



---

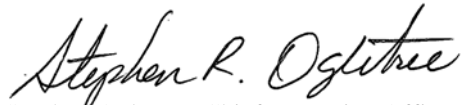
**2009**  
**Quarterly Report**  
**Second Quarter**

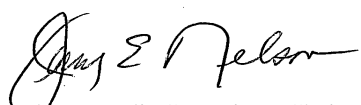



**For the Quarter Ended June 30, 2009**

## REPORT OF MANAGEMENT

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

  
Stephen Ogletree, Chief Executive Officer  
July 28, 2009

  
Jerry Nelson, Audit Committee Chairman  
July 28, 2009

  
Jenny Sloan, Chief Financial Officer  
July 28, 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 six months ended June 30, 2009. These comments should be read in conjunction with the accompanying financial statements and the December 31, 2008 Annual Report of the Association.

The Association is a member of the Farm Credit System (System), a nationwide network of cooperatively owned financial institutions established by and subject to the provisions of the Farm Credit Act of 1971, as amended, and the regulations of the Farm Credit Administration (FCA) promulgated thereunder.

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

### Loan Portfolio:

Total loans outstanding at June 30, 2009, including nonaccrual loans, were \$444,698,838 compared to \$449,887,810 at December 31, 2008, reflecting an decrease of 1.2 percent. The decrease in loan volume is related to the slowing demand for new loan financing in the first and second quarters which management attributes to the current economic environment. Nonaccrual loans as a percentage of total loans outstanding were 3.1 percent at June 30, 2009, compared to 3.4 percent at December 31, 2008.

The Association recorded \$2,181 in recoveries and \$15,925 in charge-offs for the quarter ending June 30, 2009, and no recoveries or charge-offs for the same period in 2008. The Association's allowance for loan losses was 0.5 percent and 0.4 percent of total loans outstanding as of June 30, 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.

	June 30, 2009		December 31, 2008	
	Amount	%	Amount	%
Nonaccrual	\$ 13,795,981	88.6%	\$ 15,147,104	94.6%
90 days past due and still accruing interest	965,450	6.4%	859,545	5.4%
Formally restructured	322,506	2.1%	-	0.0%
Other property owned, net	450,816	2.9%	-	0.0%
Total	\$ 15,534,753	100.0%	\$ 16,006,649	100.0%

High risk assets decreased \$471,896 from December 31, 2008. The decrease is primarily due to the reduction in nonaccrual loans of \$1,351,123, offset somewhat by the addition of \$450,816 in property acquired through foreclosure and \$322,506 related to 3 loans where the debt was restructured due to the borrower's credit conditions. The reduction in nonaccrual loans is related to several actions including the transfer of 2 loans to accrual status for a total of \$3,995,460, the foreclosure on four loans totaling \$450,816, offset somewhat by a loan placed into nonaccrual in the first quarter of 2009 for \$2,995,328. This loan was placed into nonaccrual due to delinquent installments and the borrower's stressed financial position.

## Results of Operations:

	For the Three Months Ended June 30 (\$ in thousands)				For the Six Months Ended June 30 (\$ in thousands)			
	2009	2008	\$ Change	% Change	2009	2008	\$ Change	% Change
Net Interest Income	\$ 3,098	\$ 3,010	\$ 87	2.9%	\$ 6,094	\$ 6,024	\$ 70	1.2%
Loan Loss Reversal	(327)	(1,006)	679	-67.5%	(277)	(1,007)	730	-72.5%
Noninterest Income	560	921	(361)	-39.2%	1,123	1,942	(820)	-42.2%
Noninterest Expense	(1,646)	(1,470)	(176)	11.9%	(3,175)	(2,899)	(277)	9.5%
Net Income	<u>\$ 1,685</u>	<u>\$ 1,455</u>	<u>\$ 230</u>	15.8%	<u>\$ 3,764</u>	<u>\$ 4,060</u>	<u>\$ (296)</u>	-7.3%
Average Loan Volume	\$443,360	\$433,223	10,137	2.3%	\$445,897	\$425,704	20,193	4.7%
Average Direct Loan	385,207	377,965	7,242	1.9%	387,501	370,596	16,905	4.6%
Interest Rate Spread	2.23	2.16	0.07	3.2%	2.16	2.17	(0.01)	-0.5%
Return on Average Assets	1.48	1.30	0.18	13.8%	1.64	1.85	(0.21)	-11.4%
Return on Average Equity	9.85	9.06	0.79	8.7%	11.10	12.78	(1.68)	-13.1%

