



FARM CREDIT

2013

**QUARTERLY REPORT**

T H I R D   Q U A R T E R

AGFIRST FARM CREDIT BANK  
AND DISTRICT ASSOCIATIONS

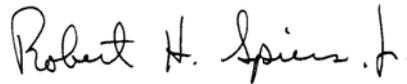
# THIRD QUARTER 2013

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### CERTIFICATION

The undersigned certify that we have reviewed the September 30, 2013 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.



Robert H. Spiers, Jr.  
Chairman of the Board



Leon T. Amerson  
Chief Executive Officer & President



Charl L. Butler  
Chief Financial Officer

November 8, 2013

## 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 September 30, 2013. In making the assessment, management used the framework in *Internal Control — Integrated Framework*, promulgated by the Committee of Sponsoring Organizations of the Treadway Commission, commonly referred to as the "COSO" criteria.

Based on the assessment performed, the Bank and each District Association concluded that as of September 30, 2013, the internal control over financial reporting was effective based upon the COSO (1992) criteria. Additionally, based on this assessment, the Bank and each District Association determined that there were no material weaknesses in the internal control over financial reporting as of September 30, 2013.



Leon T. Amerson  
Chief Executive Officer & President



Charl L. Butler  
Chief Financial Officer

November 8, 2013

# 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 nine month periods ended September 30, 2013. These comments should be read in conjunction with the accompanying financial statements, the Notes to the Combined Financial Statements, and the 2012 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 September 30, 2013, 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. See Note 14, *District Merger Activity*, in the Notes to the Combined Financial Statements for further information.

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 nine 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

Certain sections of this quarterly report contain 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, 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; and
- cyber-security risks, including "denial of service," "hacking," and "identity theft," that could adversely affect the District's business and financial performance, or reputation.

## 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. Diversification of the loan volume by type is illustrated in the following table:

<b>Loan Portfolio</b> <i>(dollars in thousands)</i>	<b>September 30, 2013</b>		<b>December 31, 2012</b>		<b>September 30, 2012</b>	
Real Estate Mortgage	\$ 10,142,047	44%	\$ 9,921,750	43%	\$ 9,807,675	43%
Production and Intermediate-Term	7,408,367	32	7,760,377	34	7,853,067	35
Rural Residential Real Estate	2,792,634	12	2,634,609	12	2,576,887	11
Processing and Marketing	1,115,607	5	1,053,247	5	1,061,451	5
Energy/Water and Waste Disposal	495,454	2	525,070	2	488,383	2
Farm-Related Business	372,910	2	354,039	2	367,113	2
Communication	353,074	2	319,320	1	284,597	1
Loans to Cooperatives	251,225	1	235,703	1	262,427	1
Loans to Other Financing Institutions (OFIs)	85,066	—	60,479	—	8,087	—
Lease Receivables	5,079	—	2,880	—	4,035	—
Other (including Mission Related)	60,281	—	61,731	—	62,145	—
<b>Total</b>	<b>\$ 23,081,744</b>	<b>100%</b>	<b>\$ 22,929,205</b>	<b>100%</b>	<b>\$ 22,775,867</b>	<b>100%</b>

Total loans outstanding were \$23.082 billion at September 30, 2013, an increase of \$152.5 million, or 0.67 percent, compared to total loans outstanding at December 31, 2012. Loan demand remains weak for a number of reasons, including current grower capital and cash levels that are higher than the historical average which has resulted in lower borrowings for capital investment in certain sectors. Also, the slow recovery of the general economy has resulted in lower production in economically dependent sectors. Relatively high unemployment and uncertainty of future employment has had a negative impact on some borrowers dependent on non-farm income. Future loan demand is difficult to predict; however, it is expected to remain weak through 2014.

