

NORTHERN CALIFORNIA FARM CREDIT, ACA



2010
ANNUAL REPORT



The Farm Credit System

Northern California Farm Credit, ACA

CHICO OFFICE

P.O. Box 929, 3435 Silverbell Road
Chico, California 95927
(530) 895-8698, FAX (530) 893-5314

NORTHERN CALIFORNIA FARM CREDIT, ACA 2010 ANNUAL REPORT

CERTIFICATION STATEMENT

The undersigned certify that this statement 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 their knowledge and belief. The undersigned certify the Northern California Farm Credit, ACA Annual Report has been reviewed, 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.

Bruce V. Strickler, President & CEO

George Swaner, Chairman of the Board

Phillip L. Downing, Chief Financial Officer

Signed this Date: March 16, 2011



Northern California Farm Credit, ACA

CHICO OFFICE

P.O. Box 929, 3435 Silverbell Road
Chico, California 95927
(530) 895-8698, FAX (530) 893-5314

MESSAGE FROM THE CHAIRMAN OF THE BOARD AND PRESIDENT

Once again Mr. Swaner and I would like to thank the members, Board of Directors and staff of Northern California Farm Credit for a very successful year. We are glad to report that 2010 was one of the most successful years we have ever enjoyed.

As you are all aware, north state agriculture has also (for the most part) enjoyed a good 2010 and a sound start to 2011. Strong commodity prices and loan values continue to support a healthy agricultural outlook. We are hopeful that input costs and water issues do not dampen this position.

As we have enjoyed for the last decade, your Association is in excellent condition. We continue to have solid credit quality, adequate earnings, and very competitive rates. Our commitment to conservative and constructive credit has served us well and we will continue on this course. The Board of Directors and management of your Association are proud to be leaders in providing this level of financial commitment to the farmers and ranchers in the north state.

As has been our pledge to you in the past, we strive to manage your Association to the benefit of our owners/borrowers. We have, once again, kept our interest rates competitive plus declared patronage payments of \$2.8 million. This payment will bring the total patronage paid since 2001 to just over \$20 million. We are all very proud of this accomplishment and believe it proves that a strong farmer/rancher-owned cooperative can be successful.

As always, we continue to direct our efforts toward improving our services to you. Please don't hesitate to share with any staff member or director your ideas that may help in this endeavor.

In this annual report we try hard to provide you with a true and in-depth financial look at your Association. Please read it carefully and let us know if you have any questions.

Thanks for a rewarding year and we look forward to another successful year for all!

George Swaner, Chairman of the Board

Bruce V. Strickler, President & CEO

Signed this Date: March 16, 2011

Five-Year Summary of Selected Consolidated Financial Data

(Dollars in Thousands)

	December 31				
	2010	2009	2008	2007	2006
Statement of Condition Data					
Loans	\$ 426,709	\$ 436,747	\$ 408,805	\$ 410,891	\$ 380,495
Less allowance for loan losses	2,480	2,294	2,053	2,059	2,131
Net loans	424,229	434,453	406,752	408,832	378,364
Investment in U.S. AgBank, FCB	8,102	8,102	8,102	8,102	8,102
Other property owned	-	-	-	-	52
Other assets	6,194	5,600	7,652	9,085	6,606
Total assets	\$ 438,525	\$ 448,155	\$ 422,506	\$ 426,019	\$ 393,124
Obligations with maturities of one year or less	\$ 365,386	\$ 379,719	\$ 357,130	\$ 363,600	\$ 333,588
Total liabilities	365,386	379,719	357,130	363,600	333,588
Capital stock and participation certificates	973	960	936	899	900
Unallocated retained earnings	72,166	67,476	64,440	61,520	59,001
Accumulated other comprehensive income/(loss)	-	-	-	-	(365)
Total shareholders' equity	73,139	68,436	65,376	62,419	59,536
Total liabilities and shareholders' equity	\$ 438,525	\$ 448,155	\$ 422,506	\$ 426,019	\$ 393,124
	For the Year Ended December 31				
	2010	2009	2008	2007	2006
Statement of Income Data					
Net interest income	\$ 11,966	\$ 11,331	\$ 9,185	\$ 8,775	\$ 7,901
Patronage distribution from U.S. AgBank, FCB	240	64	1,051	1,541	1,302
Provision for loan losses	250	250	-	-	-
Noninterest expense, net	4,580	5,513	5,079	5,287	5,347
(Benefit from)/Provision for income taxes	(80)	(4)	37	10	164
Net income	\$ 7,456	\$ 5,636	\$ 5,120	\$ 5,019	\$ 3,692
Key Financial Ratios					
For the Year					
Return on average assets	1.72%	1.35%	1.24%	1.25%	0.99%
Return on average shareholders' equity	10.39%	8.31%	7.94%	8.17%	6.14%
Net interest income as a percentage of average earning assets	2.85%	2.80%	2.30%	2.28%	2.21%
Net charge-offs as a percentage of average net loans	0.02%	<0.01%	<0.01%	0.02%	<0.01%
At Year End					
Shareholders' equity as a percentage of total assets	16.68%	15.27%	15.47%	14.65%	15.14%
Debt as a ratio to shareholders' equity	5.00:1	5.55:1	5.46:1	5.83:1	5.60:1
Allowance for loan losses as a percentage of loans	0.58%	0.53%	0.50%	0.50%	0.56%
Permanent capital ratio	14.78%	14.28%	14.37%	14.07%	13.64%
Total surplus ratio	14.57%	14.07%	14.16%	13.86%	13.40%
Core surplus ratio	13.72%	13.14%	13.00%	12.68%	13.40%
Net Income Distribution					
Cash patronage distribution paid	\$ 2,766	\$ 2,000	\$ 2,500	\$ 2,500	\$ 2,700
Cash patronage declared	\$ 2,800	\$ 2,600	\$ 2,200	\$ 2,500	\$ 2,700

MANAGEMENT'S DISCUSSION AND ANALYSIS

INTRODUCTION

The following discussion summarizes the financial position and results of operations of Northern California Farm Credit, ACA for the year ended December 31, 2010. Comparisons with prior years are included. We have emphasized material known trends, commitments, events, or uncertainties that have impacted, or are reasonably likely to impact our financial condition and results of operations. You should read these comments along with the accompanying financial statements, footnotes and other sections of this report. The accompanying financial statements were prepared under the oversight of our Audit Committee. The Management's Discussion and Analysis includes the following sections:

- Business Overview
- Economic Overview
- Loan Portfolio
- Credit Risk Management
- Results of Operations
- Liquidity
- Capital Resources
- Regulatory Matters
- Governance
- Forward-Looking Information
- Critical Accounting Policies and Estimates
- Customer Privacy

Our quarterly reports to shareholders are available approximately 40 days after the calendar quarter end and annual reports are available approximately 75 days after the calendar year end. The reports may be obtained free of charge on our website, www.norcalfc.com, or upon request. We are located at 3435 Silverbell Road, Chico, California 95973 or may be contacted by calling (530) 895-8698.

BUSINESS OVERVIEW

Farm Credit System Structure and Mission

We are one of approximately 90 associations in the Farm Credit System (System), which was created by Congress in 1916 and has served agricultural producers for over 90 years. The System mission is to provide sound and dependable credit to American farmers, ranchers, and producers or harvesters of aquatic products and farm-related businesses through a member-owned cooperative system. This is done by making loans and providing financial services. Through its commitment and dedication to agriculture, the System continues to have the largest portfolio of agricultural loans of any lender in the United States. The Farm Credit Administration (FCA) is the System's independent safety and soundness federal regulator and was established to supervise, examine and regulate System institutions.

Our Structure and Focus

As a cooperative, we are owned by the members we serve. Our territory served extends across a diverse agricultural region of Butte, Glenn, Tehama, Shasta and Trinity counties. We make long-term real estate mortgage loans to farmers, ranchers, rural residents and agribusinesses and production and intermediate-term loans for agricultural production or operating purposes. Additionally, we provide other related services to our borrowers, such as credit life insurance, multi-peril crop and crop hail insurance, and direct financing leases. Our success begins with our extensive agricultural experience and knowledge of the market and is dependent on the level of satisfaction we provide to our borrowers.

We obtain the funding for our lending and operations from U.S. AgBank, FCB (AgBank). AgBank is a cooperative of which we are a member. AgBank, its related associations, and AgVantis, Inc. (AgVantis) are referred to as the District. We are materially affected by AgBank's financial condition and results of operations. The AgBank and AgBank District quarterly and annual reports are available free of charge by accessing AgBank's website, www.usagbank.com, or may be obtained at no charge by contacting us at 3435 Silverbell Road, Chico, California 95973 or calling (530) 895-8698. Annual reports are available within 75 days after year end and quarterly reports are available within 40 days after the calendar quarter end.

In November of 2010, the AgBank Board of Directors voted to pursue a merger with CoBank, ACB, another Farm Credit System Bank. The proposed merger is targeted to be effective on October 1, 2011. The Association does not expect there to be any material negative impact to its operations as a result of the merger.

We purchase technology and other operational services from AgVantis, which is a technology service corporation. Our current Services Agreement with AgVantis expires on December 31, 2011. We are a shareholder in AgVantis, along with all other AgVantis customers. Farm Credit Foundations, a human resource service provider for a number of Farm Credit institutions, provides our payroll and human resource services.

ECONOMIC OVERVIEW

In recent years, agriculture has experienced a sustained period of favorable economic conditions due to strong commodity prices, rising land values, and, to a lesser extent, government support programs. As a result, our financial results have been positively impacted. Production agriculture, however, remains a cyclical business that is heavily influenced by commodity prices. High energy and fertilizer costs, higher feed costs, labor costs and availability, water costs and availability, increased market interest rates, adverse weather conditions, and commodity price volatility can negatively impact the profitability of agricultural producers. In an environment of less favorable economic conditions in agriculture and without sufficient government support programs, our financial performance and credit quality measures could be negatively impacted.

Global economic events created substantial turmoil in the financial sector and uncertainty in the credit markets since the end of 2008. During the latter part of 2009, the severe stress in the financial markets began to stabilize. In 2010, the System's strong capital and liquidity position enabled us to obtain the funding needed to finance loans to our farmer and rancher customers in response to loan demand.

During 2010, conditions in the general economy have become less favorable with the instability in the global markets and volatile production costs. One segment of the agricultural economy in our area particularly affected by the poor overall economy has been the dairy industry. The negative impact from less favorable overall economic conditions for our other customers is somewhat lessened by the generally strong financial condition of agriculture.

In 2010 the majority of our farmers, ranchers, and agribusiness members had generally a good year. While weather, water, and higher input expenses faced many of the commodities, most of our customer base was able to adapt to adversity to realize a profitable year. Most farmers saw good prices, and/or exceptional yields, and a weak dollar which allowed them to maintain profitable levels.

For almond growers, the 2010 crop production is expected to be over 1.6 billion pounds, one of the largest crops on record. Shipment of almonds is ahead of last year and committed shipments domestically are better than last year. With the 2010 crop plus the carry in from previous years, prices dropped early in the season but have rebounded near the end of the year. Prices received by the growers should be high enough to remain profitable.

Walnut growers also saw profitable operations in 2010 though prices dropped from all time highs in 2007. Prices have rebounded from low 2008 levels due to a weak U.S. dollar and strong exports. Like almond growers, with a large 2010 crop, prices will remain at profitable levels.

During 2010, feeder cattle prices have strengthened to all time highs. To date, fall feed and water conditions are as good as they have ever been so early in the season. Prices are expected to remain strong as long as the overall herd numbers remain at such low levels. Livestock producers are expected to have a profitable year through 2011.

Rice farmers saw profits again in 2010. Most growers have reported excellent crop yields from the high 80 cwt per acre to the low 100's. Quality has been better than average. Prices have come down from 2008 all time highs but remain at profitable levels as world supplies for Medium grain Californian rice remain strong. Prices before the 2010 harvest were quoted above \$12-\$15/cwt. This has produced a profitable situation for growers.

The farm related business, agribusinesses, as well as processors associated with commodities produced in our area, are also doing well. Their success is directly tied to the profit of the farmers/ranchers in the area who have, for the most part, had a good year.

Prospects for 2011 will see moderating prices for most of the major commodities that we finance. Prices for most of our major commodities should generate profits as long as customers can maximize production and manage input costs. Input costs in the area of petroleum products, fertilizer, chemicals, and most other input costs are expected to rise above 2010 levels. The condition of the overall economy, as well as weather, will determine the continued success for farmers, ranchers, and agricultural business.

Land and equipment values were stable or saw increases in 2010 as the general state of the agriculture economy continued to grow. Ag land values were again on the increase, brought about by profitable commodities as well as the downturn in commercial and residential land values. Investors have decided that agriculture is the place to invest their dollars which has driven up Ag land prices. However, we are starting to see a weakening in agriculture properties involving residences on small parcels (20 acres or less). Many residential lenders continue to experience a large number of delinquencies and foreclosures brought about by customers who had sub-prime mortgages and then saw their interest rates rise. With the increase in foreclosures and an increase in inventory of homes on the market, residential home prices have seen value decreases.

LOAN PORTFOLIO

Total loan volume was \$426.7 million at December 31, 2010, a decrease of \$10.0 million, or 2.30%, from loans at December 31, 2009 of \$436.7 million, and an increase of \$17.9 million, or 4.38%, from loans at December 31, 2008 of \$408.8 million. The decrease in loan volume was due to a reduction of participation interests in loans purchased from other Associations of \$7.7 million and an increase in participation interests sold to other Associations of \$3.3 million, for a net decrease in volume of \$11.0 million. The types of loans outstanding at December 31 are reflected in the following table.

<i>(dollars in thousands)</i>	2010		2009		2008	
	Volume	Percent	Volume	Percent	Volume	Percent
Real estate mortgage loans	\$ 294,689	69.1%	\$ 273,834	62.7%	\$ 264,525	64.7%
Production and intermediate-term loans	69,184	16.2%	94,901	21.7%	58,374	14.3%
Agribusiness loans to:						
Cooperatives	151	0.0%	76	—	—	—
Processing and marketing	10,542	2.5%	14,653	3.4%	3,036	0.7%
Farm related business	29,437	6.9%	28,326	6.5%	53,903	13.2%
Rural residential real estate loans	513	0.1%	532	0.1%	660	0.2%
Lease receivables	22,193	5.2%	24,425	5.6%	28,307	6.9%
Total	\$ 426,709	100.0%	\$ 436,747	100.0%	\$ 408,805	100.0%

Real estate mortgage volume increased to \$294.7 million, compared with \$273.8 million at year-end 2009, primarily due to a large disbursement to an existing customer to pay off their production and intermediate-term loan. Long-term mortgage loans are primarily used to purchase, refinance or improve real estate. These loans have maturities ranging from 5 to 40 years. Real estate mortgage loans are also made to rural homeowners. By federal regulation, a real estate mortgage loan must be secured by a first lien and may only be made in an amount up to 85% of the original appraised value of the property, or up to 97% of the appraised value, if the loan is guaranteed by certain state, federal, or other governmental agencies.