The Association had net income of \$1,684,780 for the three months ended June 30, 2009, as compared to net income of \$1,454,530 for the same period in 2008 reflecting an increase of 15.8 percent. This increase is due to the reduction in the provision for loan loss of \$679,613, somewhat offset by lower noninterest income of \$361,004 and higher noninterest expenses of \$175,690 in 2009. Provision for loan loss is less in 2009 because in 2008 a large reserve was recorded for \$817,000 primarily related to one entity. The decrease in noninterest income is partially related to not recording an accrual of direct note patronage from the Bank in 2009 as in 2008 due to the uncertainty of a patronage distribution based on current economic conditions as well as a reduction in new loan fees because of a decrease in new loan financing in 2009. The increase in noninterest expense is mainly due to the increase in salaries and benefits related to a higher defined benefit pension plan contribution in 2009 and an increase in insurance fund premiums related to the higher nonaccrual volume in 2009.

For the six months ended June 30, 2009 the Association had net income of \$3,764,171, as compared to net income of \$4,060,286 for the same period in 2008 reflecting a decrease of 7.3 percent. This decrease is related to lower noninterest income of \$819,620 and higher noninterest expenses of \$276,549, offset somewhat by a decrease in the provision for loan loss of \$729,569. The decrease in noninterest income and the provision for loan losses as well as the increase in noninterest expense is explained above.

Net interest income was \$3,097,626 and \$6,094,049 for the three and six months ended June 30, 2009, compared to \$3,010,295 and \$6,023,564 for the same periods in 2008 reflecting minor increases of 2.9 percent and 1.2 percent, respectively. The slight increase in the three months for net interest income was related to an increase in average loan volume of \$10,137,218 and the increase in interest rate spread of 7 bps, as additional interest was recognized on loans previously in nonaccrual due to repayments on those loans. The slight increase for the six months ended June 30, 2009 was attributable to an increase in average loan volume of \$20,193,378.

The Association's return on average assets for the three and six months ended June 30, 2009, was 1.48 and 1.64 percent as compared to 1.30 and 1.85 percent for the same periods in 2008. The Association's return on average equity for the three and six months ended June 30, 2009, was 9.85 and 11.10 as compared to 9.06 and 12.78 percent for the same periods in 2008. The increase in both returns for the three months ended June 30, 2009 is attributable to increased earnings of the Association primarily due to a decrease in the loan loss provision. The decrease in both returns for the six months ended June 30, 2009 is attributable to decreased earnings of the Association due to a decrease in noninterest income and an increase in noninterest expense. Detail related to changes in the loan loss provision, noninterest income, and noninterest expense is explained above.

**Liquidity and Funding Sources:**

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

	<b>June 30, 2009</b>	December 31, 2008
Note payable to the Bank	\$ <b>384,937,351</b>	\$ 388,967,769
Accrued interest on note payable	<b>1,180,067</b>	1,429,915
Total	<b>\$ 386,117,418</b>	\$ 390,397,684

**Capital Resources:**

The Association's capital position increased by \$1,858,149 at June 30, 2009, compared to December 31, 2008. The Association's debt as a percentage of members' equity was 5.72:1 as of June 30, 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 June 30, 2009, was 13.6 percent, which is in compliance with the FCA's minimum permanent capital standard. The Association's core surplus ratio and total surplus ratio at June 30, 2009, were 13.0 and 13.0 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 [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 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](http://www.heritagelandbank.com).

**HERITAGE LAND BANK, ACA**

**CONSOLIDATED BALANCE SHEET**

	<b>June 30, 2009 (unaudited)</b>	<b>December 31, 2008</b>
<b><u>ASSETS</u></b>		
Cash	\$ 345,087	\$ 430,025
Loans	444,698,838	449,887,810
Less: allowance for loan losses	(2,088,278)	(1,856,351)
Net loans	<u>442,610,560</u>	<u>448,031,459</u>
Accrued interest receivable	3,987,304	3,335,641
Investment in and receivable from the Bank:		
Capital stock	7,523,170	7,523,170
Other	420,000	668,601
Other property owned, net	450,816	-
Premises and equipment	1,743,470	1,755,410
Other assets	620,493	144,352
Total assets	<u><u>\$ 457,700,900</u></u>	<u><u>\$ 461,888,658</u></u>
<b><u>LIABILITIES</u></b>		
Note payable to the Bank	\$ 384,937,351	\$ 388,967,769
Accrued interest payable	1,180,067	1,429,915
Drafts outstanding	26,957	844,144
Patronage distributions payable	1,795,000	2,480,000
Other liabilities	1,624,209	1,887,663
Total liabilities	<u><u>389,563,584</u></u>	<u><u>395,609,491</u></u>
<b><u>MEMBERS' EQUITY</u></b>		
Capital stock and participation certificates	2,613,955	2,682,325
Allocated retained earnings	6,522,576	6,542,952
Unallocated retained earnings	58,565,825	56,596,654
Accumulated other comprehensive income	434,960	457,236
Total members' equity	<u><u>68,137,316</u></u>	<u><u>66,279,167</u></u>
Total liabilities and members' equity	<u><u>\$ 457,700,900</u></u>	<u><u>\$ 461,888,658</u></u>

