# AgGeorgia Farm Credit, ACA

# THIRD QUARTER 2014

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**CERTIFICATION**

The undersigned certify that we have reviewed the September 30, 2014 quarterly report of AgGeorgia Farm Credit, ACA, that the report has been prepared under the oversight of the Audit Committee of the Board of Directors and in accordance with all applicable statutory or regulatory requirements, and that the information contained herein is true, accurate, and complete to the best of our knowledge and belief.

Jack C. Drew, Jr.
Chief Executive Officer

Carrie B. McCall
Chief Financial Officer

J. Dan Raines, Jr.
Chairman of the Board

November 7, 2014

## AgGeorgia Farm Credit, ACA

# Report on Internal Control Over Financial Reporting

The Association's principal executives and principal financial officers, or persons performing similar functions, are responsible for establishing and maintaining adequate internal control over financial reporting for the Association's Consolidated Financial Statements. For purposes of this report, "internal control over financial reporting" is defined as a process designed by, or under the supervision of the Association's principal executives and principal financial officers, or persons performing similar functions, and effected by its Board of Directors, management and other personnel. This process provides reasonable assurance regarding the reliability of financial reporting information and the preparation of the Consolidated Financial Statements for external purposes in accordance with accounting principles generally accepted in the United States of America.

Internal control over financial reporting includes those policies and procedures that: (1) pertain to the maintenance of records that in reasonable detail accurately and fairly reflect the transactions and dispositions of the assets of the Association, (2) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial information in accordance with accounting principles generally accepted in the United States of America, and that receipts and expenditures are being made only in accordance with authorizations of management and directors of the Association, and (3) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use or disposition of the Association's assets that could have a material effect on its Consolidated Financial Statements.

The Association's management has completed an assessment of the effectiveness of internal control over financial reporting as of September 30, 2014. In making the assessment, management used the framework in *Internal Control — Integrated Framework*, promulgated by the Committee of Sponsoring Organizations of the Treadway Commission, commonly referred to as the "COSO" criteria.

Based on the assessment performed, the Association concluded that as of September 30, 2014, the internal control over financial reporting was effective based upon the COSO (1992) criteria. Additionally, based on this assessment, the Association determined that there were no material weaknesses in the internal control over financial reporting as of September 30, 2014.

Jack C. Drew, Jr.
Chief Executive Officer

Carrie B. McCall
Chief Financial Officer

November 7, 2014

# AgGeorgia Farm Credit, ACA

# Management's Discussion and Analysis of Financial Condition and Results of Operations

*(dollars in thousands)*

The following commentary reviews the financial condition and results of operations of AgGeorgia Farm Credit, ACA (Association or AgGeorgia) for the period ended September 30, 2014. These comments should be read in conjunction with the accompanying financial statements, notes to the financial statements and the 2013 Annual Report of the Association.

**LOAN PORTFOLIO**

The Association provides funds to farmers, rural homeowners and farm-related businesses for financing of short and intermediate term loans and long term real estate mortgage loans. The Association's loan portfolio is diversified over a range of agricultural commodities including poultry, cotton, timber, peanuts and livestock. Farm size varies and many of the borrowers in the region have diversified farming operations. This factor, along with the numerous opportunities for non-farm income in the area, somewhat reduces the level of dependency on any single commodity.

The gross loan volume of the Association as of September 30, 2014 was $878,070, an increase of $37,078 as compared to $840,992 at December 31, 2013. Net loans outstanding at September 30, 2014 were $871,107 as compared to $830,417 at December 31, 2013. This increase in loan volume is related to an increase in demand for loans resulting from an improvement in the economy as well as increased marketing efforts by the Association. Net loans accounted for 94.24 percent of total assets at September 30, 2014, as compared to 92.61 percent of total assets at December 31, 2013.

There is an inherent risk in the extension of any type of credit. Portfolio credit quality has increased, and credit administration remains satisfactory. Nonaccrual loans decreased from $41,064 at December 31, 2013 to $30,637 at September 30, 2014.

Association management maintains an allowance for loan losses in an amount considered sufficient to absorb possible losses in the loan portfolio based on current and expected future conditions. The allowance for loan losses at September 30, 2014, was $6,963 compared to $10,575 at December 31, 2013, and was considered by management to be adequate to cover probable losses.

**RESULTS OF OPERATIONS**

***For the three months ended September 30, 2014***

Net income for the three months ended September 30, 2014 totaled $4,497 as compared to $6,286 for the same period in 2013. This decrease is primarily due to a net gain on other property owned of ($1,163) in third quarter 2013 compared to a net loss of $14 for the same period in 2014.

Non-interest income for the three months ended September 30, 2014, totaled $1,619, as compared to $1,847 for the same period of 2013. This decrease is due to lower patronage refunds from other Farm Credit institutions in third quarter 2014 compared to the same period in 2013. Non-interest expense for the three months ended September 30, 2014 totaled $5,379, an increase of $1,531 compared to the same period of 2013. This difference is also due to the net gain on other property owned in 2013.

***For the nine months ended September 30, 2014***

Net income for the nine months ended September 30, 2014, totaled $12,117 as compared to $14,004 for the same period in 2013. Net interest income decreased $1,235 for the nine months ended September 30, 2014, as compared to the same period in 2013. This decrease is primarily related to a tightening of interest rate spreads in 2014. The Association recorded a loan loss provision of $64 for the nine months ended September 30, 2014, as compared to $835 for the same period in 2013.

Non-interest income for the nine months ended September 30, 2014, totaled $5,544, as compared to $6,657 for the same period of 2013, a decrease of $1,113. A decrease in patronage refunds and other income led to the decrease in non-interest income. The 2013 non-interest income includes a nonrecurring special patronage distribution of $524. Non-interest expense for the nine months ended September 30, 2014, increased $297 compared to the same period of 2013. This increase is the result of an increase in salary and benefits expense and other expense in 2014 compared to 2013.

**FUNDING SOURCES**

The principal source of funds for the Association is the borrowing relationship established with AgFirst Farm Credit Bank (the Bank) through a General Financing Agreement. The General Financing Agreement utilizes the Association's credit and fiscal performance as criteria for establishing a line of credit on which the Association may draw funds. The Bank advances funds to the Association in the form of notes payable. The notes payable are segmented into variable rate and fixed rate sections. The variable rate note is utilized by the Association to fund variable rate loan advances and operating funds requirements. The fixed rate note is used specifically to fund fixed rate loan advances made by the Association. The total notes payable to the Bank at September 30, 2014, was $690,454 as compared to $661,719 at December 31, 2013.

## CAPITAL RESOURCES

Total members' equity at September 30, 2014 increased $3,490 to $219,396 from the December 31, 2013 total of $215,906. The increase is related to net income for the nine months in 2014 less the revolvement of $7,487 of qualified allocated surplus in June 2014.

Total capital stock and participation certificates were $3,770 on September 30, 2014, compared to $3,774 on December 31, 2013. This decrease is attributed to the issuance of stock on new loans being less than the retirement of stock on loans liquidated in the normal course of business.

Farm Credit Administration (FCA) regulations require all Farm Credit institutions to maintain minimum permanent capital, total surplus and core surplus ratios. These ratios are calculated by dividing the Association's permanent capital, total surplus and core surplus as defined in FCA regulations, by a risk adjusted asset base. As of September 30, 2014, the Association's total surplus ratio and core surplus ratio were 23.24 percent and 19.63 percent, respectively, and the permanent capital ratio was 23.68 percent. All three ratios were well above the minimum regulatory ratios of 7.00 percent for permanent capital and total surplus ratios and 3.50 percent for the core surplus ratio.

## RECENTLY ISSUED ACCOUNTING PRONOUNCEMENTS

Please refer to Note 1, *"Organization, Significant Accounting Policies, and Recently Issued Accounting Pronouncements",* in the Notes to the Financial Statements, and the 2013 Annual Report to Shareholders for recently issued accounting pronouncements.

## REGULATORY MATTERS

On March 31, 2014, the FCA published an interim final rule rescinding all requirements for nonbinding advisory votes on senior officer compensation at System banks and associations. The comment period for the interim rule ended on April 30, 2014 and the final rule became effective on June 18, 2014.

