Puerto Rico Farm Credit, ACA

THIRD QUARTER 2013

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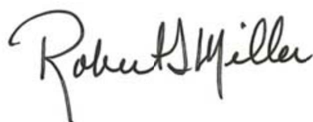
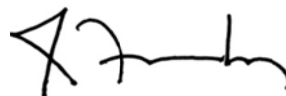
CERTIFICATION

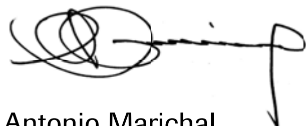
The undersigned certify that we have reviewed the September 30, 2013 quarterly report of Puerto Rico Farm Credit, ACA, that the report has been prepared under the oversight of the Audit Committee of the Board of Directors and in accordance with all applicable statutory or regulatory requirements, and that the information contained herein is true, accurate, and complete to the best of our knowledge and belief.



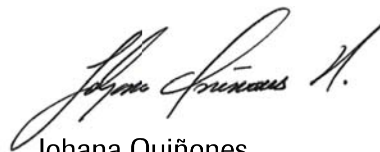
Robert G. Miller
Chairman of Board of Directors



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

November 7, 2013

Puerto Rico Farm Credit, ACA

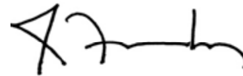
Report on Internal Control Over Financial Reporting

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.

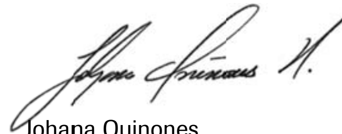
Internal control over financial reporting includes those policies and procedures that: (1) pertain to the maintenance of records that in reasonable detail accurately and fairly reflect the transactions and dispositions of the assets of the Association, (2) provide reasonable assurance that transactions 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 September 30, 2013. 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, 2013, 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, 2013.



Ricardo L. Fernández
Chief Executive Officer



Johana Quinones
Director of Finance
Risk Management and Internal Control

November 7, 2013

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 nine months ended September 30, 2013. These comments should be read in conjunction with the accompanying consolidated financial statements, notes to the consolidated financial statements, and the 2012 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, livestock, rural home and fruits which totaled approximately $92,181 or 55.43 percent of the gross principal balance, net of sold loans, at September 30, 2013.

The outstanding loan volume of the Association at September 30, 2013 was $159,806 for a decrease of $9,583 or 5.66 percent as compared to $169,389 at December 31, 2012. Loans originated within the Association's chartered territory were lower by approximately $13,254, while participation loans purchased increased by approximately $3,671.

Net loans outstanding at September 30, 2013 totaled $155,849 as compared to $164,981 at December 31, 2012. The decrease in the net loan volume is mostly attributed to a $3,792 loan that paid in full, other unexpected downpayments, among the normal amortization of the portfolio. Also, the local chartered territory continued to experience a reduction in demand for credit. Net loans made up 89.50 percent of total assets at September 30, 2013, as compared to 89.04 percent at December 31, 2012.

As a percentage of outstanding loans, non-accrual loans totaled 8.77 percent at September 30, 2013, compared with 8.22 percent at December 31, 2012. The increase in the percentage of non-accrual loan volume during the first nine months of 2013 was primarily the result of seven chartered territory loans amounting approximately $1,918 being transferred to nonaccrual offset by some principal curtailments among other payments received on various nonaccrual outstanding loans. The increase on nonaccruals was partially offset by the reinstatements to accrual status of three loans amounting approximately $200.

Several loans transferred to nonaccrual are expected to be transferred back to accrual status by year end. 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 and remains cautious about the credit quality of certain chartered territory loan through 2013. The participation portfolio credit quality has improved significantly during 2013; and is expected to continue improving in the next quarter as the portfolio increases and troubled loans are resolved.

The allowance for loan losses decreased by $451 to $3,957 at September 30, 2013, from $4,408 at December 31, 2012. The total allowance for loan losses to outstanding loan volume ratio decreased to 2.48 percent at September 30, 2013 from 2.60 percent at December 31, 2012. The decrease was primarily due to a $195 charge off recorded on an ethanol nonaccrual participation loan that decreased its specific reserve. Also, the general reserve decreased due to an improvement in the credit quality, decrease in the chartered territory portfolio and increase in high quality volume of the participation's portfolio. Management will continue to monitor certain risks, such as collateral risk, and may decide to increase the allowance in 2013.

During the first nine months of 2013, charge-offs recognized totaled $202 while recoveries totaled $2. The ACA is actively marketing acquired properties and may incur in accounting losses as sales are completed.

Prevailing economic indicators signal continued weakness in the island's economy. No growth is expected in 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 are improving with slight economic growth being expected in fiscal 2013 and 2014.

The dairy industry's production has been stable year-to-date with production slightly below the previous year. The ACA continues to monitor events within the industry and there potential impact on the dairy portfolio. The association lends just over 25.95% of total loans to this industry and is

implementing risk management practices to reduce overall risk.

The local livestock industry which, relies heavily on pastures instead of feed has not been affected by increasing corn prices. The Associations' exposure in livestock is also minimal and borrowers in the industry continue to perform well.

