Puerto Rico Farm Credit, ACA

SECOND QUARTER 2014

TABLE OF CONTENTS

CERTIFICATION

The undersigned certify that we have reviewed the June 30, 2014 quarterly report of Puerto Rico 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.

Pablo A. Rodríguez
Chairman of Board of Directors

Ricardo L. Fernández
Chief Executive Officer

Antonio Marichal
Member of Board of Directors
Chairman of the Audit Committee

Johana Quiñones
Director of Finance, Risk
Management and Internal Control

August 7, 2014

Puerto Rico 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 June 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 June 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 June 30, 2014.

Ricardo L. Fernández
Chief Executive Officer

Johana Quiñones
Director of Finance
Risk Management and Internal Control

August 7, 2014

Puerto Rico Farm Credit, ACA

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

(dollars in thousands)

The following commentary reviews the consolidated financial condition and results of operations of Puerto Rico Farm Credit, ACA (Association) for the six months ended June 30, 2014. These comments should be read in conjunction with the accompanying consolidated financial statements, notes to the consolidated financial statements, and the 2013 annual report of the Association. The accompanying consolidated financial statements were prepared under the oversight of the Audit Committee of the Board of Directors.

LOAN PORTFOLIO

The Association provides funds to farmers, rural homeowners, and farm-related businesses for financing short and intermediate-term loans and long-term real estate mortgage loans. The Association also maintains a portfolio of purchased loans, originated by other Farm Credit System entities and non-system entities. The Association's predominant chartered territory agricultural commodities were dairy, fruits, rural home and field crops which totaled approximately $98,000 or 57.36 percent of the gross principal balance, net of sold loans, at June 30, 2014.

The outstanding loan volume of the Association at June 30, 2014 was $164,495 for an increase of $2,654 or 1.64 percent as compared to $161,841 at December 31, 2013. Loans originated within the Association's chartered territory were higher by approximately $11, while participation loans purchased increased by approximately $2,643.

Net loans outstanding at June 30, 2014 totaled $161,301 as compared to $158,713 at December 31, 2013. Net loans made up 96.45 percent of total assets at June 30, 2014, as compared to 94.26 percent at December 31, 2013.

As a percentage of outstanding loans, non-accrual loans totaled 6.15 percent at June 30, 2014, compared with 7.98 percent at December 31, 2013. The decrease in the percentage of non-accrual loan volume during the first six months of 2014 was primarily the result of four dairy loans reinstated to accrual status for a total decrease of $2,663 on the non-accrual volume. Management expects that other non-accrual loans be reinstated to accrual status during the rest of the year.

The overall delinquency rate for the chartered territory accruing loan portfolio has remained stable, as a result of good credit administration practices and a low interest rate environment. Management continues to monitor the credit quality of certain chartered territory loans through 2014. The portfolio credit quality has improved during 2014; and is expected to continue this trend during the rest of the year as the portfolio increases and troubled loans are resolved.

The allowance for loan losses resulted in a minor increase to $3,194 at June 30, 2014, from $3,128 at December 31, 2013. The increase was primarily due to an increase in the loan volume evaluated partially offset by a decrease on the general specific reserve for the poultry industry in the participation loans portfolio. Management will continue to monitor certain risks, such as collateral risk and other factors that may increase the risk of the portfolio, such as climate conditions, government fiscal policy and overall economic conditions in the island. It may decide to increase the allowance in 2014. The total allowance for loan losses to outstanding loan volume ratio increased to 1.94 percent at June 30, 2014 from 1.93 percent at December 31, 2013.

During the first six months of 2014, charge-offs recognized totaled $254, mainly due to a $242 charge-off recognized on a nonaccrual chartered territory loan that is expected to be transferred to OPO during the third quarter. The Association is actively marketing acquired properties; and may incur in additional accounting losses as sales are completed.

Prevailing economic indicators signal continued weakness in the island's economy. A reduction in economic output of about 1.5% is expected in the 2014 fiscal year. In addition, the government's fiscal plan which includes increased taxes and lower incentives for investments may delay the islands ability to recover economically. On the other hand, the US economic conditions continue improving with slight to moderate economic growth expected in fiscal 2014 and 2015.

The dairy industry's production has been stable year-to-date with production slightly below the previous year. The new administrative order signed by the industry administrator increasing the price received by farmers should help stabilize production. The Association continues to monitor events within the industry and there potential impact on the dairy portfolio. The Association lends just over 27.72 percent of total loans to this industry and continues to execute risk management practices to reduce overall risk.

The state-side participation loan portfolio has experienced stability in real estate for "land-in-transition" and "real estate development". Only two loans remain in the participation loan portfolio. Management continues to work together with other associations to promptly collect on these loans.

The Association will continue to search for opportunities to fulfill its public mission. The Board of Directors and management remain cautious of the ACA's ability to quickly grow the portfolio under the prevailing economic environment. Management will focus on targeted marketing to viable farmers in sectors demonstrating the ability to grow and remain competitive in a changing marketplace.

RESULTS OF OPERATIONS

For the three months ended June 30, 2014

Net loss from operations totaled $(44) for a decrease of $232 when compared to a net income from operations of $188 for the same period ended on June 30, 2013. The primary driver for this decrease is that the provision for loan losses increased by $421 due to the calculation of the allowance for loan losses in the second quarter of 2014.