On July 25, 2014, the FCA published a proposed rule in the Federal Register to revise the requirements governing the eligibility of investments for System banks and associations. The public comment period ended on October 23, 2014. The stated objectives of the proposed rule are as follows:

- To strengthen the safety and soundness of System banks and associations.
- To ensure that System banks hold sufficient liquidity to continue operations and pay maturing obligations in the event of market disruption.
- To enhance the ability of the System banks to supply credit to agricultural and aquatic producers.
- To comply with the requirements of section 939A of the Dodd-Frank Act.
- To modernize the investment eligibility criteria for System banks.
- To revise the investment regulation for System associations to improve their investment management practices so they are more resilient to risk.

On September 4, 2014, the FCA published a proposed rule in the Federal Register to modify the regulatory capital requirements for System banks and associations. The public comment period ends on January 2, 2015. The stated objectives of the proposed rule are as follows:

- To modernize capital requirements while ensuring that institutions continue to hold sufficient regulatory capital to fulfill their mission as a government-sponsored enterprise.
- To ensure that the System's capital requirements are comparable to the Basel III framework and the standardized approach that the federal banking regulatory agencies have adopted, but also to ensure that the rules recognize the cooperative structure and the organization of the System.
- To make System regulatory capital requirements more transparent.
- To meet the requirements of section 939A of the Dodd-Frank Wall Street Reform and Consumer Protection Act (Dodd-Frank Act).

For the nine months ended September 30, 2014, the FCA took no enforcement action against the Association.

On February 1, 2012 the FCA issued a letter of special supervision requiring the Association to address several concerns relative to credit quality and risk identification and mitigation. Effective October 15, 2014 the FCA has rescinded the letter of special supervision acknowledging the Association has address all concerns noted in the special supervision letter, and the Association is now under normal supervision status.

**NOTE**:  Shareholder investment in the Association is materially affected by the financial condition and results of operations of AgFirst Farm Credit Bank.  Copies of AgFirst's annual and quarterly reports are available upon request free of charge by calling 1-800-845-1745, ext. 2832, or writing Susanne Caughman, AgFirst Farm Credit Bank, P.O. Box 1499, Columbia SC 29202.  Information concerning AgFirst Farm Credit Bank can also be obtained at their website, *www.agfirst.com*.  Copies of the Association's annual and quarterly reports are also available upon request free of charge by calling 478-987-8300 Ext. 120, writing Carrie McCall, Chief Financial Officer, AgGeorgia Farm Credit, ACA, P.O. Box 1820, Perry, GA 31069, or accessing the website, *www.aggeorgia.com*.  The Association prepares a quarterly report within 40 days after the end of each fiscal quarter, except that no report need be prepared for the fiscal quarter that coincides with the end of the fiscal year of the institution.

# AgGeorgia Farm Credit, ACA

# Consolidated Balance Sheets

| *(dollars in thousands)* | September 30, 2014 | December 31, 2013 |
|---|---|---|
| | *(unaudited)* | *(audited)* |
| **Assets** | | |
| Cash | $ 109 | $ 1,304 |
| Loans | 878,070 | 840,992 |
| Allowance for loan losses | (6,963) | (10,575) |
| Net loans | 871,107 | 830,417 |
| Accrued interest receivable | 11,863 | 10,920 |
| Investments in other Farm Credit institutions | 11,522 | 13,474 |
| Premises and equipment, net | 7,423 | 7,619 |
| Other property owned | 10,918 | 7,345 |
| Accounts receivable | 4,862 | 16,028 |
| Other assets | 6,504 | 9,607 |
| Total assets | $ 924,308 | $ 896,714 |
| **Liabilities** | | |
| Notes payable to AgFirst Farm Credit Bank | $ 690,454 | $ 661,719 |
| Accrued interest payable | 1,289 | 1,412 |
| Patronage refunds payable | 461 | 2,921 |
| Accounts payable | 981 | 984 |
| Other liabilities | 11,727 | 13,772 |
| Total liabilities | 704,912 | 680,808 |
| Commitments and contingencies | | |
| **Members' Equity** | | |
| Protected borrower stock | 5 | 8 |
| Capital stock and participation certificates | 3,770 | 3,744 |
| Retained earnings | | |
| Allocated | 86,221 | 94,741 |
| Unallocated | 129,473 | 117,487 |
| Accumulated other comprehensive income (loss) | (73) | (74) |
| Total members' equity | 219,396 | 215,906 |
| Total liabilities and members' equity | $ 924,308 | $ 896,714 |

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

# AgGeorgia Farm Credit, ACA

# Consolidated Statements of Income

*(unaudited)*

| *(dollars in thousands)* | For the three months ended September 30, 2014 | For the three months ended September 30, 2013 | For the nine months ended September 30, 2014 | For the nine months ended September 30, 2013 |
|---|---|---|---|---|
| **Interest Income** | | | | |
| Loans | $ 11,641 | $ 12,880 | $ 33,874 | $ 37,472 |
| **Interest Expense** | | | | |
| Notes payable to AgFirst Farm Credit Bank | 3,913 | 4,466 | 11,123 | 13,486 |
| Net interest income | 7,728 | 8,414 | 22,751 | 23,986 |
| Provision for (reversal of allowance for) loan losses | (561) | 125 | 64 | 835 |
| Net interest income after provision for (reversal of allowance for) loan losses | 8,289 | 8,289 | 22,687 | 23,151 |
| **Noninterest Income** | | | | |
| Loan fees | 161 | 144 | 685 | 705 |
| Fees for financially related services | 4 | 10 | 16 | 16 |
| Patronage refunds from other Farm Credit institutions | 1,409 | 1,641 | 4,620 | 5,267 |
| Gains (losses) on sales of premises and equipment, net | 39 | 44 | 62 | 95 |
| Gains (losses) on other transactions | 4 | 7 | 14 | 24 |
| Other noninterest income | 2 | 1 | 147 | 550 |
| Total noninterest income | 1,619 | 1,847 | 5,544 | 6,657 |
| **Noninterest Expense** | | | | |
| Salaries and employee benefits | 3,759 | 3,634 | 11,402 | 11,155 |
| Occupancy and equipment | 296 | 281 | 769 | 762 |
| Insurance Fund premiums | 205 | 189 | 584 | 559 |
| (Gains) losses on other property owned, net | 14 | (1,163) | (29) | 480 |
| Other operating expenses | 1,105 | 907 | 3,339 | 2,842 |
| Total noninterest expense | 5,379 | 3,848 | 16,065 | 15,798 |
| Income before income taxes | 4,529 | 6,288 | 12,166 | 14,010 |
| Provision for income taxes | 32 | 2 | 49 | 6 |
| Net income | $ 4,497 | $ 6,286 | $ 12,117 | $ 14,004 |

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

## AgGeorgia Farm Credit, ACA

# Consolidated Statements of Comprehensive Income

*(unaudited)*

| *(dollars in thousands)* | For the three months ended September 30, 2014 | For the three months ended September 30, 2013 | For the nine months ended September 30, 2014 | For the nine months ended September 30, 2013 |
|---|---|---|---|---|
| Net income | $ 4,497 | $ 6,286 | $ 12,117 | $ 14,004 |
| **Other comprehensive income net of tax** | | | | |
| Employee benefit plans adjustments | — | 1 | 1 | 2 |
| Comprehensive income | $ 4,497 | $ 6,287 | $ 12,118 | $ 14,006 |