Management expects that the ethanol industry will continue undergoing significant changes and that it will adversely impact its valuation of one loan and one acquired property in the industry. Within the state-side participation portfolio, stability is being experienced in real estate for "land-in-transition". The association has significantly reduced its exposure in such loans but, two loans remain in the 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 September 30, 2013

Net income from operations for the three months ended September 30, 2013 totaled $600, for an increase of $1,214 when compared to a net loss from operations of $314 for the same period in 2012. The primary drivers of this increase is that the provision for loan losses decreased by $539 due to the calculation of the allowance for loan losses; and the noninterest incomes increased by $371.

Net interest income for the three months ended September 30, 2013 was $1,136 compared to $1,250 for the same period ended September 30, 2012. Interest income on loans declined quarter-over-quarter since the accruing loan volume decreased. Even though, a reduction in the cost of funds and improved spreads on new and serviced loans partially offset the reduction in net interest income.

Noninterest income for the three months ended September 30, 2013, including net gains or losses on other property owned, was $326 compared to a noninterest loss of $45 for the same period in 2012, resulting in an increase of $371. This increase was mainly due to a $361 net loss on other property owned has been recognized during 2012 compared to $43 net loss for the current year three months period.

Noninterest expense decrease by $118 compared to the three months ended September 30, 2012. The decrease was primary due to salaries and employee benefits that has being lower mainly due to employees retirements.

For the nine months ended September 30, 2013

For the nine months ended September 30, 2013, the Association recognized net income of $900. A decrease of $425 compared to a net income of $1,325 for the first nine months of 2012. This reduction in net income was primarily resulted from the nonrecurrent insurance premium refund of $679 from the Farm Credit System Insurance Corporation (FCSIC) received on 2012 partially offset by a $180 reduction of net interest income after reversal of allowance for loan losses.

During the nine months of 2013, interest income, primarily from accruing loans decreased by $172. Interest expense related to the notes payable to AgFirst FCB (the Bank) decreased by $156 or 6.90 percent. Thus, net interest income decreased by $16 or .47 percent. The decrease in net interest income was due primarily to the reduction in the accruing loan volume even though the cost of funds decreased and the spreads on loans continue to improve.

Noninterest income for the nine months of 2013 was $885 or 42.90 percent lower than the $1,550 recognized during the nine months of 2012. The decrease was primarily attributable to the non-recurring income of $679 refund distributions received from the FCSIC during the third quarter of 2013.

Noninterest expense for the nine months ended September 30, 2013 decreased by $60 or 1.62 percent compared to the same nine month period of 2012. The decrease was primarily related to a decrease of $132 in other operating expenses partially offset by an increase of $28 of the salaries and employee benefits and $40 of the Insurance Fund Premiums.

Although the Association is subject to federal income tax, the Association does not expect to incur a federal tax liability in 2013 due to the taxable loss carryforward. No provision for income taxes has been recognized in 2013.

Key Results of Operations Ratios

	Annualized for the nine months ended 9/30/13	For the year ended 12/31/12
Return on Average Assets	.66%	.37%
Return on Average Equity	2.57%	1.45%
Net Interest Income as a Percentage of Average Earning Assets	2.55%	2.50%

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 the Bank at September 30, 2013 were $123,790 as compared with $135,882 at December 31, 2012. The decrease of $12,092 or 8.90 percent for the total notes payable is primarily due to loan repayments by borrowers.

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

The Association had no lines of credit outstanding with third parties as of September 30, 2013.

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 September 30, 2013 increased by 1.90 percent to $47,343 from December 31, 2012 when total members' equity was $46,459. The increase of $884 was primarily attributable to the year-to-date net income which totaled $900 at September 30, 2013 partially offset by the decrease of capital stock and participation certificates.

Total capital stock and participation certificates were $549 on September 30, 2013 compared to $604 on December 31, 2012. The decrease of $55 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 $46,469 on September 30, 2013 for an increase of $900 or 1.98 percent from December 31, 2012 when unallocated retained earnings totaled $45,569. The increase was due to the net income during the first nine months of 2013.

The Association's regulatory permanent capital ratio at September 30, 2013 was 23.27 percent compared to 20.67 percent at December 31, 2012. The Association's total surplus and core surplus ratios were both 22.88 percent at September 30, 2013. 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:

	9/30/13	12/31/12
Total Members' Equity to Asset	27.19%	25.07%
Debt to Total Members' Equity	2.68	2.99

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 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 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.

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 2012 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)	September 30, 2013	December 31, 2012
	(unaudited)	*(audited)*
Assets		
Cash	$ 44	$ 214
Loans	159,806	169,389
Less: allowance for loan losses	3,957	4,408
Net loans	155,849	164,981
Notes receivable from other Farm Credit institutions (Note 5)	10,000	10,000
Accrued interest receivable	719	604
Investments in other Farm Credit institutions	1,960	1,960
Premises and equipment, net	903	840
Other property owned	3,244	3,498
Due from AgFirst Farm Credit Bank	812	1,387
Other assets	606	1,804
Total assets	$ 174,137	$ 185,288
Liabilities		
Notes payable to AgFirst Farm Credit Bank	$ 123,790	$ 135,882
Accrued interest payable	183	245
Other liabilities	2,821	2,702
Total liabilities	126,794	138,829
Commitments and contingencies		
Members' Equity		
Capital stock and participation certificates	549	604
Unallocated retained earnings	46,469	45,569
Accumulated other comprehensive income	325	286
Total members' equity	47,343	46,459
Total liabilities and members' equity	$ 174,137	$ 185,288