Net interest income was $1,261 compared to $1,191 for the same period ended on June 30, 2013. Total interest income declined even though the accruing loan volume increased. The decrease was mainly due to a notes receivable from other Farm Credit institution that was called during the third quarter 2013 for a reduction of $225. However, the interest income on loans continues to improve as interest rate spreads on new and serviced loans increases. The total interest expense declined by $224 of which $152 was related with the note payable for other Farm Credit institution paid on the third quarter 2013, along with a reduction in the cost of funds.

Noninterest income, including net gains or losses on other transactions, was $273 compared to a noninterest income of $468 for the same period ended on June 30, 2013, resulting in a decrease of $195 or 41.67 percent. This decrease was mainly due to a decline of $135 in patronage paid by AgFirst FCB (the Bank) to the Associations.

Noninterest expense, including net gains or losses on Other Property Owned, was $1,265 compared to $1,579 for the same period ended June 30, 2013, resulting in a decrease of $314 or 19.89 percent. The decrease was primarily due to a non-recurring loss on acquired property sold (former participation loan) in June 2013.

For the six months ended June 30, 2014

For the six months ended June 30, 2014, the Association recognized net income of $162. A decrease of $138 compared to a net income of $300 for the first six months of 2013, primarily the result of a provision for loan loss expense and lower patronage from the Bank.

During the first six months of 2014, interest income decreased $324, mainly due to $450 reduction due to the call of the notes receivable from other Farm Credit Institution offset by an increase of $126 on the interest income from loans. Interest expense related to the notes payable to AgFirst FCB decreased by $453, including $310 related with the note payable paid for other Farm Credit institutions on the third quarter 2013. Also, the provision for loan loss increased $329, thus, net interest income after provision for loan losses decreased by $200 or 8.79 percent.

Noninterest income for the first half of 2014 was $548 or 35.91 percent lower than the $855 recognized during the first half of 2013. The decrease was primarily attributable to the non-recurring income of $94 paid by AgFirst to the Association in 2013; and a decrease of $117 on other noninterest income.

Noninterest expense for the six months ended June 30, 2014 decreased by $369 or 13.03 percent compared to the same six month period of 2013. The decrease was primarily related to a decrease of $168 in salaries and employee benefits; and a decrease of $184 on net losses on other property owned.

Although the Association is subject to federal income tax, the Association does not expect to incur a federal tax liability in 2014 due to the taxable loss carryforward. No provision for income taxes has been recognized in 2014.

Key Results of Operations Ratios

	Annualized for the three months ended 6/30/14	**For the year ended 12/31/13**
Return on Average Assets	.20%	1.50%
Return on Average Equity	.66%	5.67%
Net Interest Income as a Percentage of Average Earning Assets	2.94%	2.57%

LIQUIDITY AND FUNDING SOURCES

Liquidity

Liquidity management is the process whereby funds are made available to meet all financial commitments including the extension of credit, payment of operating expenses and payment of debt obligations. The Association receives access to funds through its borrowing relationship with the Bank and from income generated by operations. Sufficient liquid funds have been available to meet all financial obligations.

Funding Sources

The principal source of funds for the Association is the borrowing relationship established with 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 funds are advanced by the Bank to the Association in the form of notes payable. The notes payable are segmented into variable rate and fixed rate notes. The variable rate notes are utilized by the Association to fund variable rate loan advances and operating fund requirements. The fixed rate notes are used specifically to fund fixed rate loan advances made by the Association.

The total notes payable to AgFirst Farm Credit Bank at June 30, 2014 were $115,177 as compared with $116,275 at

December 31, 2013. The decrease of $1,098 or .94 percent for the total notes payable is primarily due to an increase in the loanable funds credit that decreased the note payable for lending.

See Note 6 in the Notes to the Consolidated Financial Statements for additional information on the status of compliance with requirements under the General Financing Agreement.

The Association had no lines of credit outstanding with third parties as of June 30, 2014.

Funds Management

Demand for loan types is a driving force in establishing a funds management strategy. The Association offers variable and fixed rate loan products which are competitively priced according to local market rates. Variable rate loans are generally indexed to either the Prime rate or the London Interbank Offered Rate (LIBOR). The majority of the interest rate risk in the Association balance sheet is transferred to the Bank through the notes payable structure. The Bank, in turn, actively utilizes funds management techniques to identify, quantify and control interest rate risk associated with the loan portfolio.

CAPITAL RESOURCES

Total members' equity at June 30, 2014 increased by $144 or .29 percent to $49,239 from December 31, 2013 when total members' equity was $49,095. The increase of $144 was primarily attributable to the year-to-date net income which totaled $162 at June 30, 2014 partially offset by the decrease of capital stock and participation certificates.

Total capital stock and participation certificates were $524 on June 30, 2014 compared to $537 on December 31, 2013. The decrease of $13 was the net result of refunding more stock to non-borrowing stockholders than new stockholders purchasing capital stock or participation certificates.

Unallocated retained earnings was $48,418 on June 30, 2014 for an increase of $162 or .34 percent from December 31, 2013 when unallocated retained earnings totaled $48,256. The increase was due to the net income during the first three months of 2014.

The Association's regulatory permanent capital ratio at June 30, 2014 was 31.53 percent compared to 29.41 percent at December 31, 2013. The Association's total surplus and core surplus ratios were both 31.17 percent at June 30, 2014. 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.

