Puerto Rico Farm Credit, ACA

THIRD QUARTER 2023

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CERTIFICATION

The undersigned certify that we have reviewed the September 30, 2023 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.

Rafael J. Borges
Chairman of The Board of Directors

Ricardo L. Fernández
Chief Executive Officer

Antonio E. Marichal
Chairman of the Audit Committee

Frances Marquez
Comptroller

November 8, 2023

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 period ended September 30, 2023. These comments should be read in conjunction with the accompanying consolidated financial statements, notes to the consolidated financial statements, and the 2022 annual report of the Association. The accompanying consolidated financial statements were prepared under the oversight of the Audit Committee of the Board of Directors.

The Association obtains funding through a borrowing relationship with AgFirst Farm Credit Bank (AgFirst or Bank). The Association is materially affected by the financial condition and results of operations of the Bank.

CLIMATE CHANGE

Agricultural production is and always has been vulnerable to weather events and climate change. The USDA has recognized that the changing climate presents threats to U.S. and global agricultural production and rural communities. The impact of climate change including its effect on weather is, and will continue to be, a challenge for agricultural producers. Among the risks of climate change are:

- rising average temperatures,
- more frequent and severe storms,
- more forest fires, and
- extremes in flooding and droughts.

However, risks associated with climate change are mitigated, to some degree, by agricultural producers' ability to navigate changing industry dynamics from numerous perspectives, including trade, government policy, consumer preferences and weather. Producers regularly adopt new technologies, agronomic practices and financial strategies in response to evolving trends to ensure their competitiveness.

ECONOMIC CONDITIONS

Puerto Rico has endured a prolonged economic downturn for more than 16 years. GDP continues a downward trend that started in 2006 with a few upticks on years after unique events have led to federal funds to increase on the island. Since then, Puerto Rico's economy has struggled for multiple reasons, including the lack of a sustainable economic plan, natural disasters and the pandemic. This economic environment is expected to continue over the next 12 months with the added component of the Ukraine and Israel wars, and the global supply chain disruption which has had an impact on farming operations on the island.

The Fiscal Planning Board continues to work on stabilizing the central government finances and settle the debt for the government-owned power company. The island began repaying certain debt but additional work is required through many of the government agencies.

Puerto Rico's economy will remain stable but fragile amidst the continuing impact of the pandemic, the Ukraine and Israel wars and the impact of Hurricane Fiona. The Association expects to continue to improve performance as interest in local agriculture slowly grows. The Board of Directors and Management will continue to work with the government and other entities in moving forward the island's agricultural sector. Economists continue to forecast a minor increase in GDP of 1% due to additional federal funds being received. The forecast over the next three years is for a stable economy which is good for the island as it continues to recover from the major events already discussed. The only impediment in maintaining economic stability is the risk of interest rates continuing to rise while inflation continues to soar to levels not seen in decades.

Through all this, the agricultural sector's outlook is stable and farmers will continue to fair well under the current market conditions. This should allow farmers to continue managing their operations profitably and maintain the credit quality of the Association's portfolio while limiting loan growth opportunities.

The local dairy industry production remained stable in 2023 compared to 2022. The Association continues to monitor events within the industry and their potential impact on the performance of the dairy portfolio. The Association lends almost 17.20% percent of total chartered territory loans to the dairy industry and has implemented risk management practices to mitigate concentration risk.

Other agricultural sectors do not represent significant risk for the association. Management monitors all sectors and does not anticipate any adverse impact to the portfolio in 2023.

The Association will continue to find creative ways to fulfill its public mission. Leadership of the ACA believes that agriculture is still viable on the island and has many opportunities ahead. However, the Board of Directors and Management remain cautious of the Association's ability to grow the portfolio under the prevailing economic and political environment.

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 (PL), originated by other Farm Credit System entities and non-system entities. The Association's predominant chartered territory (CT) agricultural commodities were dairy, fruits (including plantains and coffee) and field crops which totaled approximately $67,079 or 37.10% percent of the total gross principal balance, net of sold loans, at September 30, 2023.

The gross accruing loan volume of the Association at September 30, 2023 was $185,838 a decrease of $112 or 0.06 percent as compared to $185,949 at December 31, 2022. Loans originated within the Association's chartered territory were higher by approximately $1,140 and participation purchased loans decreased by approximately $1,252. The loan volume decrease was a result of scheduled repayments and payoffs and to a participation loan placed as non-accrual during the first quarter of 2023.

Total loans net of participation loans sold at September 30, 2023 totaled $179,615 as compared to $179,723 at December 31, 2022. Net loans made up 96.33 percent of total assets at September 30, 2023, as compared to 96.03 percent at December 31, 2022.

Non-accrual loans totaled $5,592 or 3.11 percent of total loans at September 30, 2023, compared to $5,692 or 3.17 percent of total loans at December 31, 2022.

The overall delinquency rate for the accruing loan portfolio increased to $6,224 during the third quarter from $5,196 in the second quarter. Management does not expect high risk loans to increase significantly by the end of the year.

The Association adopted the Financial Accounting Standards Board (FASB) guidance entitled "Measurement of Credit Losses on Financial Instruments" and other subsequently issued accounting standards updates related to current expected credit losses (CECL) on January 1, 2023. This guidance replaced the current incurred loss impairment methodology with a single allowance framework for financial assets carried at amortized cost and certain off-balance sheet credit exposures. This change of methodology did not have any material impact on the allowance calculation.

The allowance for credit losses increased $3,125 to $4,314 at September 30, 2023 from $1,189 at December 31, 2022. The increase was primarily related to a PL placed as non-accrual during the period. Specific and general reserves for CT loans remained stable. CECL new methodology slightly impacted the allowance by $11. Management will continue to monitor certain risks and other factors that may increase the risk of the portfolio, such as climate conditions, government fiscal policy and overall economic conditions on the island.

During 2023, charge-offs of $1 were recorded and recoveries of $79 were recognized on payments received for CT nonaccrual loans. The Association is actively marketing acquired properties and may incur additional accounting losses or gains as sales are completed.

RESULTS OF OPERATIONS

For the three months ended September 30, 2023

The Association recorded a net income for the three months ended September 30, 2023 of $224 as compared to a net loss of $94 for the same period in 2022.

