

## Non-GAAP Financial Measures

We make certain adjustments to financial measures in assessing our financial performance that are not in accordance with GAAP. These non-GAAP adjustments fall primarily into two categories: (1) adjustments related to the calculation of the TIER ratio, and (2) adjustments related to the calculation of leverage and debt to equity ratios. These adjustments reflect management's perspective on our operations, and in several cases, adjustments used to measure covenant compliance under our revolving credit agreements, and therefore we believe these are useful financial measures for investors. We refer to our non-GAAP financial measures as "adjusted" throughout this document.

### *Adjustments to Net Income and the Calculation of the TIER Ratio*

The following table provides a reconciliation between interest expense, net interest income, income prior to income taxes and net income and these financial measures adjusted to exclude the effect of derivatives for the three and six months ended November 30, 2009 and November 30, 2008. Refer to Non-GAAP Financial Measures in Item 7, *Management's Discussion and Analysis of Financial Condition and Results of Operations*, in our Form 10-K/A for the year ended May 31, 2009 for an explanation of why these adjustments to net income and the calculation of the TIER ratio reflect management's perspective on our operations and why we believe these are useful financial measures for investors.

Due to the adoption of new accounting guidance regarding noncontrolling interests on June 1, 2009, minority interest net income is included in total net income on the consolidated statement of operations for the three and six months ended November 30, 2009 and 2008. As a result, it is not necessary to adjust net income to include minority interest net income as it was in prior periods. As required, we have reflected changes in presentation and disclosure of noncontrolling interest in our consolidated financial statements for all periods presented in this Form 10-Q, including the adjusted net income and TIER calculations for the six months ended November 30, 2008.

| (dollar amounts in thousands)   | Three months ended<br>November 30, |                     | Six months ended<br>November 30, |                     |
|---|------------------------------------|---------------------|----------------------------------|---------------------|
|   | 2009                               | 2008                | 2009                             | 2008                |
| Interest expense  | \$ (226,977)                       | \$ (234,187)        | \$ (469,606)                     | \$ (454,336)        |
| Derivative cash settlements   | (10,706)                           | 12,503              | (14,200)                         | 12,934              |
| Adjusted interest expense   | <u>\$ (237,683)</u>                | <u>\$ (221,684)</u> | <u>\$ (483,806)</u>              | <u>\$ (441,402)</u> |
| Net interest income   | \$ 37,942                          | \$ 32,559           | \$ 64,770                        | \$ 75,527           |
| Derivative cash settlements   | (10,706)                           | 12,503              | (14,200)                         | 12,934              |
| Adjusted net interest income  | <u>\$ 27,236</u>                   | <u>\$ 45,062</u>    | <u>\$ 50,570</u>                 | <u>\$ 88,461</u>    |
| Income (loss) prior to income taxes   | \$ 21,578                          | \$ (237,755)        | \$ 38,043                        | \$ (225,285)        |
| Derivative forward value  | (7,562)                            | 139,383             | 3,272                            | 150,411             |
| Adjusted income (loss) prior to income taxes                                      | <u>\$ 14,016</u>                   | <u>\$ (98,372)</u>  | <u>\$ 41,315</u>                 | <u>\$ (74,874)</u>  |
| Net income (loss) prior to cumulative effect of change in<br>accounting principle | \$ 22,419                          | \$ (231,355)        | \$ 38,852                        | \$ (218,125)        |
| Derivative forward value  | (7,562)                            | 139,383             | 3,272                            | 150,411             |
| Adjusted net income (loss)  | <u>\$ 14,857</u>                   | <u>\$ (91,972)</u>  | <u>\$ 42,124</u>                 | <u>\$ (67,714)</u>  |

TIER using GAAP financial measures is calculated as follows:

$$\text{TIER} = \frac{\text{Interest expense} + \text{net income prior to cumulative effect of change in accounting principle}}{\text{Interest expense}}$$

Our adjusted TIER is calculated as follows:

$$\text{Adjusted TIER} = \frac{\text{Adjusted interest expense} + \text{adjusted net income}}{\text{Adjusted interest expense}}$$

The following table presents our TIER and adjusted TIER:

|                   | Three months ended<br>November 30, |      | Six months ended<br>November 30, |      |
|-------------------|------------------------------------|------|----------------------------------|------|
|                   | 2009                               | 2008 | 2009                             | 2008 |
| TIER (1)          | 1.10                               | -    | 1.08                             | -    |
| Adjusted TIER (1) | 1.06                               | -    | 1.09                             | -    |

(1) For the three and six months ended November 30, 2008, the Company reported a net loss of \$231 million and \$218 million, respectively. For the three and six months ended November 30, 2008, the Company reported an adjusted net loss of \$92 million and \$68 million, respectively. Thus the TIER and adjusted TIER calculations for those periods results in a value below 1.00.