Key financial condition ratios were as follows:

	6/30/14	12/31/13
Total Members' Equity to Asset	29.44%	29.16%
Debt to Total Members' Equity	2.40	2.43

REGULATORY MATTERS

FCA Supervisory Agreement

On March 17, 2011 the Farm Credit Administration (FCA) entered into a written Supervisory Agreement (SA) with the Board of Directors of the Association. This agreement supersedes FCA Supervisory Letters dated July 23, 2009, March 2, 2010, and December 10, 2010 and incorporates certain requirements from these letters. The Supervisory Agreement requires the Board of Directors to take certain corrective and precautionary measures with respect to some Association practices, including board governance and operation, director fiduciary duties, nominating committee procedures, board policies, board business planning, Association earnings and liquidity, senior management and human capital development, internal audit and review, asset quality, allowance for loan losses and collateral risk management, and capital markets and participation activities. In addition, the SA prohibits the Association from distributing patronage-sourced income without FCA consent.

Conditions and events that led to the need for this agreement include portfolio credit quality deterioration, high turnover in senior management, perceived weaknesses in board governance, and, reduced earnings and liquidity.

The Board of Directors and the Association have worked together to reach significant milestones. The regulator has provided the Board of Directors several interim progress reports on compliance with the SA and delivered a report of examination to the Board of Directors as of June 30, 2013. The Association has achieved full compliance in 13 out 17 items, substantial compliance in 3 out of 17 items and partial compliance in 1 out 17 items. Some of the results achieved in compliance with the agreement include the following:

- Hiring a board consultant and continued work with the consultant to assist the Board in fulfilling its fiduciary duties and improving board operations and governance.
- Updating its board committee charters, undergoing several training sessions and changing leadership to improve governance of the Association.
- Revising the director candidate nominating procedures to qualify new candidates, which led to stockholders electing two new directors to the Board in 2012.
- Hiring a new CEO beginning on February 1, 2011 to lead the Association after the retirement of the previous CEO on June 30, 2010.
- Building a cohesive senior management team.
- Overseeing the implementation of updated collateral risk management policies and procedures that are in line with best practices in the industry.
- Improving the methodology used to calculate the Allowance for Loan Losses of the Association.
- Hiring a specialized third party auditor that assessed the capital markets portfolio credit risk and helped, strengthened credit policies and procedures.

- Establishing a Compliance Committee to monitor management's progress in implementing the corrective actions of items identified in the SA.
- Ensuring that FCA's recommendations are incorporated in the various action plans.
- Reviewing the Association's internal audit plan to focus on areas where perceived weaknesses were identified.
- Establishing a risk assessment process to assess risks and controls in the ACA.
- Establishing an asset quality improvement plan to monitor management efforts in managing high risk loans.
- Revising the 2011 business plan to establish strategic priorities and to comply with FCA regulations governing business planning.
- Establishing a human capital plan and succession plan to assist in the long-term success of the Association.
- Revising board policies on a quarterly basis to guide management in conducting day to day operations.
- Enhancing the participation's portfolio credit underwriting and administration controls.

All required measures have not been achieved or completed as of the date of this report and the Board of Directors continues to work with the management team in improving the areas identified in the Supervisory Agreement. Besides the ongoing corrective actions already mentioned, other actions to be taken target the following areas.

- Continue execution of strategies for growing the Association's loan portfolio with high quality loans to improve asset quality and, enhance earnings and liquidity.
- Continue making progress in the execution of collateral risk management practices. Improving on perceived weaknesses in the preparation and documentation of appraisals.

The Board of Directors will continue engaging a board consultant to provide advice in understanding and fulfilling its fiduciary responsibilities and to perform other advisory functions as specified in the agreement. Both the Board of Directors and Senior Management are committed to continuing the administration of the Association in a sound manner, compliant with all FCA Regulations.

The Association remained under written supervisory agreement as of the date of this report.

Other 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 May 8, 2014, the FCA approved a proposed rule to modify the regulatory capital requirements for System Banks and Associations. 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).

Once the proposed rule is published in the Federal Register, the 120-day public comment period will commence.

On June 12, 2014, the FCA approved a proposed rule to revise the requirements governing the eligibility of investments for System Banks and Associations. 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.

The public comment period ends on October 23, 2014.

On June 30, 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. A final effective date for the rule has not yet been published.

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.

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 its website, *www.agfirst.com*. Copies of the Association's annual and quarterly reports are also available upon request free of charge by calling 1-800-981-3323, or writing Nydia J. Acevedo, Controller, Puerto Rico Farm Credit, ACA, PO Box 363649, San Juan, PR 00936-3649, or accessing the website, *www.puertoricofarmcredit.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 Association.

Puerto Rico Farm Credit, ACA

Consolidated Balance Sheets

(dollars in thousands)		June 30, 2014		December 31, 2013
		(unaudited)		*(audited)*
Assets				
Cash	$	158	$	103
Loans		164,495		161,841
Allowance for loan losses		(3,194)		(3,128)
Net loans		161,301		158,713
Other investments		70		70
Accrued interest receivable		679		588
Investments in other Farm Credit institutions		1,876		1,876
Premises and equipment, net		865		915
Other property owned		1,451		2,481
Accounts receivable		535		2,868
Other assets		298		763
Total assets	$	167,233	$	168,377
Liabilities				
Notes payable to AgFirst Farm Credit Bank	$	115,177	$	116,275
Accrued interest payable		161		169
Accounts payable		293		360
Other liabilities		2,363		2,478
Total liabilities		117,994		119,282
Commitments and contingencies				
Members' Equity				
Capital stock and participation certificates		524		537
Unallocated retained earnings		48,418		48,256
Accumulated other comprehensive income		297		302
Total members' equity		49,239		49,095
Total liabilities and members' equity	$	167,233	$	168,377

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

Puerto Rico Farm Credit, ACA

Consolidated Statements of Operations

(unaudited)

