NATIONAL RURAL UTILITIES COOPERATIVE FINANCE CORP /DC/
Form 10-Q
January 14, 2013

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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 10-Q

x QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the quarterly period ended November 30, 2012

OR

o TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the Transition Period From To

Commission File Number 1-7102

NATIONAL RURAL UTILITIES COOPERATIVE FINANCE CORPORATION

(Exact name of registrant as specified in its charter)

DISTRICT OF COLUMBIA
(State or other jurisdiction of incorporation or organization)

52-0891669
(I.R.S. Employer Identification Number)

20701 COOPERATIVE WAY, DULLES, VA 20166
(Address of principal executive offices)
(Registrant’s telephone number, including area code, is 703-467-1800)

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes x No ¨

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes x No ¨

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See the definitions of “large accelerated filer,” “accelerated filer,” and “smaller reporting company" in Rule 12b-2 of the Exchange Act.

Large accelerated filer ¨ Accelerated filer ¨ Non-accelerated filer x Smaller reporting company ¨

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes ¨ No x

The Registrant does not issue capital stock because it is a tax-exempt cooperative.

PART 1. FINANCIAL INFORMATION

Item 1. Financial Statements.

NATIONAL RURAL UTILITIES COOPERATIVE FINANCE CORPORATION

CONDENSED CONSOLIDATED BALANCE SHEETS
(UNAUDITED)
(in thousands)

A S S E T S

	November 30, 2012	May 31, 2012
Cash and cash equivalents	$ 439,183	$ 191,167
Restricted cash	8,649	7,694
Investments	309,932	59,045
Loans to members	19,105,207	18,919,612
Less: Allowance for loan losses	(148,737)	(143,326)
Loans to members, net	18,956,470	18,776,286
Accrued interest and other receivables	171,964	185,827
Fixed assets, net	103,106	102,770
Debt service reserve funds	39,803	39,803
Debt issuance costs, net	40,572	43,515
Foreclosed assets, net	245,803	223,476
Derivative assets	273,480	296,036
Other assets	21,432	25,716
	$ 20,610,394	$ 19,951,335

See accompanying notes.

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NATIONAL RURAL UTILITIES COOPERATIVE FINANCE CORPORATION

CONDENSED CONSOLIDATED BALANCE SHEETS
(UNAUDITED)
(in thousands)

L I A B I L I T I E S   A N D   E Q U I T Y

	November 30, 2012	May 31, 2012
Short-term debt	$ 6,050,861	$ 4,493,434
Accrued interest payable	155,488	161,817
Long-term debt	11,201,472	12,151,967
Deferred income	23,202	26,131
Other liabilities	61,649	63,922
Derivative liabilities	630,919	654,125
Subordinated deferrable debt	186,440	186,440
Members' subordinated certificates:		
Membership subordinated certificates	646,388	646,279
Loan and guarantee subordinated certificates	727,169	678,115
Member capital securities	398,650	398,350
Total members' subordinated certificates	1,772,207	1,722,744
Commitments and contingencies		
CFC equity:		
Retained equity	510,281	473,964
Accumulated other comprehensive income	9,592	9,199
Total CFC equity	519,873	483,163
Noncontrolling interest	8,283	7,592
Total equity	528,156	490,755
	$ 20,610,394	$ 19,951,335

See accompanying notes.

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NATIONAL RURAL UTILITIES COOPERATIVE FINANCE CORPORATION

CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS
(UNAUDITED)
(in thousands)

	For the three months ended November 30,		For the six months ended November 30,	
	2012	2011	2012	2011
Interest income	$ 241,630	$ 237,755	$ 481,715	$ 485,005
Interest expense	(174,301)	(194,680)	(350,897)	(396,724)
Net interest income	67,329	43,075	130,818	88,281
Recovery of (provision for) loan losses	3,817	2,995	(5,305)	12,125
Net interest income after recovery of (provision for) loan losses	71,146	46,070	125,513	100,406
Non-interest income:				
Fee and other income	17,807	3,986	22,765	8,709
Derivative losses	(3,766)	(47,753)	(28,358)	(159,324)
Results of operations of foreclosed assets	(909)	(6,648)	(5,674)	(16,466)
Total non-interest income	13,132	(50,415)	(11,267)	(167,081)
Non-interest expense:				
Salaries and employee benefits	(10,148)	(9,833)	(20,553)	(20,232)
Other general and administrative expenses	(9,303)	(6,859)	(16,068)	(12,849)
Recovery of guarantee liability	92	12	101	72
Loss on early extinguishment of debt	-	(6,258)	-	(15,525)
Other	(4,384)	(418)	(4,547)	(815)
Total non-interest expense	(23,743)	(23,356)	(41,067)	(49,349)
Income (loss) prior to income taxes	60,535	(27,701)	73,179	(116,024)
Income tax (expense) benefit	(454)	407	(452)	2,108
Net income (loss)	60,081	(27,294)	72,727	(113,916)
Less: Net (income) loss attributable to the noncontrolling interest	(699)	533	(704)	3,123

Net income (loss) attributable to CFC	$ 59,382	$ (26,761)	$ 72,023	$ (110,793)

See accompanying notes.

NATIONAL RURAL UTILITIES COOPERATIVE FINANCE CORPORATION

CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME
(UNAUDITED)
(in thousands)

	For the three months ended November 30,		For the six months ended November 30,	
	2012	2011	2012	2011
Net income (loss)	$ 60,081	$ (27,294)	$ 72,727	$(113,916)
Other comprehensive income (loss):				
Add: Unrealized gains (losses) on securities	893	(160)	887	(99)
Less: Realized gains on derivatives	(253)	(259)	(505)	(518)
Other comprehensive income (loss)	640	(419)	382	(617)
Total comprehensive income (loss)	60,721	(27,713)	73,109	(114,533)
Less: Total comprehensive (income) loss attributable to noncontrolling interest	(694)	539	(693)	3,136
Total comprehensive income (loss) attributable to CFC	$ 60,027	$ (27,174)	$ 72,416	$(111,397)

See accompanying notes.

NATIONAL RURAL UTILITIES COOPERATIVE FINANCE CORPORATION

CONDENSED CONSOLIDATED STATEMENT OF CHANGES IN EQUITY
(UNAUDITED)
(in thousands)

For the six months ended November 30, 2012 and 2011

	Total	Noncontrolling interest	Total CFC equity	Accumulated other comprehensive income	CFC retained equity	Unallocated net income (loss)	Members' capital reserve	Patronage capital allocated	Membership fees and education fund
Balance as of May 31, 2012	$ 490,755	$ 7,592	$ 483,163	$ 9,199	$ 473,964	$ (346,941)	$ 272,126	$ 546,366	$ 2,413
Patronage capital retirement	(35,341)	-	(35,341)	-	(35,341)	-	-	(35,341)	-
Net income	72,727	704	72,023	-	72,023	72,023	-	-	-
Other comprehensive income (loss)	382	(11)	393	393	-	-	-	-	-
Other	(367)	(2)	(365)	-	(365)	-	-	-	(365)
Balance as of November 30, 2012	$ 528,156	$ 8,283	$ 519,873	$ 9,592	$ 510,281	$ (274,918)	$ 272,126	$ 511,025	$ 2,048
Balance as of May 31, 2011	$ 687,309	$ 11,786	$ 675,523	$ 9,758	$ 665,765	$ (130,689)	$ 272,126	$ 521,897	$ 2,431
Patronage capital retirement	(46,086)	-	(46,086)	-	(46,086)	-	-	(46,086)	-
Net loss	(113,916)	(3,123)	(110,793)	-	(110,793)	(110,793)	-	-	-
Other comprehensive loss	(617)	(13)	(604)	(604)	-	-	-	-	-
Other	(446)	(4)	(442)	-	(442)	-	-	-	(442)
Balance as of November 30, 2011	$ 526,244	$ 8,646	$ 517,598	$ 9,154	$ 508,444	$ (241,482)	$ 272,126	$ 475,811	$ 1,989

See accompanying notes.