Until July 31, 2013, substantially all loans in the Bank's first lien residential mortgage portfolio had guarantees from the Federal National Mortgage Association (Fannie Mae) and/or the Federal Agricultural Mortgage Corporation (Farmer Mac), thereby limiting credit risk to AgFirst. The guarantees were in the form of Long-Term Standby Commitments to Purchase, which give AgFirst the right to deliver delinquent loans to the guarantor at par. The Fannie Mae guarantee program ended on July 31, 2013. Subsequent to this date, new loans in this portfolio purchased by the Bank are held without a Fannie Mae guarantee. The Bank has adjusted its methodology of providing allowance for this portfolio to reflect the discontinuation of the Fannie Mae guarantee. The Bank's first lien residential mortgage portfolio, which is primarily included in rural residential real estate loans in the table above, totaled \$2.374 billion at September 30, 2013, of which \$2.275 billion were guaranteed.

### Credit Quality

Credit quality has shown improvement but continues to be impacted by prolonged weakness in the economy as shown below:

<b>Total Loan Portfolio Credit Quality as of:</b>			
<b>Classification</b>	<b>September 30, 2013</b>	<b>December 31, 2012</b>	<b>September 30, 2012</b>
Acceptable	91.92%	90.19%	89.92%
OAEM *	3.62%	4.07%	4.55%
Substandard/Doubtful/Loss	4.46%	5.74%	5.53%

\* Other Assets Especially Mentioned

Most distressed property sales are now occurring at or near appraised values, indicating that real estate values have stabilized in most District markets. Production farm land maintained its value throughout the financial downturn. High commodity prices for grains during 2012 were very beneficial to row crop farmers. However, grain prices have declined in 2013 due to higher than expected inventory and an anticipated good harvest. This has been beneficial to the poultry, cattle, and swine sectors. Improved housing starts in 2013 have positively impacted certain housing-related segments such as forestry and lumber. The nursery/greenhouse segment remains stressed as those industries lag construction starts.

Slow economic growth will have an impact on credit quality for some time. Although credit quality has shown moderate improvement, it will take time to fully resolve some problem assets due to their dependency on general economic conditions including employment, the housing market, and real estate values.

#### *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 September 30, 2013 were \$477.6 million compared to \$580.9 million at December 31, 2012. Nonaccrual loans decreased \$103.4 million during the nine month period ended September 30, 2013, due primarily to repayments of \$147.3 million, transfers to other property owned of \$44.9 million, \$33.2 million of charge-offs net of recoveries on uncollectible balances, and reinstatements to accrual status of \$18.3 million. Offsetting these decreases were \$122.5 million of loan balances transferred to nonaccrual status and advances of \$19.1 million. The ten largest nonaccrual borrower relationships accounted for 22.42 percent of the total nonaccrual balance. At September 30, 2013, total nonaccrual loans were primarily in the forestry (21.21 percent of the total), nursery/greenhouse (14.68 percent), poultry (8.00 percent), cattle (7.70 percent), tree fruits/nuts (6.95 percent), field crops (6.25 percent), dairy (5.83 percent), and other real estate (5.61 percent) segments. Some of these nonaccrual loans are secured by real estate. Although the valuation of the real estate securing these loans has recently stabilized, it continues to reflect the negative impact of the economic environment of the past several years. Nonaccrual loans were 2.07 percent and 2.53 percent of total loans outstanding at September 30, 2013 and December 31, 2012, 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 totaled \$297.3 million at September 30, 2013, compared to \$277.3 million at December 31, 2012. At September 30, 2013, TDRs were comprised of \$114.7 million of accruing restructured loans and \$182.6 million of nonaccruing restructured loans. Restructured loans were primarily in the forestry (23.69 percent of the total), nursery/greenhouse (20.83 percent), poultry (6.53 percent), field crops (6.47 percent), ethanol (6.35 percent), dairy (5.53 percent), other real estate (5.42 percent), and tree fruits/nuts (5.08 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 \$18.6 million since December 31, 2012 and totaled \$91.4 million at September 30, 2013. The decrease was due to disposals of \$52.7 million and net write-downs of OPO of \$15.0 million. Offsetting these decreases were transfers to OPO of \$49.1 million. Disposals primarily included land holdings, with the four largest property disposals, primarily in the forestry segment, totaling \$15.8 million. The largest property write-down of \$8.1 million was for an ethanol facility that also was the largest OPO holding at September 30, 2013. This property had a remaining balance of \$8.3 million at September 30, 2013 (9.12 percent of the total).