(dollars in thousands)	For the three months ended June 30, 2014	For the three months ended June 30, 2013	For the six months ended June 30, 2014	For the six months ended June 30, 2013
Interest Income				
Loans	$ 1,745	$ 1,674	$ 3,367	$ 3,241
Notes receivable from other Farm Credit institutions	—	225	—	450
Total interest income	1,745	1,899	3,367	3,691
Interest Expense				
Notes payable to AgFirst Farm Credit Bank	484	708	971	1,424
Net interest income	1,261	1,191	2,396	2,267
Provision for (reversal of allowance for) loan losses	313	(108)	320	(9)
Net interest income after provision for (reversal of allowance for) loan losses	948	1,299	2,076	2,276
Noninterest Income				
Loan fees	24	35	50	70
Fees for financially related services	—	—	1	1
Patronage refunds from other Farm Credit institutions	232	368	458	639
Gains (losses) on other transactions	—	(3)	6	(5)
Other noninterest income	17	68	33	150
Total noninterest income	273	468	548	855
Noninterest Expense				
Salaries and employee benefits	726	817	1,502	1,670
Occupancy and equipment	62	73	116	136
Insurance Fund premiums	32	34	64	67
(Gains) losses on other property owned, net	71	299	112	296
Other operating expenses	374	356	668	662
Total noninterest expense	1,265	1,579	2,462	2,831
Net income (loss)	$ (44)	$ 188	$ 162	$ 300

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

Puerto Rico Farm Credit, ACA

Consolidated Statements of Comprehensive Income

(unaudited)

(dollars in thousands)	For the three months ended June 30, 2014	For the three months ended June 30, 2013	For the six months ended June 30, 2014	For the six months ended June 30, 2013
Net income	$ (44)	$ 188	$ 162	$ 300
Other comprehensive income net of tax				
Employee benefit plans adjustments	(3)	13	(5)	26
Comprehensive income	$ (47)	$ 201	$ 157	$ 326

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

Puerto Rico Farm Credit, ACA

Consolidated Statements of Changes in Members' Equity

(unaudited)

(dollars in thousands)	Capital Stock and Participation Certificates	Retained Earnings Unallocated	Accumulated Other Comprehensive Income	Total Members' Equity
Balance at December 31, 2012	$ 604	$ 45,569	$ 286	$ 46,459
Comprehensive income		300	26	326
Capital stock/participation certificates issued/(retired), net	(41)			(41)
Balance at June 30, 2013	$ 563	$ 45,869	$ 312	$ 46,744
Balance at December 31, 2013	$ 537	$ 48,256	$ 302	$ 49,095
Comprehensive income		162	(5)	157
Capital stock/participation certificates issued/(retired), net	(13)			(13)
Balance at June 30, 2014	$ 524	$ 48,418	$ 297	$ 49,239

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

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 Puerto Rico 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 May 2014 the Financial Accounting Standards Board (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. Accounting Standards Update (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. 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 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:

	June 30, 2014	December 31, 2013
Real estate mortgage	$ 93,834	$ 95,341
Production and intermediate-term	28,572	24,240
Processing and marketing	16,875	16,875
Farm-related business	2,386	2,422
Communication	5,909	5,534
Energy and water/waste disposal	2,114	2,327
Rural residential real estate	14,805	15,102
Total Loans	$ 164,495	$ 161,841

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:

June 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	$ 1,080	$ 5,847	$ –	$ –	$ 1,401	$ –	$ 2,481	$ 5,847
Production and intermediate term	9,303	1,905	–	–	5,953	–	15,256	1,905
Processing and marketing	16,252	–	–	–	517	–	16,769	–
Farm-related business	–	–	–	–	2,163	–	2,163	–
Communication	5,923	–	–	–	–	–	5,923	–
Energy and water/waste disposal	2,117	–	–	–	–	–	2,117	–
Total	$ 34,675	$ 7,752	$ –	$ –	$ 10,034	$ –	$ 44,709	$ 7,752

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	$ 1,107	$ 5,969	$ –	$ –	$ 1,446	$ –	$ 2,553	$ 5,969
Production and intermediate term	7,694	1,877	–	–	5,514	–	13,208	1,877
Processing and marketing	16,200	–	–	–	556	–	16,756	–
Farm-related business	–	–	–	–	2,193	–	2,193	–
Communication	5,550	–	–	–	–	–	5,550	–
Energy and water/waste disposal	2,330	–	–	–	–	–	2,330	–
Total	$ 32,881	$ 7,846	$ –	$ –	$ 9,709	$ –	$ 42,590	$ 7,846

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:

	June 30, 2014			
	Due less than 1 year	Due 1 Through 5 years	Due after 5 years	Total
Real estate mortgage	$ 12,829	$ 50,381	$ 30,624	$ 93,834
Production and intermediate-term	4,846	15,002	8,724	28,572
Processing and marketing	–	12,394	4,481	16,875
Farm-related business	–	1,792	594	2,386
Communication	–	5,909	–	5,909
Energy and water/waste disposal	–	115	1,999	2,114
Rural residential real estate	449	165	14,191	14,805
Total Loans	$ 18,124	$ 85,758	$ 60,613	$ 164,495
Percentage	11.02%	52.13%	36.85%	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:

	June 30, 2014	December 31, 2013
Real estate mortgage:		
Acceptable	88.70%	86.86%
OAEM	0.59	1.08
Substandard/doubtful/loss	10.71	12.06
	100.00%	100.00%
Production and intermediate-term:		
Acceptable	79.11%	75.06%
OAEM	5.87	5.36
Substandard/doubtful/loss	15.02	19.58
	100.00%	100.00%
Processing and marketing:		
Acceptable	100.00%	100.00%
OAEM	–	–
Substandard/doubtful/loss	–	–
	100.00%	100.00%
Farm-related business:		
Acceptable	100.00%	100.00%
OAEM	–	–
Substandard/doubtful/loss	–	–
	100.00%	100.00%

	June 30, 2014	December 31, 2013
Communication:		
Acceptable	100.00%	100.00%
OAEM	–	–
Substandard/doubtful/loss	–	–
	100.00%	100.00%
Energy and water/waste disposal:		
Acceptable	100.00%	100.00%
OAEM	–	–
Substandard/doubtful/loss	–	–
	100.00%	100.00%
Rural residential real estate:		
Acceptable	94.43%	94.96%
OAEM	0.82	1.29
Substandard/doubtful/loss	4.75	3.75
	100.00%	100.00%
Total Loans:		
Acceptable	89.42%	88.05%
OAEM	1.43	1.56
Substandard/doubtful/loss	9.15	10.39
	100.00%	100.00%

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

	June 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	$ 1,335	$ 6,320	$ 7,655	$ 86,564	$ 94,219	$ –
Production and intermediate-term	–	1,620	1,620	27,116	28,736	–
Processing and marketing	–	–	–	16,945	16,945	–
Farm-related business	–	–	–	2,398	2,398	–
Communication	–	–	–	5,910	5,910	–
Energy and water/waste disposal	–	–	–	2,115	2,115	–
Rural residential real estate	473	103	576	14,275	14,851	–
Total	$ 1,808	$ 8,043	$ 9,851	$ 155,323	$ 165,174	$ –

	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	$ 2,569	$ 7,780	$ 10,349	$ 85,290	$ 95,639	$ –
Production and intermediate-term	181	1,620	1,801	22,608	24,409	–
Processing and marketing	–	–	–	16,945	16,945	–
Farm-related business	–	–	–	2,434	2,434	–
Communication	–	–	–	5,535	5,535	–
Energy and water/waste disposal	–	–	–	2,327	2,327	–
Rural residential real estate	296	102	398	14,742	15,140	–
Total	$ 3,046	$ 9,502	$ 12,548	$ 149,881	$ 162,429	$ –

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:

	June 30, 2014	December 31, 2013
Nonaccrual loans:		
Real estate mortgage	$ 7,951	$ 10,741
Production and intermediate-term	1,820	1,886
Rural residential real estate	352	284
Total nonaccrual loans	$ 10,123	$ 12,911
Accruing restructured loans:		
Real estate mortgage	$ 2,239	$ 1,161
Production and intermediate-term	1,210	1,192
Total accruing restructured loans	$ 3,449	$ 2,353
Accruing loans 90 days or more past due:		
Total accruing loans 90 days or more past due	$ –	$ –
Total nonperforming loans	$ 13,572	$ 15,264
Other property owned	1,451	2,481
Total nonperforming assets	$ 15,023	$ 17,745
Non-accrual loans as a percentage of total loans	6.15%	7.98%
Nonperforming assets as a percentage of total loans and other property owned	9.05%	10.80%
Nonperforming assets as a percentage of capital	30.51%	36.14%

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.

	June 30, 2014	December 31, 2013
Impaired non-accrual loans:		
Current as to principal and interest	$ 1,942	$ 1,612
Past due	8,181	11,299
Total impaired non-accrual loans	10,123	12,911
Impaired accrual loans:		
Restructured	3,449	2,353
90 days or more past due	–	–
Total impaired accrual loans	3,449	2,353
Total impaired loans	$ 13,572	$ 15,264

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

	June 30, 2014			Quarter Ended June 30, 2014		Six Months Ended June 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	$ 5,242	$ 7,580	$ 689	$ 6,095	$ 58	$ 5,975	$ 84
Production and intermediate-term	2,559	5,711	461	2,975	29	2,916	41
Rural residential real estate	–	–	–	–	–	–	–
Total	$ 7,801	$ 13,291	$ 1,150	$ 9,070	$ 87	$ 8,891	$ 125
Impaired loans with no related allowance for credit losses:							
Real estate mortgage	$ 4,948	$ 6,064	$ –	$ 5,750	$ 56	$ 5,637	$ 79
Production and intermediate-term	471	519	–	549	5	538	8
Rural residential real estate	352	413	–	409	4	401	6
Total	$ 5,771	$ 6,996	$ –	$ 6,708	$ 65	$ 6,576	$ 93
Total impaired loans:							
Real estate mortgage	$ 10,190	$ 13,644	$ 689	$ 11,845	$ 114	$ 11,612	$ 163
Production and intermediate-term	3,030	6,230	461	3,524	34	3,454	49
Rural residential real estate	352	413	–	409	4	401	6
Total	$ 13,572	$ 20,287	$ 1,150	$ 15,778	$ 152	$ 15,467	$ 218

	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	$ 2,634	$ 2,947	$ 719	$ 2,739	$ 36
Production and intermediate-term	1,148	4,304	413	1,194	15
Rural residential real estate	–	–	–	–	–
Total	$ 3,782	$ 7,251	$ 1,132	$ 3,933	$ 51
Impaired loans with no related allowance for credit losses:					
Real estate mortgage	$ 9,268	$ 12,155	$ –	$ 9,637	$ 125
Production and intermediate-term	1,930	1,977	–	2,006	27
Rural residential real estate	284	343	–	296	4
Total	$ 11,482	$ 14,475	$ –	$ 11,939	$ 156
Total impaired loans:					
Real estate mortgage	$ 11,902	$ 15,102	$ 719	$ 12,376	$ 161
Production and intermediate-term	3,078	6,281	413	3,200	42
Rural residential real estate	284	343	–	296	4
Total	$ 15,264	$ 21,726	$ 1,132	$ 15,872	$ 207