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

AgGeorgia Farm Credit, ACA

# Consolidated Statements of Changes in Members' Equity

*(unaudited)*

| *(dollars in thousands)* | Protected Borrower Stock | Capital Stock and Participation Certificates | Retained Earnings Allocated | Retained Earnings Unallocated | Accumulated Other Comprehensive Income (Loss) | Total Members' Equity |
|---|---|---|---|---|---|---|
| Balance at December 31, 2012 | $ 33 | $ 3,889 | $ 89,580 | $ 107,979 | $ (106) | $ 201,375 |
| Comprehensive income | | | | 14,004 | 2 | 14,006 |
| Protected borrower stock issued/(retired), net | (25) | | | | | (25) |
| Capital stock/participation certificates issued/(retired), net | | (145) | | | | (145) |
| Retained earnings retired | | | (1,542) | | | (1,542) |
| Patronage distribution adjustment | | | 707 | (741) | | (34) |
| Balance at September 30, 2013 | $ 8 | $ 3,744 | $ 88,745 | $ 121,242 | $ (104) | $ 213,635 |
| Balance at December 31, 2013 | $ 8 | $ 3,744 | $ 94,741 | $ 117,487 | $ (74) | $ 215,906 |
| Comprehensive income | | | | 12,117 | 1 | 12,118 |
| Protected borrower stock issued/(retired), net | (3) | | | | | (3) |
| Capital stock/participation certificates issued/(retired), net | | 26 | | | | 26 |
| Retained earnings retired | | | (8,607) | | | (8,607) |
| Patronage distribution adjustment | | | 87 | (131) | | (44) |
| Balance at September 30, 2014 | $ 5 | $ 3,770 | $ 86,221 | $ 129,473 | $ (73) | $ 219,396 |

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

# AgGeorgia Farm Credit, ACA

# Notes to the Consolidated Financial Statements

*(dollars in thousands, except as noted)*
*(unaudited)*

**Note 1 — Organization, Significant Accounting Policies, and Recently Issued Accounting Pronouncements**

**Organization**

The accompanying financial statements include the accounts of AgGeorgia Farm Credit, ACA (the Association). A description of the organization and operations, the significant accounting policies followed, and the financial condition and results of operations for the Association as of and for the year ended December 31, 2013, are contained in the 2013 Annual Report to Shareholders. These unaudited interim consolidated financial statements should be read in conjunction with the latest Annual Report to Shareholders.

**Basis of Presentation**

In the opinion of management, 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 (GAAP) and prevailing practices within the banking industry.

Certain amounts in the prior period's consolidated financial statements may have been reclassified to conform to the current period presentation. Such reclassifications had no effect on the prior period net income or total capital as previously reported.

The results of any interim period are not necessarily indicative of the results to be expected for a full year.

**Significant Accounting Policies**

The Association maintains an allowance for loan losses at a level considered adequate by management to provide for probable and estimable losses inherent in the loan portfolio as of the report date. The allowance for loan losses is increased through provisions for loan losses and loan recoveries and is decreased through loan charge-offs and allowance reversals. A review of individual loans in each respective portfolio is performed periodically to determine the appropriateness of risk ratings and to ensure loss exposure to the Association has been identified.

**Recently Issued Accounting Pronouncements**

In August 2014, the Financial Accounting Standards Board (FASB) issued Accounting Standards Update (ASU) 2014-15, "Presentation of Financial Statements—Going Concern (Subtopic 205-40): Disclosure of Uncertainties about an Entity's Ability to Continue as a Going Concern." The Update is intended to define management's responsibility to evaluate whether there is substantial doubt about an organization's ability to continue as a going concern and to provide related footnote disclosures. Under Generally Accepted Accounting Principles (GAAP), financial statements are prepared under the presumption that the reporting organization will continue to operate as a going concern, except in limited circumstances. Financial reporting under this presumption is commonly referred to as the going concern basis of accounting. The going concern basis of accounting is critical to financial reporting because it establishes the fundamental basis for measuring and classifying assets and liabilities. Currently, GAAP lacks guidance about management's responsibility to evaluate whether there is substantial doubt about the organization's ability to continue as a going concern or to provide related footnote disclosures. The Update provides guidance to an organization's management, with principles and definitions that are intended to reduce diversity in the timing and content of disclosures that are commonly provided by organizations today in the financial statement footnotes. The amendments in this Update apply to all companies and not-for-profit organizations and become effective in the annual period ending after December 15, 2016, with early application permitted.

In August 2014, the FASB issued ASU 2014-14, "Receivables—Troubled Debt Restructurings by Creditors (Subtopic 310-40): Classification of Certain Government-Guaranteed Mortgage Loans upon Foreclosure." Currently, there is diversity in practice related to how creditors classify certain government-guaranteed mortgage loans upon foreclosure. The amendments in this Update require that a mortgage loan be derecognized and that a separate other receivable be recognized upon foreclosure if the following conditions are met: 1. The loan has a government guarantee that is not separable from the loan before foreclosure; 2. At the time of foreclosure, the creditor has the intent to convey the real estate property to the guarantor and make a claim on the guarantee, and the creditor has the ability to recover under that claim; 3. At the time of foreclosure, any amount of the claim that is determined on the basis of the fair value of the real estate is fixed. Upon foreclosure, the separate other receivable should be measured based on the amount of the loan balance (principal and interest) expected to be recovered from the guarantor. The amendments in this Update are effective for public business entities for annual periods, and interim periods within those annual periods, beginning after December 15, 2014. For all other entities, the amendments in this Update are effective for annual periods ending after December 15, 2015, and interim periods beginning after December 15, 2015.

In June 2014, the FASB issued ASU 2014-11, “Transfers and Servicing (Topic 860): Repurchase-to-Maturity Transactions, Repurchase Financings, and Disclosures,” which changes the accounting for repurchase-to-maturity transactions and repurchase financing arrangements. It also requires enhanced disclosures about repurchase agreements and other similar transactions. The new guidance aligns the accounting for repurchase-to-maturity transactions and repurchase agreements executed as a repurchase financing with the accounting for other typical repurchase agreements such that, these transactions would all be accounted for as secured borrowings. The accounting changes in this Update are effective for public companies for the first interim or annual period beginning after December 15, 2014. In addition, for public companies, the disclosure for certain transactions accounted for as a sale is effective for the first interim or annual period beginning on or after December 15, 2014, and the disclosure for transactions accounted for as secured borrowings is required to be presented for annual periods beginning after December 15, 2014, and interim periods beginning after March 15, 2015. For all other entities, all changes are effective for annual periods beginning after December 15, 2014, and interim periods beginning after December 15, 2015. Earlier application for a public company is prohibited, but all other companies and organizations may elect to apply the requirements for interim periods beginning after December 15, 2014.

In May 2014, the FASB, responsible for U.S. Generally Accepted Accounting Principles (U.S. GAAP), and the International Accounting Standards Board (IASB), responsible for International Financial Reporting Standards (IFRS), jointly issued converged standards on the recognition of revenue from contracts with customers. ASU 2014-09, “Revenue from Contracts with Customers (Topic 606)” and IFRS 15 “Revenue from Contracts with Customers” are intended to improve the financial reporting of revenue and comparability of the top line in financial statements globally and supersede substantially all previous revenue recognition guidance. The core principle of the new standards is for companies to recognize revenue to depict the transfer of goods or services to customers in amounts that reflect the consideration (that is, payment) to which the company expects to be entitled in exchange for those goods or services. The new standard also will result in enhanced disclosures about revenue, provide guidance for transactions that were not previously addressed comprehensively (for example, service revenue and contract modifications) and improve guidance for multiple-element arrangements. Because of the pervasive nature of the new guidance, the boards have established a joint transition resource group in order to aid transition to the new standard. For public entities reporting under U.S. GAAP, the amendments in the Update are effective for annual reporting periods beginning after December 15, 2016, including interim periods within that reporting period. Early application is not permitted. For nonpublic entities, the amendments are effective for annual reporting periods beginning after December 15, 2017, and interim periods within annual periods beginning after December 15, 2018. A nonpublic entity may elect to adopt this guidance earlier under certain circumstances. The amendments are to be applied retrospectively. The Association has identified ancillary revenues that will be subject to this guidance. However, because financial instruments are not within the scope of the guidance, it is expected that adoption will not have a material impact on the Association’s financial condition or results of operations, but may result in additional disclosures.