Net interest income was $1,478 for the three months ended September 30, 2023 compared to $831 for the same period in 2022, representing an increase of $647 or 77.86 percent primarily resulting from higher interest rates.

Provision for credit losses was $520 for the three months ended September 30, 2023 compared to $62 for the same period in 2022, mainly related to the PL loan placed as non-accrual during the first quarter of 2023.

Noninterest income for the three months ended September 30, 2023 totaled $251 compared to $282 for the same period of 2022, resulting in a decrease of $31 or 10.99 percent, mainly due to an increase in the loan fees.

Noninterest expense was $985 for the three months ended September 30, 2023 as compared to $1,145 for the same period in 2022, resulting in a decrease of $160 or 13.97 percent. This decrease was primarily driven by lower purchase services by $97 and a recovery of $97 from a nonaccrual loan reninstated as accrual during the current period, mainly offset by higher training and public/member relations expenses by $34.

For the nine months ended September 30, 2023

Net loss for the nine months ended September 30, 2023 totaled $1,098 compared to net income of $287 for the same period in 2022, a decrease of $1,385. Association's net loss was directly impacted by an specific provision of $3,343. Excluding such provision our net income would have ended at $2,245.

Net interest income increased $1,411 or 46.98 percent to $4,414 for the nine months ended September 30, 2023, from $3,003 for the same period in 2022 due to higher interest rates as still increasing prices as part of inflation control efforts from the Federal Reserve.

Provision for credit losses was $3,147 for the nine months ended September 30, 2023 compared to $88 for the same period in 2022, an increase of $3,059, mainly related to the PL loan placed as non-accrual in the first quarter of 2023 impacting by $3,343.

Noninterest income for the nine months ended September 30, 2023 totaled $927 as compared to $832 for the same period in 2022, an increase of $95 or 11.42 percent, mainly from higher loan fees.

Noninterest expense was $3,292 for the nine months ended September 30, 2023 as compared to $3,460 for the same period in 2022, a decrease of $168 or 4.86 percent.

Although the Association is subject to federal income tax, the Association does not expect to incur a federal tax liability in 2023.

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, 2023 was $120,172 as compared to $122,638 at December 31, 2022. The decrease of $2,466 or 2.01 percent is primarily due to a decrease in loan volume outstanding during the period. The Association had no lines of credit outstanding with third parties as of September 30, 2023.

Funds Management

The Bank and the Association manage assets and liabilities to provide a broad range of loan products and funding options, which are designed to allow the Association to be competitive in all interest rate environments. The primary objective of the asset/liability management process is to provide stable earnings, while maintaining adequate capital levels by managing exposure to credit and interest rate risks.

Demand for loan types is a driving force in establishing a funds management strategy. The Association offers fixed and variable rate loan products that are marginally priced according to financial market rates. Variable rate loans may be indexed to market indices such as the Prime Rate or the Secured Overnight Financing Rate (SOFR). Fixed rate loans are priced based on the current cost of Farm Credit System debt of similar terms to maturity. The Association does not offer or include adjustable rate mortgages (ARMS) in its portfolio of loan products.

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, 2023 decreased by $993 or 1.64 percent to $59,473 from December 31, 2022 total of $60,466. The decrease was primarily attributable to year-to-date net loss.

Total capital stock and participation certificates were $515 at September 30, 2023 compared to $514 at December 31, 2022. The increase of $1 was the result of the capital stock and participation certificates issued and redeemed in the normal course of business.

Unallocated retained earnings was $58,958 at September 30, 2023 compared to $59,952 at December 31, 2022.

Key financial condition ratios were as follows:

	9/30/2023	12/31/2022
Total Members' Equity to Asset	2.06%	2.07%

Regulatory Capital Ratios

The Association's regulatory capital ratios are shown in the following table:

	Regulatory Minimum, Including Buffer*	9/30/2023	12/31/2022	9/30/2022
Common Equity Tier 1 (CET1) Capital Ratio	7.0%	32.64%	32.27%	30.88%
Tier 1 Capital Ratio	8.5%	32.64%	32.27%	30.88%
Total Regulatory Capital Ratio	10.5%	33.90%	33.08%	31.65%
Permanent Capital Ratio	7.0%	33.04%	32.50%	31.10%
Tier 1 Leverage Ratio**	5.0%	32.44%	31.32%	29.78%
Unallocated Retained Earnings (URE) and URE Equivalents Leverage Ratio	1.5%	32.15%	31.05%	29.51%

**Includes fully phased-in capital conservation buffers which became effective on January 1, 2020.*
***The Tier 1 Leverage Ratio must include a minimum of 1.50% of URE and URE Equivalents.*

The FCA sets minimum regulatory capital adequacy requirements for System banks and associations. The requirements are based on regulatory ratios as defined by the FCA and include common equity tier 1 (CET1), tier 1, total capital, permanent capital, tier 1 leverage, and unallocated retained earnings (URE) and URE equivalents leverage ratios.

The permanent capital, CET1, tier 1, and total capital ratios are calculated by dividing the three-month average daily balance of the capital numerator, as defined by the FCA, by a risk-adjusted asset base. Unlike these ratios, the tier 1 leverage and URE and URE equivalents leverage ratios do not incorporate any risk-adjusted weighting of assets. Risk-adjusted assets refer to the total dollar amount of the institution's assets adjusted by an appropriate credit conversion factor as defined by regulation. Generally, higher credit conversion factors are applied to assets with more inherent risk. The tier 1 leverage and URE and URE equivalents leverage ratios are calculated by dividing the three-month average daily balance of the capital numerator, as defined by the FCA, by the three-month average daily balance of total assets adjusted for regulatory deductions.

If the capital ratios fall below the minimum regulatory requirements, including the buffer amounts, capital distributions (equity redemptions, dividends, and patronage) and discretionary senior executive bonuses are restricted or prohibited without prior FCA approval. For all periods presented, the Association exceeded minimum regulatory standards for all capital ratios. There are no trends, commitments, contingencies, or events that are likely to affect the Association's ability to meet regulatory minimum capital standards and capital adequacy requirements.