The production and intermediate-term volume decreased 27% to \$69.2 million compared with 2009 loan volume of \$94.9 million, primarily due to the pay-off discussed above. Production loans are used to finance the ongoing operating needs of agricultural producers. Production loans generally match the borrower's normal production and marketing cycle, which is typically 12 months. Intermediate-term loans are generally used to finance depreciable capital assets of a farm or ranch. Intermediate-term loans are written for a specific term, 1 to 15 years, with most loans being less than 10 years.

We have a program which provides leases to eligible parties in our chartered territory and specified others. All leases are classified in the same manner as we classify loans. While pickups and mobile transportation vehicles represent the majority of our leases by number, our portfolio also includes farm equipment as well as processing equipment for nuts and fresh fruit. We have been providing leases to eligible customers since 1996.

In recent years we have seen an increase in the number of processing and marketing facilities. However, in 2009 that volume saw an above normal increase as customers expanded or updated their operations to include processing facilities. Customers in the almond and walnut industries have decided to build, improve, or increase capacity in their huller/sheller/dryer facilities in response to the vast increase of acreage in these commodities. The decrease in 2010 can be attributed primarily to paydowns and a "backing off" from the unusually large investments in 2009.

Portfolio Diversification

While we make loans and provide financially related services to qualified borrowers in agricultural and rural sectors and to certain related entities, our loan portfolio is diversified by participations purchased and sold, geographic locations served and commodities financed, as illustrated in the following three tables.

We purchase participation interests in loans from other System entities to generate additional earnings and diversify risk related to existing commodities financed and our geographic area served. In addition, we sell a portion of certain large loans to other System entities to reduce risk and comply with lending limits we have established.

Our volume of participations purchased and sold as of December 31 follows.

<i>(dollars in thousands)</i>	2010	2009	2008
Participations purchased	\$ 29,859	\$ 37,577	\$ 34,064
Participations sold	\$ 15,027	\$ 11,680	\$ 3,812

We have no loans sold with recourse, retained subordinated participation interests in loans sold or interests in pools of subordinated participation interests that are held in lieu of retaining a subordinated participation interest in the loans sold.

The geographic distribution of loans by county at December 31 follows. As previously mentioned we purchase loans outside our territory, which are included in Other in the following table.

	2010	2009	2008
Butte	29.99%	28.74%	30.56%
Glenn	26.36%	25.72%	22.29%
Tehama	18.97%	18.40%	19.69%
Shasta	7.42%	7.65%	8.48%
Trinity	0.34%	0.34%	0.37%
Other	16.92%	19.15%	18.61%
Total	100.00%	100.00%	100.00%

The following table shows the primary agricultural commodities produced by our borrowers based on the Standard Industrial Classification System (SIC) published by the federal government. This system is used to assign commodity or industry categories based on the primary business of the customer. A primary business category is assigned when the commodity or industry accounts for 50% or more of the total value of sales for a business; however, a large percentage of agricultural operations typically includes more than one commodity.

SIC Category	December 31		
	2010	2009	2008
Almonds	18.27%	18.14%	16.55%
Walnuts	14.88%	14.48%	13.10%
Livestock	14.62%	14.01%	15.57%
Rice	13.58%	12.56%	11.16%
Dairy	8.02%	7.81%	8.07%
Irrigated field crops	6.84%	6.28%	6.49%
Prunes	4.18%	3.92%	4.34%
Other orchards	3.69%	5.41%	5.55%
Related business	3.69%	4.03%	3.22%
Other	12.23%	13.36%	15.95%
Total	100.00%	100.00%	100.00%

There were no material changes in commodity concentrations from 2009 to 2010. Almond, walnut, livestock and rice volume has increased as a direct result of the profitability of those commodities. Repayment ability of our borrowers is closely related to the production and profitability of the commodities they raise. If a loan fails to perform, restructuring and/or other servicing alternatives are influenced by the underlying value of the collateral which is impacted by industry economics. Our future performance would be negatively impacted by adverse agricultural conditions. The degree of the adverse impact would be correlated to the commodities negatively affected and the magnitude and duration of the adverse agricultural conditions to our borrowers.

In addition to commodity diversification noted in the previous table, further diversification is also achieved from loans to rural residents and part-time farmers which typically derive most of their earnings from non-agricultural sources. These borrowers are less subject to agricultural cycles and would likely be more affected by weaknesses in the general economy.

The principal balance outstanding at December 31, 2010 for loans less than \$250 thousand accounted for 23.89% of loan volume and 80.32% of the number of loans. Credit risk on small loans, in many instances, may be reduced by non-farm income sources. The following table details loan principal by dollar size at December 31.

<i>(dollars in thousands)</i>	2010		2009		2008	
	Amount outstanding	Number of loans	Amount outstanding	Number of loans	Amount outstanding	Number of loans
\$1 - \$250	\$ 101,962	1,780	\$ 107,097	1,889	\$ 105,447	1,917
\$251 - \$500	84,981	243	81,895	231	83,825	239
\$501 - \$1,000	83,315	118	83,261	116	86,718	123
\$1,001 - \$5,000	122,595	71	130,792	73	119,407	65
\$5,001 - \$25,000	33,856	4	33,702	4	13,408	2
Total	\$ 426,709	2,216	\$ 436,747	2,313	\$ 408,805	2,346

Approximately 8% of our loan volume is attributable to 4 borrowers. Due to their size, the loss of any of these loans or the failure of any of these loans to perform would adversely affect the portfolio and our future operating results.

The credit risk of some long-term real estate loans has been reduced by entering into agreements that provide long-term standby commitments by Federal Agricultural Mortgage Corporation (Farmer Mac) to purchase the loans in the event of default. The amount of loans subject to these Farmer Mac credit enhancements was \$8.1 million at December 31, 2010, \$10.6 million at December 31, 2009 and \$15.3 million at December 31, 2008. Included in other operating expenses were fees paid for these Farmer Mac commitments totaling \$44 thousand in 2010, \$64 thousand in 2009 and \$77 thousand in 2008. Under the Farmer Mac long-term standby commitment to purchase agreements, we continue to hold the loans in our portfolio, and we pay commitment fees to Farmer Mac for the right to put a loan designated in these agreements to Farmer Mac at par in the event the loan becomes significantly delinquent (typically four months past due). If the borrower cures the default, we must repurchase the loan and the commitment remains in place. Farmer Mac long-term standby commitments to purchase agreements are further described in Note 3. Other than the contractual obligations arising from these business transactions with Farmer Mac, Farmer Mac is not liable for any debt or obligation of ours and we are not liable for any debt or obligation of Farmer Mac. For more information on Farmer Mac, refer to their website at www.farmermac.com.

Credit enhancements with government agencies of \$3.1 million at year-end 2010 and \$3.2 million at year-end 2009 and 2008 were outstanding.

Credit Commitments

We may participate in financial instruments with off-balance-sheet risk to satisfy the financing needs of our borrowers and to manage our exposure to interest rate risk. These financial instruments include commitments to extend credit. The instruments involve, to varying degrees, elements of credit risk in excess of the amount recognized in our consolidated 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. Commitments generally have fixed expiration dates or other termination clauses and may require payment of a fee by the borrower. The following table summarizes the maturity distribution of unfunded credit commitments on loans at December 31, 2010.

<i>(dollars in thousands)</i>	Less than 1 year	1 – 3 years	3 – 5 years	Over 5 years	Total
Commitments to extend credit	\$ 27,649	\$ 38,769	\$ 2,270	\$ 45,197	\$ 113,885

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 Statement of Condition until funded or drawn upon. The credit risk associated with issuing commitments is substantially the same as that involved in extending loans to borrowers and we apply the same credit policies to these commitments. The amount of collateral obtained, if deemed necessary upon extension of credit, is based on our credit evaluation of the borrower. No material losses are anticipated as a result of these credit commitments.

High Risk Assets

Nonperforming loan volume is comprised of nonaccrual loans, restructured loans, and loans 90 days past due still accruing interest and are referred to as impaired loans. High risk assets consist of impaired loans and leases and other property owned. Year-end comparative information regarding high risk assets in the portfolio, including accrued interest, follows:

<i>(dollars in thousands)</i>	2010	2009	2008
Nonaccrual loans:			
Real estate mortgage	\$ 204	\$ 255	\$ 69
Production and intermediate-term	199	–	10
Lease receivables	19	5	9
Total nonaccrual loans	422	260	88
Total high risk assets	\$ 422	\$ 260	\$ 88
Nonaccrual loans to total loans	0.10%	0.06%	0.02%
High risk assets to total loans	0.10%	0.06%	0.02%
High risk assets to total shareholders' equity	0.58%	0.38%	0.13%

We had no loans classified as restructured or 90 days past due still accruing interest and no other property owned for the years presented.

Total high risk assets increased \$162 thousand, or 62.30%, to \$422 thousand at December 31, 2010 compared with year-end 2009.

Nonaccrual loans represent all loans where there is a reasonable doubt as to collection of all principal and/or interest. Nonaccrual volume increased \$162 thousand compared with December 31, 2009 primarily due to the downgrading of one additional loan complex. The following table provides additional information on nonaccrual loans as of December 31.

<i>(dollars in thousands)</i>	2010	2009	2008
Nonaccrual loans current as to principal and interest	\$ 56	\$ 7	\$ 10
Cash basis nonaccrual loans	\$ –	\$ 193	\$ –

For the years presented, we had no restructured loans in nonaccrual status.

We acquired one small property during 2010 with a carrying value of \$45 thousand. The property was sold during 2010 at a gain of \$4 thousand.

High risk asset volume is anticipated to remain relatively static for the next year or two.

Credit Quality

We review the credit quality of the loan portfolio on an on-going basis as part of our risk management practices. Each loan is classified according to the Uniform Classification System (UCS), which is used by all 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 as substandard assets. However, doubtful assets have additional weaknesses in existing facts that make collection in full highly questionable.
- Loss – Assets are not considered collectible.

The following table presents statistics based on UCS related to the credit quality of the loan portfolio, including accrued interest at December 31.

	2010	2009	2008
Acceptable	98.86%	99.15%	98.19%
OAEM	0.15%	0.04%	0.34%
Substandard	0.99%	0.81%	1.47%
Total	100.00%	100.00%	100.00%

During 2010, overall credit quality remained relatively static over 2009 levels. Loans classified as "Acceptable" and "OAEM" were 99.01% at December 31, 2010 and 99.19% at December 31, 2009. We had no loans classified as Doubtful or Loss for any of the three years presented. With our borrowers' generally strong financial positions and the continued emphasis on sound underwriting standards, the credit quality of our loan portfolio remains strong. Agriculture remains a cyclical business that is heavily influenced by production, operating costs and commodity prices. Each of these can be significantly impacted by uncontrollable events. While credit quality is anticipated to remain sound in 2011, we expect that the less favorable economic conditions and less government support programs may lead to weakening in the loan portfolio. Loan delinquencies (accruing loans 30 days or more past due) as a percentage of accruing loans increased, however, remained at a low level of 0.05% at December 31, 2010, compared with 0.02% at December 31, 2009.

Allowance for Loan Losses

We maintain an allowance for loan losses at a level consistent with the probable losses identified by management. The allowance for loan losses at each period end was considered to be adequate to absorb probable losses existing in the loan portfolio. Because the allowance for loan losses considers factors such as current agricultural and economic conditions, loan loss experience, portfolio quality and loan portfolio composition, there will be a direct impact to the allowance for loan losses and our income statement when there is a change in any of those factors. The following table provides relevant information regarding the allowance for loan losses as of December 31.

<i>(dollars in thousands)</i>	2010	2009	2008
Balance at beginning of year	\$ 2,294	\$ 2,053	\$ 2,059
Charge-offs:			
Agribusiness	65	–	–
Lease receivables	–	9	9
Recoveries:			
Agribusiness	1	–	3
Net charge-offs	64	9	6
Provision for loan losses	250	250	–
Balance at December 31	\$ 2,480	\$ 2,294	\$ 2,053
Net charge-offs as a percentage of average net loans	0.02%	<0.01%	<0.01%

The following table presents the allowance for loan losses by loan type as of December 31.

<i>(dollars in thousands)</i>	2010	2009	2008
Real estate mortgage	\$ 1,601	\$ 1,666	\$ 1,416
Production and intermediate-term	475	225	225
Agribusiness	278	277	277
Rural residential real estate	4	4	4
Lease receivables	122	122	131
Total	\$ 2,480	\$ 2,294	\$ 2,053

The allowance for loan losses increased \$186 thousand from December 31, 2009, to \$2.5 million at December 31, 2010. The increase in allowance for loan losses was primarily due to the provision for loan losses totaling \$250 thousand that was recorded to provide for loan losses in the loan portfolio that are not yet specifically identified. Net charge-offs of \$64 thousand were recorded during 2010. Overall, charge-off activity remains low relative to the size of our loan portfolio. Comparative allowance for loan losses coverage as a percentage of loans and certain other credit quality indicators as of December 31 are presented in the following table.

	2010	2009	2008
Allowance as a percentage of:			
Loans	0.58%	0.53%	0.50%
Impaired loans	587.68%	882.31%	2,332.95%
Nonaccrual loans	587.68%	882.31%	2,332.95%

Young, Beginning and Small Farmers and Ranchers Program

As part of the Farm Credit System, we are committed to providing sound and constructive credit and related services to young, beginning and small (YBS) farmers and ranchers. To establish and encourage a sound and constructive program to provide for the special credit needs for YBS farmers, ranchers and harvesters of aquatic products in accordance with the Farm Credit Act. This policy is intended to provide for both the mortgage and commercial credit, and other related service needs of a group of borrowers who may not be eligible for financing under our existing policies.

The FCA regulatory definitions for YBS farmers and ranchers are shown below.

- Young Farmer: A farmer, rancher, or producer or harvester of aquatic products who was age 35 or younger as of the date the loan was originally made.
- Beginning Farmer: A farmer, rancher, or producer or harvester of aquatic products who had 10 years or less farming or ranching experience as of the date the loan was originally made.
- Small Farmer: A farmer, rancher, or producer or harvester of aquatic products who normally generated less than \$250 thousand in annual gross sales of agricultural or aquatic products at the date the loan was originally made.

The following table outlines our percentage of YBS loans as a percentage of our loan portfolio (by number) as of December 31. The USDA column represents the percent of farmers and ranchers classified as YBS within our territory per the 2007 USDA Agricultural Census, which is the most current data available. A loan may be included in more than one category.

	USDA	December 31		
		2010	2009	2008
Young	5%	73%	73%	77%
Beginning	33%	14%	15%	15%
Small	91%	9%	9%	9%

While we have not established a specific marketing plan, we regularly include our YBS program in our advertising and website. Our loan officers try to utilize the program to meet the needs of our qualifying customers.

