment securities. Management utilizes significant estimates and assumptions to value items for which an observable liquid market does not exist. Examples of these items include impaired loans, pension and other postretirement benefit obligations, and certain other financial instruments. These valuations require the use of various assumptions, including, among others, discount rates, rates of return on assets, repayment rates, cash flows, default rates, costs of servicing and liquidation values. The use of different assumptions could produce significantly different results, which could have material positive or negative effects on the Association's results of operations. For additional information, refer to the Recently Issued Accounting Pronouncements disclosed in this Annual Report.
- *Pensions* — The Bank and its related Associations participate in defined benefit retirement plans. These plans are noncontributory and benefits are based on salary and years of service. In addition, the Bank and its related Associations also participate in defined contribution retirement savings plans. Pension expense for all plans is recorded as part of salaries and employee benefits. Pension expense is determined by actuarial valuations based on certain assumptions, including expected long-term rate of return on plan assets and discount rate. The expected return on plan assets for the year is calculated based on the composition of assets at the beginning of the year and the expected long-term rate of return on that portfolio of assets. The discount rate is used to determine the present value of our future benefit obligations. We selected the discount rate by reference to Moody's Investors Service Aa long-term corporate bond index, actuarial analyses and industry norms. For additional information, refer to the Recently Issued Accounting Pronouncements disclosed in this Annual Report.

REGIONAL ECONOMICS

The non-farm economy in the region served by the Association continues to outperform the national economy despite some slowdown in the last two quarters of 2006. Throughout 2005 and 2006, the Florida economy continued to grow but began to cool in the area of land development and housing starts near the end of 2006. Both the state and regional economic activity has been driven by real estate, new home construction, tourism, expansion in government services, growth in business services and healthcare. The regional pattern of state growth has southern metro areas most active with Tampa, Orlando and Jacksonville growth rates close behind. Construction activity

moderated on the housing side but commercial building activity has continued at a steady pace. Consumer credit quality is better than average, income growth is strong, and demographic trends remain very favorable. Cargo volumes continue to grow rapidly at state ports driven by stronger imports of both agricultural and non-farm goods, particularly gasoline.

In the housing area, single family permits declined in 2006 from 209 thousand in 2005 to 193 thousand. Single family permits are projected to again decline in 2007 to 171 thousand as builders attempt to work off inventory of new homes. The House Price index rose another 19% in 2006 to 485 with 1980 representing the base year of 100. Actual population net migration reached 297.2 thousand in 2006 and is expected to decline slightly to 260 thousand in 2007. The value of land for future development continued to rise in the period. While there is no indication of land price declines, contract and sales activity on idle land has slowed. Skyrocketing insurance premiums and real estate taxes impact the cost of living, particularly to new residents. These issues will add an economic hurdle to the state's economy over the next several years.

Despite soaring gasoline and jet fuel prices, which push up travel costs, Florida's tourism industry continues to report strong growth. Hotel occupancy rates remain high and appear to be very stable at current high levels. Major attractions in the Orlando area continue to report record attendance numbers.

Agriculture, agribusiness, and food processing and manufacturing are still a significant economic driver to the local and state economy. These business segments provided significant jobs and revenues to the state and local economies.

The agricultural industry in the Central Florida region produces a wide variety of farm commodities with horticulture, citrus, and fruit and vegetables the largest market segments. None of the commodities produced in the region are included in any USDA government support programs and are not materially impacted by U.S. farm bill legislation. While the overall agricultural economy in the region has been good, there are several significant factors that continue to affect the area. These factors include the introduction of pest and plant diseases, weather-related risks, water-use regulations, environmental rules and regulations, and competition for agricultural lands. All Florida producers, particularly fruit and vegetable producers, are concerned about foreign trade issues, primarily the Free Trade of the America's Agreement (FTAA) and World Trade Organization initiatives. State agencies continue to pursue the purchase of significant parcels of agricultural property for water resource protection and environmental protection purposes. Florida rural property owners are now facing new challenges as special interest groups and government officials attempt to limit their future land use through growth management regulations.

The region served by the Association was spared any natural disaster in both 2005 and 2006. There were no impacts by hurricanes and the region has enjoyed generally favorable weather conditions. The region continues to experience significantly below average rainfall and water authorities are beginning to tighten restrictions.

A significantly reduced orange crop estimate has boosted citrus prices to record levels which should enhance grower returns. Despite improved profits, citrus growers face an uncertain future as reports of canker infestation and citrus greening disease continue to increase. Canker and greening control practices add to costs. Strawberry growers experienced good growing conditions in the 2005-06 season and expect better than average results in the 2006-07 season. Cow-calf operators have enjoyed good prices and returns over the past two years. Growing cow inventories and decreased per capita consumption is beginning to weaken beef pricing. Floriculture (nursery) growers reported good financial results in 2005 and 2006 and expect demand for their products to continue to be favorable in 2007. Association management continually reviews its loan portfolio and has continued to report very satisfactory credit quality and loan repayment performance throughout 2006. At year end 2006, loans rated acceptable were greater than 98% and the rolling 12 month average delinquency rate at 0.18%.

There has been little change in the Association's market region over the past year. The Association's Agribusiness Lending Group continues to serve and target large high-quality farm and agribusiness customers. The group continues to report good growth in 2005 and 2006. The Consumer and Small Business Lending Group has maintained a consistent market presence in consumer and middle market lending and is also reporting growth. The Association continues to increase its marketing efforts and activity in the life-style farm and rural residential market segments. The Association also continues to serve young, beginning and small farm customers in this lending group. Positive results have been achieved over the last two years to streamline the credit delivery processes on small agricultural loans. These efforts are intended to improve customer response times and reduce costs associated with serving the consumer and small farm market segment.

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 through numerous product types.

The gross loan volume of the Association as of December 31, 2006, was \$349,172, a decrease of \$51,277 or 12.79 percent as compared to \$400,399 at December 31, 2005 and an increase of \$419 or 0.12 percent as compared to \$348,753 at December 31, 2004. Net loans outstanding (gross loans net of the allowance for loan losses) on December 31, 2006, were \$347,533 as compared to \$398,266 at December 31, 2005 and \$346,799 at December 31, 2004. Net loans accounted for 83.45 percent of total assets on December 31, 2006 as compared to 88.25 percent of total assets at December 31, 2005 and 95.74 percent of total assets at December 31, 2004.

The diversification of the Association loan volume by type for each of the past three years is shown below. See Note 4, "Loans and Allowance for Loan Losses," of the Notes to the Consolidated Financial Statements for the loans outstanding amounts.

Loan Type	12/31/06	12/31/05	12/31/04
Real estate mortgage	54.28%	61.35%	60.37%
Production and intermediate term	29.59	26.20	29.94
Agribusiness:			
Loans to cooperatives	.54	.63	—
Processing and marketing	5.79	3.97	1.91
Farm related business	.86	1.10	1.20
Communication	.28	.25	.29
Energy	1.10	1.03	1.23
Rural residential real estate	7.56	5.46	5.06
Total	100.00%	100.00%	100.00%

The following table presents the contractual maturity distribution of loans at December 31, 2006:

Loan Type	Due after			Total
	Due in 1 year or less	1 year through 5 years	Due after 5 years	
	<i>(dollars in thousands)</i>			
Real estate mortgage	\$ 10,318	\$ 54,966	\$ 124,310	\$ 189,594
Production and intermediate term	46,722	46,393	10,192	103,307
Agribusiness:				
Loans to cooperatives	1,879	—	—	1,879
Processing and marketing	18,764	—	1,436	20,200
Farm-related business	575	1,395	1,028	2,998
Communication	971	4	—	975
Energy	3,827	—	—	3,827
Rural residential real estate	893	11,343	14,156	26,392
Total	\$ 83,949	\$ 114,101	\$ 151,122	\$ 349,172

While we make loans and provide financially related services to qualified borrowers in the agricultural and rural sectors and to certain related entities, our loan portfolio is diversified. The following tables reflect the commodities financed and the geographic locations served.

The geographic distribution of the loans by service center, all within the State of Florida, for the past three years is as follows:

Service Center	12/31/06	12/31/05	12/31/04
Apopka	12.17%	14.66%	13.54%
Plant City	6.73	8.37	8.13
Brooksville	5.81	5.72	5.90
Lake Wales	5.22	4.64	5.44
Lakeland	3.92	4.15	5.95
Agribusiness Lending Group	64.84	62.03	60.52
Residential Lending Group	.07	.12	.16
Special Assets	1.24	.31	.36
Total	100.00%	100.00%	100.00%

Commodity and industry categories are based upon the Standard Industrial Classification system published by the federal government. The system is used to assign commodity or industry categories based upon the largest agricultural commodity of the customer.

The major commodities in the Association loan portfolio are shown below. The predominant commodities are horticulture (predominately nurseries), fruits & vegetables, livestock, and citrus which constitute almost 80 percent of the entire portfolio.

Commodity Group	Percent of Portfolio		
	2006	2005	2004
Horticulture	31.73%	22.87%	23.84%
Fruits & Vegetables	19.50	24.55	24.73
Livestock	14.79	15.08	15.95
Citrus	13.48	22.26	20.67
Rural Housing	5.83	3.38	3.31
Dairy	.87	1.46	2.15
Other	13.80	10.40	9.35
Total	100.00%	100.00%	100.00%

Repayment ability is closely related to the commodities produced by our borrowers, and increasingly, the off-farm income of borrowers. The Association's loan portfolio contains a concentration of fruit & vegetable producers, nursery operations, and citrus growers. Although a large percentage of the loan portfolio is concentrated in these enterprises, many of these operations are diversified within their enterprise and/or with crop production that reduces overall risk exposure. Even though the concentration of large loans has increased over the past several years, the agricultural enterprise mix of these loans is diversified and similar to that of the overall portfolio. The risk in the portfolio associated with commodity concentration and large loans is reduced by the range of diversity of enterprises in the Association's territory.

The decrease in gross loan volume for the twelve months ended December 31, 2006, is primarily attributed to increased loan participations sold to the Bank. The Association has been fortunate to regain several large, former accounts and has attracted some large real estate loans in addition to normal business. Also, there is increased interest in intermediate-term loans for equipment purchases.

Recently, the Association has experienced a shift in loan assets. The percentage of long-term loans in the portfolio has been upward while the percentage of short and intermediate-term loans is downward. The short-term portfolio, which is cyclical in nature and heavily influenced by operating-type loans, normally reaches a minimum balance in August or September and rapidly increases in the fall months as strawberry and other winter vegetable growers increase their borrowings to prepare for the next crop production season. The Association has grown the long-term portfolio through increased mortgage lending on real estate and facilities used for agricultural production.

During 2006, the Association increased activity in the buying and selling of loan participations within and outside of the System. This provides a means for the Association to spread credit concentration risk and realize non-patronage sourced interest and fee income, which may strengthen their capital position.

Loan Participations	2006	2005	2004
	<i>(dollars in thousands)</i>		
Participations Purchased			
– FCS Institutions	\$ 34,929	\$ 24,090	\$ 24,302
Participations Sold	(239,249)	(113,406)	(77,078)
Total	<u>\$ (204,320)</u>	<u>\$ (89,316)</u>	<u>\$ (52,776)</u>

The Association sells qualified long-term mortgage loans into the secondary market. For the period ended December 31, 2006, the Association originated loans for resale totaling \$1,290, which were sold into the secondary market.

INVESTMENT SECURITIES

At December 31, 2006, the Association had investments in loan pools of Small Business Administration (SBA) guaranteed loans. These investments carry the full faith and credit of the United States government. At December 31, 2006, the balance in these investments amounted to \$38,704. It is the Association's objective that liquid, high-quality investments shall be utilized as an asset liability management strategy to manage and diversify its income sources.

RISK EXPOSURE

Credit risk arises from the potential inability of an obligor to meet its repayment obligation. As part of the process to evaluate the success of a loan, the Association continues to review the credit quality of the loan portfolio on an ongoing basis. With the approval of the Association Board of Directors, the Association establishes underwriting standards and lending policies that provide direction to loan officers. Underwriting standards include, among other things, an evaluation of:

- *Character* – borrower integrity and credit history
- *Capacity* – repayment capacity of the borrower based on cash flows from operations or other sources of income
- *Collateral* – protection for the lender in the event of default and a potential secondary source of repayment
- *Capital* – ability of the operation to survive unanticipated risks
- *Conditions* – intended use of the loan funds

The credit risk management process begins with an analysis of the borrower's credit history, repayment capacity, and financial position. Repayment capacity focuses on the borrower's ability to repay the loan based upon cash flows from operations or other sources of income, including non-farm income. Real estate loans must be collateralized by first liens on the real estate (collateral). As required by FCA regulations, each institution that makes loans on a collateralized basis must have collateral evaluation policies and procedures. Real estate mortgage loans may be made only in amounts up to 85 percent of the original appraised value of the property taken as collateral or up to 97 percent of the appraised value if guaranteed by a state, federal, or other governmental agency. The actual loan to appraised value when loans are made is generally lower than the statutory maximum percentage. Appraisals are required for loans of more than \$250,000. In addition, each loan is assigned a credit risk weighting based upon the underwriting standards. This credit risk rating process incorporates objective and subjective criteria to identify inherent strengths, weaknesses, and risks in a particular relationship.

The Association's loan portfolio is divided into performing and high-risk categories. A Special Assets Management Department is responsible for servicing loans classified as

high-risk. The high-risk assets, including accrued interest, are detailed below:

	12/31/06	12/31/05	12/31/04
	<i>(dollars in thousands)</i>		
High-risk Assets			
Nonaccrual loans	\$ 3,519	\$ 250	\$ 58
Restructured loans	199	523	564
Accruing loans 90 days past due	—	—	—
Total high-risk loans	3,718	773	622
Other property owned	—	—	—
Total high-risk assets	\$ 3,718	\$ 773	\$ 622
Ratios			
Nonaccrual loans to total loans	1.01%	.06%	.02%
High-risk assets to total assets	.89%	.17%	.17%

Nonaccrual loans represent all loans where there is a reasonable doubt as to the collection of principal and/or future interest accruals, under the contractual terms of the loan. In substance, nonaccrual loans reflect loans where the accrual of interest has been suspended. Nonaccrual loans increased \$3,269, or 1,307.60 percent in 2006. This increase resulted from the weakness associated with one large loan in the nursery industry. Of the \$3,519 in nonaccrual volume at December 31, 2006, \$45 or 1.28%, compared to 99.25% and 96.55% at December 31, 2005 and 2004, respectively, was current as to scheduled principal and interest payments, but did not meet all regulatory requirements to be transferred into accrual status.

Loan restructuring is available to financially distressed borrowers. Restructuring of loans occurs when the Association grants a concession to a borrower based on either a court order or good faith in a borrower's ability to return to financial viability. The concessions can be in the form of a modification of terms or rates, a compromise of amounts owed, or deed in lieu of foreclosure. Other receipts of assets and/or equity to pay the loan in full or in part are also considered restructured loans. The type of alternative financing structure chosen is based on minimizing the loss incurred by both the Association and the borrower.