In April 2014, the FASB issued ASU 2014-08, “Presentation of Financial Statements (Topic 205) and Property, Plant, and Equipment (Topic 360): Reporting Discontinued Operations and Disclosures of Disposals of Components of an Entity.” The amendments in this Update change the requirements for reporting discontinued operations in Subtopic 205-20. A discontinued operation may include a component of an entity or a group of components of an entity, or a business or nonprofit activity. A disposal of a component of an entity or a group of components of an entity is required to be reported in discontinued operations only if the disposal represents a strategic shift that has (or will have) a major effect on an entity’s operations and financial results. A public business entity and a not-for-profit entity that has issued, or is a conduit bond obligor for, securities that are traded, listed, or quoted on an exchange or an over-the-counter market should apply the amendments in this Update prospectively to both of the following: (1) All disposals (or classifications as held for sale) of components of an entity that occur within annual periods beginning on or after December 15, 2014, and interim periods within those years and (2) All businesses or nonprofit activities that, on acquisition, are classified as held for sale that occur within annual periods beginning on or after December 15, 2014, and interim periods within those years.

In March 2014, the FASB issued ASU 2014-06, “Technical Corrections and Improvements Related to Glossary Terms (Master Glossary).” The amendments in this Update relate to glossary terms, cover a wide range of Topics in the Codification and are presented in four sections: Deletion of Master Glossary Terms, Addition of Master Glossary Term Links, Duplicate Master Glossary Terms, and Other Technical Corrections Related to Glossary Terms. These amendments did not have transition guidance and were effective upon issuance for both public entities and nonpublic entities.

In January 2014, the FASB issued ASU 2014-04, “Receivables—Troubled Debt Restructurings by Creditors (Subtopic 310-40) - Reclassification of Residential Real Estate Collateralized Consumer Mortgage Loans upon Foreclosure.” The objective of the amendments in this Update is to reduce diversity by clarifying when an in substance repossession or foreclosure occurs, that is, when a creditor should be considered to have received physical possession of residential real estate property collateralizing a consumer mortgage loan such that the loan receivable should be derecognized and the real estate property recognized. The amendments are effective for public business entities for annual periods, and interim periods within those annual periods, beginning after December 15, 2014. For entities other than public business entities, the amendments in this Update are effective for annual periods beginning after December 15, 2014, and interim periods within annual periods beginning after December 15, 2015. An entity can elect to adopt the amendments in this Update using either a modified retrospective transition method or a prospective transition method. Early adoption is permitted.

Other recently issued accounting pronouncements are discussed in the 2013 Annual Report to Shareholders.

**Note 2 — Loans and Allowance for Loan Losses**

For a complete description of the Association's accounting for loans (including impaired loans and the allowance for loan losses) and definitions of loan types, see the 2013 Annual Report to Shareholders.

Credit risk arises from the potential inability of an obligor to meet its repayment obligation. The Association manages credit risk associated with lending activities through an assessment of the credit risk profile of an individual obligor. The Association sets its own underwriting standards and lending policies that provide direction to loan officers and are approved by the board of directors.

A summary of loans outstanding at period end follows:

| | September 30, 2014 | December 31, 2013 |
|---|---|---|
| Real estate mortgage | $ 413,901 | $ 413,890 |
| Production and intermediate-term | 429,038 | 398,987 |
| Loans to cooperatives | – | 23 |
| Processing and marketing | 17,923 | 12,671 |
| Farm-related business | 5,408 | 4,510 |
| Communication | 3,319 | 2,772 |
| Rural residential real estate | 8,481 | 8,139 |
| Total Loans | $ 878,070 | $ 840,992 |

A substantial portion of the Association's lending activities is collateralized, and exposure to credit loss associated with lending activities is reduced accordingly.

The Association may purchase or sell participation interests with other parties in order to diversify risk, manage loan volume, and comply with Farm Credit Administration (FCA) regulations. The following tables present participation loan balances at periods ended:

| September 30, 2014 | Within AgFirst District | | Within Farm Credit System | | Outside Farm Credit System | | Total | |
|---|---|---|---|---|---|---|---|---|
| | Participations Purchased | Participations Sold | Participations Purchased | Participations Sold | Participations Purchased | Participations Sold | Participations Purchased | Participations Sold |
| Real estate mortgage | $ 1,852 | $ 5,175 | $ – | $ – | $ – | $ – | $ 1,852 | $ 5,175 |
| Production and intermediate-term | 4,137 | 32,079 | – | – | 423 | – | 4,560 | 32,079 |
| Processing and marketing | 11,079 | – | – | – | – | – | 11,079 | – |
| Farm-related business | 2,217 | 267 | – | – | – | – | 2,217 | 267 |
| Communication | 3,318 | – | – | – | – | – | 3,318 | – |
| Total | $ 22,603 | $ 37,521 | $ – | $ – | $ 423 | $ – | $ 23,026 | $ 37,521 |

| December 31, 2013 | Within AgFirst District | | Within Farm Credit System | | Outside Farm Credit System | | Total | |
|---|---|---|---|---|---|---|---|---|
| | Participations Purchased | Participations Sold | Participations Purchased | Participations Sold | Participations Purchased | Participations Sold | Participations Purchased | Participations Sold |
| Real estate mortgage | $ 1,961 | $ 21,026 | $ – | $ – | $ – | $ – | $ 1,961 | $ 21,026 |
| Production and intermediate-term | 5,820 | 9,760 | – | – | 447 | – | 6,267 | 9,760 |
| Processing and marketing | 5,938 | – | – | – | – | – | 5,938 | – |
| Farm-related business | – | 1,500 | – | – | – | – | – | 1,500 |
| Communication | 2,775 | – | – | – | – | – | 2,775 | – |
| Total | $ 16,494 | $ 32,286 | $ – | $ – | $ 447 | $ – | $ 16,941 | $ 32,286 |

A significant source of liquidity for the Association is the repayments and maturities of loans. The following table presents the contractual maturity distribution of loans by loan type at the latest period end:

| | September 30, 2014 | | | |
|---|---|---|---|---|
| | Due less than 1 year | Due 1 Through 5 years | Due after 5 years | Total |
| Real estate mortgage | $ 30,529 | $ 93,929 | $ 289,443 | $ 413,901 |
| Production and intermediate term | 164,455 | 128,647 | 135,936 | 429,038 |
| Processing and marketing | 4,998 | 8,361 | 4,564 | 17,923 |
| Farm-related business | 1,147 | 3,551 | 710 | 5,408 |
| Communication | – | 3,319 | – | 3,319 |
| Rural residential real estate | 480 | 1,632 | 6,369 | 8,481 |
| Total Loans | $ 201,609 | $ 239,439 | $ 437,022 | $ 878,070 |
| Percentage | 22.96% | 27.27% | 49.77% | 100.00% |

The following table shows loans and related accrued interest, classified under the FCA Uniform Loan Classification System, as a percentage of total loans and related accrued interest receivable by loan type as of:

| | September 30, 2014 | December 31, 2013 |
|---|---|---|
| **Real estate mortgage:** | | |
| Acceptable | 89.28% | 86.80% |
| OAEM | 5.08 | 6.13 |
| Substandard/doubtful/loss | 5.64 | 7.07 |
| | 100.00% | 100.00% |
| **Production and intermediate-term:** | | |
| Acceptable | 87.36% | 79.81% |
| OAEM | 6.64 | 10.30 |
| Substandard/doubtful/loss | 6.00 | 9.89 |
| | 100.00% | 100.00% |
| **Loans to cooperatives:** | | |
| Acceptable | –% | 100.00% |
| OAEM | – | – |
| Substandard/doubtful/loss | – | – |
| | –% | 100.00% |
| **Processing and marketing:** | | |
| Acceptable | 92.21% | 95.63% |
| OAEM | 7.79 | 4.37 |
| Substandard/doubtful/loss | – | – |
| | 100.00% | 100.00% |

| | September 30, 2014 | December 31, 2013 |
|---|---|---|
| **Farm-related business:** | | |
| Acceptable | 87.23% | 84.98% |
| OAEM | 12.77 | 14.98 |
| Substandard/doubtful/loss | – | 0.04 |
| | 100.00% | 100.00% |
| **Communication** | | |
| Acceptable | 100.00% | 100.00% |
| OAEM | – | – |
| Substandard/doubtful/loss | – | – |
| | 100.00% | 100.00% |
| **Rural residential real estate:** | | |
| Acceptable | 91.50% | 84.64% |
| OAEM | 5.17 | 12.29 |
| Substandard/doubtful/loss | 3.33 | 3.07 |
| | 100.00% | 100.00% |
| **Total Loans:** | | |
| Acceptable | 88.45% | 83.63% |
| OAEM | 5.93 | 8.17 |
| Substandard/doubtful/loss | 5.62 | 8.20 |
| | 100.00% | 100.00% |