#### *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. The allowance for loan losses was \$184.7 million at September 30, 2013, as compared with \$213.5 million at December 31, 2012, which was a decrease of \$28.8 million for the nine month period. Activity within the allowance for the nine months ended September 30, 2013 included loan charge-offs of \$48.2 million, as loan collectability became more measurable and apparent during the nine month period. Offsetting this decrease were \$4.4 million provision for loan losses and recoveries of \$15.0 million. Charge-offs during the nine month period were related primarily to borrowers in the nursery/greenhouse (35.60 percent of the total), ethanol (18.44 percent), and forestry (13.14 percent) segments. The allowance at September 30, 2013 included

specific reserves of \$58.3 million (31.58 percent of the total) and \$126.4 million (68.42 percent) of general reserves. The largest commodity segments included in the allowance at September 30, 2013 were the forestry (19.46 percent of the total), nursery/greenhouse (14.04 percent), and cattle (9.44 percent) segments. See Note 3, *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 details regarding the effects on the allowance from provision for loan losses.

### *Liquidity and Funding Sources*

One of AgFirst's primary responsibilities is to maintain sufficient liquidity to fund the lending operations of the District Associations, in addition to its own needs. Along with normal cash flows associated with lending operations, AgFirst has two primary sources of liquidity: the capacity to issue Systemwide Debt Securities through the Federal Farm Credit Banks Funding Corporation; and its cash and investments portfolio. The Bank also maintains several lines of credit with commercial banks, as well as securities repurchase agreement facilities.

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. However, concerns regarding the government's borrowing limit and budget imbalances have further highlighted the risks to the System relating to the U.S. fiscal situation. These risks include the implied link between the credit rating of the System and the U.S. Government given the System's status as a GSE.

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.

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 F-1, respectively. Standard & Poor's and Moody's outlook for the System is stable. In October 2013, Fitch changed its outlook for the System from stable to negative in connection with Fitch's placement of the U.S. government on negative watch. 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 and Bank's needs.

At September 30, 2013, AgFirst had \$25.982 billion in total debt outstanding compared to \$26.287 billion at December 31, 2012. Total interest-bearing liabilities decreased primarily due to the decrease in liquidity investments, which when combined with an increase in retained earnings, reduced funding requirements.

Cash and cash equivalents, which increased \$37.4 million from December 31, 2012 to a total of \$962.9 million at September 30, 2013, 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 primarily due to changes in liquidity needs in relation to upcoming debt maturities between reporting periods.

Investment securities totaled \$7.365 billion, or 23.06 percent of total assets at September 30, 2013, compared to \$7.649 billion, or 23.83 percent, as of December 31, 2012. Investment securities decreased \$284.3 million (3.72 percent), compared to December 31, 2012. 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 order to maintain the portfolio size within revised regulatory limits, during the quarter ended March 31, 2013, the Bank sold \$114.6 million of agency mortgage backed securities which resulted in a gain of \$7.6 million.

Investment securities classified as being available-for-sale totaled \$6.630 billion at September 30, 2013. Available-for-sale investments at September 30, 2013 included \$4.563 billion in U.S. government guaranteed securities, \$1.806 billion in U.S. government agency guaranteed securities, \$179.6 million in non-agency collateralized mortgage obligations (CMOs), \$45.5 million in mission related investments, and \$37.0 million in asset-backed securities. Since the majority of the portfolio is invested in agency securities, the portfolio is highly liquid and potential credit loss exposure is limited.

As of September 30, 2013, 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. Eligible liquidity investments are classified according to three liquidity quality levels with level 1 being the highest. The first 15 days of liquidity coverage are met using only level 1 instruments, which include cash and cash equivalents. Days 16 through 30 of 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. Additionally, a supplemental liquidity buffer in excess of the 90-day minimum liquidity reserve is set to provide coverage to at least 120 days.