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

Puerto Rico Farm Credit, ACA

Consolidated Statements of Operations

(unaudited)

(dollars in thousands)	For the three months ended September 30, 2013	For the three months ended September 30, 2012	For the nine months ended September 30, 2013	For the nine months ended September 30, 2012
Interest Income				
Loans	$ 1,591	$ 1,764	$ 4,832	$ 5,004
Notes receivable from other Farm Credit institutions (Note 5)	225	225	675	675
Total interest income	1,816	1,989	5,507	5,679
Interest Expense				
Notes payable to AgFirst Farm Credit Bank	680	739	2,104	2,260
Net interest income	1,136	1,250	3,403	3,419
Provision for (reversal of allowance for) loan losses	(243)	296	(252)	(56)
Net interest income after provision for (reversal of allowance for) loan losses	1,379	954	3,655	3,475
Noninterest Income				
Loan fees	48	(28)	118	50
Patronage rebate fees	33	51	138	166
Patronage refunds from other Farm Credit institutions	266	275	905	918
Gains (losses) on other property owned, net	(43)	(361)	(339)	(330)
Insurance Fund refunds	—	—	—	679
Other noninterest income	22	18	63	67
Total noninterest income (loss)	326	(45)	885	1,550
Noninterest Expense				
Salaries and employee benefits	691	782	2,361	2,333
Occupancy and equipment	61	55	203	199
Insurance Fund premiums	33	19	100	60
Other operating expenses	320	367	976	1,108
Total noninterest expense	1,105	1,223	3,640	3,700
Net income (loss)	$ 600	$ (314)	$ 900	$ 1,325

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

Puerto Rico Farm Credit, ACA

Consolidated Statements of Comprehensive Income

(unaudited)

(dollars in thousands)	For the three months ended September 30, 2013	For the three months ended September 30, 2012	For the nine months ended September 30, 2013	For the nine months ended September 30, 2012
Net income (loss)	$ 600	$ (314)	$ 900	$ 1,325
Other comprehensive income net of tax				
Employee benefit plans adjustments (Note 8)	13	16	39	48
Comprehensive income	$ 613	$ (298)	$ 939	$ 1,373

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

Puerto Rico Farm Credit, ACA

Consolidated Statements of Changes in Members' Equity

(unaudited)

(dollars in thousands)	Capital Stock and Participation Certificates	Unallocated Retained Earnings	Accumulated Other Comprehensive Income	Total Members' Equity
Balance at December 31, 2011	$ 648	$ 44,886	$ 279	$ 45,813
Comprehensive income		1,325	48	1,373
Capital stock/participation certificates issued/(retired), net	(30)			(30)
Balance at September 30, 2012	$ 618	$ 46,211	$ 327	$ 47,156
Balance at December 31, 2012	$ 604	$ 45,569	$ 286	$ 46,459
Comprehensive income		900	39	939
Capital stock/participation certificates issued/(retired), net	(55)			(55)
Balance at September 30, 2013	$ 549	$ 46,469	$ 325	$ 47,343

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

Puerto Rico 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 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, 2012, are contained in the 2012 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 February 2013 the Financial Accounting Standards Board (FASB) issued Accounting Standards Update (ASU) 2013-04, "Liabilities (Topic 405): Obligations Resulting from Joint and Several Liability Arrangements for which the Total Amount of the Obligation Is Fixed at the Reporting Date," which addresses the recognition, measurement and disclosure of certain obligations including debt arrangements, other contractual obligations, and settled litigation and judicial rulings. The amendments are to be applied retrospectively to all prior periods presented for those obligations resulting from joint and several liability arrangements within the ASU's scope that exist at the beginning of an entity's fiscal year of adoption. An entity may elect to use hindsight for the comparative periods (if it changed its accounting as a result of adopting the amendments in the ASU) and should disclose that fact. The amendments are effective for public entities for fiscal years, and interim periods within those years, beginning after December 15, 2013. For nonpublic entities, the amendments are effective for fiscal years ending after December 15, 2014, and interim periods and annual periods thereafter. Early application is permitted. It is not anticipated the adoption of this guidance will have a material impact on the Association's financial condition or results of operations but could result in additional disclosures.

In February 2013 the FASB issued ASU 2013-02, "Comprehensive Income (Topic 220): Reporting of Amounts Reclassified Out of Accumulated Other Comprehensive Income." The ASU is intended to improve the transparency of reporting reclassifications out of accumulated other comprehensive income (AOCI). The amendments do not change the requirements for reporting net income or other comprehensive income in financial statements. However, the amendments require an entity to provide information about the amounts reclassified out of accumulated other comprehensive income by component. In addition, an entity is required to present, either on the face of the statement where net income is presented or in the notes, significant amounts reclassified out of accumulated other comprehensive income by the respective line items of net income but only if the amount reclassified is required under U.S. GAAP to be reclassified to net income in its entirety in the same reporting period. For other amounts that are not required to be reclassified in their entirety to net income, an entity is required to cross-reference to other disclosures required under U.S. GAAP that provide additional detail about those amounts. For public entities, the amendments are effective prospectively for reporting periods beginning after December 15, 2012. For nonpublic entities, the

amendments are effective prospectively for reporting periods beginning after December 15, 2013. Early application is permitted.