REGULATORY MATTERS

On October 12, 2023, the Farm Credit Administration approved a final rule governing the Farm Credit System's service to young, beginning, and small (YBS) farmers and ranchers. The rule requires banks that fund the direct-lender associations to annually review and approve the association YBS programs. The rule also requires direct-lender associations to enhance the strategic plan of its YBS program. The strategic plan must contain specific elements that will be evaluated as part of a rating system to measure year-over-year internal progress, which would allow the Farm Credit Administration to compare the success of the direct-lender' association's YBS program. The final rule becomes effective on February 1, 2024.

On October 5, 2023, the Farm Credit Administration approved a final rule on cyber risk management that requires each System institution to develop and implement a comprehensive, written cyber risk management program. Each institution's cyber risk plan must require the institution to take the actions to assess internal and external risk factors, identify potential system and software vulnerabilities, establish a risk management program for the risks identified, develop a cyber risk training program, set policies for managing third-party relationships, maintain robust internal controls and establish board reporting requirements. The final rule will become effective on January 1, 2025.

On April 14, 2022, the FCA approved a final rule that amends certain regulations to address changes in accounting principles generally accepted in the United States. Such changes reflect the Current Expected Credit Losses (CECL) methodology that replaced the incurred loss methodology upon adoption. Credit loss allowances related to loans, lessor's net investments in leases, and held-to-maturity debt securities are included in a System institution's Tier 2 capital up to 1.25 percent of the System institution's total risk weighted assets. Credit loss allowances for available-for-sale debt securities and purchased credit impaired assets are not eligible for inclusion in a System institution's Tier 2 capital. The regulation did not include a transition phase-in period for the CECL day 1 cumulative effect adjustment to retained earnings on a System institution's regulatory capital ratios. In addition, the regulation did not include an exclusion for the CECL day 1 cumulative effective adjustment from the "safe harbor" deemed prior approval provision for distributions. The rule became effective on January 1, 2023.

On August 26, 2021, the FCA issued a proposed rule to revise its regulatory capital requirements to define and establish risk-weightings for High Volatility Commercial Real Estate (HVCRE) by assigning a 150 percent risk-weighting to such exposures, instead of the current 100 percent. The proposed rule would ensure that the FCA's rule remains comparable with the capital rule of other federal banking regulatory agencies and recognizes the increased risk posed by HVCRE exposures. The public comment period ended on January 24, 2022.

LIBOR Transition

U.S. dollar LIBOR settings (including with respect to overnight, one, three, six, and twelve month tenors of U.S. dollar LIBOR) were discontinued or declared non-representative immediately after June 30, 2023.

The Association implemented LIBOR transition plans in accordance with FCA's guidance to address the risks associated with the discontinuation of LIBOR. See the Association's 2022 Annual Report for further discussion on the LIBOR transition plans.

Prior to the discontinuance of LIBOR, the Association exposure to LIBOR arose from loans made to customers, investment securities purchased, and Systemwide Debt Securities issued by the Funding Corporation on the Bank's behalf. To the extent necessary, substantially all financial instruments that referenced LIBOR were amended to incorporate adequate fallbacks, including, where appropriate, the Secured Overnight Finance Rate (SOFR)-based fallbacks recommended by the Alternative Reference Rates Committee (ARRC). To the extent that any Association contracts were not amended to include adequate fallback provisions to replace LIBOR, such contracts were amended by operation of law under the federal Adjustable Interest Rate (LIBOR) Act and rules thereunder to include a statutorily designated fallback to LIBOR. Under the Federal Reserve Board's rule implementing certain provisions of the LIBOR Act (Regulation ZZ), on the LIBOR replacement date (the first London banking day after June 30, 2023), the Federal Reserve Board-selected benchmark replacement, based on the SOFR and including any tenor spread adjustment as provided by Regulation ZZ, automatically replaced references to overnight, one, three, six, and twelve month LIBOR in all remaining contracts that did not mature before the LIBOR replacement date and did not contain adequate fallback language.

The Associations' variable-rate financial instruments outstanding with LIBOR exposure as of September 30, 2023 equaled 0.003% of total assets.

OTHER MATTERS

During October 2022, the Association sold various Other Property Owned properties with a total recorded investment of $916 and recorded gains on sale of $4,115 and write down recoveries of $719.

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 2022 Annual Report to Shareholders for recently adopted accounting pronouncements.

There were no ASUs issued by the Financial Accounting Standards Board (FASB) during the quarter that impacted the Association's Financial Statements.

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. 2764, or writing Matthew Miller, 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 Alice Rivera, Puerto Rico Farm Credit, ACA, PO Box 363649, San Juan, PR 00936-3649, or accessing the website, *www.prfarmcredit.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, 2023	December 31, 2022
	(unaudited)	*(audited)*
Assets		
Cash	**$ 1,172**	$ 1,244
Loans	**179,615**	179,723
Allowance for loan losses	**(4,314)**	(1,189)
Net loans	**175,301**	178,534
Accrued interest receivable	**1,123**	1,251
Equity investments in other Farm Credit institutions	**1,973**	1,982
Premises and equipment, net	**811**	844
Other property owned	**691**	755
Accounts receivable	**839**	1,256
Other assets	**66**	54
Total assets	**$ 181,976**	$ 185,920
Liabilities		
Notes payable to AgFirst Farm Credit Bank	**$ 120,172**	$ 122,638
Accrued interest payable	**493**	415
Patronage refunds payable	**45**	1,007
Accounts payable	**386**	402
Other liabilities	**1,407**	992
Total liabilities	**122,503**	125,454
Commitments and contingencies (Note 7)		
Members' Equity		
Capital stock and participation certificates	**515**	514
Unallocated retained earnings	**58,958**	59,952
Total members' equity	**59,473**	60,466
Total liabilities and members' equity	**$ 181,976**	$ 185,920

