



AgFirst Farm Credit Bank & District Associations

SECOND QUARTER

2015 Quarterly Report




SECOND QUARTER 2015

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CERTIFICATION

The undersigned certify that we have reviewed the June 30, 2015 quarterly report of AgFirst Farm Credit Bank and District Associations, 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.



Dale R. Hershey
Chairman of the Board



Leon T. Amerson
Chief Executive Officer & President



Charl L. Butler
Chief Financial Officer

August 7, 2015

Report on Internal Control Over Financial Reporting

AgFirst Farm Credit Bank's (Bank) and each affiliated District Agricultural Credit Association's (District Association) 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 Bank's and each District Association's respective 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 Bank's and each District 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 respective 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 Bank and each District 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 Bank and each District Association, and (3) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use or disposition of the Bank's and each District Association's assets that could have a material effect on its Consolidated Financial Statements.

The Bank's and each District Association's management has completed an assessment of the effectiveness of internal control over financial reporting as of June 30, 2015. In making the assessment, management used the framework in *Internal Control — Integrated Framework (2013)*, promulgated by the Committee of Sponsoring Organizations of the Treadway Commission, commonly referred to as the "COSO" criteria.

Based on the assessment performed, the Bank's and each District Association's management concluded that as of June 30, 2015, the internal control over financial reporting was effective based upon the COSO criteria. Additionally, based on this assessment, the Bank's and each District Association's management determined that there were no material weaknesses in the internal control over financial reporting as of June 30, 2015.



Leon T. Amerson
Chief Executive Officer & President



Charl L. Butler
Chief Financial Officer

August 7, 2015

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

The following discussion reviews the combined financial condition and results of operations of AgFirst Farm Credit Bank (AgFirst or Bank) and the District Agricultural Credit Associations (Associations or District Associations), collectively referred to as the District, as of and for the three and six month periods ended June 30, 2015. These comments should be read in conjunction with the accompanying financial statements, the Notes to the Combined Financial Statements, and the 2014 Annual Report of AgFirst Farm Credit Bank and District Associations. The accompanying combined financial statements were prepared under the oversight of the Audit Committee of the AgFirst Board of Directors.

As of June 30, 2015, the District included nineteen Associations, all of which were structured as Agricultural Credit Association (ACA) holding companies, with Federal Land Credit Association (FLCA) and Production Credit Association (PCA) subsidiaries. PCAs originate and service short- and intermediate-term loans; FLCAs originate and service long-term real estate mortgage loans; and ACAs originate both long-term and short- and intermediate-term loans.

Key ratios and data reported below, and in the accompanying financial statements, address the financial performance of the District. However, neither the three months nor the six months results of operations may be indicative of an entire year due to the seasonal nature of a portion of the District's business.

FORWARD-LOOKING INFORMATION

This quarterly report contains forward-looking statements. These statements are not guarantees of future performance and involve certain risks, uncertainties, and assumptions that are difficult to predict. Words such as "anticipates," "believes," "could," "estimates," "may," "should," "will," or other variations of these terms are intended to identify the forward-looking statements. These statements are based on assumptions and analyses made in light of experience and other historical trends, current conditions, and expected future developments. However, actual results and developments may differ materially from the District's expectations and predictions due to a number of risks and uncertainties, many of which are beyond the District's control. These risks and uncertainties include, but are not limited to:

- political, legal, regulatory, financial markets, and economic conditions and developments in the United States and abroad;
- economic fluctuations in the agricultural, rural infrastructure, international, and farm-related business sectors, as well as in the general economy;
- weather-related, disease, and other adverse climatic or biological conditions that periodically occur that impact agricultural productivity and income of District borrowers;
- changes in United States government support of the agricultural industry and the Farm Credit System (System) as a government-sponsored enterprise (GSE), as well as investor and rating agency reactions to events involving the U.S. government, other GSEs and other financial institutions;
- actions taken by the Federal Reserve System in implementing monetary and fiscal policy, as well as other policies and actions of the federal government that impact the financial services industry and the debt markets;
- credit, interest rate and liquidity risk inherent in lending activities; and
- changes in assumptions for determining the allowance for loan losses, other than temporary impairment and fair value measurements.

FINANCIAL CONDITION

Loan Portfolio

The District’s aggregate loan portfolio consists primarily of direct loans made by the Associations to eligible borrowers located within their chartered territories. Bank loans to District Associations have been eliminated in the combined District presentation. Diversification of the loan volume by Farm Credit Administration (FCA) regulatory type is illustrated in the following table:

Loan Portfolio <i>(dollars in thousands)</i>	June 30, 2015		December 31, 2014		June 30, 2014	
Real Estate Mortgage	\$ 11,063,436	45%	\$ 10,749,817	44%	\$ 10,398,344	44%
Production and Intermediate-Term	7,501,544	30	7,650,543	31	7,394,728	31
Rural Residential Real Estate	3,032,383	12	2,954,004	12	2,872,188	12
Processing and Marketing	1,463,561	6	1,404,051	6	1,398,417	6
Energy and Water/Waste Disposal	437,379	2	468,589	2	470,951	2
Farm-Related Business	428,296	2	410,026	2	369,301	2
Communication	365,156	2	356,825	2	383,977	2
Loans to Cooperatives	245,526	1	261,652	1	281,097	1
Loans to Other Financing Institutions (OFIs)	104,633	–	95,512	–	95,975	–
Other (including Mission Related)	57,047	–	60,005	–	61,512	–
International	19,809	–	–	–	–	–
Lease Receivables	3,913	–	4,945	–	3,945	–
Total	\$ 24,722,683	100%	\$ 24,415,969	100%	\$ 23,730,435	100%

Total loans outstanding were \$24.723 billion at June 30, 2015, an increase of \$306.7 million, or 1.26 percent, compared to total loans outstanding at December 31, 2014 and an increase of \$992.2 million, or 4.18 percent, since June 30, 2014. The increase in loan volume resulted from improved economic conditions positively impacting borrowers in economically sensitive segments such as forestry and borrowers dependent on non-farm income. Also, loan demand over the previous twelve months benefitted from improved conditions in specific commodities such as the poultry, cattle, and swine sectors. Future loan demand is difficult to predict; however, it is expected to modestly increase for the remainder of 2015.

Credit Quality

Credit quality of the District’s loans is shown below:

Classification	Total Loan Portfolio Credit Quality as of:		
	June 30, 2015	December 31, 2014	June 30, 2014
Acceptable	94.55%	94.28%	93.21%
OAEM *	2.71%	2.92%	3.46%
Adverse**	2.74%	2.80%	3.33%

*Other Assets Especially Mentioned
 **Adverse loans include substandard, doubtful, and loss loans.

Loan portfolio credit quality improved at June 30, 2015 compared to December 31, 2014 and June 30, 2014. Loan portfolio credit quality at the producer level reflected improvement primarily due to incremental improvement of economic conditions. District real estate values have also continued to improve. Grain prices have declined due to higher than expected inventory and harvest levels. This benefitted the poultry, cattle, and swine sectors but pressured margins of grain producers. Due to geographic location, District borrowers are predominately net grain consumers. Improved housing starts continue to positively impact certain housing-related segments such as forestry and nursery/greenhouse. Credit quality is expected to remain stable for the remainder of 2015 given anticipated economic conditions.

Nonaccrual Loans

Nonaccrual loans represent all loans for which there is a reasonable doubt as to the collection of principal and/or interest under the contractual terms of the loan. Nonaccrual loans for the combined District at June 30, 2015 were \$265.6 million compared to \$311.0 million at December 31, 2014. The decrease of \$45.3 million resulted primarily from repayments of \$65.1 million, reinstatements to accrual status of \$15.0 million, transfers to other property owned of \$11.6 million, and charge-offs of \$5.3 million. Offsetting these decreases were \$52.8 million of loan balances transferred to nonaccrual

status, advances of \$6.4 million, and recoveries of charge-offs of \$4.0 million. The ten largest nonaccrual borrower relationships at June 30, 2015 accounted for 23.80 percent of the total nonaccrual balance. At June 30, 2015, total nonaccrual loans were primarily classified in the forestry (20.63 percent of the total), nursery/greenhouse (13.61 percent), poultry (12.76 percent), field crops (8.64 percent), and cattle (7.39 percent) segments. Nonaccrual loans were 1.07 percent and 1.27 percent of total loans outstanding at June 30, 2015 and December 31, 2014, respectively.

Troubled Debt Restructurings

A troubled debt restructuring (TDR) occurs when a borrower is experiencing financial difficulties and a concession is granted to the borrower that the Bank and District Associations would not otherwise consider. Concessions are granted to borrowers based on either an assessment of the borrower's ability to return to financial viability or a court order. The concessions can be in the form of a modification of terms, rates, or amounts owed. Acceptance of other assets and/or equity as payment may also be considered a concession. The type of alternative financing granted is chosen in order to minimize the loss incurred by the Bank and District Associations. TDRs decreased \$15.8 million since December 31, 2014 and totaled \$241.1 million at June 30, 2015. TDRs at June 30, 2015 were comprised of \$117.3 million of accruing restructured loans and \$123.8 million of nonaccrual restructured loans. Restructured loans were primarily in the nursery/greenhouse (19.67 percent of the total), forestry (17.61 percent), poultry (10.66 percent), and field crops (7.62 percent) segments.

Other Property Owned

Other property owned (OPO) consists primarily of assets once pledged as loan collateral that were acquired through foreclosure or deeded to the Bank and District Associations (or a lender group) in satisfaction of secured loans. OPO is generally comprised of real estate, equipment, and equity interests in companies or partnerships. OPO decreased \$5.5 million since December 31, 2014 and totaled \$40.5 million at June 30, 2015. The decrease was due to disposals of \$18.5 million and writedowns of \$1.2 million offset by transfers to OPO of \$14.2 million. The largest OPO holding at June 30, 2015 was in the other real estate segment and totaled \$5.3 million. See discussion of OPO expense in the *Noninterest Expenses* section below.

Allowance for Loan Losses

The District maintains an allowance for loan losses at a level management considers adequate to provide for probable and estimable credit losses within the loan portfolio as of each reported balance sheet date. Although aggregated in the District's combined financial statements, the allowance for loan losses of each District entity is particular to that institution and is not available to absorb losses realized by other District entities.

The allowance for loan losses was \$178.6 million at June 30, 2015, as compared with \$174.9 million at December 31, 2014, which was an increase of \$3.7 million. Activity which increased the allowance during the six months ended June 30, 2015 included provision expense of \$5.1 million and loan recoveries of \$4.0 million. Offsetting these increases were charge-offs of \$5.4 million as loan collectability became more measurable and apparent. Charge-offs during the six month period were related primarily to borrowers in the dairy (13.43 percent of the total), cattle (11.40 percent), poultry (10.22 percent), forestry (9.97 percent), and nursery/greenhouse (7.94 percent) segments. Recoveries during the six month period were related primarily to borrowers in the nursery/greenhouse (39.73 percent of the total), forestry (11.25 percent), and field crops (8.32 percent) segments. The allowance at June 30, 2015 included specific reserves of \$30.2 million (16.91 percent of the total) and \$148.4 million (83.09 percent) of general reserves. The largest commodity segments included in the allowance at June 30, 2015 were the forestry (13.51 percent of the total), field crops (10.53 percent), poultry (9.86 percent), cattle (7.87 percent), grain (6.67 percent), and nursery/greenhouse (6.12 percent) segments. See Note 2, *Loans and Allowance for Loan Losses*, in the Notes to the Combined Financial Statements for further information. See *Provision for Loan Losses* section below for additional details regarding loan loss provision expense and reversals.

Liquidity and Funding Sources

AgFirst and the District Associations maintain adequate liquidity to satisfy the District's daily cash needs. Along with normal cash flows associated with lending operations, the District has two primary sources of liquidity: the capacity to issue Systemwide Debt Securities through the Federal Farm Credit Banks Funding Corporation; and cash and investments.

The Bank also maintains several lines of credit with commercial banks, as well as securities repurchase agreement facilities. Providing liquidity for the District's operations is primarily the responsibility of the Bank.

The U.S. government does not guarantee, directly or indirectly, Systemwide Debt Securities. However, the Farm Credit System, as a GSE, has benefited from broad access to the domestic and global capital markets. This access has provided the System with a dependable source of competitively priced debt which is critical for supporting the System's mission of providing credit to agriculture and rural America. The implied link between the credit rating of the System and the U.S. government, given the System's status as a GSE and continued concerns regarding the government's borrowing limit and budget imbalances, could pose risk to the System in the future.

AgFirst's primary source of liquidity comes from its ability to issue Systemwide Debt Securities, which are the general unsecured joint and several obligations of the System banks. AgFirst continually raises funds in the debt markets to support its mission, to repay maturing Systemwide Debt Securities, and to meet other obligations.

The System does not have a guaranteed line of credit from the U.S. Treasury or the Federal Reserve. However, the Farm Credit System Insurance Corporation (FCSIC) has an agreement with the Federal Financing Bank (FFB), a federal instrumentality subject to the supervision and direction of the U.S. Treasury, pursuant to which the FFB could advance funds to the FCSIC. Under its existing statutory authority, the FCSIC may use these funds to provide assistance to the System banks in exigent market circumstances which threaten the banks' ability to pay maturing debt obligations. The agreement provides for advances of up to \$10 billion and terminates on September 30, 2015, unless otherwise renewed. The decision whether to seek funds from the FFB is at the discretion of the FCSIC. Each funding obligation of the FFB is subject to various terms and conditions and, as a result, there can be no assurance that funding would be available if needed by AgFirst or the System.

Currently, Standard & Poor's Ratings Services, Moody's Investor Service and Fitch Ratings have assigned long-term debt ratings for the System of AA+, Aaa, and AAA and short-term debt ratings of A-1+, P-1, and F1, respectively. All three ratings agencies' outlook for the System is stable. The Standard & Poor's Ratings Services rating of the System's long-term debt reflects a previous downgrade of the U.S. sovereign rating. These rating agencies base their ratings on many quantitative and qualitative factors, including the System's status as a GSE. Negative changes to the System's credit ratings could reduce earnings by increasing debt funding costs, and could also have a material adverse effect on liquidity, the ability to conduct normal business operations, and the Bank's overall financial condition and results of operations. However, AgFirst anticipates continued access to funding necessary to support the District's needs.

At June 30, 2015, AgFirst had \$26.288 billion in total debt outstanding compared to \$26.847 billion at December 31, 2014. Total interest-bearing liabilities declined slightly primarily due to lower funding needs related to decreases in liquidity investments and increased capital as discussed elsewhere in this report. However, on an average balance basis there was an increase during the period, which is reflected in the net interest income analysis below.

Cash and cash equivalents, which decreased \$512.1 million from December 31, 2014 to a total of \$384.1 million at June 30, 2015, consist primarily of cash on deposit and money market securities that are short-term in nature (from overnight maturities to maturities that range up to 90 days). Incremental movements in cash balances are due primarily to changes in liquidity needs in relation to upcoming debt maturities between reporting periods.

Investment securities totaled \$7.453 billion, or 22.60 percent of total assets at June 30, 2015, compared to \$7.543 billion, or 22.67 percent, as of December 31, 2014. Investment securities decreased \$90.2 million (1.20 percent), compared to December 31, 2014. Management maintains the available-for-sale liquidity investment portfolio size generally proportionate with that of the loan portfolio and within regulatory and policy guidelines. In March 2015, the Bank sold 204 agency mortgage-backed securities totaling \$28.0 million which resulted in gains of \$1.1 million. The proceeds were used to purchase one U.S. government guaranteed security. These transactions benefitted the Bank by reducing carrying costs and improving liquidity.

Investment securities classified as being available-for-sale totaled \$6.710 billion at June 30, 2015. Available-for-sale investments at June 30, 2015 included \$3.718 billion in U.S. government guaranteed securities, \$2.261 billion in U.S. government agency guaranteed securities, \$590.1 million in non-agency asset-backed securities, and \$140.8 million in non-agency collateralized mortgage obligations. Since the majority of the portfolio is invested in U.S. government guaranteed and agency securities, the portfolio is highly liquid and potential credit loss exposure is limited.