NATIONAL RURAL UTILITIES COOPERATIVE FINANCE CORPORATION

CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
(UNAUDITED)
(in thousands)

	For the six months ended November 30, 2012	2011
CASH FLOWS FROM OPERATING ACTIVITIES		
Net income (loss)	$ 72,727	$ (113,916)
Adjustments to reconcile net income (loss) to net cash provided by operating activities		
Amortization of deferred income	(4,710)	(5,617)
Amortization of debt issuance costs and deferred charges	3,842	6,038
Depreciation	2,625	1,719
Provision for (recovery of) loan losses	5,305	(12,125)
Recovery of guarantee liability	(101)	(72)
Results of operations of foreclosed assets	5,674	16,466
Derivative forward value	(961)	158,510
Changes in operating assets and liabilities:		
Accrued interest and other receivables	13,386	7,238
Accrued interest payable	(6,329)	(12,236)
Other	4,921	10,300
Net cash provided by operating activities	96,379	56,305
CASH FLOWS FROM INVESTING ACTIVITIES		
Advances made on loans	(2,584,296)	(3,260,727)
Principal collected on loans	2,300,104	4,187,593
Net investment in fixed assets	(2,961)	(11,432)
Proceeds from foreclosed assets	29,110	18,849
Investments in foreclosed assets	(57,111)	(29,179)
Net proceeds from sale of loans	98,147	81,897
Investments	(250,000)	-
Change in restricted cash	(955)	(955)
Net cash (used in) provided by investing activities	(467,962)	986,046
CASH FLOWS FROM FINANCING ACTIVITIES		
Proceeds from (repayments of) issuances of short-term debt, net	215,087	(181,095)
Issuance costs for revolving bank lines of credit	(1,447)	(3,626)
Proceeds from issuance of long-term debt	1,254,167	299,132
Payments for retirement of long-term debt	(730,293)	(810,286)

Proceeds from issuance of members' subordinated certificates		55,548		18,145
Payments for retirement of members' subordinated certificates		(6,066)		(54,892)
Payments for retirement of patronage capital		(33,991)		(43,697)
Cash paid portion of debt exchange premium		(133,406)		-
Net cash provided by (used in) financing activities		619,599		(776,319)
NET INCREASE IN CASH AND CASH EQUIVALENTS		248,016		266,032
BEGINNING CASH AND CASH EQUIVALENTS		191,167		293,615
ENDING CASH AND CASH EQUIVALENTS	$	439,183	$	559,647

See accompanying notes.

NATIONAL RURAL UTILITIES COOPERATIVE FINANCE CORPORATION

CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
(UNAUDITED)
(in thousands)

	For the six months ended November 30, 2012	For the six months ended November 30, 2011
SUPPLEMENTAL DISCLOSURE OF CASH FLOW INFORMATION		
Cash paid for interest	$ 353,383	$ 402,922
Cash paid for income taxes	89	210
Non-cash financing and investing activities:		
Net decrease in debt service reserve funds/debt service reserve certificates	$ -	$ (5,859)
Collateral trust bonds issued as debt exchange premium	39,647	-

See accompanying notes.

NATIONAL RURAL UTILITIES COOPERATIVE FINANCE CORPORATION

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(UNAUDITED)

(1) General Information and Accounting Policies

(a) Basis of Presentation

The accompanying financial statements include the consolidated accounts of National Rural Utilities Cooperative Finance Corporation ("CFC"), Rural Telephone Finance Cooperative ("RTFC"), National Cooperative Services Corporation ("NCSC") and certain entities created and controlled by CFC to hold foreclosed assets and accommodate loan securitization transactions, after elimination of intercompany accounts and transactions.

Unless stated otherwise, references to "we," "our" or "us" represent the consolidation of CFC, RTFC, NCSC and certain entities created and controlled by CFC to hold foreclosed assets and accommodate loan securitization transactions. Foreclosed assets are held by two groups of subsidiaries wholly-owned by CFC. Our Denton Realty Partners entities ("DRP") hold assets, including a land development loan, limited partnership interests in certain real estate developments and developed lots and land and raw land in Texas. Caribbean Asset Holdings LLC ("CAH") holds our investment in cable and telecommunications operating entities in the United States Virgin Islands ("USVI"), British Virgin Islands and St. Maarten.

The preparation of financial statements in conformity with accounting principles generally accepted in the United States ("GAAP") requires management to make estimates and assumptions that affect the assets, liabilities, revenue and expenses reported in the financial statements, as well as amounts included in the notes thereto, including discussion and disclosure of contingent liabilities. The accounting estimates that require our most significant and subjective judgments include the allowance for loan losses and the determination of the fair value of our derivatives and certain aspects of our foreclosed assets. While we use our best estimates and judgments based on the known facts at the date of the financial statements, actual results could differ from these estimates as future events occur.

These interim unaudited condensed consolidated financial statements should be read in conjunction with the audited consolidated financial statements and notes thereto included in our Annual Report on Form 10-K for the fiscal year ended May 31, 2012.

In the opinion of management, the accompanying condensed consolidated financial statements contain all adjustments (which consist only of normal recurring accruals) necessary for a fair presentation of our results of operations and financial position for the interim periods presented.

(b) Variable Interest Entities

We are required to consolidate the financial results of RTFC and NCSC because CFC is the primary beneficiary of variable interests in RTFC and NCSC due to its exposure to absorbing the majority of their expected losses and because CFC manages the business activities of RTFC and NCSC. Under separate guarantee agreements, RTFC and NCSC pay CFC a fee to indemnify against loan losses. CFC manages the business activities of RTFC and NCSC through separate management agreements. Additionally, CFC is the sole lender to RTFC and the primary source of funding to NCSC. NCSC funds its lending programs through loans from CFC and debt guaranteed by CFC.

RTFC and NCSC creditors have no recourse against CFC in the event of a default by RTFC and NCSC, unless there is a guarantee agreement under which CFC has guaranteed NCSC or RTFC debt obligations to a third party. At

November 30, 2012, CFC had guaranteed $79 million of NCSC debt, derivative instruments and guarantees with third parties, and CFC's maximum potential exposure for these instruments totaled $88 million. The maturities for NCSC obligations guaranteed by CFC run through 2031. Guarantees of NCSC debt and derivative instruments are not included in Note 10, Guarantees, as the debt and derivatives are reported on the consolidated balance sheet. At November 30, 2012, CFC guaranteed $5 million of RTFC guarantees with third parties. The maturities for RTFC obligations guaranteed by CFC run through 2013. All CFC loans to RTFC and NCSC are secured by all assets and revenue of RTFC and NCSC. At November 30, 2012, RTFC had total assets of $662 million and NCSC had total assets of $722 million. At November 30, 2012, CFC had committed to lend RTFC up to $4,000 million, of which $523 million was outstanding. At November 30, 2012, CFC had committed to provide up to $2,000 million of credit to NCSC, of which $754 million was outstanding, representing $675 million of outstanding loans and $79 million of credit enhancements. In December 2012, CFC increased its commitment to provide up to $3,000 million of credit to NCSC.

(c) Loan Sales

We account for the sale of loans resulting from direct loan sales to third parties and securitization transactions by removing the financial assets from our consolidated balance sheets when control has been surrendered. We recognize related servicing fees on an accrual basis over the period for which servicing activity is provided. Deferred transaction costs and unamortized deferred loan origination costs related to the loans sold are included in the calculation of the gain or loss on the sale. We do not hold any continuing interest in the loans sold to date other than servicing performance obligations. We have no obligation to repurchase loans from the purchaser, except in the case of breaches of representations and warranties. We retain the servicing performance obligations on these loans. We have not recorded a servicing asset or liability.

During the six months ended November 30, 2012 and 2011, we sold CFC loans with outstanding balances totaling $98 million and $82 million, respectively, at par for cash. We recorded a loss on sale of loans, representing the unamortized deferred loan origination costs and transaction costs for the loans sold, which was immaterial during the six months ended November 30, 2012 and 2011.