The following tables provide an age analysis of past due loans and related accrued interest as of:

| | September 30, 2014 | | | | | |
|---|---|---|---|---|---|---|
| | 30 Through 89 Days Past Due | 90 Days or More Past Due | Total Past Due | Not Past Due or Less Than 30 Days Past Due | Total Loans | Recorded Investment 90 Days or More Past Due and Accruing Interest |
| Real estate mortgage | $ 694 | $ 3,477 | $ 4,171 | $ 415,495 | $ 419,666 | $ – |
| Production and intermediate-term | 1,742 | 7,459 | 9,201 | 425,677 | 434,878 | – |
| Processing and marketing | 1,408 | – | 1,408 | 16,675 | 18,083 | – |
| Farm-related business | – | – | – | 5,471 | 5,471 | – |
| Communication | – | – | – | 3,322 | 3,322 | – |
| Rural residential real estate | 107 | 62 | 169 | 8,344 | 8,513 | – |
| Total | $ 3,951 | $ 10,998 | $ 14,949 | $ 874,984 | $ 889,933 | $ – |

| | December 31, 2013 | | | | | |
|---|---|---|---|---|---|---|
| | 30 Through 89 Days Past Due | 90 Days or More Past Due | Total Past Due | Not Past Due or Less Than 30 Days Past Due | Total Loans | Recorded Investment 90 Days or More Past Due and Accruing Interest |
| Real estate mortgage | $ 4,821 | $ 6,258 | $ 11,079 | $ 408,363 | $ 419,442 | $ – |
| Production and intermediate-term | 6,728 | 10,878 | 17,606 | 386,516 | 404,122 | – |
| Loans to cooperatives | – | – | – | 23 | 23 | – |
| Processing and marketing | – | – | – | 12,792 | 12,792 | – |
| Farm-related business | – | 2 | 2 | 4,571 | 4,573 | – |
| Communication | – | – | – | 2,775 | 2,775 | – |
| Rural residential real estate | 570 | 79 | 649 | 7,536 | 8,185 | – |
| Total | $ 12,119 | $ 17,217 | $ 29,336 | $ 822,576 | $ 851,912 | $ – |

The recorded investment in a receivable is the face amount increased or decreased by applicable accrued interest, unamortized premium, discount, finance charges, or acquisition costs and may also reflect a previous direct write-down of the investment.

Nonperforming assets (including related accrued interest) and related credit quality statistics at period end were as follows:

| | September 30, 2014 | December 31, 2013 |
|---|---|---|
| **Nonaccrual loans:** | | |
| Real estate mortgage | $ 14,072 | $ 17,314 |
| Production and intermediate-term | 16,467 | 23,630 |
| Farm-related business | – | 2 |
| Rural residential real estate | 98 | 118 |
| Total | $ 30,637 | $ 41,064 |
| **Accruing restructured loans:** | | |
| Real estate mortgage | $ 7,504 | $ 8,201 |
| Production and intermediate-term | 6,896 | 6,084 |
| Rural residential real estate | 130 | – |
| Total | $ 14,530 | $ 14,285 |
| **Accruing loans 90 days or more past due:** | | |
| Total | $ – | $ – |
| Total nonperforming loans | $ 45,167 | $ 55,349 |
| Other property owned | 10,918 | 7,345 |
| Total nonperforming assets | $ 56,085 | $ 62,694 |
| Nonaccrual loans as a percentage of total loans | 3.49% | 4.88% |
| Nonperforming assets as a percentage of total loans and other property owned | 6.31% | 7.39% |
| Nonperforming assets as a percentage of capital | 25.56% | 29.04% |

The following table presents information related to impaired loans (including accrued interest) at period end. Impaired loans are loans for which it is probable that all principal and interest will not be collected according to the contractual terms of the loan.

| | September 30, 2014 | December 31, 2013 |
|---|---|---|
| Impaired nonaccrual loans: | | |
| Current as to principal and interest | $ 17,802 | $ 15,910 |
| Past due | 12,835 | 25,154 |
| Total | 30,637 | 41,064 |
| Impaired accrual loans: | | |
| Restructured | 14,530 | 14,285 |
| Total | 14,530 | 14,285 |
| Total impaired loans | $ 45,167 | $ 55,349 |

The following tables present additional impaired loan information at period end. Unpaid principal balance represents the contractual principal balance of the loan.

| | September 30, 2014 | | | Quarter Ended September 30, 2014 | | Nine Months Ended September 30, 2014 | |
|---|---|---|---|---|---|---|---|
| | Recorded Investment | Unpaid Principal Balance | Related Allowance | Average Impaired Loans | Interest Income Recognized on Impaired Loans | Average Impaired Loans | Interest Income Recognized on Impaired Loans |
| **Impaired loans with a related allowance for credit losses:** | | | | | | | |
| Real estate mortgage | $ 4,923 | $ 5,757 | $ 890 | $ 5,255 | $ 30 | $ 5,644 | $ 96 |
| Production and intermediate-term | 7,950 | 11,255 | 1,320 | 8,486 | 48 | 9,116 | 154 |
| Rural residential real estate | 49 | 60 | 3 | 52 | – | 56 | 1 |
| Total | $ 12,922 | $ 17,072 | $ 2,213 | $ 13,793 | $ 78 | $ 14,816 | $ 251 |
| **Impaired loans with no related allowance for credit losses:** | | | | | | | |
| Real estate mortgage | $ 16,653 | $ 20,480 | $ – | $ 17,775 | $ 100 | $ 19,093 | $ 324 |
| Production and intermediate-term | 15,413 | 18,863 | – | 16,452 | 93 | 17,671 | 300 |
| Rural residential real estate | 179 | 196 | – | 191 | 1 | 205 | 3 |
| Total | $ 32,245 | $ 39,539 | $ – | $ 34,418 | $ 194 | $ 36,969 | $ 627 |
| **Total impaired loans:** | | | | | | | |
| Real estate mortgage | $ 21,576 | $ 26,237 | $ 890 | $ 23,030 | $ 130 | $ 24,737 | $ 420 |
| Production and intermediate-term | 23,363 | 30,118 | 1,320 | 24,938 | 141 | 26,787 | 454 |
| Rural residential real estate | 228 | 256 | 3 | 243 | 1 | 261 | 4 |
| Total | $ 45,167 | $ 56,611 | $ 2,213 | $ 48,211 | $ 272 | $ 51,785 | $ 878 |

| | December 31, 2013 | | | Year Ended December 31, 2013 | |
|---|---|---|---|---|---|
| | Recorded Investment | Unpaid Principal Balance | Related Allowance | Average Impaired Loans | Interest Income Recognized on Impaired Loans |
| **Impaired loans with a related allowance for credit losses:** | | | | | |
| Real estate mortgage | $ 8,308 | $ 9,402 | $ 1,854 | $ 9,745 | $ 288 |
| Production and intermediate-term | 16,500 | 21,166 | 3,409 | 19,355 | 572 |
| Farm-related business | – | – | – | – | – |
| Rural residential real estate | 50 | 60 | 4 | 59 | 2 |
| Total | $ 24,858 | $ 30,628 | $ 5,267 | $ 29,159 | 862 |
| **Impaired loans with no related allowance for credit losses:** | | | | | |
| Real estate mortgage | $ 17,207 | $ 21,285 | $ – | $ 20,184 | $ 597 |
| Production and intermediate-term | 13,214 | 17,013 | – | 15,500 | 458 |
| Farm-related business | 2 | 705 | – | 2 | – |
| Rural residential real estate | 68 | 74 | – | 79 | 2 |
| Total | $ 30,491 | $ 39,077 | $ – | $ 35,765 | 1,057 |
| **Total impaired loans:** | | | | | |
| Real estate mortgage | $ 25,515 | $ 30,687 | $ 1,854 | $ 29,929 | $ 885 |
| Production and intermediate-term | 29,714 | 38,179 | 3,409 | 34,855 | 1,030 |
| Farm-related business | 2 | 705 | – | 2 | – |
| Rural residential real estate | 118 | 134 | 4 | 138 | 4 |
| Total | $ 55,349 | $ 69,705 | $ 5,267 | $ 64,924 | 1,919 |

There were no material commitments to lend additional funds to debtors whose loans were classified as impaired at each reporting period.