As of June 30, 2015, AgFirst exceeded all applicable regulatory liquidity requirements. FCA regulations require that the Bank have a liquidity policy that establishes a minimum total “coverage” level of 90 days and that short-term liquidity requirements must be met by certain high quality investments or cash. “Coverage” is defined as the number of days that maturing debt could be funded with eligible cash, cash equivalents, and available-for-sale investments maintained by the Bank.

The FCA classifies eligible liquidity investments according to four liquidity quality levels with level 1 being the highest. The first 15 days of minimum liquidity coverage are met using only level 1 instruments, which include cash and cash equivalents. Days 16 through 30 of minimum liquidity coverage are met using level 1 and level 2 instruments. Level 2 consists primarily of U.S. government guaranteed securities. Days 31 through 90 are met using level 1, level 2, and level 3 securities. Level 3 consists primarily of U.S. agency investments. The fourth level is a supplemental liquidity buffer in excess of the 90-day minimum liquidity reserve which is set to provide coverage to at least 120 days.

At June 30, 2015, AgFirst met each of the individual level criteria above and had a total of 197 days of maturing debt coverage compared to 222 days at December 31, 2014. As previously discussed, this decrease resulted from a change in the level of upcoming maturing debt. Cash provided by the Bank’s operating activities, primarily generated from net interest income in excess of operating expenses and maturities in the loan portfolio, is an additional source of liquidity for the Bank that is not reflected in the coverage calculation.

Net unrealized gains related to investment securities were \$95.2 million at June 30, 2015, compared to \$108.9 million at December 31, 2014. These net unrealized gains are reflected in Accumulated Other Comprehensive Income (AOCI) in the Financial Statements. The net unrealized gains stem from normal market factors such as the current interest rate environment.

The District performs periodic credit reviews, including other-than-temporary impairment analyses, on its entire investment securities portfolio. Based on the results of all analyses, the District recognized other-than-temporary credit related impairment of \$384 thousand and \$1.5 million for the six months ended June 30, 2015 and 2014, respectively, which was included in Net Other-than-temporary Impairment Losses in the Statements of Income. If there is a significant increase in collected or expected cash flows of a previously impaired security, the Bank accretes those additional amounts to interest income, as appropriate, over the remaining life of the security in a prospective manner, based on the difference between the amortized cost basis and the cash flows expected to be collected. The District recognized additional interest income of \$833 thousand and \$419 thousand for the six months ended June 30, 2015 and 2014, respectively. See Note 3, *Investments*, in the Notes to the Combined Financial Statements for further information.

Capital Resources

Total shareholders’ equity increased \$245.3 million (4.54 percent) from December 31, 2014 to a total of \$5.648 billion at June 30, 2015. This increase is primarily attributed to 2015 unallocated retained earnings from net income of \$271.3 million.

On September 4, 2014, the FCA published a proposed rule to modify the regulatory capital requirements for System banks and associations. See *Regulatory Matters* section below for further discussion on the proposed rule.

RESULTS OF OPERATIONS

Net income for the three months ended June 30, 2015 was \$136.2 million compared to \$153.9 million for the three months ended June 30, 2014, a decrease of \$17.7 million, or 11.51 percent. Net income for the six months ended June 30, 2015 was \$271.3 million, compared to \$302.5 million for the corresponding period in 2014, a decrease of \$31.2 million, or 10.31 percent. See below for further discussion of change in net income by major components.

Key Results of Operations Comparisons

	Annualized for the six months ended June 30, 2015	For the year ended December 31, 2014	Annualized for the six months ended June 30, 2014
Return on average assets	1.65%	1.96%	1.93%
Return on average shareholders' equity	10.35%	11.85%	11.77%
Net interest margin	3.14%	3.32%	3.34%
Operating expense as a percentage of net interest income and noninterest income	46.37%	42.35%	42.99%
Net (charge-offs) recoveries to average loans	(0.01)%	–%	0.02%

The first three ratios above have declined in 2015 primarily due to a decrease in net interest income. For the operating expense as a percentage of net interest income and noninterest income ratio, operating expense consists primarily of noninterest expense excluding losses (gains) from other property owned. This ratio also was negatively impacted by the decline in net interest income as well as an increase in operating expenses. See *Allowance for Loan Losses*, *Net Interest Income*, *Noninterest Income*, and *Noninterest Expenses* sections for further discussion.

Net Interest Income

Net interest income for the three months ended June 30, 2015 was \$250.2 million compared to \$255.9 million for the same period of 2014, a decrease of \$5.6 million or 2.20 percent. For the six months ended June 30, 2015, net interest income was \$ 498.2 million compared to \$507.5 million for the same period of 2014, a decrease of \$9.3 million, or 1.83 percent. The net interest margin, which is net interest income as a percentage of average earning assets, was 3.11 percent and 3.14 percent, a decrease of 23 and 20 basis points, respectively, for the three and six month periods of 2015 compared to the prior year. The decline for both periods was primarily the result of lower yields on interest-earning assets, due to the lower interest rate environment for interest-earning assets and the impact of competitive pressures on loan yields, and higher rates paid on interest bearing liabilities. In addition, it was negatively impacted by higher average balances for interest bearing liabilities. Over time, as interest rates change and as assets prepay or reprice, the positive impact on the net interest margin that the Bank has experienced over the last several years from calling debt will continue to diminish. The positive impact of higher average balances of earning assets partially offset some of the decline in net interest income.

The effects of changes in volume and interest rates on net interest income in the three and six months ended June 30, 2015, as compared with the same periods of 2014, are presented in the following table. The table distinguishes between the changes in interest income and interest expense related to average outstanding balances and to the levels of average interest rates. Accordingly, the benefit derived from funding earning assets with interest-free funds (principally capital) is reflected solely as a volume increase.

<i>(dollars in thousands)</i>	For the three months ended June 30, 2015 vs. June 30, 2014			For the six months ended June 30, 2015 vs. June 30, 2014		
	Increase (decrease) due to changes in:			Increase (decrease) due to changes in:		
	Volume	Rate	Total	Volume	Rate	Total
Interest Income:						
Loans	\$ 11,446	\$ (4,109)	\$ 7,337	\$ 22,579	\$ (10,191)	\$ 12,388
Investments & Cash Equivalents	1,924	(5,760)	(3,836)	4,246	(11,859)	(7,613)
Total Interest Income	\$ 13,370	\$ (9,869)	\$ 3,501	\$ 26,825	\$ (22,050)	\$ 4,775
Interest Expense:						
Interest-Bearing Liabilities	\$ 2,755	\$ 6,387	\$ 9,142	\$ 4,694	\$ 9,375	\$ 14,069
Changes in Net Interest Income	\$ 10,615	\$ (16,256)	\$ (5,641)	\$ 22,131	\$ (31,425)	\$ (9,294)

Provision for Loan Losses

AgFirst and the Associations measure risks inherent in their individual loan portfolios on an ongoing basis and, as necessary, recognize provision for loan loss expense so that appropriate allowances for loan losses are maintained. Provision for loan losses was a net expense of \$3.4 million and \$5.1 million for the three and six months periods ended June 30, 2015, respectively, compared to a net reversal (recovery) of \$316 thousand and \$2.7 million for three and six months ended June 30, 2014. For the three months ended June 30, 2015, the net provision expense consisted of \$5.0

million of general reserve expense partially offset by \$1.6 million of specific reserve reversals. For the second quarter of 2015, the net provision expense was comprised primarily of provision expense related to the field crops (\$2.3 million), grain (\$2.2 million), non-farm income (\$1.2 million), corn (\$1.2 million), processing (\$1.1 million), and poultry (\$1.0 million) segments, partially offset by net provision reversals related to the cattle (\$2.4 million), nursery/greenhouse (\$1.5 million), and forestry (\$1.0 million) segments. For the six months ended June 30, 2015, the net provision expense consisted of \$7.5 million of general reserve expense partially offset by \$2.4 million of specific reserve reversals. The net provision expense for the six month period was comprised primarily of provision expense related to the field crops (\$2.6 million), processing (\$2.6 million), grain (\$2.2 million), non-farm income (\$1.2 million), and corn (\$1.0 million) segments, partially offset by net provision reversals in the nursery/greenhouse (\$2.4 million), cattle (\$1.7 million), and forestry (\$1.0 million) segments. See Note 2, *Loans and Allowance for Loan Losses*, in the Notes to the Combined Financial Statements for further information.

Noninterest Income

The following table illustrates the changes in noninterest income:

Change in Noninterest Income <i>(dollars in thousands)</i>	For the three months ended June 30,			For the six months ended June 30,		
	2015	2014	Increase/ (Decrease)	2015	2014	Increase/ (Decrease)
Loan fees	\$ 6,956	\$ 7,807	\$ (851)	\$ 14,501	\$ 14,796	\$ (295)
Fees for financially related services	1,715	1,348	367	3,066	2,693	373
Building lease income	900	663	237	1,844	1,693	151
Net impairment losses on investments	(277)	(101)	(176)	(384)	(1,452)	1,068
Gains (losses) on investments, net	—	—	—	1,126	149	977
Gains (losses) on called debt	(1,681)	(2,352)	671	(5,985)	(5,215)	(770)
Gains (losses) on other transactions	671	1,840	(1,169)	1,386	3,192	(1,806)
Other noninterest income	595	910	(315)	3,668	3,871	(203)
Total noninterest income	\$ 8,879	\$ 10,115	\$ (1,236)	\$ 19,222	\$ 19,727	\$ (505)

Noninterest income decreased \$1.2 million for the three months ended June 30, 2015 compared to the corresponding period in 2014. The decrease was primarily due to lower loan fees and lower gains on other transactions, primarily reserve expense for unfunded commitments, partially offset by lower losses on called debt. Noninterest income decreased \$505 thousand for the six months ended June 30, 2015 compared to the corresponding period in 2014 primarily due to lower gains on other transactions, primarily reserve expense for unfunded commitments, and higher losses on called debt, partially offset by higher gains and lower impairment losses on investments.

Loan fees decreased \$851 thousand and \$295 thousand for the three and six month periods ended June 30, 2015, respectively, compared to the same period in the prior year. For the three month periods, the decrease resulted from an \$814 thousand decline in loan origination fees. The decrease for the six month period was primarily due to competitive market conditions resulting in a decrease of \$723 thousand in fee income on loan participations partially offset by a \$369 thousand increase in fee income from the first lien residential mortgage portfolio, primarily in underwriting and origination fees.

Higher fee income from crop and multi-peril insurance of \$197 thousand and \$204 thousand for the three and six month periods, respectively, was the primary reason for the increases in fees for financially related services for both the three and six month periods.

Building lease income increased \$237 thousand and \$151 thousand for the three and six month periods, respectively. Lease renegotiations in the second quarter of 2014 resulted in higher rent received in 2015 from tenants of the Bank office building.

Lower net impairment losses on investments for the six month periods of \$1.1 million resulted primarily from improvement in credit quality of home equity loans which collateralize most of the District's impaired investments. The increase in impairment losses of \$176 thousand for the three months periods resulted from writedowns of an equity investment held by several Associations.

For the six months ended June 30, 2015 gains on investments increased \$977 thousand compared to the six months ended June 30, 2014. In March 2015, the Bank sold 204 agency mortgage-backed securities totaling \$28.0 million which resulted in gains of \$1.1 million. The proceeds were used to purchase one U.S. government guaranteed security. These transactions benefitted the Bank by reducing carrying costs and improving liquidity. See discussion of investments in *Liquidity and Funding Sources* section above and in Note 3, *Investments*, in the Notes to the Combined Financial Statements for further information.

Debt issuance expense is amortized over the life of the underlying debt security. When debt securities are called prior to maturity, any unamortized issuance cost is expensed. Losses on called debt decreased \$671 thousand and increased \$770 thousand for the three and six month periods ending June 30, 2015, respectively. Call options were exercised on bonds totaling \$1.362 billion and \$3.404 billion for the three and six month periods, respectively, compared to \$2.296 billion and \$5.151 billion for the same periods in 2014. Debt is called to take advantage of favorable market interest rate changes. The amount of debt issuance cost expensed is dependent upon both the volume and remaining maturity of the debt when called. The called debt expense is more than offset by interest expense savings realized as called debt is replaced by new debt issued at a lower rate of interest. Over time, the favorable effect on net interest income is diminished as earning assets reprice downward.

For the three and six month periods, gains on other transactions decreased \$1.2 million and \$1.8 million, respectively. This decline primarily resulted from reserve expense for unfunded commitments which increased by \$896 thousand and \$1.8 million for the three and six month periods, respectively. Changes in the reserve for unfunded commitments result from fluctuations in both the balance and composition of unfunded commitments between periods. The decrease for three month periods was also due to lower gains realized on benefit trusts of \$466 thousand.

Other noninterest income decreased \$315 thousand and \$203 thousand for the three and six month periods ended June 30, 2015, respectively, compared to the same periods in the prior year. The decrease for the three month periods resulted from a decrease in captive insurance refunds. The decline for the six month periods resulted from numerous and varied income items, none of which individually had a significant decrease.

Noninterest Expenses

The following table illustrates the changes in noninterest expense:

Change in Noninterest Expenses	For the three months ended June 30,			For the six months ended June 30,		
	2015	2014	Increase/ (Decrease)	2015	2014	Increase/ (Decrease)
<i>(dollars in thousands)</i>						
Salaries and employee benefits	\$ 75,415	\$ 68,253	\$ 7,162	\$ 152,064	\$ 139,403	\$ 12,661
Occupancy and equipment	9,768	9,965	(197)	19,741	19,920	(179)
Insurance Fund premiums	7,202	6,096	1,106	14,161	12,113	2,048
Other operating expenses	27,052	27,844	(792)	53,995	55,205	(1,210)
Losses (gains) from other property owned	(391)	(100)	(291)	140	(128)	268
Total noninterest expenses	\$ 119,046	\$ 112,058	\$ 6,988	\$ 240,101	\$ 226,513	\$ 13,588

Noninterest expense increased \$7.0 million and \$13.6 million for the three and six months ended June 30, 2015, respectively, compared to the corresponding period in 2014. For both periods, the increase was due primarily to an increase in salaries and employee benefits and higher insurance fund premiums, partially offset by a decrease in other operating expenses.

Salaries and employee benefits increased \$7.2 million and \$12.7 million for the three and six month periods, respectively. For the three and six month periods ended June 30, 2015 compared to the same periods in 2014, this increase resulted primarily from a \$2.2 million and \$3.1 million increase, respectively, in salaries due mainly to normal salary administration and a \$4.5 million and \$9.2 million increase, respectively, in pension and other postretirement benefits expenses. The higher pension and other postretirement expenses in 2015 resulted primarily from a decrease in the discount rate in 2015 used to calculate net periodic pension and other postretirement benefit costs as well as from the adoption of updated mortality tables reflecting increases in life expectancy.

Occupancy and equipment expense decreased \$197 thousand and \$179 thousand for the three and six month periods in 2015 compared to the same periods in 2014, respectively. Lower hardware and software maintenance costs were the main reason for the decline for both periods.

Insurance Fund premiums increased \$1.1 million and \$2.0 million for the three and six month periods in 2015, respectively, compared to the same periods in 2014. This increase resulted primarily from an increase in the base annual premium rate and a change in the composition of the Bank's investment portfolio. The base annual premium rate was increased to 13 basis points in 2015 from 12 basis points in 2014. The FCSIC Board makes premium rate adjustments, as necessary, to maintain the secure base amount which is based upon insured debt outstanding at System banks. The Bank's investment portfolio in 2015 has reflected a reduction in federally guaranteed investments and an increase in GSE guaranteed and other investments compared to 2014, resulting in less of the investment portfolio balance excluded from the insurance premium calculation.