Our program is targeted to address the most common credit factors that this population tends to have difficulty meeting. Recognizing that young and beginning farmers typically will not have built up significant equity, our differential credit requirements compensate for that fact. We offer much lower interest rates than most young or beginning farmers would normally qualify for, thus enhancing their cash flow. Utilizing differential credit analysis and Credit Scoring, we are able to reduce the paperwork requirements for smaller loans, as well as our costs, which benefits most small farmers.

Our qualitative goals have not changed from recent years; we emphasize outreach to targeted groups such as junior college and university students involved in agricultural programs, 4-H and FFA members, Farm Bureau and commodity groups in order to make as many qualified customers within our territory aware of what we have available.

Quarterly reports are provided to our Board of Directors detailing the number, volume and credit quality of our YBS customers. We have developed quantitative targets to monitor our progress. Our quantitative goals for 2010, as well as our actual performance, are as follows:

	Volume		Numbers of loans	
	Goal	Actual	Goal	Actual
Young	5%	-5%	3%	0%
Beginning	3%	-11%	1%	-4%
Small	5%	-2%	3%	1%

The numbers which have declined are, in part, due to a number of the loans we originally put on which met the YBS characteristics, starting to pay off or pay down, and are being replaced by other loans to these same borrowers (no longer classified as YBS). We consider this an indication of success within the program in that these members are still in business, and qualify for credit based on our general underwriting standards. We have seen a number of new young borrowers either getting new loans or joining family operations.

To ensure that credit and services offered to our YBS farmers and ranchers are provided in a safe and sound manner and within our risk-bearing capacity, we utilize special loan underwriting standards that recognize the difficulty of capitalizing a start-up operation. However, we do require repayment ability similar to our non-YBS loans in order to adequately shield both us and individual members from undue risk.

CREDIT RISK MANAGEMENT

Credit risk arises from the potential failure of a borrower to meet repayment obligations that result in a financial loss to the lender. Credit risk exists in our loan portfolio and also in our unfunded loan commitments. Credit risk is actively managed on an individual and portfolio basis through application of sound lending and underwriting standards, policies and procedures.

Underwriting standards are utilized to determine an applicant’s operational, financial, and managerial resources available for repaying debt within the terms of the note and loan agreement. 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 – to protect the lender in the event of default and also serve as a secondary source of loan repayment;
- capital – ability of the operation to survive unanticipated risks; and,
- conditions – intended use of the loan funds, terms, restrictions, etc.

Processes for information gathering, balance sheet and income statement verification, loan analysis, credit approvals, disbursements of proceeds and subsequent loan servicing actions are established and followed. Underwriting standards vary by industry and are updated periodically to reflect market and industry conditions.

By regulation, we cannot have loan commitments to one borrower for more than 25% of our permanent capital. Through lending delegations, AgBank restricts individual loan size limits to one borrower to 15% of our permanent capital; exceptions must be reported to AgBank. Within these parameters, we set our own lending limits to manage loan concentration risk. Lending limits are established for individual loan size, commodity type, special lending programs and geographic concentrations. We have adopted an individual lending limit maximum of 15% of permanent capital for our highest quality borrowers.

We have established internal lending delegations to properly control the loan approval process. Delegations to staff are based on our risk-bearing ability, loan size, complexity, type and risk, as well as the expertise and position of the credit staff member. Larger and more complex loans or loans perceived to have higher risk are typically approved by our loan committee with the most experienced and knowledgeable credit staff serving as members.

The majority of our lending is first mortgage real estate loans which must be secured by a first lien on real estate. Production and intermediate-term lending accounts for most of the remaining volume and is also typically secured. Collateral evaluations are completed in compliance with FCA and Uniform Standards of Professional Appraisal Practices requirements. All property is appraised at market value. All collateral evaluations must be performed by a qualified appraiser. Certain appraisals must be performed by individuals with a state certification or license.

We use a two-dimensional risk rating model (Model) based on the Farm Credit System's Combined System Risk Rating Guidance which estimates each loan's probability of default (PD) and loss given default (LGD). PD estimates the probability that a borrower will experience a default within twelve months from the date of determination. LGD provides an estimation of the anticipated loss with respect to a specific financial obligation of a borrower assuming a default has occurred or will occur within the next twelve months. The Model uses objective and subjective criteria to identify inherent strengths, weaknesses, and risks in each loan. The PDs and LGDs are utilized in loan and portfolio management processes and are partially utilized for the allowance for loan losses estimate. This Model also serves as the basis for economic capital modeling.

The Model's 14-point probability of default scale provides for nine acceptable categories, one OAEM category, two substandard categories, one doubtful category and one loss category; each carrying a distinct percentage of default probability. The Model's LGD scale provides 6 categories that have the following anticipated principal loss and range of economic loss expectations:

- A 0% anticipated principal loss; 0% to 5% range of economic loss
- B 0% to 3% anticipated principal loss; 5% to 15% range of economic loss
- C > 3% to 7% anticipated principal loss; 15% to 20% range of economic loss
- D > 7% to 15% anticipated principal loss; 20% to 25% range of economic loss
- E > 15% to 40% anticipated principal loss; 25% to 50% range of economic loss
- F above 40% anticipated loss; above 50% range of economic loss

RESULTS OF OPERATIONS

Earnings Summary

In 2010, we recorded net income of \$7.5 million, compared with \$5.6 million in 2009, and \$5.1 million in 2008. The increase in 2010 was primarily due to higher spreads on loans, higher patronage from AgBank and a refund from the Farm Credit System Insurance Corporation. The following table presents the changes in the significant components of net income from the previous year.

<i>(dollars in thousands)</i>	2010 vs. 2009	2009 vs. 2008
Net income, prior year	\$ 5,636	\$ 5,120
Increase/(Decrease) from changes in:		
Interest income	378	(3,581)
Interest expense	257	5,727
Net interest income	635	2,146
Provision for loan losses	–	(250)
Noninterest income	615	(996)
Noninterest expense	494	(425)
Provision for income taxes	76	41
Total increase in net income	1,820	516
Net income, current year	\$ 7,456	\$ 5,636

Return on average assets increased to 1.72% from 1.35% in 2009, and return on average shareholders' equity increased to 10.39% from 8.31% in 2009, primarily as a result of increased income.

Net Interest Income

Net interest income for 2010 was \$12.0 million compared with \$11.3 million for 2009 and \$9.2 million for 2008. Net interest income is our principal source of earnings and is impacted by interest earning asset volume, yields on assets and cost of debt. The increase in net interest income was largely due to increased spreads on loans. The table below provides an analysis of the individual components of the change in net interest income during 2010 and 2009.

<i>(dollars in thousands)</i>	2010 vs. 2009	2009 vs. 2008
Net interest income, prior year	\$ 11,331	\$ 9,185
Increase/(Decrease) in net interest income from changes in:		
Interest rates earned	(336)	(3,863)
Interest rates paid	461	5,821
Volume of interest-bearing assets and liabilities	443	157
Interest income on nonaccrual loans	67	31
Increase in net interest income	635	2,146
Net interest income, current year	\$ 11,966	\$ 11,331

The following table illustrates net interest margin and the average interest rates on loans and debt cost and interest rate spread.

	For the Year Ended December 31		
	2010	2009	2008
Net interest margin	2.85%	2.80%	2.30%
Interest rate on:			
Average loan volume	4.42%	4.48%	5.44%
Average debt	1.83%	1.96%	3.66%
Interest rate spread	2.59%	2.52%	1.78%

Interest rates on average debt decreased 13 basis points offset by the decrease in interest rates on average loan volume of 6 basis points. The increase in interest rate spread resulted from a decision made in early 2009 to increase all spreads. Interest rates we earn on our own capital have dropped significantly and, in order to make up the lost earnings, this step was deemed necessary. Additionally, in the uncertain times during the past year, we felt it best to continue the practice of generating earnings for any future contingencies.

Provision for Loan Losses/(Loan Loss Reversals)

We monitor our loan portfolio on a regular basis to determine if any increase through provision for loan losses or decrease through a loan loss reversal in our allowance for loan losses is warranted based on our assessment of the probable losses in our loan portfolio. We recorded provision for loan losses of \$250 thousand in 2010 and in 2009. We did not record a provision for loan losses or a loan loss reversal during 2008. The provision for loan losses recorded during 2010 was primarily to provide for losses in the loan portfolio that are not yet specifically identified.

Noninterest Income

During 2010, we recorded noninterest income of 940 thousand, compared with \$325 thousand in 2009 and \$1.3 million in 2008. Patronage distributions from AgBank are our primary source of noninterest income. Beginning in 2009, patronage from AgBank was determined annually instead of quarterly and, except for certain priority patronage, paid after the end of the year. As a result, our patronage income increased in 2010, compared with 2009 where only priority patronage was paid. Patronage received was \$240 thousand in 2010, \$64 thousand in 2009, and \$1.1 million in 2008. AgBank patronage was paid in cash. During 2010, we received from Farm Credit System Insurance Company (FCSIC) a distribution of \$459 thousand representing our allocated portion of the excess amount in the System's insurance fund above the 2% secure base amount. As a result, our noninterest income increased compared with 2009. Noninterest income also includes loan fees, financially related services income and other noninterest income. Loan fees in 2010 were \$139 thousand, a decrease of \$10 thousand, from 2009.

Noninterest Expense

Noninterest expense for 2010 decreased \$494 thousand, or 8.56%, to \$5.3 million compared with 2009. Noninterest expense for each of the three years ended December 31 is summarized below:

<i>(dollars in thousands)</i>	Percent of Change				
	2010	2009	2008	2010/2009	2009/2008
Salaries & employee benefits	\$ 3,712	\$ 3,745	\$ 3,304	(0.88%)	13.4%
Occupancy & equipment	170	163	190	4.29%	(14.2%)
Purchased services from AgVantis	321	281	257	14.23%	9.3%
Supervisory & examination costs	166	155	148	7.10%	4.7%
Other	725	726	842	(0.14%)	(13.8%)
Total operating expense	5,094	5,070	4,741	0.47%	6.9%
Gains on other property owned, net	(4)	—	—	—	—
Farm Credit Insurance Fund premium	190	704	608	(73.01%)	15.8%
Total noninterest expense	\$ 5,280	\$ 5,774	\$ 5,349	(8.56%)	8.0%

For the year ended December 31, 2010, total operating expense increased \$24 thousand, or 0.47%, compared with the year ended December 31, 2009, primarily due to the Insurance Fund premium decreasing \$514 thousand to \$190 thousand due to a decrease in the premium rate. As of July 1, 2008, the Farm Credit System Insurance Corporation began charging premiums based on debt rather than loan volume. Rates were decreased to 5 basis points during 2010 compared with 20 basis points during 2009. Premium rates were 15 basis points on average loan volume during

the first six months of 2008. During the last six months of 2008 premiums were charged on average debt at 15 basis points for the third quarter and 18 basis points for the fourth quarter.

Provision for income taxes/Benefit from income taxes

We recorded \$80 thousand in benefit from income taxes during 2010, compared with benefit from income taxes of \$4 thousand in 2009 and provision for income taxes of \$37 thousand in 2008. The change was primarily due to the decline in taxable income. Tax expense was also impacted by our patronage refund program. We operate as a Subchapter T cooperative for tax purposes and thus may deduct from taxable income certain amounts that are distributed from net earnings to borrowers. See Note 9 for additional details.

LIQUIDITY

Liquidity is necessary to meet our financial obligations. Obligations that require liquidity include paying our note with AgBank, funding loans and other commitments, and funding operations in a cost-effective manner. Our liquidity policy is intended to manage short-term cash flow, maximize debt reduction and liquidate nonearning assets. Our direct loan with AgBank, cash on hand and loan repayments provide adequate liquidity to fund our on-going operations and other commitments. Even with the volatility in the financial markets, we anticipate liquidity levels will be adequate to meet our obligations.

Funding Sources

Our primary source of liquidity is the ability to obtain funds for our operations through a borrowing relationship with AgBank. Our note payable to AgBank is collateralized by a pledge to AgBank of substantially all of our assets. Substantially all cash received is applied to the note payable and all cash disbursements are drawn on the note payable. The indebtedness is governed by a General Financing Agreement (GFA). The GFA is subject to renewal at its expiration date of April 30, 2012 in accordance with normal business practices. We expect renewal of the GFA after the expiration date. The annual average principal balance of the note payable to AgBank was \$339.7 million in 2010, \$327.5 million in 2009 and \$314.8 million in 2008.

We plan to continue to fund lending operations through the utilization of our borrowing relationship with AgBank, retained earnings from current and prior years and from borrower stock investments. AgBank's primary source of funds is the ability to issue Systemwide Debt Securities to investors through the Federal Farm Credit Bank Funding Corporation. This access has traditionally provided a dependable source of competitively priced debt that is critical for supporting our mission of providing credit to agriculture and rural America. Although financial markets have experienced significant volatility in 2008 and 2009, we were able to obtain sufficient funding to meet the needs of our customers.

Interest Rate Risk

The interest rate risk inherent in our loan portfolio is substantially mitigated through our funding relationship with AgBank which allows for loans to be match-funded. Borrowings from AgBank match the pricing, maturity, and option characteristics of our loans to borrowers. AgBank manages interest rate risk through the direct loan pricing and their asset/liability management processes. Although AgBank incurs and manages the primary sources of interest rate risk, we may still be exposed to interest rate risk through the impact of interest rate changes on earnings generated from our loanable funds. To stabilize earnings from loanable funds, we have committed excess funds with AgBank at a fixed rate as a part of AgBank's Earnings Stabilization Management Program (ESMP). This enables us to stabilize earnings without significantly increasing our overall interest rate risk position.

Our ESMP commitment balance and the average interest rate as of December 31 in the various maturities are reflected below:

<i>(dollars in thousands)</i>	2010		2009		2008	
	Balance	Average Rate	Balance	Average Rate	Balance	Average Rate
Maturing in 1 year or less	\$ 8,100	1.54%	\$ 14,800	1.07%	\$ 500	4.09%
Maturing in 1 to 3 years	3,700	2.14%	5,800	2.24%	—	—
Maturing in over 3 years	5,000	3.23%	5,000	3.15%	—	—
Total	\$ 16,800	2.18%	\$ 25,600	1.74%	\$ 500	4.09%

Funds Management

We offer variable, fixed, adjustable prime-based and LIBOR-based rate loans to borrowers. Our Board of Directors determines the interest rate charged based on the following factors: 1) the interest rate charged by AgBank; 2) our existing rates and spreads; 3) the competitive rate environment; and 4) our profitability objectives.

CAPITAL RESOURCES

Capital supports asset growth and provides protection for unexpected credit and operating losses. Capital is also needed for investments in new products and services. We believe a sound capital position is critical to our long-term financial success due to the volatility and cycles in agriculture. Over the past several years, we have been able to build capital primarily through net income retained after patronage. Shareholders' equity at December 31, 2010 totaled \$73.1 million, compared with \$68.4 million at December 31, 2009 and \$65.4 million at December 31, 2008. The increase of \$4.7 million in shareholder's equity reflects net income and net stock issuances, partially offset by patronage refunds. Our capital position is reflected in the following ratio comparisons.