In January 2013, the FASB issued ASU 2013-01 "Balance Sheet (Topic 210): Clarifying the Scope of Disclosures about Offsetting Assets and Liabilities." The ASU clarifies that ordinary trade receivables and payables are not in the scope of ASU 2011-11, "Balance Sheet (Topic 210): Disclosures about Offsetting Assets and Liabilities." Specifically, ASU 2011-11 applies only to derivatives, repurchase agreements and reverse repurchase agreements, and securities borrowing and securities lending transactions that are either offset in accordance with specific criteria or subject to a master netting arrangement or similar agreement. The effective date is the same as that for ASU 2011-11 below.

In December 2011, the FASB issued ASU 2011-11, "Balance Sheet (Topic 210) - Disclosures about Offsetting Assets and Liabilities." The guidance requires an entity to disclose information about offsetting and related arrangements to enable users of its financial statements to understand the effect of those arrangements on its financial position. This includes the effect or potential effect of rights of setoff associated with an entity's recognized assets and recognized liabilities. The requirements apply to recognized financial instruments and derivative instruments that are offset in accordance with accounting guidance and for those recognized financial instruments and derivative instruments that are subject to an enforceable master netting arrangement or similar agreement, irrespective of whether they are offset or not. This guidance is to be applied retrospectively for all comparative periods and is effective for annual reporting periods beginning on or after January 1, 2013, and interim periods within those annual periods. The adoption of this guidance, in conjunction with ASU 2013-01 above, did not impact the Association's financial condition or its results of operations, but did result in additional disclosures.

Other recently issued accounting pronouncements are discussed in the 2012 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 2012 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, 2013	December 31, 2012
Real estate mortgage	$ 93,190	$ 102,418
Production and intermediate-term	24,951	42,328
Processing and marketing	15,959	3,334
Farm-related business	2,470	928
Communication	5,649	970
Energy and water/waste disposal	2,221	2,479
Rural residential real estate	15,366	16,932
Total Loans	$ 159,806	$ 169,389

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, 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	$ 1,120	$ 8,301	$ –	$ –	$ 919	$ –	$ 2,039	$ 8,301
Production and intermediate term	8,171	1,567	–	–	4,967	–	13,138	1,567
Processing and marketing	15,259	–	–	–	579	–	15,838	–
Farm-related business	–	–	–	–	2,239	–	2,239	–
Communication	5,666	–	–	–	–	–	5,666	–
Energy and water/waste disposal	2,224	–	–	–	–	–	2,224	–
Total	$ 32,440	$ 9,868	$ –	$ –	$ 8,704	$ –	$ 41,144	$ 9,868

	December 31, 2012							
	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	$ –	$ 11,523	$ –	$ –	$ 972	$ –	$ 972	$ 11,523
Production and intermediate term	24,577	831	–	–	4,536	–	29,113	831
Processing and marketing	2,606	–	–	–	670	–	3,276	–
Farm-related business	–	–	–	–	882	–	882	–
Communication	975	–	–	–	–	–	975	–
Energy and water/waste disposal	2,479	–	–	–	–	–	2,479	–
Total	$ 30,637	$ 12,354	$ –	$ –	$ 7,060	$ –	$ 37,697	$ 12,354

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, 2013			
	Due less than 1 year	Due 1 Through 5 years	Due after 5 years	Total
Real estate mortgage	$ 20,612	$ 41,347	$ 31,231	$ 93,190
Production and intermediate-term	5,665	13,487	5,799	24,951
Processing and marketing	999	9,013	5,947	15,959
Farm-related business	–	1,813	657	2,470
Communication	(3)	3,319	2,333	5,649
Energy and water/waste disposal	–	222	1,999	2,221
Rural residential real estate	63	172	15,131	15,366
Total Loans	$ 27,336	$ 69,373	$ 63,097	$ 159,806
Percentage	17.11%	43.41%	39.48%	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, 2013	December 31, 2012
Real estate mortgage:		
Acceptable	85.27%	86.59%
OAEM	1.31	0.76
Substandard/doubtful/loss	13.42	12.65
	100.00%	100.00%
Production and intermediate-term:		
Acceptable	74.82%	79.11%
OAEM	6.10	1.75
Substandard/doubtful/loss	19.08	19.14
	100.00%	100.00%
Processing and marketing:		
Acceptable	97.72%	44.56%
OAEM	–	14.13
Substandard/doubtful/loss	2.28	41.31
	100.00%	100.00%
Farm-related business:		
Acceptable	100.00%	100.00%
OAEM	–	–
Substandard/doubtful/loss	–	–
	100.00%	100.00%

	September 30, 2013	December 31, 2012
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	94.69%	92.30%
OAEM	0.82	1.73
Substandard/doubtful/loss	4.49	5.97
	100.00%	100.00%
Total Loans:		
Acceptable	86.73%	84.81%
OAEM	1.80	1.35
Substandard/doubtful/loss	11.47	13.84
	100.00%	100.00%

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

	September 30, 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	$ 2,263	$ 8,815	$ 11,078	$ 82,506	$ 93,584	$ –
Production and intermediate-term	981	1,244	2,225	22,874	25,099	–
Processing and marketing	–	365	365	15,629	15,994	–
Farm-related business	–	–	–	2,480	2,480	–
Communication	–	–	–	5,657	5,657	–
Energy and water/waste disposal	–	–	–	2,222	2,222	–
Rural residential real estate	612	231	843	14,571	15,414	–
Total	$ 3,856	$ 10,655	$ 14,511	$ 145,939	$ 160,450	$ –