At September 30, 2013, AgFirst met all individual level criteria and had a total of 217 days of debt coverage compared to 218 days at December 31, 2012. 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 \$92.1 million at September 30, 2013, compared to \$180.4 million at December 31, 2012. 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 \$2.3 million for the nine months ended September 30, 2013, which was included in Net Other-Than-Temporary Impairment Losses on Investments in the Statements of Income. See Note 2, *Investment Securities*, in the Notes to the Combined Financial Statements for further information.

#### *Capital Resources*

Total shareholders’ equity increased \$218.5 million (4.47 percent) from December 31, 2012 to a total of \$5.106 billion at September 30, 2013. This increase resulted primarily from 2013 unallocated retained earnings from net income of \$504.0 million and \$24.5 million in employee benefit plan adjustments in AOCI. Offsetting these increases were decreases for the redemption of preferred stock referenced below of \$150.0 million, retained earnings retired of \$63.0 million, net decreases of \$88.3 million in unrealized gains on investment securities, \$7.6 million of patronage refunds to members, and dividends paid on preferred stock of \$5.9 million.

On May 15, 2013, the Bank redeemed and cancelled the entire \$150.0 million of Perpetual Non-Cumulative Preferred Stock issued October 14, 2003. The stock was redeemed at its par value together with accrued and unpaid dividends. See Note 8, *Perpetual Preferred Stock*, in the Notes to the Combined Financial Statements for further information.

Favorable earnings and minimal balance sheet growth in recent years have resulted in stronger than historical Bank capital levels. After considering current capital levels and projected capital needs, on October 21, 2013, the Bank’s Board of Directors declared a special cash patronage distribution totaling \$200.0 million to be paid January 1, 2014 primarily to District Associations. Consistent with other patronage distributions from the Bank, each District Association will assess how much of the distribution will be retained by the Association for capital needs and how much will be distributed as patronage from the Association to its borrowers. Also see Note 15, *Subsequent Events*, in the Notes to the Combined Financial Statements.

## **RESULTS OF OPERATIONS**

Net income for the three months ended September 30, 2013 was \$177.4 million, compared to \$143.3 million for the same period of 2012, an increase of \$34.1 million, or 23.79 percent. For the nine months ended September 30, 2013, net income was \$504.0 million, compared to \$500.0 million for the same period of 2012, an increase of \$4.0 million, or 0.80 percent.

Key Results of Operations Comparisons

	<u>Annualized for the nine months ended September 30, 2013</u>	<u>For the year ended December 31, 2012</u>	<u>Annualized for the nine months ended September 30, 2012</u>
Return on average assets	2.12%	1.99%	2.09%
Return on average shareholders' equity	13.91%	13.30%	14.09%
Net interest income as a percentage of average earning assets	3.49%	3.70%	3.72%
Net (charge-offs) recoveries to average loans	(0.19)%	(0.26)%	(0.24)%

Net Interest Income

Net interest income for the three months ended September 30, 2013 was \$265.1 million compared to \$283.4 million for the same period of 2012, a decrease of \$18.3 million or 6.47 percent. Net interest income for the nine months ended September 30, 2013 was \$799.9 million compared to \$850.7 million for the same period of 2012, a decrease of \$50.8 million or 5.97 percent. The net interest margin was 3.42 percent and 3.49 percent, a decrease of 26 and 23 basis points, respectively, for the three and nine month periods compared to the prior year. The decrease was primarily the result of lower earning asset yields. Over time, as interest rates change and as assets prepay or reprice, the positive impact on the net interest margin that the District has experienced over the last several years from calling debt will continue to diminish. For the three and nine month periods ended September 30, 2013 compared with the corresponding periods in 2012, the negative impact of the rate related decrease was slightly offset by the positive impact of an increase in the average balance of loans.