	2010	2009	2008
Debt to shareholders' equity	5.00:1	5.55:1	5.46:1
Shareholders' equity as a percent of net loans	17.24%	15.75%	16.07%
Shareholders' equity as a percent of total assets	16.68%	15.27%	15.47%

Debt to shareholders' equity decreased and shareholders' equity as a percent of net loans and of total assets increased from 2009 primarily due to decreased loan volume and an increase in shareholders' equity due to earnings.

Retained Earnings

Our retained earnings increased \$4.7 million to \$72.2 million at December 31, 2010 from \$67.5 million at December 31, 2009. The increase was a result of net income of \$7.5 million, partially offset by \$2.8 million of patronage distributions declared.

Patronage Program

We have a Patronage Program that allows us to distribute our available net earnings to our shareholders. This program provides for the application of net earnings in the manner described in our Bylaws. In addition to determining the amount and method of patronage to be distributed, this includes increasing surplus to meet capital adequacy standards established by Regulations; increasing surplus to a level necessary to support competitive pricing at targeted earnings levels; and increasing surplus for reasonable reserves. Patronage distributions are based on business done with us during the year. We paid cash patronage of \$2.8 million in 2010, \$2.0 million in 2009 and \$2.5 million in 2008.

Stock

Our total stock and participation certificates increased \$13 thousand to \$973 thousand at December 31, 2010, from \$960 thousand at December 31, 2009. The increase was due to \$104 thousand of stock issuances, partially offset by \$91 thousand of stock retirements. We require a stock investment for each borrower. The current stock requirement for each borrower is the lesser of one thousand dollars or 2.00% of the collective total balance of each borrower's loan(s).

Capital Plan and Regulatory Requirements

Our Board of Directors establishes a formal capital adequacy plan that addresses capital goals in relation to risks. The capital adequacy plan assesses the capital level necessary for financial viability and to provide for growth. Our plan is updated annually and approved by our Board of Directors. FCA regulations require the plan consider the following factors in determining optimal capital levels, including:

- Regulatory capital requirements;
- Asset quality;
- Needs of our customer base; and
- Other risk-oriented activities, such as funding and interest rate risks, contingent and off-balance sheet liabilities and other conditions warranting additional capital.

FCA regulations establish minimum capital standards expressed as a ratio of capital to assets, taking into account relative risk factors for all System institutions. In general, the regulations provide for a relative risk weighting of assets and establish a minimum ratio of permanent capital, total surplus and core surplus to risk-weighted assets. Our capital ratios as of December 31 and the FCA minimum requirements follow.

	Regulatory Minimum	2010	2009	2008
Permanent capital ratio	7.00%	14.78%	14.28%	14.37%
Total surplus ratio	7.00%	14.57%	14.07%	14.16%
Core surplus ratio	3.50%	13.72%	13.14%	13.00%

As of December 31, 2010, we exceeded the regulatory minimum capital ratios and are expected to do so throughout 2011. However, the minimum ratios established were not meant to be adopted as the optimum capital level, so we have established goals in excess of the regulatory minimum. As of December 31, 2010, we have exceeded our goals. Due to our strong capital position, we will continue to be able to retire at-risk stock.

REGULATORY MATTERS

As of December 31, 2010, we had no enforcement actions in effect and FCA took no enforcement actions on us during the year.

The Farm Credit Administration is considering the promulgation of Tier 1 and Tier 2 capital standards for Farm Credit System institutions. The Tier 1/Tier 2 capital structure would be similar to the capital tiers delineated in the Basel Accord that the other Federal financial regulatory agencies have adopted for the banking organizations they regulate. Comments on the advance notice of proposed rulemaking are due in May 2011.

On June 16, 2008, the Farm Credit Administration published a proposed rule in the Federal Register that would authorize Banks, Associations or service corporations to invest in rural communities, i.e., communities that have fewer than 50,000 residents and are outside of an urbanized area, under certain conditions. The proposed rule would authorize two types of rural community investments: (1) investment in debt securities that would involve projects or programs that benefit the public in rural communities, and (2) equity investment in venture capital funds, which funds create economic opportunities and jobs in rural communities by providing capital to small or start-up businesses. Under the proposed rule, these investments would be limited to 150% of the institution's total surplus. The comment period closed August 15, 2008. A date for final action on the rule has not been determined.

GOVERNANCE

Board of Directors

We are governed by an 8 member board that provides direction and oversees our management. Of these directors, 7 are elected by the shareholders and 1 is appointed by the elected directors. Our Board of Directors represents the interests of our shareholders. The Board of Directors meets regularly to perform the following functions, among others:

- selects, evaluates and compensates the chief executive officer;
- approves the strategic plan, capital plan, financial plan and the annual operating budget;
- oversees the lending operations;
- directs management on significant issues and,
- oversees the financial reporting process, communications with shareholders and our legal and regulatory compliance.

Director Independence

All directors must exercise sound judgment in deciding matters in our interest. All our directors are independent from the perspective that none of our management or staff serves as Board members. However, we are a financial services cooperative, and the Farm Credit Act and FCA Regulations require our elected directors to have a loan relationship with us.

The elected directors, as borrowers, have a vested interest in ensuring our Association remains strong and successful. However, our borrowing relationship could be viewed as having the potential to compromise the independence of an elected director. For this reason, the Board has established independence criteria to ensure that a loan relationship does not compromise the independence of our Board. Annually, in conjunction with our independence analysis and reporting on our loans to directors, each director provides financial information and any other documentation and/or assertions needed for the Board to determine the independence of each Board member.

Audit Committee

The Audit Committee reports to the Board of Directors. The Audit Committee is composed of 8 members. During 2010, 9 meetings were held. The Audit Committee responsibilities generally include, but are not limited to: oversight of the financial reporting risk and the accuracy of the quarterly and annual shareholder reports;

- the oversight of the system of internal controls related to the preparation of quarterly and annual shareholder reports;
- the review and assessment of the impact of accounting and auditing developments on the consolidated financial statements; and,
- the establishment and maintenance of procedures for the receipt, retention and treatment of confidential and anonymous submission of concerns, regarding accounting, internal accounting controls or auditing matters.

Credit Committee

The Credit Committee is responsible for the oversight of credit risk, including lending and underwriting standards and assesses the conditions that may materially impact the loan portfolio. The Credit Committee consists of 6 members.

Compensation Committee

The Compensation Committee is responsible for the oversight of employee and director compensation. The Compensation Committee is composed of the full Board. The Committee annually reviews, evaluates and approves the compensation policies, programs and plans for senior officers and employees including benefits programs.

Other Governance

The Board has monitored the requirements of public companies under the Sarbanes-Oxley Act. While we are not subject to the requirements of this law, we are striving to implement steps to strengthen governance and financial reporting. We strive to maintain strong governance and financial reporting through the following actions:

- a system for the receipt and treatment of whistleblower complaints,
- a code of ethics for our President/CEO, Chief Financial Officer and Chief Credit Officer,
- open lines of communication between the independent auditors, management, and the Audit Committee,
- "plain English" disclosures,
- officer certification of accuracy and completeness of the consolidated financial statements, and
- information disclosure through our website.

FORWARD-LOOKING INFORMATION

Our discussion contains forward-looking statements. These statements are not guarantees of future performance and involve certain risks, uncertainties and assumptions that are difficult to predict. Words such as "anticipates," "believes," "could," "estimates," "may," "should," and "will," or other variations of these terms are intended to identify forward-looking statements. These statements are based on assumptions and analyses made in light of experience and other historical trends, current conditions, and expected future developments. However, actual results and developments may differ materially from our expectations and predictions due to a number of risks and uncertainties, many of which are beyond our control. These risks and uncertainties include, but are not limited to:

- political, legal, regulatory and economic conditions and developments in the United States and abroad;
- economic fluctuations in the agricultural, rural utility, international, and farm-related business sectors;
- weather, disease, and other adverse climatic or biological conditions that periodically occur that impact agricultural productivity and income;
- changes in United States government support of the agricultural industry and/or the Farm Credit System; and,
- actions taken by the Federal Reserve System in implementing monetary policy.

CRITICAL ACCOUNTING POLICIES AND ESTIMATES

Our consolidated financial statements are based on 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 we have to make judgments about matters that are inherently uncertain. For a complete discussion of significant accounting policies, see Note 2 of the accompanying consolidated financial statements. The development and selection of critical accounting policies, and the related disclosures, have been reviewed by our Audit Committee. A summary of critical policies relating to determination of the allowance for loan losses follows.

Allowance for Loan Losses

The allowance for loan losses is our best estimate of the amount of probable loan losses existing in and inherent in our loan portfolio as of the balance sheet date. The allowance for loan losses is increased through provisions for loan losses and loan recoveries and is decreased through loan loss reversals and loan charge-offs. We determine the allowance for loan losses based on a regular evaluation of the loan portfolio, which generally considers recent historic charge-off experience adjusted for relevant factors.

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 we consider in the evaluation of losses in the loan portfolio could occur for various credit related reasons and could result in a change in the allowance for loan losses, which would have a direct impact on the provision for loan losses and results of operations. See Notes 2 and 3 to the accompanying consolidated financial statements for detailed information regarding the allowance for loan losses.

CUSTOMER PRIVACY

FCA regulations require that borrower information be held in confidence by Farm Credit institutions, their directors, officers and employees. FCA regulations and our Standards of Conduct Policies specifically restrict Farm Credit institution directors and employees from disclosing information not normally contained in published reports or press releases about the institution or its borrowers or members. These regulations also provide Farm Credit institutions clear guidelines for protecting their borrowers' nonpublic information.



Northern California Farm Credit, ACA

CHICO OFFICE
P.O. Box 929, 3435 Silverbell Road
Chico, California 95927
(530) 895-8698, FAX (530) 893-5314


REPORT OF MANAGEMENT

The financial statements of Northern California Farm Credit, ACA (Association) are prepared by management, who is responsible for their integrity and objectivity, including amounts that must necessarily be based on judgments and estimates. The financial statements have been prepared in conformity with generally accepted accounting principles appropriate in the circumstances, and in the opinion of management, fairly present the financial condition of the Association. Other financial information included in the 2010 annual report is consistent with that in the financial statements.


To meet its responsibility for reliable financial information, management depends on the Association's accounting and internal control systems, which have been designed to provide reasonable, but not absolute, assurance assets are safeguarded and transactions are properly authorized and recorded. A third party internal auditor is used to monitor compliance, perform audits of the accounting records, review accounting systems and internal controls, and recommends improvements as appropriate. The financial statements are examined by PricewaterhouseCoopers LLP, independent auditors, who also conduct a review of internal controls to the extent necessary to comply with auditing standards generally accepted in the United States of America. The Association is also examined by the Farm Credit Administration.

The Audit Committee of the Board of Directors has overall responsibility for the Association's system of internal control and financial reporting. The Audit Committee consults regularly with management and reviews the results of the examinations by the various entities named above. The independent auditors have direct access to the Audit Committee.

The undersigned certify the Northern California Farm Credit, ACA Annual Report has been reviewed, 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.



George Swaner, Chairman of the Board



Bruce V. Strickler, President & CEO



Phillip L. Downing, Chief Financial Officer

Signed this Date: March 16, 2011



Northern California Farm Credit, ACA

CHICO OFFICE

P.O. Box 929, 3435 Silverbell Road
Chico, California 95927
(530) 895-8698, FAX (530) 893-5314

AUDIT COMMITTEE REPORT

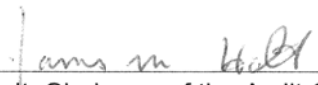
The Audit Committee (Committee) includes members from the Board of Directors of Northern California Farm Credit, ACA (Association). In 2010, nine Committee meetings were held. The Committee oversees the scope of the Association's internal audit program, the independence of the outside auditors, the adequacy of the Association's system of internal controls and procedures, and the adequacy of management's action with respect to recommendations arising from those auditing activities. The Committee's responsibilities are described more fully in the Internal Control Policy and the Audit Committee Charter. The Committee approved the appointment of PricewaterhouseCoopers, LLP (PwC) as the Association's independent auditors for 2010.

The fees for professional services rendered for the Association by its independent auditor, PwC, during 2010 were \$38,910 for audit services.

Management is responsible for the Association's internal controls and the preparation of the consolidated financial statements in accordance with accounting principles generally accepted in the United States of America. PwC is responsible for performing an independent audit of the Association's consolidated financial statements in accordance with auditing standards generally accepted in the United States of America and to issue a report thereon. The Committee's responsibilities include monitoring and overseeing these processes.

In this context, the Committee reviewed and discussed the Association's Quarterly Reports and the Association's financial statements for the year ended December 31, 2010 (the "Audited Financial Statements") with management. The Committee also receives from PwC the matters required to be discussed by Statement on Auditing Standards No. 114 (The Auditor's Communication with Those Charged with Governance). Both PwC and the Association's internal auditors directly provide reports on significant matters to the Committee.

Based on the foregoing review and discussions and relying thereon, the Committee recommended that the Board of Directors include the Financial Statements in the Association's Annual Report to Shareholders for the year ended December 31, 2010.



