

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

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**2007  
Quarterly Report  
Second Quarter**



**For the Quarter Ended June 30, 2007**



Part of the Farm Credit System

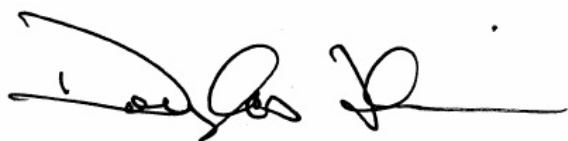
## REPORT OF MANAGEMENT

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

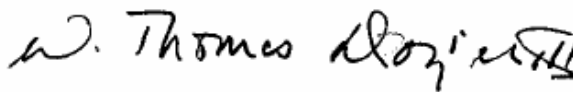
To meet its responsibility for reliable financial information, management depends on the Farm Credit Bank of Texas' (Bank) and the Association's accounting and internal control systems, which have been designed to provide reasonable, but not absolute, assurance that assets are safeguarded and transactions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

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

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



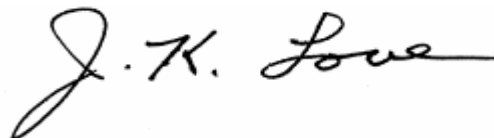
Douglas Thiessen, Chief Executive Officer  
August 1, 2007



W. Thomas Dozier, III, Chairman, Board of Directors  
August 1, 2007



M. Scott Sellers, CPA, Chief Financial Officer  
August 1, 2007



J.K. Love, CPA, Chairman, Audit Committee  
August 1, 2007

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

The following commentary reviews the financial performance of the Federal Land Bank Association of South Alabama, FLCA (Federal Land Credit Association), referred to as the Association, for the quarter and the six months ended June 30, 2007. These comments should be read in conjunction with the accompanying financial statements and the December 31, 2006 Annual Report of the Association.

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

### **Results of Operations:**

The Association had net income of \$679,731 and \$3,664,163 for the three and six months ended June 30, 2007, as compared to net income of \$1,818,653 and \$4,560,519 for the same periods in 2006, reflecting a decrease of 62.6 and 19.7 percent, respectively. Net interest income was \$3,846,488 and \$7,835,661, respectively, for the three and six months ended June 30, 2007, compared to \$3,600,535 and \$7,200,731 for the same periods in 2006. Interest income increased by \$2,495,586 or 14.7 percent, from the first six months of 2006, primarily due to a slight increase in yields on earning assets coupled with an increase in average loan volume. Interest expense for the first six months of 2007 increased by \$1,860,656, or 18.9 percent, from the same period of 2006 due to a slight increase in interest rates and an increase in average debt volume. The provision for loan losses for the first six months of 2007 increased by \$1,120,931, or 124.6 percent, over the same period of 2006, due to specific reserves recorded for two large credits, the larger of which is explained further in the "Loan Portfolio" section of Management's Discussion and Analysis, below. Average loan volume for the second quarter of 2007 was \$514,369,185, compared to \$471,094,041 in the second quarter of June 30, 2006.

Noninterest income for the three months ended June 30, 2007 decreased by \$51,546, or 11.4 percent, over the same period of 2006. This is due primarily to a decrease in loan fees resulting from lower origination fees and less activity from the Capital Markets of the South group (CMS) in the second quarter of 2007 versus the second quarter of 2006. The reduced origination fees were caused by lower average closing fee per loan as a result of competitive pressures, despite the fact that more loans were closed, in number and volume, in the second quarter of 2007 compared to the same time frame in 2006. CMS activity was less in the second quarter of 2007 as a result of the CMS member associations deciding to discontinue the joint venture during the quarter, as explained further in Note 4 to the financial statements included in this quarterly report. These decreases were partially offset by higher patronage income from Farm Credit Bank of Texas (the Bank) in the second quarter of 2007 as compared to the second quarter of 2006. The patronage income was higher due to a higher investment in the Bank thus far in 2007 as compared to 2006.

Noninterest income for the six months ended June 30, 2007 decreased by \$8,757, or 1.0 percent, over the same period of 2006. This overall slight decrease is due primarily to competitive pressures driving origination fees lower, as noted above. The decrease in origination fees was mostly offset by increases in income from CMS activity, patronage income from the Bank, and the Association's pro-rata share of earnings in the Farm Credit System Association Captive Insurance Company (the Captive).