Other operating expenses decreased \$792 thousand and \$1.2 million for the three and six month periods ended June 30, 2015, respectively, compared to the same periods in 2014. The decline for the three month periods resulted primarily from the timing of consulting and service provider fees required for system enhancements which resulted in a decrease of \$706 thousand. The primary reason for the decrease for the six month periods was \$1.1 million in lower nonaccrual loan period costs, primarily legal fees and property taxes.

Gains on other property owned increased \$291 thousand and decreased \$268 thousand for the three and six month periods in 2015, respectively, compared with the same period in the prior year. Both the three and six months periods reflected lower writedowns and lower expenses for OPO. For the three month periods, the decrease was partially offset by lower gains on sales. For the six month periods, the decrease was exceeded by lower gains on sales. See *Other Property Owned* section above for further information.

REGULATORY MATTERS

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

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

On September 4, 2014, the FCA published a proposed rule in the Federal Register to modify the regulatory capital requirements for System banks and associations. The initial public comment period ended on February 16, 2015. On June 15, 2015, the Farm Credit Administration reopened the comment period from June 26 to July 10, 2015. The stated objectives of the proposed rule are as follows:

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

FINANCIAL REGULATORY REFORM

See discussion of the Dodd-Frank Act in the Financial Regulatory Reform section of the 2014 Annual Report of AgFirst Farm Credit Bank and District Associations.

RECENTLY ISSUED ACCOUNTING PRONOUNCEMENTS

Please refer to Note 1, *Organization, Significant Accounting Policies, and Recently Issued Accounting Pronouncements*, in the Notes to the Combined Financial Statements, and the 2014 Annual Report of AgFirst Farm Credit Bank and District Associations for recently issued accounting pronouncements.

NOTE: Shareholder investment in a District 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, Reporting Manager, AgFirst Farm Credit Bank, P.O. Box 1499, Columbia, SC 29202. Combined information concerning AgFirst Farm Credit Bank and District Associations can also be obtained at the Bank's website, www.agfirst.com. AgFirst prepares a quarterly report within 40 days after the end of each fiscal quarter, except that no quarterly report need be prepared for the fiscal quarter that coincides with the end of the fiscal year of the institution.

Combined Balance Sheets

<i>(dollars in thousands)</i>	June 30, 2015 <i>(unaudited)</i>	December 31, 2014 <i>(audited)</i>
Assets		
Cash	\$ 158,681	\$ 671,342
Cash equivalents	225,408	224,847
Investment securities:		
Available for sale (amortized cost of \$6,615,970 and \$6,646,772, respectively)	6,709,952	6,754,419
Held to maturity (fair value of \$762,660 and \$819,047, respectively)	743,174	788,939
Total investment securities	7,453,126	7,543,358
Loans held for sale	13,870	7,185
Loans	24,722,683	24,415,969
Allowance for loan losses	(178,579)	(174,853)
Net loans	24,544,104	24,241,116
Accrued interest receivable	197,357	184,705
Accounts receivable	50,282	64,218
Investments in other Farm Credit System institutions	29,682	28,885
Other investments	80	251
Premises and equipment, net	187,911	190,833
Other property owned	40,520	45,986
Other assets	70,276	69,241
Total assets	\$ 32,971,297	\$ 33,271,967
Liabilities		
Systemwide bonds payable	\$ 21,850,508	\$ 22,814,656
Systemwide notes payable	4,870,236	4,243,708
Accrued interest payable	52,015	47,528
Accounts payable	40,334	230,196
Advanced conditional payments	9,264	8,468
Other liabilities	501,263	525,052
Total liabilities	27,323,620	27,869,608
Commitments and contingencies (Note 8)		
Shareholders' Equity		
Perpetual preferred stock	125,250	125,250
Protected borrower equity	622	655
Capital stock and participation certificates	165,893	154,471
Additional paid-in-capital	60,270	60,270
Retained earnings		
Allocated	1,790,601	1,818,123
Unallocated	3,797,878	3,540,901
Accumulated other comprehensive income (loss)	(292,837)	(297,311)
Total shareholders' equity	5,647,677	5,402,359
Total liabilities and equity	\$ 32,971,297	\$ 33,271,967

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

Combined Statements of Income

(unaudited)

<i>(dollars in thousands)</i>	For the three months ended June 30,		For the six months ended June 30,	
	2015	2014	2015	2014
Interest Income				
Investments	\$ 29,665	\$ 33,501	\$ 61,136	\$ 68,749
Loans	281,136	273,799	556,145	543,757
Total interest income	310,801	307,300	617,281	612,506
Interest Expense				
	60,557	51,415	119,056	104,987
Net interest income	250,244	255,885	498,225	507,519
Provision for (reversal of allowance for) loan losses	3,392	(316)	5,105	(2,660)
Net interest income after provision for (reversal of allowance for) loan losses	246,852	256,201	493,120	510,179
Noninterest Income				
Loan fees	6,956	7,807	14,501	14,796
Fees for financially related services	1,715	1,348	3,066	2,693
Building lease income	900	663	1,844	1,693
Total other-than-temporary impairment losses	(171)	—	(171)	(74)
Portion of loss recognized in other comprehensive income	(106)	(101)	(213)	(1,378)
Net other-than-temporary impairment losses	(277)	(101)	(384)	(1,452)
Gains (losses) on investments, net	—	—	1,126	149
Gains (losses) on called debt	(1,681)	(2,352)	(5,985)	(5,215)
Gains (losses) on other transactions	671	1,840	1,386	3,192
Other noninterest income	595	910	3,668	3,871
Total noninterest income	8,879	10,115	19,222	19,727
Noninterest Expenses				
Salaries and employee benefits	75,415	68,253	152,064	139,403
Occupancy and equipment	9,768	9,965	19,741	19,920
Insurance Fund premiums	7,202	6,096	14,161	12,113
Other operating expenses	27,052	27,844	53,995	55,205
Losses (gains) from other property owned	(391)	(100)	140	(128)
Total noninterest expenses	119,046	112,058	240,101	226,513
Income before income taxes	136,685	154,258	272,241	303,393
Provision for income taxes	505	370	937	910
Net income	\$136,180	\$153,888	\$271,304	\$302,483

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

Combined Statements of Comprehensive Income

(unaudited)

<i>(dollars in thousands)</i>	For the three months ended June 30,		For the six months ended June 30,	
	2015	2014	2015	2014
Net income	\$ 136,180	\$ 153,888	\$ 271,304	\$ 302,483
Other comprehensive income net of tax:				
Unrealized gains (losses) on investments:				
Other-than-temporarily impaired	(505)	2,492	1,489	9,421
Not other-than-temporarily impaired	(10,635)	1,679	(15,184)	1,209
Change in value of cash flow hedges	(115)	(191)	(268)	(454)
Employee benefit plans adjustments	9,218	5,097	18,437	10,193
Other comprehensive income (Note 5)	(2,037)	9,077	4,474	20,369
Comprehensive income	\$ 134,143	\$ 162,965	\$ 275,778	\$ 322,852

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

Combined Statements of Changes in Shareholders' Equity

(unaudited)

(dollars in thousands)	Perpetual Preferred Stock	Protected Borrower Equity	Capital Stock and Participation Certificates	Additional Paid-in-Capital	Retained Earnings		Accumulated Other Comprehensive Income	Total Shareholders' Equity
					Allocated	Unallocated		
Balance at December 31, 2013	\$ 125,250	\$ 901	\$ 156,382	\$ 60,270	\$ 1,693,689	\$ 3,313,471	\$ (175,289)	\$ 5,174,674
Comprehensive income						302,483	20,369	322,852
Protected borrower equity retired		(76)						(76)
Capital stock/participation certificates issued (retired), net			2,511					2,511
Dividends declared/paid			227			(325)		(98)
Dividends paid on perpetual preferred stock						(866)		(866)
Cash patronage distribution						(9,500)		(9,500)
Retained earnings retired					(35,998)	61		(35,937)
Patronage distribution adjustment			(5)		335	(627)		(297)
Balance at June 30, 2014	\$ 125,250	\$ 825	\$ 159,115	\$ 60,270	\$ 1,658,026	\$ 3,604,697	\$ (154,920)	\$ 5,453,263
Balance at December 31, 2014	\$ 125,250	\$ 655	\$ 154,471	\$ 60,270	\$ 1,818,123	\$ 3,540,901	\$ (297,311)	\$ 5,402,359
Comprehensive income						271,304	4,474	275,778
Protected borrower equity retired		(33)						(33)
Capital stock/participation certificates issued (retired), net			11,174					11,174
Dividends declared/paid			248			(342)		(94)
Dividends paid on perpetual preferred stock						(877)		(877)
Cash patronage distribution						(6,000)		(6,000)
Retained earnings retired					(35,050)	33		(35,017)
Patronage distribution adjustment					7,528	(7,141)		387
Balance at June 30, 2015	\$ 125,250	\$ 622	\$ 165,893	\$ 60,270	\$ 1,790,601	\$ 3,797,878	\$ (292,837)	\$ 5,647,677

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

Combined Statements of Cash Flows

(unaudited)

For the six months
ended June 30,

(dollars in thousands)

	2015	2014
Cash flows from operating activities:		
Net income	\$ 271,304	\$ 302,483
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation on premises and equipment	9,317	9,034
Amortization of net deferred loan (fees) costs and premium amortization (discount accretion)	(1,288)	(2,151)
Premium amortization (discount accretion) on investment securities	4,883	4,472
(Premium amortization) discount accretion on bonds and notes	3,756	3,421
Amortization (accretion) of yield mark resulting from merger	(1,084)	(1,216)
Provision for (reversal of allowance for) loan losses	5,105	(2,660)
(Gains) losses on other property owned	(109)	(2,683)
Net impairment losses on investments	384	1,452
(Gains) losses on investments, net	(1,126)	(149)
(Gains) losses on other transactions	(1,386)	(3,192)
Net change in loans held for sale	(23)	1,695
Changes in operating assets and liabilities:		
(Increase) decrease in accrued interest receivable	(12,652)	(12,632)
(Increase) decrease in accounts receivable	13,936	(1,249)
(Increase) decrease in other assets	(6,273)	(2,720)
Increase (decrease) in accrued interest payable	4,487	(9,463)
Increase (decrease) in accounts payable	(17,416)	11,002
Increase (decrease) in other liabilities	(6,056)	(3,697)
Total adjustments	(5,545)	(10,736)
Net cash provided by (used in) operating activities	265,759	291,747
Cash flows from investing activities:		
Investment securities purchased	(830,433)	(365,784)
Proceeds from investment securities sold or matured	902,782	696,767
Net (increase) decrease in loans	(323,620)	(479,930)
(Increase) decrease in investments in other Farm Credit System institutions	(797)	(731)
Proceeds from payments received on other investments	—	83,954
Purchase of premises and equipment, net	(6,790)	(22,511)
Proceeds from sale of premises and equipment, net	1,010	1,151
Proceeds from sale of other property owned	18,122	40,400
Net cash provided by (used in) investing activities	(239,726)	(46,684)
Cash flows from financing activities:		
Bonds and notes issued	11,388,116	12,560,870
Bonds and notes retired	(11,724,139)	(13,086,408)
Net increase (decrease) in advanced conditional payments	796	3,608
Protected borrower equity retired	(33)	(76)
Capital stock and participation certificates issued/retired, net	11,174	2,511
Patronage refunds and dividends paid	(178,153)	(152,308)
Dividends paid on perpetual preferred stock	(877)	(866)
Retained earnings retired	(35,017)	(35,937)
Net cash provided by (used in) financing activities	(538,133)	(708,606)
Net increase (decrease) in cash and cash equivalents	(512,100)	(463,543)
Cash and cash equivalents, beginning of period	896,189	1,230,374
Cash and cash equivalents, end of period	\$ 384,089	\$ 766,831
Supplemental schedule of non-cash investing and financing activities:		
Financed sales of other property owned	\$ 1,693	\$ 1,699
Receipt of property in settlement of loans	14,240	21,922
Change in unrealized gains (losses) on investments, net	(13,695)	10,630
Employee benefit plans adjustments (Note 7)	(18,437)	(10,193)
Non-cash changes related to interest rate hedging activities:		
Increase (decrease) in bonds and notes	\$ (5,238)	\$ (5,142)
Decrease (increase) in other assets	5,238	5,142
Supplemental information:		
Interest paid	\$ 110,930	\$ 111,290
Taxes paid, net	477	1,161

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

Notes to the Combined Financial Statements

(unaudited)

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

Organization

The accompanying combined financial statements include the accounts of AgFirst Farm Credit Bank (AgFirst or Bank) and its related Agricultural Credit Associations (Associations or District Associations), collectively referred to as the AgFirst District (District). A complete description of the organization and operations, the significant accounting policies followed, and the financial condition and results of operations of the District as of and for the year ended December 31, 2014 are contained in the 2014 Annual Report to Shareholders. These unaudited interim financial statements should be read in conjunction with the latest Annual Report to Shareholders.

Basis of Presentation

In the opinion of management, the accompanying combined 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 combined 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 those to be expected for a full year.

Significant Accounting Policies

The District'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 loan losses (Note 2, *Loans and Allowance for Loan Losses*), investment securities and other-than-temporary impairment (Note 3, *Investments*), and financial instruments (Note 6, *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 Updates (ASUs) Issued During the Period

The following ASUs were issued by the Financial Accounting Standards Board (FASB) since the most recent Annual Report:

- 2015-10 Technical Corrections and Improvements – In June, 2015, the FASB issued ASU 2015-10, Technical Corrections and Improvements (numerous Topics). The amendments in the Update represent changes to make minor corrections or minor improvements to the Codification that are not expected to have a significant effect on current accounting practice or create a significant administrative cost to most entities. The amendments that require transition guidance are effective for all entities for fiscal years, and interim periods within those fiscal years, beginning after December 15, 2015. Early adoption is permitted, including adoption in an interim period. All other amendments were effective upon the issuance of the Update.

- 2015-07 Fair Value Measurement – In May, 2015, the FASB issued ASU 2015-07, Fair Value Measurement (Topic 820): Disclosures for Investments in Certain Entities That Calculate Net Asset Value per Share (or Its Equivalent). Topic 820 permits a reporting entity, as a practical expedient, to measure the fair value of certain investments using the net asset value per share of the investment. Currently, investments valued using the practical expedient are categorized within the fair value hierarchy on the basis of whether the investment is redeemable with the investee at net asset value on the measurement date, never redeemable with the investee at net asset value, or redeemable with the investee at net asset value at a future date. To address diversity in practice related to how certain investments measured at net asset value with future redemption dates are categorized, the amendments in this Update remove the requirement to categorize investments for which fair values are measured using the net asset value per share practical expedient. It also limits disclosures to investments for which the entity has elected to measure the fair value using the practical expedient. For public business entities, the guidance is effective for fiscal years beginning after December 15, 2015, and interim periods within those fiscal years. For all other entities, the guidance is effective for fiscal years beginning after December 15, 2016, and interim periods within those fiscal years. Earlier application is permitted. The guidance is to be applied retrospectively to all periods presented. Application of this guidance is not expected to have an impact on the District's financial condition or results of operations, but will require modifications to footnote disclosures.
- 2015-03 Imputation of Interest – In April, 2015, the FASB issued ASU 2015-03, Interest—Imputation of Interest (Subtopic 835-30): Simplifying the Presentation of Debt Issuance Costs. To simplify presentation of debt issuance costs, the amendments in this Update require that debt issuance costs related to a recognized debt liability be presented in the balance sheet as a direct deduction from the carrying amount of that debt liability, consistent with debt discounts. Prior to the Update, debt issuance costs were required to be presented in the balance sheet as a deferred charge (asset). The recognition and measurement guidance for debt issuance costs are not affected by the amendments. For public business entities, the amendments in this Update are effective for financial statements issued for fiscal years beginning after December 15, 2015, and interim periods within those fiscal years. Based on the balance at June 30, 2015, this guidance would result in a reclassification of approximately \$19.9 million from Other Assets to Systemwide Bonds Payable.