James M. Holt, Chairman of the Audit Committee

Audit Committee Members

George Swaner
Thomas B. Martin (Vice Chair)
Michael R. Chambers
Harry L. Cinquini
Glenn E. Hawes
Gregory W. Long
George R. Nicolaus

Signed this Date: March 16, 2011

Consolidated Statement of Condition

(Dollars in Thousands)

	December 31		
	2010	2009	2008
ASSETS			
Loans	\$ 426,709	\$ 436,747	\$ 408,805
Less allowance for loan losses	2,480	2,294	2,053
Net loans	424,229	434,453	406,752
Cash	1,007	637	990
Accrued interest receivable	3,261	3,104	4,349
Investment in U.S. AgBank, FCB	8,102	8,102	8,102
Premises and equipment, net	1,337	1,315	1,362
Prepaid benefit expense	301	410	538
Other assets	288	134	413
Total assets	\$ 438,525	\$ 448,155	\$ 422,506
LIABILITIES			
Note payable to U.S. AgBank, FCB	\$ 348,827	\$ 357,784	\$ 325,873
Advance conditional payments	11,007	15,433	21,293
Accrued interest payable	3,079	3,372	7,538
Patronage distributions payable	1,800	1,800	1,200
Accrued benefits liability	148	143	139
Deferred tax liability	77	158	162
Other liabilities	448	1,029	925
Total liabilities	365,386	379,719	357,130
Commitments and Contingencies (See Note 12)			
SHAREHOLDERS' EQUITY			
Capital stock and participation certificates	973	960	936
Unallocated retained earnings	72,166	67,476	64,440
Total shareholders' equity	73,139	68,436	65,376
Total liabilities and shareholders' equity	\$ 438,525	\$ 448,155	\$ 422,506

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

Consolidated Statement of Income

(Dollars in Thousands)

	For the Year Ended December 31		
	2010	2009	2008
INTEREST INCOME			
Loans	\$ 18,521	\$ 18,143	\$ 21,724
Total interest income	18,521	18,143	21,724
INTEREST EXPENSE			
Note payable to U.S. AgBank, FCB	6,485	6,760	11,824
Other	70	52	715
Total interest expense	6,555	6,812	12,539
Net interest income	11,966	11,331	9,185
Provision for loan losses	250	250	-
Net interest income after provision for loan losses	11,716	11,081	9,185
NONINTEREST INCOME			
Financially related services income	70	77	87
Loan fees	139	149	148
Patronage distribution from U.S. AgBank, FCB	240	64	1,051
Farm Credit Insurance Fund distributions	459	-	-
Other noninterest income	32	35	35
Total noninterest income	940	325	1,321
NONINTEREST EXPENSE			
Salaries and employee benefits	3,712	3,745	3,304
Occupancy and equipment	170	163	190
Purchased services from AgVantis, Inc.	321	281	257
Gains on other property owned, net	(4)	-	-
Farm Credit Insurance Fund premium	190	704	608
Supervisory and examination costs	166	155	148
Other noninterest expense	725	726	842
Total noninterest expense	5,280	5,774	5,349
Income before income taxes	7,376	5,632	5,157
(Benefit from)/Provision for income taxes	(80)	(4)	37
Net income	\$ 7,456	\$ 5,636	\$ 5,120

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

Consolidated Statement of Changes in Shareholders' Equity

(Dollars in Thousands)

	Capital Stock and Participation Certificates	Unallocated Retained Earnings	Total Shareholders' Equity
Balance at December 31, 2007	\$ 899	\$ 61,520	\$ 62,419
Net income		5,120	5,120
Stock and participation certificates issued	126		126
Stock and participation certificates retired	(89)		(89)
Patronage Distributions: Cash		(2,200)	(2,200)
Balance at December 31, 2008	936	64,440	65,376
Net income		5,636	5,636
Stock and participation certificates issued	113		113
Stock and participation certificates retired	(89)		(89)
Patronage Distributions: Cash		(2,600)	(2,600)
Balance at December 31, 2009	960	67,476	68,436
Net income		7,456	7,456
Stock and participation certificates issued	104		104
Stock and participation certificates retired	(91)		(91)
Patronage Distributions:			
Cash		(2,800)	(2,800)
Other		34	34
Balance at December 31, 2010	\$ 973	\$ 72,166	\$ 73,139

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

Consolidated Statement of Cash Flows

(Dollars in Thousands)

	For the Year Ended December 31		
	2010	2009	2008
CASH FLOWS FROM OPERATING ACTIVITIES:			
Net income	\$ 7,456	\$ 5,636	\$ 5,120
Adjustments to reconcile net income to net cash provided by/(used in) operating activities:			
Depreciation	88	80	120
Provision for loan losses	250	250	-
Losses/(Gains) on sales of premises and equipment	-	1	(3)
Change in assets and liabilities:			
(Increase)/Decrease in accrued interest receivable	(157)	1,245	1,660
Decrease/(Increase) in prepaid benefit expense	109	128	(538)
(Increase)/Decrease in other assets	(154)	279	(197)
(Decrease)/Increase in accrued interest payable	(293)	(4,166)	819
Increase/(Decrease) in accrued benefits liability	5	4	(802)
(Decrease)/Increase in deferred tax liability	(81)	(4)	35
(Decrease)/Increase in other liabilities	(581)	104	81
Total adjustments	(814)	(2,079)	1,175
Net cash provided by operating activities	6,642	3,557	6,295
CASH FLOWS FROM INVESTING ACTIVITIES:			
Decrease/(Increase) in loans, net	9,929	(27,951)	2,038
Expenditures for premises and equipment, net	(110)	(34)	(223)
Proceeds from sales of other property owned	45	-	42
Net cash provided by/(used in) investing activities	9,864	(27,985)	1,857
CASH FLOWS FROM FINANCING ACTIVITIES:			
Net (repayment of)/draw on note payable to U.S. AgBank, FCB	(8,957)	31,911	(493)
Decrease in advance conditional payments	(4,426)	(5,860)	(5,810)
Capital stock retired	(91)	(89)	(89)
Capital stock issued	104	113	126
Cash patronage distributions paid	(2,766)	(2,000)	(2,500)
Net cash (used by)/provided by financing activities	(16,136)	24,075	(8,766)
Net increase/(decrease) in cash	370	(353)	(614)
Cash at beginning of year	637	990	1,604
Cash at end of year	\$ 1,007	\$ 637	\$ 990
SUPPLEMENTAL CASH INFORMATION:			
Cash paid during the year for:			
Interest	\$ 6,848	\$ 10,978	\$ 11,720
Income taxes	\$ 2	\$ -	\$ 2
SUPPLEMENTAL SCHEDULE OF NON-CASH INVESTING AND FINANCING ACTIVITIES:			
Loans transferred to other property owned	\$ 45	\$ -	\$ 51
Net charge-offs	\$ 64	\$ 9	\$ 6
Patronage distributions payable	\$ 1,800	\$ 1,800	\$ 1,200

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

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(Dollars in Thousands, Except as Noted)

NOTE 1 – ORGANIZATION AND OPERATIONS

- A. Organization: Northern California Farm Credit, ACA and its subsidiaries, Northern California Federal Land Bank Association, FLCA, (Federal Land Credit Association (FLCA)) and Northern California Production Credit Association, (PCA), (collectively called “the Association”) are member-owned cooperatives which provide credit and credit-related services to or for the benefit of eligible borrowers/shareholders for qualified agricultural purposes in the counties of Butte, Glenn, Tehama, Trinity and Shasta in the state of California.

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 (the Farm Credit Act). At December 31, 2010, the System was comprised of four Farm Credit Banks, one Agricultural Credit Bank and approximately 90 associations.

U.S. AgBank, FCB (AgBank), its related associations and AgVantis, Inc. (AgVantis) are collectively referred to as the District. AgBank provides the majority of funding to associations within the District and is responsible for supervising certain activities of the District Associations. AgVantis, which is owned by the entities it serves, provides technology and other operational services to AgBank and certain associations. On December 31, 2010, the District consisted of AgBank, 24 Agricultural Credit Association (ACA) parent companies, which each have two wholly owned subsidiaries, (a FLCA and a PCA), two FLCAs and AgVantis.

In November of 2010, the U.S. AgBank Board of Directors voted to pursue a merger with CoBank, another Farm Credit System Bank. The proposed merger is targeted to be effective on October 1, 2011. The Association does not expect there to be any material negative impact to its operations as a result of the merger.

ACA parent companies provide financing and related services through their FLCA and PCA subsidiaries. Generally, the FLCA makes secured long-term agricultural real estate and rural home mortgage loans and the PCA makes short- and intermediate-term loans for agricultural production or operating purposes.

The Farm Credit Administration (FCA) is delegated authority by Congress to regulate the System Banks and Associations. The FCA examines the activities of System institutions to ensure their compliance with the Farm Credit Act, FCA regulations and safe and sound banking practices.

The Farm Credit Act established the Farm Credit System Insurance Corporation (Insurance Corporation) to administer the Farm Credit Insurance Fund (Insurance Fund). By law, 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 stock at par or stated value, and (3) for other specified purposes. The Insurance Fund is also available for discretionary use by the Insurance Corporation in providing assistance to certain troubled System institutions and to cover the operating expenses of the Insurance Corporation. Each System Bank has been required to pay premiums, which may be passed on to the Associations, into the Insurance Fund based on its annual average outstanding insured debt adjusted to reflect the reduced risk on loans or investments guaranteed by federal or state governments until the assets in the Insurance Fund reach the “secure base amount,” which is defined in the Farm Credit Act as 2.0 percent of the aggregate Insured Debt or such other percentage of the Insured Debt 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, as necessary to maintain the Insurance Fund at the 2 percent level. As required by the Farm Credit Act, as amended, the Insurance Corporation may return excess funds above the secure base amount to System institutions. AgBank passes this premium expense through to each Association based on the Association’s average adjusted note payable with AgBank.

- B. Operations: The Farm Credit Act sets forth the types of authorized lending activity, persons eligible to borrow, and financial services which can be provided 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, their cooperatives, rural residents and farm-related businesses.

The Association also provides other related services such as credit life insurance, multi-peril crop and hail insurance and direct financing leases.

The Association's financial condition may be impacted by factors affecting AgBank. Certain District expenses are allocated to the Associations. Disclosure of certain accounting policies related to these costs is included in the U.S. AgBank District Annual Report to Shareholders (District's Annual Report). The District's Annual Report is available free of charge on AgBank's website, www.usagbank.com; or may be obtained at no charge by contacting the Association at 3435 Silverbell Road, Chico, California 95973 or by calling (530) 895-8698. Upon request, Association shareholders will be provided with a copy of the District's Annual Report, which includes the combined financial statements of AgBank and its related Associations, and AgVantis. The District'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 by the Insurance Corporation.

The lending and financial services offered by AgBank are described in Note 1 of AgBank's Annual Report.

NOTE 2 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The accounting and reporting policies of the Association conform to 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 Association management to make estimates and assumptions that affect the amounts reported in the consolidated financial statements and accompanying notes. Actual results may differ from these estimates. Significant estimates are discussed in these footnotes as applicable.

The consolidated financial statements include the accounts of Northern California FLCA and Northern California PCA. All significant inter-company transactions have been eliminated in consolidation. Recently issued or adopted accounting pronouncements follow.

In July 2010, the Financial Accounting Standards Board (FASB) issued guidance on "Disclosures about the Credit Quality of Financing Receivables and the Allowance for Credit Losses," which is intended to provide additional information to assist financial statement users in assessing an entity's credit risk exposures and evaluating the adequacy of the allowance for credit losses. Existing disclosures are amended to include additional disclosures of financing receivables on a disaggregated basis (by portfolio segment and class of financing receivable) including among others, a rollforward schedule of the allowance for credit losses from the beginning of the reporting period to the end of the period on a portfolio segment basis, with the ending balance further disaggregated on the basis of the method of impairment (individually or collectively evaluated). The guidance also calls for new disclosures including but not limited to credit quality indicators at the end of the reporting period by class of financing receivables, the aging of past due financing receivables, nature and extent of financing receivables modified as troubled debt restructurings by class and the effect on the allowance for credit losses. For non-public entities, all disclosures are effective for interim and annual reporting periods ending after December 15, 2011. The adoption of this Standard will not have an impact on the Association's financial condition or results of operations.

In January 2010, the FASB issued guidance on "Fair Value Measurements and Disclosures," which is to improve disclosures about fair value measurement by increasing transparency in financial reporting. The changes will provide a greater level of disaggregated information and more robust disclosures of valuation techniques and inputs to fair value measurement. The new disclosures and clarification of existing disclosures were effective for interim and annual reporting periods beginning after December 15, 2009, except for the disclosures about purchases, sales, issuances and settlements in the rollforward of activity in Level 3 fair value measurements. Those disclosures were effective for fiscal years beginning after December 15, 2010, and for interim periods within those fiscal years. The adoption of this Standard had no impact on the Association's financial condition and results of operations but resulted in expanded disclosures.

In June 2009, the FASB issued guidance on "Accounting for Transfers of Financial Assets," which amends previous guidance by improving the relevance, representational faithfulness, and comparability of the information that a reporting entity provides in its financial statements about a transfer of financial assets; the effects of a transfer on its financial position, financial performance, and cash flows; and a transferor's continuing involvement, if any, in transferred financial assets. This guidance was effective as of the beginning of each reporting entity's first annual reporting period that begins after November 15, 2009, for interim periods within that first annual reporting period and for interim and annual reporting periods thereafter. Earlier application was prohibited. This Statement must be applied to transfers occurring on or after the effective date. System institutions reviewed their loan participation agreements to ensure that participations would meet the requirements for sales treatment and not be required to be

consolidated. The impact of adoption on January 1, 2010 was immaterial to the Association's financial condition and results of operations.

Below is a summary of our significant accounting policies.

- A. Loans and Allowance for Loan Losses: Long-term real estate mortgage loans generally have original maturities ranging from five to 40 years. Substantially all short- and intermediate-term loans made for agricultural production or operating purposes have maturities of ten years or less. Loans are carried at their principal amount outstanding adjusted for charge-offs and deferred loan fees or costs. Interest on loans is accrued and credited to interest income based upon the daily principal amount outstanding. Loan origination fees and direct loan origination costs are capitalized and the net fee or cost is amortized over the life of the related loan as an adjustment to yield.

Impaired loans are loans for which it is probable that all principal and interest will not be collected according to the contractual terms of the loan and are generally considered substandard or doubtful, which is in accordance with the loan rating model, as described below. 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 contract 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 is collected in full or otherwise discharged.

Loans are generally placed in nonaccrual status when principal or interest is delinquent for 90 days or more (unless adequately collateralized and in the process of collection) or when 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) and/or included in the recorded nonaccrual balance (if accrued in prior years). Loans are charged-off at the time they are determined to be uncollectible.

A restructured loan constitutes a troubled debt restructuring if for economic or legal reasons related to the debtor's financial difficulties the Association grants a concession to the debtor that it would not otherwise consider.

When loans are in nonaccrual status, loan payments are generally applied against the recorded nonaccrual balance. A nonaccrual loan may, at times, be maintained on a cash basis. As a cash basis nonaccrual loan, the recognition of interest income from cash payments received is allowed when the collectibility of the recorded investment in the loan is no longer in doubt and the loan does not have a remaining unrecovered charge-off associated with it. Nonaccrual loans may be returned to accrual status when all contractual principal and interest is current, prior charge-offs have been recovered in full, the ability of the borrower to fulfill the contractual repayment terms is fully expected and the loan is not classified Doubtful or Loss under the Uniform Classification System (UCS).

The Association uses a two-dimensional loan rating model based on an internally generated combined system risk rating guidance that incorporates a 14-point risk-rating scale to identify and track the probability of borrower default and a separate scale addressing loss given default over a period of time. Probability of default is the probability that a borrower will experience a default within 12 months from the date of the determination of the risk rating. A default is considered to have occurred if the lender believes the borrower will not be able to pay its obligation in full or the borrower is past due more than 90 days. The loss given default is management's estimate as to the anticipated economic loss on a specific loan assuming default has occurred or is expected to occur within the next 12 months.

Each of the probability of default categories carries a distinct percentage of default probability. The 14-point risk rating scale provides for granularity of the probability of default, especially in the acceptable ratings. There are nine acceptable categories that range from a borrower of the highest quality to a borrower of minimally acceptable quality. The probability of default between 1 and 9 is very narrow and would reflect almost no default to a minimal default percentage. The probability of default grows more rapidly as a loan moves from a "9" to other assets especially mentioned and grows significantly as a loan moves to a substandard (viable) level. A substandard (non-viable) rating indicates that the probability of default is almost certain.