Noninterest expenses for the three months ended June 30, 2007 increased by \$161,828, or 12.1 percent, as compared to the same period in 2006. Noninterest expenses for the six months ended June 30, 2007 increased by \$401,598, or 15.2 percent, as compared to the same period in 2006. The increase for both time frames is due primarily to increases in each of the following categories: salaries and employee

benefits costs, directors' expense, purchased services expense, and Farm Credit System Insurance Corporation (FCSIC) premium expense. These expense increases were offset partially by an increase in CMS expense reimbursements. The increase in salaries and employee benefits is primarily due to the normal annual increase in compensation rates from the prior year for all employees, plus the unusual circumstance of overlapping cost from hiring the Association's new CEO in January 2007 and still having the retiring CEO on the payroll until his official retirement date of June 1, 2007. Directors' expense increased as a result of having one additional outside director, appointed in early 2007, and more director-related activities in the second quarter and YTD in 2007 than the same measurement periods in 2006. Purchased services increased primarily due to legal and consulting fees incurred in connection with protecting the Association's interests in credit-related matters with borrowers with large credits from the Association, as noted below in the "Loan Portfolio" section of the Management's Discussion and Analysis. FCSIC premiums increased on the basis of the Association having higher loan volume in the second quarter and YTD in 2007 than the same measurement periods in 2006. CMS expense reimbursements increased because the majority of the legal and consulting fees incurred as mentioned above were related to a CMS loan.

The Association recorded \$1,025,200 in charge-offs and no recoveries for the quarter ending June 30, 2007, and \$1,076,880 in charge-offs and no recoveries for the same period in 2006. The Association's allowance for loan losses was 0.3 percent and 0.1 percent of total loans outstanding as of June 30, 2007, and 2006, respectively.

The Association's return on average assets for the six months ended June 30, 2007, was 1.40 and 1.91 percent for the same period in 2006. The Association's return on average equity for the six months ended June 30, 2007, was 8.12 and 11.23 percent for the same period in 2006.

### **Loan Portfolio:**

The Association's loan portfolio at June 30, 2007 consisted of 3,749 loans that totaled \$528,171,893. The total loan volume, stated as recorded investment plus accrued interest, increased \$19.6 million (3.8 percent) since December 31, 2006, primarily due to the continued demand for real estate and continued marketing and service efforts.

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

	<u>June 30, 2007</u>	<u>December 31, 2006</u>
Acceptable	98.5 %	97.6 %
Special Mention	0.3 %	1.7 %
Substandard	1.2 %	0.7 %
Total	<u>100.0 %</u>	<u>100.0 %</u>

The major commodity concentrations within the Association's loan volume are timber, cattle, poultry, and field crops.

High-risk assets include nonaccrual loans, loans that are past due 90 days or more and still accruing interest, formally restructured loans and other property owned. The following table illustrates the Association's components and trends of high-risk assets.

	<b>June 30, 2007</b>		December 31, 2006	
	<b>Amount</b>	<b>%</b>	Amount	%
Nonaccrual	<b>\$ 6,153,656</b>	<b>98.5%</b>	\$ 595,219	100.0%
90 days past due and still accruing interest	-	<b>0.0%</b>	-	0.0%
Formally restructured	-	<b>0.0%</b>	-	0.0%
Other property owned, net	<b>92,075</b>	<b>1.5%</b>	-	0.0%
Total	<b>\$ 6,245,731</b>	<b>100.0%</b>	<b>\$ 595,219</b>	<b>100.0%</b>

Nonaccrual loans as a percentage of total loans outstanding were 1.2 percent at June 30, 2007, compared to 0.1 percent at December 31, 2006. Nonaccrual loans increased compared to December 31, 2006 because two large loans were placed in nonaccrual status; one loan was reclassified due to the deteriorating financial condition of the borrower, and the other loan is described in the paragraph below. These same two loans were previously classified as Special Mention at December 31, 2006.