	December 31, 2012					
	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	$ 5,984	$ 5,658	$ 11,642	$ 91,092	$ 102,734	$ –
Production and intermediate-term	–	1,786	1,786	40,666	42,452	–
Processing and marketing	–	–	–	3,360	3,360	–
Farm-related business	–	–	–	934	934	–
Communication	–	–	–	971	971	–
Energy and water/waste disposal	–	–	–	2,491	2,491	–
Rural residential real estate	671	223	894	16,082	16,976	–
Total	$ 6,655	$ 7,667	$ 14,322	$ 155,596	$ 169,918	$ –

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, 2013	December 31, 2012
Non-accrual loans:		
Real estate mortgage	$ 11,624	$ 9,714
Production and intermediate-term	1,721	2,949
Processing and marketing	366	560
Rural residential real estate	311	701
Total nonaccrual loans	$ 14,022	$ 13,924
Accruing restructured loans:		
Real estate mortgage	$ 135	$ –
Production and intermediate-term	1,223	1,338
Total accruing restructured loans	$ 1,358	$ 1,338
Accruing loans 90 days or more past due:	$ –	$ –
Total nonperforming loans	$ 15,380	$ 15,262
Other property owned	3,244	3,498
Total nonperforming assets	$ 18,624	$ 18,760
Non-accrual loans as a percentage of total loans	8.77%	8.22%
Nonperforming assets as a percentage of total loans and other property owned	11.42%	10.85%
Nonperforming assets as a percentage of capital	39.34%	40.38%

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, 2013	December 31, 2012
Impaired non-accrual loans:		
Current as to principal and interest	$ 2,653	$ 2,611
Past due	11,369	11,313
Total impaired non-accrual loans	14,022	13,924
Impaired accrual loans:		
Restructured	1,358	1,338
90 days or more past due	–	–
Total impaired accrual loans	1,358	1,338
Total impaired loans	$ 15,380	$ 15,262

The following tables present additional impaired loan information at period end.

	September 30, 2013			Quarter Ended September 30, 2013		Nine Months Ended September 30, 2013	
	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	$ 4,734	$ 7,274	$ 1,012	$ 4,780	$ 20	$ 4,929	$ 55
Production and intermediate-term	2,376	5,528	1,076	2,400	10	2,475	27
Processing and marketing	355	560	85	359	2	370	4
Rural residential real estate	–	–	–	–	–	–	–
Total	$ 7,465	$ 13,362	$ 2,173	$ 7,539	$ 32	$ 7,774	$ 86
Impaired loans with no related allowance for credit losses:							
Real estate mortgage	$ 7,025	$ 7,643	$ –	$ 7,096	$ 30	$ 7,317	$ 81
Production and intermediate-term	568	598	–	574	3	591	7
Processing and marketing	11	–	–	10	–	10	–
Rural residential real estate	311	374	–	314	1	324	4
Total	$ 7,915	$ 8,615	$ –	$ 7,994	$ 34	$ 8,242	$ 92
Total impaired loans:							
Real estate mortgage	$ 11,759	$ 14,917	$ 1,012	$ 11,876	$ 50	$ 12,246	$ 136
Production and intermediate-term	2,944	6,126	1,076	2,974	13	3,066	34
Processing and marketing	366	560	85	369	2	380	4
Rural residential real estate	311	374	–	314	1	324	4
Total	$ 15,380	$ 21,977	$ 2,173	$ 15,533	$ 66	$ 16,016	$ 178

	December 31, 2012			Year Ended December 31, 2012	
	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	$ 2,199	$ 2,300	$ 529	$ 2,692	$ 44
Production and intermediate-term	3,653	6,961	1,226	4,473	72
Processing and marketing	550	560	280	673	11
Rural residential real estate	378	408	38	462	8
Total	$ 6,780	$ 10,229	$ 2,073	$ 8,300	$ 135
Impaired loans with no related allowance for credit losses:					
Real estate mortgage	$ 7,515	$ 9,886	$ –	$ 9,201	$ 150
Production and intermediate-term	634	665	–	776	13
Processing and marketing	10	–	–	13	–
Rural residential real estate	323	400	–	396	6
Total	$ 8,482	$ 10,951	$ –	$ 10,386	$ 169
Total impaired loans:					
Real estate mortgage	$ 9,714	$ 12,186	$ 529	$ 11,893	$ 194
Production and intermediate-term	4,287	7,626	1,226	5,249	85
Processing and marketing	560	560	280	686	11
Rural residential real estate	701	808	38	858	14
Total	$ 15,262	$ 21,180	$ 2,073	$ 18,686	$ 304

Unpaid principal balance represents the contractual principal balance of the loan.