ASUs Pending Effective Date

For a detailed description of the ASUs below, see the latest Annual Report to Shareholders.

Potential effects of ASUs issued in previous periods:

- 2014-09 Revenue from Contracts with Customers – On July 9, 2015, the FASB voted to delay the effective date by one year. A final ASU reflecting the revised effective date will be issued in third quarter of 2015.

ASUs Effective During the Period

There were no changes in the accounting principles applied from the latest Annual Report, other than any discussed below. No recently adopted accounting guidance issued by the FASB had a significant effect on the current period reporting. See the most recent Annual Report for a detailed description of each of the ASUs below.

Impact of ASUs which became effective during the period:

- 2014-14 Classification of Certain Government-Guaranteed Mortgage Loans – The District did not have a significant amount of loans that met the criteria of the guidance.
- 2014-11 Repurchase-to-Maturity Transactions – The criteria of the standard were not significantly different from the District's policy in place at adoption.
- 2014-08 Discontinued Operations – The District has not had and does not anticipate any significant disposals.
- 2014-04 Reclassification of Consumer Mortgage Loans – The criteria of the standard were not significantly different from the District's policy in place at adoption. The amendment was adopted prospectively. See Note 2, *Loans and Allowance for Loan Losses*, for the additional disclosures required by this guidance.

Note 2 — Loans and Allowance for Loan Losses

The District 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 District has been identified. See Note 3, *Loans and Allowance for Loan Losses*, from the latest Annual Report for further discussion.

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

A summary of loans outstanding at period end follows:

<i>(dollars in thousands)</i>	June 30, 2015	December 31, 2014
Real estate mortgage	\$ 11,063,436	\$ 10,749,817
Production and intermediate-term	7,501,544	7,650,543
Loans to cooperatives	245,526	261,652
Processing and marketing	1,463,561	1,404,051
Farm-related business	428,296	410,026
Communication	365,156	356,825
Energy and water/waste disposal	437,379	468,589
Rural residential real estate	3,032,383	2,954,004
International	19,809	-
Lease receivables	3,913	4,945
Loans to other financing institutions (OFIs)	104,633	95,512
Other (including Mission Related)	57,047	60,005
Total Loans	<u>\$ 24,722,683</u>	<u>\$ 24,415,969</u>

The District 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:

<i>(dollars in thousands)</i>	June 30, 2015					
	Within Farm Credit System		Outside Farm Credit System		Total	
	Participations Purchased	Participations Sold	Participations Purchased	Participations Sold	Participations Purchased	Participations Sold
Real estate mortgage	\$ 254,603	\$ 47,048	\$ 59,164	\$ 4,557	\$ 313,767	\$ 51,605
Production and intermediate-term	600,963	267,693	414,023	33,280	1,014,986	300,973
Loans to cooperatives	212,069	-	15,508	-	227,577	-
Processing and marketing	603,092	175,755	898,318	-	1,501,410	175,755
Farm-related business	93,618	8,899	123,208	-	216,826	8,899
Communication	366,343	-	-	-	366,343	-
Energy and water/waste disposal	432,788	-	6,331	-	439,119	-
Rural residential real estate	-	-	2,350	-	2,350	-
International	19,829	-	-	-	19,829	-
Lease receivables	2,053	-	-	-	2,053	-
Other (including Mission Related)	12,000	-	6,702	-	18,702	-
Total	<u>\$ 2,597,358</u>	<u>\$ 499,395</u>	<u>\$ 1,525,604</u>	<u>\$ 37,837</u>	<u>\$ 4,122,962</u>	<u>\$ 537,232</u>

	December 31, 2014					
	Within Farm Credit System		Outside Farm Credit System		Total	
	Participations Purchased	Participations Sold	Participations Purchased	Participations Sold	Participations Purchased	Participations Sold
<i>(dollars in thousands)</i>						
Real estate mortgage	\$ 255,972	\$ 41,303	\$ 74,472	\$ 4,530	\$ 330,444	\$ 45,833
Production and intermediate-term	582,468	366,108	469,793	34,034	1,052,261	400,142
Loans to cooperatives	226,648	—	10,993	—	237,641	—
Processing and marketing	600,381	186,418	839,640	—	1,440,021	186,418
Farm-related business	119,902	1,743	87,567	—	207,469	1,743
Communication	357,623	—	—	—	357,623	—
Energy and water/waste disposal	463,833	—	6,524	—	470,357	—
Rural residential real estate	—	—	2,261	—	2,261	—
Lease receivables	2,663	—	—	—	2,663	—
Other (including Mission Related)	12,000	—	7,623	—	19,623	—
Total	\$ 2,621,490	\$ 595,572	\$ 1,498,873	\$ 38,564	\$ 4,120,363	\$ 634,136

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

	June 30, 2015			
	Due less than 1 year	Due 1 through 5 years	Due after 5 years	Total
<i>(dollars in thousands)</i>				
Real estate mortgage	\$ 524,069	\$ 2,525,165	\$ 8,014,202	\$ 11,063,436
Production and intermediate-term	2,112,580	3,337,548	2,051,416	7,501,544
Loans to cooperatives	58,643	112,316	74,567	245,526
Processing and marketing	69,852	819,300	574,409	1,463,561
Farm-related business	64,179	273,476	90,641	428,296
Communication	—	344,515	20,641	365,156
Energy and water/waste disposal	1,753	159,659	275,967	437,379
Rural residential real estate	35,701	71,245	2,925,437	3,032,383
International	—	19,809	—	19,809
Lease receivables	1,887	2,026	—	3,913
Loans to OFIs	104,633	—	—	104,633
Other (including Mission Related)	2,058	14,887	40,102	57,047
Total Loans	\$ 2,975,355	\$ 7,679,946	\$ 14,067,382	\$ 24,722,683
Percentage	12.03%	31.07%	56.90%	100.00%

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

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

	June 30, 2015	December 31, 2014		June 30, 2015	December 31, 2014
Real estate mortgage:			Energy and water/waste disposal:		
Acceptable	94.19%	93.38%	Acceptable	87.54%	90.91%
OAEM	2.93	3.17	OAEM	12.46	8.79
Substandard/doubtful/loss	2.88	3.45	Substandard/doubtful/loss	—	0.30
	<u>100.00%</u>	<u>100.00%</u>		<u>100.00%</u>	<u>100.00%</u>
Production and intermediate-term:			Rural residential real estate:		
Acceptable	92.65%	92.66%	Acceptable	99.25%	99.21%
OAEM	3.49	3.86	OAEM	0.28	0.30
Substandard/doubtful/loss	3.86	3.48	Substandard/doubtful/loss	0.47	0.49
	<u>100.00%</u>	<u>100.00%</u>		<u>100.00%</u>	<u>100.00%</u>
Loans to cooperatives:			International:		
Acceptable	99.91%	99.25%	Acceptable	100.00%	—%
OAEM	0.09	0.75	OAEM	—	—
Substandard/doubtful/loss	—	—	Substandard/doubtful/loss	—	—
	<u>100.00%</u>	<u>100.00%</u>		<u>100.00%</u>	<u>—%</u>
Processing and marketing:			Lease receivables:		
Acceptable	96.79%	97.72%	Acceptable	96.32%	96.72%
OAEM	0.49	0.50	OAEM	3.07	2.66
Substandard/doubtful/loss	2.72	1.78	Substandard/doubtful/loss	0.61	0.62
	<u>100.00%</u>	<u>100.00%</u>		<u>100.00%</u>	<u>100.00%</u>
Farm-related business:			Loans to OFIs:		
Acceptable	96.60%	98.05%	Acceptable	100.00%	100.00%
OAEM	0.79	1.31	OAEM	—	—
Substandard/doubtful/loss	2.61	0.64	Substandard/doubtful/loss	—	—
	<u>100.00%</u>	<u>100.00%</u>		<u>100.00%</u>	<u>100.00%</u>
Communication:			Other (including Mission Related):		
Acceptable	97.48%	97.73%	Acceptable	96.09%	89.16%
OAEM	2.52	2.27	OAEM	—	5.17
Substandard/doubtful/loss	—	—	Substandard/doubtful/loss	3.91	5.67
	<u>100.00%</u>	<u>100.00%</u>		<u>100.00%</u>	<u>100.00%</u>
			Total Loans:		
			Acceptable	94.55%	94.28%
			OAEM	2.71	2.92
			Substandard/doubtful/loss	2.74	2.80
				<u>100.00%</u>	<u>100.00%</u>

The following tables provide an age analysis of the recorded investment in past due loans as of:

	June 30, 2015					Recorded Investment 90 Days or More Past Due and Accruing Interest
	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	
<i>(dollars in thousands)</i>						
Real estate mortgage	\$ 49,418	\$ 48,306	\$ 97,724	\$ 11,064,914	\$ 11,162,638	\$ 893
Production and intermediate-term	32,505	51,654	84,159	7,486,744	7,570,903	1,049
Loans to cooperatives	—	—	—	246,037	246,037	—
Processing and marketing	1,417	1,228	2,645	1,463,993	1,466,638	—
Farm-related business	712	331	1,043	429,002	430,045	—
Communication	—	—	—	365,423	365,423	—
Energy and water/waste disposal	—	—	—	438,690	438,690	—
Rural residential real estate	8,812	3,845	12,657	3,031,022	3,043,679	1,237
International	—	—	—	19,809	19,809	—
Lease receivables	8	12	20	3,899	3,919	—
Loans to OFIs	—	—	—	104,776	104,776	—
Other (including Mission Related)	—	835	835	56,830	57,665	149
Total	\$ 92,872	\$ 106,211	\$ 199,083	\$ 24,711,139	\$ 24,910,222	\$ 3,328

December 31, 2014

<i>(dollars in thousands)</i>	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	\$ 60,519	\$ 61,763	\$ 122,282	\$ 10,715,330	\$ 10,837,612	\$ 712
Production and intermediate-term	27,730	60,645	88,375	7,629,402	7,717,777	2,130
Loans to cooperatives	12	-	12	262,190	262,202	-
Processing and marketing	109	1,567	1,676	1,405,430	1,407,106	-
Farm-related business	116	631	747	410,725	411,472	-
Communication	-	-	-	357,083	357,083	-
Energy and water/waste disposal	-	-	-	470,614	470,614	-
Rural residential real estate	40,678	5,314	45,992	2,918,662	2,964,654	2,382
Lease receivables	-	15	15	4,940	4,955	-
Loans to OFIs	-	-	-	95,646	95,646	-
Other (including Mission Related)	779	2,632	3,411	57,226	60,637	-
Total	\$ 129,943	\$ 132,567	\$ 262,510	\$ 24,327,248	\$ 24,589,758	\$ 5,224

Nonperforming assets (including the recorded investment for loans) and related credit quality statistics are summarized as follows:

<i>(dollars in thousands)</i>	June 30, 2015	December 31, 2014
Nonaccrual loans:		
Real estate mortgage	\$ 132,340	\$ 174,528
Production and intermediate-term	111,639	115,917
Processing and marketing	15	5,693
Farm-related business	13,360	3,416
Energy and water/waste disposal	19	1,400
Rural residential real estate	6,783	7,378
Lease receivables	12	15
Other (including Mission Related)	1,458	2,627
Total	\$ 265,626	\$ 310,974
Accruing restructured loans:		
Real estate mortgage	\$ 52,972	\$ 59,690
Production and intermediate-term	51,806	58,536
Farm-related business	733	761
Rural residential real estate	2,470	3,000
Other (including Mission Related)	9,335	9,532
Total	\$ 117,316	\$ 131,519
Accruing loans 90 days or more past due:		
Real estate mortgage	\$ 893	\$ 712
Production and intermediate-term	1,049	2,130
Rural residential real estate	1,237	2,382
Other (including Mission Related)	149	-
Total	\$ 3,328	\$ 5,224
Total nonperforming loans	\$ 386,270	\$ 447,717
Other property owned	40,520	45,986
Total nonperforming assets	\$ 426,790	\$ 493,703
Nonaccrual loans as a percentage of total loans	1.07%	1.27%
Nonperforming assets as a percentage of total loans and other property owned	1.72%	2.02%
Nonperforming assets as a percentage of capital	7.56%	9.14%

The following table presents information related to the recorded investment of impaired loans 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.

<i>(dollars in thousands)</i>	June 30, 2015	December 31, 2014
Impaired nonaccrual loans:		
Current as to principal and interest	\$ 138,174	\$ 155,112
Past due	127,452	155,862
Total	<u>265,626</u>	<u>310,974</u>
Impaired accrual loans:		
Restructured	117,316	131,519
90 days or more past due	3,328	5,224
Total	<u>120,644</u>	<u>136,743</u>
Total impaired loans	<u>\$ 386,270</u>	<u>\$ 447,717</u>
Additional commitments to lend	<u>\$ 8,782</u>	<u>\$ 6,832</u>

Additional impaired loan information at period end is summarized as follows. Unpaid principal balance represents the contractual principal balance of the loan.

<i>(dollars in thousands)</i>	June 30, 2015			Quarter Ended June 30, 2015		Six Months Ended June 30, 2015	
	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
With a related allowance for credit losses:							
Real estate mortgage	\$ 50,861	\$ 58,025	\$ 10,756	\$ 54,284	\$ 633	\$ 58,961	\$ 1,010
Production and intermediate-term	53,638	77,425	15,954	59,953	293	56,806	1,011
Processing and marketing	-	-	-	-	-	-	-
Farm-related business	13,430	14,051	2,197	13,628	188	8,391	216
Energy and water/waste disposal	19	-	19	20	(14)	697	-
Rural residential real estate	2,758	3,141	688	2,822	31	3,114	54
Lease receivables	-	-	-	-	-	-	-
Other (including Mission Related)	7,916	7,902	580	8,038	150	7,913	233
Total	<u>\$ 128,622</u>	<u>\$ 160,544</u>	<u>\$ 30,194</u>	<u>\$ 138,745</u>	<u>\$ 1,281</u>	<u>\$ 135,882</u>	<u>\$ 2,524</u>
With no related allowance for credit losses:							
Real estate mortgage	\$ 135,344	\$ 192,194	\$ -	\$ 137,000	\$ 3,042	\$ 146,006	\$ 4,182
Production and intermediate-term	110,856	156,307	-	115,511	873	116,788	2,567
Processing and marketing	15	4,586	-	15	(61)	2,938	-
Farm-related business	663	1,194	-	676	7	736	15
Energy and water/waste disposal	-	-	-	-	-	-	-
Rural residential real estate	7,732	10,021	-	7,183	70	6,894	140
Lease receivables	12	66	-	12	-	12	-
Other (including Mission Related)	3,026	3,809	-	3,064	67	3,814	80
Total	<u>\$ 257,648</u>	<u>\$ 368,177</u>	<u>\$ -</u>	<u>\$ 263,461</u>	<u>\$ 3,998</u>	<u>\$ 277,188</u>	<u>\$ 6,984</u>
Total:							
Real estate mortgage	\$ 186,205	\$ 250,219	\$ 10,756	\$ 191,284	\$ 3,675	\$ 204,967	\$ 5,192
Production and intermediate-term	164,494	233,732	15,954	175,464	1,166	173,594	3,578
Processing and marketing	15	4,586	-	15	(61)	2,938	-
Farm-related business	14,093	15,245	2,197	14,304	195	9,127	231
Energy and water/waste disposal	19	-	19	20	(14)	697	-
Rural residential real estate	10,490	13,162	688	10,005	101	10,008	194
Lease receivables	12	66	-	12	-	12	-
Other (including Mission Related)	10,942	11,711	580	11,102	217	11,727	313
Total	<u>\$ 386,270</u>	<u>\$ 528,721</u>	<u>\$ 30,194</u>	<u>\$ 402,206</u>	<u>\$ 5,279</u>	<u>\$ 413,070</u>	<u>\$ 9,508</u>