The Association originated a loan to one borrower through CMS and participated the loan to 13 other Farm Credit associations, with the Association serving as the lead lender. The original funded balance of the loan was \$68.5 million, and the Association retained 5.56% of the loan. During the second quarter of 2007, the loan was deemed to be nonaccrual due to its significant undercollateralized position and a credit default. Accordingly, the Association recorded a specific reserve of \$1.761 million, and subsequently charged off \$1.025 million, resulting in a remaining specific reserve of \$736 thousand at June 30, 2007. As of June 30, 2007 the Association's portion of the loan principal balance outstanding is \$2.711 million. The Association is currently pursuing collection efforts regarding this loan. For more information on impaired loans and the allowance for loan losses, see Note 2 to the financial statements included in this quarterly report.

### **Liquidity and Funding Sources:**

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

	<b>June 30, 2007</b>	December 31, 2006
Note payable to the Bank	<b>\$ 441,967,999</b>	\$ 423,598,301
Accrued interest on note payable	<b>2,014,354</b>	1,925,238
Total	<b>\$ 443,982,353</b>	<b>\$ 425,523,539</b>

### **Capital Resources:**

The Association's capital position increased by \$751,746 at June 30, 2007, compared to December 31, 2006. The Association's debt as a ratio to members' equity was 4.91:1 as of June 30, 2007, compared to 4.74:1 as of 2006.

In January 2007, the Association's board of directors declared a cash patronage of \$3,000,000 of the Association's 2006 earnings to be paid to the stockholders. The patronage distribution was completed in the second quarter of 2007. See Note 3 to the financial statements included in this quarterly report and Note 6 to the financial statements included in the 2006 Annual Report for further discussion.

Under regulations governing minimum permanent capital adequacy and other capitalization issues, the Association is required to maintain a minimum adjusted permanent capital of seven percent of risk-adjusted assets as defined by the FCA. The Association's permanent capital ratio at June 30, 2007, was 16.1 percent, which is in compliance with the FCA's minimum permanent capital standard. The Association's core surplus ratio and total surplus ratio at June 30, 2007, were 15.4 and 15.4 percent, respectively, which is in compliance with the FCA's minimum surplus standard.

### **Other Accounting Issues:**

On September 30, 2006, the Financial Accounting Standards Board issued Statement of Financial Accounting Standards No. 158 – Employers' Accounting for Defined Benefit Pension and Other Postretirement Plans. Beginning in 2007, FAS 158 requires certain disclosures about the funded status of the Association's postretirement plans, as well as a change in the measurement date of related plan liabilities. For further discussion on the Association's Defined Benefit and other employee benefit plans, see Notes 1 and 5 to the financial statements included in this quarterly report, and Notes 2 and 8 to the financial statements included in the December 31, 2006 Annual Report.

### **Relationship with the Farm Credit Bank of Texas:**

The Association's financial condition may be impacted by factors that affect the Bank. The financial condition and results of operations of the Bank may materially affect the stockholder's investment in the Association. The Management's Discussion and Analysis and Notes to Financial Statements contained in the December 31, 2006 Annual Report of Federal Land Bank Association of South Alabama, FLCA more fully describe the Association's relationship with the Bank.

The Tenth Farm Credit District's (District) annual and quarterly stockholder reports are available free of charge, upon request. These reports can be obtained by writing to Farm Credit Bank of Texas, The Ag Agency, P.O. Box 202590, Austin, Texas 78720, or by calling (512) 483-9260. Copies of the District's quarterly and annual stockholder reports also can be requested by e-mail at [fcf@farmcreditbank.com](mailto:fcf@farmcreditbank.com). The District makes its annual and quarterly stockholder reports available on its Web site at [www.farmcreditbank.com](http://www.farmcreditbank.com).

The Association's quarterly stockholder reports are also available free of charge, upon request. These reports can be obtained by writing to Federal Land Bank Association of South Alabama, FLCA, P.O. Box 241687, Montgomery, Alabama, 36124-1687, or by calling (334) 270-8687. Copies of the reports can also be requested by e-mailing [awolf@farmcreditbank.com](mailto:awolf@farmcreditbank.com). The Association makes its annual and quarterly stockholder reports available on its Web site at [www.alabamalandloan.com](http://www.alabamalandloan.com).