Credit Quality

We review the credit quality of the loan portfolio on an ongoing basis as part of our risk management practices. Each loan is classified according to the Uniform Classification System, which is used by all Farm Credit System institutions. Below are the classification definitions.

- *Acceptable* – Assets are expected to be fully collectible and represent the highest quality.
- *Other Assets Especially Mentioned (OAEM)* – Assets are currently collectible but exhibit some potential weakness.
- *Substandard* – Assets exhibit some serious weakness in repayment capacity, equity, and/or collateral pledged on the loan.
- *Doubtful* – Assets exhibit similar weaknesses to substandard assets. However, doubtful assets have additional weaknesses in existing facts, conditions and values that make collection in full highly questionable.
- *Loss* – Assets are considered uncollectible.

The following table presents selected statistics related to the credit quality of loans including accrued interest at December 31.

Credit Quality	2006	2005	2004
Acceptable & OAEM	98.87%	98.56%	98.25%
Substandard	1.13	1.44	1.75
Doubtful	—	—	—
Loss	—	—	—
Total	100.00%	100.00%	100.00%

Allowance for Loan Losses

During 2004, the Association completed its study to further refine the allowance for loan losses methodology, taking into account guidance issued by FCA, as well as the Securities and Exchange Commission (SEC) and Federal Financial Institutions Examination Council. As a result of this study and resulting refinements in methodology, during the fourth quarter of 2004, the Association recorded a reversal of the allowance for loan losses of \$8,815.

Previously, the Association's allowance for loan losses methodology had been based upon criteria developed in the late 1980s and reflected the credit losses experienced in the mid-to-late 1980s, which was a period of unusually adverse economic conditions in American agriculture. Given the long cyclical nature of the agricultural economy, loss factors utilized to determine the allowance for loan losses subsequent to 1989 continued to reflect, to some extent, the loss history of the mid-to-late 1980s, which resulted in conservative estimates of the allowance for loan losses. The Association's allowance for loan losses methodology utilized throughout the period was in accordance with generally accepted accounting principles and was consistently applied.

While conservative in estimating the allowance for loan losses, the methodology used resulted in annual provisions for loan losses over the periods that reflected changes in credit quality and loss experience. Accordingly, the reserves provided in the mid-to-late 1980s had, in effect, remained part of the allowance for loan losses. The Association's allowance for loan loss methodology has consistently adhered to proper accounting policies, under the regulatory supervision of the FCA in its role as a "safety and soundness" regulator. It was the FCA's view that the allowance for loan losses should include, among others, an assessment of probable losses, historical loss experience and economic conditions.

In April 2004, the FCA issued an Informational Memorandum to System institutions regarding the criteria and methodologies that would be used in evaluating the adequacy of a System institution's allowance for loan losses. The FCA endorsed the direction provided by other bank regulators and the SEC and indicated that the conceptual framework addressed in their guidelines would be included as part of their examination process.

The refinement in methodology resulted in a calculated allowance for loan losses that was significantly less than the previously recorded balance due to revised loss factors that are more indicative of actual loss experience in recent years and current borrower analysis. The factors considered in determining

the revised level of allowance for loan losses are generally based on recent historical charge-off experience adjusted for relevant environmental factors. The Association considers the following when adjusting the historical charge-off experience:

- changes in credit risk classifications,
- changes in collateral values,
- changes in risk concentrations,
- changes in weather related conditions and
- changes in economic conditions.

While the reversal had a significant impact on 2004 results of operations and the previously recorded allowance for loan losses, the refinement in methodology is not expected to have a significant impact on comparative results of operations in future periods. Additionally, the refinement in methodology did not have a significant impact on the level of risk bearing capacity of the Association, generally referred to as "risk funds" (capital plus the allowance for loan losses), which totaled \$70,739 at December 31, 2006 (20.26 percent of Association loans), as compared with \$68,590 at December 31, 2005 (17.13 percent of Association loans) and \$66,291 at December 31, 2004 (19.01 percent of Association loans).

The allowance for loan losses at each period end is considered by Association management to be adequate to absorb probable losses existing in and inherent to its loan portfolio. The allowance for loan losses was \$1,639 at December 31, 2006, as compared with \$2,133 and \$1,954 at December 31, 2005 and 2004, respectively.

Net loan recoveries of \$118, \$111 and \$127 were recorded in 2006, 2005 and 2004, respectively. Net loan recoveries as a percentage of average loans remained at low levels of .03 percent, .03 percent, and .04 percent for 2006, 2005 and 2004, respectively.

The following table presents the activity in the allowance for loan losses for the most recent three years:

Allowance for Loan Losses Activity:	2006	2005	2004
	<i>(dollars in thousands)</i>		
Balance at beginning of year	\$ 2,133	\$ 1,954	\$ 10,642
Charge-offs:			
Real estate mortgage	\$ (3)	\$ -	\$ -
Production and intermediate term	(6)	(3)	-
Total charge-offs	(9)	(3)	-
Recoveries:			
Production and intermediate term	\$ 18	\$ 114	\$ 127
Agribusiness	109	-	-
Total recoveries	127	114	127
Net (charge-offs) recoveries	118	111	127
Provision for (reversal of allowance for) loan losses	\$ (612)	\$ 68	\$ -
Nonrecurring allowance for loan losses reversal*	-	-	(8,815)
Balance at end of year	\$ 1,639	\$ 2,133	\$ 1,954
Ratio of net charge-offs during the period to average loans outstanding during the period	.03%	.03%	.04%

* Represents the amount of allowance reversal due to the refinement in methodology.

The allowance for loan losses by loan type for the most recent three years is as follows:

Allowance for Loan Losses by Type	December 31,		
	2006	2005	2004
	<i>(dollars in thousands)</i>		
Real estate mortgage	\$ 891	\$ 1,308	\$ 1,180
Production and intermediate term	485	559	585
Agribusiness	117	122	60
Communication	5	5	6
Energy	18	22	24
Rural residential real estate	123	117	99
Total loans	\$ 1,639	\$ 2,133	\$ 1,954

The allowance for loan losses as a percentage of loans outstanding and as a percentage of certain other credit quality indicators is shown below:

Allowance for Loan Losses as a Percentage of:	2006	December 31, 2005	2004
Total loans	.47%	.53%	.56%
Nonperforming loans	44.08%	275.94%	346.45%
Nonaccrual loans	46.58%	854.16%	3,368.97%

The financial positions of our borrowers have generally strengthened during the past decade as farmers' net cash income has been at a favorable level and steady increases in land values over the period. With borrowers' strengthened financial positions and the continued emphasis on sound underwriting standards, the credit quality of our loan portfolio has remained healthy. Please refer to Note 4, "Loans and Allowance for Loan Losses," of the Notes to the Consolidated Financial Statements, for further information concerning the allowance for loan losses.

EMPLOYEE RETIREMENT PLANS

For the years ended December 31, 2006, 2005 and 2004, the Association contributed \$1, \$733 and \$3,075, respectively, to the District-wide defined benefit retirement plan. The funding brought the retirement plan's assets to an amount exceeding the accumulated benefit obligation as of the Plan's measurement date, eliminating the minimum pension liability and the charge to accumulated other comprehensive income. For additional information, refer to the Recently Issued Accounting Pronouncements disclosed in this Annual Report.

RESULTS OF OPERATIONS

Net income for the year ended December 31, 2006, totaled \$11,464, an increase of \$1,747 or 17.98 percent, as compared to \$9,717 for the same period of 2005 and a decrease of \$4,597 or 28.62 percent, as compared to \$16,061 for the same period of 2004. Interest income for the year ended December 31, 2006, was \$32,694, an increase of \$7,599 or 30.28 percent as compared to \$25,095 for the same period of 2005. Interest income increased by \$6,670 for the period ended December 31, 2005, compared to December 31, 2004. Major components of the change in net income for the past two years are outlined in the following table.

Change in Net Income:	2006-2005	2005-2004
	<i>(dollars in thousands)</i>	
Net income (prior year)	\$ 9,717	\$ 16,061
Increase (decrease) in net income due to:		
Interest income	7,599	6,670
Interest expense	(6,342)	(4,853)
Net interest income	1,257	1,817
Provision for loan losses	680	(8,883)
Noninterest income	420	890
Noninterest expense	(653)	(207)
Provision for income taxes	43	39
Total changes in income	1,747	(6,344)
Net income	\$ 11,464	\$ 9,717

Net Interest Income

Net interest income increased by \$1,257 or 11.84 percent in 2006 and increased by \$3,074 or 34.94 percent, compared to 2005 and 2004, respectively. Interest income on nonaccrual loans for 2006 totaled \$28 compared to \$27 for 2005 and a decrease of \$139 compared to \$167 for 2004. The Association's net interest income as a percentage of average earning assets was 2.84 percent on December 31, 2006, compared to 2.88 percent on December 31, 2005 and 2.71 percent on December 31, 2004. The sources of change in net interest income are summarized, as follows:

Change in Net Interest Income:

	Volume*	Rate	Nonaccrual		Total
			Income	Total	
	<i>(dollars in thousands)</i>				
12/31/06 - 12/31/05					
Interest income	\$ 3,424	\$ 4,174	\$ 1	\$ 7,599	
Interest expense	2,489	3,853	-	6,342	
Change in net interest income	\$ 935	\$ 321	\$ 1	\$ 1,257	
12/31/05 - 12/31/04					
Interest income	\$ 2,398	\$ 4,411	\$ (139)	\$ 6,670	
Interest expense	1,569	3,284	-	4,853	
Change in net interest income	\$ 829	\$ 1,127	\$ (139)	\$ 1,817	

* Volume variances can be the result of increased/decreased loan volume or from changes in the percentage composition of assets and liabilities between periods.

Please refer to the Consolidated Five-Year Summary of Selected Financial Data in this Annual Report to review key financial ratios pertaining to earnings and net interest income.

Noninterest Income

Noninterest income for each of the three years ended December 31 are shown in the following table:

Noninterest Income	For the Year Ended			Percentage	
	December 31,			Increase/(Decrease)	
	2006	2005	2004	2006/	2005/
	<i>(dollars in thousands)</i>				
Loan fees	\$ 1,050	\$ 885	\$ 671	18.64%	31.89%
Fees for financially related services	9	7	5	28.57	40.00
Patronage refund from other Farm Credit Institutions	4,646	3,808	3,493	22.01	9.02
Gains (losses) on sale of other property owned, net	-	-	(1)	-	(100.00)
Gains (losses) from sale of premises & equipment, net	38	553	121	(93.13)	361.16
Other noninterest income	53	123	197	(56.91)	(40.10)
Total noninterest income	\$ 5,796	\$ 5,376	\$ 4,486	7.81%	19.84%

Regarding patronage refunds received from other Farm Credit Institutions, the Association received \$3,948 in a patronage refund and \$575 in a special distribution from the Bank for the year ended December 31, 2006, compared to \$2,814 and \$977 for 2005, and \$2,494 and \$982 for 2004. Loan fees increased \$165 and increased \$379 for the period ended December 31, 2006, compared to comparable periods in 2005 and 2004, respectively.

Noninterest Expense

Noninterest expense for each of the three years ended December 31 is shown in the following table:

Noninterest Expense	For the Year Ended			Percentage	
	December 31,			Increase/(Decrease)	
	2006	2005	2004	2006/	2005/
	<i>(dollars in thousands)</i>				
Salaries and employee benefits	\$ 4,170	\$ 4,061	\$ 4,074	2.68%	(.32)%
Occupancy and equipment expense	675	695	518	(2.88)	34.17
Insurance Fund premium	572	177	164	223.16	7.93
Other operating expense	1,385	1,216	1,186	13.90	2.53
Total noninterest expense	\$ 6,802	\$ 6,149	\$ 5,942	10.62%	3.48%

Noninterest expense increased \$653 or 10.62 percent for December 31, 2006, as compared to the same period of 2005 and increased \$860 or 14.47 percent compared to December 31, 2004. Salaries and employee benefits increased \$109 or 2.68 percent for December 31, 2006 as compared to an increase of \$96 or 2.36 percent for 2004. Also contributing to the increase in noninterest expense were increases in insurance fund premiums (\$395) and other operating expenses (\$169).

The Association recorded a provision for income taxes of \$13 for the year ended December 31, 2006, as compared to a provision of \$56 for 2005 and a provision of \$95 for 2004.

Key Results of Operations Comparisons

Key results of operations comparisons for each of the twelve months ended December 31 are shown in the following table:

Key Results of Operations Comparisons	For the 12 Months Ended 12/31/06	For the 12 Months Ended 12/31/05	For the 12 Months Ended 12/31/04
Return on average assets	2.63%	2.56%	4.96%
Return on average members' equity	16.71%	14.73%	30.06%
Net interest income as a percentage of average earning assets	2.84%	2.89%	2.71%
Net charge-offs (recoveries) to average loans	(0.03)%	(0.03)%	(0.04)%

A key factor in the growth of net income for future years will be continued improvement in net interest and noninterest income. Our goal is to generate earnings sufficient to fund operations, adequately capitalize the Association, and achieve an adequate rate of return for our members. To meet this goal, the agricultural economy must continue the improvement shown in recent years and the Association must meet certain objectives. These objectives are to attract and maintain high quality loan volume priced at competitive rates and to manage

credit risk in our entire portfolio, while efficiently meeting the credit needs of our members.

LIQUIDITY AND FUNDING SOURCES

Liquidity

Liquidity management is the process whereby funds are made available to meet all financial commitments including the extension of credit, payment of operating expenses and payment of debt obligations. The Association receives access to funds through its borrowing relationship with the Bank and from income generated by operations. The Association's investments and other secondary market programs provides additional liquidity. Sufficient liquid funds have been available to meet all financial obligations.

Funding Sources

The principal source of funds for the Association is the borrowing relationship established with the Bank through a General Financing Agreement (GFA.). The GFA utilizes the Association's credit and fiscal performance as criteria for establishing a line of credit on which the Association may draw funds. The Bank advances the funds to the Association, creating notes payable to the Bank. The notes payable are segmented into variable rate and fixed rate components. 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.

Total notes payable to the Bank at December 31, 2006, was \$334,575 as compared to \$374,294 at December 31, 2005 and \$288,746 at December 31, 2004. The decrease of 10.61 percent compared to December 31, 2005 and the increase of 15.87 percent compared to December 31, 2004, is attributable to the application of proceeds from increased loan participations sold, and from increased borrowings to fund new loan advances respectively. The average volume of outstanding notes payable to the Bank was \$358,411 and \$305,849 for the years ended December 31, 2006 and 2005, respectively. Refer to Note 7, "Notes Payable to AgFirst Farm Credit Bank," of the Notes to the Consolidated Financial Statements, for additional information concerning the Association's debt.

The Association had no lines of credit from third party financial institutions as of December 31, 2006.