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 September 30, 2023	For the Three Months Ended September 30, 2022	For the Nine Months Ended September 30, 2023	For the Nine Months Ended September 30, 2022
Interest Income				
Loans	**$ 2,916**	$ 1,807	**$ 8,541**	$ 5,185
Interest Expense				
Notes payable to AgFirst Farm Credit Bank	**1,438**	976	**4,127**	2,182
Net interest income	**1,478**	831	**4,414**	3,003
Provision for credit losses	**520**	62	**3,147**	88
Net interest income after provision for credit losses	**958**	769	**1,267**	2,915
Noninterest Income				
Loan fees	**(7)**	36	**138**	90
Patronage refunds from other Farm Credit institutions	**258**	271	**789**	795
Gains (losses) on other transactions	**—**	(25)	**—**	(53)
Total noninterest income	**251**	282	**927**	832
Noninterest Expense				
Salaries and employee benefits	**548**	516	**1,645**	1,461
Occupancy and equipment	**48**	67	**155**	168
Insurance Fund premiums	**47**	54	**141**	152
Purchased services	**159**	256	**541**	766
Data processing	**7**	11	**30**	37
Other operating expenses	**164**	228	**705**	739
(Gains) losses on other property owned, net	**12**	13	**75**	137
Total noninterest expense	**985**	1,145	**3,292**	3,460
Net income (loss)	**$ 224**	$ (94)	**$ (1,098)**	$ 287
Other comprehensive income	**—**	—	**—**	—
Comprehensive income (loss)	**$ 224**	$ (94)	**$ (1,098)**	$ 287

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	Unallocated Retained Earnings	Total Members' Equity
Balance at December 31, 2021	$ 470	$ 54,840	$ 55,310
Comprehensive income (loss)		287	287
Capital stock/participation certificates issued/(retired), net	25		25
Balance at September 30, 2022	$ 495	$ 55,127	$ 55,622
Balance at December 31, 2022	**$ 514**	**$ 59,952**	**$ 60,466**
Cumulative effect of change in accounting principle		**104**	**104**
Comprehensive income (loss)		**(1,098)**	**(1,098)**
Capital stock/participation certificates issued/(retired), net	**1**		**1**
Balance at September 30, 2023	**$ 515**	**$ 58,958**	**$ 59,473**

The accompanying notes are an integral part of these consolidated 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 and its Production Credit Association (PCA) and Federal Land Credit Association (FLCA) subsidiaries (collectively, the Association). Descriptions 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, 2022, are contained in the 2022 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 statement of results for the periods presented. These adjustments are of a normal recurring nature, unless otherwise disclosed.

Certain amounts in the prior period's consolidated financial statements 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 those to be expected for a full year.

Significant Accounting Policies
The Association's accounting and reporting policies conform with U.S. generally accepted accounting principles (GAAP) and practices in the financial services industry. To prepare the financial statements in conformity with GAAP, management must make estimates based on assumptions about future economic and market conditions (for example, unemployment, market liquidity, real estate prices, etc.) that affect the reported amounts of assets and liabilities at the date of the financial statements, income and expenses during the reporting period, and the related disclosures. Although these estimates contemplate current conditions and expectations of change in the future, it is reasonably possible that actual conditions may be different than anticipated, which could materially affect results of operations and financial condition.

Management has made significant estimates in several areas, including loans and allowance for credit losses (Note 2, *Loans and Allowance for Credit Losses*) and financial instruments (Note 5, *Fair Value Measurement*). Actual results could differ from those estimates.

For further details of significant accounting policies, see Note 2, *Summary of Significant Accounting Policies*, from the latest Annual Report.

Accounting Standards Effective During the Period
The Association adopted the Financial Accounting Standards Board (FASB) guidance entitled "Measurement of Credit Losses on Financial Instruments" and other subsequently issued accounting standards updates related to credit losses on January 1, 2023. This guidance replaced the current incurred loss impairment methodology with a single allowance framework for financial assets that estimates the current expected credit losses (CECL) over the remaining contractual life for all financial assets measured at amortized cost and certain off-balance sheet credit exposures. This guidance is applied on a modified retrospective basis. This framework requires management to consider in its estimate of the allowance for credit losses (ACL) relevant historical events, current conditions and reasonable and supportable forecasts that consider macroeconomic conditions. In addition, the guidance amends existing impairment guidance for held-to-maturity and available-for-sale investments to incorporate an allowance for credit losses related to these securities, which will allow for the reversal of credit impairments in the event that the credit of an issuer improves.

Also adopted effective January 1, 2023, was the updated guidance entitled "Financial Instruments – Credit Losses: Troubled Debt Restructurings and Vintage Disclosure." This guidance requires the creditor to determine whether a modification results in a new loan or a continuation of an existing loan, among other disclosures specific to modifications with borrowers that are experiencing financial difficulties. The update eliminated the accounting guidance for troubled debt restructurings by creditors. The update also requires disclosure of current period gross write-offs by year of origination for financing receivables and net investments in leases on a prospective basis.

The following table presents the impact to the allowance for credit losses and retained earnings upon adoption of this guidance on January 1, 2023:

	December 31, 2022	CECL Adoption Impact	January 1, 2023
Assets:			
Allowance for loan losses	$ 1,189	$ (11)	$ 1,178
Liabilities:			
Allowance for credit losses on unfunded commitments	$ 167	$ (93)	$ 74
Retained earnings:			
Unallocated retained earnings	$ 59,952	$ 104	$ 60,056

Loans and Allowance for Credit Losses

Loans are recorded at amortized cost basis, which is the principal amount outstanding adjusted for charge-offs, deferred loan fees or costs, and valuation adjustments relating to hedging activities, if any. Loan origination fees and direct loan origination costs are netted and capitalized and the net fee or cost is amortized over the average life of the related loan as an adjustment to interest income. Loan prepayment fees are reported in interest income. Interest on loans is accrued and credited to interest income based on the daily principal amount outstanding.

Nonaccrual Loans

Nonaccrual loans are loans for which there is reasonable doubt that all principal and interest will be collected according to the original contractual terms and are generally considered substandard or doubtful, which is in accordance with the loan rating model, as described below. A loan is considered contractually past due when any principal repayment or interest payment required by the loan instrument is not received on or before the due date. A loan shall remain contractually past due until it is modified or until the entire amount past due, including principal, accrued interest, and penalty interest incurred as the result of past due status, is collected or otherwise discharged in full.