AgFirst Farm Credit Bank and District Associations

<i>(dollars in thousands)</i>	December 31, 2014			Year Ended December 31, 2014	
Impaired Loans	Recorded Investment	Unpaid Principal Balance	Related Allowance	Average Impaired Loans	Interest Income Recognized on Impaired Loans
With a related allowance for credit losses:					
Real estate mortgage	\$ 66,102	\$ 83,694	\$ 13,671	\$ 70,001	\$ 2,799
Production and intermediate-term	55,710	68,737	16,858	68,642	2,610
Processing and marketing	5,684	5,684	745	5,987	357
Farm-related business	3,377	3,895	370	3,539	191
Energy and water/waste disposal	1,400	1,426	805	685	88
Rural residential real estate	3,136	3,497	900	3,623	159
Lease receivables	—	—	—	—	—
Other (including Mission Related)	8,069	8,070	574	9,357	425
Total	<u>\$ 143,478</u>	<u>\$ 175,003</u>	<u>\$ 33,923</u>	<u>\$ 161,834</u>	<u>\$ 6,629</u>
With no related allowance for credit losses:					
Real estate mortgage	\$ 168,828	\$ 226,865	\$ —	\$ 180,094	\$ 7,499
Production and intermediate-term	120,873	172,489	—	123,154	6,507
Processing and marketing	9	5,529	—	237	—
Farm-related business	800	1,254	—	839	45
Communication	—	—	—	—	—
Energy and water/waste disposal	—	—	—	—	—
Rural residential real estate	9,624	11,674	—	10,914	396
Lease receivables	15	69	—	19	1
Other (including Mission Related)	4,090	4,827	—	3,631	163
Total	<u>\$ 304,239</u>	<u>\$ 422,707</u>	<u>\$ —</u>	<u>\$ 318,888</u>	<u>\$ 14,611</u>
Total:					
Real estate mortgage	\$ 234,930	\$ 310,559	\$ 13,671	\$ 250,095	\$ 10,298
Production and intermediate-term	176,583	241,226	16,858	191,796	9,117
Processing and marketing	5,693	11,213	745	6,224	357
Farm-related business	4,177	5,149	370	4,378	236
Communication	—	—	—	—	—
Energy and water/waste disposal	1,400	1,426	805	685	88
Rural residential real estate	12,760	15,171	900	14,537	555
Lease receivables	15	69	—	19	1
Other (including Mission Related)	12,159	12,897	574	12,988	588
Total	<u>\$ 447,717</u>	<u>\$ 597,710</u>	<u>\$ 33,923</u>	<u>\$ 480,722</u>	<u>\$ 21,240</u>

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

(dollars in thousands)	Real Estate Mortgage	Production and Intermediate-term	Agribusiness*	Communication	Energy and Water/Waste Disposal	Rural Residential Real Estate	Lease Receivables	Other***	Total
Activity related to the allowance for credit losses:									
Balance at March 31, 2015	\$ 70,884	\$ 82,272	\$ 12,025	\$ 1,659	\$ 2,367	\$ 5,934	\$ 65	\$ 940	\$ 176,146
Charge-offs	(698)	(1,510)	—	—	(414)	(145)	—	—	(2,767)
Recoveries	821	968	7	—	—	7	—	5	1,808
Provision for loan losses	1,522	950	946	213	(211)	(12)	2	(18)	3,392
Loan type reclassifications	(1,753)	1,084	669	—	—	—	—	—	—
Balance at June 30, 2015	\$ 70,776	\$ 83,764	\$ 13,647	\$ 1,872	\$ 1,742	\$ 5,784	\$ 67	\$ 927	\$ 178,579
Balance at December 31, 2014	\$ 69,773	\$ 82,467	\$ 11,930	\$ 1,519	\$ 2,406	\$ 5,681	\$ 80	\$ 997	\$ 174,853
Charge-offs	(1,626)	(3,110)	—	—	(414)	(249)	—	—	(5,399)
Recoveries	1,546	1,465	985	—	—	14	—	10	4,020
Provision for loan losses	2,836	1,906	63	353	(250)	338	(13)	(128)	5,105
Loan type reclassifications	(1,753)	1,036	669	—	—	—	—	48	—
Balance at June 30, 2015	\$ 70,776	\$ 83,764	\$ 13,647	\$ 1,872	\$ 1,742	\$ 5,784	\$ 67	\$ 927	\$ 178,579
Balance at March 31, 2014	\$ 74,016	\$ 90,441	\$ 10,898	\$ 1,108	\$ 1,643	\$ 7,443	\$ 82	\$ 917	\$ 186,548
Charge-offs	(1,761)	(3,404)	—	—	—	(108)	—	—	(5,273)
Recoveries	2,213	2,596	591	—	—	43	—	246	5,689
Provision for loan losses	(2,428)	2,389	(1,452)	186	(113)	1,213	(6)	(105)	(316)
Balance at June 30, 2014	\$ 72,040	\$ 92,022	\$ 10,037	\$ 1,294	\$ 1,530	\$ 8,591	\$ 76	\$ 1,058	\$ 186,648
Balance at December 31, 2013	\$ 74,933	\$ 92,180	\$ 10,049	\$ 1,065	\$ 1,427	\$ 6,487	\$ 91	\$ 1,205	\$ 187,437
Charge-offs	(3,444)	(4,554)	(1)	—	—	(198)	—	—	(8,197)
Recoveries	3,780	3,820	2,156	—	—	62	—	250	10,068
Provision for loan losses	(3,229)	576	(2,167)	229	103	2,240	(15)	(397)	(2,660)
Balance at June 30, 2014	\$ 72,040	\$ 92,022	\$ 10,037	\$ 1,294	\$ 1,530	\$ 8,591	\$ 76	\$ 1,058	\$ 186,648
Allowance on loans evaluated for impairment:									
Individually	\$ 10,599	\$ 15,954	\$ 2,197	\$ —	\$ 19	\$ 688	\$ —	\$ 580	\$ 30,037
Collectively	60,020	67,810	11,450	1,872	1,723	5,096	67	347	148,385
PCI**	157	—	—	—	—	—	—	—	157
Balance at June 30, 2015	\$ 70,776	\$ 83,764	\$ 13,647	\$ 1,872	\$ 1,742	\$ 5,784	\$ 67	\$ 927	\$ 178,579
Individually	\$ 13,514	\$ 16,858	\$ 1,115	\$ —	\$ 805	\$ 900	\$ —	\$ 574	\$ 33,766
Collectively	56,102	65,609	10,815	1,519	1,601	4,781	80	423	140,930
PCI**	157	—	—	—	—	—	—	—	157
Balance at December 31, 2014	\$ 69,773	\$ 82,467	\$ 11,930	\$ 1,519	\$ 2,406	\$ 5,681	\$ 80	\$ 997	\$ 174,853
Recorded investment in loans evaluated for impairment:									
Individually	\$ 248,077	\$ 145,186	\$ 17,426	\$ —	\$ 19	\$ 1,849,897	\$ —	\$ 12,240	\$ 2,272,845
Collectively	10,911,137	7,424,783	2,125,294	365,423	438,671	1,193,643	3,919	170,010	22,632,880
PCI**	3,424	934	—	—	—	139	—	—	4,497
Balance at June 30, 2015	\$ 11,162,638	\$ 7,570,903	\$ 2,142,720	\$ 365,423	\$ 438,690	\$ 3,043,679	\$ 3,919	\$ 182,250	\$ 24,910,222
Individually	\$ 283,362	\$ 147,187	\$ 18,317	\$ —	\$ 1,400	\$ 1,961,185	\$ 151	\$ 7,070	\$ 2,418,672
Collectively	10,550,203	7,569,548	2,062,463	357,083	469,214	1,003,313	4,804	149,213	22,165,841
PCI**	4,047	1,042	—	—	—	156	—	—	5,245
Balance at December 31, 2014	\$ 10,837,612	\$ 7,717,777	\$ 2,080,780	\$ 357,083	\$ 470,614	\$ 2,964,654	\$ 4,955	\$ 156,283	\$ 24,589,758

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

**Purchased credit impaired loans.

***Includes mission related loans, international loans, and loans to OFIs.

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

(dollars in thousands)		Three months ended June 30, 2015				
Outstanding	Recorded Investment	Interest Concessions	Principal Concessions	Other Concessions	Total	Charge-offs
Pre-modification						
Real estate mortgage		\$ 318	\$ 4,686	\$ —	\$ 5,004	
Production and intermediate-term		268	10,737	106	11,111	
Total		\$ 586	\$ 15,423	\$ 106	\$ 16,115	
Post-modification						
Real estate mortgage		\$ 318	\$ 5,316	\$ —	\$ 5,634	\$ —
Production and intermediate-term		268	10,759	106	11,133	(53)
Total		\$ 586	\$ 16,075	\$ 106	\$ 16,767	\$ (53)

(dollars in thousands)

Outstanding Recorded Investment	Six months ended June 30, 2015				
	Interest Concessions	Principal Concessions	Other Concessions	Total	Charge-offs
Pre-modification					
Real estate mortgage	\$ 702	\$ 9,881	\$ –	\$ 10,583	
Production and intermediate-term	1,668	20,790	106	22,564	
Rural residential real estate	–	390	–	390	
Other (including Mission Related)	–	–	1,000	1,000	
Total	\$ 2,370	\$ 31,061	\$ 1,106	\$ 34,537	
Post-modification					
Real estate mortgage	\$ 705	\$ 9,621	\$ –	\$ 10,326	\$ (43)
Production and intermediate-term	1,667	20,962	106	22,735	(54)
Rural residential real estate	–	390	–	390	–
Other (including Mission Related)	–	–	1,000	1,000	–
Total	\$ 2,372	\$ 30,973	\$ 1,106	\$ 34,451	\$ (97)

(dollars in thousands)

Outstanding Recorded Investment	Three months ended June 30, 2014				
	Interest Concessions	Principal Concessions	Other Concessions	Total	Charge-offs
Pre-modification					
Real estate mortgage	\$ 484	\$ 7,622	\$ –	\$ 8,106	
Production and intermediate-term	–	10,909	–	10,909	
Rural residential real estate	71	14	93	178	
Total	\$ 555	\$ 18,545	\$ 93	\$ 19,193	
Post-modification					
Real estate mortgage	\$ 441	\$ 7,874	\$ –	\$ 8,315	\$ (10)
Production and intermediate-term	–	11,057	–	11,057	(1)
Rural residential real estate	72	13	93	178	(4)
Total	\$ 513	\$ 18,944	\$ 93	\$ 19,550	\$ (15)

(dollars in thousands)

Outstanding Recorded Investment	Six months ended June 30, 2014				
	Interest Concessions	Principal Concessions	Other Concessions	Total	Charge-offs
Pre-modification					
Real estate mortgage	\$ 1,815	\$ 10,833	\$ –	\$ 12,648	
Production and intermediate-term	885	21,067	–	21,952	
Rural residential real estate	326	131	93	550	
Total	\$ 3,026	\$ 32,031	\$ 93	\$ 35,150	
Post-modification					
Real estate mortgage	\$ 2,447	\$ 10,636	\$ –	\$ 13,083	\$ (10)
Production and intermediate-term	885	20,182	–	21,067	(1)
Rural residential real estate	325	114	93	532	(4)
Total	\$ 3,657	\$ 30,932	\$ 93	\$ 34,682	\$ (15)

Interest concessions may include interest forgiveness and interest deferment. Principal concessions may include principal forgiveness, principal deferment, and maturity extension.

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

	Three months ended June 30,		Six months ended June 30,	
	2015	2014	2015	2014
Real estate mortgage	\$ 3,053	\$ 5,926	\$ 3,649	\$ 5,965
Production and intermediate-term	1,922	2,082	3,208	2,907
Rural residential real estate	35	66	70	66
Total	\$ 5,010	\$ 8,074	\$ 6,927	\$ 8,938

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

	Total TDRs		Nonaccrual TDRs	
	June 30, 2015	December 31, 2014	June 30, 2015	December 31, 2014
<i>(dollars in thousands)</i>				
Real estate mortgage	\$ 106,906	\$ 133,794	\$ 53,934	\$ 74,104
Production and intermediate-term	104,309	104,300	52,503	45,764
Processing and marketing	—	—	—	—
Farm-related business	13,832	3,808	13,099	3,047
Rural residential real estate	5,213	5,466	2,743	2,466
Other (including Mission Related)	10,809	9,532	1,474	—
Total Loans	\$ 241,069	\$ 256,900	\$ 123,753	\$ 125,381
Additional commitments to lend	\$ 7,495	\$ 7,338		

The following table presents foreclosure information as of period end:

<i>(dollars in thousands)</i>	June 30, 2015
Carrying amount of foreclosed residential real estate properties held as a result of obtaining physical possession	\$ 2,287
Recorded investment of consumer mortgage loans secured by residential real estate for which formal foreclosure proceedings are in process	\$ 1,260

PCI Loans

For further discussion of the District's accounting for PCI loans, see Note 2, *Summary of Significant Accounting Policies*, of the District's most recent Annual Report.

In connection with past mergers, certain Associations purchased impaired loans that are not accounted for as debt securities. The carrying amounts of those loans included in the balance sheet amounts of loans receivable at June 30, 2015, were as follows.

<i>(dollars in thousands)</i>	
Real estate mortgage	\$ 3,424
Production and intermediate-term	934
Rural residential real estate	139
Total Loans	\$ 4,497

At both June 30, 2015 and December 31, 2014, the allowance for loan losses related to these loans was \$157 thousand. During the three and six months ended June 30, 2015, provision for loan losses on these loans was an expense reversal of \$56 thousand and an expense reversal of \$96 thousand, respectively, compared with an expense reversal of \$664 thousand and an expense reversal of \$826 thousand for the three and six month periods ended June 30, 2014. See above for a summary of changes in the total allowance for loan losses for the period ended June 30, 2015. There were no loans acquired for 2015 or 2014 for which it was probable at acquisition that all contractually required payments would not be collected.

Certain loans that are within the scope of purchased impaired loan guidance are accounted for using a cash basis method of income recognition because the acquiring Associations could not reasonably estimate cash flows expected to be collected. Substantially all of the loans acquired were real estate collateral dependent loans. At the time of purchase, the real estate markets were very unpredictable, making estimation of the amount and timing of a sale of loan collateral in essentially the same condition as received upon foreclosure indeterminate. As such, the acquiring Associations did not have the information necessary to reasonably estimate cash flows expected to be collected to compute their yield. Management determined a nonaccrual classification would be the most appropriate and that no income would be recognized on these loans as is allowed under accounting guidance.

Note 3 — Investments

Investment Securities

District investments consist primarily of mortgage-backed securities (MBSs) collateralized by U.S. government or U.S. agency guaranteed residential and commercial mortgages. They are held to maintain a liquidity reserve, manage short-term surplus funds, and manage interest rate risk. These securities meet the applicable FCA regulatory guidelines related to government agency guaranteed investments.

Included in the available-for-sale investments are non-agency collateralized mortgage obligations (CMOs) and asset-backed securities (ABSs). These securities must meet the applicable FCA regulatory guidelines, which require them to be high quality, senior class, and rated in the top category (AAA/Aaa) by Nationally Recognized Statistical Rating Organizations (NRSROs) at the time of purchase. To achieve these ratings, the securities may have a guarantee of timely payment of principal and interest, credit enhancements achieved through over-collateralization or other means, priority of payments for senior classes over junior classes, or bond insurance. All of the non-agency securities owned have one or more credit enhancement features.

The FCA considers a non-agency security ineligible if it falls below AAA/Aaa credit rating criteria and requires Farm Credit System (System) institutions to provide notification to the FCA when a security becomes ineligible. Non-agency CMO and ABS securities not rated in the top category by at least one of the NRSROs at June 30, 2015 had a fair value of \$139.7 million and \$33.5 million, respectively.

Held-to-maturity investments consist of Mission Related Investments acquired primarily under the Rural Housing Mortgage-Backed Securities (RHMS) and Rural America Bond (RAB) pilot programs. RHMS must be fully guaranteed by a government agency or government sponsored enterprise. RABs are private placement securities which generally have some form of credit enhancement.