Funds Management

The Bank and the Association manage assets and liabilities to provide a broad range of loan products and funding options, which are designed to allow the Association to be competitive in all interest rate environments. The primary objective of the asset/liability management process is to provide stable and rising earnings, while maintaining adequate capital levels by managing exposure to credit and interest rate risks.

Demand for loan types is a driving force in establishing a funds management strategy. The Association offers fixed, adjustable

and variable rate loan products that are marginally priced according to financial market rates. Variable rate loans may be indexed to either the Prime Rate or the 90-day London Interbank Offered Rate (LIBOR). Adjustable rate mortgages are indexed to U.S. Treasury Rates. Fixed rate loans are priced based on the current cost of System debt of similar terms to maturity.

The majority of the interest rate risk in the Association's Consolidated Balance Sheets is transferred to the Bank through the notes payable structure. The Bank, in turn, actively utilizes funds management techniques to identify, quantify and control risk associated with the loan portfolio.

CAPITAL RESOURCES

Total members' equity at December 31, 2006, increased 3.98 percent to \$69,100 from the December 31, 2005, total of \$66,457 and increased 7.40 percent from the December 31, 2004 total of \$64,337. The increase was primarily attributed to increased net income being partially offset by cash patronage, the revolvment of allocated equities, and the reduction of capital stock and participation certificates.

Total capital stock and participation certificates were \$1,306 on December 31, 2006, compared to \$1,315 on December 31, 2005 and \$1,504 on December 31, 2004. The decrease was attributed to the retirement of protected borrower stock and participation certificates on loans liquidated in the normal course of business, retirement of excess stock through revolvment and new loans being capitalized at lower regulatory levels.

The Association Board of Directors establishes, adopts, and maintains a formal written capital adequacy plan. There were no material changes to the capital plan for 2006 that would affect minimum stock purchases or would have an effect on the Association's ability to retire stock and distribute earnings.

The Association's capital ratios as of December 31 and the FCA minimum requirements follow:

	<u>2006</u>	<u>2005</u>	<u>2004</u>	<u>Regulatory Minimum</u>
Permanent Capital	16.55%	15.36%	15.40%	7.00%
Total Surplus	15.88%	15.06%	15.15%	7.00%
Core Surplus	13.46%	12.70%	12.13%	3.50%

At December 31, 2006, the Association's permanent capital ratio, (average at-risk capital divided by average risk adjusted assets), calculated in accordance with FCA regulations, exceeded the regulatory minimum of 7.00 percent. In addition to these regulatory requirements, the Association has established a permanent capital ratio goal in excess of the 7.00 percent FCA minimum requirement. As of December 31, 2006, the Association has met the goal. The increase in the Association's permanent capital, total surplus, and core surplus for December 31, 2006 and December 31, 2005 was attributed to the reduction in average risk adjusted assets through increased sales of loan participations coupled with the increase in earned surplus being partially offset by reduction through revolvment of allocated surplus issued in 2001 and 2000.

See Note 9, "Members' Equity," of the Notes to the Consolidated Financial Statements, for further information concerning capital resources.

PATRONAGE PROGRAM

Prior to the beginning of any fiscal year, the Association's Board of Directors, by adoption of a resolution, may establish a Patronage Allocation Program to distribute its available consolidated net earnings. This resolution provides for the application of net earnings in the manner described in the Association's Bylaws. This includes the setting aside of funds to increase surplus to meet minimum capital adequacy standards established by FCA Regulations, to increase surplus to meet Association capital adequacy standards to a level necessary to support competitive pricing at targeted earnings levels, and for reasonable reserves for necessary purposes of the Association. After excluding net earnings attributable to (a) the portion of loans participated to another institution, (b) participation loans purchased, and (c) other non-patronage sourced activities, the remaining consolidated net earnings are eligible for allocation to borrowers. Refer to Note 9, "Members' Equity," of the Notes to the Consolidated Financial Statements, for more information concerning the patronage distributions. The Association declared patronage distributions of \$10,154 in 2006, \$8,024 in 2005, and \$5,935 in 2004.

YOUNG, BEGINNING AND SMALL (YBS) FARMERS AND RANCHERS PROGRAM

The Association's mission is to provide financial services to agriculture and the rural community, which includes providing credit to young*, beginning** and small*** farmers. Because of the unique needs of these individuals, and their importance to the future growth of the Association, the Association has established annual marketing goals to increase our market share of loans to YBS farmers. Specific marketing plans have been developed to target these groups, and resources have been designated to help ensure YBS borrowers have access to a stable source of credit.

The following table outlines the loan volume and number of YBS loans in the loan portfolio for the Association.

	As of December 31, 2006	
	Number of Loans	Amount of Loans
Young	184	\$ 13,307
Beginning	515	74,886
Small	809	80,241

Note: For purposes of the above table, a loan could be classified in more than one category, depending upon the characteristics of the underlying borrower.

The 2002 USDA (2002 is the latest USDA Ag census data available; next census will be available in 2008.) Ag census data has been used as a benchmark to measure penetration of the Association's marketing efforts. The census data indicated that within the Association's chartered territory (counties)

there were 14,630 reported farmers of which by definition 574 or 3.92 percent were Young, 4,660 or 31.85 percent were Beginning, and 13,759 or 94.05 percent were Small. Comparatively, as of December 31, 2006, the demographics of the Association's agricultural portfolio contained 1,349 farmers, of which by definition 184 or 13.64 percent were Young, 515 or 38.18 percent were Beginning and 809 or 59.97 percent were Small.

The Association Board of Directors has adopted a Young, Beginning, and Small Farmer Plan with specific goals for the number of loans and new volume closed for 2007 and two succeeding years. The association will continue to review the demographics of its territory during 2007 utilizing 2002 Ag census data.

The following strategies and outreach programs have been conducted which assists and supports the Association's efforts to meet its objectives and goals for financing to the young, beginning, and small farmers.

- Support of 4-H, FFA, and young farmer organizations through sponsorships and donations.
- Sponsor seminars on farm transition planning and financial management.
- Youth livestock financing program for Youth Steer and Swine Shows. Available territory wide.
- Financial Training in cooperation with Florida Southern College, Citrus and Horticulture Dept.
- Employees serve as judges for youth livestock project record books.
- Sponsor participants and participate in Florida Council of Coops, Young Cooperator Conference.
- Sponsor Florida Nursery Growers Young Professional Award.

In addition, the association's lending personnel actively participate in various commodity trade group conferences and continuing education programs.

Association lenders have established performance goals to provide informational and financial training to agricultural youth groups and industry trade associations.

The Association is committed to the future success of young, beginning and small farmers.

- * *Young farmers* are defined as those farmers, ranchers, producers or harvesters of aquatic products who are age 35 or younger as of the date the loan is originally made.
- ** *Beginning farmers* are defined as those farmers, ranchers, producers or harvesters of aquatic products who have 10 years or less farming or ranching experience as of the date the loan is originally made.
- *** *Small farmers* are defined as those farmers, ranchers, producers or harvesters of aquatic products who normally generate less than \$250 in annual gross sales of agricultural or aquatic products at the date the loan is originally made.

RECENTLY ISSUED ACCOUNTING PRONOUNCEMENTS

Accounting for Uncertainty in Income Taxes

In June 2006, the Financial Accounting Standards Board (FASB) released Interpretation No. 48, "Accounting for Uncertainty in Income Taxes" (FIN 48). This interpretation clarifies the accounting for uncertainty in income taxes recognized in an enterprise's financial statements in accordance with FASB Statement No. 109, "Accounting for Income Taxes." FIN 48 prescribes a recognition threshold and measurement attribute for the financial statement recognition and measurement of a tax position taken or expected to be taken in a tax return. FIN 48 is effective for fiscal years beginning after December 15, 2006. Adoption of FIN 48 is not expected to have a material impact on the Association's Consolidated Balance Sheet or Consolidated Statement of Income.

Accounting for Defined Benefit Pension and Other Postretirement Plans

On September 29, 2006, the FASB issued Statement of Financial Accounting Standards No. 158, "Employers' Accounting for Defined Benefit Pension and Other Postretirement Plans" (FAS 158). FAS 158 requires an employer to recognize the overfunded or underfunded status of a defined benefit postretirement plan as an asset or liability in its statement of financial position and recognize through comprehensive income changes in that funded status in the year in which the changes occur. FAS 158 also provides guidance relating to the discount rate, which may require the Association to adjust its basis for selecting the discount rate for its pension and non-pension postretirement benefit plans. The Association will be required to implement FAS 158 for the year ended December 31, 2007. In addition, FAS 158 requires that the funded status of a plan be measured as of the date of the year-end financial statements. Currently, the Association uses a measurement date of September 30th. The requirement to measure the funded status as of the fiscal year-end is effective for fiscal years ending after December 15, 2008. The Association is currently evaluating the impact of implementing FAS 158.

FORWARD LOOKING INFORMATION

Certain information included in this discussion constitutes forward-looking statements and information that are based upon management's belief as well as certain assumptions made by and information currently available to management. When used in this discussion, the words "anticipate," "project," "expect," "believe," and similar expressions are intended to identify forward-looking statements. Although management of the Association believes that the expectations reflected in such forward-looking statements are reasonable, it can give no assurance that such expectations and projections will prove to have been correct. Such forward-looking statements are subject to certain risks, uncertainties and assumptions. Should one or more of these risks materialize, or should such underlying assumptions prove to be incorrect, actual results may vary materially from those anticipated,

projected, or expected. Among key factors that may have a direct bearing on the Association's operating results are fluctuations in the economy, the relative strengths and weaknesses in the agricultural credit sectors and in the real estate market, the actions taken by the Federal Reserve for the purpose of managing the economy, and the continued growth of the agricultural market consistent with recent historical experience.

Disclosure Required by Farm Credit Administration Regulations

Description of Business

Descriptions of the territory served, persons eligible to borrow, types of lending activities engaged in, financial services offered and related Farm Credit organizations are incorporated herein by reference to Note 1 to the consolidated financial statements, "Organization and Operations," included in this annual report to shareholders.

The description of significant developments that had or could have a material impact on earnings or interest rates to borrowers, acquisitions or dispositions of material assets, material changes in the manner of conducting the business, seasonal characteristics, and concentrations of assets, if any, is incorporated in "Management's Discussion and Analysis of Financial Condition and Results of Operations" included in this annual report to shareholders.

Description of Property

The following table sets forth certain information regarding the properties of the reporting entity, all of which are located in Florida:

<u>Location</u>	<u>Description</u>	<u>Form of Ownership</u>
115 S. Missouri Ave.* Lakeland	Administrative/ Branch	Leased
507 E. Third Street Apopka	Branch	Owned
36 W. Polk Avenue Lake Wales	Branch	Owned
2301 Thonotosassa Road Plant City	Branch	Owned
31081 Cortez Blvd.** Brooksville	Branch	Leased

* The Administrative / branch office located at 115 S. Missouri Ave. is leased through December 31, 2016 with a 4-year option to renew.

** The branch office located at 31081 Cortez Blvd. is leased through November 30, 2009 with a 3-year option to renew.

Legal Proceedings

Information, if any, to be disclosed in this section is incorporated herein by reference to Note 14 to the consolidated financial statements, "Commitments and Contingencies," included in this annual report to shareholders.

Description of Capital Structure

Information to be disclosed in this section is incorporated herein by reference to Note 9 to the consolidated financial statements, "Members' Equity," included in this annual report to shareholders.

Description of Liabilities

The description of liabilities, contingent liabilities and intrasystem financial assistance rights and obligations to be disclosed in this section is incorporated herein by reference to Notes 2, 8, 12 and 14 to the consolidated financial statements included in this annual report to shareholders.

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

"Management's Discussion and Analysis of Financial Condition and Results of Operations," which appears in this annual report to shareholders and is to be disclosed in this section, is incorporated herein by reference.

Senior Officers

The following represents certain information regarding the senior officers of the Association:

<u>Senior Officer</u>	<u>Position</u>
Richard W. Joyner	<i>President and Chief Executive Officer since 1997.</i>
Robert W. Teston	<i>Executive Vice President and Chief Operating and Lending Officer since 1992.</i>
Gregory D. Ellis	<i>Sr. Vice President and Corporate Treasurer / CFO since 1993.</i>
Reginald T. Holt	<i>Sr. Vice President since 1997.</i>
Wayne R. Montgomery	<i>Sr. Vice President since 2005 and previously served as Vice President and Special Assets Officer since 1993.</i>

The business experience for the past five years for senior officers is with the Farm Credit System.

The total amount of compensation earned by the CEO and the highest paid officers as a group during the years ended December 31, 2006, 2005 and 2004, is as follows:

<u>Name of Individual or Number in Group</u>	<u>Year</u>	<u>Annual</u>				<u>Other</u>	<u>Total</u>
		<u>Salary</u>	<u>Bonus</u>	<u>Perquisites</u>	<u>Deferred/-</u>		
Richard W. Joyner	2006*	\$242,010	–	\$5,764	–	\$247,774	
Richard W. Joyner	2005	\$210,008	–	–	–	\$210,008	
	5	2006*	\$538,354	\$131,092	\$5,235	–	\$674,681
	5	2005	\$728,652	\$104,400	–	–	\$833,052
	5	2004	\$582,473	\$ 55,055	–	–	\$637,478

* Note: Beginning with year-end 2006, CEO compensation must be disclosed as a separate line item and is not included in the aggregate amount. The CEO salary is included in the aggregate amount for 2004 and 2005.

Regulatory reporting changes have affected the content of the compensation reported for 2006 and those changes may not be reflected in the 2004 and 2005 amounts.

In addition to base salary, all Association employees (except the President and Chief ACA Reviewer) may earn additional compensation under a corporate bonus plan. The Association bonus plan is designed to motivate employees to exceed business plan goals during the fiscal year. Level 1 of the Association plan covers all non-exempt employees (for wage and salary administration purposes) and is based on increasing budgeted final net income. Payments under Level 1 are calculated at year-end with eligible employees receiving up to 5 percent of their annual salary in cash.

Level 2 of the Association plan covers all exempt employees (except the President, other Senior Officers, the Chief ACA Reviewer, Residential Lending Group employees, and employees identified as "lenders") and is based on increasing loan volume and fee income. This portion of the plan is divided into three categories; percent increase (over budget) in Average Gross Accruing Volume outstanding (33.33 percent), percent increase (over budget) in Dollar Volume of New Loans Closed (33.33 percent), and percent increase (over budget) in Fee Income (33.33 percent). Payments at this level are calculated at year-end based on the weighted average performance in each category, paid 100 percent in cash. The maximum award at this level shall not exceed 12 percent of their annual salary and requires a certain minimum individual employee evaluation score.

Level 3 of the Association plan covers all employees identified as "lenders" and is based upon their personal performance relative to their individual standards of performance. Award percentage points are earned for Marketing and Business Development and deductions for Asset Quality and Delinquencies. Payments at this level are calculated at year-end based on the weighted average performance in each category, paid 100 percent in cash. The maximum award at this level shall not exceed 25 percent of their annual salary and requires a certain minimum individual employee evaluation score.