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	Energy and Water/Waste Disposal	Rural Residential Real Estate	Total
Allowance for credit losses:							
Balance at March 31, 2014	$ 1,430	$ 1,042	$ 417	$ 13	$ 1	$ 230	$ 3,133
Charge-offs	(247)	(5)	–	–	–	–	(252)
Recoveries	–	–	–	–	–	–	–
Provision for loan losses	(277)	584	(4)	15	–	(5)	313
Balance at June 30, 2014	$ 906	$ 1,621	$ 413	$ 28	$ 1	$ 225	$ 3,194
Balance at December 31, 2013	$ 1,359	$ 1,002	$ 565	$ 12	$ 2	$ 188	$ 3,128
Charge-offs	(248)	(5)	–	–	–	(1)	(254)
Recoveries	–	–	–	–	–	–	–
Provision for loan losses	(205)	624	(152)	16	(1)	38	320
Balance at June 30, 2014	$ 906	$ 1,621	$ 413	$ 28	$ 1	$ 225	$ 3,194
Balance at March 31, 2013	$ 1,453	$ 1,656	$ 1,242	$ 16	$ 3	$ 137	$ 4,507
Charge-offs	–	–	(103)	–	–	–	(103)
Recoveries	(1)	1	–	–	–	–	–
Provision for loan losses	(497)	321	–	–	–	68	(108)
Balance at June 30, 2013	$ 955	$ 1,978	$ 1,139	$ 16	$ 3	$ 205	$ 4,296
Balance at December 31, 2012	$ 1,336	$ 1,685	$ 1,241	$ 16	$ 3	$ 127	$ 4,408
Charge-offs	(2)	–	(103)	–	–	–	(105)
Recoveries	1	1	–	–	–	–	2
Provision for loan losses	(380)	292	1	–	–	78	(9)
Balance at June 30, 2013	$ 955	$ 1,978	$ 1,139	$ 16	$ 3	$ 205	$ 4,296
Loans individually evaluated for impairment	$ 689	$ 461	$ –	$ –	$ –	$ –	$ 1,150
Loans collectively evaluated for impairment	217	1,160	413	28	1	225	2,044
Balance at June 30, 2014	$ 906	$ 1,621	$ 413	$ 28	$ 1	$ 225	$ 3,194
Loans individually evaluated for impairment	$ 719	$ 413	$ –	$ –	$ –	$ –	$ 1,132
Loans collectively evaluated for impairment	640	589	565	12	2	188	1,996
Balance at December 31, 2013	$ 1,359	$ 1,002	$ 565	$ 12	$ 2	$ 188	$ 3,128
Recorded investment in loans outstanding:							
Loans individually evaluated for impairment	$ 9,836	$ 3,036	$ –	$ –	$ –	$ 112	$ 12,984
Loans collectively evaluated for impairment	84,383	25,700	19,343	5,910	2,115	14,739	152,190
Ending balance at June 30, 2014	$ 94,219	$ 28,736	$ 19,343	$ 5,910	$ 2,115	$ 14,851	$ 165,174
Loans individually evaluated for impairment	$ 13,022	$ 1,883	$ –	$ –	$ –	$ 218	$ 15,123
Loans collectively evaluated for impairment	82,617	22,526	19,379	5,535	2,327	14,922	147,306
Ending balance at December 31, 2013	$ 95,639	$ 24,409	$ 19,379	$ 5,535	$ 2,327	$ 15,140	$ 162,429

**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. There were no TDRs that occurred during the three months ended June 30, 2013.

	Three months ended June 30, 2014				
	Interest Concessions	Principal Concessions	Other Concessions	Total	Charge-offs
Pre-modification Outstanding Recorded Investment					
Production and intermediate-term	$ –	$ 210	$ –	$ 210	
Total	$ –	$ 210	$ –	$ 210	
Post-modification Outstanding Recorded Investment					
Production and intermediate-term	$ –	$ 207	$ –	$ 207	$ –
Total	$ –	$ 207	$ –	$ 207	$ –

	Six months ended June 30, 2014				
	Interest Concessions	Principal Concessions	Other Concessions	Total	Charge-offs
Pre-modification Outstanding Recorded Investment					
Real estate mortgage	$ 115	$ –	$ –	$ 115	
Production and intermediate-term	–	210	–	210	
Total	$ 115	$ 210	$ –	$ 325	
Post-modification Outstanding Recorded Investment					
Real estate mortgage	$ 116	$ –	$ –	$ 116	$ –
Production and intermediate-term	–	207	–	207	–
Total	$ 116	$ 207	$ –	$ 323	$ –

	Six months ended June 30, 2013				
	Interest Concessions	Principal Concessions	Other Concessions	Total	Charge-offs
Pre-modification Outstanding Recorded Investment					
Real estate mortgage	$ –	$ 128	$ –	$ 128	
Total	$ –	$ 128	$ –	$ 128	
Post-modification Outstanding Recorded Investment					
Real estate mortgage	$ –	$ 128	$ –	$ 128	$ –
Total	$ –	$ 128	$ –	$ 128	$ –

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.

There were no TDRs that occurred during the previous twelve months and for which there was a subsequent payment default during the periods presented. Payment default is defined as a payment that was thirty days or more past due.