#### ***Adjustments to the Calculation of Leverage and Debt to Equity***

The following table provides a reconciliation between the liabilities and equity used to calculate the leverage and debt to equity ratios and these financial measures adjusted to exclude the non-cash effects of derivatives and foreign currency adjustments, to subtract debt used to fund loans that are guaranteed by RUS from total liabilities, to subtract from total liabilities, and add to total equity, debt with equity characteristics and to include minority interest as equity. Due to the adoption of new accounting guidance regarding noncontrolling interests on June 1, 2009, minority interest is reported as equity on the consolidated balance sheets as of November 30, 2009 and May 31, 2009. As a result, it is not necessary to adjust equity to include minority interest in the leverage and debt to equity ratio as it was in prior periods. As required, we have reflected the changes in presentation and disclosure of noncontrolling interest in our consolidated financial statements for all periods presented in this Form 10-Q including the leverage and debt to equity ratios at May 31, 2009.

Refer to *Non-GAAP Financial Measures* in Item 7, *Management's Discussion and Analysis of Financial Condition and Results of Operations*, in our Form 10-K/A for the year ended May 31, 2009 for an explanation of why these adjustments to the calculation of leverage and debt to equity ratios reflect management's perspective on our operations and why we believe these are useful financial measures for investors.

|   | November 30,<br>2009 | May 31,<br>2009 |
|---|----------------------|-----------------|
| (dollar amounts in thousands)   |                      |                 |
| Liabilities   | \$ 19,922,325        | \$ 20,463,605   |
| Less:   |                      |                 |
| Derivative liabilities  | (544,655)            | (493,002)       |
| Debt used to fund loans guaranteed by RUS                                       | (239,482)            | (243,997)       |
| Subordinated deferrable debt  | (311,440)            | (311,440)       |
| Subordinated certificates   | (1,790,206)          | (1,740,054)     |
| Adjusted liabilities  | \$ 17,036,542        | \$ 17,675,112   |
| Total equity  | \$ 515,601           | \$ 519,100      |
| Less:   |                      |                 |
| Prior year cumulative derivative forward value and foreign currency adjustments | 103,493              | (44,056)        |
| Year-to-date derivative forward value loss (1)                                  | 925                  | 147,549         |
| Accumulated other comprehensive income  | (7,789)              | (8,115)         |
| Plus:   |                      |                 |
| Subordinated certificates   | 1,790,206            | 1,740,054       |
| Subordinated deferrable debt  | 311,440              | 311,440         |
| Adjusted equity   | \$ 2,713,876         | \$ 2,665,972    |
| Guarantees  | \$ 1,195,739         | \$ 1,275,455    |

(1) Represents the derivative forward value loss recorded by CFC for the year-to-date period.

The leverage and debt to equity ratios using GAAP financial measures are calculated as follows:

$$\text{Leverage ratio} = \frac{\text{Liabilities} + \text{guarantees outstanding}}{\text{Total equity}}$$

$$\text{Debt to equity ratio} = \frac{\text{Liabilities}}{\text{Total equity}}$$

The adjusted leverage and debt to equity ratios are calculated as follows:

$$\text{Adjusted leverage ratio} = \frac{\text{Adjusted liabilities} + \text{guarantees outstanding}}{\text{Adjusted equity}}$$

$$\text{Adjusted debt to equity ratio} = \frac{\text{Adjusted liabilities}}{\text{Adjusted equity}}$$

The following table provides the calculated ratio for leverage and debt to equity, as well as the adjusted ratio calculations.

|                               | November 30,<br>2009 | May 31,<br>2009 |
|-------------------------------|----------------------|-----------------|
| Leverage ratio                | <u>40.96</u>         | <u>41.88</u>    |
| Adjusted leverage ratio       | <u>6.72</u>          | <u>7.11</u>     |
| Debt to equity ratio          | <u>38.64</u>         | <u>39.42</u>    |
| Adjusted debt to equity ratio | <u>6.28</u>          | <u>6.63</u>     |

### **Item 3. Quantitative and Qualitative Disclosures About Market Risk**

See Market Risk discussion beginning on page 56.

### **Item 4T. Controls and Procedures**

Senior management, including the Chief Executive Officer and Chief Financial Officer, evaluated the effectiveness of our disclosure controls and procedures as defined in Rules 13a-15(e) and 15d-15(e) of the Securities Exchange Act of 1934 ("the Exchange Act"). At the end of the period covered by this report, based on this evaluation process, the Chief Executive Officer and Chief Financial Officer have concluded that our disclosure controls and procedures are effective. There were no changes in our internal control over financial reporting that occurred during our last fiscal quarter that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.