Held-to-maturity securities also include ABSs issued through the Small Business Administration and guaranteed by the full faith and credit of the United States government. They are held for managing short-term surplus funds and reducing interest rate risk. These securities meet the applicable FCA regulatory guidelines related to government agency guaranteed investments.

In its Conditions of Approval for the program, the FCA considers an RAB ineligible if its investment rating, based on the internal 14-point risk rating scale used to also grade loans, falls below 9. The FCA requires System institutions to provide notification when a security becomes ineligible. At June 30, 2015, the District held four RABs whose credit quality had deteriorated beyond the program limits.

Effective December 31, 2014, the FCA ended the pilot programs approved after 2004 as part of the Investment in Rural America initiative. Each institution participating in such programs may continue to hold its investment through the maturity dates for the investments, provided the institution continues to meet all approval conditions. The FCA can consider future participation in these programs on a case-by-case basis.

During the first six months of 2015, proceeds from sales of investments were \$29.1 million and realized gains were \$1.1 million. During the first six months of 2014, proceeds from sales of investments were \$7.6 million and realized gains were \$149 thousand.

Available-for-sale

A summary of the amortized cost and fair value of debt securities held as available-for-sale investments follows:

	June 30, 2015				
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value	Yield
<i>(dollars in thousands)</i>					
U.S. Govt. Guaranteed	\$ 3,648,235	\$ 73,971	\$ (3,837)	\$ 3,718,369	1.68%
U.S. Govt. Agency Guaranteed	2,246,443	21,239	(7,036)	2,260,646	0.84
Non-Agency CMOs (a)	157,167	17	(16,385)	140,799	0.67
ABSs	564,125	26,746	(733)	590,138	1.25
Total	<u>\$ 6,615,970</u>	<u>\$ 121,973</u>	<u>\$ (27,991)</u>	<u>\$ 6,709,952</u>	<u>1.34%</u>

December 31, 2014					
<i>(dollars in thousands)</i>	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value	Yield
U.S. Govt. Guaranteed	\$ 3,774,428	\$ 91,316	\$ (6,538)	\$ 3,859,206	1.85%
U.S. Govt. Agency Guaranteed	2,400,460	21,608	(6,537)	2,415,531	0.84
Non-Agency CMOs (b)	171,290	23	(18,302)	153,011	0.64
ABSs	300,594	26,523	(446)	326,671	0.87
Total	<u>\$ 6,646,772</u>	<u>\$ 139,470</u>	<u>\$ (31,823)</u>	<u>\$ 6,754,419</u>	<u>1.41%</u>

- (a) Gross unrealized losses included non-credit related other-than-temporary impairment included in Accumulated Other Comprehensive Income (AOCI) of \$11.6 million for Non-Agency CMOs.
- (b) Gross unrealized losses included non-credit related other-than temporary impairment included in AOCI of \$13.1 million for Non-Agency CMOs.

Held-to-maturity

A summary of the amortized cost and fair value of debt securities held as held-to-maturity investments follows:

June 30, 2015					
<i>(dollars in thousands)</i>	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value	Yield
U.S. Govt. Agency Guaranteed	\$ 499,400	\$ 18,050	\$ (6,596)	\$ 510,854	3.42%
ABSs	36,622	709	(109)	37,222	1.70
RABs and Other (a)	207,152	10,067	(2,635)	214,584	5.80
Total	<u>\$ 743,174</u>	<u>\$ 28,826</u>	<u>\$ (9,340)</u>	<u>\$ 762,660</u>	<u>4.00%</u>

December 31, 2014					
<i>(dollars in thousands)</i>	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value	Yield
U.S. Govt. Agency Guaranteed	\$ 535,299	\$ 22,151	\$ (4,164)	\$ 553,286	3.63%
ABSs	41,897	802	(107)	42,592	1.83
RABs and Other (b)	211,743	12,557	(1,131)	223,169	5.69
Total	<u>\$ 788,939</u>	<u>\$ 35,510</u>	<u>\$ (5,402)</u>	<u>\$ 819,047</u>	<u>4.09%</u>

- (a) Gross unrealized losses included non-credit related other-than-temporary impairment included in AOCI of \$104 thousand for RABs and Other.
- (b) Gross unrealized losses included non-credit related other-than-temporary impairment included in AOCI of \$107 thousand for RABs and Other.

A summary of the contractual maturity, estimated fair value and amortized cost of investment securities at June 30, 2015 follows:

Available-for-sale

<i>(dollars in thousands)</i>	Due in 1 year or less		Due after 1 year through 5 years		Due after 5 years through 10 years		Due after 10 years		Total	
	Amount	Weighted Average Yield	Amount	Weighted Average Yield	Amount	Weighted Average Yield	Amount	Weighted Average Yield	Amount	Weighted Average Yield
U.S. Govt. Guaranteed	\$ —	— %	\$ 15	0.39 %	\$ 73,793	0.53 %	\$ 3,644,561	1.71 %	\$ 3,718,369	1.68 %
U.S. Govt. Agency Guaranteed	18,942	0.71	205,935	1.11	147,769	0.85	1,888,000	0.81	2,260,646	0.84
Non-Agency CMOs	—	—	—	—	1,062	0.89	139,737	0.67	140,799	0.67
ABSs	—	—	536,493	0.70	20,103	1.48	33,542	39.99	590,138	1.25
Total fair value	<u>\$ 18,942</u>	<u>0.71 %</u>	<u>\$ 742,443</u>	<u>0.82 %</u>	<u>\$ 242,727</u>	<u>0.81 %</u>	<u>\$ 5,705,840</u>	<u>1.43 %</u>	<u>\$ 6,709,952</u>	<u>1.34 %</u>
Total amortized cost	<u>\$ 18,937</u>		<u>\$ 741,455</u>		<u>\$ 241,777</u>		<u>\$ 5,613,801</u>		<u>\$ 6,615,970</u>	

Held-to-maturity

<i>(dollars in thousands)</i>	Due in 1 year or less		Due after 1 year through 5 years		Due after 5 years through 10 years		Due after 10 years		Total	
	Amount	Weighted Average Yield	Amount	Weighted Average Yield	Amount	Weighted Average Yield	Amount	Weighted Average Yield	Amount	Weighted Average Yield
U.S. Govt. Agency Guaranteed	\$ —	— %	\$ 182	4.47 %	\$ —	— %	\$ 499,218	3.42 %	\$ 499,400	3.42 %
ABSs	127	2.10	29,069	1.51	5,177	2.01	2,249	3.46	36,622	1.70
RABs and Other	335	3.75	19,628	5.74	48,011	6.02	139,178	5.74	207,152	5.80
Total amortized cost	<u>\$ 462</u>	<u>3.30 %</u>	<u>\$ 48,879</u>	<u>3.22 %</u>	<u>\$ 53,188</u>	<u>5.63 %</u>	<u>\$ 640,645</u>	<u>3.92 %</u>	<u>\$ 743,174</u>	<u>4.00 %</u>
Total fair value	<u>\$ 461</u>		<u>\$ 50,433</u>		<u>\$ 56,912</u>		<u>\$ 654,854</u>		<u>\$ 762,660</u>	

A substantial portion of these investments has contractual maturities in excess of ten years. However, expected maturities for these types of securities will differ from contractual maturities because borrowers may have the right to prepay obligations with or without prepayment penalties.

An investment is considered impaired if its fair value is less than its amortized cost. This also applies to those securities other-than-temporarily impaired for which a credit loss has been recognized but noncredit-related losses continue to remain unrealized. The following tables show the fair value and gross unrealized losses for all investments that have been in a continuous unrealized loss position aggregated by investment category at each reporting period. A continuous unrealized loss position for an investment is measured from the date the impairment was first identified.

	June 30, 2015					
	Less than 12 Months		12 Months or Greater		Total	
	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
<i>(dollars in thousands)</i>						
U.S. Govt. Guaranteed	\$ 620,838	\$ (1,197)	\$ 425,413	\$ (2,640)	\$ 1,046,251	\$ (3,837)
U.S. Govt. Agency Guaranteed	523,500	(4,623)	633,748	(9,009)	1,157,248	(13,632)
Non-Agency CMOs	9,027	(713)	131,603	(15,672)	140,630	(16,385)
ABSs	258,823	(339)	7,342	(503)	266,165	(842)
RABs and Other	62,431	(1,978)	13,312	(657)	75,743	(2,635)
Total	\$ 1,474,619	\$ (8,850)	\$ 1,211,418	\$ (28,481)	\$ 2,686,037	\$ (37,331)

	December 31, 2014					
	Less than 12 Months		12 Months or Greater		Total	
	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
<i>(dollars in thousands)</i>						
U.S. Govt. Guaranteed	\$ 679,802	\$ (2,094)	\$ 504,943	\$ (4,444)	\$ 1,184,745	\$ (6,538)
U.S. Govt. Agency Guaranteed	504,898	(1,306)	816,972	(9,395)	1,321,870	(10,701)
Non-Agency CMOs	14,324	(647)	137,670	(17,655)	151,994	(18,302)
ABSs	185,727	(206)	7,168	(347)	192,895	(553)
RABs and Other	17,173	(147)	33,068	(984)	50,241	(1,131)
Total	\$ 1,401,924	\$ (4,400)	\$ 1,499,821	\$ (32,825)	\$ 2,901,745	\$ (37,225)

The recording of an impairment is predicated on: (1) whether or not management intends to sell the security, (2) whether it is more likely than not that management would be required to sell the security before recovering its costs, and (3) whether management expects to recover the security's entire amortized cost basis (even if there is no intention to sell). If the District intends to sell the security or it is more likely than not that it would be required to sell the security, the impairment loss recognized equals the full difference between amortized cost and fair value of the security. When the District does not intend to sell securities in an unrealized loss position and it is not more likely than not that it would be required to sell the securities, other-than-temporary impairment loss is separated into credit loss and noncredit loss. Credit loss is defined as the shortfall of the present value of the cash flows expected to be collected in relation to the amortized cost basis.

The District performs periodic credit reviews, including other-than-temporary impairment (OTTI) analyses, on its investment securities portfolio. The objective is to quantify future possible loss of principal or interest due on securities in the portfolio. Factors considered in determining whether an impairment is other-than-temporary include among others: (1) the length of time and the extent to which the fair value is less than cost, (2) adverse conditions specifically related to the industry, (3) geographic area and the condition of the underlying collateral, (4) payment structure of the security, (5) ratings by rating agencies, (6) the creditworthiness of bond insurers, and (7) volatility of the fair value changes.

The District uses the present value of cash flows expected to be collected from each debt security to determine the amount of credit loss. This technique requires assumptions related to the underlying collateral, including default rates, amount and timing of prepayments, and loss severity. Assumptions can vary widely from security to security and are influenced by such factors as loan interest rate, geographical location of the borrower, borrower characteristics, and collateral type.

Significant inputs used to estimate the amount of credit loss include, but are not limited to, performance indicators of the underlying assets in the security (including default rates, delinquency rates, and percentage of nonperforming assets), loan-to-collateral value ratios, third-party guarantees, current levels of subordination, vintage, geographic concentration,

and credit ratings. The District obtains assumptions for the default rate, prepayment rate, and loss severity rate from an independent third party.

Following are the assumptions used for the periods ended:

Assumptions Used	MBSs	ABSs
June 30, 2015		
Default rate by range	0.20% to 31.21%	7.86% to 44.13%
Prepayment rate by range	6.90% to 17.15%	4.37% to 11.22%
Loss severity by range	12.10% to 66.21%	68.54% to 100.54%
December 31, 2014		
Default rate by range	0.83% to 31.49%	6.72% to 52.16%
Prepayment rate by range	6.17% to 16.72%	5.36% to 12.04%
Loss severity by range	4.37% to 68.03%	64.72% to 100.00%

Based on the results of all analyses, the District has recognized \$213 thousand of credit-related OTTI for 2015, which is included in Net Other-than-temporary Impairment Losses in the Combined Statements of Income. Since the District does not intend to sell these other-than-temporarily impaired debt securities and is not more likely than not to be required to sell before recovery, the total OTTI is reflected in the Statements of Income with: (1) a net other-than-temporary impairment amount related to estimated credit loss, and (2) an amount relating to all other factors, recognized as a reclassification to or from Other Comprehensive Income (OCI).

For the six months ended June 30, 2015, net unrealized losses of \$15.2 million were recognized in OCI on available-for-sale investments that are not other-than-temporarily impaired.

The following schedule details the activity related to cumulative credit losses on investments recognized in earnings for which a portion of an other-than-temporary impairment was recognized in other comprehensive income:

<i>(dollars in thousands)</i>	For the three months ended June 30,		For the six months ended June 30,	
	2015	2014	2015	2014
Amount related to credit loss-beginning balance	\$ 60,187	\$ 61,354	\$ 60,217	\$ 60,071
Additions for initial credit impairments	—	—	—	—
Additions for subsequent credit impairments	106	101	213	1,452
Reductions for increases in expected cash flows	(696)	(242)	(833)	(419)
Reductions for securities sold/settled/matured	—	—	—	109
Amount related to credit loss-ending balance	59,597	61,213	59,597	61,213
Life to date incurred credit losses	(20,111)	(20,626)	(20,111)	(20,626)
Remaining unrealized credit losses	\$ 39,486	\$ 40,587	\$ 39,486	\$ 40,587

For all other impaired investments, the District has not recognized any credit losses as the impairments are deemed temporary and result from non-credit related factors. The District has the ability and intent to hold these investments until a recovery of unrealized losses occurs, which may be at maturity, and at this time expects to collect the full principal amount and interest due on these securities. Substantially all of these investments were in U.S. government agency securities and the District expects these securities would not be settled at a price less than their amortized cost.

Note 4 — Debt

Bonds and Notes

AgFirst, unlike commercial banks and other depository institutions, obtains funds for its lending operations primarily from the sale of Systemwide Debt Securities issued jointly by the System banks through the Funding Corporation. Certain conditions must be met before AgFirst can participate in the issuance of Systemwide Debt Securities. As one condition of participation, AgFirst is required by the Farm Credit Act and FCA regulations to maintain specified eligible assets at least equal in value to the total amount of debt obligations outstanding for which it is primarily liable. This requirement does not provide holders of Systemwide Debt Securities with a security interest in any assets of the banks.

In accordance with FCA regulations, each issuance of Systemwide Debt Securities ranks equally with other unsecured Systemwide Debt Securities. Systemwide Debt Securities are not issued under an indenture and no trustee is provided

with respect to these securities. Systemwide Debt Securities are not subject to acceleration prior to maturity upon the occurrence of any default or similar event.

The System may issue the following types of Systemwide Debt Securities:

- Federal Farm Credit Banks Consolidated Systemwide Bonds,
- Federal Farm Credit Banks Consolidated Systemwide Discount Notes,
- Federal Farm Credit Banks Consolidated Systemwide Master Notes,
- Federal Farm Credit Banks Global Debt Securities, and
- Federal Farm Credit Banks Consolidated Systemwide Medium-Term Notes.

Additional information regarding Systemwide Debt Securities can be found in their respective offering circulars.

The following table provides a summary of AgFirst's participation in outstanding Systemwide Debt Securities by maturity. Weighted average interest rates include the effect of related derivative financial instruments. The table does not include \$433.1 million of intra-system obligations.

<i>(dollars in thousands)</i>	June 30, 2015					
	Bonds		Discount Notes		Total	
	Amortized Cost	Weighted Average Interest Rate	Amortized Cost	Weighted Average Interest Rate	Amortized Cost	Weighted Average Interest Rate
Maturities						
One year or less	\$ 5,294,147	0.39%	\$ 4,437,171	0.17%	\$ 9,731,318	0.29%
Greater than one year to two years	4,967,566	0.68	—	—	4,967,566	0.68
Greater than two years to three years	4,087,034	0.79	—	—	4,087,034	0.79
Greater than three years to four years	1,894,352	1.34	—	—	1,894,352	1.34
Greater than four years to five years	1,556,450	1.77	—	—	1,556,450	1.77
Greater than five years	4,050,959	2.49	—	—	4,050,959	2.49
Total	\$ 21,850,508	1.10%	\$ 4,437,171	0.17%	\$ 26,287,679	0.94%

Discount notes are issued with maturities ranging from 1 to 365 days. The average maturity of discount notes at June 30, 2015 was 104 days.