HERITAGE LAND BANK, ACA

CONSOLIDATED STATEMENT OF INCOME  
(unaudited)

	Quarter Ended June 30,		Six Months Ended June 30,	
	2009	2008	2009	2008
<b><u>INTEREST INCOME</u></b>				
Loans	\$ 6,711,016	\$ 7,349,400	\$ 13,519,685	\$ 14,912,834
<b><u>INTEREST EXPENSE</u></b>				
Note payable to the Bank	3,613,390	4,339,105	7,425,636	8,889,270
Net interest income	3,097,626	3,010,295	6,094,049	6,023,564
<b><u>PROVISION FOR LOSSES</u></b>				
Provision for loan losses	327,135	1,006,748	277,179	1,006,748
Net interest income after provision for loan losses	2,770,491	2,003,547	5,816,870	5,016,816
<b><u>NONINTEREST INCOME</u></b>				
Patronage Income from the Bank	290,300	521,401	563,607	1,031,381
Patronage Income from other Farm Credit Institutions	6,811	52,917	114,863	52,917
Loan fees	221,831	262,039	400,828	700,002
Financially related services income	2,412	2,699	6,543	7,707
Gain on other property owned, net	10,666	79,126	7,699	109,664
Gain on sale of premises and equipment, net	-	-	-	8,037
Other noninterest income	28,383	3,225	28,974	32,426
Total noninterest income	560,403	921,407	1,122,514	1,942,134
<b><u>NONINTEREST EXPENSES</u></b>				
Salaries and employee benefits	963,342	823,832	1,883,809	1,696,542
Directors' expense	48,947	59,764	114,585	107,465
Purchased services	97,273	91,258	186,769	168,756
Travel	49,344	49,813	81,449	90,319
Occupancy and equipment	65,325	63,626	137,505	135,408
Communications	16,912	15,576	32,321	32,881
Advertising	37,528	55,314	53,135	79,553
Public and member relations	75,893	59,568	115,566	105,018
Supervisory and exam expense	38,218	35,035	76,436	70,070
Insurance Fund premiums	186,897	161,440	374,546	317,313
Other noninterest expense	66,435	55,198	119,092	95,339
Total noninterest expenses	1,646,114	1,470,424	3,175,213	2,898,664
Net income	\$ 1,684,780	\$ 1,454,530	\$ 3,764,171	\$ 4,060,286

**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	-	-	4,060,286	-	4,060,286
Amortization of costs included in periodic retirement benefit costs	-	-	-	(17,400)	(17,400)
Total comprehensive income	-	-	4,060,286	(17,400)	4,042,886
Capital stock/participation certificates issued	272,480	-	-	-	272,480
Capital stock/participation certificates and allocated retained earnings retired	(217,385)	(6,454)	-	-	(223,839)
Patronage Cash Accrual	-	-	(1,794,282)	-	(1,794,282)
<b>Balance at June 30, 2008</b>	<b>\$ 2,710,970</b>	<b>\$ 6,551,799</b>	<b>\$ 54,892,500</b>	<b>\$ 526,175</b>	<b>\$ 64,681,444</b>
Balance at December 31, 2008	\$ 2,682,325	\$ 6,542,952	\$ 56,596,654	\$ 457,236	\$ 66,279,167
Comprehensive income					
Net income	-	-	3,764,171	-	3,764,171
Amortization of costs included in periodic retirement benefit costs	-	-	-	(22,276)	(22,276)
Total comprehensive income	-	-	3,764,171	(22,276)	3,741,895
Capital stock/participation certificates issued	128,055	-	-	-	128,055
Capital stock/participation certificates and allocated retained earnings retired	(196,425)	(20,376)	-	-	(216,801)
Patronage Cash Accrual	-	-	(1,795,000)	-	(1,795,000)
<b>Balance at June 30, 2009</b>	<b>\$ 2,613,955</b>	<b>\$ 6,522,576</b>	<b>\$ 58,565,825</b>	<b>\$ 434,960</b>	<b>\$ 68,137,316</b>

**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.

Effective January 1, 2009, the Association adopted FSP No. 157-2, "Effective Date of FASB Statement No. 157." This FSP delayed the effective date of Statement No. 157 for nonfinancial assets and nonfinancial liabilities. The impact of adoption resulted in additional fair value disclosures but does not have an impact on our financial condition or results of operations. See Note 5 for fair value measurement of the Association's nonfinancial assets.