Level 4 of the Association plan covers all employees in the Residential Lending Group. Underwriters and Sales Coordinators earn awards based upon their personal performance relative to their individual standards of performance. Processors and Closers earn a set dollar amount on each loan originated. Payments are made quarterly and require a certain minimum individual employee evaluation score.

Level 5 of the Association plan covers the senior officers listed above with the exception of the President. The Association must meet certain objectives for Shareholder Value (measured by the Return on Equity ratio; weighted 20 percent), Safety & Soundness (measured by FCA "CAMELS" rating and CIPA Score; weighted 20 percent), Growth, (measured by increase in Gross Volume, Net Volume, and New Loans Closed; weighted 20 percent), Credit Quality (measured by Acceptable & OAEM volume, Nonaccrual loan volume, Other Property Owned, and Delinquencies; weighted 20 percent), and Operating Efficiency (measured by the ratio of Operating Expenses to Final Net Interest Income, Noninterest Income to Operating Expenses ratio and the Return on Assets ratio; weighted 20 percent). Payments at this level are calculated at year-end based on the weighted average performance in each category, paid 75 percent in cash and 25 percent deferred until surplus allocated received by members is revolved to equity holders from the same period. The maximum award at this level shall not exceed 25 percent of their annual salary and requires a certain minimum individual employee evaluation score.

An overall plan restriction limits the total of all payments to a maximum of 25 percent of the total gain over budget. Payment of the Corporate Bonus is in the first quarter of 2007. Bonuses are shown in the year earned, which may be different than the year of payment.

Disclosure of information on the total compensation paid during 2006 to any senior officer, or to any other individual included in the total, is available to shareholders upon request.

Directors

Directors and senior officers are reimbursed on an actual cost basis for all expenses incurred in the performance of official duties. Such expenses may include transportation, lodging, meals, tips, tolls, parking of cars, laundry, registration fees, and other expenses associated with travel on official business. A copy of the policy is available to shareholders of the Association upon request.

The aggregate amount of reimbursement for travel, subsistence and other related expenses for all directors as a group was \$39,064 for 2006, \$32,667 for 2005, and \$22,812 for 2004.

Subject to approval by the board, the Association may allow directors an annual retainer of \$3,000 to be paid monthly and honoraria of \$400 for attendance at meetings and committee meetings and honoraria of \$300 for special assignments. Total compensation paid to directors as a group was \$163,000.

The following represents certain information regarding the directors of the Association:

Al Bellotto, Chairman, is a cattleman and citrus grower and serves on the boards of the Florida Cattlemen's Association and the Polk County Cattlemen's Association (Beef Promotion). His principal occupation and employment for the past 5 years was with Al Bellotto, Inc. Mr. Bellotto has served on the Association board since April 1991, and his current term of office expires in April 2009. During 2006, he served 12 days at Association board meetings and 64 days in other official activities and was paid \$32,500.

David J. Stanford, Vice Chairman, is a citrus grower and now retired citrus processor and serves on the board of South Lake Apopka Citrus Growers Association (citrus cooperative). For the past 5 years, Mr. Stanford has been self-employed. Mr. Stanford has served on the Association board since April 1992, and his current term of office expires in April 2008. During 2006, he served 12 days at Association board meetings and 32 days in other official activities and was paid \$17,600.

W. T. Bice, Sr. is a citrus grower and serves on the board of Star Lake, Inc. (investments). His principal occupation and employment for the past 5 years was with W.T. Bice Groves. Mr. Bice has served on the Association board since April 1991, and his current term of office expires in April 2008. During 2006, he served 11 days at Association board meetings and 47 days in other official activities and was paid \$25,800.

C. Dennis Carlton, Sr. is a cattleman, citrus grower and real estate developer and serves on the boards of Valrico State Bank (Valrico, FL), Hillsborough County Farm Bureau, and the Soil and Water Conservation District. For the past 5 years, Mr. Carlton has been self-employed. Mr. Carlton has served on the Association board since February 2004, and his current term of

office expires in April 2007. During 2006, he served 10 days at Association board meetings and 8 days in other official activities and was paid \$9,800.

W. Rex Clonts, Jr. is a citrus grower and serves on the board of Florida Citrus Mutual and the Florida Fruit and Vegetable Association. His principal occupation and employment for the past 5 years was with Clonts Farms, Inc. Mr. Clonts has served on the Association board since February 1997, and his current term of office expires in April 2009. During 2006, he served 9 days at Association board meetings and 10 days in other official activities and was paid \$10,000.

Homer E. Hunnicutt, Jr. is an egg producer and serves on the boards of Hillandale Farms, LLC, Columbia Grain & Ingredients, Inc., SunTrust Bank – Nature Coast, and the Hernando County Farm Bureau. His principal occupation and employment for the past 5 years was with Finest Farms. Mr. Hunnicutt has served on the Association board since April 1991, and his current term of office expires in April 2007. During 2006, he served 12 days at Association board meetings and 16 days in other official activities and was paid \$13,100.

John S. Langford is a citrus grower, commercial caretaker, citrus harvester and real estate broker and serves on the boards of Community Southern Bank (Lakeland, FL), the Polk County Farm Bureau, and as a commissioner on the Polk County Planning Commission. His principal occupation and employment for the past 5 years was with John Langford, Inc. Mr. Langford has served on the Association board since August 24, 2005, and his current term of office expires in April 2009. During 2006, he served 12 days at Association board meetings and 19 days in other official activities and was paid \$14,000.

Robert R. Roberson is a nurseryman and serves on the boards of Bank First (Apopka, FL) and the Orange County Farm Bureau. His principal occupation and employment for the past 5 years was with Foliage Factory Too, Inc. Mr. Roberson also owns Less Energy Systems LLC in Apopka, FL and has an active real estate license with Lou Haubner Realty. Mr. Roberson has served on the Association Board since December 1997, and his current term of office will expire in April 2007. During 2006, he served 10 days at Association board meetings and 16 days in other official activities and was paid \$12,100.

Lewis S. Stidham is a former commercial banker from Citrus & Chemical Bank. His principal occupation and employment for the past 5 years was with Citrus & Chemical Bank (now retired) and self-employment. Mr. Stidham has served on the Association board since May 1995, and his current term of office expires in April 2007. During 2006, he served 11 days at Association board meetings and 17 days in other official activities and was paid \$13,100.

Ronald R. Wetherington is a strawberry and citrus grower and serves on the boards of the Hillsborough County Farm Bureau, Florida Farm Bureau Insurance Company, Florida Farm Bureau Federation, and Hillsborough County Law Enforcement Association. His principal occupation and employment for the past 5 years was with Wetherington Farms. Mr. Wetherington has served on the Association Board since May 1993, and his current term of office expires in April 2008. During 2006, he served 12 days at Association board meetings and 24 days in other official activities and was paid \$15,000.

Transactions with Senior Officers and Directors

The reporting entity's policies on loans to and transactions with its officers and directors, to be disclosed in this section are incorporated herein by reference to Note 13 to the consolidated financial statements, "Related Party Transactions," included in this annual report to shareholders.

Involvement in Certain Legal Proceedings

There were no matters which came to the attention of management or the board of directors regarding involvement of current directors or senior officers in specified legal proceedings which should be disclosed in this section.

Relationship with Independent Public Accountants

There were no material disagreements with our independent public accountants on any matter of accounting principles or financial statement disclosure during this period.

Consolidated Financial Statements

The consolidated financial statements, together with the report thereon of PricewaterhouseCoopers LLP dated February 28, 2007 and the report of management, which appear in this annual report to shareholders are incorporated herein by reference.

Copies of the Association's quarterly reports are available upon request free of charge by calling 1-800-533-2773 or writing Gregory D. Ellis, Chief Financial Officer, Farm Credit of Central Florida, ACA, P.O. Box 8009, Lakeland, FL 33802 or accessing the website, www.farmcreditfl.com. The Association prepares a quarterly report within 45 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.

Borrower Information Regulations

Since 1972, Farm Credit Administration (FCA) regulations have required that borrower information be held in strict confidence by Farm Credit System (FCS) institutions, their directors, officers and employees. These regulations provide Farm Credit institutions clear guidelines for protecting their borrowers' nonpublic personal information.

On November 10, 1999, the FCA Board adopted a policy that requires FCS institutions to formally inform new borrowers at loan closing of the FCA regulations on releasing borrower information and to address this information in the annual report to shareholders. The implementation of these measures ensures that new and existing borrowers are aware of the privacy protections afforded them through FCA regulations and Farm Credit System institution efforts.

Shareholder Investment

Shareholder investment in the Association could be affected by the financial condition and results of operations of AgFirst Farm Credit Bank. Copies of the District annual and quarterly reports are available upon request free of charge by calling 1-800-845-1745, ext. 316, or writing Wanda Martin, AgFirst Farm Credit Bank, P. O. Box 1499, Columbia, SC 29202. Information concerning AgFirst Farm Credit Bank can also be obtained by going to AgFirst's website at www.agfirst.com.

Report of the Audit Committee


The Audit Committee of the Board of Directors (Committee) is comprised of the directors named below. None of the directors who serve on the Committee is an employee of Farm Credit of Central Florida, ACA (Association) and in the opinion of the Board of Directors, each is free of any relationship with the Association or management that would interfere with the director's independent judgment on the Committee.

The Committee has adopted a written charter that has been approved by the Board of Directors. The Committee has reviewed and discussed the Association's audited financial statements with management, which has primary responsibility for the financial statements.

PricewaterhouseCoopers LLP (PwC), the Association's independent auditor for 2006, is responsible for expressing an opinion on the conformity of the Association's audited financial statements with accounting principles generally accepted in the United States of America. The Committee has discussed with PwC the matters that are required to be discussed by Statement on Auditing Standards No. 61 (*Communication With Audit Committees*). PwC has provided to the Committee the written disclosures and the letter required by Independence Standards Board Standard No. 1 (*Independence Discussions with Audit Committees*), and the Committee has discussed with PwC that firm's independence.

The Committee has also concluded that PwC's provision of non-audit services, if any, to the Association is compatible with PwC's independence.

Based on the considerations referred to above, the Committee recommended to the Board of Directors that the audited financial statements be included in the Association's Annual Report for 2006. The foregoing report is provided by the following independent directors, who constitute the Committee:



Lewis S. Stidham, Chairman
Chairman of the Audit Committee

Members of Audit Committee

W. Rex Clonts, Jr.
Homer E. Hunnicutt, Jr.
John S. Langford
Robert R. Roberson
Ronald R. Wetherington

Report of Independent Auditors



PricewaterhouseCoopers LLP
10 Tenth Street, Suite 1400
Atlanta, GA 30309
Telephone (678) 419 1000

Report of Independent Auditors

To the Board of Directors and Members
of Farm Credit of Central Florida, ACA

In our opinion, the accompanying consolidated balance sheets and the related consolidated statements of income, of changes in members' equity and of cash flows present fairly, in all material respects, the financial position of Farm Credit of Central Florida, ACA (the Association) and its subsidiaries at December 31, 2006, 2005 and 2004, and the results of their operations and their cash flows for each of the three years in the period ended December 31, 2006 in conformity with accounting principles generally accepted in the United States of America. These financial statements are the responsibility of the Association's management. Our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audits of these statements in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

PricewaterhouseCoopers LLP

February 28, 2007

Consolidated Balance Sheets

<i>(dollars in thousands)</i>	December 31, 2006	December 31, 2005	December 31, 2004
Assets			
Cash	\$ 63	\$ 799	\$ 203
Investment securities, held to maturity	38,704	34,682	—
Loans	349,172	400,399	348,753
Less: allowance for loan losses	1,639	2,133	1,954
Net loans	347,533	398,266	346,799
Accrued interest receivable	3,582	3,196	2,066
Investment in other Farm Credit institutions	15,822	4,034	3,951
Premises and equipment, net	1,139	1,107	1,363
Prepaid retirement expense	3,609	4,136	3,929
Due from AgFirst Farm Credit Bank	4,523	3,790	3,477
Other assets	1,469	1,265	438
Total assets	<u>\$ 416,444</u>	<u>\$ 451,275</u>	<u>\$ 362,226</u>
Liabilities			
Notes payable to AgFirst Farm Credit Bank	\$ 334,575	\$ 374,294	\$ 288,746
Accrued interest payable	1,680	1,652	981
Patronage refund payable	3,603	2,866	2,766
Other liabilities	7,486	6,006	5,396
Total liabilities	<u>347,344</u>	<u>384,818</u>	<u>297,889</u>
Commitments and contingencies			
Members' Equity			
Protected borrower stock	97	146	275
Capital stock and participation certificates	1,209	1,169	1,229
Retained earnings			
Allocated	28,995	27,008	26,153
Unallocated	38,799	38,134	36,680
Total members' equity	<u>69,100</u>	<u>66,457</u>	<u>64,337</u>
Total liabilities and members' equity	<u>\$ 416,444</u>	<u>\$ 451,275</u>	<u>\$ 362,226</u>

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

Consolidated Statements of Income

<i>(dollars in thousands)</i>	For the year ended December 31,		
	2006	2005	2004
Interest Income			
Loans	\$ 30,783	\$ 24,603	\$ 18,425
Investment securities	1,911	492	—
Total interest income	32,694	25,095	18,425
Interest Expense			
Notes payable to AgFirst Farm Credit Bank	20,823	14,481	9,628
Net interest income	11,871	10,614	8,797
Provision for (reversal of allowance for) loan losses	(612)	68	(8,815)
Net interest income after provision for (reversal of allowance for) loan losses	12,483	10,546	17,612
Noninterest Income			
Loan fees	1,050	885	671
Fees for financially related services	9	7	5
Patronage refund from other Farm Credit institutions	4,646	3,808	3,493
Gains (losses) on other property owned, net	—	—	(1)
Gains (losses) on sales of premises and equipment, net	38	553	121
Other noninterest income	53	123	197
Total noninterest income	5,796	5,376	4,486
Noninterest Expense			
Salaries and employee benefits	4,170	4,061	4,074
Occupancy and equipment	675	695	518
Insurance Fund premiums	572	177	164
Other operating expenses	1,385	1,216	1,186
Total noninterest expense	6,802	6,149	5,942
Income before income taxes	11,477	9,773	16,156
Provision (benefit) for income taxes	13	56	95
Net income	\$ 11,464	\$ 9,717	\$ 16,061