The credit risk rating methodology is a key component of the Association's allowance for loan losses evaluation, and is generally incorporated into the institution's loan underwriting standards and internal lending limit. 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 provision for loan losses and loan recoveries and is decreased through loan loss reversals and loan charge-offs. The allowance is based on a periodic evaluation of the loan portfolio by management in which numerous factors are considered, including economic conditions, environmental conditions, loan portfolio composition, collateral value, portfolio quality, current production conditions and prior loan loss experience. The allowance for loan losses encompasses various judgments, evaluations and appraisals with respect to the loans and their underlying security that, by their nature, contain elements of uncertainty, imprecision and variability. Changes in the agricultural economy and environment and their impact on borrower repayment capacity will cause various judgments, evaluations and appraisals to change over time. Accordingly, actual circumstances could vary significantly from the Association's expectations and predictions of those circumstances. Management considers the following factors in determining and supporting the level of allowance for loan losses: the concentration of lending in agriculture, combined with uncertainties associated with farmland values, commodity prices, exports, government assistance programs, regional economic effects and weather-related influences.

A specific allowance may be established for impaired loans under GAAP. Impairment of these loans is measured by the present value of expected future cash flows discounted at the loan's effective interest rate or, as practically expedient, by the loan's observable market price, or fair value of the collateral, if the loan is collateral dependent.

- B. Cash: Cash, as included in the consolidated financial statements, represents cash on hand and on deposit at financial institutions.
- C. Investment in AgBank: The Association's investment in AgBank is in the form of Class A Stock. The minimum required investment in AgBank is 5.00 percent of average direct loan volume, net of excess investment. The required investment will be adjusted on a quarterly basis to reflect changes in direct loan volume. The required investment may consist of AgBank surplus attributed to the Association, patronage based stock and purchased stock.
- D. Premises and Equipment: Land is carried at cost. Premises and equipment are carried at cost less accumulated depreciation. 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 operating results. Maintenance and repairs are charged to operating expense and improvements above certain thresholds are capitalized.
- E. Other Assets and Other Liabilities: Other assets are comprised primarily of accounts receivable, prepaid expenses, and investment in Farm Credit institutions. Significant components of other liabilities primarily include accounts payable and employee benefits.
- F. Advance 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. Unrestricted advanced conditional payments are included in other interest bearing liabilities. Restricted advanced conditional payments are primarily associated with mortgage loans, while non-restricted are primarily related to production and intermediate-term loans and insurance proceeds on mortgage loans. Advance conditional payments are not insured. Interest is generally paid by the Association on advance conditional payments.
- G. Employee Benefit Plans: Substantially all employees of the Association participate in the Eleventh District Defined Benefit Retirement Plan (Defined Benefit Plan) and/or the Farm Credit Foundations Defined Contribution/401(k) Plan (Defined Contribution Plan). The Defined Benefit Plan is a noncontributory plan. Benefits are based on compensation and years of service. The Association recognizes its proportional share of expense and contributes its proportional share of funding. Detailed financial information for the Defined Benefit Plan may be found in the District's Annual Report. The Defined Benefit Plan was closed to employees hired after December 31, 1997.

The Defined Contribution Plan has two components. Employees who do not participate in the Defined Benefit Plan may receive benefits through the Employer Contribution portion of the Defined Contribution Plan. In this plan, the Association provides a monthly contribution based on a defined percentage of the employee's salary. Employees may also participate in a Salary Deferral Plan governed by Section 401(k) of the Internal Revenue Code. The Association matches a certain percentage of employee contributions. Employees hired on or after January 1, 1998 are eligible to participate only in the Defined Contribution Plan. All defined contribution costs are expensed in the same period that participants earn employer contributions.

The Association also provides certain health and life insurance benefits to eligible current and retired employees through the Farm Credit Foundation Retiree Medical and Retiree Life Plans. Substantially all employees may become eligible for those benefits if they reach normal retirement age while working for the Association. The anticipated costs of these benefits are accrued during the period of the employee's active service.

- H. Patronage Distribution from AgBank: Patronage distributions are made by AgBank annually, except for certain priority patronage. The Association records patronage distributions from AgBank upon receipt of the distribution.
- I. Income Taxes: As previously described, the ACA holding company conducts its business activities through two wholly owned subsidiaries. Long-term mortgage lending activities are operated through a wholly owned FLCA subsidiary which is exempt from federal and state income tax. Short- and intermediate-term lending activities are operated through a wholly owned PCA subsidiary. Operating expenses are allocated to each subsidiary based on estimated relative service. All significant transactions between the subsidiaries and the parent company have been eliminated in consolidation. The ACA, along with the PCA subsidiary, is subject to income taxes. The Association accounts for income taxes under the liability method. Accordingly, deferred taxes are recognized for estimated taxes ultimately payable or recoverable based on federal, state or local laws.

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 retained earnings. Provisions for income taxes are made only on those earnings that will not be distributed as qualified patronage distributions. Deferred taxes are recorded on the tax effect of all temporary differences based on the assumption that such temporary differences are retained by the Association and will therefore impact future tax payments. A valuation allowance is provided against deferred tax assets to the extent that it is more likely than not (over 50 percent probability), based on management's estimate, the deferred tax assets will not be realized. The consideration of valuation allowances involves various estimates and assumptions as to future taxable earnings, including the effects of the Association's expected patronage program, which reduces taxable earnings.

Deferred income taxes have not been recorded by the Association on stock patronage distributions received from AgBank prior to January 1, 1993, the adoption date of FASB guidance on income taxes. Association management intent is to permanently invest these and other undistributed earnings in AgBank, or if converted to cash, to pass through any such earnings to Association borrowers through qualified patronage allocations.

The Association has not provided deferred income taxes on amounts allocated to the Association which relate to AgBank's post-1992 earnings to the extent that such earnings will be passed through to Association borrowers through qualified patronage allocations. Additionally, deferred income taxes have not been provided on AgBank's post-1992 unallocated earnings. AgBank currently has no plans to distribute unallocated AgBank earnings and does not contemplate circumstances that, if distributions were made, would result in taxes being paid at the Association level.

For California tax purposes, the Association can exclude from taxable income all patronage sourced income. Therefore, the provision for state income taxes is made only on non-patronage sourced earnings.

- J. Fair Value Measurement: FASB guidance defines fair value, establishes a framework for measuring fair value and expands disclosures about fair value measurements. It describes three levels of inputs that may be used to measure fair value:

Level 1 — Quoted prices in active markets for identical assets or liabilities that the reporting entity has the ability to access at the measurement date. Level 1 assets include assets held in trust funds which relate to deferred compensation and the supplemental retirement plan. The trust funds include investments that are actively traded and have quoted net asset values that are observable in the marketplace.

Level 2 — Observable inputs other than quoted prices included within Level 1 that are observable for the asset or liability either directly or indirectly. Level 2 inputs include the following: (a) quoted prices for similar assets or liabilities in active markets; (b) quoted prices for identical or similar assets or liabilities in markets that are not active so that they are traded less frequently than exchange-traded instruments, the prices are not current or principal market information is not released publicly; (c) inputs

other than quoted prices that are observable such as interest rates and yield curves, prepayment speeds, credit risks and default rates; and, (d) inputs derived principally from or corroborated by observable market data by correlation or other means.

Level 3 — Unobservable inputs are those that are supported by little or no market activity and that are significant to the determination of the fair value of the assets or liabilities. These unobservable inputs reflect the reporting entity's own assumptions that market participants would use in pricing the asset or liability. Level 3 assets include certain loans and other property owned.

The fair value disclosures are presented in Note 14.

- K. Off-balance-sheet credit exposures: Commitments to extend credit are agreements to lend to customers, generally having fixed expiration dates or other termination clauses that may require payment of a fee. Commercial letters of credit are conditional commitments issued to guarantee the performance of a customer to a third party. These letters of credit are issued to facilitate commerce and typically result in the commitment being funded when the underlying transaction is consummated between the customer and third party. The credit risk associated with commitments to extend credit and commercial letters of credit is essentially the same as that involved with extending loans to customers and is subject to normal credit policies. Collateral may be obtained based on management's assessment of the customer's creditworthiness.

NOTE 3 – LOANS AND ALLOWANCE FOR LOAN LOSSES

A summary of loans follows.

	December 31		
	2010	2009	2008
Real estate mortgage	\$ 294,689	\$ 273,834	\$ 264,525
Production and intermediate-term	69,184	94,901	58,374
Agribusiness:			
Loans to cooperatives	151	76	–
Processing and marketing	10,542	14,653	3,036
Farm-related business	29,437	28,326	53,903
Rural residential real estate	513	532	660
Lease receivables	22,193	24,425	28,307
Total loans	\$ 426,709	\$ 436,747	\$ 408,805

The Association's concentration of credit risk in various agricultural commodities is shown in the following table.

SIC Category	December 31					
	2010		2009		2008	
	Amount	Percent	Amount	Percent	Amount	Percent
Almonds	\$ 77,960	18.27%	\$ 79,226	18.14%	\$ 67,657	16.55%
Walnuts	63,494	14.88%	63,241	14.48%	53,553	13.10%
Livestock	62,385	14.62%	61,188	14.01%	63,651	15.57%
Rice	57,947	13.58%	54,855	12.56%	45,623	11.16%
Dairy	34,222	8.02%	34,110	7.81%	32,991	8.07%
Irrigated field crops	29,187	6.84%	27,429	6.28%	26,531	6.49%
Prunes	17,835	4.18%	17,120	3.92%	17,742	4.34%
Other orchards	15,746	3.69%	23,628	5.41%	22,689	5.55%
Related business	15,746	3.69%	17,601	4.03%	13,164	3.22%
Other	52,187	12.23%	58,349	13.36%	65,204	15.95%
Total	\$ 426,709	100.00%	\$ 436,747	100.00%	\$ 408,805	100.00%

While the percentages shown in the previous table represent the relative amounts of the Association's potential credit risk as it relates to recorded loan principal, a substantial portion of the Association's loans are collateralized. Accordingly, the Association's exposure to credit loss associated with lending activities is considerably less than the recorded loan balances. An estimate of the Association's current loss exposure is indicated in the consolidated financial statements in the allowance for loan losses.

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 secured by 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 or enhanced 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 loan to value ratios in excess of the regulatory maximum.

The Association has obtained credit enhancements by entering into Standby Commitment to Purchase Agreements (Agreements) with the Federal Agricultural Mortgage Corporation (Farmer Mac), covering loans with principal balance outstanding of \$8.1 million, \$10.6 million and \$15.3 million at December 31, 2010, 2009 and 2008, respectively. Under the Agreements, Farmer Mac agrees to purchase loans from the Association in the event of default (typically four months past due), subject to certain conditions, thereby mitigating the risk of loss from covered loans. In return, the Association pays Farmer Mac commitment fees based on the outstanding balance of loans covered by the Agreements. Such fees, totaling \$44 for 2010, \$64 for 2009 and \$77 for 2008 are reflected in noninterest expense.

Credit enhancements with government agencies of \$3,085 at year-end 2010, \$3,171 at year-end 2009 and \$3,231 at year-end 2008 were outstanding.

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

	December 31		
	2010	2009	2008
Nonaccrual loans:			
Current as to principal and interest	\$ 56	\$ 7	\$ 10
Past due	366	253	78
Total nonaccrual loans	422	260	88
Total impaired loans	\$ 422	\$ 260	\$ 88

There were no loans classified as accruing restructured or accruing loans 90 days or more past due for the years presented.

There were no material commitments to lend additional funds to debtors whose loans were classified impaired for the years presented.

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 and average impaired loans.

	Year Ended December 31		
	2010	2009	2008
Interest income recognized on:			
Nonaccrual loans	\$ 67	\$ 31	\$ 36
Accrual loans 90 days or more past due	1	10	6
Interest income recognized on impaired loans	\$ 68	\$ 41	\$ 42
Average impaired loans	\$ 498	\$ 466	\$ 202

No impaired loans had a related allowance for the periods presented.

Interest income on nonaccrual and accruing restructured loans that would have been recognized under the original terms of the loans follows.

	For the Year Ended December 31		
	2010	2009	2008
Interest income which would have been recognized under the original loan terms	\$ 325	\$ 29	\$ 31
Less: interest income recognized	67	31	36
Interest income not recognized/(recognized)	\$ 258	\$ (2)	\$ (5)

A summary of the changes in the allowance for loan losses follows.

	2010	2009	2008
Balance at beginning of year	\$ 2,294	\$ 2,053	\$ 2,059
Charge-offs:			
Real estate mortgage	65	–	–
Lease receivables	–	9	9
Recoveries:			
Agribusiness	1	–	3
Net charge-offs	64	9	6
Provision for loan losses	250	250	–
Balance at December 31	\$ 2,480	\$ 2,294	\$ 2,053
Net charge-offs as a percentage of average net loans	0.02%	<0.01%	<0.01%

A breakdown of the allowance for loan losses by type of loan and the percent of total allowance follows.

	December 31					
	2010		2009		2008	
	Amount	Percent	Amount	Percent	Amount	Percent
Real estate mortgage	\$ 1,601	64.56%	\$ 1,666	72.63%	\$ 1,416	68.97%
Production and intermediate-term	475	19.15%	225	9.81%	225	10.96%
Agribusiness	278	11.21%	277	12.07%	277	13.49%
Rural residential real estate	4	0.16%	4	0.17%	4	0.20%
Lease receivables	122	4.92%	122	5.32%	131	6.38%
Total	\$ 2,480	100.00%	\$ 2,294	100.00%	\$ 2,053	100.00%

NOTE 4 – INVESTMENT IN AGBANK

The Association is required to maintain an investment in AgBank equal to 5.00 percent of average direct loan volume, net of excess investment. The Association's investment in AgBank may consist of AgBank surplus attributed to the Association patronage based stock and purchased stock. The Association's stock investment in AgBank is in the form of Class A Stock. The investment in AgBank is adjusted on a quarterly basis to reflect changes in direct loan volume, attributed surplus and stock investment balances. If needed to meet capital adequacy requirements, AgBank may require the Association to purchase at-risk stock subject to a limit of one percent of the Association's average Direct Loan Volume in a twelve month period.

NOTE 5 – PREMISES AND EQUIPMENT

Premises and equipment consisted of the following.