Consistent with prior practice, loans are generally placed in nonaccrual status when principal or interest is delinquent for 90 days (unless adequately secured and in the process of collection), circumstances indicate that collection of principal and interest is in doubt or legal action, including foreclosure or other forms of collateral conveyance, has been initiated to collect the outstanding principal and interest. At the time a loan is placed in nonaccrual status, accrued interest that is considered uncollectible is reversed (if accrued in the current year) or charged against the ACL (if accrued in prior years). Loans are charged-off at the time they are determined to be uncollectible.

When loans are in nonaccrual status, interest payments received in cash are generally recognized as interest income if the collectability of the loan principal is fully expected and certain other criteria are met. Otherwise, payments received on nonaccrual loans are applied against the recorded investment in the loan asset. Nonaccrual loans are returned to accrual status if all contractual principal and interest is current, the borrower is fully expected to fulfill the contractual repayment terms and after remaining current as to principal and interest for a sustained period or have a recent repayment pattern demonstrating future repayment capacity to make on-time payments. If previously unrecognized interest income exists at the time the loan is transferred to accrual status, cash received at the time of or subsequent to the transfer should first be recorded as interest income until such time as the recorded balance equals the contractual indebtedness of the borrower.

Accrued Interest Receivable

The Association adopted the practical expecient to classify accrued interest on loans and investment securities in accrued interest receivable and not as part of loans or investments in the Consolidated Balance Sheets. The Association also elected to not estimate an allowance on interest receivable balances because the nonaccrual policies in place provide for the accrual of interest to cease on a timely basis when all contractual amounts are not expected.

Loan Modifications to Borrowers Experiencing Financial Difficulty

Loan modifications may be granted to borrowers experiencing financial difficulty. Modifications can be in the form of one or a combination of principal forgiveness, interest rate reduction, other-than-insignificant payment delay or a term extension. Covenant waivers and modifications of contingent acceleration clauses are not considered term extensions.

Collateral Dependent Loans

Collateral dependent loans are loans secured by collateral, including but not limited to agricultural real estate, crop inventory, equipment and livestock. CECL requires an entity to measure the expected credit losses based on fair value of the collateral at the reporting date when the entity determines that foreclosure is probable. Additionally, the Association adopted the fair value practical expedient as a measurement approach for loans when the repayment is expected to be provided substantially through the operation or sale of the collateral when the borrower is experiencing financial difficulties. Under the practical expedient measurement approach, the expected credit loss is based on the difference between the fair value of the collateral less estimated costs to sell and the amortized cost basis of the loan.

Allowance for Credit Losses

Beginning January 1, 2023, the ACL represents the estimated current expected credit losses over the remaining contractual life of financial assets measured at amortized cost and certain off-balance sheet credit exposures. The ACL takes into consideration relevant information about past events, current conditions and reasonable and supportable macroeconomic forecasts of future conditions. The contractual term excludes expected extensions, renewals and modifications unless the extension or renewal options are not unconditionally cancellable. The ACL comprises:

- the allowance for loan losses
- the allowance for unfunded commitments, which is presented on the Consolidated Balance Sheets in Other Liabilities, and
- the allowance for credit losses on investment securities, which covers held-to-maturity and available-for-sale securities and is recognized within each investment securities classification on the Consolidated Balance Sheets.

Determining the appropriateness of the allowance is complex and requires judgment by management about the effect of matters that are inherently uncertain. Subsequent evaluations of the loan portfolio, considering macroeconomic conditions, forecasts and other factors prevailing at the time, may result in significant changes in the ACL in those future periods.

Methodology for Allowance for Credit Losses on Loans

The allowance for loan losses represents management’s estimate of credit losses over the remaining expected life of loans. Loans are evaluated on the amortized cost basis, including premiums, discounts, and fair value hedge accounting adjustments.

The Association employs a disciplined process and methodology to establish its allowance for loan losses that has two basic components: first, an asset-specific component involving individual loans that do not share risk characteristics with other loans and the measurement of expected credit losses for such individual loans; and second, a pooled component for estimated expected credit losses for pools of loans that share similar risk characteristics.

Asset-specific loans are generally collateral-dependent loans (including those loans for which foreclosure is probable) and nonaccrual loans. For an asset-specific loan, expected credit losses are measured as the difference between the amortized cost basis in the loan and the present value of expected future cash flows discounted at the loan’s effective interest rate except that, for collateral-dependent loans, credit loss is measured as the difference between the amortized cost basis in the loan and the fair value of the underlying collateral. The fair value of the collateral is adjusted for the estimated cost to sell if repayment or satisfaction of a loan is dependent on the sale (rather than only on the operation) of the collateral. In accordance with the Association’s appraisal policy, the fair value of collateral-dependent loans is based upon independent third-party appraisals or on collateral valuations prepared by in-house appraisers. When an updated appraisal or collateral valuation is received, management reassesses the need for adjustments to the loan’s expected credit loss measurements and, where appropriate, records an adjustment. If the calculated expected credit loss is determined to be permanent, fixed, or non-recoverable, the credit loss portion of the loan will be charged off against the ACL.

In estimating the component of the allowance for loan losses that relates to loans that share common risk characteristics, loans are evaluated collectively and segregated into loan pools considering the risk associated with the specific pool. Relevant risk characteristics include loan type, commodity, credit quality rating, delinquency category or business segment or a combination of these classes. The allowance is determined based on a quantitative calculation of the expected life-of-loan loss percentage for each loan category by considering the probability of default, based on the migration of loans from performing to loss by credit quality rating or delinquency buckets using historical life-of-loan analysis periods for loan types, and the severity of loss, based on the aggregate net lifetime losses incurred per loan pool.

The component of the allowance for loan losses also considers factors for each loan pool to adjust for differences between the historical period used to calculate historical default and loss severity rates and expected conditions over the remaining lives of the loans in the portfolio related to:

- lending policies and procedures;
- national, regional and local economic business conditions and developments that affect the collectability of the portfolio, including the condition of various markets;
- the nature of the loan portfolio, including the terms of the loans;
- the experience, ability and depth of the lending management and other relevant staff;
- the volume and severity of past due and adversely classified or graded loans and the volume of nonaccrual loans;
- the quality of the loan review and process;
- the value of underlying collateral for collateral-dependent loans;
- the existence and effect of any concentrations of credit and changes in the level of such concentrations; and
- the effect of external factors such as competition and legal and regulatory requirements on the level of estimated credit losses in the existing portfolio.