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

Consolidated Statements of Changes in Members' Equity

<i>(dollars in thousands)</i>	Protected	Capital	Retained Earnings		Accumulated	Total
	Borrower Stock	Stock and Participation Certificates	Allocated	Unallocated	Other Comprehensive Income	Members' Equity
Balance at December 31, 2003	\$ 399	\$ 1,190	\$ 27,842	\$ 26,228	\$ (2,925)	\$ 52,734
Comprehensive income						
Net income				16,061		16,061
Minimum pension liability adjustment					2,925	2,925
Total comprehensive income						18,986
Protected borrower stock retired	(124)					(124)
Capital stock/participation certificates issued		216				216
Capital stock/participation certificates retired		(177)				(177)
Cash dividends declared/paid				(1,000)		(1,000)
Patronage distribution						
Cash				(1,727)		(1,727)
Qualified allocated retained earnings			3,208	(3,208)		—
Retained earnings retired			(4,702)			(4,702)
Distribution adjustment			(195)	326		131
Balance at December 31, 2004	275	1,229	26,153	36,680	—	64,337
Net income				9,717		9,717
Protected borrower stock retired	(129)					(129)
Capital stock/participation certificates issued		239				239
Capital stock/participation certificates retired		(299)				(299)
Patronage distribution						
Cash				(2,808)		(2,808)
Nonqualified allocated retained earnings			4,658	(4,658)		—
Nonqualified retained earnings			558	(558)		—
Retained earnings retired			(4,515)			(4,515)
Distribution adjustment			154	(239)		(85)
Balance at December 31, 2005	146	1,169	27,008	38,134	—	66,457
Net income				11,464		11,464
Protected borrower stock retired	(49)					(49)
Capital stock/participation certificates issued		228				228
Capital stock/participation certificates retired		(188)				(188)
Patronage distribution						
Cash				(3,554)		(3,554)
Qualified allocated retained earnings			59	(59)		—
Nonqualified allocated retained earnings			6,541	(6,541)		—
Retained earnings retired			(5,037)			(5,037)
Distribution adjustment			424	(645)		(221)
Balance at December 31, 2006	\$ 97	\$ 1,209	\$ 28,995	\$ 38,799	\$ —	\$ 69,100

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

Consolidated Statements of Cash Flows

<i>(dollars in thousands)</i>	For the year ended December 31,		
	2006	2005	2004
Cash flows from operating activities:			
Net income	\$ 11,464	\$ 9,717	\$ 16,061
Adjustments to reconcile net income to net cash provided by (used in) operating activities:			
Depreciation on premises and equipment	193	215	228
Provision for (reversal of allowance for) loan losses	(612)	68	(8,815)
(Gains) losses on other property owned, net	—	—	1
(Gains) losses from sales of premises and equipment, net	(38)	(553)	(121)
Changes in operating assets and liabilities:			
(Increase) decrease in accrued interest receivable	(386)	(1,130)	(198)
(Increase) decrease in prepaid retirement expense	527	(207)	(3,929)
(Increase) decrease in due from AgFirst Farm Credit Bank	(733)	(313)	(829)
(Increase) decrease in other assets	(204)	(827)	2,735
Increase (decrease) in accrued interest payable	28	671	200
Increase (decrease) in minimum pension liability	—	—	(1,455)
Increase (decrease) in other liabilities	1,480	610	509
Total adjustments	255	(1,466)	(11,674)
Net cash provided by (used in) operating activities	11,719	8,251	4,387
Cash flows from investing activities:			
Purchases of investment securities, held to maturity	(16,805)	(38,394)	—
Proceeds from maturities of or principal payments received on investment securities, held to maturity	12,783	3,712	—
Net (increase) decrease in loans	51,345	(51,535)	(18,834)
(Increase) decrease in investment in other Farm Credit institutions	(11,788)	(83)	155
Purchases of premises and equipment	(187)	(241)	(392)
Proceeds from sales of premises and equipment, net	—	835	195
Proceeds from sale of other property owned	—	—	(1)
Net cash provided by (used in) investing activities	35,348	(85,706)	(18,877)
Cash flows from financing activities:			
Advances on (repayment of) notes payable to AgFirst Farm Credit Bank, net	(39,719)	85,548	21,814
Protected borrower stock retired	(49)	(129)	(124)
Capital stock and participation certificates issued	228	239	216
Capital stock and participation certificates retired	(188)	(299)	(177)
Patronage refunds paid	(3,038)	(2,793)	(2,418)
Retained earnings retired	(5,037)	(4,515)	(4,702)
Net cash provided by (used in) financing activities	(47,803)	78,051	14,609
Net increase (decrease) in cash	(736)	596	119
Cash, beginning of period	799	203	84
Cash, end of period	\$ 63	\$ 799	\$ 203
Supplemental schedule of non-cash activities:			
Cash dividends or patronage distributions declared or payable	\$ 3,554	\$ 2,808	\$ 2,727
Decrease (increase) in accumulated other comprehensive income related to minimum pension liability	—	—	2,925
Supplemental information:			
Interest paid	\$ 20,795	\$ 13,810	\$ 9,428
Taxes paid, net	4	38	194

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

Notes to the Consolidated Financial Statements

(dollars in thousands, except as noted)

Note 1 — Organization and Operations

A. **Organization:** Farm Credit of Central Florida, ACA (the Association or ACA) is a member-owned cooperative which provides credit and credit-related services to or for the benefit of eligible borrowers/shareholders for qualified purposes in the counties of Brevard, Citrus, Hernando, Hillsborough, Lake, Orange, Osceola, Pasco, Pinellas, Polk, Seminole, Sumter, and Volusia in the state of Florida.

The Association is a lending institution of the Farm Credit System (System), a nationwide system of cooperatively owned banks and associations, which was established by Acts of Congress to meet the credit needs of American agriculture and is subject to the provisions of the Farm Credit Act of 1971, as amended (Farm Credit Act). The most recent significant amendment to the Farm Credit Act was the Agricultural Credit Act of 1987. At December 31, 2006, the System was comprised of four Farm Credit Banks, one Agricultural Credit Bank and ninety-six Associations.

AgFirst Farm Credit Bank (Bank) and its related Associations are collectively referred to as the "District." The Bank provides funding to all associations within the District and is responsible for supervising certain activities of the Association, as well as the other Associations operating within the District. The District consists of the Bank and twenty-three Agricultural Credit Associations (ACAs), all of which have reorganized as ACA parent-companies, which have two wholly owned subsidiaries, a Federal Land Credit Association (FLCA) and a Production Credit Association (PCA). FLCAs are tax-exempt while ACAs and PCAs are taxable.

Effective January 1, 2005, pursuant to a plan of restructuring approved by the Farm Credit Administration (FCA) and Association shareholders, the Association reorganized its existing organizational structure. Prior to the restructuring, the ACA was subject to federal and state income tax. Pursuant to this restructuring, a FLCA and a PCA were formed as wholly owned subsidiaries of the Association. The formation of these subsidiaries enables the Association to take advantage of the tax-exempt status of net income from long-term mortgage operations of the FLCA. This restructuring was accounted for as a reorganization of entities under common control similar to a pooling of interests.

ACA parent-companies provide financing and related services through its FLCA and PCA subsidiaries. The FLCA makes collateralized long-term agricultural real estate and rural home mortgage loans. The PCA is authorized to make short- and intermediate-term loans for agricultural production or operating purposes; however, the Association is operating its short- and intermediate-term business through the ACA instead of the PCA.

The Farm Credit Administration (FCA) is delegated authority by Congress to regulate the System banks and associations. The FCA examines the activities of the associations and certain actions by the associations are subject to the prior approval of the FCA and the supervising Bank.

The Farm Credit Act established the Farm Credit System Insurance Corporation (Insurance Corporation) to administer the Farm Credit Insurance Fund (Insurance Fund). The Insurance Fund is required to be used (1) to ensure the timely payment of principal and interest on Systemwide debt obligations (Insured debt), (2) to ensure the retirement of protected borrower capital at par or stated value, and (3) for other specified purposes. The Insurance Fund is also available for discretionary uses by the Insurance Corporation to provide assistance to certain troubled System institutions and to cover the operating expenses of the Insurance Corporation. Each System bank is required to pay premiums, which may be passed on to the Association, into the Insurance Fund, based on its annual average loan principal outstanding until the monies in the Insurance Fund reach the "secure base amount." The secure base amount is defined in the Farm Credit Act as 2.0 percent of the aggregate insured obligations (Systemwide debt obligations) or such other percentage of the aggregate obligations as the Insurance Corporation in its sole discretion determines to be actuarially sound. When the amount in the Insurance Fund exceeds the secure base amount, the Insurance Corporation is required to reduce premiums, but it still must ensure that reduced premiums are sufficient to maintain the level of the Insurance Fund at the secure base amount.

B. **Operations:** The Farm Credit Act sets forth the types of authorized lending activity, persons eligible to borrow, and financial services which can be offered by the Association. The Association is authorized to provide, either directly or in participation with other lenders, credit, credit commitments and related services to eligible borrowers. Eligible borrowers include farmers, ranchers, producers or harvesters of aquatic products, rural residents, and farm-related businesses.

The Association may sell to any System borrowing member, on an optional basis, credit or term life insurance appropriate to protect the loan commitment in the event of death of the debtor(s). The sale of other insurance necessary to protect a member's farm or aquatic unit is permitted, but limited to hail and multi-peril crop insurance, and insurance necessary to protect the facilities and equipment of aquatic borrowers.

The AgFirst Annual Report to Shareholders, the AgFirst District Annual Report to Shareholders, and the AgFirst District's quarterly reports are available on its web site, www.agfirst.com. Upon request, shareholders of the Association will be provided with copies of these reports at no charge by calling 1-800-845-1745, Ext. 316. The

Association's financial condition may be impacted by factors that affect the Bank. The Bank's Annual Report discusses the material aspects of the District's financial condition, changes in financial condition, and results of operations. In addition, the District's Annual Report identifies favorable and unfavorable trends, significant events, uncertainties and the impact of activities of the Insurance Corporation.

The lending and financial services offered by the Bank are described in Note 1 of the AgFirst Annual Report to Shareholders.

Note 2 — Summary of Significant Accounting Policies

The accounting and reporting policies of the Association conform with accounting principles generally accepted in the United States of America (GAAP) and prevailing practices within the banking industry. The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the amounts reported in the consolidated financial statements and accompanying notes. Significant estimates are discussed in these footnotes, as applicable. Actual results may differ from these estimates.

The consolidated financial statements include the accounts of the FLCA and the PCA. All significant inter-company transactions have been eliminated in consolidation.

- A. **Cash:** Cash, as included in the statements of cash flows, represents cash on hand and on deposit at banks.
- B. **Investment Securities:** The Association, as permitted under the FCA regulations, holds investments to manage and diversify its income sources. The Association's investments are classified as held to maturity and accordingly have been reported at amortized cost. Premiums and discounts are amortized or accreted ratably over the term of the respective security. In addition, the Association may also hold additional investments in accordance with mission-related investment programs, approved by the FCA.

The Association reviews all investments that are in a loss position in order to determine whether the unrealized loss, which is considered an impairment, is temporary or permanent. In the event of permanent impairment, the cost basis of the investment would be written down to its fair value, and the realized loss would be included in current earnings.

- C. **Loans and Allowance for Loan Losses:** Long-term real estate mortgage loans generally have original maturities ranging from 5 to 30 years. Substantially all short- and intermediate-term loans for agricultural production or operating purposes have maturities of 10 years or less. Loans are carried at their principal amount outstanding less unearned income. Interest on loans is accrued and credited to interest income based upon the daily principal amount outstanding.

Loans are generally placed in nonaccrual status when principal or interest is delinquent for 90 days (unless adequately collateralized and in the process of collection) or circumstances indicate that collection of principal and/or interest is in doubt. When a loan is placed in nonaccrual

status, accrued interest deemed uncollectible is reversed (if accrued in the current year) or charged against the allowance for loan losses (if accrued in the prior year).

When loans are in nonaccrual status, the interest portion of payments received in cash is recognized as interest income if collection of the recorded investment in the loan is fully expected and the loan does not have a remaining unrecovered prior charge-off associated with it. Otherwise, loan payments are applied against the recorded investment in the loan. Nonaccrual loans may be returned to accrual status when principal and interest are current, prior charge-offs have been recovered, the ability of the borrower to fulfill the contractual repayment terms is fully expected and the loan is not classified "doubtful" or "loss."

Loans are charged-off, wholly or partially, as appropriate, at the time they are determined to be uncollectible.

In cases where a borrower experiences financial difficulties and the Association makes certain monetary concessions to the borrower through modifications to the contractual terms of the loan, the loan is classified as a restructured loan. If the borrower's ability to meet the revised payment schedule is uncertain, the loan is classified as a nonaccrual loan.

Loan origination fees and direct loan origination costs are deferred as part of the carrying amount of the loan and the net fee or cost is amortized over the life of the related loan as an adjustment to interest income.

The allowance for loan losses is a valuation account used to reasonably estimate loan and lease losses existing as of the financial statement date. Determining the appropriate allowance for loan losses balance involves significant judgment about when a loss has been incurred and the amount of that loss.

The 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. It is based on estimates, appraisals and evaluations of loans which, by their nature, contain elements of uncertainty and imprecision. The possibility exists that changes in the economy and its impact on borrower repayment capacity will cause these estimates, appraisals and evaluations to change.

The level of allowance for loan losses is generally based on recent charge-off experience adjusted for relevant environmental factors. The Association considers the following factors when adjusting the historical charge-offs experience:

- Changes in credit risk classifications,
- Changes in collateral values,
- Changes in risk concentrations,
- Changes in weather related conditions, and
- Changes in economic conditions.

Impaired loans are loans for which it is probable that not all principal and interest will be collected according to the contractual terms of the loan. Impaired loans include nonaccrual loans, restructured loans, and loans past due 90 days or more and still accruing interest. A loan is considered contractually past due when any principal repayment or interest payment required by the loan instrument is not

received on or before the due date. A loan shall remain contractually past due until it is formally restructured or until the entire amount past due, including principal, accrued interest, and penalty interest incurred as the result of past due status, is collected or otherwise discharged in full.

A specific allowance may be established for impaired loans under Statement of Financial Accounting Standards No. 114. Impairment of these loans is measured based on the present value of expected future cash flows discounted at the loan's effective interest rate or, as practically expedient, at the loan's observable market price or fair value of the collateral if the loan is collateral dependent. See Note 3 for a discussion on the refinement of the allowance for loan losses methodology.

The allowance for loan losses is maintained at a level considered adequate by management to provide for probable and estimable losses inherent in the loan portfolio. The allowance is increased through provisions for loan losses and loan recoveries and is decreased through allowance reversals and loan charge-offs.