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	
	June 30, 2014	December 31, 2013	June 30, 2014	December 31, 2013
Real estate mortgage	$ 6,699	$ 6,677	$ 4,460	$ 5,516
Production and intermediate-term	1,411	1,277	201	85
Total Loans	$ 8,110	$ 7,954	$ 4,661	$ 5,601
Additional commitments to lend	$ –	$ –		

Note 3 — Investments

Subordinated Notes Receivable from Other Farm Credit Institutions

In September 2008, the Association used capital reserves to purchase $10,000 total of 9.00 percent fixed rate unsecured subordinated notes issued by two other associations in the District, both notes due in 2018 with a prepayment option beginning in October 2013. On October 15, 2013, the notes receivable were redeemed in full by the issuing associations.

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.

A Special Credit Agreement (SCA) addressing the Association's GFA earnings covenant default was executed effective January 31, 2013 and expired on January 31, 2014. The Association was in compliance with the earnings covenant under the SCA at December 31, 2013 and financial covenants under the GFA at December 31, 2013 and June 30, 2014. The Association operated under the terms and requirements of the 2014 GFA from February 1, 2014 until April 11, 2014. On April 11, 2014, the Association entered into a SCA with the Bank pursuant to its GFA as a result of events of default under the GFA related to continued regulatory enforcement matters discussed in Note 9. This SCA expires on April 11, 2015.

Note 5 — Members' Equity

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

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

	Three Months Ended June 30,		Six Months Ended June 30,	
	2014	**2013**	**2014**	**2013**
Employee Benefit Plans:				
Balance at beginning of period	$ 300	$ 299	$ 302	$ 286
Other comprehensive income before reclassifications	–	–	–	–
Amounts reclassified from AOCI	(3)	13	(5)	26
Net current period other comprehensive income	(3)	13	(5)	26
Balance at end of period	$ 297	$ 312	$ 297	$ 312

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

	For the Three Months Ended June 30,		For the Six Months Ended June 30,		
	2014	**2013**	**2014**	**2013**	**Income Statement Line Item**
Defined Benefit Pension Plans:					
Periodic pension costs	$ 3	$ (13)	$ 5	$ (26)	See Note 7.
Net amounts reclassified	$ 3	$ (13)	$ 5	$ (26)	

(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 Association owns 0.75 percent of the issued stock of the Bank as of June 30, 2014 net of any reciprocal investment. As of that date, the Bank's assets totaled $28.2 billion and shareholders' equity totaled $2.3 billion. The Bank's earnings were $183 million for the first six months of 2014. In addition, the Association has no investment related to other Farm Credit institutions.

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.

The following table presents the changes in 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.

	Standby Letters of Credit	
	For the six months ended June 30,	
	2014	**2013**
Balance at beginning of period	$ 6	$ 17
Issuances	–	–
Settlements	–	(5)
Balance at end of period	$ 6	$ 12

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.

Other Property Owned/Impaired Loans

Other property owned and impaired loans are valued using appraisals, market comparable sales, replacement costs and income and expense (cash flow) techniques. Certain unobservable inputs are used within these techniques to determine the level 3 fair value of these properties. The significant unobservable inputs are primarily sensitive only to industry, geographic and overall economic conditions, and/or specific attributes of each property.

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	$ 14,008	Appraisal	Income and expense	*
			Comparable sales	*
			Replacement cost	*
			Comparability adjustments	*
Other investments – RBIC	$ 70	Third party evaluation	Income, expense, capital	Not applicable

** 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 forecast
		Probability of default
		Loss severity
Notes receivable from other Farm Credit institutions	Discounted cash flow	Prepayment rates
		Risk adjusted discount rate
Notes payable to AgFirst Farm Credit Bank	Discounted cash flow	Prepayment forecasts
		Probability of default
		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 Three Months Ended June 30, 2014					
	Total Carrying Amount	Level 1	Level 2	Level 3	Total Fair Value	Fair Value Effects On Earnings
Recurring Measurements						
Assets:						
Recurring Assets	$ –	$ –	$ –	$ –	$ –	
Liabilities:						
Standby letters of credit	$ 6	$ –	$ –	$ 6	$ 6	
Recurring Liabilities	$ 6	$ –	$ –	$ 6	$ 6	
Nonrecurring Measurements						
Assets:						
Impaired loans	$ 12,422	$ –	$ –	$ 12,422	$ 12,422	$ (272)
Other property owned	1,451	–	–	1,586	1,586	(39)
Other investments	70	–	–	70	70	–
Nonrecurring Assets	$ 13,943	$ –	$ –	$ 14,078	$ 14,078	$ (311)
Other Financial Instruments						
Assets:						
Cash	$ 158	$ 158	$ –	$ –	$ 158	
Loans	148,879	–	–	148,121	148,121	
Other Financial Assets	$ 149,037	$ 158	$ –	$ 148,121	$ 148,279	
Liabilities:						
Notes payable to AgFirst Farm Credit Bank	$ 115,177	$ –	$ –	$ 115,263	$ 115,263	
Other Financial Liabilities	$ 115,177	$ –	$ –	$ 115,263	$ 115,263	