In May 2009, the FASB issued SFAS No. 165, "Subsequent Events," which sets forth general standards of accounting for and disclosure of events that occur after the balance sheet date but before financial statements are issued or are available to be issued. Recognized subsequent events should be recognized in the financial statements since the conditions existed at the date of the balance sheet. Nonrecognized subsequent events are not recognized in the financial statements since the conditions arose after the balance sheet date but before the financial statements are issued or are available to be issued. This Standard, which includes a required disclosure of the date through which an entity has evaluated subsequent events, is effective for interim or annual periods ending after June 15, 2009. See Note 7 for the date through which subsequent events were evaluated by the Association.

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

The consolidated financial statements comprise the operations of the ACA and its wholly-owned subsidiaries. The preparation of these consolidated financial statements requires the use of management's estimates. The results for the quarter and the six months ended June 30, 2009, are not necessarily indicative of the results to be expected for the year ended December 31, 2009.

**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, 2009</b>	June 30, 2008
Balance at beginning of quarter	\$ 1,774,887	\$ 903,855
Provision for loan losses	327,135	1,006,748
Charge-offs	(15,925)	-
Recoveries	2,181	-
Balance at end of quarter	<u>\$ 2,088,278</u>	<u>\$ 1,910,603</u>

The following table presents information concerning impaired loans:

	<b>June 30, 2009</b>	June 30, 2008
Impaired loans with related allowance	\$ 5,822,711	\$ 5,042,088
Impaired loans with no related allowance	9,261,226	2,597,906
Total impaired loans	<b>\$ 15,083,937</b>	<b>\$ 7,639,994</b>
Allowance on impaired loans	\$ 1,659,000	\$ 1,520,000
Average impaired loans	\$ 14,393,343	\$ 6,129,168
Interest income recognized on impaired loans for the quarter	\$ 77,343	\$ 7,386

### 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 and lease portfolios; sufficiency of liquid funds; needs of an institution's customer base; and any other risk-oriented activities, such as funding and interest rate risk, potential obligations under joint and several liability, contingent and off-balance-sheet liabilities or other conditions warranting additional capital. At least quarterly, management reviews the Association's goals and objectives with the board.

### NOTE 4 — INCOME TAXES:

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 June 30, 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 six months ended June 30, 2009, and 2008 the Association carries a deferred tax asset of \$931,502 and \$530,586 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 – FAIR VALUE MEASUREMENTS:

SFAS No. 157 defines fair value as the exchange price that would be received for an asset or paid to transfer a liability in the principal or most advantageous market for the asset or liability. See Note 2 to the 2008 Annual Report to Stockholders for a more complete description.

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

	<b>Fair Value Measurement Using</b>			<b>Total Fair Value</b>
	<b>Level 1</b>	<b>Level 2</b>	<b>Level 3</b>	
<b>Assets:</b>				
Loans	\$-	\$-	\$4,163,711	\$4,163,711
Other property owned	\$-	\$-	\$491,550	\$491,550

## **Valuation Techniques**

As more fully discussed in Note 2 of the 2008 Annual Report, SFAS No. 157 establishes a fair value hierarchy, which requires an entity to maximize the use of observable inputs and minimize the use of unobservable inputs when measuring fair value. The following represent a brief summary of the valuation techniques used for the Associations' assets and liabilities. For a more complete description, see Notes to the 2008 Annual Report.

### *Loans*

For certain loans evaluated for impairment under SFAS No. 114, the fair value is based upon the underlying collateral since the loans were collateral dependent loans for which real estate is the collateral. The fair value measurement process uses independent appraisals and other market-based information, but in many cases it also requires significant input based on management's knowledge of and judgment about current market conditions, specific issues relating to the collateral and other matters. As a result, these fair value measurements fall within Level 3 of the hierarchy. When the value of the real estate, less estimated costs to sell, is less than the principal balance of the loan, a specific reserve is established.

### *Other Property Owned*

Other property owned is generally classified as Level 3. The fair value is based upon collateral values.

## **NOTE 6 — EMPLOYEE BENEFIT PLANS:**

The Association previously disclosed in its financial statements for the year ended December 31, 2008, that it expected to contribute \$31,042 to its postretirement benefit plan in 2009. As of June 30, 2009, \$10,983 of contributions has been made. The Association presently anticipates contributing an additional \$10,978 to fund its postretirement benefit plan in 2009 for a total \$21,961. The unfunded accumulated benefit obligation related to this plan at June 30, 2009 was \$703,251.

## **NOTE 7 – SUBSEQUENT EVENTS:**

The Association has evaluated subsequent events through July 28, 2009, which is the date the financial statements were available to be issued.