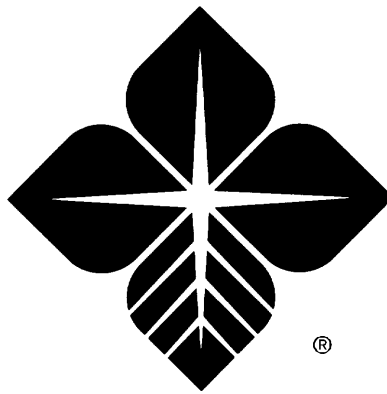


HERITAGE LAND BANK, ACA

2009 Quarterly Report First Quarter



For the Quarter Ended March 31, 2009

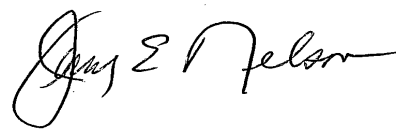
REPORT OF MANAGEMENT

The undersigned certify that we have reviewed this report, that it has been prepared in accordance with all applicable statutory or regulatory requirements, and that the information contained herein is true, accurate and complete to the best of his or her knowledge and belief.



Stephen Ogletree, Chief Executive Officer

April 29, 2009



Jerry Nelson, Audit Committee Chairman

April 29, 2009



Jenny Sloan, Chief Financial Officer

April 29, 2009

**HERITAGE LAND BANK, ACA
MANAGEMENT'S DISCUSSION AND ANALYSIS**

The following commentary reviews the financial performance of the Heritage Land Bank, ACA (Agricultural Credit Association), referred to as the Association, for the quarter and three months ended March 31, 2009. These comments should be read in conjunction with the accompanying financial statements and the December 31, 2008 Annual Report of the Association.

The consolidated financial statements comprise the operations of the ACA and its wholly-owned subsidiaries. The consolidated financial statements were prepared under the oversight of the Association's audit committee.

Loan Portfolio:

Total loans outstanding at March 31, 2009, including nonaccrual loans were \$449,466,787 compared to \$449,887,810 at December 31, 2008, reflecting a decrease of 0.1 percent. The slight decrease in loan volume is related to the slowing in demand for new loan financing in the first quarter which management attributes to the current economic environment. Nonaccrual loans as a percentage of total loans outstanding were 3.9 percent at March 31, 2009, compared to 3.4 percent at December 31, 2008. The increase in nonaccrual loan volume in the first quarter of 2009 is primarily related to one loan. The specifics about this loan are discussed in the next section, Risk Exposure.

The Association recorded \$14,616 in recoveries and \$46,124 in charge-offs for the quarter ending March 31, 2009, and no recoveries or charge-offs for the same period in 2008. The Association's allowance for loan losses was 0.4 percent and 0.4 percent of total loans outstanding as of March 31, 2009, and December 31, 2008, respectively.

Risk Exposure:

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

	<u>March 31, 2009</u>		<u>December 31, 2008</u>	
	Amount	%	Amount	%
Nonaccrual	\$ 17,518,312	95.2%	\$ 15,147,104	94.6%
90 days past due and still accruing interest	407,135	2.2%	859,545	5.4%
Formally restructured	303,142	1.6%	-	0.0%
Other property owned, net	181,595	1.0%	-	0.0%
Total	<u>\$ 18,410,184</u>	<u>100.0%</u>	<u>\$ 16,006,649</u>	<u>100.0%</u>

The increase in nonaccrual loans of \$2,371,208 from December 31, 2008 is primarily related to one loan for \$2,995,328 coupled with three other loans in nonaccrual as of December 31, 2008 which were foreclosed on in 2009 as well as principal payments on other nonaccrual loans. The one loan was placed into nonaccrual in 2009 due to delinquent installments and the borrower's stressed financial position.