(d) Interest Income

Interest income on loans is recognized using the effective interest method. The following table presents the components of interest income:

	For the three months ended November 30,		For the six months ended November 30,	
(dollar amounts in thousands)	2012	2011	2012	2011
Interest on long-term fixed-rate loans	$ 218,247	$ 219,841	$ 436,187	$ 445,187
Interest on long-term variable-rate loans	4,893	4,655	10,918	12,907
Interest on line of credit loans	7,413	6,738	15,105	16,364
Interest on restructured loans	7,625	4,084	13,087	4,776
Interest on investments	1,576	853	2,514	1,781
Fee income (1)	1,876	1,584	3,904	3,990
Total interest income	$ 241,630	$ 237,755	$ 481,715	$ 485,005

(1) Primarily related to conversion fees that are deferred and recognized using the effective interest method over the remaining original loan interest rate pricing term, except for a small portion of the total fee charged to cover administrative costs related to the conversion, which is recognized immediately.

Deferred income on the consolidated balance sheets primarily includes deferred conversion fees totaling $18 million and $20 million at November 30, 2012 and May 31, 2012, respectively.

(e) Interest Expense

The following table presents the components of interest expense:

	For the three months ended November 30,		For the six months ended November 30,	
(dollar amounts in thousands)	2012	2011	2012	2011
Interest expense on debt (1):				

Commercial paper and bank bid notes	$ 1,697	$ 1,391	$ 3,316	$ 3,160
Medium-term notes	24,833	47,733	52,716	101,574
Collateral trust bonds	82,271	77,346	163,710	154,618
Subordinated deferrable debt	2,807	2,807	5,613	5,613
Subordinated certificates	20,528	20,075	40,882	38,376
Long-term notes payable	37,915	39,071	76,311	78,898
Debt issuance costs (2)	1,905	2,380	3,842	7,505
Fee expense (3)	2,345	3,877	4,507	6,980
Total interest expense	$ 174,301	$ 194,680	$ 350,897	$ 396,724

(1) Represents interest expense and the amortization of discounts on debt.
(2) Includes amortization of all deferred charges related to the issuance of debt, principally underwriters' fees, legal fees, printing costs and comfort letter fees. Amortization is calculated using the effective interest method or a method approximating the effective interest method. Also includes issuance costs related to dealer commercial paper, which are recognized as incurred.
(3) Includes various fees related to funding activities, including fees paid to banks participating in our revolving credit agreements. Fees are recognized as incurred or amortized on a straight-line basis over the life of the respective agreement.

We exclude indirect costs, if any, related to funding activities from interest expense.

(f) Derivative Financial Instruments

We are an end user of financial derivative instruments. We use derivatives such as interest rate swaps and treasury rate locks to mitigate interest rate risk. Consistent with the accounting standards for derivative financial instruments, we record derivative instruments on the consolidated balance sheets as either an asset or liability measured at fair value. In recording the fair value of derivative assets and liabilities, we do not net our positions under contracts with individual counterparties. Changes in the fair value of derivative instruments along with realized gains and losses from cash settlements are recognized in the derivative gains (losses) line item of the consolidated statement of operations unless specific hedge accounting criteria are met.

We formally document, designate and assess the effectiveness of transactions that receive hedge accounting treatment. If applicable hedge accounting criteria are satisfied, the change in fair value of derivative instruments is recorded to other comprehensive income, and net cash settlements are recorded in interest expense. The gain or loss on derivatives used as a cash flow hedge of a forecasted debt transaction is recorded as a component of other comprehensive income (loss) and amortized through interest expense using the effective interest method over the term of the hedged debt. Any ineffectiveness in the hedging relationship is recognized in the derivative gains (losses) line of the statement of operations.

A transition adjustment was recorded as an other comprehensive loss on June 1, 2001, the date we implemented the accounting standards for derivative financial instruments. This amount will be amortized into earnings through April 2029 in the derivative gains (losses) line of the statement of operations.

Cash activity associated with interest rate swaps is classified as an operating activity in the consolidated statements of cash flows.

(g) Early Extinguishment of Debt

We redeem outstanding debt early from time to time to manage liquidity and interest rate risk. When we redeem outstanding debt early, we recognize a gain or loss related to the difference between the amount paid to redeem the debt and the net book value of the extinguished debt as a component of non-interest expense in the gain (loss) on early extinguishment of debt line item.

In August 2011 and October 2011, we redeemed a total of $500 million of our $1,500 million, 7.25 percent Series C medium-term notes with an original maturity of March 1, 2012 at a premium. Both the premium and unamortized issuance costs totaling $16 million were recorded as a loss on extinguishment of debt during the six months ended November 30, 2011.

(h) Reclassifications

Reclassifications of prior period amounts have been made to conform to the current reporting format and the presentation in our Form 10-Q for the three and six months ended November 30, 2012. Specifically, the fair value adjustments on DRP foreclosed assets have been reclassified into results of operations of foreclosed assets in the condensed consolidated statement of operations for the three and six months ended November 30, 2011. The corresponding non-cash adjustments were reclassified to the results of operations of foreclosed assets on the condensed consolidated statement of cash flows for the six months ended November 30, 2011.

(2) Investments

Our investments at November 30, 2012 and May 31, 2012 include Farmer Mac Series C preferred stock totaling $58 million and Farmer Mac Series A common stock totaling $2 million and $1 million, respectively. The Series C preferred stock is valued at cost, while the Series A common stock is accounted for as available-for-sale and recorded at fair value. Our investments also include a $250 million deposit that we made with a financial institution in an interest bearing account with a maturity of less than one year at the reporting date.

(3) Loans and Commitments

Loans outstanding to members and unadvanced commitments by loan type and by member class are summarized as follows:

	November 30, 2012		May 31, 2012	
(dollar amounts in thousands)	Loans outstanding	Unadvanced commitments (1)	Loans outstanding	Unadvanced commitments (1)
Total by loan type (2):				
Long-term fixed-rate loans	$ 16,982,140	$ -	$ 16,742,914	$ -
Long-term variable-rate loans	607,312	5,754,729	764,815	5,437,881
Loans guaranteed by RUS (3)	213,275	-	219,084	-
Line of credit loans	1,294,447	9,160,920	1,184,929	8,691,543
Total loans outstanding	19,097,174	14,915,649	18,911,742	14,129,424
Deferred origination costs	8,033	-	7,870	-
Less: Allowance for loan losses	(148,737)	-	(143,326)	-
Net loans outstanding	$ 18,956,470	$ 14,915,649	$ 18,776,286	$ 14,129,424
Total by member class (2):				
CFC:				
Distribution	$ 13,883,982	$ 9,344,109	$ 14,075,471	$ 9,191,227
Power supply	3,909,155	3,962,776	3,596,820	3,714,241
Statewide and associate	73,566	119,891	73,606	123,189
CFC total	17,866,703	13,426,776	17,745,897	13,028,657
RTFC	536,759	318,664	571,566	341,792
NCSC	693,712	1,170,209	594,279	758,975
Total loans outstanding	$ 19,097,174	$ 14,915,649	$ 18,911,742	$ 14,129,424

(1) The interest rate on unadvanced commitments is not set until drawn, therefore, the long-term unadvanced loan commitments have been classified in this table as variable-rate unadvanced commitments. However, at the time of the advance, the borrower may select a fixed or a variable rate on the new loan.
(2) Includes non-performing and restructured loans.
(3) "RUS" is the Rural Utilities Service.

Non-performing and restructured loans outstanding and unadvanced commitments to members included in the table above are summarized as follows by loan type and by company:

	November 30, 2012		May 31, 2012	
(dollar amounts in thousands)	Loans outstanding	Unadvanced commitments (1)	Loans outstanding	Unadvanced commitments (1)
Non-performing and restructured loans:				
Non-performing loans:				
CFC:				
Long-term variable-rate loans	$ 8,194	$ -	$ 8,194	$ -
Line of credit loans (2)	27,955	1,828	26,049	-

RTFC:								
Long-term fixed-rate loans		6,577		-		6,970		-
Total non-performing loans	$	42,726	$	1,828	$	41,213	$	-
Restructured loans:								
CFC:								
Long-term fixed-rate loans	$	39,717	$	-	$	455,689	$	-
Long-term variable-rate loans (3)		-		-		-		45,918
Line of credit loans (3)		-		5,000		-		5,000
Total restructured loans	$	39,717	$	5,000	$	455,689	$	50,918

(1) The interest rate on unadvanced commitments is not set until drawn, therefore, the long-term unadvanced loan commitments have been classified in this table as variable-rate unadvanced commitments. However, at the time of the advance, the borrower may select a fixed or a variable rate on the new loan.