A summary of changes in the allowance for loan losses and recorded investment in loans for each reporting period follows:

| | Real Estate Mortgage | Production and Intermediate-term | Agribusiness* | Communication | Rural Residential Real Estate | Total |
|---|---|---|---|---|---|---|
| **Activity related to the allowance for credit losses:** | | | | | | |
| Balance at June 30, 2014 | $ 3,568 | $ 4,904 | $ 114 | $ 4 | $ 31 | $ 8,621 |
| Charge-offs | (1,004) | (502) | – | – | – | (1,506) |
| Recoveries | 66 | 343 | – | – | – | 409 |
| Provision for loan losses | (14) | (566) | 20 | – | (1) | (561) |
| Balance at September 30, 2014 | $ 2,616 | $ 4,179 | $ 134 | $ 4 | $ 30 | $ 6,963 |
| Balance at December 31, 2013 | $ 3,860 | $ 6,579 | $ 101 | $ 4 | $ 31 | $ 10,575 |
| Charge-offs | (1,981) | (2,901) | – | – | (6) | (4,888) |
| Recoveries | 353 | 859 | – | – | – | 1,212 |
| Provision for loan losses | 384 | (358) | 33 | – | 5 | 64 |
| Balance at September 30, 2014 | $ 2,616 | $ 4,179 | $ 134 | $ 4 | $ 30 | $ 6,963 |
| Balance at June 30, 2013 | $ 4,744 | $ 6,063 | $ 200 | $ 4 | $ 27 | $ 11,038 |
| Charge-offs | (855) | (902) | (138) | – | (1) | (1,896) |
| Recoveries | 56 | 89 | 74 | – | – | 219 |
| Provision for loan losses | 26 | 157 | (58) | – | – | 125 |
| Balance at September 30, 2013 | $ 3,971 | $ 5,407 | $ 78 | $ 4 | $ 26 | $ 9,486 |
| Balance at December 31, 2012 | $ 4,589 | $ 5,996 | $ 369 | $ – | $ 22 | $ 10,976 |
| Charge-offs | (1,029) | (1,869) | (293) | – | (5) | (3,196) |
| Recoveries | 496 | 301 | 74 | – | – | 871 |
| Provision for loan losses | (85) | 979 | (72) | 4 | 9 | 835 |
| Balance at September 30, 2013 | $ 3,971 | $ 5,407 | $ 78 | $ 4 | $ 26 | $ 9,486 |
| **Allowance on loans evaluated for impairment:** | | | | | | |
| Individually | $ 890 | $ 1,320 | $ – | $ – | $ 3 | $ 2,213 |
| Collectively | 1,726 | 2,859 | 134 | 4 | 27 | 4,750 |
| Balance at September 30, 2014 | $ 2,616 | $ 4,179 | $ 134 | $ 4 | $ 30 | $ 6,963 |
| Individually | $ 1,854 | $ 3,409 | $ – | $ – | $ 4 | $ 5,267 |
| Collectively | 2,006 | 3,170 | 101 | 4 | 27 | 5,308 |
| Balance at December 31, 2013 | $ 3,860 | $ 6,579 | $ 101 | $ 4 | $ 31 | $ 10,575 |
| **Recorded investment in loans evaluated for impairment:** | | | | | | |
| Individually | $ 20,054 | $ 23,329 | $ – | $ – | $ 227 | $ 43,610 |
| Collectively | 399,612 | 411,549 | 23,554 | 3,322 | 8,286 | 846,323 |
| Balance at September 30, 2014 | $ 419,666 | $ 434,878 | $ 23,554 | $ 3,322 | $ 8,513 | $ 889,933 |
| Individually | $ 23,803 | $ 28,819 | $ 2 | $ – | $ 118 | $ 52,742 |
| Collectively | 395,639 | 375,303 | 17,386 | 2,775 | 8,067 | 799,170 |
| Balance at December 31, 2013 | $ 419,442 | $ 404,122 | $ 17,388 | $ 2,775 | $ 8,185 | $ 851,912 |

**Includes the loan types; Loans to cooperatives, Processing and marketing, and Farm-related business.*

A restructuring of a debt constitutes a troubled debt restructuring (TDR) if the creditor for economic or legal reasons related to the debtor's financial difficulties grants a concession to the debtor that it would not otherwise consider. The following tables present additional information about pre-modification and post-modification outstanding recorded investment and the effects of the modifications that occurred during the periods presented.

| | Three months ended September 30, 2014 | | | | |
|---|---|---|---|---|---|
| | Interest Concessions | Principal Concessions | Other Concessions | Total | Charge-offs |
| **Pre-modification Outstanding Recorded Investment** | | | | | |
| Real estate mortgage | $ – | $ 3,183 | $ – | $ 3,183 | |
| Production and intermediate-term | – | 1,149 | – | 1,149 | |
| Total | $ – | $ 4,332 | $ – | $ 4,332 | |
| **Post-modification Outstanding Recorded Investment** | | | | | |
| Real estate mortgage | $ – | $ 1,842 | $ – | $ 1,842 | $ – |
| Production and intermediate-term | – | 1,149 | – | 1,149 | – |
| Total | $ – | $ 2,991 | $ – | $ 2,991 | $ – |

| | Nine months ended September 30, 2014 | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|
| | Interest Concessions | | Principal Concessions | | Other Concessions | | Total | | Charge-offs |
| **Pre-modification Outstanding Recorded Investment** | | | | | | | | | |
| Real estate mortgage | $ | – | $ | 7,835 | $ | – | $ | 7,835 | |
| Production and intermediate-term | | – | | 7,629 | | – | | 7,629 | |
| Total | $ | – | $ | 15,464 | $ | – | $ | 15,464 | |
| **Post-modification Outstanding Recorded Investment** | | | | | | | | | |
| Real estate mortgage | $ | – | $ | 6,292 | $ | – | $ | 6,292 | $ – |
| Production and intermediate-term | | – | | 6,647 | | – | | 6,647 | (1) |
| Total | $ | – | $ | 12,939 | $ | – | $ | 12,939 | $ (1) |

| | Three months ended September 30, 2013 | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|
| | Interest Concessions | | Principal Concessions | | Other Concessions | | Total | | Charge-offs |
| **Pre-modification Outstanding Recorded Investment** | | | | | | | | | |
| Real estate mortgage | $ | – | $ | 507 | $ | – | $ | 507 | |
| Production and intermediate-term | | – | | 2,891 | | – | | 2,891 | |
| Total | $ | – | $ | 3,398 | $ | – | $ | 3,398 | |
| **Post-modification Outstanding Recorded Investment** | | | | | | | | | |
| Real estate mortgage | $ | – | $ | 534 | $ | – | $ | 534 | $ – |
| Production and intermediate-term | | – | | 2,936 | | – | | 2,936 | – |
| Total | $ | – | $ | 3,470 | $ | – | $ | 3,470 | $ – |

| | Nine months ended September 30, 2013 | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|
| | Interest Concessions | | Principal Concessions | | Other Concessions | | Total | | Charge-offs |
| **Pre-modification Outstanding Recorded Investment** | | | | | | | | | |
| Real estate mortgage | $ | – | $ | 9,033 | $ | – | $ | 9,033 | |
| Production and intermediate-term | | – | | 7,079 | | – | | 7,079 | |
| Total | $ | – | $ | 16,112 | $ | – | $ | 16,112 | |
| **Post-modification Outstanding Recorded Investment** | | | | | | | | | |
| Real estate mortgage | $ | – | $ | 9,169 | $ | – | $ | 9,169 | $ – |
| Production and intermediate-term | | – | | 7,208 | | – | | 7,208 | (4) |
| Total | $ | – | $ | 16,377 | $ | – | $ | 16,377 | $ (4) |

Interest concessions may include interest forgiveness and interest deferment. Principal concessions may include principal forgiveness, principal deferment, and maturity extension. Other concessions may include additional compensation received which might be in the form of cash or other assets.