Results of Operations:

For the Three Months Ended March 31

(\$ in thousands)

	<u>2009</u>	<u>2008</u>	<u>\$ Change</u>	<u>% Change</u>
Net Interest Income	\$ 2,996	\$ 3,013	\$ (16)	-0.5%
Loan Loss Reversal	50	-	50	100.0%
Noninterest Income	562	1,021	(459)	-44.9%
Noninterest Expense	<u>(1,529)</u>	<u>(1,428)</u>	<u>(101)</u>	7.1%
Net Income	<u>\$ 2,079</u>	<u>\$ 2,606</u>	<u>\$ (526)</u>	-20.2%
Return on Average Assets	1.80	2.41	(0.61)	-25.3%
Return on Average Equity	12.37	16.57	(4.20)	-25.3%

The Association had net income of \$2,079,391 for the three months ended March 31, 2009, as compared to net income of \$2,605,755 for the same periods in 2008 reflecting a decrease of 20.2 percent. The decrease is primarily due to lower noninterest income of \$458,615 in 2009. The decrease in noninterest income is partially related to not recording an accrual of direct note

patronage from the Bank in the first quarter of 2009 as in 2008 because of the uncertainty of a patronage distribution in 2009 based on current economic conditions. The decrease is also related to a reduction in new loan fees because of a decrease in new loan financing in 2009 versus the same time period in 2008.

Net interest income was \$2,996,423 for the three months ended March 31, 2009, compared to \$3,012,751 for the same time period in 2008, representing a decrease of \$16,328 or 0.5 percent. Net interest income is the principal source of earnings for the Association and is impacted by volume, yields on assets, and cost of debt. The decrease is due to a decline in spread of 4 basis points in 2009 offset by an increase in average loan volume of \$30.1 million. The decline in spread is due to an increase in nonaccrual loan volume of \$11,685,907 from March 31, 2008 to March 31, 2009, in addition to competition within the lending industry that has caused compression in spreads on loans within the Association's mortgage and capital markets portfolios. The effects of changes in average volume and interest rates for the three months ended March 31, 2009 and 2008 are presented in the following tables:

For the Three Months Ended March 31				
(\$ in thousands)				
	<u>2009</u>	<u>2008</u>	<u>\$ Change</u>	<u>% Change</u>
Average loan volume	\$449,243	\$419,108	\$30,135	7.2%
Average direct loan	\$389,821	\$363,226	\$26,595	7.3%
Yield on loans	6.15%	7.26%	-1.11%	-15.3%
Cost of direct note	3.97%	5.04%	-1.07%	-21.3%
Interest rate spread	2.18%	2.22%	-0.04%	-1.8%

March 31, 2009 vs. March 31, 2008			
Increase (decrease) due to			
(\$ in Thousands)			
	<u>Volume</u>	<u>Rate</u>	<u>Total</u>
Interest Income	\$ 539	\$ (1,293)	\$ (754)
Interest Expense	330	(1,068)	(738)
Net Interest Income	<u>\$ 209</u>	<u>\$ (225)</u>	<u>\$ (16)</u>

Noninterest expense increased \$101,377 or 7.1 percent, for the first three months ended March 31, 2009 as compared to the same time period in 2008. The increase is primarily related to an increase in salaries and benefits due mainly to a higher defined benefit pension plan contribution in 2009 and an increase in insurance fund premiums related to the higher nonaccrual loan volume in 2009 versus the same time period in 2008.

The Association's return on average assets for the three months ended March 31, 2009, was 1.80 and 2.41 percent for the same time period in 2008. The Association's return on average equity for the three months ended March 31, 2009, was 12.37 and 16.57 percent for the same time period in 2008. The decrease in the returns on average assets and average members' equity in 2009 is attributable to the reduced earnings of the Association due to decreases in noninterest income and the increase in noninterest expenses as explained above.

Liquidity and Funding Sources:

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

	<u>March 31,</u> <u>2009</u>	<u>December 31,</u> <u>2008</u>
Note payable to the Bank	\$ 390,677,972	\$ 388,967,769
Accrued interest on note payable	1,258,522	1,429,915
Total	<u>\$ 391,936,494</u>	<u>\$ 390,397,684</u>

Capital Resources:

The Association's capital position increased by \$1,154,193 at March 31, 2009, compared to December 31, 2008. The Association's debt as a percentage of members' equity was 5.86:1 as of March 31, 2009, compared to 5.97:1 as of December 31, 2008.