	December 31		
	2010	2009	2008
Land	\$ 279	\$ 279	\$ 279
Buildings and leasehold improvements	1,546	1,546	1,548
Furniture, equipment and automobiles	757	697	742
	2,582	2,522	2,569
Less: accumulated depreciation	1,245	1,207	1,207
Total	\$ 1,337	\$ 1,315	\$ 1,362

NOTE 6 – NOTE PAYABLE TO AGBANK

The Association's indebtedness to AgBank 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 is governed by a General Financing Agreement (GFA) which provides for a \$400.0 million line of credit. The GFA and promissory note are subject to periodic renewals in the normal course of business. The Association was in compliance with the terms and conditions of the GFA as of December 31, 2010. Substantially all borrower loans are match-funded with AgBank. Payments and disbursements are made on the note payable to AgBank on the same basis the Association collects payments from and disburses on borrower loans. The interest rate may periodically be adjusted by AgBank based on

the terms and conditions of the borrowing. The weighted average interest rate was 1.91 percent for the year ended December 31, 2010. The line of credit expires on April 30, 2011; however, the Association expects renewal of the line of credit. Upon expiration of the line of credit, undisbursed amounts available under the line of credit expire. So long as the Association is not in material default under the GFA, AgBank will continue to make advances (that do not exceed the amount payable under the promissory note) for undisbursed outstanding commitments on borrower loans which are not in default. The note payable to AgBank will continue until it has been fully discharged.

The Association has the opportunity to commit funds with AgBank in the Earnings Stabilization Management Program at a fixed rate for a specified timeframe. Participants in the program receive a fixed rate credit on the committed funds balance classified as a reduction of interest expense. These committed funds, which are netted against the note payable to AgBank, as of December 31, follow.

	2010	2009	2008
Committed funds	\$16,800	\$25,600	\$ 500
Average rates	2.18%	1.74%	4.09%

Under the Farm Credit Act, the Association is obligated to borrow only from AgBank, unless AgBank gives approval to borrow elsewhere. AgBank, 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, 2010, the Association's notes payable are within the specified limitations.

NOTE 7 – SHAREHOLDERS' EQUITY

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

A. Stock and Participation Certificates

In accordance with the Farm Credit Act, each borrower is required to invest in the Association as a condition of borrowing. The borrower normally acquires ownership of the stock or participation certificates at the time the loan is made, but usually does not make a cash investment. Generally, the aggregate par value of the stock is added to the principal amount of the related loan obligation. The Association has a first lien on the stock or participation certificates owned by its 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.

Capitalization bylaws allow stock requirements to range from the lesser of one thousand dollars or 2.00 percent of the amount of the loan to 10.00 percent of the loan. The Board of Directors has the authority to change the minimum required stock level of a shareholder as long as the change is within this range. Currently, the Association has a stock requirement of the lesser of one thousand dollars or 2.00 percent of the amount of the borrower's combined loan volume.

B. Regulatory Capitalization Requirements and Restrictions

The FCA's capital adequacy regulations require the Association to maintain permanent capital of 7.00 percent of average risk-adjusted assets. Failure to meet the 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 consolidated financial statements. The Association is prohibited from reducing permanent capital by retiring stock or making certain other distributions to shareholders unless the prescribed capital standard is met. The FCA regulations also require other additional minimum standards for capital be maintained. These standards require all System institutions to achieve and maintain ratios of total surplus as a percentage of average risk-adjusted assets of 7.00 percent and of core surplus (generally unallocated surplus) as a percentage of average risk-adjusted assets of 3.50 percent. At December 31, 2010, the Association's permanent capital ratio was 14.78 percent, total surplus ratio was 14.57 percent and core surplus ratio was 13.72 percent.

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

C. Description of Equities

Each owner of class C capital stock is entitled to a single vote. Other classes of borrower equities do not provide voting rights to their owners. Voting stock may not be transferred to another person unless such person is eligible to hold voting stock.

At December 31, 2010, the Association had 190,747 shares of common stock and 3,805 shares of participation certificates outstanding, all at a par value of \$5 per share/unit.

The Association has the authority to issue other classes of stock, no shares of which are outstanding. The voting rights, duties and liabilities of such classes of stock are similar to the classes of stock discussed above.

Any net losses, to the extent that they exceed any contingency reserve and unallocated surplus shall, except as otherwise provided in the Farm Credit Act, be treated as impairing; first, unallocated surplus evidenced by nonqualified written notices of allocation; second, allocated surplus evidenced by qualified written notices of allocation in the reverse order of issuance until all such allocated surplus has been impaired; third, to all classes of common stock and participation certificates until fully impaired; and fourth, to preferred stock (if any) until fully impaired.

In the event of liquidation or dissolution of the Association, any assets remaining after payment or retirement of all liabilities shall be distributed in the following order of priority. First, to the holders, pro rata, of all classes of preferred stock (if any) until an amount equal to the aggregate par value of all such shares then issued and outstanding has been distributed to such holders. Second, to the holders, pro rata, of all classes of common stock and participation certificates, until an amount equal to the aggregate par value of all such shares then issued and outstanding has been distributed to such holders. Third, to the holders of allocated surplus evidenced by qualified written notices of allocation. Fourth, to the holders of unallocated surplus evidenced by non-qualified written notices of allocation. Fifth, any remaining assets after such distributions shall be distributed to present and former patrons on a patronage basis, to the extent practicable.

D. Patronage and/or Dividends

The Association's bylaws provide for the payment of patronage distributions. All patronage distributions to a borrower shall be on such proportionate patronage basis as may be approved by the Association's Board of Directors, consistent with the requirement of Subchapter T of the Internal Revenue Code.

At each year end, the Board of Directors evaluates whether to retain the Association's net income to strengthen its capital position or to distribute a portion of the net income to customers by declaring a qualified/cash patronage refund. For 2010, the Association allocated 37.96 percent of its patronage-sourced net income to its patrons.

For 2010, the Board approved patronage distributions to the borrowers of the ACA of \$1.0 million of 2010 income, which was disbursed in 2010. Another \$1.8 million was declared by the Board in 2010 and will be paid in 2011.

For 2009, the Board approved patronage distributions to the borrowers of the ACA of \$800 thousand of 2009 income, which was disbursed in 2009. Another \$1.8 million was declared by the Board in 2009 and was paid in 2010.

For 2008, the Board approved patronage distributions to the borrowers of the ACA of \$1.0 million of 2008 income, which was disbursed in 2008. Another \$1.2 million was declared by the Board in 2008 and was paid in 2009.

NOTE 8 – PATRONAGE DISTRIBUTION FROM AGBANK

The patronage distribution from AgBank was distributed in cash. Patronage paid by AgBank to the Association was \$240 in 2010, \$64 in 2009 and \$1,051 in 2008.

NOTE 9 – INCOME TAXES

The (benefit from)/provision for income taxes follows.

	For the Year Ended December 31		
	2010	2009	2008
Current:			
State	\$ 2	\$ –	\$ 2
Deferred:			
Federal	(82)	(4)	35
(Benefit from)/Provision for income taxes	\$ (80)	\$ (4)	\$ 37

The (benefit from)/provision 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.

	Year Ended December 31		
	2010	2009	2008
Federal tax at statutory rate	\$ 2,508	\$ 1,915	\$ 1,753
State tax, net	2	–	2
Effect of non-taxable entity	(2,322)	(1,664)	(1,546)
Change in valuation allowance	(1)	–	–
Patronage distributions	(257)	(255)	(169)
Other	(10)	–	(3)
(Benefit from)/Provision for income taxes	\$ (80)	\$ (4)	\$ 37

Deferred tax assets and liabilities are comprised of the following.

	December 31		
	2010	2009	2008
Deferred income tax assets:			
Allowance for loan losses	\$ 227	\$ 142	\$ 145
Accrued annual leave	31	20	24
Nonaccrual loan interest	102	117	107
Net operating loss carryforwards	382	365	365
Gross deferred tax assets	742	644	641
Deferred tax asset valuation allowance	(382)	(365)	(365)
Deferred income tax liabilities:			
Patronage refunds from AgBank	(437)	(437)	(437)
Net deferred tax liability	\$ (77)	\$ (158)	\$ (161)

The calculation of deferred tax assets and liabilities involves various management estimates and assumptions as to future taxable earnings, including the amount of non-patronage income and patronage income retained. The expected future tax rates are based upon enacted tax laws.

The Association recorded a valuation allowance of \$382 during 2010, \$365 during 2009 and 2008. The Association will continue to evaluate the realizability of the deferred tax assets and adjust the valuation allowance accordingly. At December 31, 2010, the Association had federal net operating loss carryforwards that expire from 2022 to 2028.

The Association has no uncertain tax positions as of December 31, 2010, 2009 or 2008. The tax years that remain open for federal and major state income tax jurisdictions are 2007 and forward.

NOTE 10 – EMPLOYEE BENEFIT PLANS

The employees of the Association may participate in the District's defined benefit pension plan (Pension Plan). The Pension Plan is noncontributory and covers a significant number of employees. Benefits are based on compensation and years of service. The Association recognizes its proportional share of expense and contributes its proportional share of funding. As a participant in the District's defined benefit plan, the Association funded \$264 for 2010, \$381 for 2009 and \$1,513 for 2008, through its note payable to AgBank. Pension Plan expenses included in salaries and

employee benefits expense were \$373 for 2010, \$508 for 2009 and \$218 for 2008. Additional financial information for the Pension Plan may be found in the District's Annual Report.

Postretirement benefits other than pensions are also provided through the Farm Credit Foundations Retiree Medical and Retiree Life Plans to eligible current and retired employees of the Association. Benefits provided are determined on a graduated scale, based on years of service. The anticipated costs of these benefits are accrued during the period of the employee's active service. Postretirement benefits expense (primarily health care benefits and life insurance) included in salaries and employee benefits were \$13 for 2010, \$9 for 2009 and \$22 for 2008. Additional financial information for this plan may be found in the District's Annual Report.

The Association also participates in the Farm Credit Foundations Defined Contribution/401(k) Plan (Contribution Plan). The Contribution Plan has two components. Employees who do not participate in the Pension Plan may receive benefits through the Employer Contribution portion of the Contribution Plan. In this plan, the Association provides a monthly contribution based on a defined percentage of the employee's salary. Employees may also participate in a Salary Deferral Plan governed by Section 401(k) of the Internal Revenue Code. The Association matches a certain percentage of employee contributions. Employer contributions to these plans were \$170 for 2010, \$164 for 2009 and \$167 for 2008.

NOTE 11 – 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, amortization schedules and collateral, as those prevailing at the time for comparable transactions with unrelated borrowers.

The Association has a policy that loans to directors and senior officers must be maintained at an Acceptable or Other Assets Especially Mentioned (OAEM) credit classification. If the loan falls below the OAEM credit classification, corrective action must be taken and the loan brought back to either Acceptable or OAEM within a year. If not, the director or senior officer must resign from the Board or employment.

Loan information to related parties for the years ended December 31 is shown below.

	2010	2009	2008
New loans	\$ 985	\$ 360	\$ 119
Repayments	\$ 451	\$ 500	\$ 344
Ending balance	\$ 2,536	\$ 1,991	\$ 2,103

In the opinion of management, none of the loans outstanding to officers and directors at December 31, 2010 involved more than a normal risk of collectibility.

The Association also has business relationships with certain other System entities. The Association paid \$321 in 2010, \$281 in 2009 and \$257 in 2008 to AgVantis for technology services and \$41 in 2009 and \$33 in 2008 to AgBank for operational services. No payments were made to AgBank in 2010.

NOTE 12 – REGULATORY ENFORCEMENT MATTERS

There are no regulatory enforcement actions in effect for the Association.

NOTE 13 – 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. The instruments involve, to varying degrees, elements of credit risk in excess of the amount recognized in the consolidated 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. At December 31, 2010, \$113,885 of commitments to extend 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 Statement of Condition until

funded or drawn upon. The credit risk associated with issuing commitments 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.

With regard to contingent liabilities, there are no actions pending against the Association in which claims for monetary damages are asserted.

NOTE 14 – FAIR VALUE MEASUREMENTS

Accounting guidance defines fair value as the exchange price that would be received for an asset or paid to transfer a liability in an orderly transaction between market participants in the principal or most advantageous market for the asset or liability. The fair value measurement is not an indication of liquidity. See Note 2 for additional information.

The Association has no assets or liabilities measured at fair value on a recurring basis for the periods presented.

At December 31, 2010, the Association had loans measured at fair value on a non-recurring basis that are determined to be Level 3 of \$402 with a recorded loss of \$20. The Association had no assets measured at fair value on a non-recurring basis at December 31, 2009 and 2008 and no liabilities measured at fair value on a non-recurring basis for any of the periods presented.

Valuation Techniques

As more fully discussed in Note 2, accounting guidance establishes a fair value hierarchy, which requires an entity to maximize the use of observable inputs and minimize the use of unobservable inputs when measuring fair value. The following presents a brief summary of the valuation techniques used by the Association for assets and liabilities subject to fair value measurement:

Loans

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

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. Quoted market prices are generally not available for certain 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 follow.

	December 31					
	2010		2009		2008	
	Carrying Amount	Fair Value	Carrying Amount	Fair Value	Carrying Amount	Fair Value
Financial assets:						
Loans, net of allowance	\$ 424,229	\$ 424,627	\$ 434,453	\$ 433,063	\$ 406,752	\$ 410,032
Cash	\$ 1,007	\$ 1,007	\$ 637	\$ 637	\$ 990	\$ 990
Investment in AgBank	\$ 8,102	\$ 8,102	\$ 8,102	\$ 8,102	\$ 8,102	\$ 8,102
Financial liabilities:						
Note payable to AgBank	\$ 348,827	\$ 351,015	\$ 357,784	\$ 359,140	\$ 325,873	\$ 329,280
Advance conditional payments	\$ 11,007	\$ 11,007	\$ 15,433	\$ 15,433	\$ 21,293	\$ 21,293
Commitments to extend credit	\$ –	\$ –	\$ –	\$ NA	\$ –	\$ NA

NA – Not available

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 the value follows.

- A. 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. Since the discount rates are based on the Association'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 the fair value of accruing loans, the loan portfolio is segregated into pools of loans with homogeneous characteristics. 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 as described above, with appropriately higher interest rates, which reflect the uncertainty of continued cash flows. For noncurrent nonaccrual loans, it is assumed that collection will result only from the disposition of the underlying collateral. Fair value of these loans is estimated to equal the aggregate net realizable value of the underlying collateral, discounted at an interest rate, which appropriately reflects the uncertainty of the expected future cash flows over the average disposal period. Where the net realizable value of the collateral exceeds the legal obligation for a particular loan, the legal obligation is generally used in place of the net realizable value.

- B. Cash: The carrying value is a reasonable estimate of fair value.
- C. Investment in AgBank: Estimating the fair value of the Association's investment in AgBank is not practicable because the stock is not traded. As described in Note 4, the investment is a requirement of borrowing from AgBank and is carried at cost plus allocated equities in the accompanying balance sheet. The Association owns 1.28 percent of the issued stock of AgBank as of December 31, 2010. As of that date, AgBank's assets total \$25.39 billion and shareholders' equity totaled \$1.37 billion. AgBank's earnings were \$136.6 million during 2010.
- D. Notes payable to AgBank: 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 interest rate that would be charged for borrowings. For purposes of this estimate, it is assumed the cash flow on the notes payable is equal to the principal payments on the Association's loan receivables plus accrued interest on the notes payable.
- E. Advance conditional payments: The carrying value is a reasonable estimate of fair value as these funds are held in cash.
- F. Commitments to Extend Credit: The fair value of commitments reflects the estimated gain/(loss) assuming undrawn loan commitments are recorded as new loan volume on the fair value measurement date, and considers the difference between current levels of interest rates and the committed rates.