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 June 30, 2013	$ 955	$ 1,978	$ 1,139	$ 16	$ 3	$ 205	$ 4,296
Charge-offs	(5)	–	(92)	–	–	–	(97)
Recoveries	1	–	–	–	–	–	1
Provision for loan losses	310	(189)	(368)	(3)	(1)	8	(243)
Loan type reclassification	144	(144)	–	–	–	–	–
Balance at September 30, 2013	$ 1,405	$ 1,645	$ 679	$ 13	$ 2	$ 213	$ 3,957
Balance at December 31, 2012	$ 1,336	$ 1,685	$ 1,241	$ 16	$ 3	$ 127	$ 4,408
Charge-offs	(7)	–	(195)	–	–	–	(202)
Recoveries	2	1	–	–	–	–	3
Provision for loan losses	(70)	103	(367)	(3)	(1)	86	(252)
Loan type reclassification	144	(144)	–	–	–	–	–
Balance at September 30, 2013	$ 1,405	$ 1,645	$ 679	$ 13	$ 2	$ 213	$ 3,957
Balance at June 30, 2012	$ 1,709	$ 615	$ 670	$ 10	$ 12	$ 174	$ 3,190
Charge-offs	(256)	–	(1)	–	–	–	(257)
Recoveries	–	–	–	–	–	–	–
Provision for loan losses	(274)	45	574	3	(8)	(44)	296
Balance at September 30, 2012	$ 1,179	$ 660	$ 1,243	$ 13	$ 4	$ 130	$ 3,229
Balance at December 31, 2011	$ 1,359	$ 657	$ 1,273	$ 7	$ 2	$ 184	$ 3,482
Charge-offs	(303)	(46)	(1)	–	–	–	(350)
Recoveries	153	–	–	–	–	–	153
Provision for loan losses	(30)	49	(29)	6	2	(54)	(56)
Balance at September 30, 2012	$ 1,179	$ 660	$ 1,243	$ 13	$ 4	$ 130	$ 3,229
Loans individually evaluated for impairment	$ 1,012	$ 1,076	$ 85	$ –	$ –	$ –	$ 2,173
Loans collectively evaluated for impairment	393	569	594	13	2	213	1,784
Balance at September 30, 2013	$ 1,405	$ 1,645	$ 679	$ 13	$ 2	$ 213	$ 3,957
Loans individually evaluated for impairment	$ 529	$ 1,226	$ 280	$ –	$ –	$ 38	$ 2,073
Loans collectively evaluated for impairment	807	459	961	16	3	89	2,335
Balance at December 31, 2012	$ 1,336	$ 1,685	$ 1,241	$ 16	$ 3	$ 127	$ 4,408
Recorded investment in loans outstanding:							
Loans individually evaluated for impairment	$ 11,476	$ 2,854	$ 365	$ –	$ –	$ 231	$ 14,926
Loans collectively evaluated for impairment	82,108	22,245	18,109	5,657	2,222	15,183	145,524
Ending balance at September 30, 2013	$ 93,584	$ 25,099	$ 18,474	$ 5,657	$ 2,222	$ 15,414	$ 160,450
Loans individually evaluated for impairment	$ 9,251	$ 4,221	$ 560	$ –	$ –	$ 491	$ 14,523
Loans collectively evaluated for impairment	93,483	38,231	3,734	971	2,491	16,485	155,395
Ending balance at December 31, 2012	$ 102,734	$ 42,452	$ 4,294	$ 971	$ 2,491	$ 16,976	$ 169,918

**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 activity that occurred during the periods presented related to TDRs. There were no TDRs for the three months ended September 30, 2012.

	Three months ended September 30, 2013			
	Pre-modification Outstanding Recorded Investment			
	Interest Concessions	Principal Concessions	Other Concessions	Total
Troubled debt restructurings:				
Real estate mortgage	$ –	$ 271	$ –	$ 271
Total	$ –	$ 271	$ –	$ 271

Three months ended September 30, 2013						
	Post-modification Outstanding Recorded Investment				Effects of Modification	
	Interest Concessions	Principal Concessions	Other Concessions	Total	Provisions	Charge-offs
Troubled debt restructurings:						
Real estate mortgage	$ –	$ 268	$ –	$ 268	$ –	$ –
Total	$ –	$ 268	$ –	$ 268	$ –	$ –

Nine months ended September 30, 2013				
	Pre-modification Outstanding Recorded Investment			
	Interest Concessions	Principal Concessions	Other Concessions	Total
Troubled debt restructurings:				
Real estate mortgage	$ –	$ 399	$ –	$ 399
Total	$ –	$ 399	$ –	$ 399

Nine months ended September 30, 2013						
	Post-modification Outstanding Recorded Investment				Effects of Modification	
	Interest Concessions	Principal Concessions	Other Concessions	Total	Provisions	Charge-offs
Troubled debt restructurings:						
Real estate mortgage	$ –	$ 396	$ –	$ 396	$ 1	$ –
Total	$ –	$ 396	$ –	$ 396	$ 1	$ –

Nine months ended September 30, 2012				
	Pre-modification Outstanding Recorded Investment			
	Interest Concessions	Principal Concessions	Other Concessions	Total
Troubled debt restructurings:				
Real estate mortgage	$ –	$ –	$ 34	$ 34
Total	$ –	$ –	$ 34	$ 34

Nine months ended September 30, 2012						
	Post-modification Outstanding Recorded Investment				Effects of Modification	
	Interest Concessions	Principal Concessions	Other Concessions	Total	Provisions	Charge-offs
Troubled debt restructurings:						
Real estate mortgage	$ –	$ –	$ 19	$ 19	$ (12)	$ –
Total	$ –	$ –	$ 19	$ 19	$ (12)	$ –