(2) The unadvanced commitment is available under a debtor-in-possession facility for which the principal and interest has priority over all other claims.

(3) The unadvanced commitment is part of the terms outlined in the related restructure agreement. Loans advanced under these commitments would be classified as performing. Principal and interest due under these performing loans would be in addition to scheduled payments due under the restructured loan agreement.

Unadvanced Loan Commitments

A total of $1,444 million and $1,303 million of unadvanced commitments at November 30, 2012 and May 31, 2012, respectively, represented unadvanced commitments related to committed lines of credit loans that are not subject to a material adverse change clause at the time of each loan advance. As such, we will be required to advance amounts on these committed facilities as long as the borrower is in compliance with the terms and conditions of the facility.

The following table summarizes the available balance under committed lines of credit at November 30, 2012, and the related maturities by fiscal year and thereafter as follows:

(dollar amounts in thousands)	Available balance	Notional maturities of committed lines of credit 2013	2014	2015	2016	2017	Thereafter
Committed lines of credit	$1,444,133	$ 9,333	$ 281,733	$ 116,754	$ 223,492	$ 559,562	$ 253,259

The remaining unadvanced commitments totaling $13,472 million and $12,826 million at November 30, 2012 and May 31, 2012, respectively, were generally subject to material adverse change clauses. Prior to making an advance on these facilities, we confirm that there has been no material adverse change in the business or condition, financial or otherwise, of the borrower since the time the loan was approved and confirm that the borrower is currently in compliance with loan terms and conditions. In some cases, the borrower's access to the full amount of the facility is further constrained by the imposition of borrower-specific restrictions, or by additional conditions that must be met prior to advancing funds.

Unadvanced commitments related to line of credit loans are typically for periods not to exceed five years and are generally revolving facilities used for working capital and backup liquidity purposes. Historically, we have experienced a very low utilization rate on line of credit loan facilities, whether or not there is a material adverse change clause. Since we generally do not charge a fee on the unadvanced portion of the majority of our loan facilities, our borrowers will typically request long-term facilities to cover maintenance and capital expenditure work plans for periods of up to five years and draw down on the facility over that time. In addition, borrowers will typically request an amount in excess of their immediate estimated loan requirements to avoid the expense related to seeking additional loan funding for unexpected items.

The above items all contribute to our expectation that the majority of the unadvanced commitments will expire without being fully drawn upon and that the total unadvanced amount does not necessarily represent future cash funding requirements.

Payment Status of Loans

The tables below show an analysis of the age of the recorded investment in loans outstanding by member class:

	November 30, 2012					
(dollar amounts in thousands)	30-89 days past due	90 days or more past due (1)	Total past due	Current	Total financing receivables	Non-accrual loans
CFC:						
Distribution	$ 1,530	$ 29,619	$ 31,149	$ 13,852,833	$ 13,883,982	$ 31,149
Power supply	-	5,000	5,000	3,904,155	3,909,155	5,000
Statewide and associate	-	-	-	73,566	73,566	-
CFC total	1,530	34,619	36,149	17,830,554	17,866,703	36,149
RTFC	-	4,156	4,156	532,603	536,759	6,577
NCSC	-	-	-	693,712	693,712	-
Total loans outstanding	$ 1,530	$ 38,775	$ 40,305	$ 19,056,869	$ 19,097,174	$ 42,726

As a % of total loans	0.01%	0.20%	0.21%	99.79%	100.00%	0.22%

(1) All loans 90 days or more past due are on non-accrual status.

	May 31, 2012					
(dollar amounts in thousands)	30-89 days past due	90 days or more past due (1)	Total past due	Current	Total financing receivables	Non-accrual loans
CFC:						
Distribution	$ -	$ 29,243	$ 29,243	$ 14,046,228	$ 14,075,471	$ 29,243
Power supply	-	5,000	5,000	3,591,820	3,596,820	5,000
Statewide and associate	-	-	-	73,606	73,606	-
CFC total	-	34,243	34,243	17,711,654	17,745,897	34,243
RTFC	-	4,306	4,306	567,260	571,566	6,970
NCSC	-	-	-	594,279	594,279	-
Total loans outstanding	$ -	$ 38,549	$ 38,549	$ 18,873,193	$ 18,911,742	$ 41,213
As a % of total loans	-%	0.20%	0.20%	99.80%	100.00%	0.22%

(1) All loans 90 days or more past due are on non-accrual status.

Credit Quality

We monitor the credit quality and performance statistics of our financing receivables in an ongoing manner to provide a balance between the credit needs of our members and the requirements for sound credit quality of the loan portfolio. We

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evaluate the credit quality of our loans using an internal risk rating system that employs similar criteria for all member classes.

Our internal risk rating system is based on a determination of a borrower's risk of default utilizing both quantitative and qualitative measurements.

We have grouped our risk ratings into the categories of pass and criticized based on the criteria below.
(i) Pass: Borrowers that are not experiencing difficulty and/or not showing a potential or well-defined credit weakness.
(ii) Criticized: Includes borrowers categorized as special mention, substandard and doubtful as described below:

- Special mention: Borrowers that may be characterized by a potential credit weakness or deteriorating financial condition that is not sufficiently serious to warrant a classification of substandard or doubtful.
- Substandard: Borrowers that display a well-defined credit weakness that may jeopardize the full collection of principal and interest.
- Doubtful: Borrowers that have a well-defined weakness and the full collection of principal and interest is questionable or improbable.

Each risk rating is reassessed annually based on the receipt of the borrower's audited financial statements; however, interim downgrades and upgrades may take place at any time as significant events or trends occur.

The following table presents our loan portfolio by risk rating category and member class based on available data as of:

	November 30, 2012			May 31, 2012		
(dollar amounts in thousands)	Pass	Criticized	Total	Pass	Criticized	Total
CFC:						
Distribution	$ 13,851,402	$ 32,580	$ 13,883,982	$ 14,046,228	$ 29,243	$ 14,075,471
Power supply	3,904,155	5,000	3,909,155	3,591,820	5,000	3,596,820
Statewide and associate	73,566	-	73,566	73,606	-	73,606
CFC total	17,829,123	37,580	17,866,703	17,711,654	34,243	17,745,897
RTFC	529,642	7,117	536,759	564,596	6,970	571,566
NCSC	693,712	-	693,712	594,279	-	594,279
Total loans outstanding	$ 19,052,477	$ 44,697	$ 19,097,174	$ 18,870,529	$ 41,213	$ 18,911,742

Loan Security
Except when providing line of credit loans, we typically lend to our members on a senior secured basis. Long-term loans are typically secured on a parity with other secured lenders (primarily RUS), if any, by all assets and revenue of the borrower with exceptions typical in utility mortgages. Line of credit loans are generally unsecured. In addition to the lien and security interest we receive under the mortgage, our member borrowers are also required to achieve certain financial ratios as required by loan covenants.

The following table summarizes our secured and unsecured loans outstanding by loan type and by company:

(dollar amounts in thousands)	November 30, 2012				May 31, 2012			
Total by loan type:	Secured	%	Unsecured	%	Secured	%	Unsecured	%

Long-term fixed-rate loans	$ 16,361,860	96%	$ 620,280	4%	$ 16,168,857	97%	$ 574,057	3%
Long-term variable-rate loans	508,490	84	98,822	16	661,115	86	103,700	14
Loans guaranteed by RUS	213,275	100	-	-	219,084	100	-	-
Line of credit loans	245,427	19	1,049,020	81	205,143	17	979,786	83
Total loans outstanding	$ 17,329,052	91	$ 1,768,122	9	$ 17,254,199	91	$ 1,657,543	9
Total by company:								
CFC	$ 16,369,535	92%	$ 1,497,168	8%	$ 16,317,195	92%	$ 1,428,702	8%
RTFC	514,384	96	22,375	4	549,085	96	22,481	4
NCSC	445,133	64	248,579	36	387,919	65	206,360	35
Total loans outstanding	$ 17,329,052	91	$ 1,768,122	9	$ 17,254,199	91	$ 1,657,543	9

Loan Loss Allowance

We maintain an allowance for loan losses at a level estimated by management to provide for probable losses inherent in the loan portfolio. Under a guarantee agreement, CFC reimburses RTFC and NCSC for loan losses, therefore, RTFC and NCSC do not maintain separate loan loss allowances.