- D. **Gains/(Losses) on Loans Held for Sale:** Certain rural home loans originated by the Association are sold on a servicing released basis primarily to the Bank or into the secondary market to unrelated third parties. For loans sold to the Bank, the Association locks into a selling price with the Bank at the time that the Association enters into a commitment to lend to the potential borrower. Gains or losses on sales of these mortgage loans are recognized based on the difference between the selling price and the carrying value of the related mortgage loans sold.
- E. **Investment in AgFirst Farm Credit Bank and Other Farm Credit Institutions:** The Association is required to maintain ownership in the Bank in the form of Class B and Class C stock. Accounting for this investment is on the cost plus allocated equities basis. Patronage refunds from the Bank are accrued as earned. The receivable for such patronage refunds is classified as due from AgFirst Farm Credit Bank.
- F. **Other Property Owned:** Other property owned, consisting of real and personal property acquired through a collection action, is recorded upon acquisition at fair value less estimated selling costs. Revised estimates to the fair value less cost to sell are reported as adjustments to the carrying amount of the asset, provided that such adjusted value is not in excess of the carrying amount at acquisition. Income and expenses from operations and carrying value adjustments are included in gains (losses) on other property owned, net.
- G. **Premises and Equipment:** Premises and equipment are carried at cost less accumulated depreciation. Land is carried at cost. Depreciation is provided on the straight-line method over the estimated useful lives of the assets. Gains and losses on dispositions are reflected in current operations. Maintenance and repairs are charged to operating expense and improvements are capitalized.
- H. **Advanced Conditional Payments:** The Association is authorized under the Farm Credit Act to accept advance payments from borrowers. To the extent the borrower's access to such advance payments is restricted, the advanced

conditional payments are netted against the borrower's related loan balance. Amounts in excess of the related loan balance and amounts to which the borrower has unrestricted access are presented as interest-bearing liabilities in the accompanying consolidated balance sheets. Advanced conditional payments are not insured. Interest is generally paid by the Association on such accounts.

- I. **Employee Benefit Plans:** Substantially all employees of the Association may participate in the retirement plan (Plan) of the AgFirst District, which is a defined benefit plan. The District utilizes the "Projected Unit Credit" actuarial method for financial reporting purposes and for funding purposes. As a result of the funded status at the Plan's measurement date (September 30) of the underlying Plan, the Association may record a minimum liability, an intangible asset relating to unrecognized prior service cost and other comprehensive income (loss). The adjustment to other comprehensive income (loss) would be net of deferred taxes, if significant. For participants hired before January 1, 2003, benefits are determined based on a final average pay formula. For those participants hired on or after January 1, 2003, benefits are determined using a cash balance formula.

Substantially all employees of the Association may also be eligible to participate in the District's thrift plan (Thrift Plan), which qualifies as a 401(k) plan as defined by the Internal Revenue Code. For employees hired on or prior to December 31, 2002, the Association contributes \$.50 for each \$1.00 of the maximum employee contribution of 6 percent of total compensation. For employees hired on or after January 1, 2003, the Association contributes \$1.00 for each \$1.00 of the maximum employee contribution of 6 percent of total compensation. Employee deferrals are not to exceed the maximum deferral as adjusted by the Internal Revenue Service. Thrift Plan costs are expensed as funded.

Effective January 1, 2006 the Districtwide 401(k) Plan known as the AgFirst Farm Credit Employee Thrift Plan merged with the Farm Credit Bank of Texas Thrift Plus Plan. The new plan is known as the AgFirst/FCBT 401(k) Employee Benefit Plan.

The Association may provide certain health care and life insurance benefits to eligible retired employees. Substantially all employees may become eligible for these benefits if they reach early retirement age while working for the Association.

- J. **Income Taxes:** Effective January 1, 2005, the Association formed a tax exempt subsidiary as described in Note 1. The Association is generally subject to Federal and certain other income taxes. As previously described, the ACA holding company has two wholly-owned subsidiaries, a PCA and a FLCA. The FLCA subsidiary is exempt from federal and state income taxes as provided in the Farm Credit Act. The ACA holding company and the PCA subsidiary are subject to federal, state and certain other income taxes.

The Association is eligible to operate as a cooperative that qualifies for tax treatment under Subchapter T of the Internal Revenue Code. Accordingly, under specified conditions, the Association 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 taxable earnings that will not be distributed as qualified patronage refunds. The Association distributes patronage on the basis of book income.

The Association accounts for income taxes under the asset and liability method, recognizing deferred tax assets and liabilities for the expected future tax consequences of the temporary differences between the carrying amounts and tax bases of assets and liabilities. Deferred tax assets and liabilities are measured using enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be realized or settled.

The Association records a valuation allowance at the balance sheet dates against that portion of the Association's deferred tax assets that, based on management's best estimates of future events and circumstances, more likely than not (a likelihood of more than 50 percent) will not be realized. The consideration of valuation allowances involves various estimates and assumptions as to future taxable earnings, including the effects of our expected patronage program, which reduces taxable earnings.

K. Patronage Refund from AgFirst and Other Financial Institutions: The Association records patronage refunds from the Bank and certain District Associations on an accrual basis.

L. Recently Issued Accounting Pronouncements: In June 2006, the Financial Accounting Standards Board (FASB) released Interpretation No. 48, *Accounting for Uncertainty in Income Taxes* (FIN 48). FIN 48 clarifies the accounting for uncertainty in income taxes recognized in an enterprise's financial statements in accordance with FASB Statement No. 109, *Accounting for Income Taxes*. FIN 48 prescribes a recognition threshold and measurement attribute for the financial statement recognition and measurement of a tax position taken or expected to be taken in a tax return. FIN 48 is effective for fiscal years beginning after December 15, 2006. Adoption of FIN 48 is not expected to have a material impact on the Association's Consolidated Balance Sheet or Consolidated Statement of Income.

On September 30, 2006, the FASB issued Statement of Financial Accounting Standards No. 158, *Employers' Accounting for Defined Benefit Pension and Other Postretirement Plans* (FAS 158). FAS 158 requires an employer to recognize the overfunded or underfunded status of a defined benefit postretirement plan as an asset or liability in its statement of financial position and recognize through comprehensive income changes in that funded status in the year in which the changes occur. The Bank and its related Associations will be required to implement FAS 158 for the year ended December 31, 2007. In addition, FAS 158 requires that the funded status of a plan be measured as of the date of the year-end financial statements. Currently, the Bank and its related Associations use a measurement date of September 30th. The requirement to measure the funded status as of the fiscal year-end is effective for fiscal years ending after December 15, 2008. The Bank and its related Associations are currently evaluating the impact of implementing FAS 158.

Note 3 — Refinement of the Allowance for Loan Losses Methodology

During 2004, the Association conducted a study to further refine its allowance for loan losses methodology taking into account recently issued guidance by FCA, as well as the Securities and Exchange Commission (SEC) and Federal Financial Institutions Examination Council guidelines.

Previously, the Association's allowance for loan losses methodology had been based upon criteria developed in the late 1980s and reflected the credit losses experienced in the mid-to-late 1980s, which was a period of unusually adverse economic conditions in American agriculture. Given the long cyclical nature of the agricultural economy, loss factors utilized to determine the allowance for loan losses subsequent to 1989 continued to reflect, to some extent, the loss history of the mid-to-late 1980s, which resulted in conservative estimates of the allowance for loan losses. The Association's allowance for loan losses methodology utilized throughout the period was in accordance with generally accepted accounting principles and was consistently applied.

While conservative in estimating the allowance for loan losses, the methodology used resulted in annual provisions for loan losses over the periods that reflected changes in credit quality and loss experience. Accordingly, the reserves provided in the mid-to-late 1980s have, in effect, remained part of the allowance for loan losses. The Association's allowance for loan losses methodology has consistently adhered to proper accounting policies, under the regulatory supervision of FCA in its role as a "safety and soundness" regulator. It was FCA's view that the allowance for loan losses should include among others, an assessment of probable losses, historical loss experience and economic conditions.

In April 2004, FCA issued an "Informational Memorandum" to System institutions regarding the criteria and methodologies that would be used in evaluating the adequacy of a System institution's allowance for loan losses. FCA endorsed the direction provided by other bank regulators and the SEC and indicated the conceptual framework addressed in their guidance would be included as part of their examination process.

During the fourth quarter of 2004, the Association completed its study and refined its methodology to be in compliance with the guidance discussed in the previous paragraph. The refinement in methodology resulted in a calculated allowance for loan losses that was significantly less than the previously recorded balance due to revised loss factors that are more indicative of actual loss experience in recent years and current borrower analysis.

While the \$8,815 reversal had a significant impact on 2004 results of operations and the previously recorded allowance for loan losses, the refinement in methodology did not have a significant impact on 2006 comparative results of operations and is not expected to have a significant impact in future periods. Additionally, the refinement in methodology did not have a significant impact on the level of the risk bearing capacity of the Association, generally referred to as "risk funds" (capital plus the allowance for loan losses), which totaled \$70,739 at December 31, 2006 (20.26 percent of Association loans), as compared with \$68,590 at December 31, 2005 (17.13 percent of Association loans), and \$66,291 at December 31, 2004 (19.01 percent of Association loans).

Note 4 — Investment Securities

A summary of the amortized cost and fair value of investment securities held to maturity at December 31, 2006 and 2005 follows:

	December 31, 2006				
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value	Yield
Asset backed securities	\$ 38,704	\$ 167	\$ (484)	\$ 38,387	8.51%

	December 31, 2005				
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value	Yield
Asset backed securities	\$ 34,682	\$ 160	\$ (834)	\$ 34,008	7.00%

The Association's investments consist primarily of asset-backed securities (ABSs). These ABSs are rated AAA, as they are guaranteed by the full faith and credit of the United States government. All unrealized losses referenced above are related to changes in interest rates and are not credit related.

The following table shows the fair value and gross unrealized losses for investments in a loss position by the length of time the securities have been in a continuous unrealized loss position at December 31, 2006. The continuous loss position is based on the date the impairment occurred. The unrealized losses on these investments resulted from interest rate volatility and are not credit related. The Association expects to recover substantially all of our cost in these investments. All of these investments were in U.S. government securities and we expect that these securities would not be settled at a price less than their amortized cost. Because the decline in market value was caused by interest rate increases and not credit quality, and because the Association has the ability and intent to hold these investments to maturity, the Association has not recognized any other-than-temporary impairment in connection with these investments.

	Less than 12 Months		Greater than 12 Months	
	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
Asset-backed securities	\$ 348	\$ (16)	\$ 18,914	\$ (468)

A summary of the expected maturity, amortized cost and estimated fair value of investment securities at December 31, 2006, follows:

	Amortized Cost	Fair Value	Weighted Average Yield
In one year or less	\$ 283	\$ 284	8.71%
After one year through five years	3,649	3,628	8.86
After five years through ten years	9,373	9,252	8.59
After ten years	25,399	25,223	8.43
Total	\$ 38,704	\$ 38,387	8.51%

Note 5 — Loans and Allowance for Loan Losses

A summary of loans follows:

	December 31,		
	2006	2005	2004
Real estate mortgage	\$ 189,594	\$ 245,656	\$ 210,512
Production and intermediate term	103,307	104,904	104,419
Agribusiness:			
Loans to cooperatives	1,879	2,520	—
Processing and marketing	20,200	15,913	6,675
Farm related business	2,998	4,417	4,191
Communication	975	985	995
Energy	3,827	4,132	4,298
Rural residential real estate	26,392	21,872	17,663
Total loans	\$ 349,172	\$ 400,399	\$ 348,753

The Association's concentration of credit risk in various agricultural commodities is shown in the following table. While the amounts represent the Association's maximum potential credit risk as it relates to recorded loan principal, a substantial portion of the Association's lending activities is collateralized and the Association's exposure to credit loss associated with lending activities is reduced accordingly. An estimate of the Association's credit risk exposure is considered in the determination of the allowance for loan losses.

Total loans at December 31, 2006, 2005 and 2004 consisted of the following commodity types:

Commodity Type	December 31,		
	2006	2005	2004
Horticulture	31.73%	22.87%	23.84%
Fruits & Vegetables	19.50	24.55	24.73
Livestock	14.79	15.08	15.95
Other	13.80	10.40	9.35
Citrus Fruits	13.48	22.26	20.67
Rural Home	5.83	3.38	3.31
Dairy	.87	1.46	2.15
Total	100.00%	100.00%	100.00%

The amount of collateral obtained, if deemed necessary upon extension of credit, is based on management's credit evaluation of the borrower. Collateral held varies, but typically includes farmland and income-producing property, such as crops and livestock, as well as receivables. Long-term real estate loans are collateralized by the first liens on the underlying real property. Federal regulations state that long-term real estate loans are not to exceed 85 percent (97 percent if guaranteed by a government agency) of the property's appraised value. However, a decline in a property's market value subsequent to loan origination or advances, or other actions necessary to protect the financial interest of the Association in the collateral, may result in the loan to value ratios in excess of the regulatory maximum.

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 relating to impaired loans.

	December 31,		
	2006	2005	2004
Nonaccrual loans:			
Current as to principal and interest	\$ 45	\$ 248	\$ 56
Past due	3,474	2	2
Total nonaccrual loans	<u>3,519</u>	<u>250</u>	<u>58</u>
Impaired accrual loans:			
Restructured accrual loans	199	523	564
Accrual loans 90 days or more past due	—	—	—
Total impaired accrual loans	<u>199</u>	<u>523</u>	<u>564</u>
Total impaired loans	<u>\$3,718</u>	<u>\$ 773</u>	<u>\$ 622</u>

There were no material commitments to lend additional funds to debtors whose loans were classified as impaired at December 31, 2006.

Interest income is recognized and cash payments are applied on nonaccrual impaired loans as described in Note 2. The following table presents interest income recognized on impaired loans.

	Year Ended December 31,		
	2006	2005	2004
Interest income recognized on nonaccrual loans	\$ 28	\$ 27	\$ 167
Interest income on impaired accrual loans	1	4	—
Interest income recognized on impaired loans	<u>\$ 29</u>	<u>\$ 31</u>	<u>\$ 167</u>

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

	2006	2005	2004
	Impaired loans with related allowance	\$ 856	\$ 30
Impaired loans with no related allowance	2,862	743	622
Total impaired loans	<u>\$ 3,718</u>	<u>\$ 773</u>	<u>\$ 622</u>
Allowance on impaired loans	<u>\$ 105</u>	<u>\$ 30</u>	<u>\$ —</u>

The following table summarizes impaired loan information for the year ended December 31,

	2006	2005	2004
Average impaired loans	<u>\$ 2,852</u>	<u>\$ 298</u>	<u>\$ 970</u>

The following table summarizes interest income on nonaccrual and accruing restructured loans that would have been recognized under the original terms of the loans:

	Year Ended December 31,		
	2006	2005	2004
Interest income which would have been recognized under the original loan terms	\$ 265	\$ 32	\$ 173
Less: interest income recognized	28	27	167
Foregone interest income	<u>\$ 237</u>	<u>\$ 5</u>	<u>\$ 6</u>

The changes in the allowance for loan losses are as follows:

	Year Ended December 31,		
	2006	2005	2004
Balance at beginning of year	\$ 2,133	\$ 1,954	\$ 10,642
Charge-offs:			
Production and intermediate term	\$ (3)	\$ (3)	\$ —
Agribusiness	(6)	—	—
Total charge-offs	<u>(9)</u>	<u>(3)</u>	<u>—</u>
Recoveries:			
Production and intermediate term	\$ 18	\$ 114	\$ 127
Agribusiness	109	—	—
Total recoveries	<u>127</u>	<u>114</u>	<u>127</u>
Net (charge-offs) recoveries	<u>118</u>	<u>111</u>	<u>127</u>
Provision for (reversal of allowance for) loan losses	\$ (612)	\$ 68	\$ —
Nonrecurring allowance for loan losses reversal	—	—	(8,815)
	<u>(612)</u>	<u>68</u>	<u>(8,815)</u>
Balance at end of year	<u>\$ 1,639</u>	<u>\$ 2,133</u>	<u>\$ 1,954</u>
Ratio of net recoveries during the period to average loans outstanding during the period	<u>0.03%</u>	<u>0.03%</u>	<u>0.04%</u>

As previously discussed in Note 3, the nonrecurring allowance for loan losses reversal resulted from the refinement of the Association's allowance for loan losses methodology.