The following table presents outstanding recorded investment for TDRs that occurred during the previous twelve months and for which there was a subsequent payment default during the period. Payment default is defined as a payment that was thirty days or more past due.

| | Three Months Ended September 30, | | | | Nine Months Ended September 30, | | | |
|---|---|---|---|---|---|---|---|---|
| | 2014 | | 2013 | | 2014 | | 2013 | |
| Real estate mortgage | $ | 144 | $ | – | $ | 144 | $ | 699 |
| Production and intermediate-term | | 93 | | 2,347 | | 272 | | 4,865 |
| Total | $ | 237 | $ | 2,347 | $ | 416 | $ | 5,564 |

The following table provides information at period end on outstanding loans restructured in troubled debt restructurings. These loans are included as impaired loans in the impaired loan table:

| | Total TDRs | | Nonaccrual TDRs | |
|---|---|---|---|---|
| | September 30, 2014 | December 31, 2013 | September 30, 2014 | December 31, 2013 |
| Real estate mortgage | $ 17,161 | $ 15,885 | $ 9,657 | $ 7,684 |
| Production and intermediate-term | 15,144 | 14,163 | 8,248 | 8,079 |
| Rural residential real estate | 161 | 39 | 31 | 39 |
| Total Loans | $ 32,466 | $ 30,087 | $ 17,936 | $ 15,802 |
| Additional commitments to lend | $ – | $ 5 | | |

## Note 3 — Investments

***Investments in other Farm Credit Institutions***

The Association is required to maintain ownership in the Bank of Class B and Class C stock as determined by the Bank. The Bank may require additional capital contributions to maintain its capital requirements. The Association owns 4.26 percent of the issued stock of the Bank as of September 30, 2014 net of any reciprocal investment. As of that date, the Bank's assets totaled $29.0 billion and shareholders' equity totaled $2.4 billion. The Bank's earnings were $282 million for the first nine months of 2014. In addition, the Association has an investment of $889 related to other Farm Credit institutions.

## Note 4 — Debt

***Notes Payable to AgFirst Farm Credit Bank***

The Association's indebtedness to AgFirst Farm Credit Bank (AgFirst or the Bank) represents borrowings by the Association primarily to fund its loan portfolio. This indebtedness is collateralized by a pledge of substantially all of the Association's assets. The contractual terms of the revolving line of credit are contained in the General Financing Agreement (GFA). The GFA also defines Association performance criteria for borrowing from the Bank, which includes borrowing base margin, earnings and capital covenants, among others.

## Note 5 — Members' Equity

***Accumulated other Comprehensive Income (AOCI)***

The following tables present activity related to AOCI for the periods presented:

**Changes in Accumulated Other Comprehensive income by Component** *(a)*

| | Three Months Ended September 30, | | Nine Months Ended September 30, | |
|---|---|---|---|---|
| | 2014 | 2013 | 2014 | 2013 |
| **Employee Benefit Plans:** | | | | |
| Balance at beginning of period | $ (73) | $ (105) | $ (74) | $ (106) |
| Other comprehensive income before reclassifications | – | – | – | – |
| Amounts reclassified from AOCI | – | 1 | 1 | 2 |
| Net current period other comprehensive income | – | 1 | 1 | 2 |
| Balance at end of period | $ (73) | $ (104) | $ (73) | $ (104) |

**Reclassifications Out of Accumulated Other Comprehensive Income** *(b)*

| | For the three months ended September 30, | | For the nine months ended September 30, | | |
|---|---|---|---|---|---|
| | 2014 | 2013 | 2014 | 2013 | Income Statement Line Item |
| **Defined Benefit Pension Plans:** | | | | | |
| Periodic pension costs | $ – | $ (1) | $ (1) | $ (2) | See Note 7. |
| Net amounts reclassified | $ – | $ (1) | $ (1) | $ (2) | |

*(a) Amounts in parentheses indicate debits to AOCI.*
*(b) Amounts in parentheses indicate debits to profit/loss.*

## Note 6 — Fair Value Measurement

Fair value is defined as the exchange price that would be received for an asset or paid to transfer a liability in an orderly transaction between market participants in the principal or most advantageous market for the asset or liability.

Accounting guidance establishes a hierarchy for disclosure of fair value measurements to maximize the use of observable inputs, that is, inputs that reflect the assumptions market participants would use in pricing an asset or liability based on market data obtained from sources independent of the reporting entity. The hierarchy is based upon the transparency of inputs to the valuation of an asset or liability as of the measurement date. A financial instrument's categorization within the hierarchy tiers is based upon the lowest level of input that is significant to the fair value measurement.

Estimating the fair value of the Association's investment in the Bank and Other Farm Credit Institutions is not practicable because the stock is not traded. The net investment is a requirement of borrowing from the Bank and is carried at cost plus allocated equities in the accompanying Consolidated Balance Sheets.

The classifications within the fair value hierarchy are as follows:

Level 1 inputs to the valuation methodology are unadjusted quoted prices for identical assets or liabilities in active markets.

Level 2 inputs include quoted prices for similar assets and liabilities in active markets; quoted prices in markets that are not active; and inputs that are observable, or can be corroborated, for substantially the full term of the asset or liability.

Level 3 inputs are unobservable and supported by little or no market activity. Valuation is determined using pricing models, discounted cash flow methodologies, or similar techniques, and could include significant management judgment or estimation. Level 3 assets and liabilities also could include instruments whose price has been adjusted based on dealer quoted pricing that is different than the third-party valuation or internal model pricing.

For a complete discussion of the inputs and other assumptions considered in assigning various assets and liabilities to the fair value hierarchy levels, see the latest Annual Report to Shareholders.

There were no Level 3 assets and liabilities measured at fair value on a recurring basis for the periods presented. The Association had no transfers of assets or liabilities into or out of Level 1 or Level 2 during the periods presented.

**SENSITIVITY TO CHANGES IN SIGNIFICANT UNOBSERVABLE INPUTS**

Discounted cash flow or similar modeling techniques are generally used to determine the recurring fair value measurements for Level 3 assets and liabilities. Use of these techniques requires determination of relevant inputs and assumptions, some of which represent significant unobservable inputs as indicated in the tables that follow. Accordingly, changes in these unobservable inputs may have a significant impact on fair value.

Certain of these unobservable inputs will (in isolation) have a directionally consistent impact on the fair value of the instrument for a given change in that input. Alternatively, the fair value of the instrument may move in an opposite direction for a given change in another input. Where multiple inputs are used within the valuation technique of an asset or liability, a change in one input in a certain direction may be offset by an opposite change in another input having a potentially muted impact to the overall fair value of that particular instrument. Additionally, a change in one unobservable input may result in a change to another unobservable input (that is, changes in certain inputs are interrelated with one another), which may counteract or magnify the fair value impact.

**Inputs to Valuation Techniques**

Management determines the Association's valuation policies and procedures. The Bank performs the majority of the Association's valuations, and its valuation processes are calibrated annually by an independent consultant. The fair value measurements are analyzed on a quarterly basis. For other valuations, documentation is obtained for third party information, such as pricing, and periodically evaluated alongside internal information and pricing that is available.

Quoted market prices are generally not available for the instruments presented below. Accordingly fair values are based on judgments regarding anticipated cash flows, future expected loss experience, current economic conditions, risk characteristics of various financial instruments, and other factors. These estimates involve uncertainties and matters of judgment, and therefore cannot be determined with precision. Changes in assumptions could significantly affect the estimates.