The activity in the loan loss allowance summarized in the tables below reflects a disaggregation by company of the allowance for loan losses held at CFC based on borrower type:

	As of and for the three months ended November 30, 2012			
(dollar amounts in thousands)	CFC	RTFC	NCSC	Total
Balance as of August 31, 2012	$ 136,781	$ 8,877	$ 6,843	$ 152,501
(Recovery of) provision for loan losses	(3,256)	(563)	2	(3,817)
Recoveries of loans previously charged-off	53	-	-	53
Balance as of November 30, 2012	$ 133,578	$ 8,314	$ 6,845	$ 148,737

	As of and for the three months ended November 30, 2011			
(dollar amounts in thousands)	CFC	RTFC	NCSC	Total
Balance as of August 31, 2011	$ 134,457	$ 8,649	$ 8,994	$ 152,100
(Recovery of) provision for loan losses	(3,625)	824	(194)	(2,995)
Recoveries of loans previously charged-off	53	-	-	53
Balance as of November 30, 2011	$ 130,885	$ 9,473	$ 8,800	$ 149,158

	As of and for the six months ended November 30, 2012			
(dollar amounts in thousands)	CFC	RTFC	NCSC	Total
Balance as of May 31, 2012	$ 126,941	$ 8,562	$ 7,823	$ 143,326
Provision for (recovery of) loan losses	6,531	(248)	(978)	5,305
Recoveries of loans previously charged-off	106	-	-	106
Balance as of November 30, 2012	$ 133,578	$ 8,314	$ 6,845	$ 148,737

	As of and for the six months ended November 30, 2011			
(dollar amounts in thousands)	CFC	RTFC	NCSC	Total
Balance as of May 31, 2011	$ 143,706	$ 8,389	$ 9,082	$ 161,177
(Recovery of) provision for loan losses	(12,927)	1,084	(282)	(12,125)
Recoveries of loans previously charged-off	106	-	-	106
Balance as of November 30, 2011	$ 130,885	$ 9,473	$ 8,800	$ 149,158

Our allowance for loan losses includes a specific valuation allowance related to individually-evaluated impaired loans, as well as a general reserve for other probable incurred losses for loans that are collectively evaluated. The tables below present the loan loss allowance and the recorded investment in outstanding loans by impairment methodology and by company:

	November 30, 2012			
(dollar amounts in thousands)	CFC	RTFC	NCSC	Total
Ending balance of the allowance:				
Collectively evaluated	$ 113,627	$ 6,695	$ 6,845	$ 127,167
Individually evaluated	19,951	1,619	-	21,570
Total ending balance of the allowance	$ 133,578	$ 8,314	$ 6,845	$ 148,737
Recorded investment in loans:				
Collectively evaluated	$ 17,790,837	$ 530,182	$ 693,712	$ 19,014,731
Individually evaluated	75,866	6,577	-	82,443
Total recorded investment in loans	$ 17,866,703	$ 536,759	$ 693,712	$ 19,097,174
Loans to members, net (1)	$ 17,733,125	$ 528,445	$ 686,867	$ 18,948,437

	May 31, 2012			
(dollar amounts in thousands)	CFC	RTFC	NCSC	Total
Ending balance of the allowance:				
Collectively evaluated	$ 103,681	$ 6,561	$ 7,823	$ 118,065
Individually evaluated	23,260	2,001	-	25,261
Total ending balance of the allowance	$ 126,941	$ 8,562	$ 7,823	$ 143,326
Recorded investment in loans:				
Collectively evaluated	$ 17,255,965	$ 564,596	$ 594,279	$ 18,414,840
Individually evaluated	489,932	6,970	-	496,902
Total recorded investment in loans	$ 17,745,897	$ 571,566	$ 594,279	$ 18,911,742
Loans to members, net (1)	$ 17,618,956	$ 563,004	$ 586,456	$ 18,768,416

(1) Excludes deferred origination costs of $8 million at November 30, 2012 and May 31, 2012.

Impaired Loans

Our recorded investment in individually-impaired loans and the related specific valuation allowance is summarized below by member class:

	November 30, 2012		May 31, 2012	
(dollar amounts in thousands)	Recorded investment	Related allowance	Recorded investment	Related allowance
With no specific allowance recorded:				
CFC/Distribution	$ 39,717	$ -	$ 415,692	$ -
With a specific allowance recorded:				
CFC/Distribution	31,149	19,709	69,240	23,009
CFC/Power Supply	5,000	242	5,000	251
RTFC	6,577	1,619	6,970	2,001
Total	42,726	21,570	81,210	25,261
Total impaired loans	$ 82,443	$ 21,570	$ 496,902	$ 25,261

The recorded investment for impaired loans was equal to the total unpaid principal balance for impaired loans as of November 30, 2012 and May 31, 2012. The table below represents the average recorded investment in impaired loans and the interest income recognized by member class:

	For the three months ended November 30,			
	2012	2011	2012	2011
(dollar amounts in thousands)	Average recorded investment		Interest income recognized	
CFC/Distribution	$ 70,706	$ 491,101	$ 7,625	$ 4,084
CFC/Power Supply	5,000	2,667	-	-
RTFC	6,618	7,962	-	-
Total impaired loans	$ 82,324	$ 501,730	$ 7,625	$ 4,084

	For the six months ended November 30,			
	Average recorded investment		Interest income recognized	
(dollar amounts in thousands)	2012	2011	2012	2011
CFC/Distribution	$ 277,891	$ 494,620	$ 13,087	$ 4,776
CFC/Power Supply	5,000	1,333	-	-
RTFC	6,754	5,322	-	-
Total impaired loans	$ 289,645	$ 501,275	$ 13,087	$ 4,776

Non-performing and Restructured Loans

Interest income was reduced as a result of holding loans on non-accrual status as follows:

For the three months ended November 30,		For the six months ended November 30,	
2012	2011	2012	2011

(dollar amounts in thousands)								
Non-performing loans	$	373	$	388	$	780	$	805
Restructured loans		-		1,384		-		6,714
Total	$	373	$	1,772	$	780	$	7,519

At November 30, 2012 and May 31, 2012, non-performing loans included $43 million, or 0.2 percent, of loans outstanding and $41 million or 0.2 percent, of loans outstanding, respectively. Two borrowers in this group are currently in bankruptcy. In one of the bankruptcy cases, the borrower filed a disclosure statement and draft plan of reorganization on November 27, 2012. The disclosure statement and draft plan are subject to certain changes and approval of the bankruptcy court, which is expected to occur in January 2013. In the other bankruptcy case, the borrower has until February 15, 2013 to file a disclosure statement and a Chapter 11 plan. There are two other borrowers that are currently seeking buyers for their systems, as it is not anticipated that they will have sufficient cash flow to repay their loans without the proceeds from the sale of the business. It is currently anticipated that even with the sale of the business, there will not be sufficient funds to repay the full amount owed. We have approval rights with respect to the sale of either or both of these companies.

At November 30, 2012 and May 31, 2012, we had restructured loans totaling $40 million, or 0.2 percent, of loans outstanding and $456 million, or 2.4 percent, of loans outstanding, respectively, all of which were performing according to their restructured terms. Approximately $8 million and $13 million of interest income was accrued on restructured loans during the three and six months ended November 30, 2012, respectively, compared with $4 million and $5 million of interest income in the prior-year periods, respectively. One of the restructured loans totaling $40 million at November 30, 2012 and May 31, 2012, has been on accrual status since the time of restructuring. The other restructured loan totaling $416 million at May 31, 2012, was on non-accrual status through September 30, 2011, with all amounts collected being applied against the principal balance. On October 1, 2011, the principal balance of the loan was reduced below the level of a buyout option and as such we placed the loan on accrual status at that time at a rate based on the effective rate returned by the future scheduled cash flows. This loan was paid off early by the borrower on September 13, 2012.