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	
	September 30, 2013	December 31, 2012	September 30, 2013	December 31, 2012
Real estate mortgage	$ 5,611	$ 4,779	$ 5,476	$ 4,779
Production and intermediate-term	1,223	2,529	–	1,191
Processing and marketing	365	560	365	560
Total Loans	$ 7,199	$ 7,868	$ 5,841	$ 6,530
Additional commitments to lend	$ –	$ –		

NOTE 3 – 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 4 – 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,	
	2013	2012	2013	2012
Pension	$ 249	$ 263	$ 746	$ 788
401(k)	17	14	55	40
Other postretirement benefits	39	45	117	136
Total	$ 305	$ 322	$ 918	$ 964

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

	Actual YTD Through 9/30/13	Projected Contributions For Remainder of 2013	Projected Total Contributions 2013
Pension	$ –	$ 804	$ 804
Other postretirement benefits	87	14	101
Total	$ 87	$ 818	$ 905

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, 2013.

Further details regarding employee benefit plans are contained in the 2012 Annual Report to Shareholders.

NOTE 5 – NOTES RECEIVABLE FROM OTHER FARM CREDIT INSTITUTIONS

In September 2008, the Association used capital reserves to purchase $10,000 total of fixed rate unsecured subordinated notes issued by two other associations in the District, both notes due in 2018. The notes receivable are subordinate to all other categories of creditors of the issuing associations, including any claims of the Bank and general creditors, but are senior to all classes of shareholders of the issuing associations. The notes receivable are not considered System debt, and thus are not guaranteed by the System and not insured by the Insurance Corporation. Since the notes receivable are only guaranteed by the issuing associations, repayment could be negatively impacted by funding, credit, and/or counterparty risks encountered by the two issuing associations in their business operations. As of the end of 2012, one of the two associations had merged with another association in the district and is considered by management to be acceptable risk as when the debt was issued. The second association continues to perform at an acceptable level and management does not consider it to carry higher than average risk. Both associations are expected to pay their principal debt in October 2013, when the prepayment option can be exercised. Management will continue to inform the Board of Directors on the financial performance of those Associations on a quarterly basis.

The notes receivable bear interest at an annual fixed rate of 9.00 percent, payable on the fifteenth day of each month, beginning on October 15, 2008. Interest will be deferred if, as of the fifth business day prior to an interest payment date, any applicable minimum regulatory capital ratios are not satisfied by the issuing association(s). A deferral period may not last for more than five consecutive years or beyond the maturity date of the note(s). During such a period, the issuing association(s) may not declare or pay any dividends or patronage refunds, among other certain restrictions, until interest payments are resumed and all deferred interest has been paid. The note(s) may be redeemed, at the issuing Association's option, on October 15, 2013, or upon the occurrence of certain defined regulatory events, at a redemption price of 100 percent of the principal amount, plus any accrued but unpaid interest to the date of redemption, provided the issuing association(s) have made payment in full of all amounts then due in respect of their senior indebtedness.

NOTE 6 – 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.

The Association failed to meet its earnings covenant under the GFA at December 31, 2012. The default allows the Bank to accelerate repayment of all indebtedness. The Bank approved a waiver of the GFA default and allowed the Association to continue to borrow under the GFA pursuant to a special credit agreement (SCA). At March 31, 2013, the Association failed to meet its earnings covenant under the SCA, and the Bank provided a waiver of the SCA earnings covenant default effective March 31, 2013, subject to certain terms and conditions. Such waiver expires December 31, 2013.

NOTE 7 – 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 0.71 percent of the issued stock of the Bank as of September 30, 2013 net of any reciprocal investment. As of that date, the Bank's assets totaled $28.5 billion and shareholders' equity totaled $2.4 billion. The Bank's earnings were $350 million for the first nine months of 2013. In addition, the Association has no investment related to other Farm Credit institutions. The classifications of the Association's financial instruments within the fair value hierarchy are as follows:

Level 1

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

For cash, the carrying value is primarily utilized as a reasonable estimate of fair value.

Level 2

Level 2 inputs to the valuation methodology 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. The Association had no Level 2 assets or liabilities measured at fair value.

Level 3

Level 3 inputs to the valuation methodology 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.

Because no active market exists for the Association's accruing loans, fair value is estimated by discounting the expected future cash flows using the Association's current interest rates at which similar loans currently would be made to borrowers with similar credit risk. The loan portfolio is segregated into pools of loans with homogeneous characteristics based upon repricing and credit risk. Expected future cash flows and interest rates reflecting appropriate credit risk are separately determined for each individual pool.

Fair values of loans in a nonaccrual status are estimated to be the carrying amount of the loan less specific reserves. Certain loans evaluated for impairment under FASB guidance have fair values based upon the underlying collateral, as the loans were collateral-dependent. Specific reserves were established for these loans when the value of the collateral, less estimated cost to sell, was less than the principal balance of the loan. The fair value measurement process uses independent appraisals and other market-based information, but in many cases it also requires significant input based on management's knowledge of and judgment about current market conditions, specific issues relating to the collateral and other matters.

The notes payable are segregated into pricing pools according to the types and terms of the loans (or other assets) which they fund. Fair value of the notes payable is estimated by discounting the anticipated cash flows of each pricing pool using the current rate that would be charged for additional borrowings. For purposes of this estimate it is assumed the cash flow on the notes is equal to the principal payments on the Association's loan receivables. This assumption implies that earnings on the Association's interest margin are used to fund operating expenses and capital expenditures.