**Quantitative Information about Recurring and Nonrecurring Level 3 Fair Value Measurements**

| | Fair Value | Valuation Technique(s) | Unobservable Input | Range |
|---|---|---|---|---|
| Impaired loans and other property owned | $ 55,076 | Appraisal | Income and expense | * |
| | | | Comparable sales | * |
| | | | Replacement cost | * |
| | | | Comparability adjustments | * |

** Ranges for this type of input are not useful because each collateral property is unique.*

**Information about Other Financial Instrument Fair Value Measurements**

| | Valuation Technique(s) | Input |
|---|---|---|
| Cash | Carrying Value | Par/Principal and appropriate interest yield |
| Loans | Discounted cash flow | Prepayment forecasts<br>Probability of default<br>Loss severity |
| Notes payable to AgFirst Farm Credit Bank | Discounted cash flow | Prepayment forecasts<br>Probability of default<br>Loss severity |

The following tables present the carrying amounts and fair values of assets and liabilities that are measured at fair value on a recurring and nonrecurring basis, as well as those financial instruments not measured at fair value, for each of the hierarchy levels at the period ended:

**At or for the Nine Months Ended September 30, 2014**

| | Total Carrying Amount | Level 1 | Level 2 | Level 3 | Total Fair Value | Fair Value Effects On Earnings |
|---|---|---|---|---|---|---|
| **Recurring Measurements** | | | | | | |
| **Assets:** | | | | | | |
| Assets held in Trust funds | $ 240 | $ 240 | $ – | $ – | $ 240 | |
| Recurring Assets | $ 240 | $ 240 | $ – | $ – | $ 240 | |
| **Liabilities:** | | | | | | |
| Recurring Liabilities | $ – | $ – | $ – | $ – | $ – | |
| **Nonrecurring Measurements** | | | | | | |
| **Assets:** | | | | | | |
| Impaired loans | $ 42,954 | $ – | $ – | $ 42,954 | $ 42,954 | $ (622) |
| Other property owned | 10,918 | – | – | 12,122 | 12,122 | 393 |
| Nonrecurring Assets | $ 53,872 | $ – | $ – | $ 55,076 | $ 55,076 | $ (229) |
| **Other Financial Instruments** | | | | | | |
| **Assets:** | | | | | | |
| Cash | $ 109 | $ 109 | $ – | $ – | $ 109 | |
| Loans | 828,153 | – | – | 829,914 | 829,914 | |
| Other Financial Assets | $ 828,262 | $ 109 | $ – | $ 829,914 | $ 830,023 | |
| **Liabilities:** | | | | | | |
| Notes payable to AgFirst Farm Credit Bank | $ 690,454 | $ – | $ – | $ 686,165 | $ 686,165 | |
| Other Financial Liabilities | $ 690,454 | $ – | $ – | $ 686,165 | $ 686,165 | |

**At or for the Year Ended December 31, 2013**

| | Total Carrying Amount | Level 1 | Level 2 | Level 3 | Total Fair Value | Fair Value Effects On Earnings |
|---|---|---|---|---|---|---|
| **Recurring Measurements** | | | | | | |
| **Assets:** | | | | | | |
| Assets held in Trust funds | $ 259 | $ 259 | $ – | $ – | $ 259 | |
| Recurring Assets | $ 259 | $ 259 | $ – | $ – | $ 259 | |
| **Liabilities:** | | | | | | |
| Recurring Liabilities | $ – | $ – | $ – | $ – | $ – | |
| **Nonrecurring Measurements** | | | | | | |
| **Assets:** | | | | | | |
| Impaired loans | $ 50,082 | $ – | $ – | $ 50,082 | $ 50,082 | $ (3,951) |
| Other property owned | 7,345 | – | – | 8,150 | 8,150 | (4,578) |
| Nonrecurring Assets | $ 57,427 | $ – | $ – | $ 58,232 | $ 58,232 | $ (8,529) |
| **Other Financial Instruments** | | | | | | |
| **Assets:** | | | | | | |
| Cash | $ 1,304 | $ 1,304 | $ – | $ – | $ 1,304 | |
| Loans | 780,335 | – | – | 782,802 | 782,802 | |
| Other Financial Assets | $ 781,639 | $ 1,304 | $ – | $ 782,802 | $ 784,106 | |
| **Liabilities:** | | | | | | |
| Notes payable to AgFirst Farm Credit Bank | $ 661,719 | $ – | $ – | $ 658,008 | $ 658,008 | |
| Other Financial Liabilities | $ 661,719 | $ – | $ – | $ 658,008 | $ 658,008 | |

## Note 7 — Employee Benefit Plans

The following is a table of retirement and other postretirement benefit expenses for the Association:

| | For the three months ended September 30, | | For the nine months ended September 30, | |
|---|---|---|---|---|
| | 2014 | 2013 | 2014 | 2013 |
| Pension | $ 1,090 | $ 1,078 | $ 3,270 | $ 3,233 |
| 401(k) | 78 | 69 | 242 | 213 |
| Other postretirement benefits | 167 | 161 | 500 | 482 |
| Total | $ 1,335 | $ 1,308 | $ 4,012 | $ 3,928 |

The following is a table of retirement and other postretirement benefit contributions for the Association:

| | Actual YTD Through 9/30/14 | Projected Contributions For Remainder of 2014 | Projected Total Contributions 2014 |
|---|---|---|---|
| Pension | $ 36 | $ 3,380 | $ 3,416 |
| Other postretirement benefits | 436 | 164 | 600 |
| Total | $ 472 | $ 3,544 | $ 4,016 |

Contributions in the above table include allocated estimates of funding for multi-employer plans in which the Association participates. These amounts may change when a total funding amount and allocation is determined by the respective Plan's Sponsor Committee. Also, market conditions could impact discount rates and return on plan assets which could change contributions necessary before the next plan measurement date of December 31, 2014.

Further details regarding employee benefit plans are contained in the 2013 Annual Report to Shareholders.

In May 2014, the AgFirst Plan Sponsor Committee voted to approve changes to certain employee benefit plans as follows:

(1) On January 1, 2015, the AgFirst Farm Credit Cash Balance Retirement Plan (Cash Balance Plan) will be frozen, employer contributions will cease, and the Cash Balance Plan will be closed to new entrants.
(2) In lieu of participation in and contributions to the Cash Balance Plan, additional employer contributions will be made to the Farm Credit Benefits Alliance 401(k) Plan.

The above changes are expected to become officially executed plan amendments in November 2014. The Cash Balance Plan will not be terminated on January 1, 2015, but is expected to be terminated in 2015 or 2016 once all necessary actions have been performed and approvals obtained. Participants in the Cash Balance Plan will continue to receive employer contributions to their hypothetical cash balance accounts through the end of 2014, at which time contributions will cease. Participants will continue receiving interest credits on the same basis as currently being provided until the Cash Balance Plan is terminated. Participants who are not already fully vested in their accounts will automatically become 100 percent vested on December 31, 2014. Following the termination of the Cash Balance Plan, vested benefits will be distributed to participants.

Beginning on January 1, 2015, for participants in the Cash Balance Plan and eligible employees hired on or after this date, an additional employer contribution will be made to the Farm Credit Benefits Alliance 401(k) Plan equal to 3 percent of the participants' eligible compensation.

Accounting related to the curtailment of future benefit service under the Cash Balance Plan, as prescribed in ASC 715 "Compensation – Retirement Benefits", is expected to be triggered in November 2014 when the plan amendments are officially executed. This accounting is not expected to have a material impact on the Association's financial condition or results of operations.

## Note 8 — Commitments and Contingent Liabilities

From time to time, legal actions are pending against the Association in which claims for money damages are asserted. On at least a quarterly basis, the Association assesses its liabilities and contingencies in connection with outstanding legal proceedings utilizing the latest information available. While the outcome of legal proceedings is inherently uncertain, on the basis of information presently available, management, after consultation with legal counsel, is of the opinion that the ultimate liability, if any, from these actions, would not be material in relation to the financial position of the Association. Because it is not probable that the Association will incur a loss or the loss is not estimable, no liability has been recorded for any claims that may be pending.

## Note 9 — Subsequent Events

The Association has evaluated subsequent events and has determined that, except as described below, there are none requiring disclosure through November 7, 2014, which is the date the financial statements were issued.

On October 20, 2014, AgFirst's Board of Directors declared a special patronage distribution to be paid on January 1, 2015. The Association will receive approximately $7,884 which will be recorded in October 2014 as patronage refunds from other Farm Credit institutions.