Under regulations governing minimum permanent capital adequacy and other capitalization issues, the Association is required to maintain a minimum adjusted permanent capital of seven percent of risk-adjusted assets as defined by the FCA. The Association's permanent capital ratio at March 31, 2009, was 12.9 percent, which is in compliance with the FCA's minimum permanent capital standard. The Association's core surplus ratio and total surplus ratio at March 31, 2009, were 12.3 and 12.3 percent, respectively, which is in compliance with the FCA's minimum surplus standard.

Relationship with the Farm Credit Bank of Texas:

The Association's financial condition may be impacted by factors that affect the Bank. The financial condition and results of operations of the Bank may materially affect the stockholder's investment in the Association. The Management's Discussion and Analysis and Notes to Financial Statements contained in the December 31, 2008 Annual Report of Heritage Land Bank, ACA more fully describe the Association's relationship with the Bank.

The Tenth Farm Credit District's (District) annual and quarterly stockholder reports are available free of charge, upon request. These reports can be obtained by writing to Farm Credit Bank of Texas, The Ag Agency, P.O. Box 202590, Austin, Texas 78720, or by calling (512) 483-9260. Copies of the District's quarterly and annual stockholder reports also can be requested by e-mail at fcb@farmcreditbank.com. The District makes its annual and quarterly stockholder reports available on its web site at www.farmcreditbank.com. The Association's quarterly stockholder reports are also available free of charge, upon request. These reports can be obtained by writing to Heritage Land Bank, ACA, 4608 Kinsey Drive, Suite 100, Tyler, Texas 75703, or calling 903-534-4975. The Association also makes its annual and quarterly stockholder reports available on its web site at www.heritagelandbank.com

HERITAGE LAND BANK, ACA

CONSOLIDATED BALANCE SHEET

	March 31, 2009 (unaudited)	December 31, 2008
<u>ASSETS</u>		
Cash	\$ 417,293	\$ 430,025
Loans	449,466,787	449,887,810
Less: allowance for loan losses	(1,774,887)	(1,856,351)
Net loans	<u>447,691,900</u>	<u>448,031,459</u>
Accrued interest receivable	3,883,370	3,335,641
Investment in and receivable from the Bank:		
Capital stock	7,523,170	7,523,170
Other	200,000	668,601
Other property owned, net	181,595	-
Premises and equipment	1,720,070	1,755,410
Other assets	843,935	144,352
Total assets	<u><u>\$ 462,461,333</u></u>	<u><u>\$ 461,888,658</u></u>
<u>LIABILITIES</u>		
Note payable to the Bank	\$ 390,677,972	\$ 388,967,769
Accrued interest payable	1,258,522	1,429,915
Drafts outstanding	309,469	844,144
Patronage distributions payable	887,000	2,480,000
Other liabilities	1,895,010	1,887,663
Total liabilities	<u><u>395,027,973</u></u>	<u><u>395,609,491</u></u>
<u>MEMBERS' EQUITY</u>		
Capital stock and participation certificates	2,659,270	2,682,325
Allocated retained earnings	6,538,947	6,542,952
Unallocated retained earnings	57,789,045	56,596,654
Accumulated other comprehensive income	446,098	457,236
Total members' equity	<u><u>67,433,360</u></u>	<u><u>66,279,167</u></u>
Total liabilities and members' equity	<u><u>\$ 462,461,333</u></u>	<u><u>\$ 461,888,658</u></u>

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

HERITAGE LAND BANK, ACA

CONSOLIDATED STATEMENT OF INCOME

(unaudited)