Note 5 — Shareholders' Equity

Perpetual Preferred Stock

Payment of dividends or redemption price on issued Preferred Stock may be restricted if the Bank fails to satisfy applicable minimum capital adequacy, surplus, and collateral requirements.

Accumulated Other Comprehensive Income

The following presents activity related to AOCI for the periods presented below:

<i>(dollars in thousands)</i>	Changes in Accumulated Other Comprehensive Income by Component (a)			
	For the three months ended June 30,		For the six months ended June 30,	
	2015	2014	2015	2014
Investment Securities:				
Balance at beginning of period	\$ 106,331	\$ 106,324	\$ 108,886	\$ 99,865
Other comprehensive income before reclassifications	(11,231)	4,070	(12,752)	9,327
Amounts reclassified from AOCI	91	101	(943)	1,303
Net current period other comprehensive income	(11,140)	4,171	(13,695)	10,630
Balance at end of period	\$ 95,191	\$ 110,495	\$ 95,191	\$ 110,495
Cash Flow Hedges:				
Balance at beginning of period	\$ (701)	\$ 26	\$ (548)	\$ 289
Other comprehensive income before reclassifications	(29)	92	105	92
Amounts reclassified from AOCI	(86)	(283)	(373)	(546)
Net current period other comprehensive income	(115)	(191)	(268)	(454)
Balance at end of period	\$ (816)	\$ (165)	\$ (816)	\$ (165)
Employee Benefit Plans:				
Balance at beginning of period	\$ (396,430)	\$ (270,347)	\$ (405,649)	\$ (275,443)
Other comprehensive income before reclassifications	—	—	—	—
Amounts reclassified from AOCI	9,218	5,097	18,437	10,193
Net current period other comprehensive income	9,218	5,097	18,437	10,193
Balance at end of period	\$ (387,212)	\$ (265,250)	\$ (387,212)	\$ (265,250)
Total Accumulated Other Comprehensive Income:				
Balance at beginning of period	\$ (290,800)	\$ (163,997)	\$ (297,311)	\$ (175,289)
Other comprehensive income before reclassifications	(11,260)	4,162	(12,647)	9,419
Amounts reclassified from AOCI	9,223	4,915	17,121	10,950
Net current period other comprehensive income	(2,037)	9,077	4,474	20,369
Balance at end of period	\$ (292,837)	\$ (154,920)	\$ (292,837)	\$ (154,920)

Reclassifications Out of Accumulated Other Comprehensive Income (b)

<i>(dollars in thousands)</i>	For the three months ended June 30,				For the six months ended June 30,				Income Statement Line Item
	2015		2014		2015		2014		
Investment Securities:									
Sales gains & losses	\$	—	\$	—	\$	1,126	\$	149	Gains (losses) on investments, net
Holding gains & losses		(106)		(101)		(213)		(1,452)	Net other-than-temporary impairment
Amortization		15		—		30		—	Interest income on investments
Net amounts reclassified		(91)		(101)		943		(1,303)	
Cash Flow Hedges:									
Interest income		115		191		268		454	See Note 10.
Gains (losses) on other transactions		(29)		92		105		92	See Note 10.
Net amounts reclassified		86		283		373		546	
Employee Benefit Plans:									
Periodic pension costs		(9,218)		(5,097)		(18,437)		(10,193)	See Note 7.
Net amounts reclassified		(9,218)		(5,097)		(18,437)		(10,193)	
Total reclassifications for period	\$	(9,223)	\$	(4,915)	\$	(17,121)	\$	(10,950)	

(a) Amounts in parentheses indicate debits to AOCI.

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

Note 6 — Fair Value Measurement

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

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

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 1 assets and liabilities could include investment securities and derivative contracts that are traded in an active exchange market, in addition to certain U.S. Treasury securities that are highly-liquid and are actively traded in over-the-counter 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 2 assets and liabilities could include investment securities that are traded in active, non-exchange markets and derivative contracts that are traded in active, over-the-counter markets.

Level 3 inputs are unobservable and supported by little or no market activity. Level 3 assets and liabilities could include investments and derivative contracts whose value is determined using pricing models, discounted cash flow methodologies, or similar techniques, and other instruments for which the determination of fair value requires significant management judgment or estimation. Level 3 assets and liabilities could also include investments and derivative contracts 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 most recent Annual Report to Shareholders.

In 2009, the Bank began adjusting the pricing it received for the Non-Agency ABS and CMO securities from the third party pricing service with that obtained from an investment analysis consultant due to the inherent illiquidity and dislocation in the market for these bonds. At that time, these securities were also reclassified and reported as Level 3 fair value measurements because of this market unobservable pricing input. In 2012, this valuation input was discontinued because of a reduction in volatilities and risk, as measured by the pricing differences and changes over time, for these bonds.

Price discovery for these two portfolio segments has not presented a problem for a number of years and has been quite transparent. Valuations have been corroborated by various information providers, brokers, and dealers. Documentation from the third party pricing service indicates market observable inputs are used in their valuations of these securities. On June 30, 2015, the Non-Agency ABS and CMO bonds were transferred to Level 2 of the fair value hierarchy.

The District had no other transfers of assets or liabilities measured on a recurring basis into or out of Level 1 or Level 2 during the reporting period. For Level 3 assets and liabilities measured at fair value on a recurring basis, the tables below present a reconciliation from the opening balances to the closing balances, and any transfers into or out of Level 3.

<i>(dollars in thousands)</i>	ABSs	Non-Agency CMOs	RABs and Other
Balance at December 31, 2014	\$ 34,783	\$ 153,011	\$ -
Gains or (losses) included in earnings	-	(213)	-
Gains or (losses) included in OCI	(153)	1,910	-
Purchases	-	-	-
Sales	-	-	-
Settlements	(1,088)	(13,909)	-
Transfers in and/or out of Level 3	(33,542)	(140,799)	-
Balance at June 30, 2015	\$ -	\$ -	\$ -

<i>(dollars in thousands)</i>	ABS	Non-Agency CMOs	RABs and Other
Balance at December 31, 2013	\$ 38,798	\$ 173,486	\$ 41,286
Gains or (losses) included in earnings	—	(1,321)	96
Gains or (losses) included in OCI	3,168	7,839	1,818
Purchases	—	—	—
Sales	—	—	(4,886)
Issuances	—	—	—
Settlements	(1,969)	(12,590)	(5,018)
Transfers in and/or out of Level 3	—	—	—
Balance at June 30, 2014	<u>\$ 39,997</u>	<u>\$ 167,414</u>	<u>\$ 33,296</u>

Fair values are estimated at each period end date for assets and liabilities measured at fair value on a recurring basis. Fair values are estimated at least annually, or when information suggests a significant change in value, for assets measured at fair value on a nonrecurring basis. Other Financial Instruments are not measured at fair value in the statement of financial position, but their fair values are estimated as of each period end date. The following tables summarize the carrying amounts of these assets and liabilities at period end, and their related fair values.

<i>(dollars in thousands)</i>	At or for the Six Months Ended June 30, 2015					Fair Value	Fair Value Effects On Earnings
	Total Carrying Amount	Level 1	Level 2	Level 3	Total Fair Value		
<u>Recurring Measurements</u>							
Assets:							
Investments available-for-sale:							
U.S. Govt. Guaranteed	\$ 3,718,369	\$ —	\$ 3,718,369	\$ —	\$ 3,718,369		
U.S. Govt. Agency Guaranteed	2,260,646	—	2,260,646	—	2,260,646		
Non-Agency CMOs	140,799	—	140,799	—	140,799		
ABSs	590,138	—	590,138	—	590,138		
Total investments available-for-sale	<u>6,709,952</u>	<u>—</u>	<u>6,709,952</u>	<u>—</u>	<u>6,709,952</u>		
Federal funds sold, securities purchased under resale agreements, and other	225,408	—	225,408	—	225,408		
Interest rate swaps and other derivative instruments	11,029	—	11,029	—	11,029		
Assets held in trust funds	22,533	22,533	—	—	22,533		
Recurring Assets	<u>\$ 6,968,922</u>	<u>\$ 22,533</u>	<u>\$ 6,946,389</u>	<u>\$ —</u>	<u>\$ 6,968,922</u>		
Liabilities:							
Interest rate swaps and other derivative instruments	\$ —	\$ —	\$ —	\$ —	\$ —		
Collateral liabilities	—	—	—	—	—		
Recurring Liabilities	<u>\$ —</u>	<u>\$ —</u>	<u>\$ —</u>	<u>\$ —</u>	<u>\$ —</u>		
<u>Nonrecurring Measurements</u>							
Assets:							
Impaired loans	\$ 356,076	\$ —	\$ —	\$ 356,076	\$ 356,076	\$	2,351
Other property owned	40,520	—	—	44,765	44,765		109
Other Investments	80	—	—	80	80		—
Nonrecurring Assets	<u>\$ 396,676</u>	<u>\$ —</u>	<u>\$ —</u>	<u>\$ 400,921</u>	<u>\$ 400,921</u>	<u>\$</u>	<u>2,460</u>
<u>Other Financial Instruments</u>							
Assets:							
Cash	\$ 158,681	\$ 158,681	\$ —	\$ —	\$ 158,681		
Investments held to maturity	743,174	—	548,076	214,584	762,660		
Loans	24,201,898	—	—	24,191,355	24,191,355		
Other investments	—	—	—	—	—		
Other Financial Assets	<u>\$ 25,103,753</u>	<u>\$ 158,681</u>	<u>\$ 548,076</u>	<u>\$ 24,405,939</u>	<u>\$ 25,112,696</u>		
Liabilities:							
Systemwide debt securities	\$ 26,720,744	\$ —	\$ —	\$ 26,718,039	\$ 26,718,039		
Other Financial Liabilities	<u>\$ 26,720,744</u>	<u>\$ —</u>	<u>\$ —</u>	<u>\$ 26,718,039</u>	<u>\$ 26,718,039</u>		

At or for the Year Ended December 31, 2014

<i>(dollars in thousands)</i>	Total Carrying Amount	Level 1	Level 2	Level 3	Total Fair Value	Fair Value Effects On Earnings
Recurring Measurements						
Assets:						
Investments available-for-sale:						
U.S. Govt. Guaranteed	\$ 3,859,206	\$ —	\$ 3,859,206	\$ —	\$ 3,859,206	
U.S. Govt. Agency Guaranteed	2,415,531	—	2,415,531	—	2,415,531	
Non-Agency CMOs	153,011	—	—	153,011	153,011	
ABSs	326,671	—	291,888	34,783	326,671	
Total investments available-for-sale	6,754,419	—	6,566,625	187,794	6,754,419	
Federal funds sold, securities purchased under resale agreements, and other	224,847	—	224,847	—	224,847	
Interest rate swaps and other derivative instruments	16,267	—	16,267	—	16,267	
Assets held in trust funds	20,239	20,239	—	—	20,239	
Recurring Assets	\$ 7,015,772	\$ 20,239	\$ 6,807,739	\$ 187,794	\$ 7,015,772	
Liabilities:						
Interest rate swaps and other derivative instruments	\$ —	\$ —	\$ —	\$ —	\$ —	\$ —
Collateral liabilities	—	—	—	—	—	—
Recurring Liabilities	\$ —	\$ —	\$ —	\$ —	\$ —	\$ —
Nonrecurring Measurements						
Assets:						
Impaired loans	\$ 413,794	\$ —	\$ —	\$ 413,794	\$ 413,794	\$ 13,115
Other property owned	45,986	—	—	50,536	50,536	(1,762)
Other investments	251	—	—	251	251	—
Nonrecurring Assets	\$ 460,031	\$ —	\$ —	\$ 464,581	\$ 464,581	\$ 11,353
Other Financial Instruments						
Assets:						
Cash	\$ 671,342	\$ 671,342	\$ —	\$ —	\$ 671,342	
Investments held to maturity	788,939	—	595,878	223,169	819,047	
Loans	23,834,507	—	—	23,866,235	23,866,235	
Other Financial Assets	\$ 25,294,788	\$ 671,342	\$ 595,878	\$ 24,089,404	\$ 25,356,624	
Liabilities:						
Systemwide debt securities	\$ 27,058,364	\$ —	\$ —	\$ 27,009,191	\$ 27,009,191	
Other Financial Liabilities	\$ 27,058,364	\$ —	\$ —	\$ 27,009,191	\$ 27,009,191	

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.

Investment Securities

The fair values of predominantly all Level 3 investment securities have consistent inputs, valuation techniques and correlation to changes in underlying inputs. The models used to determine fair value for these instruments use certain significant unobservable inputs within a discounted cash flow or market comparable pricing valuation technique. Such inputs generally include discount rate components including risk premiums, prepayment estimates, default estimates and loss severities.

These Level 3 assets would decrease (increase) in value based upon an increase (decrease) in discount rates, defaults, or loss severities. Conversely, the fair value of these assets would generally increase (decrease) in value if the prepayment input were to increase (decrease).

Generally, a change in the assumption used for defaults is accompanied by a directionally similar change in the risk premium component of the discount rate (specifically, the portion related to credit risk) and a directionally opposite change in the assumption used for prepayments. Unobservable inputs for loss severities do not normally increase or decrease based on movements in the other significant unobservable inputs for these Level 3 assets.

Derivative Instruments

Level 3 derivative instruments consist of forward contracts that represent a hedge of an unrecognized firm commitment to purchase agency securities at a future date. The value of the forward is the difference between the fair value of the security at inception of the forward and the measurement date. Significant inputs for these valuations would be discount rate and volatility. These Level 3 derivatives would decrease (increase) in value based upon an increase (decrease) in the discount rate.

Generally, for derivative instruments which are subject to changes in the value of the underlying referenced instrument, change in the assumption used for default rate is accompanied by directionally similar change in the risk premium component of the discount rate (specifically, the portion related to credit risk) and a directionally opposite change in the assumption used for prepayment rates.

Unobservable inputs for discount rate and volatility do not increase or decrease based on movements in other significant unobservable inputs for these Level 3 instruments.

Inputs to Valuation Techniques

Management determines the District's valuation policies and procedures. Internal valuation processes are calibrated annually by an independent consultant. Fair value measurements are analyzed on a periodic basis. Documentation is obtained for third party information, such as pricing, and periodically evaluated alongside internal information and pricing.

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

Quantitative Information about Recurring and Nonrecurring Level 3 Fair Value Measurements

	Fair Value	Valuation Technique(s)	Unobservable Input	Range
Forward contracts – when-issued securities	\$ –	Broker/Consensus pricing	Offered quotes	None outstanding
Impaired loans and other property owned	\$ 400,841	Appraisal	Income and expense	*
			Comparable sales	*
			Replacement cost	*
			Comparability adjustments	*
Other investments – RBIC	\$ 80	Third party evaluation	Income, expense, capital	Not applicable

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

Information about Recurring and Nonrecurring Level 2 Fair Value Measurements

	Valuation Technique(s)	Input
Investments available-for-sale	Discounted cash flow	Constant prepayment rate
		Probability of default
Federal funds sold, securities purchased under resale agreements and other	Quoted prices	Loss severity
		Price for similar security
Interest rate swaps	Carrying value	Par/principal and appropriate interest yield
	Discounted cash flow	Annualized volatility
		Counterparty credit risk
		Own credit risk

Information about Other Financial Instrument Fair Value Measurements

	Valuation Technique(s)	Input
Loans	Discounted cash flow	Prepayment forecasts Probability of default Loss severity
Cash and cash equivalents	Carrying value	Par/principal and appropriate interest yield
RABs and other	Discounted cash flow	Risk adjusted spread Prepayment rates Probability of default Loss severity
Assets held in trust funds	Quoted prices	Price for identical security
Bonds and notes	Discounted cash flow	Benchmark yield curve Derived yield spread Own credit risk
Cash collateral	Carrying value	Par/principal and appropriate interest yield

Note 7 — Employee Benefit Plans

Following are retirement and other postretirement benefit expenses for the District:

<i>(dollars in thousands)</i>	For the three months ended June 30,		For the six months ended June 30,	
	2015	2014	2015	2014
Pension	\$ 11,067	\$ 8,951	\$ 22,134	\$ 17,902
401k	2,694	1,920	5,666	4,023
Other postretirement benefits	4,259	2,615	8,518	5,230
Total	\$ 18,020	\$ 13,486	\$ 36,318	\$ 27,155

Following are retirement and other postretirement benefit contributions for the District. Projections are based upon actuarially determined amounts as of the most recent measurement date of December 31, 2014.