The Association's macroeconomic forecast includes a weighted selection of the Moody's baseline, upside 10th percent and downside 90th percent over reasonable and supportable forecast periods of three years. Subsequent to the forecast period, the Association reverts to long run historical loss experience beyond two years gradually after the determined forecast horizon using a transition function to inform the estimate of losses for the remaining contractual life of the loan portfolio.

The economic forecasts incorporate macroeconomic variables, including unemployment rates, Dow Jones Total Stock Market Index, and corporate bond spreads. Also considered are loan and borrower characteristics, such as internal risk ratings, delinquency status, collateral type, and the remaining term of the loan, adjusted for expected prepayments.

In addition to the quantitative calculation, the Association considers the imprecision inherent in the process and methodology, emerging risk assessments and other subjective factors, which may lead to a management adjustment to the modeled allowance for loan loss results. Expected credit loss estimates also include consideration of expected cash recoveries on loans previously charged-off or expected recoveries on collateral dependent loans where recovery is expected through sale of the collateral. The economic forecasts are updated on a quarterly basis.

Prior to January 1, 2023, the allowance for loan losses was maintained at a level considered adequate to provide for probable losses existing in and inherent in the loan portfolio. The allowance was based on a periodic evaluation of the loan portfolio in which numerous factors were considered, including economic conditions, collateral values, borrowers' financial conditions, loan portfolio composition and prior loan loss experience. The allowance for loan losses encompassed various judgments, evaluations and appraisals with respect to the loans and their underlying collateral that, by their nature, contain elements of uncertainty and imprecision. Changes in the agricultural economy and their impact on borrower repayment capacity would cause these various judgments, evaluations, and appraisals to change over time. Management considered a number of factors in determining and supporting the levels of the allowance for loan losses, which included, but were not limited to, the concentration of lending in agriculture, combined with uncertainties associated with farmland values, commodity prices, exports, government assistance programs, regional economic effects and weather-related influences.

Allowance for Credit Losses on Unfunded Commitments

The Association evaluates the need for an allowance for credit losses on unfunded commitments under CECL and, if required, an amount is recognized and included in Other Liabilities on the Consolidated Balance Sheets. The amount of expected losses is determined by calculating a commitment usage factor over the contractual period for exposures that are not unconditionally cancellable by the Association and applying the loss factors used in the allowance for loan losses methodology to the results of the usage calculation. No allowance for credit losses is recorded for commitments that are unconditionally cancellable.

Note 2 — Loans and Allowance for Credit Losses

A summary of loans outstanding at period end follows:

	September 30, 2023	December 31, 2022
Real estate mortgage	$ 57,958	$ 57,743
Production and intermediate-term	57,821	60,752
Agribusiness:		
Loans to cooperatives	1,203	1,866
Processing and marketing	40,156	40,261
Farm-related business	78	47
Rural infrastructure:		
Communication	12,907	10,673
Power and water/waste disposal	2,196	–
Rural residential real estate	5,140	5,878
Other:		
International	2,156	2,503
Total loans	$ 179,615	$ 179,723

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 the principal balance of participation loans at periods ended:

	September 30, 2023							
	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	$ 6,157	$ 3,385	$ –	$ –	$ –	$ –	$ 6,157	$ 3,385
Production and intermediate-term	17,228	–	–	–	4,059	–	21,287	–
Agribusiness	33,261	8,430	–	–	–	–	33,261	8,430
Rural infrastructure	15,211	–	–	–	–	–	15,211	–
Other	2,172	–	–	–	–	–	2,172	–
Total	$ 74,029	$ 11,815	$ –	$ –	$ 4,059	$ –	$ 78,088	$ 11,815

	December 31, 2022							
	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	$ 6,270	$ 3,690	$ –	$ –	$ –	$ –	$ 6,270	$ 3,690
Production and intermediate-term	17,835	–	–	–	5,540	–	23,375	–
Agribusiness	32,655	8,231	–	–	–	–	32,655	8,231
Rural infrastructure	10,677	–	–	–	–	–	10,677	–
Other	2,503	–	–	–	–	–	2,503	–
Total	$ 69,940	$ 11,921	$ –	$ –	$ 5,540	$ –	$ 75,480	$ 11,921

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

	September 30, 2023	December 31, 2022*
Real estate mortgage:		
Acceptable	99.43%	98.75%
OAEM	0.03	0.65
Substandard/doubtful/loss	0.54	0.60
	100.00%	100.00%
Production and intermediate-term:		
Acceptable	84.25%	84.67%
OAEM	0.04	–
Substandard/doubtful/loss	15.71	15.33
	100.00%	100.00%
Agribusiness:		
Acceptable	92.96%	100.00%
OAEM	7.04	–
Substandard/doubtful/loss	–	–
	100.00%	100.00%
Rural infrastructure:		
Acceptable	90.72%	100.00%
OAEM	9.28	–
Substandard/doubtful/loss	–	–
	100.00%	100.00%
Rural residential real estate:		
Acceptable	95.49%	95.71%
OAEM	–	3.25
Substandard/doubtful/loss	4.51	1.04
	100.00%	100.00%
Other:		
Acceptable	100.00%	100.00%
OAEM	–	–
Substandard/doubtful/loss	–	–
	100.00%	100.00%
Total loans:		
Acceptable	92.21%	94.27%
OAEM	2.43	0.32
Substandard/doubtful/loss	5.36	5.41
	100.00%	100.00%

**Prior to adoption of CECL on January 1, 2023, loans were presented with accrued interest receivable.*

Accrued interest receivable on loans of $1,123 and $1,251 at September 30, 2023 and December 31, 2022, respectively, has been excluded from the amortized cost of loans and reported separately in the Consolidated Balance Sheets.