	Quarter Ended	
	March 31,	
	2009	2008
<u>INTEREST INCOME</u>		
Loans	\$ 6,808,669	\$ 7,562,915
<u>INTEREST EXPENSE</u>		
Note payable to the Bank	3,812,246	4,550,164
Net interest income	2,996,423	3,012,751
<u>PROVISION FOR LOSSES</u>		
Loan losses reversal	(49,956)	-
Net interest income after provision for loan losses	3,046,379	3,012,751
<u>NONINTEREST INCOME</u>		
Patronage income from the Bank	272,997	557,046
Patronage income from other Farm Credit Institutions	108,363	-
Loan fees	178,997	390,896
Financially related services income	4,131	5,008
(Loss) Gain on other property owned, net	(2,967)	30,538
Gain on sale of premises and equipment, net	-	8,037
Other noninterest income	590	29,201
Total noninterest income	562,111	1,020,726
<u>NONINTEREST EXPENSES</u>		
Salaries and employee benefits	920,467	872,710
Directors' expense	65,638	47,701
Purchased services	89,496	77,498
Travel	32,105	40,506
Occupancy and equipment	72,180	71,783
Communications	15,408	17,305
Advertising	15,606	24,239
Public and member relations	39,672	45,450
Supervisory and exam expense	38,218	35,035
Insurance Fund premiums	187,650	155,873
Other noninterest expense	52,659	39,622
Total noninterest expenses	1,529,099	1,427,722
Net income	\$ 2,079,391	\$ 2,605,755

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

HERITAGE LAND BANK, ACA

CONSOLIDATED STATEMENT OF CHANGES IN MEMBERS' EQUITY

(unaudited)

	Capital Stock/ Participation Certificates	Retained Earnings		Accumulated Other Comprehensive Income (Loss)	Total Members' Equity
		Allocated	Unallocated		
Balance at December 31, 2007	\$ 2,655,875	\$ 6,558,253	\$ 52,632,017	\$ 543,575	\$ 62,389,720
Adjustment to beginning balance due to FAS No. 158 accounting change	-	-	(5,521)	-	(5,521)
Balance at January 1, 2008	2,655,875	6,558,253	52,626,496	543,575	62,384,199
Comprehensive income					
Net income	-	-	2,605,755	-	2,605,755
Amortization of costs included in periodic retirement benefit costs	-	-	-	(8,700)	(8,700)
Total comprehensive income	-	-	2,605,755	(8,700)	2,597,055
Capital stock/participation certificates issued	122,380	-	-	-	122,380
Capital stock/participation certificates and allocated retained earnings retired	(108,335)	(5,321)	-	-	(113,656)
Patronage Cash Accrual	-	-	(952,886)	-	(952,886)
Balance at March 31, 2008	<u>\$ 2,669,920</u>	<u>\$ 6,552,932</u>	<u>\$ 54,279,365</u>	<u>\$ 534,875</u>	<u>\$ 64,037,092</u>
Balance at December 31, 2008	\$ 2,682,325	\$ 6,542,952	\$ 56,596,654	\$ 457,236	\$ 66,279,167
Comprehensive income					
Net income	-	-	2,079,391	-	2,079,391
Amortization of costs included in periodic retirement benefit costs	-	-	-	(11,138)	(11,138)
Total comprehensive income	-	-	2,079,391	(11,138)	2,068,253
Capital stock/participation certificates issued	52,985	-	-	-	52,985
Capital stock/participation certificates and allocated retained earnings retired	(76,040)	(4,005)	-	-	(80,045)
Patronage Cash Accrual	-	-	(887,000)	-	(887,000)
Balance at March 31, 2009	<u>\$ 2,659,270</u>	<u>\$ 6,538,947</u>	<u>\$ 57,789,045</u>	<u>\$ 446,098</u>	<u>\$ 67,433,360</u>

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

HERITAGE LAND BANK, ACA
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
(UNAUDITED)

NOTE 1 — ORGANIZATION AND SIGNIFICANT ACCOUNTING POLICIES:

The Heritage Land Bank, ACA (Agricultural Credit Association), referred to as the Association, is a member-owned cooperative that provides credit and credit-related services to or for the benefit of eligible borrowers/stockholders for qualified agricultural purposes. The Association serves the counties of Dallas, Tarrant, Collin, Hunt, Rockwall, Smith, Henderson, Rusk, Cherokee, Anderson, Nacogdoches, Panola, Sabine, Angelina, San Augustine, and Shelby in the State of Texas. The Association is a lending institution of the Farm Credit System (the System), which was established by Acts of Congress to meet the needs of American agriculture.