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

**BALANCE SHEET**

	<b>June 30, 2007 (unaudited)</b>	December 31, 2006
	<hr/>	<hr/>
<b><u>ASSETS</u></b>		
Cash	\$ 3,094,549	\$ 1,699,487
Loans	518,915,086	500,257,260
Less: allowance for loan losses	1,450,921	455,588
Net loans	<hr/> 517,464,165	<hr/> 499,801,672
Accrued interest receivable	9,256,807	8,344,502
Investment in and receivable from the Bank:		
Capital stock	8,047,100	8,047,100
Accrued patronage receivable	-	267,470
Other property owned, net	92,075	-
Premises and equipment	1,696,529	1,710,844
Other assets	273,077	185,478
Total assets	<hr/> <b>\$ 539,924,302</b> <hr/>	<hr/> <b>\$ 520,056,553</b> <hr/>
 <b><u>LIABILITIES</u></b>		
Note payable to the Bank	\$ 441,967,999	\$ 423,598,301
Accrued interest payable	2,014,354	1,925,238
Drafts outstanding	2,529,297	1,311,196
Other liabilities	2,121,970	2,682,882
Total liabilities	<hr/> <b>448,633,620</b> <hr/>	<hr/> <b>429,517,617</b> <hr/>
 <b><u>MEMBERS' EQUITY</u></b>		
Capital stock and participation certificates	3,223,305	3,150,865
Unallocated retained earnings	88,067,377	87,388,071
Total members' equity	<hr/> <b>91,290,682</b> <hr/>	<hr/> <b>90,538,936</b> <hr/>
Total liabilities and members' equity	<hr/> <b>\$ 539,924,302</b> <hr/>	<hr/> <b>\$ 520,056,553</b> <hr/>

The accompanying notes are an integral part of these financial statements

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

**STATEMENT OF INCOME**

(unaudited)

	<b>For the Three Months Ended June 30,</b>		<b>For the Six Months Ended June 30,</b>	
	<b>2007</b>	2006	<b>2007</b>	2006
<b><u>INTEREST INCOME</u></b>				
Loans	<b>\$ 9,779,691</b>	\$ 8,723,554	<b>\$ 19,530,476</b>	\$ 17,034,890
<b><u>INTEREST EXPENSE</u></b>				
Note payable to the Bank	<b>5,933,203</b>	5,123,019	<b>11,694,815</b>	9,834,159
Net interest income	<b>3,846,488</b>	3,600,535	<b>7,835,661</b>	7,200,731
<b><u>PROVISION FOR LOSSES</u></b>				
Provision for loan losses	<b>2,070,626</b>	899,125	<b>2,020,534</b>	899,603
Net interest income after provision for loan losses	<b>1,775,862</b>	2,701,410	<b>5,815,127</b>	6,301,128
<b><u>NONINTEREST INCOME</u></b>				
Patronage income from the Bank	<b>109,547</b>	92,881	<b>218,755</b>	179,974
Loan fees	<b>294,464</b>	349,531	<b>627,022</b>	673,690
Financially related services income	<b>1,147</b>	1,133	<b>2,741</b>	2,966
Gain (loss) on sale of premises and equipment, net	<b>(5,994)</b>	4,665	<b>(5,994)</b>	4,665
Other noninterest income	<b>-</b>	2,500	<b>44,878</b>	34,864
Total noninterest income	<b>399,164</b>	450,710	<b>887,402</b>	896,159
<b><u>NONINTEREST EXPENSES</u></b>				
Salaries and employee benefits	<b>895,327</b>	774,802	<b>1,842,346</b>	1,590,932
Directors' expense	<b>63,615</b>	45,517	<b>124,188</b>	99,269
Purchased services	<b>195,111</b>	176,592	<b>392,082</b>	291,540
Travel	<b>62,636</b>	60,577	<b>129,949</b>	116,019
Occupancy and equipment	<b>61,222</b>	52,695	<b>115,106</b>	105,994
Communications	<b>19,152</b>	15,030	<b>39,316</b>	32,704
Advertising	<b>24,357</b>	30,957	<b>39,668</b>	53,721
Public and member relations	<b>18,512</b>	21,948	<b>55,443</b>	59,521
Supervisory and exam expense	<b>46,654</b>	43,985	<b>93,309</b>	87,970
FCSIC insurance expense	<b>208,894</b>	168,625	<b>417,574</b>	353,879
Other noninterest expense	<b>37,099</b>	31,675	<b>55,577</b>	49,617
CMS expense reimbursements	<b>(137,284)</b>	(88,936)	<b>(266,192)</b>	(204,398)
Total noninterest expenses	<b>1,495,295</b>	1,333,467	<b>3,038,366</b>	2,636,768
Net income	<b>\$ 679,731</b>	\$ 1,818,653	<b>\$ 3,664,163</b>	\$ 4,560,519