Other property owned is classified as a level 3 asset. The fair value is generally determined using formal appraisals of each individual property. These assets are held for sale. Costs to sell represent transaction costs and are not included as a component of the fair value of other property owned. Other property owned consists of real and personal property acquired through foreclosure or deed in lieu of foreclosure and is carried as an asset held for sale, which is generally not its highest and best use. These properties are part of the Association's credit risk mitigation efforts, not its ongoing business. In addition, FCA regulations require that these types of property be disposed of within a reasonable period of time.

For notes receivable from other Farm Credit institutions, fair value is determined by discounting the expected future cash flows using appropriate interest rates for similar assets.

For commitments to extend credit, the estimated market value of off-balance-sheet commitments is minimal since the committed rate approximates current rates offered for commitments with similar rate and maturity characteristics; therefore, the related credit risk is not significant.

The following tables present 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
Balance at January 1, 2013	$ 17
Issuances	–
Settlements	(11)
Transfers in and/or out of level 3	–
Balance at September 30, 2013	$ 6

	Standby Letters Of Credit
Balance at January 1, 2012	$ 22
Issuances	–
Settlements	(10)
Transfers in and/or out of level 3	–
Balance at September 30, 2012	$ 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 instuments 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	$ 16,633	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 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 Nine Months Ended September 30, 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	$ 13,207	$ –	$ –	$ 13,207	$ 13,207	$ (299)
Other property owned	3,244	–	–	3,426	3,426	(341)
Nonrecurring Assets	$ 16,451	$ –	$ –	$ 16,633	$ 16,633	$ (640)
Other Financial Instruments						
Assets:						
Cash	$ 44	$ 44	$ –	$ –	$ 44	
Loans	142,642	–	–	141,059	141,059	
Notes receivable from other Farm Credit institutions	10,000	–	–	10,006	10,006	
Other Assets	$ 152,686	$ 44	$ –	$ 151,065	$ 151,109	
Liabilities:						
Notes payable to AgFirst Farm Credit Bank	$ 123,790	$ –	$ –	$ 123,942	$ 123,942	
Other Liabilities	$ 123,790	$ –	$ –	$ 123,942	$ 123,942	

	At or for the Year Ended December 31, 2012					
	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	$ 17	$ –	$ –	$ 17	$ 17	
Recurring Liabilities	$ 17	$ –	$ –	$ 17	$ 17	
Nonrecurring Measurements						
Assets:						
Impaired loans	$ 13,189	$ –	$ –	$ 13,189	$ 13,189	$ (785)
Other property owned	3,498	–	–	3,672	3,672	(533)
Nonrecurring Assets	$ 16,687	$ –	$ –	$ 16,861	$ 16,861	$ (1,318)
Other Financial Instruments						
Assets:						
Cash	$ 214	$ 214	$ –	$ –	$ 214	
Loans	151,792	–	–	150,685	150,685	
Notes receivable from other Farm Credit institutions	10,000	–	–	10,330	10,330	
Other Assets	$ 162,006	$ 214	$ –	$ 161,015	$ 161,229	
Liabilities:						
Notes payable to AgFirst Farm Credit Bank	$ 135,882	$ –	$ –	$ 136,384	$ 136,384	
Other Liabilities	$ 135,882	$ –	$ –	$ 136,384	$ 136,384	

NOTE 8 - ACCUMULATED OTHER COMPREHENSIVE INCOME

The following tables present activity related to AOCI for the three month and nine month periods ended September 30:

	Changes in Accumulated Other Comprehensive income by Component *(a)*			
	Three Months		Year to Date	
	2013	2012	2013	2012
Employee Benefit Plans:				
Balance at beginning of period	$ 312	$ 311	$ 286	$ 279
Other comprehensive income before reclassifications	–	–	–	–
Amounts reclassified from AOCI	13	16	39	48
Net current period other comprehensive income	13	16	39	48
Balance at end of period	$ 325	$ 327	$ 325	$ 327

	Reclassifications Out of Accumulated Other Comprehensive Income *(b)*				
	Three Months		Year to Date		
	2013	2012	2013	2012	Income Statement Line Item
Defined Benefit Pension Plans:					
Periodic pension costs	$ (13)	$ (16)	$ (39)	$ (48)	See footnote 4.
Net amounts reclassified	$ (13)	$ (16)	$ (39)	$ (48)	

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

NOTE 9 – REGULATORY ENFORCEMENT MATTERS

As previously disclosed, on March 17, 2011 the 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 SA 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 several 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 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 strengthen 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.

NOTE 10 – SUBSEQUENT EVENTS

The Association has evaluated subsequent events and has determined that, except as described below, there are none requiring disclosure through November 7, 2013, which is the date the financial statements were issued.

On October 15, 2013, the Association's notes receivable from other Farm Credit institutions were redeemed in full by the issuing associations. See Note 5, *Notes Receivable from Other Farm Credit Institutions*.

On October 21, 2013, AgFirst's Board of Directors declared a special patronage distribution to be paid on January 1, 2014. The Association will receive approximately $1,823 which will be recorded in October 2013 as patronage refunds from other Farm Credit institutions.