We believe our allowance for loan loss is adequate to cover the losses inherent in our loan portfolio at November 30, 2012.

Pledging of Loans and Loans on Deposit

We are required to pledge eligible mortgage notes in an amount at least equal to the outstanding balance of our secured debt.

The following table summarizes our loans outstanding as collateral pledged to secure our collateral trust bonds, Clean Renewable Energy Bonds and notes payable to the Federal Agricultural Mortgage Corporation and the amount of the corresponding debt outstanding (see Note 5, Short-Term Debt and Credit Arrangements and Note 6, Long-Term Debt).

(dollar amounts in thousands)		November 30, 2012		May 31, 2012
Collateral trust bonds:				
2007 indenture				
Distribution system mortgage notes	$	5,839,885	$	5,833,475
RUS guaranteed loans qualifying as permitted investments		167,953		170,024
Total pledged collateral	$	6,007,838	$	6,003,499
Collateral trust bonds outstanding		4,979,372		4,850,000
1994 indenture				
Distribution system mortgage notes	$	1,724,015	$	1,574,823
Collateral trust bonds outstanding		1,465,000		1,470,000
Federal Agricultural Mortgage Corporation:				
Distribution and power supply system mortgage notes	$	1,579,274	$	1,379,989
Notes payable outstanding		1,298,506		1,165,100
Clean Renewable Energy Bonds Series 2009A:				
Distribution and power supply system mortgage notes	$	24,605	$	25,640
Cash		7,218		7,669
Total pledged collateral	$	31,823	$	33,309
Notes payable outstanding		21,545		23,487

We are required to maintain collateral on deposit in an amount at least equal to the balance of debt outstanding to the Federal Financing Bank of the United States Treasury issued under the Guaranteed Underwriter program of the U.S. Department of Agriculture (see Note 6, Long-Term Debt).

The following table shows the collateral on deposit and the amount of the corresponding debt outstanding:

(dollar amounts in thousands)	November 30, 2012	May 31, 2012
Federal Financing Bank		
Distribution and power supply system mortgage notes on deposit	$ 4,053,511	$ 3,814,311
Notes payable outstanding	3,674,000	3,419,000

(4) Foreclosed Assets

Assets received in satisfaction of loan receivables are initially recorded at fair value when received and are subsequently evaluated periodically for impairment. These assets are classified on the consolidated balance sheets as foreclosed assets. At November 30, 2012 all foreclosed assets were held by DRP and CAH, which are wholly-owned subsidiaries of CFC.

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The activity for foreclosed assets is summarized below:

	As of and for the six months ended November 30, 2012		
(dollar amounts in thousands)	CAH	DRP	Total
Balance as of May 31, 2012	$ 201,558	$ 21,918	$ 223,476
Results of operations:			
Operating loss	(5,327)	(171)	(5,498)
Impairment	-	(176)	(176)
Cash investments	28,001	-	28,001
Balance as of November 30, 2012	$ 224,232	$ 21,571	$ 245,803

(5) Short-Term Debt and Credit Arrangements

The following is a summary of short-term debt outstanding:

(dollar amounts in thousands)	November 30, 2012	May 31, 2012
Short-term debt:		
Commercial paper sold through dealers, net of discounts (1)	$ 1,009,898	$ 1,404,901
Commercial paper sold directly to members, at par (1)	1,408,371	997,778
Commercial paper sold directly to non-members, at par (1)	39,828	70,479
Select notes	51,852	-
Daily liquidity fund notes sold directly to members	656,701	478,406
Bank bid notes	295,000	295,000
Subtotal short-term debt	3,461,650	3,246,564
Long-term debt maturing within one year:		
Medium-term notes sold through dealers	630,262	232,830
Medium-term notes sold to members	396,806	409,961
Secured collateral trust bonds	1,204,783	254,962
Member subordinated certificates	15,080	16,710
Secured notes payable	336,872	327,006
Unsecured notes payable	5,408	5,401
Total long-term debt maturing within one year	2,589,211	1,246,870
Total short-term debt	$ 6,050,861	$ 4,493,434

(1) Backup liquidity provided by bank lines of credit.

Revolving Credit Agreements

At November 30, 2012 and May 31, 2012, we had $2,845 million of commitments under revolving credit agreements. We may request letters of credit for up to $100 million under each agreement in place at November 30, 2012, which then reduces the amount available under the facility. The following table presents the total available and the outstanding letters of credit under our revolving credit agreements:

	Total available		Letters of credit outstanding			
(dollar amounts in thousands)	November 30, 2012	May 31, 2012	November 30, 2012	May 31, 2012	Original maturity	Facility fee per year (1)
Three-year agreement	$ 1,125,000	$1,125,000	$ -	$ -	March 21, 2014	15 basis points
Four-year agreement	883,875	883,875	1,000	1,000	October 21, 2015	10 basis points
Five-year agreement	831,387	834,875	3,488	-	October 21, 2016	10 basis points
Total	$ 2,840,262	$2,843,750	$ 4,488	$ 1,000		

(1) Facility fee determined by CFC's senior unsecured credit ratings based on the pricing schedules put in place at the inception of the related agreement.

The following represents our required and actual financial ratios under the revolving credit agreements:

		Actual	
	Requirement	November 30, 2012	May 31, 2012
Minimum average adjusted TIER over the six most recent fiscal quarters (1)	1.025	1.19	1.21
Minimum adjusted TIER for the most recent fiscal year (1) (2)	1.05	1.18	1.18
Maximum ratio of adjusted senior debt to total equity (1)	10.00	5.96	5.97

(1) In addition to the adjustments made to the leverage ratio set forth in the Non-GAAP Financial Measures section, senior debt excludes guarantees to member systems that have certain investment-grade ratings from Moody's Investors Service and Standard & Poor's Corporation. The TIER and debt-to-equity calculations include the adjustments set forth in the Non-GAAP Financial Measures section and exclude the results of operations for CAH.
(2) We must meet this requirement to retire patronage capital.

At November 30, 2012 and May 31, 2012, we were in compliance with all covenants and conditions under our revolving credit agreements and there were no borrowings outstanding under these agreements.

(6) Long-Term Debt

The following is a summary of long-term debt outstanding:

(dollar amounts in thousands)	November 30, 2012	May 31, 2012
Unsecured long-term debt:		
Medium-term notes sold through dealers	$ 1,295,252	$ 1,692,605
Medium-term notes sold to members	156,403	89,261
Subtotal	1,451,655	1,781,866
Unamortized discount	(634)	(971)
Total unsecured medium-term notes	1,451,021	1,780,895
Unsecured notes payable	3,712,982	3,457,982
Unamortized discount	(1,011)	(1,093)
Total unsecured notes payable	3,711,971	3,456,889
Total unsecured long-term debt	5,162,992	5,237,784
Secured long-term debt:		
Collateral trust bonds	5,239,372	6,065,000
Unamortized discount	(184,070)	(12,398)
Total secured collateral trust bonds	5,055,302	6,052,602
Secured notes payable	983,178	861,581
Total secured long-term debt	6,038,480	6,914,183
Total long-term debt	$ 11,201,472	$ 12,151,967

At November 30, 2012 and May 31, 2012, we had unsecured notes payable totaling $3,674 million and $3,419 million, respectively, outstanding under a bond purchase agreement with the Federal Financing Bank and a bond guarantee agreement with RUS issued under the Guaranteed Underwriter program of the U.S. Department of Agriculture, which provides guarantees to the Federal Financing Bank. During the six months ended November 30, 2012, we borrowed $255 million under our committed loan facilities with the Federal Financing Bank. In the aggregate at November 30, 2012, we had up to $325 million available under committed loan facilities from the Federal Financing Bank as part of this program.