The following table provides an aging analysis of past due loans as of:

	September 30, 2023					
	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	90 Days or More Past Due and Accruing
Real estate mortgage	$ 2,025	$ 292	$ 2,317	$ 55,641	$ 57,958	$ –
Production and intermediate-term	2,715	1,032	3,747	54,074	57,821	–
Agribusiness	–	–	–	41,437	41,437	–
Rural infrastructure	–	–	–	15,103	15,103	–
Rural residential real estate	160	–	160	4,980	5,140	–
Other	–	–	–	2,156	2,156	–
Total	$ 4,900	$ 1,324	$ 6,224	$ 173,391	$ 179,615	$ –

Prior to the adoption of CECL, the aging analysis of past due loans reported included accrued interest as follows:

	December 31, 2022					
	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	90 Days or More Past Due and Accruing
Real estate mortgage	$ 20	$ 357	$ 377	$ 57,883	$ 58,260	$ –
Production and intermediate-term	2,748	432	3,180	58,088	61,268	–
Agribusiness	–	–	–	42,344	42,344	–
Rural infrastructure	–	–	–	10,677	10,677	–
Rural residential real estate	446	–	446	5,458	5,904	–
Other	–	–	–	2,521	2,521	–
Total	$ 3,214	$ 789	$ 4,003	$ 176,971	$ 180,974	$ –

The following tables reflect nonperforming assets and related credit quality statistics as of:

	September 30, 2023
Nonaccrual loans:	
Real estate mortgage	$ 293
Production and intermediate-term	5,299
Total	$ 5,592
Accruing loans 90 days or more past due:	
Total	$ –
Total nonperforming loans	$ 5,592
Other property owned	691
Total nonperforming assets	$ 6,283
Nonaccrual loans as a percentage of total loans	3.11%
Nonperforming assets as a percentage of total loans and other property owned	3.48%
Nonperforming assets as a percentage of capital	10.56%

	December 31, 2022*
Nonaccrual loans:	
Real estate mortgage	$ 1,404
Production and intermediate-term	4,288
Total	$ 5,692
Accruing restructured loans:	
Real estate mortgage	$ 879
Production and intermediate-term	2,051
Rural residential real estate	140
Total	$ 3,070
Accruing loans 90 days or more past due:	
Total	$ –
Total nonperforming loans	$ 8,762
Other property owned	755
Total nonperforming assets	$ 9,517
Nonaccrual loans as a percentage of total loans	3.17%
Nonperforming assets as a percentage of total loans and other property owned	5.27%
Nonperforming assets as a percentage of capital	15.74%

**Prior to adoption of CECL, nonperforming assets included accruing restructured loans and loans were presented including accrued interest receivable.*

The following table provides the amortized cost for nonaccrual loans, with and without a related allowance for loan losses, and interest income recognized on nonaccrual loans during the period:

	September 30, 2023			Interest Income Recognized on Nonaccrual Loans	
Nonaccrual loans:	**Amortized Cost with Allowance**	**Amortized Cost without Allowance**	**Total**	**Three Months Ended September 30, 2023**	**Nine Months Ended September 30, 2023**
Real estate mortgage	$ –	$ 293	$ 293	$ 3	$ 4
Production and intermediate-term	3,607	1,692	5,299	61	79
Rural residential real estate	11	(11)	–	–	–
Total	$ 3,618	$ 1,974	$ 5,592	$ 64	$ 83

Effective January 1, 2023, the Association adopted the CECL accounting guidance as described in Note 1. A summary of changes in the allowance for credit losses by portfolio segment is as follows:

	Real Estate Mortgage	Production and Intermediate-term	Agribusiness	Rural Infrastructure	Rural Residential Real Estate	Other	Total
Allowance for Loan Losses:							
Balance at June 30, 2023	$ 170	$ 3,462	$ 154	$ 14	$ 82	$ 1	$ 3,883
Charge-offs	–	–	–	–	–	–	–
Recoveries	–	–	–	–	–	–	–
Provision for loan losses	15	360	21	12	23	–	431
Balance at September 30, 2023	$ 185	$ 3,822	$ 175	$ 26	$ 105	$ 1	$ 4,314
Allowance for Unfunded Commitments:							
Balance at June 30, 2023	$ –	$ 25	$ 47	$ 2	$ –	$ –	$ 74
Provision for unfunded commitments	–	17	70	1	–	1	89
Balance at September 30, 2023	$ –	$ 42	$ 117	$ 3	$ –	$ 1	$ 163
Total allowance for credit losses	$ 185	$ 3,864	$ 292	$ 29	$ 105	$ 2	$ 4,477
Allowance for Loan Losses:							
Balance at December 31, 2022	$ 378	$ 385	$ 289	$ 69	$ 42	$ 26	$ 1,189
Cumulative effect of a change in accounting principle	(219)	461	(146)	(60)	(23)	(24)	(11)
Balance at January 1, 2023	$ 159	$ 846	$ 143	$ 9	$ 19	$ 2	$ 1,178
Charge-offs	–	(1)	–	–	–	–	(1)
Recoveries	–	2	–	–	77	–	79
Provision for loan losses	26	2,975	32	17	9	(1)	3,058
Balance at September 30, 2023	$ 185	$ 3,822	$ 175	$ 26	$ 105	$ 1	$ 4,314
Allowance for Unfunded Commitments:							
Balance at December 31, 2022	$ 12	$ 43	$ 87	$ 15	$ –	$ 10	$ 167
Cumulative effect of a change in accounting principle	(12)	(18)	(40)	(13)	–	(10)	(93)
Balance at January 1, 2023	$ –	$ 25	$ 47	$ 2	$ –	$ –	$ 74
Provision for unfunded commitments	–	17	70	1	–	1	89
Balance at September 30, 2023	$ –	$ 42	$ 117	$ 3	$ –	$ 1	$ 163
Total allowance for credit losses	$ 185	$ 3,864	$ 292	$ 29	$ 105	$ 2	$ 4,477
Allowance for Loan Losses*:							
Balance at June 30, 2022	$ 369	$ 461	$ 272	$ 60	$ 44	$ 12	$ 1,218
Charge-offs	–	(4)	–	–	–	–	(4)
Recoveries	–	8	–	–	–	–	8
Provision for loan losses	12	8	20	10	(2)	14	62
Balance at September 30, 2022	$ 381	$ 473	$ 292	$ 70	$ 42	$ 26	$ 1,284
Balance at December 31, 2021	$ 414	$ 411	$ 261	$ 39	$ 55	$ 13	$ 1,193
Charge-offs	(24)	(12)	–	–	–	–	(36)
Recoveries	30	8	–	–	1	–	39
Provision for loan losses	(39)	66	31	31	(14)	13	88
Balance at September 30, 2022	$ 381	$ 473	$ 292	$ 70	$ 42	$ 26	$ 1,284