In addition, the following is a breakdown of the allowance for loan losses for the end of the last three fiscal years:

	December 31, 2006		December 31, 2005	
	Amount	%	Amount	%
Real estate mortgage	\$ 891	54%	\$ 1,308	61%
Production and intermediate term	485	30	559	26
Agribusiness	117	7	122	6
Communication	5	—	5	—
Energy	18	1	22	2
Rural residential real estate	123	8	117	5
Total	<u>\$ 1,639</u>	<u>100%</u>	<u>\$ 2,133</u>	<u>100%</u>
	December 31, 2004			
	Amount	%		
Real estate mortgage	\$ 1,180	60%		
Production and intermediate term	585	30		
Agribusiness	60	3		
Communication	6	—		
Energy	24	2		
Rural residential real estate	99	5		
Total	<u>\$ 1,954</u>	<u>100%</u>		

Note 6 — Investment in AgFirst Farm Credit Bank

The Association is required to maintain ownership in the Bank of Class B and Class C stock as determined by the Bank. The Bank may require additional capital contributions to maintain its capital requirements.

Note 7 — Premises and Equipment

Premises and equipment consisted of the following:

	December 31,		
	2006	2005	2004
Land	\$ 224	\$ 224	\$ 306
Buildings and improvements	831	814	1,277
Furniture and equipment	1,261	1,218	1,148
	<u>2,316</u>	<u>2,256</u>	<u>2,731</u>
Less: accumulated depreciation	1,177	1,149	1,368
Total	<u>\$ 1,139</u>	<u>\$ 1,107</u>	<u>\$ 1,363</u>

The Association is obligated under various noncancellable operating leases for automobiles and offices. At December 31, 2006, future minimum lease payments for all noncancellable operating leases are as follows:

2007	\$ 323
2008	333
2009	343
20010	328
2011	338
Subsequent years	<u>1,846</u>
Total minimum lease payments	<u>\$ 3,511</u>

Note 8 — Notes Payable to AgFirst Farm Credit Bank

The Association's indebtedness to the Bank represents borrowings by the Association to fund its loan portfolio. This indebtedness is collateralized by a pledge of substantially all of the Association's assets and the terms of the revolving lines of credit are governed by a general financing agreement. Interest rates on both variable and fixed rate notes payable are generally established loan-by-loan based on the Bank's marginal cost of funds, capital position, operating costs and return objectives. The interest rate is periodically adjusted by the Bank based upon agreement between the Bank and Association. The weighted average interest rates on the variable rate notes were 6.25 percent for LIBOR-based loans, 6.47 percent for Prime-based loans, and the weighted average remaining maturities were 4.1 years and 4.0 years, respectively, at December 31, 2006. The weighted average interest rate on the fixed rate and adjustable rate mortgage (ARM) notes payable which are match funded by the Bank was 5.92 percent and the weighted average remaining maturity was 8.6 years at December 31, 2006. The weighted average interest rate on all interest-bearing notes payable was 6.11 percent and the weighted average remaining maturity was 6.5 years at December 31, 2006.

Variable rate and fixed rate notes payable represent approximately 36.08 percent and 63.92 percent, respectively, of total notes payable at December 31, 2006.

Under the Farm Credit Act, the Association is obligated to borrow only from the Bank, unless the Bank approves borrowing from other funding sources. The Bank, consistent with FCA regulations, has established limitations on the Association's ability to borrow funds based on specified factors or formulas relating primarily to credit quality and financial condition. At December 31, 2006, the Association's notes payable were within the specified limitations.

Note 9 — Members' Equity

A description of the Association's capitalization requirements, protection mechanisms, regulatory capitalization requirements and restrictions, and equities are provided below.

A. Protected Borrower Equity

Protection of certain borrower equity is provided under the Farm Credit Act which requires the Association, when retiring protected borrower equity, to retire such equity at par or stated value regardless of its book value. Protected borrower equity includes capital stock, participation certificates and allocated equities which were outstanding as of January 6, 1988, or were issued or allocated prior to October 6, 1988. If an Association is unable to retire protected borrower equity at par value or stated value, amounts required to retire this equity would be obtained from the Insurance Fund.

B. Capital Stock and Participation Certificates

In accordance with the Farm Credit Act and the Association's capitalization bylaws, each borrower is required to invest in Class C stock for agricultural loans, or participation certificates in the case of rural home and farm related business loans, as a condition of borrowing. The initial borrower investment, through either purchase or transfer, must be in an amount equal to the lesser of \$1 thousand or two percent of the amount of the loan. The Board of Directors may increase the amount of investment if necessary to meet the Association's capital needs. Loans designated for sale or sold into the Secondary Market on or after April 16, 1996 will have no voting stock or participation certificate purchase requirement if sold within 180 days following the date of designation.

The borrower acquires ownership of the capital stock or participation certificates at the time the loan is made, but usually does not make a cash investment. The aggregate par value is generally added to the principal amount of the related loan obligation. The Association retains a first lien on the stock or participation certificates owned by borrowers. Retirement of such equities will generally be at the lower of par or book value, and repayment of a loan does not automatically result in retirement of the corresponding stock or participation certificates.

C. Regulatory Capitalization Requirements and Restrictions

FCA's capital adequacy regulations require the Association to achieve permanent capital of seven percent of risk-adjusted assets and off-balance-sheet commitments. Failure to meet the seven percent capital requirement can initiate certain mandatory and possibly additional discretionary actions by FCA that, if undertaken, could have a direct material effect on the Association's financial statements. The Association is prohibited from reducing permanent capital by retiring stock or making certain other distributions to shareholders unless prescribed capital standards are met. FCA regulations also require that additional minimum standards for capital be achieved. These standards require all System institutions to achieve and maintain ratios as defined by FCA regulations. These required ratios are total surplus as a percentage of risk-adjusted assets of seven percent and of core surplus as a percentage of risk-adjusted assets of three and one-half

percent. The Association's permanent capital, total surplus and core surplus ratios at December 31, 2006 were 16.55 percent, 15.88 percent and 13.46 percent, respectively.

An FCA regulation empowers it to direct a transfer of funds or equities by one or more System institutions to another System institution under specified circumstances. The Association has not been called upon to initiate any transfers and is not aware of any proposed action under this regulation.

D. Description of Equities

The Association is authorized to issue or have outstanding Classes A and D Preferred Stock, Classes A, B and C Common Stock, Classes B and C Participation Certificates and such other classes of equity as may be provided for in amendments to the bylaws in such amounts as may be necessary to conduct the Association's business. All stock and participation certificates have a par or face value of five dollars (\$5.00) per share.

The Association had the following shares outstanding at December 31, 2006:

Class	Protected	Shares Outstanding	
		Number	Aggregate Par Value
B Common/Nonvoting	Yes	17,452	\$ 87
C Common/Voting	No	200,149	1,001
B Participation Certificates/Nonvoting	Yes	1,993	10
C Participation Certificates/Nonvoting	No	41,656	208
Total Capital Stock and Participation Certificates		261,250	\$ 1,306

Protected common stock and participation certificates are retired at par or face value in the normal course of business. At-risk common stock and participation certificates are retired at the sole discretion of the Board at book value not to exceed par or face amounts, provided the minimum capital adequacy standards established by the Board are met.

Retained Earnings

The Association maintains an unallocated retained earnings account and an allocated retained earnings account. The minimum aggregate amount of these two accounts is determined by the Board. At the end of any fiscal year, if the retained earnings accounts otherwise would be less than the minimum amount determined by the Board as necessary to maintain adequate capital reserves to meet the commitments of the Association, the Association shall apply earnings for the year to the unallocated retained earnings account in such amounts as may be determined necessary by the Board. Unallocated retained earnings are maintained for each borrower to permit liquidation on a patronage basis.

The Association maintains an allocated retained earnings account consisting of earnings held and allocated to borrowers on a patronage basis. In the event of a net loss for any fiscal year, such allocated retained earnings account will be subject to full impairment in the order specified in the bylaws beginning with the most recent allocation.

The Association has a first lien and security interest on all retained earnings account allocations owned by any borrowers, and all distributions thereof, as additional collateral for their indebtedness to the Association. When the debt of a borrower is in default or is in the process of final liquidation by payment or otherwise, the Association, upon approval of the Board, may order any and all retained earnings account allocations owned by such borrower to be applied on the indebtedness.

Allocated equities shall be retired solely at the discretion of the Board; provided, however, that minimum capital standards established by the FCA and the Board are met.

At December 31, 2006, allocated members' equity consisted of \$16,753 of qualified and \$12,242 of nonqualified allocated surplus distributions. Nonqualified distributions are tax deductible only when redeemed.

Dividends

The Association may declare noncumulative dividends on its capital stock and participation certificates provided the dividend rate does not exceed 20 percent of the par value of the respective capital stock and participation certificates. Such dividends may be paid solely on Classes A and D Preferred Stock, or on all classes of stock and participation certificates.

The rate of dividends paid on Class A Preferred Stock for any fiscal year may not be less than the rate of dividends paid on Classes A, B or C Common Stock or participation certificates for such year. The rate of dividends on Classes A, B and C Common Stock and participation certificates shall be at the same rate per share.

Dividends may not be declared if, after recording the liability, the Association would not meet its capital adequacy standards. No dividends were declared by the Association for any of the periods included in these consolidated financial statements.

Patronage Distributions

Prior to the beginning of any fiscal year, the Board, by adoption of a resolution, may obligate the Association to distribute to borrowers on a patronage basis all or any portion of available net earnings for such fiscal year or for that and subsequent fiscal years. Patronage distributions are based on the proportion of the borrower's interest to the amount of interest earned by the Association on its total loans unless another proportionate patronage basis is approved by the Board.

If the Association meets its capital adequacy standards after making the patronage distributions, the patronage distributions may be in cash, authorized stock of the Association, allocations of earnings retained in an allocated members' equity account, or any one or more of such forms of distribution. Patronage distributions of the Association's earnings may be paid on either a qualified or nonqualified basis, or a combination of both, as determined by the Board. A minimum of 20 percent of the total qualified patronage distribution to any borrower for any fiscal year shall always be paid in cash.

Transfer

Classes A and D Preferred, Classes A, B and C Common Stocks, and Classes B and C Participation Certificates may be transferred to persons or entities eligible to purchase or hold such equities.

Impairment

Any net losses recorded by the Association shall first be applied against unallocated members' equity. To the extent that such losses would exceed unallocated members' equity, such losses would be applied consistent with the Association's bylaws and distributed pro rata to each share and/or unit outstanding in the class, in the following order:

- a) **First**, Assistance Preferred Stock issued and outstanding (if any);
- b) **Second**, allocated surplus evidenced by nonqualified written notices of allocation, in its entirety, with application to most recent allocation first and then in reverse order until all such allocated surplus has been exhausted;
- c) **Third**, allocated surplus evidenced by qualified written notices of allocation, in its entirety, with application to most recent allocation first and then in reverse order until all such allocated surplus has been exhausted;
- d) **Fourth**, Class A Common and Class B Common Stock, Class C Common Stock, Class E Common Stock, Class C Participation Certificates and Class B Participation Certificates issued and outstanding, pro rata until such stock is fully impaired;
- e) **Fifth**, Class A Preferred and Class D Preferred Stock issued and outstanding, if any.

Liquidation

In the event of liquidation or dissolution of the Association, any assets of the Association remaining after payment or retirement of all liabilities should be distributed to the holders of the outstanding stock and participation certificates in the following order:

- a) **First**, to the holders of Class A Preferred and Class D Preferred Stock until an amount equal to the aggregate par value of all shares of said stock then issued and outstanding has been distributed to such holders;
- b) **Second**, to the holders of Class A Common, Class B Common, Class C Common Stock, Class E Common Stock, and Class B Participation Certificates and Class C Participation Certificates, pro rata in proportion to the number of shares or units of each such class of stock or participation certificate then issued and outstanding, until an amount equal to the aggregate par value or face amount of all such shares or units has been distributed to such holders;
- c) **Third**, to the holders of allocated surplus evidenced by qualified written notices of allocation, in the order of year of issuance and pro rata by year of issuance, until the total amount of such allocated surplus has been distributed;

- d) **Fourth**, to the holders of allocated surplus evidenced by nonqualified written notices of allocation, in the order of year of issuance and pro rata by year of issuance, until the total amount of such allocated surplus has been distributed;
- e) **Fifth**, in so far as practicable, all unallocated surplus issued after April 15, 1999, shall be distributed to Patrons of the Association from the period beginning April 15, 1999, through the date of liquidation, on a patronage basis; and
- f) **Sixth**, any remaining assets of the Association after such distributions shall be distributed ratably to the holders of all classes of stock and participation certificates in proportion to the number of shares or units of such class of stock or participation certificates held by such holders.

All distributions to the holders of any class of stock and/or participation certificate holders shall be made pro rata in proportion to the number of shares or units of such class of stock or participation certificates held by such holders.

E. Other Comprehensive Income (Loss)

The Association reports other comprehensive income (loss) in its Consolidated Statements of Changes in Members' Equity. During 2004, the District Associations funded the pension plans sufficiently to eliminate the pension-related component of other comprehensive income (loss) at December 31, 2004. See Note 11 for further information.