<i>(dollars in thousands)</i>	Actual YTD Through 6/30/15	Projected Contributions for Remainder of 2015	Projected Total Contributions 2015
Pensions	\$ 515	\$ 61,591	\$ 62,106
Other postretirement benefits	3,794	3,816	7,610
Total	\$ 4,309	\$ 65,407	\$ 69,716

Contributions in the above table include allocated estimates of funding for multi-employer plans in which the District participates. These amounts may change when a total funding amount and allocation is determined by the respective Plans' Sponsor Committees. 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, 2015.

Further details regarding employee benefit plans are contained in the most recent Annual Report to Shareholders, including a discussion of benefit plan changes related to the termination of the AgFirst Farm Credit Cash Balance Retirement Plan.

Note 8 — Commitments and Contingencies

Under the Farm Credit Act of 1971, each System bank is primarily liable for its portion of Systemwide bond and discount note obligations. Additionally, the four banks are jointly and severally liable for the bonds and notes of the other System banks under the terms of the Joint and Several Liability Reallocation Agreement. Published in the Federal Register, the agreement prescribes the payment mechanisms to be employed in the event one of the banks is unable to meet its debt obligations.

In the event a bank is unable to timely pay principal or interest on an insured debt obligation for which the bank is primarily liable, the Farm Credit System Insurance Corporation (FCSIC) must expend amounts in the Insurance Fund to

the extent available to ensure the timely payment of principal and interest on the insured debt obligation. The provisions of the Farm Credit Act providing for joint and several liability of the banks on the obligation cannot be invoked until the amounts in the Insurance Fund have been exhausted. However, because of other mandatory and discretionary uses of the Insurance Fund, there is no assurance that there will be sufficient funds to pay the principal or interest on the insured debt obligation.

Once joint and several liability is initiated, the FCA is required to make “calls” to satisfy the liability first on all non-defaulting banks in the proportion that each non-defaulting bank’s available collateral (collateral in excess of collateralized obligations) bears to the aggregate available collateral of all non-defaulting banks. If these calls do not satisfy the liability, then a further call would be made in proportion to each non-defaulting bank’s remaining assets. Upon making a call on non-defaulting banks with respect to a Systemwide Debt Security issued on behalf of a defaulting bank, the FCA is required to appoint FCSIC as the receiver for the defaulting bank. The receiver would be required to expeditiously liquidate assets of the bank.

During the periods presented, AgFirst did not make any payments, and as of the report date does not anticipate making any payments, on behalf of its co-obligors under the Joint and Several Liability Reallocation Agreement.

<i>(dollars in billions)</i>	6/30/15	12/31/14
Total System bonds and notes	\$ 225.273	\$ 225.437
AgFirst bonds and notes	\$ 26.288	\$ 26.847

From time to time, legal actions are pending against the District in which claims for money damages are asserted. On at least a quarterly basis, the District 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 and legal counsel are of the opinion that the ultimate liability, if any, from these actions, would not be material in relation to the financial position of the District. Because it is not probable that the District will incur a loss or the loss is not estimable, no liability has been recorded for any claims that may be pending.

Note 9 — Additional Financial Information

Offsetting of Financial and Derivative Assets

		June 30, 2015					
		Gross Amounts Not Offset in the Balance Sheets					
<i>(dollars in thousands)</i>	Gross Amounts of Recognized Assets	Gross Amounts Offset in the Balance Sheets	Net Amounts of Assets Presented in the Balance Sheets	Financial Instruments	Cash Collateral Received	Net Amount	
Derivatives	\$ 11,029	\$ —	\$ 11,029	\$ —	\$ —	\$ 11,029	
Reverse repurchase and similar arrangements	225,408	—	225,408	(225,408)	—	—	
Total	\$ 236,437	\$ —	\$ 236,437	\$ (225,408)	\$ —	\$ 11,029	

		December 31, 2014					
		Gross Amounts Not Offset in the Balance Sheets					
<i>(dollars in thousands)</i>	Gross Amounts of Recognized Assets	Gross Amounts Offset in the Balance Sheets	Net Amounts of Assets Presented in the Balance Sheets	Financial Instruments	Cash Collateral Received	Net Amount	
Derivatives	\$ 16,267	\$ —	\$ 16,267	\$ —	\$ —	\$ 16,267	
Reverse repurchase and similar arrangements	224,847	—	224,847	(224,847)	—	—	
Total	\$ 241,114	\$ —	\$ 241,114	\$ (224,847)	\$ —	\$ 16,267	

There were no liabilities subject to master netting arrangements or similar agreements during the reporting periods.

A description of the rights of setoff associated with recognized derivative assets and liabilities subject to enforceable master netting arrangements is located in Note 10, *Derivative Financial Instruments and Hedging Activities*.

The reverse repurchase agreements are accounted for as collateralized lending.

Bank Only Financial Data

Condensed financial information of the Bank follows:

Balance Sheets		
<i>(dollars in thousands)</i>	June 30, 2015	December 31, 2014
	<i>(unaudited)</i>	<i>(audited)</i>
Cash, cash equivalents and investment securities	\$ 7,685,420	\$ 8,261,289
Loans		
To District Associations	14,256,815	14,280,193
To others	6,508,329	6,613,426
Total loans	20,765,144	20,893,619
Allowance for loan losses	(16,067)	(15,535)
Net loans	20,749,077	20,878,084
Other assets	332,375	363,849
Total assets	<u>\$ 28,766,872</u>	<u>\$ 29,503,222</u>
Bonds and notes	\$ 26,287,679	\$ 26,847,246
Other liabilities	119,145	448,569
Total liabilities	<u>26,406,824</u>	<u>27,295,815</u>
Perpetual preferred stock	125,250	125,250
Capital stock and participation certificates	302,642	303,180
Additional paid-in-capital	36,580	36,580
Retained earnings	1,807,361	1,640,449
Accumulated other comprehensive income (loss)	88,215	101,948
Total shareholders' equity	<u>2,360,048</u>	<u>2,207,407</u>
Total liabilities and equity	<u>\$ 28,766,872</u>	<u>\$ 29,503,222</u>

Statements of Income		
<i>(dollars in thousands)</i>	For the six months ended June 30,	
	2015	2014
	<i>(unaudited)</i>	
Interest income	\$ 345,379	\$ 342,116
Interest expense	117,760	104,413
Net interest income	227,619	237,703
Provision for (reversal of) loan losses	1,045	(1,867)
Net interest income after provision for loan losses	226,574	239,570
Noninterest expense, net	58,703	56,089
Net income	<u>\$ 167,871</u>	<u>\$ 183,481</u>

Note 10 — Derivative Financial Instruments and Hedging Activities

One of the District's goals is to minimize interest rate sensitivity by managing the repricing characteristics of assets and liabilities so that the net interest margin is not adversely affected by movements in interest rates. The District maintains an overall interest rate risk management strategy that may incorporate the use of derivative instruments to achieve that goal. Currently, the primary derivative type used by the District is interest rate swaps, which convert fixed interest rate debt to a lower floating interest rate than was achievable from issuing floating rate debt with identical repricing characteristics. They may allow the District to lower funding costs, diversify sources of funding, or alter interest rate exposures arising from mismatches between assets and liabilities. Under these arrangements, the District agrees with other parties to exchange, at specified intervals, payment streams calculated on a specified notional principal amount, with at least one stream based on a specified floating rate index.

The District may also purchase interest rate derivatives, such as caps, in order to reduce the impact of rising interest rates on its floating-rate debt, and floors, in order to reduce the impact of falling interest rates on its floating-rate assets. In addition, the District may also fix a price to be paid in the future which qualifies as a derivative forward contract.

As a result of interest rate fluctuations, interest income and interest expense related to hedged variable-rate assets and liabilities, respectively, will increase or decrease. Another result of interest rate fluctuations is that hedged fixed-rate assets and liabilities will appreciate or depreciate in market value. The effects of any earnings variability or unrealized changes in market value are expected to be substantially offset by the District's gains or losses on the derivative instruments that are linked to these hedged assets and liabilities. The District considers its strategic use of derivatives to be a prudent method of managing interest rate sensitivity, as it prevents earnings from being exposed to undue risk posed by changes in interest rates.

The primary types of derivative instruments used and the amount of activity for the periods presented is summarized in the following table:

Notional Amounts (dollars in millions)	For the Six Months Ended June 30,			
	2015		2014	
	Receive- Fixed Swaps	Forward Contracts	Receive- Fixed Swaps	Forward Contracts
Balance at beginning of period	\$ 250	\$ 1	\$ 250	\$ -
Additions	-	3	-	2
Maturities/amortization	-	(4)	-	(2)
Terminations	-	-	-	-
Balance at end of period	\$ 250	\$ -	\$ 250	\$ -

By using derivative instruments, the District exposes itself to credit and market risk. If a counterparty fails to fulfill its performance obligations under a derivative contract, the District's credit risk will equal the fair value gain in the derivative. Generally, when the fair value of a derivative contract is positive, this indicates that the counterparty owes the District, thus creating a repayment risk for the District. When the fair value of the derivative contract is negative, the District owes the counterparty and, therefore, assumes no repayment risk.

To minimize the risk of credit losses, the District transacts with counterparties that have an investment grade credit rating from a major rating agency and also monitors the credit standing of, and levels of exposure to, individual counterparties. The District typically enters into master agreements that contain netting provisions. These provisions allow the District to require the net settlement of covered contracts with the same counterparty in the event of default by the counterparty on one or more contracts. A number of swaps are supported by collateral arrangements with counterparties.

Counterparty exposure related to derivatives at:

(dollars in millions)	June 30, 2015	December 31, 2014
Estimated Gross Credit Risk	\$11.0	\$16.3
Percent of Notional	4.41%	6.51%
Cash Collateral Held (on balance sheet)	\$-	\$-
Securities Collateral Held (off balance sheet)	\$-	\$-
Cash Collateral Posted (off balance sheet)	\$-	\$-
Securities Collateral Posted (on balance sheet)	\$-	\$-

The District's derivative activities, which are performed by the Bank, are monitored by the Asset-Liability Management Committee (ALCO) as part of its oversight of the District's asset/liability and treasury functions. The Bank's ALCO is responsible for approving hedging strategies that are developed within parameters established by the Bank's Board of Directors through the analysis of data derived from financial simulation models and other internal and industry sources. The resulting hedging strategies are then incorporated into the overall interest rate risk-management strategies.

Fair Value Hedges

For derivative instruments designated as fair value hedges, the gains or losses on the derivative, as well as the offsetting loss or gain on the hedged item attributable to the hedged risk, are recognized in current earnings. The District includes the gain or loss on the hedged items in the same line item (interest expense) as the offsetting loss or gain on the related interest rate swaps. The amount of the loss on interest rate swaps recognized in interest expense for the six months ended June 30, 2015 was \$5.2 million, while the amount of the gain on the Systemwide Debt Securities was \$5.2 million. The amount of the loss on interest rate swaps recognized in interest expense for the six months ended June 30, 2014 was \$5.1 million, while the amount of the gain on the Systemwide Debt Securities was \$5.1 million. Gains and losses on each

derivative representing either hedge ineffectiveness or hedge components excluded from the assessment of effectiveness are recognized in current earnings.

Cash Flow Hedges

From time to time, the District may acquire when-issued securities, generally government agency guaranteed bonds. The when-issued transactions are contracts to purchase securities that will not be delivered until 30 or more days in the future. These purchase commitments are considered derivatives (cash flow hedges) in the form of forward contracts. Any differences in market value of the contracted securities, between the purchase and reporting or settlement date, represent the value of the forward contracts. These amounts are included in OCI and Other Liabilities or Other Assets as appropriate, as firm commitments in the District's Balance Sheet for each period end. As of the periods presented, the District had not committed to purchase any when-issued bonds.

For derivative instruments that are designated and qualify as a cash flow hedge, such as the District's forward contracts, the effective portion of the gain or loss on the derivative is reported as a component of other comprehensive income and reclassified into earnings in the same period or periods during which the hedged transaction affects earnings. Gains and losses on the derivative representing either hedge ineffectiveness or hedge components excluded from the assessment of effectiveness are recognized in current earnings.

Fair Values of Derivative Instruments

The following tables represent the fair value of derivative instruments designated as hedging instruments for the periods presented:

<i>(dollars in thousands)</i>	Balance Sheet Classification – Assets	6/30/15 Fair Value	Balance Sheet Classification – Liabilities	6/30/15 Fair Value
Receive-fixed swaps	Other Assets	\$ 11,029	Other Liabilities	\$ –
Forward contracts	Other Assets	–	Other Liabilities	–
Total		\$ 11,029		\$ –

<i>(dollars in thousands)</i>	Balance Sheet Classification – Assets	12/31/14 Fair Value	Balance Sheet Classification – Liabilities	12/31/14 Fair Value
Receive-fixed swaps	Other Assets	\$ 16,267	Other Liabilities	\$ –
Forward contracts	Other Assets	–	Other Liabilities	–
Total		\$ 16,267		\$ –

The following table sets forth the amount of net gain (loss) on derivatives recognized in earnings and, for cash flow hedges, the amount of net gain (loss) recognized in AOCI for the periods presented. See Note 5, *Shareholders' Equity*.

<i>(dollars in thousands)</i>	Location of Gain or (Loss) Recognized in, or Reclassified from AOCI into, Income	Amount of Gain or (Loss) Recognized in, or Reclassified from AOCI into, Income *		Amount of Gain or (Loss) Recognized in Income on Derivative (Ineffective Portion and Amount Excluded from Effectiveness Testing)		Amount of Gain or (Loss) Recognized in OCI on Derivative (Effective Portion)	
		2015	2014	2015	2014	2015	2014
		Fair Value Hedges:					
Receive-fixed swaps	Noninterest income	\$ –	\$ –				
Cash Flow Hedges:							
Firm Commitments	Interest Income	\$ 268	\$ 454	\$ –	\$ –	\$ –	\$ –
Forward Contracts	Gains (Losses) on Other Transactions	105	92	–	–	105	92

* Represents total gain or loss for fair value hedges and effective portion for cash flow hedges.

Note 11 — Regulatory Enforcement Matters

At June 30, 2015, two District Associations, with combined total assets of approximately \$1.039 billion, were operating under written agreements with the FCA. Those agreements require the District Associations to take corrective actions with respect to specific areas of their operations. These enforcement actions are not expected to have a significant impact on the District's financial condition or results of operations.

Note 12 — Subsequent Events

The District evaluated subsequent events and determined that, except as described below, there were none requiring disclosure through August 7, 2015, which was the date the financial statements were issued.

On August 6, 2015, the Bank repurchased, through a privately negotiated transaction, Class B Perpetual Non-Cumulative Fixed-to-Floating Rate Subordinated Preferred Stock with a par value of \$10.3 million. The effect of the repurchase on shareholders' equity will be to reduce preferred stock outstanding by \$10.3 million and increase additional paid-in capital by \$3.4 million.