**For periods prior to January 1, 2023, the allowance for loan losses was based on probable and estimable losses inherent in the loan portfolio.*

Loan modifications may be granted to borrowers experiencing financial difficulty. Qualifying disclosable modifications are one, or a combination of, principal forgiveness, interest rate reduction, or a term or payment extension. Covenant waivers and modifications of contingent acceleration clauses are not considered term extensions. Modified loans to borrowers experiencing financial difficulty and activity on these loans were not material during the three and nine months ended September 30, 2023. There were no material commitments to lend to borrowers experiencing financial difficulty whose loans have been modified at September 30, 2023.

The Association had no loans held for sale at September 30, 2023 and December 31, 2022.

Troubled Debt Restructurings

Prior to the adoption of updated FASB guidance on loan modifications on January 1, 2023, a restructuring of a loan constituted a troubled debt restructuring (TDR) if the creditor for economic or legal reasons related to the borrower's financial difficulties granted a concession to the borrower that it would not otherwise consider. Concessions varied by program, were borrower-specific, and could include interest rate reductions, term extensions, payment deferrals or the acceptance of additional collateral in lieu of payments. In limited circumstances, principal may have been forgiven. When a restructured loan constituted a TDR, these loans were included within impaired loans under nonaccrual or accruing restructured loans. There were no new TDRs that occurred during the three and nine months ended September 30, 2022.

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 three and nine months ended September 30, 2022. 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:

	December 31, 2022*	
	Total TDRs	Nonaccrual TDRs
Real estate mortgage	$ 1,906	$ 1,027
Production and intermediate-term	6,207	4,156
Rural residential real estate	140	–
Total loans	$ 8,253	$ 5,183
Additional commitments to lend	$ –	

**Prior to adoption of CECL on January 1, 2023, loans were presented with accrued interest receivable.*

Note 3 — Investments

Equity Investments in Other Farm Credit System Institutions

Equity investments in other Farm Credit System institutions are generally nonmarketable investments consisting of stock and participation certificates, allocated surplus, and reciprocal investments in other institutions regulated by the FCA. These investments are carried at cost and evaluated for impairment based on the ultimate recoverability of the par value rather than by recognizing temporary declines in value.

Associations are required to maintain ownership in AgFirst (AgFirst or the Bank) in the form of Class B or Class C stock as determined by the Bank. The Bank may require additional capital contributions to maintain its capital requirements. The Association owned 0.48 percent of the issued stock and allocated retained earnings of the Bank as of September 30, 2023 net of any reciprocal investment. As of that date, the Bank's assets totaled $43.4 billion and shareholders' equity totaled $1.4 billion. The Bank's earnings were $195 million for the first nine months of 2023. In addition, the Association held $135 in investments related to other Farm Credit institutions.

Note 4 — Debt

Notes Payable to AgFirst Farm Credit Bank

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

Note 5 — 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.

The classifications within the fair value hierarchy are as follows:

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

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

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

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

There were no Level 3 assets or 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.

Fair values are estimated at each period end date for assets and liabilities measured at fair value on a recurring basis. The following tables summarize assets measured at fair value at period end.

	September 30, 2023			
	Fair Value Measurement Using			Total Fair
	Level 1	Level 2	Level 3	Value
Recurring assets				
Assets held in trust funds	$ –	$ –	$ –	$ –
Nonrecurring assets				
Nonaccrual loans	$ –	$ –	$ 46	$ 46
Other property owned	$ –	$ –	$ 737	$ 737

	December 31, 2022			
	Fair Value Measurement Using			Total Fair
	Level 1	Level 2	Level 3	Value
Recurring assets				
Assets held in trust funds	$ –	$ –	$ –	$ –
Nonrecurring assets				
Impaired loans*	$ –	$ –	$ 242	$ 242
Other property owned	$ –	$ –	$ 805	$ 805

**Prior to the adoption of CECL on January 1, 2023, the fair value of impaired loans included accruing restructured loans and loans past due 90 days and accruing.*

Valuation Techniques

Assets held in trust funds
Assets held in trust funds, related to deferred compensation plans, are classified as Level 1. The trust funds include investments in securities that are actively traded and have quoted net asset value prices that are directly observable in the marketplace.

Nonaccrual loans
Fair values of nonaccrual loans 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.

Other property owned

For other property owned, 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. If the process uses observable market-based information, the assets are classified as Level 2. If the process requires significant input based upon management's knowledge of and judgment about current market conditions, specific issues relating to the property and other matters, the assets are classified as Level 3.

Note 6 — Employee Benefit Plans

The following is a table of retirement expenses for the Association:

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2023	**2022**	**2023**	**2022**
Pension	$ 57	$ 62	$ 159	$ 184
401(k)	33	25	98	70
Total	$ 90	$ 87	$ 257	$ 254

Expenses in the above table are computed using allocated estimates of funding for multi-employer plans in which the Association participates. These amounts may change when a total funding amount and allocation is determined by the respective Plan's Sponsor Committee. Also, market conditions could impact discount rates and return on plan assets which could change contributions necessary before the next plan measurement date of December 31, 2023.

Further details regarding employee benefit plans are contained in the 2022 Annual Report to Shareholders.

Note 7 — 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 remote 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 8 — Subsequent Events

The Association evaluated subsequent events and determined that, except for as described below, there were none requiring disclosure through November 8, 2023, which was the date the financial statements were issued.

On October 27, 2023 the AgFirst Board of Directors approved an increase to the Association Investment in AgFirst from 1.00 percent to 1.50 percent effective October 31, 2023. This resulted in an increase in the equity investment in AgFirst of $656 thousand to $2.5 million.