Note 10 — Income Taxes

The provision (benefit) for income taxes follows:

	Year Ended December 31,		
	2006	2005	2004
Current:			
Federal	\$ —	\$ 24	\$ 79
State	—	4	15
	<u>—</u>	<u>28</u>	<u>94</u>
Deferred:			
Federal	12	24	1
State	1	4	—
	<u>13</u>	<u>28</u>	<u>1</u>
Total provision (benefit) for income taxes	<u>\$ 13</u>	<u>\$ 56</u>	<u>\$ 95</u>

The provision (benefit) for income tax differs from the amount of income tax determined by applying the applicable U.S. statutory federal income tax rate to pretax income as follows:

	December 31,		
	2006	2005	2004
Federal tax at statutory rate	\$ 3,902	\$ 3,323	\$ 5,493
State tax, net	1	5	10
Effect of non-taxable FLCA subsidiary	(3,127)	(2,521)	—
Patronage distributions	(1,228)	(707)	(2,433)
Allowance for loan loss adjustment	—	—	(2,997)
Change in valuation allowance	530	24	—
Bank equity redemption	—	—	56
Other	(65)	(68)	(34)
Provision (benefit) for income taxes	<u>\$ 13</u>	<u>\$ 56</u>	<u>\$ 95</u>

Deferred tax assets and liabilities result from the following at:

	December 31,		
	2006	2005	2004
Deferred income tax assets:			
Allowance for loan losses	\$ 274	\$ 261	\$ -
Annual leave	-	49	8
Nonaccrual loan interest	6	-	-
Postretirement benefits other than pensions	-	309	51
Alternative minimum tax credit carryforward	-	-	19
Deferred incentive	-	16	8
Loss carryforward	334	-	-
Other	-	11	4
Gross deferred tax assets	614	646	90
Less: valuation allowance	(554)	(24)	-
Gross deferred tax assets, net of valuation allowance	60	622	90
Deferred income tax liabilities:			
Future Bank equity redemption	-	-	(22)
Loan origination fees	(60)	(60)	-
Pensions	-	(548)	(26)
Gross deferred tax liability	(60)	(608)	(48)
Net deferred tax asset (liability)	\$ -	\$ 14	\$ 42

At December 31, 2006, deferred income taxes have not been provided by the Association on approximately \$1.2 million of patronage refunds received from the Bank prior to January 1, 1993. Such refunds, distributed in the form of stock, are subject to tax only upon conversion to cash. The tax liability related to future conversions is not expected to be material.

The Association recorded a valuation allowance of \$554 and \$24 during 2006 and 2005, respectively. The Association will continue to evaluate the realizability of these deferred tax assets and adjust the valuation allowance accordingly.

Note 11 — Employee Benefit Plans

The employees of the Association may participate in a Districtwide defined benefit retirement plan. This plan is noncontributory and covers substantially all Association employees. Benefits are based on salary and years of service. The assets, liabilities and costs of the plan are not segregated by participating entities but are allocated among the participating entities. Pension costs are allocated by multiplying the District's net pension expense times the Association's salary expense as a percentage of the District's salary expense.

The Association participates in a Districtwide Thrift Plan. For employees hired on or prior to December 31, 2002, the Association will contribute \$.50 for each \$1.00 of the maximum employee contribution of 6 percent of total compensation. For employees hired on or after January 1, 2003, the Association will contribute \$1.00 for each \$1.00 of the maximum employee contribution of 6 percent of total compensation. Employee deferrals are not to exceed the maximum deferral as adjusted by the Internal Revenue Service.

The District sponsors a plan providing certain benefits (primarily health care) to its retirees. Certain Association charges related to this plan are an allocation of District charges based on the Association's proportional share of the plan liability.

On December 8, 2003, the Medicare Prescription Drug, Improvement and Modernization Act of 2003 (Medicare Act) was signed into law. This act introduces a prescription drug benefit under Medicare (Medicare Part D) as well as a federal subsidy to sponsors of retiree health care benefit plans that provide a benefit that is at least actuarially equivalent to Medicare Part D. In May 2004, the FASB issued FASB Staff Position (FSP) 106-2, Accounting and Disclosure Requirements Related to the Medicare Prescription Drug, Improvement and Modernization Act of 2003" (the Act). This Staff Position provides guidance on the accounting for the effects of the Act for employers that sponsor postretirement health care plans that provide prescription drug benefits. The District sponsored plan adopted FSP 106-2 effective July 1, 2004 (measured as of March 31, 2004). The benefit obligation valuation as of December 31, 2004 reflects the impact of the Medicare Act.

In determining the benefit obligation as of December 31, 2004, the expected per capita claims cost were estimated to be reduced by 12 percent beginning in 2006, for Medicare-eligible participants receiving actuarially equivalent drug benefits, due to a government reimbursement of a portion of prescription drug benefits. The District reduced its accumulated postretirement benefit obligation (APBO) for the subsidy related to benefits attributed to past service. The effect of the subsidy on the measurement of net periodic postretirement cost for 2005 was a reduction of 2005 expense. The effect included lower amortization of actuarial losses, lower service costs and lower interest costs on the APBO.

The Retiree and Disabled Medical Plan was amended effective January 1, 2006 to change the medical and prescription drug coverage for Medicare-eligible retirees and/or eligible spouses 65 years and older. Beginning in 2006, the AgFirst/FCBT Retiree and Disabled Medical Plan will provide medical and prescription drug coverage to Medicare-eligible retirees and/or eligible spouses 65 years and older through fully-insured AARP endorsed Medicare Supplement policies and subsidized basic Medicare D coverage through a selected Prescription Drug Plan. Dental coverage was not changed. Certain other retirees who are grandfathered under insured arrangements were not impacted by the change. The benefit obligation valuation as of December 31, 2005 reflects the impact of this plan amendment.

In determining the benefit obligation as of December 31, 2005, there was no impact due to government reimbursement of prescription drug benefits. After the plan amendment, the plan no longer provides prescription drug benefits directly for retirees and/or eligible spouses 65 years and older. Instead, the District subsidizes the cost of coverage obtained under the Medicare D program through the selected Prescription Drug Provider.

For further information on postretirement costs, see "Postretirement Benefits" section in the Notes to the AgFirst Farm Credit District Consolidated Financial Statements.

The following is a table of retirement and postretirement benefits expenses (credits):

	2006	2005	2004
Pension	\$ 527	\$ 527	\$ 615
Thrift/deferred compensation	106	87	83
Other postretirement benefits	173	333	468
Total	<u>\$ 806</u>	<u>\$ 947</u>	<u>\$ 1,166</u>

For the years ended December 31, 2006, 2005 and 2004, the Association had contributed \$1, \$733 and \$3,075, respectively, to the Districtwide defined benefit retirement plan, which was sufficient to meet its accumulated benefit obligation. For 2004, the contributions eliminated the minimum pension liability and the pension-related charge to accumulated other comprehensive income (OCI) in members' equity. As a result of the fundings and the reclassification of the OCI, the Association ended 2006, 2005 and 2004 with \$3,609, \$4,136 and \$3,929, respectively, in Prepaid retirement expense in Other assets on the Consolidated Balance Sheets.

Note 12 — Intra-System Financial Assistance

The Farm Credit Act provided for capital assistance to System institutions experiencing severe financial stress through the issuance, prior to October 1, 1992, by the Financial Assistance Corporation of U.S. Treasury-guaranteed 15-year bonds, of which \$1.261 billion in principal amount was originally issued. The last remaining Financial Assistance Corporation bonds matured and were repaid on June 10, 2005.

Pursuant to the Farm Credit Act, the U.S. Treasury paid \$440 million, on behalf of the System, in interest costs on \$844 million of the Financial Assistance Corporation bonds issued for purposes other than funding Capital Preservation Agreement accruals. The Banks had irrevocably set aside funds, including interest earned, that totaled the \$440 million needed to repay the interest advanced by the U.S. Treasury. On June 10, 2005, the Banks repaid the U.S. Treasury the interest advanced. The Farm Credit Act provided that the Financial Assistance Corporation would continue in existence no longer than two years following the maturity of the debt in June 2005. The Financial Assistance Corporation was dissolved effective as of December 31, 2006.

Note 13 — Related Party Transactions

In the ordinary course of business, the Association enters into loan transactions with officers and directors of the Association, their immediate families and other organizations with which such persons may be associated. Such loans are subject to special approval requirements contained in the FCA regulations and are made on the same terms, including interest rates and collateral, as those prevailing at the time for comparable transactions with unrelated borrowers.

Total loans to such persons at December 31, 2006 amounted to \$8,676. During 2006, \$261 of new loans were made and repayments totaled \$5,720. In the opinion of management, none of these loans outstanding at December 31, 2006 involved more than a normal risk of collectibility.

Note 14 — Commitments and Contingencies

The Association has various commitments outstanding and contingent liabilities.

The Association may participate in financial instruments with off-balance-sheet risk to satisfy the financing needs of its borrowers and to manage their exposure to interest-rate risk. These financial instruments include commitments to extend credit and/or commercial letters of credit. The instruments involve, to varying degrees, elements of credit risk in excess of the amount recognized in the financial statements. Commitments to extend credit are agreements to lend to a borrower as long as there is not a violation of any condition established in the contract. Commercial letters of credit are agreements to pay a beneficiary under conditions specified in the letter of credit. Commitments and letters of credit generally have fixed expiration dates or other termination clauses and may require payment of a fee. At December 31, 2006, \$67,634 of commitments to extend credit were outstanding. No commercial letters of credit were outstanding.

Since many of these commitments are expected to expire without being drawn upon, the total commitments do not necessarily represent future cash requirements. However, these credit-related financial instruments have off-balance-sheet credit risk because their amounts are not reflected on the consolidated balance sheets until funded or drawn upon. The credit risk associated with issuing commitments and letters of credit is substantially the same as that involved in extending loans to borrowers and management applies the same credit policies to these commitments. Upon fully funding a commitment, the credit risk amounts are equal to the contract amounts, assuming that borrowers fail completely to meet their obligations and the collateral or other security is of no value. The amount of collateral obtained, if deemed necessary upon extension of credit, is based on management's credit evaluation of the borrower.

The Association also participates in standby letters of credit to satisfy the financing needs of its borrowers. These letters of credit are irrevocable agreements to guarantee payments of specified financial obligations. Outstanding standby letters of credit have expiration dates ranging from January 4, 2007 to June 5, 2011. The maximum potential amount of future payments the Association is required to make under the guarantees is \$6,963.

Note 15 — Disclosures About Fair Value of Financial Instruments

The following table presents the carrying amounts and fair values of the Association's financial instruments at December 31, 2006, 2005 and 2004. The fair value of a financial instrument is generally defined as the amount at which the instrument could be exchanged in a current transaction between willing parties, other than in a forced or liquidation sale.

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:

	December 31, 2006		December 31, 2005	
	Carrying Amount	Estimated Fair Value	Carrying Amount	Estimated Fair Value
Financial assets:				
Cash	\$ 63	\$ 63	\$ 799	\$ 799
Loans	\$ 349,172	\$ 352,510	\$ 400,399	\$ 399,614
Allowance for loan losses	1,639	—	2,133	—
Loans, net	<u>\$ 347,533</u>	<u>\$ 352,510</u>	<u>\$ 398,266</u>	<u>\$ 399,614</u>
Investment securities	\$ 38,704	\$ 38,387	\$ 34,682	\$ 34,008
Financial liabilities:				
Notes payable to AgFirst Farm Credit Bank	\$ 334,575	\$ 333,609	\$ 374,294	\$ 369,964

	December 31, 2004	
	Carrying Amount	Estimated Fair Value
Financial assets:		
Cash	\$ 203	\$ 203
Loans	\$ 348,753	\$ 350,255
Allowance for loan losses	1,954	—
Loans, net	<u>\$ 346,799</u>	<u>\$ 350,255</u>
Investment securities	\$ —	\$ —
Financial liabilities:		
Notes payable to AgFirst Farm Credit Bank	<u>\$ 288,746</u>	<u>\$ 287,067</u>

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 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. As the discount rates are based on the Bank's loan rates, as well as management estimates, management has no basis to determine whether the fair values presented would be indicative of the value negotiated in an actual sale.

For purposes of determining fair value of accruing loans, the loan portfolio is segregated into pools of loans with homogeneous characteristics 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 less specific reserves.

The carrying value of accrued interest approximates its fair value.

- C. **Investment Securities:** Fair value is based upon quoted broker price.

- D. **Investment in AgFirst Farm Credit Bank and Other Farm Credit Institutions:** Estimating the fair value of the Association's investment in the Bank and Other Farm Credit Institutions is not practicable because the stocks are not traded. As described in Note 6, 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 6.07 percent of the issued stock of the Bank as of December 31, 2006 net of any reciprocal investment. As of that date, the Bank's assets totaled \$24.4 billion and shareholders' equity totaled \$1,181 million. The Bank's earnings were \$190 million during 2006.

In addition, the Association has an investment of \$214 related to other Farm Credit institutions.

- E. **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.
- F. **Commitments to Extend Credit and Standby Letters of 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.

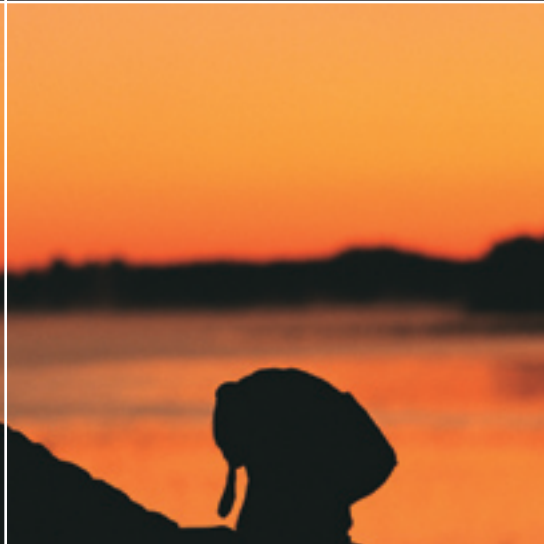
Note 16 — Quarterly Financial Information (Unaudited)

Quarterly results of operations for the years ended December 31, 2006, 2005 and 2004 follow:

	2006				
	First	Second	Third	Fourth	Total
Net interest income	\$ 2,857	\$ 3,044	\$ 3,088	\$ 2,882	\$ 11,871
Provision for (reversal of allowance for) loan losses	—	—	(112)	(500)	(612)
Noninterest income (expense), net	(592)	(558)	(377)	508	(1,019)
Net income	<u>\$ 2,265</u>	<u>\$ 2,486</u>	<u>\$ 2,823</u>	<u>\$ 3,890</u>	<u>\$ 11,464</u>
	2005				
	First	Second	Third	Fourth	Total
Net interest income	\$ 2,468	\$ 2,598	\$ 2,687	\$ 2,861	\$ 10,614
Provision for (reversal of allowance for) loan losses	—	—	68	—	68
Noninterest income (expense), net	(557)	(600)	(90)	418	(829)
Net income	<u>\$ 1,911</u>	<u>\$ 1,998</u>	<u>\$ 2,529</u>	<u>\$ 3,279</u>	<u>\$ 9,717</u>
	2004				
	First	Second	Third	Fourth	Total
Net interest income	\$ 2,107	\$ 2,101	\$ 2,224	\$ 2,365	\$ 8,797
Provision for (reversal of allowance for) loan losses	—	—	—	(8,815)	(8,815)
Noninterest income (expense), net	(742)	(867)	(246)	304	(1,551)
Net income	<u>\$ 1,365</u>	<u>\$ 1,234</u>	<u>\$ 1,978</u>	<u>\$ 11,484</u>	<u>\$ 16,061</u>



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