The accompanying notes are an integral part of these financial statements

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

**STATEMENT OF CHANGES IN MEMBERS' EQUITY**

(unaudited)

	<b>Capital Stock/ Participation Certificates</b>	<b>Unallocated Retained Earnings</b>	<b>Total Members' Equity</b>
Balance at December 31, 2005	\$ 2,888,490	\$ 77,298,045	\$ 80,186,535
Net income	-	4,560,519	4,560,519
Capital stock/participation certificates issued	331,440	-	331,440
Capital stock/participation certificates retired	(196,775)	-	(196,775)
Patronage refunds:			
Cash	-	(1,200,000)	(1,200,000)
<b>Balance at June 30, 2006</b>	<b>\$ 3,023,155</b>	<b>\$ 80,658,564</b>	<b>\$ 83,681,719</b>
Balance at December 31, 2006	\$ 3,150,865	\$ 87,388,071	\$ 90,538,936
Net income	-	3,664,163	3,664,163
Capital stock/participation certificates issued	354,260	-	354,260
Capital stock/participation certificates retired	(281,820)	-	(281,820)
Patronage refunds:			
Cash	-	(3,000,000)	(3,000,000)
Change in patronage declared and paid	-	15,143	15,143
<b>Balance at June 30, 2007</b>	<b>\$ 3,223,305</b>	<b>\$ 88,067,377</b>	<b>\$ 91,290,682</b>

The accompanying notes are an integral part of these financial statements

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

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

The Federal Land Bank Association of South Alabama, FLCA (Federal Land Credit Association), referred to as the Association, is a member-owned cooperative that provides credit and credit-related services to or for the benefit of eligible borrowers/stockholders for qualified agricultural purposes. The Association serves the counties of Autauga, Baldwin, Barbour, Bibb, Bullock, Butler, Chambers, Chilton, Choctaw, Clarke, Coffee, Conecuh, Coosa, Covington, Crenshaw, Dale, Dallas, Elmore, Escambia, Geneva, Greene, Hale, Henry, Houston, Lee, Lowndes, Macon, Marengo, Mobile, Monroe, Montgomery, Perry, Pickens, Pike, Russell, Sumter, Tallapoosa, Tuscaloosa, Washington and Wilcox in the state of Alabama. The Association is a lending institution of the Farm Credit System (the System), which was established by Acts of Congress to meet the needs of American agriculture.

A description of the Association's significant accounting policies and the financial condition and results of operations as of December 31, 2006 are contained in the 2006 Annual Report to the stockholders. These unaudited second quarter 2007 financial statements should be read in conjunction with the 2006 Annual Report to the stockholders.

On September 30, 2006, the Financial Accounting Standards Board issued Statement of Financial Accounting Standards No. 158 – Employers' Accounting for Defined Benefit Pension and Other Postretirement Plans. The Standard requires an employer to recognize the overfunded or underfunded status of a defined benefit postretirement plan as an asset or liability in its statement of financial position and recognize changes in that funded status in the year in which the changes occur through comprehensive income. The Standard is effective for employers with publicly traded securities for the fiscal year ending after December 15, 2006 and for employers without publicly traded securities for the fiscal year ending after June 15, 2007. The Association will be required to implement the Standard for the year ended December 31, 2007. In addition, this Standard requires that the funded status of a plan be measured as of the date of the year-end financial statements. Currently, the Association uses a measurement date of September 30<sup>th</sup>. The requirement to measure the funded status as of the fiscal year-end is effective for fiscal years ending after December 15, 2008. The Association is currently evaluating the impact of implementing this Standard. It is anticipated that the implementation of this Standard will have no impact on the income statement and, based on the current funded status of the defined benefit plans, it is not expected to have a material or significant impact on the balance sheet.