At November 30, 2012 and May 31, 2012, secured notes payable include $1,299 million and $1,165 million, respectively, in debt outstanding to the Federal Agricultural Mortgage Corporation under a note purchase agreement totaling $3,900 million. All note purchase agreements previously entered into with the Federal Agricultural Mortgage Corporation were consolidated into one agreement in March 2011. Under the terms of the March 2011 note purchase agreement, we can borrow up to $3,900 million at any time from the date of the agreement through January 11, 2016 and thereafter automatically extend the agreement on each anniversary date of the closing for an additional year, unless prior to any such anniversary date, the Federal Agricultural Mortgage Corporation provides CFC with a notice that the draw period will not be extended beyond the then-remaining term. The agreement with the Federal Agricultural Mortgage Corporation is a revolving credit facility that allows us to borrow, repay and re-borrow funds at any time through maturity or from time to time as market conditions permit, provided that the principal amount at any time outstanding under the note purchase agreement is not more than the total available under the agreement. In

November 2012, we issued notes totaling $133 million under the agreement with the Federal Agricultural Mortgage Corporation.

In September 2012, CFC commenced an offer to exchange a portion of its outstanding 8 percent medium-term notes, Series C, due 2032 for consideration of collateral trust bonds due 2032 and cash. On October 10, 2012, following the expiration of the offering period, CFC announced that it had accepted $340 million aggregate principal amount of medium-term notes for exchange. At settlement, on October 16, 2012, holders whose medium-term notes were accepted for exchange received $379 million aggregate principal amount of 4.023 percent collateral trust bonds due 2032 and $134 million in cash.

(7) Subordinated Deferrable Debt

The following table is a summary of subordinated deferrable debt outstanding:

(dollar amounts in thousands)		November 30, 2012		May 31, 2012
NRC 6.10% due 2044	$	88,201	$	88,201
NRU 5.95% due 2045		98,239		98,239
Total	$	186,440	$	186,440

All subordinated deferrable debt currently outstanding is callable at par at any time.

(8) Derivative Financial Instruments

We are an end-user of financial derivative instruments. We utilize derivatives such as interest rate swaps and treasury rate locks for forecasted transactions to mitigate interest rate risk. The following table shows the notional amounts outstanding and the weighted average interest rate paid and received for our interest rate swaps by type:

	November 30, 2012			May 31, 2012		
(dollar amounts in thousands)	Notional amount	Weighted-average rate paid	Weighted-average rate received	Notional amount	Weighted-average rate paid	Weighted-average rate received
Pay fixed-receive variable	$ 5,790,832	3.62%	0.30%	$ 5,275,553	3.78%	0.45%
Pay variable-receive fixed	3,500,440	1.12	4.75	3,720,440	1.29	4.68
Total interest rate swaps	$ 9,291,272	2.68	1.98	$ 8,995,993	2.75	2.20

The derivative losses line item of the consolidated statement of operations includes cash settlements and derivative forward value for derivative instruments that do not meet hedge accounting criteria. Cash settlements includes periodic amounts paid and received related to our interest rate swaps, as well as amounts accrued from the prior settlement date. Derivative forward value includes changes in the fair value of derivative instruments unless specific hedge accounting criteria are met. If applicable hedge accounting criteria are satisfied, the change to the fair value is recorded to other comprehensive income (loss) and net cash settlements are recorded in interest expense. Gains and losses recorded on the consolidated statements of operations for our interest rate swaps are summarized below:

	For the three months ended November 30,				For the six months ended November 30,			
(dollar amounts in thousands)		2012		2011		2012		2011
Derivative cash settlements	$	(15,456)	$	(982)	$	(29,319)	$	(814)
Derivative forward value		11,690		(46,771)		961		(158,510)
Derivative losses	$	(3,766)	$	(47,753)	$	(28,358)	$	(159,324)

Rating Triggers

Some of our interest rate swaps have credit risk-related contingent features referred to as rating triggers. Rating triggers are not separate financial instruments and are not required to be accounted for separately as derivatives. At November 30, 2012, the following notional amounts of derivative instruments had rating triggers based on our senior unsecured credit ratings from Moody's Investors Service or Standard & Poor's Corporation falling to a level specified in the applicable agreements and are grouped into the categories below. In calculating the payments and collections required upon termination, we netted the agreements for each counterparty, as allowed by the underlying master agreements. At November 30, 2012, our senior unsecured credit ratings from Moody's Investors Service and Standard & Poor's Corporation were A2 and A, respectively. At November 30, 2012, both Moody's Investors Service and Standard & Poor's Corporation had our ratings on stable outlook.

(dollar amounts in thousands)	Notional amount	Our required payment	Amount we would collect	Net total
Mutual rating trigger if ratings:				
fall to Baa1/BBB+ (1)	$ 3,000	$ (157)	$ -	$ (157)
fall below Baa1/BBB+ (1)	6,890,779	(290,678)	38,257	(252,421)
Total	$ 6,893,779	$ (290,835)	$ 38,257	$ (252,578)

(1) Stated senior unsecured credit ratings are for Moody's Investors Service and Standard & Poor's Corporation, respectively. Under these rating triggers, if the credit rating for either counterparty falls to the level specified in the agreement, the other counterparty may, but is not obligated to, terminate the agreement. If either counterparty terminates the agreement, a net payment may be due from one counterparty to the other based on the fair value, excluding credit risk, of the underlying derivative instrument.

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In addition to the rating triggers listed above, at November 30, 2012 we had a total notional amount of $650 million of derivative instruments with one counterparty that would require the pledging of collateral totaling $16 million (the fair value of such derivative instruments excluding credit risk) if our senior unsecured ratings from Moody's Investors Service were to fall below Baa2 or if the ratings from Standard & Poor's Corporation were to fall below BBB. The aggregate fair value of all interest rate swaps with rating triggers that were in a net liability position at November 30, 2012 was $299 million.

(9) Equity

In July 2012, the CFC Board of Directors authorized the allocation of the fiscal year 2012 net earnings as follows: $1 million to the cooperative educational fund and $71 million to members in the form of patronage. In July 2012, the CFC Board of Directors authorized the retirement of allocated net earnings totaling $35 million, representing 50 percent of the fiscal year 2012 allocation. This amount was returned to members in cash in September 2012. Future allocations and retirements of net earnings may be made annually as determined by the CFC Board of Directors with due regard for its financial condition. The CFC Board of Directors has the authority to change the current practice for allocating and retiring net earnings at any time, subject to applicable laws and regulations.

(10) Guarantees

The following table summarizes total guarantees by type of guarantee and member class:

(dollar amounts in thousands)	November 30, 2012	May 31, 2012
Total by type:		
Long-term tax-exempt bonds	$ 555,960	$ 573,110
Indemnifications of tax benefit transfers	2,419	49,771
Letters of credit	452,373	504,920
Other guarantees	116,916	121,529
Total	$ 1,127,668	$ 1,249,330
Total by member class:		
CFC:		
Distribution	$ 269,610	$ 340,385
Power supply	816,296	854,444
Statewide and associate	6,514	7,202
CFC total	1,092,420	1,202,031
RTFC	4,738	1,026
NCSC	30,510	46,273
Total	$ 1,127,668	$ 1,249,330

The maturities for the long-term tax-exempt bonds and the related guarantees run through calendar year 2042. Amounts in the table represent the outstanding principal amount of the guaranteed bonds. At November 30, 2012, our maximum potential exposure for the $75 million of fixed-rate tax-exempt bonds is $125 million, representing principal and interest. Of the amounts shown in the table above for long-term tax-exempt bonds, $481 million and $498 million as of November 30, 2012 and May 31, 2012, respectively, are adjustable or floating-rate bonds that may be converted to a fixed rate as specified in the applicable indenture for each bond offering. We are unable to determine the maximum amount of interest that we could be required to pay related to the remaining adjustable and floating-rate bonds. Many of these bonds have a call provision that in the event of a default allow us to trigger the call provision. This would limit our exposure to future interest payments on these bonds. Our maximum potential exposure is secured by a mortgage lien on all of the system's assets and future revenue. If the debt is accelerated because of a determination that the interest thereon is not tax-exempt, the system's obligation to reimburse us for any guarantee payments will be treated as a long-term loan.