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

The consolidated financial statements comprise the operations of the ACA and its wholly-owned subsidiaries. The preparation of these consolidated financial statements requires the use of management's estimates. The results for the quarter and the three months ended March 31, 2009, are not necessarily indicative of the results to be expected for the year ended December 31, 2009.

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:

	March 31, 2009	March 31, 2008
Balance at beginning of quarter	\$ 1,856,351	\$ 903,855
Provision for loan losses	(49,956)	-
Charge-offs	(46,124)	-
Recoveries	14,616	-
Balance at end of quarter	<u>\$ 1,774,887</u>	<u>\$ 903,855</u>

The following table presents information concerning impaired loans:

	March 31, 2009	March 31, 2008
Impaired loans with related allowance	\$ 4,713,680	\$ 2,956,044
Impaired loans with no related allowance	13,514,909	5,525,271
Total impaired loans	<u>\$ 18,228,589</u>	<u>\$ 8,481,315</u>
Allowance on impaired loans	\$ 1,419,800	\$ 725,000
Average impaired loans	\$ 15,262,097	\$ 8,641,838
Interest income on impaired loans for the quarter	\$ 55,618	\$ 56,788

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 patronage distributions, equity retirements and other actions that may decrease the Association's permanent capital. In addition to factors that must be considered in meeting the minimum standards, the board of directors also monitors the following factors: capability of management; quality of operating policies, procedures, and internal controls; quality and quantity of earnings;

asset quality and the adequacy of the allowance for losses to absorb potential loss within the loan 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.

NOTE 4 — INCOME TAXES:

Heritage Land Bank, ACA and its subsidiary, Heritage Production Credit, PCA (Associations) are subject to federal and certain other income taxes. The Associations are eligible to operate as cooperatives that qualify for tax treatment under Subchapter T of the Internal Revenue code. Under specified conditions, the Associations can exclude from taxable income amounts distributed as qualified patronage refunds in the form of cash, stock or allocated surplus. Provisions for income taxes are made only on those earnings that will not be distributed as qualified patronage refunds. No provision for income taxes was recorded as of March 31, 2009.

Deferred taxes are recorded at the tax effect of all temporary differences based on the assumption that such temporary differences are retained by the institution and will therefore impact future tax payments. A valuation allowance is provided against deferred tax assets to the extent that it is more likely than not (over 50 percent probability), based on management's estimate, that they will not be realized. For the three months ended March 31, 2009, and 2008 the Association carries a deferred tax asset of \$900,203 and \$492,386 respectively, with a full valuation allowance recorded against the asset each year.

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

NOTE 5 — EMPLOYEE BENEFIT PLANS:

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

Under this alternative, postretirement benefit income measured for the three-month period October 1, 2007 to December 31, 2007 (determined using the September 2007 measurement date) was recorded as an adjustment to beginning 2008 retained earnings. As a result, the Association decreased retained earnings by \$5,521 net of taxes and increased the other postretirement benefit liability by \$5,521.

The Association previously disclosed in its financial statements for the year ended December 31, 2008, that it expected to contribute \$31,042 to its other postretirement benefit plan in 2009. As of March 31, 2009, \$5,411 of contributions has been made. The Association presently anticipates contributing an additional \$16,275 to fund its other postretirement benefit plan in 2009 for a total \$21,686. The unfunded accumulated benefit obligation related to this plan at March 31, 2009 was \$693,096.