The accompanying financial statements contain all adjustments necessary for a fair presentation of the interim financial condition and results of operations and conform with generally accepted accounting principles, except for the inclusion of a statement of cash flows. Generally accepted accounting principles require a business enterprise that provides a set of financial statements reporting both financial position and results of operations to also provide a statement of cash flows for each period for which results of operations are provided. In regulations issued by FCA, associations have the option to exclude statements of cash flows in interim financial statements. Therefore, the Association has elected not to include a statement of cash flows in these financial statements.

The preparation of these financial statements requires the use of management's estimates. The results for the quarter and the six months ended June 30, 2007, are not necessarily indicative of the results to be expected for the year ended December 31, 2007. Certain amounts in the prior period's financial statements have been reclassified to conform to current financial statement presentation.

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

The allowance for loan losses is maintained at a level considered adequate by management to provide for estimated losses inherent in the loan portfolio. The allowance is based on a periodic evaluation of the loan portfolio by management in which numerous factors are considered, including economic conditions, loan portfolio composition and prior loan loss experience. An analysis of the allowance for loan losses follows:

	<b>June 30, 2007</b>	June 30, 2006
Balance at beginning of quarter	\$ 405,495	\$ 513,343
Provision for loan losses	2,070,626	899,125
Charge-offs	(1,025,200)	(1,076,880)
Recoveries	-	-
Balance at end of quarter	<u>\$ 1,450,921</u>	<u>\$ 335,588</u>

The following table presents information concerning impaired loans:

	<b>June 30, 2007</b>	June 30, 2006
Impaired loans with related allowance	\$ 5,891,701	\$ 343,355
Impaired loans with no related allowance	261,955	288,503
Total impaired loans	<u>\$ 6,153,656</u>	<u>\$ 631,858</u>
Allowance on impaired loans	\$ 1,287,760	\$ 122,187
Average impaired loans	\$ 3,853,383	\$ 653,095
Interest income on impaired loans for the quarter	\$ 15,645	\$ -

**NOTE 3 — CAPITAL:**

The Association's board of directors has established a Capital Adequacy Plan (Plan) that includes the capital targets that are necessary to achieve the institution's capital adequacy goals as well as the minimum permanent capital standards. The Plan monitors projected dividends, equity retirements and other actions that may decrease the Association's permanent capital. In addition to factors that must be considered in meeting the minimum standards, the board of directors also monitors the following factors: capability of management; quality of operating policies, procedures, and internal controls; quality and quantity of earnings; asset quality and the adequacy of the allowance for losses to absorb losses inherent within the loan portfolio; sufficiency of liquid funds; needs of an institution's customer base; and any other risk-oriented activities, such as funding and interest rate risk, potential obligations under joint and several liability, contingent and off-balance-sheet liabilities or other conditions warranting additional capital. At least quarterly, management reviews the Association's goals and objectives with the board.

In January 2007 the board declared a \$3,000,000 cash patronage to be paid to stockholders from the Association's 2006 earnings. The patronage distribution to the stockholders was completed in the second quarter of 2007.

#### NOTE 4 — CAPITAL MARKETS:

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

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

As of June 30, 2007 and 2006, the Association had CMS-related loan volume outstanding of \$28,672,811 and \$30,349,191, respectively. In addition, the Association had remaining commitments on CMS loans to lend an additional \$21,371,123 as of June 30, 2007.

#### NOTE 5 — EMPLOYEE BENEFIT PLANS:

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

	Other Benefits	
	2007	2006
Service cost	\$ 22,484	\$ 26,042
Interest cost	31,394	26,996
Expected return on plan assets	-	-
Amortization of prior service costs	(21,750)	(21,186)
Amortization of net (gain) loss	394	2,388
Net periodic benefit cost	<u>\$ 32,522</u>	<u>\$ 34,240</u>

The Association previously disclosed in its Annual Report to the stockholders for the year ended December 31, 2006, that it expected to contribute \$13,119 to its post-retirement health and welfare benefits plan in 2007. As of June 30, 2007, \$3,786 of contributions have been made. The Association's liability for the plan's unfunded accumulated benefit obligation at June 30, 2007 was \$1,342,527 and is included in "Other liabilities" in the balance sheet.