	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:						
Recurring Assets	$ –	$ –	$ –	$ –	$ –	
Liabilities:						
Standby letters of credit	$ 6	$ –	$ –	$ 6	$ 6	
Recurring Liabilities	$ 6	$ –	$ –	$ 6	$ 6	
Nonrecurring Measurements						
Assets:						
Impaired loans	$ 14,132	$ –	$ –	$ 14,132	$ 14,132	$ 749
Other property owned	2,481	–	–	2,619	2,619	(1,105)
Other investments	70	–	–	70	70	(180)
Nonrecurring Assets	$ 16,683	$ –	$ –	$ 16,821	$ 16,821	$ (536)
Other Financial Instruments						
Assets:						
Cash	$ 103	$ 103	$ –	$ –	$ 103	
Loans	144,581	–	–	143,494	143,494	
Notes receivable from other Farm Credit institutions	–	–	–	–	–	
Other Financial Assets	$ 144,684	$ 103	$ –	$ 143,494	$ 143,597	
Liabilities:						
Notes payable to AgFirst Farm Credit Bank	$ 116,275	$ –	$ –	$ 116,000	$ 116,000	
Other Financial Liabilities	$ 116,275	$ –	$ –	$ 116,000	$ 116,000	

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 June 30,		For the six months ended June 30,	
	2014	2013	2014	2013
Pension	$ 261	$ 248	$ 523	$ 497
401(k)	20	19	36	38
Other postretirement benefits	27	39	55	78
Total	$ 308	$ 306	$ 614	$ 613

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

	Actual YTD Through 6/30/14	Projected Contributions For Remainder of 2014	Projected Total Contributions 2014
Pension	$ –	$ 813	$ 813
Other postretirement benefits	107	5	112
Total	$ 107	$ 818	$ 925

Contributions in the above table include an allocated estimate of funding for the multi-employer pension plan in which the Association participates. The projected amount may change when a total funding amount and allocation is determined by the pension Plan's Sponsor Committee. Also, market conditions could impact discount rates and return on plan assets which could change the contribution 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% 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% 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 — Regulatory Enforcement Matters

On March 17, 2011 the Farm Credit Administration (FCA) entered into a written Supervisory Agreement (SA) with the Board of Directors of the Association. This agreement supersedes FCA Supervisory Letters dated July 23, 2009, March 2, 2010, and December 10, 2010 and incorporates certain requirements from these letters. The Supervisory Agreement requires the Board of Directors to take certain corrective and precautionary measures with respect to some Association practices, including board governance and operation, director fiduciary duties, nominating committee procedures, board policies, board business planning, Association earnings and liquidity, senior management and human capital development, internal audit and review, asset quality, allowance for loan losses and collateral risk management, and capital markets and participation activities. In addition, the SA prohibits the Association from distributing patronage-sourced income without FCA consent.

Conditions and events that led to the need for this agreement include portfolio credit quality deterioration, high turnover in senior management, perceived weaknesses in board governance, and, reduced earnings and liquidity.

The Board of Directors and the Association have worked together to reach significant milestones. The regulator has provided the Board of Directors several interim progress reports on compliance with the SA and delivered a report of examination to the Board of Directors as of June 30, 2013. The Association has achieved full compliance in 13 out of 17 items, substantial compliance in 3 out of 17 items and partial compliance in 1 out of 17 items. Some of the results achieved in compliance with the agreement include the following:

- Hiring a board consultant and working with the consultant to assist the Board in fulfilling its fiduciary duties and improving board operations and governance.
- Updating its board committee charters, undergoing several training sessions and changing leadership to improve governance of the Association.
- Revising the director candidate nominating procedures to qualify new candidates, which led to stockholders electing two new directors to the Board in 2012.
- Hiring a new CEO beginning on February 1, 2011 to lead the Association after the retirement of the previous CEO on September 30, 2010.
- Building a cohesive senior management team.
- Overseeing the implementation of updated collateral risk management policies and procedures that are in line with best practices in the industry.
- Improving the methodology used to calculate the Allowance for Loan Losses of the Association.
- Hiring a specialized third party auditor that assessed the capital markets portfolio credit risk and helped, strengthened credit policies and procedures.
- Establishing a Compliance Committee to monitor management's progress in implementing the corrective actions of items identified in the SA.
- Ensuring that FCA's recommendations are incorporated in the various action plans.
- Reviewing the Association's internal audit plan to focus on areas where perceived weaknesses were identified.
- Establishing a risk assessment process to assess risks and controls in the ACA.
- Establishing an asset quality improvement plan to monitor management efforts in managing high risk loans.
- Revising the 2011 business plan to establish strategic priorities and to comply with FCA regulations governing business planning.
- Establishing a human capital plan and succession plan to assist in the long-term success of the Association.
- Revising board policies on a quarterly basis to guide management in conducting day to day operations.
- Enhancing the participation's portfolio credit underwriting and administration controls.

All required measures have not been achieved or completed as of the date of this report and the Board of Directors continues to work with the management team in improving the areas identified in the Supervisory Agreement. Besides the ongoing corrective actions already mentioned, other actions to be taken target the following areas.

- Continue executing strategies to grow the Association's loan portfolio with high quality loans to improve asset quality and, enhance earnings and liquidity.
- Continue making progress in the execution of collateral risk management practices. Improving on perceived weaknesses in the preparation and documentation of appraisals.

The Board of Directors will continue engaging a board consultant to provide advice in understanding and fulfilling its fiduciary responsibilities and to perform other advisory functions as specified in the agreement. Both the Board of Directors and Senior Management are committed to continuing the administration of the Association in a sound manner, compliant with all FCA Regulations.

The Association remained under written supervisory agreement as of the date of this report.

Note 10 — Subsequent Events

The Association has evaluated subsequent events and has determined that, except as described in Note 4 above, there are none requiring disclosure through August 7, 2014, which is the date the financial statements were issued.