The maturities for the indemnifications of tax benefit transfers run through calendar year 2015. The amounts shown represent our maximum potential exposure for guaranteed indemnity payments. A member's obligation to reimburse CFC for any guarantee payments would be treated as a long-term loan to the extent of any cash received by the member at the outset of the transaction. This amount is secured by a mortgage lien on substantially all of the system's assets and future revenue. The remainder would be treated as a line of credit loan secured by a subordinated mortgage on substantially all of the member's property. Due to changes in federal tax law, no further guarantees of this nature are anticipated.

The maturities for letters of credit run through calendar year 2024. The amounts shown in the table above represent our maximum potential exposure, of which $185 million is secured at November 30, 2012. At November 30, 2012, and May 31, 2012, the letters of credit include $125 million to provide the standby liquidity for adjustable and floating-rate tax-exempt bonds issued for the benefit of our members. Security provisions include a mortgage lien on substantially all of the system's assets, future revenue and the system's investment in our commercial paper.

In addition to the letters of credit listed in the table, under master letter of credit facilities in place at November 30, 2012, we may be required to issue up to an additional $837 million in letters of credit to third parties for the benefit of our members. Of this amount, $649 million represents commitments that may be used for the issuance of letters of credit or line of credit loan advances, at the option of the borrower, and are included in unadvanced loan commitments for line of credit loans reported in Note 3, Loans and Commitments. Master letter of credit facilities subject to material adverse change clauses at the time of issuance totaled $496 million at November 30, 2012. Prior to issuing a letter of credit, we would confirm that there has been no material adverse change in the business or condition, financial or otherwise, of the borrower since the time the loan was approved and confirm that the borrower is currently in compliance with the letter of credit terms and conditions. The remaining commitment under master letter of credit facilities of $341 million may be used for the issuance of letters of credit as long as the borrower is in compliance with the terms and conditions of the facility.

The maturities for other guarantees run through calendar year 2025. The maximum potential exposure for these guarantees is $118 million, all of which is unsecured.

At November 30, 2012 and May 31, 2012, we had $384 million and $385 million of guarantees, representing 34 percent and 31 percent, respectively, of total guarantees, under which our right of recovery from our members was not secured.

In addition to the guarantees in the chart above, at November 30, 2012, we are the liquidity provider for a total of $606 million of variable-rate tax-exempt bonds issued for our member cooperatives. While the bonds are in variable-rate mode, we have, in return for a fee, unconditionally agreed to purchase bonds tendered or put for redemption if the remarketing agents are unable to sell such bonds to other investors. During the six months ended November 30, 2012, we were not required to perform as liquidity provider pursuant to these obligations.

Guarantee Liability

At November 30, 2012 and May 31, 2012, we recorded a guarantee liability of $27 million and $29 million, respectively, which represents the contingent and non-contingent exposures related to guarantees and liquidity obligations associated with our members' debt. The contingent guarantee liability at November 30, 2012 and May 31, 2012 was $6 million for both periods, based on management's estimate of exposure to losses within the guarantee portfolio. The remaining balance of the total guarantee liability of $21 million and $23 million at November 30, 2012 and May 31, 2012, respectively, relates to our non-contingent obligation to stand ready to perform over the term of our guarantees and liquidity obligations that we have entered into or modified since January 1, 2003.

Activity in the guarantee liability account is summarized below:

(dollar amounts in thousands)	As of and for the six months ended November 30, 2012
Beginning balance as of May 31, 2012	$ 28,663

Net change in non-contingent liability		(1,584)
Recovery of contingent guarantee liability		(101)
Ending balance as of November 30, 2012	$	26,978
Liability as a percentage of total guarantees		2.39%

(11) Fair Value Measurement

Assets and liabilities measured at fair value on either a recurring or non-recurring basis on the consolidated balance sheets at November 30, 2012 and May 31, 2012 consisted of investments in common stock, derivative instruments, and collateral-dependent non-performing loans.

Assets and Liabilities Measured at Fair Value on a Recurring Basis
We account for derivative instruments (including certain derivative instruments embedded in other contracts) in the consolidated balance sheets as either an asset or liability measured at fair value. Since there is not an active secondary market for the types of interest rate swaps we use, we obtain market quotes from the interest rate swap counterparties to adjust all swaps to fair value on a quarterly basis. The market quotes are based on the expected future cash flow and the estimated yield curve.

We perform analysis to validate the market quotes obtained from our swap counterparties. We adjust the market values received from the counterparties using credit default swap levels for us and the counterparties. The credit default swap levels represent the credit risk premium required by a market participant based on the available information related to us and the counterparty. We only enter into exchange agreements with counterparties that are participating in our revolving lines of credit at the time the exchange agreements are executed. All of our exchange agreements are subject to master netting agreements.

Our valuation techniques for interest rate swaps are based on observable inputs, which reflect market data. Fair values for our interest rate swaps are classified as a Level 2 valuation. We record the change in the fair value of our derivatives for each reporting period in the derivative gains (losses) line, included in non-interest income in the consolidated statements of operations, as currently none of our derivatives qualify for hedge accounting.

At November 30, 2012 and May 31, 2012, our investments in equity securities included investments in the Federal Agricultural Mortgage Corporation Series A common stock that is recorded in the consolidated balance sheets at fair value. We calculate fair value based on the quoted price on the stock exchange where the stock is traded. That stock exchange is an active market based on the volume of shares transacted. Fair values for these securities are classified as a Level 1 valuation.

The following table presents our assets and liabilities that are measured at fair value on a recurring basis:

	November 30, 2012		May 31, 2012	
(dollar amounts in thousands)	Level 1	Level 2	Level 1	Level 2
Derivative assets	$ -	$ 273,480	$ -	$ 296,036
Derivative liabilities	-	630,919	-	654,125
Investments in common stock	2,354	-	1,467	-

Assets and Liabilities Measured at Fair Value on a Non-recurring Basis
We may be required, from time to time, to measure certain assets at fair value on a non-recurring basis in accordance with GAAP. Any adjustments to fair value usually result from application of lower-of-cost or fair value accounting or write-downs of individual assets. At November 30, 2012 and May 31, 2012, we measured certain collateral-dependent non-performing loans at fair value. In certain instances when a loan is non-performing, we utilize the collateral fair value underlying the loan in estimating the specific loan loss allowance. To estimate the fair value of the collateral, we may use third party valuation specialists, internal estimates or a combination of both. The approaches used by both our internal staff and third party specialists include the discounted cash flow, market multiple and replacement cost methods. The material inputs used in estimating the fair value of such collateral, by both internal staff and third party specialists, are Level 3 within the fair value hierarchy. In these instances, the valuation is considered to be a non-recurring item. The significant unobservable inputs for Level 3 assets that are valued using fair values obtained from third party specialists are reviewed by our Credit Risk Management group to assess the reasonableness of the assumptions used and the accuracy of the work performed. In cases where we rely on third party inputs, we use the final unadjusted third party valuation analysis as support for any financial statement adjustments and disclosures to the financial statements. The valuation techniques and significant unobservable inputs for assets classified as Level 3 in the fair value hierarchy, which are measured using an internal model, are independently reviewed by other internal staff.

For assets measured at fair value on a non-recurring basis at November 30, 2012 and May 31, 2012 that are classified as Level 3 within the fair value hierarchy, any increase or decrease to significant unobservable inputs used in the determination of fair value, will not have a material impact on the fair value measurement of those assets or to the results of operations of the Company.

Assets measured at fair value on a non-recurring basis at November 30, 2012 and May 31, 2012 were classified as Level 3 within the fair value hierarchy. The following table provides the carrying/fair value of the related individual assets at November 30, 2012 and May 31, 2012 and the total losses for the three and six months ended November 30, 2012 and 2011:

	Level 3 Fair Value		Total losses for the three months ended November 30,		Total losses for the six months ended November 30,	
(dollar amounts in thousands)	November 30, 2012	May 31, 2012	2012	2011	2012	2011
Non-performing loans, net of specific reserves	$ 21,156	$ 16,517	$ -	$ (167)	$ -	$ (2,220)

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(12) Fair Value of Financial Instruments

Carrying and fair values for our financial instruments are presented as follows:

	November 30, 2012		May 31, 2012	
(dollar amounts in thousands)	Carrying value	Fair value	Carrying value	Fair value
Assets:				
Cash and cash equivalents	$ 439,183	$ 439,183		