NOTE 16 – QUARTERLY FINANCIAL INFORMATION (UNAUDITED)

Quarterly results of operations for the years ended December 31, 2010, 2009 and 2008, follow.

	2010				
	First	Second	Third	Fourth	Total
Net interest income	\$ 2,828	\$ 4,644	\$ 3,028	\$ 1,466	\$ 11,966
Provision for loan losses	—	—	—	250	250
Noninterest expense, net	799	2,867	1,245	(651)	4,260
Net income	\$ 2,029	\$ 1,777	\$ 1,783	\$ 1,867	\$ 7,456

	2009				
	First	Second	Third	Fourth	Total
Net interest income	\$ 2,674	\$ 2,782	\$ 2,920	\$ 2,955	\$ 11,331
Noninterest expense, net	1,373	1,291	1,440	1,591	5,695
Net income	\$ 1,301	\$ 1,491	\$ 1,480	\$ 1,364	\$ 5,636

	2008				
	First	Second	Third	Fourth	Total
Net interest income	\$ 2,130	\$ 2,308	\$ 2,297	\$ 2,450	\$ 9,185
Noninterest expense, net	1,004	955	1,003	1,103	4,065
Net income	\$ 1,126	\$ 1,353	\$ 1,294	\$ 1,347	\$ 5,120

NOTE 17 – SUBSEQUENT EVENTS

The Association has evaluated subsequent events through March 16, 2011, which is the date the financial statements were issued, and no material subsequent events were identified.



Report of Independent Auditors

To the Board of Directors and Shareholders of
Northern California Farm Credit, ACA:

In our opinion, the accompanying consolidated statements of condition and the related consolidated statements of income, of changes in shareholders' equity, and of cash flows present fairly, in all material respects, the financial position of Northern California Farm Credit, ACA and subsidiaries (the Association) at December 31, 2010, 2009 and 2008, and the results of its operations and its cash flows for the years then ended 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

March 16, 2011

DISCLOSURE INFORMATION REQUIRED BY FARM CREDIT ADMINISTRATION REGULATIONS

(Amounts in Whole Dollars, except as noted)

DESCRIPTION OF BUSINESS

The description of the territory served, persons eligible to borrow, types of lending activities engaged in and financial services offered, and related Farm Credit organizations required to be disclosed in this section is incorporated herein by reference from Note 1 to the 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, required to be disclosed in this section, is incorporated herein by reference from "Management's Discussion and Analysis" (MD&A) included in this annual report to shareholders.

DESCRIPTION OF PROPERTY

The following table sets forth certain information regarding the properties of the Association:

Locations

Main Office

3435 Silverbell Road
Chico, California
530-895-8698

Red Bluff Branch

255 Sale Lane
Red Bluff, California
530-527-1941

Willows Branch

201-A North Tehama Street
Willows, California
530-934-7071

LEGAL PROCEEDINGS AND ENFORCEMENT ACTIONS

Information required to be disclosed in this section is incorporated herein by reference from Note 12 to the financial statements, "Regulatory Enforcement Matters," and Note 13 to the financial statements, "Commitments and Contingencies," included in this annual report to shareholders.

DESCRIPTION OF CAPITAL STRUCTURE

Information required to be disclosed in this section is incorporated herein by reference from Note 7 to the financial statements, "Shareholders' Equity," included in this annual report to shareholders.

DESCRIPTION OF LIABILITIES

The description of debt outstanding required to be disclosed in this section is incorporated herein by reference from Note 6 to the financial statements, "Note Payable to AgBank," included in this annual report to shareholders.

The description of advance conditional payments is incorporated herein by reference to Note 2 to the financial statements, "Summary of Significant Accounting Policies," to the financial statements, included in this annual report to shareholders.

The description of contingent liabilities required to be disclosed in this section is incorporated herein by reference from Note 13 included in this annual report to shareholders.

SELECTED FINANCIAL DATA

The selected financial data for the five years ended December 31, 2010, required to be disclosed in this section is incorporated herein by reference from the "Five-Year Summary of Selected Consolidated Financial Data," included in this annual report to shareholders.

MANAGEMENT'S DISCUSSION AND ANALYSIS

"Management's Discussion and Analysis," which appears within this annual report to shareholders and is required to be disclosed in this section, is incorporated herein by reference.

DIRECTORS AND SENIOR OFFICERS

The following represents certain information regarding the directors and senior officers of the Association.

DIRECTORS

George Swaner, Director, Chairman of the Board

Term of Office: 1996-2011

Mr. Swaner grows rice, hay and has a rice drying operation. He also does custom farming and has a cow-calf operation with his son in the Glenn area. He is involved with the Bayliss Fire Department and California Rice Research Board. He resides in Glenn, California in the county of Glenn.

Thomas B. Martin, Director, Vice Chairman of the Board and Audit Committee

Term of Office: 2004-2013

Mr. Martin grows almonds and walnuts. He is involved with Chico Rotary Club, Butte County Farm Bureau, board member at Superior Ag, member Board of Trustees at Enloe Hospital Foundation and member of California State University Chico Advisory Board. He resides in Chico, California in the county of Butte.

Michael R. Chambers, Director

Term of Office: 1987-2011

Mr. Chambers grows walnuts, prunes, and pears in the Gridley area. He is involved with Butte County Farm Bureau and Sunsweet Growers, Inc. He resides in Gridley, California.

Harry L. "Rick" Cinquini, Director

Term of Office: 2000-2012

Mr. Cinquini grows almonds and walnuts and operates an orchard and vineyard development service which consists of planting and the installation of irrigation systems for growers. He is involved with Butte County Farm Bureau and the North State Hulling Co-Op. He resides in Chico, California.

Glenn E. Hawes, Director

Term of Office: 1995-2013

Mr. Hawes grows walnuts, cereals, peaches, winter pasture and operates a farm and ranch supply business. He is involved with the Shasta County Farm Bureau, Anderson Rotary Club, and California Crop Improvement Association and is on the Shasta County Board of Supervisors. He also owns and operates Stillwater Plains Wetlands Mitigation Bank. He serves on the Sacramento Valley-Wide Air Pollution Control Counsel, the Sacramento River Conservation Area Forum and is a member of the Shasta County Resource Advisory Committee (RAC). He resides in Palo Cedro, California in the county of Shasta.

James M. Holt, Outside Director, Chair of Audit Committee

Term of Office: 1995-2012

Mr. Holt is a certified public accountant with Matson & Isom, Incorporated. Mr. Holt was appointed to the Board in December, 1995. Mr. Holt resides in Chico, California in the county of Butte.

Gregory W. Long, Director

Term of Office: 2005-2011

Mr. Long grows almonds and does custom farm management of almonds, walnuts and prunes. He is involved as a member of the Farm Bureau and Red Bluff High School AG Advisory Committee. He resides in Corning, California in the county of Tehama.

George R. Nicolaus, Director

Term of Office: (March) 2006-2012

Mr. Nicolaus grows almonds and walnuts in the greater Chico area in addition to custom farming and harvest operations. He is also a general partner in two partnerships engaged in residential property development. Mr. Nicolaus is vice-chairman of the North State Hulling, Inc., Cooperative, and chair of the Zimmerman Foundation scholarship committee and is a member of the Butte County Farm Bureau. He resides in Chico, California in the county of Butte.

SENIOR OFFICERS

Bruce V. Strickler

Mr. Strickler has served as president of Northern California Farm Credit, ACA since February 16, 1986. Prior to moving to Chico, he served as president of the Salinas Production Credit Association.

Daniel S. Stevenson

Mr. Stevenson has served as senior vice president since January 1, 1991. Prior to this, he was vice president of the Association.

Robert J. O'Sullivan

Mr. O'Sullivan has served as senior vice president since January 1, 1991. Prior to this, he was vice president of the Association.

Phillip L. Downing

Mr. Downing has served as vice president since 2004 and treasurer since 1987.

Roger L. Limberg

Mr. Limberg has served as regional vice president since 1987.

Joseph L. Macon

Mr. Macon has served as regional vice president since 1987.

Larry E. Mello

Mr. Mello has served as regional vice president since 1987.

Tim Gray

Mr. Gray has served as chief financial officer since November 2010. He is a CPA and most recently served as Controller for a commercial and real estate development firm for the previous six years. Tim also served as Controller for Dole Nut Company (almond & pistachio processor), a wholly-owned subsidiary of Dole Food Company for ten years.

COMPENSATION OF DIRECTORS AND SENIOR OFFICERS

Directors are compensated for their services based on daily honorarium of \$250 and \$100 preparation fee. Directors are also reimbursed for mileage at the rate of \$.50 per mile, as well as documented business expenses while serving in an official capacity. The Compensation and Audit committee meetings were held in conjunction with the regular board meetings, so no additional compensation was paid to the directors for these meetings.

Additional information for each director is provided below.

Name	Number of Days Served at Board Meetings	Number of Days Served in Other Official Activities	Total Compensation Paid During 2010
George Swaner	9	6	\$ 4,650
Thomas B. Martin	8	8	4,800
Michael R. Chambers	9	0	3,150
Rick Cinquini	8	0	2,800
Glenn E. Hawes	9	4	4,150
James M. Holt	9	0	3,150
Gregory W. Long	9	0	3,150
George R. Nicolaus	8	0	2,800
Total Compensation			\$ 28,650

Directors, officers, and employees of the Association are reimbursed for travel, subsistence, and other related expenses which are incurred in the performance of their duties. Each traveler is required to submit travel expenses on forms provided by the Association. They are then reviewed for appropriateness and reimbursed upon approval. A copy of the Association's travel and expense reimbursement policy is available to shareholders upon request. Aggregate reimbursements to directors for travel, subsistence and other related expenses were \$10,146.71 in 2010, \$7,038.49 in 2009 and \$16,986.47 in 2008. There was no noncash compensation paid to directors in 2010.

Information on the Chief Executive Officer (CEO) and senior officer compensations is provided below.

President and CEO	Year	Salary	Non Equity Incentive Plan Compensation	Other	Total
Bruce V. Strickler	2010	\$ 218,500	\$ 37,054	\$ 6,303	\$ 261,857
Bruce V. Strickler	2009	\$ 212,100	\$ 30,673	\$ 4,079	\$ 246,852
Bruce V. Strickler	2008	\$ 202,000	\$ 19,913	\$ 3,497	\$ 225,410

Aggregate Number of Senior Officers	Year	Salary	Non Equity Incentive Plan Compensation	Other	Total
7	2010	\$ 645,888	\$ 108,342	\$ 2,565	\$ 756,795
6	2009	\$ 614,175	\$ 101,969	\$ 3,558	\$ 719,702
6	2008	\$ 591,584	\$ 103,382	\$ 5,157	\$ 700,123

All Association employees, including the herein stated group of senior officers, are covered by the compensation plans described below. Additionally, all employees are covered by district-wide pension and retirement plans described in the notes to the financial statements.

- A. **Base Salary:** All officers and employees are paid a base salary which is primarily established by position class descriptions adopted by the Association. Also, the officer's or employee's length of service, their performance, and competitive compensation factors are considered in establishing their base annual salary.
- B. **Non Equity Incentive Plan Compensation:** All officers and employees participate in two separate bonus programs that are approved annually by the board of directors. The first plan uses criteria based on new loan volume originated and Association profitability as measured by return on average assets. The plan year is the same as the calendar year and is paid out during the year earned. The second plan is a program based on Association success as measured by patronage paid to the borrowers and the amount to be paid is a percentage of the patronage paid to borrowers. Payment is made in the same year as patronage is distributed to borrowers – generally the year following the declaration of the patronage.
- C. **Other:** Other compensation consists of the sale back of unused vacation hours.

Disclosure of information on total compensation paid during the last fiscal year to any senior officer is available to shareholders upon request.

TRANSACTIONS WITH SENIOR OFFICERS AND DIRECTORS

The Association's policies on loans to and transactions with its officers and directors, required to be disclosed in this section are incorporated herein by reference from Note 11 to the financial statements, "Related Party Transactions," included in this annual report to shareholders.

INVOLVEMENT OF SENIOR OFFICERS AND DIRECTORS IN CERTAIN LEGAL PROCEEDINGS

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

BORROWER PRIVACY STATEMENT

Since 1972, Farm Credit Administration (FCA) regulations have forbidden the directors and employees of Farm Credit institutions from disclosing personal borrower information to others without borrower consent. The Association does not sell or trade customers' personal information to marketing companies or information brokers. Additional information regarding FCA rules governing the disclosure of customer information can be obtained by contacting the Association.

RELATIONSHIP WITH INDEPENDENT AUDITORS

There were no changes in independent auditors since the prior annual report to shareholders and there were no material disagreements with our independent auditors on any matter of accounting principles or financial statement disclosure during this period.

RELATIONSHIP WITH U.S. AGBANK, FCB (AGBANK)

The Association is materially affected by AgBank's financial condition and results of operations.

The Association's statutory obligation to borrow from AgBank is discussed in Note 6. Financial assistance agreements between the Association and AgBank are discussed in Note 7. Association requirement to invest in AgBank and AgBank's ability to access capital of the Association is discussed in Note 4 to the financial statements, "Investment in AgBank." AgBank's role in mitigating the Association's exposure to interest rate risk is discussed in the MD&A section – Liquidity.

AgBank is required to distribute its Annual Report to shareholders of the Association if a "significant event," as defined by FCA regulations occurs.

FINANCIAL STATEMENTS

The financial statements, together with the report thereon of PricewaterhouseCoopers LLP dated March 16, 2011, and the Report of Management, appearing as part of this annual report to shareholders, are incorporated herein by reference.

AGBANK ANNUAL AND QUARTERLY REPORTS TO SHAREHOLDERS

The shareholders' investment in the Association is materially affected by the financial condition and results of operations of AgBank. Consequently, the Association's annual and quarterly reports should be read in conjunction with AgBank's Annual and Quarterly Reports to Shareholders. Quarterly reports are available approximately 40 days after the calendar quarter end and annual reports are available approximately 75 days after the calendar year end. A copy of these reports may be obtained free upon request from the Association. The Association is located at 3435 Silverbell Road, Chico, California 95973, or may be contacted by calling (530) 895-8698. The reports may also be obtained free of charge by visiting AgBank's website at www.usagbank.com.

AFFIRMATIVE ACTION PLAN AND EQUAL EMPLOYMENT OPPORTUNITY POLICY

The Association has adopted an Affirmative Action Plan and Equal Employment Opportunity Policy.