The following table illustrates the changes in net interest income:

<i>(dollars in thousands)</i>	<u>For the three months ended September 30, 2013 vs. September 30, 2012</u>			<u>For the nine months ended September 30, 2013 vs. September 30, 2012</u>		
	<u>Increase (decrease) due to changes in:</u>			<u>Increase (decrease) due to changes in:</u>		
	<u>Volume</u>	<u>Rate</u>	<u>Total</u>	<u>Volume</u>	<u>Rate</u>	<u>Total</u>
Interest Income:						
Loans	\$ 4,321	\$ (10,961)	\$ (6,640)	\$ 14,597	\$ (49,792)	\$ (35,195)
Investments & Cash Equivalents	(1,380)	(10,664)	(12,044)	(4,718)	(28,076)	(32,794)
Total Interest Income	\$ 2,941	\$ (21,625)	\$ (18,684)	\$ 9,879	\$ (77,868)	\$ (67,989)
Interest Expense:						
Interest-Bearing Liabilities	\$ (748)	\$ 391	\$ (357)	\$ (1,671)	\$ (15,511)	\$ (17,182)
Changes in Net Interest Income	\$ 3,689	\$ (22,016)	\$ (18,327)	\$ 11,550	\$ (62,357)	\$ (50,807)

Provision for Loan Losses

The District measures risks inherent in its loan portfolio on an ongoing basis and, as necessary, recognizes loan loss expense so that appropriate reserves for loan losses are maintained. Provision for loan losses was a net reversal (income) of \$4.0 million for the three month period and provision expense was \$4.4 million for the nine month period ended September 30, 2013. For the three and nine months ended September 30, 2012, provision for loan losses was expense of \$38.2 million and \$63.1 million, respectively.

Provision for loan losses for the three months ended September 30, 2013 included net reversals of \$6.0 million for specific reserves and provision expense of \$2.0 million for general reserves. For the nine months ended September 30, 2013, the provision for loan losses included net reversals of \$430 thousand for specific reserves and provision expense of \$4.9 million for general reserves. Provision expense for the nine month period ended September 30, 2013 was related primarily to the cattle (\$3.7 million), nursery/greenhouse (\$3.2 million), forestry (\$1.8 million), and rural home loan (\$1.5 million) segments, partially offset by reversals in the processing (\$4.2 million) and non-farm income (\$3.1 million) segments. See Note 3, *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 September 30,			For the nine months ended September 30,		
	2013	2012	Increase/ (Decrease)	2013	2012	Increase/ (Decrease)
Loan fees	\$ 7,545	\$ 8,706	\$ (1,161)	\$ 25,100	\$ 27,981	\$ (2,881)
Fees for financially related services	3,192	3,546	(354)	6,371	6,798	(427)
Building lease income	1,149	18	1,131	3,376	42	3,334
Net impairment losses on investments	109	(158)	267	(2,254)	(3,338)	1,084
Gains (losses) on investments, net	—	—	—	7,592	—	7,592
Gains (losses) on called debt	(115)	(11,675)	11,560	(4,117)	(32,044)	27,927
Gains (losses) on other transactions	898	2,444	(1,546)	3,445	3,624	(179)
Insurance premium refund	—	—	—	—	33,744	(33,744)
Other noninterest income	800	726	74	5,596	4,243	1,353
Total noninterest income	\$ 13,578	\$ 3,607	\$ 9,971	\$ 45,109	\$ 41,050	\$ 4,059

Noninterest income increased \$10.0 million and \$4.1 million for the three and nine months ended September 30, 2013, respectively, compared to the corresponding periods in 2012. The increase for both periods was primarily due to a decrease in losses on called debt. Contributing to the nine month increase was \$7.6 million in gains on sale of investments. These increases were offset by the District's recording \$33.7 million of insurance premium refunds during the second quarter of 2012 from the Farm Credit System Insurance Corporation (FCSIC), which insures the System's debt obligations. The insurance premium refund was nonrecurring and resulted from the assets of the FCSIC exceeding the secure base amount as defined by the Farm Credit Act.

Building lease income increased \$1.1 million and \$3.3 million for the three and nine months ended September 30, 2013, compared to the same periods in 2012. This income was received in 2013 from tenants of the Bank office building which was purchased in the fourth quarter of 2012. The Bank is in the process of upfitting vacant space in the building and will relocate its operations there in 2014. Related expenses are recorded in occupancy and equipment expenses discussed below.

Net impairment losses on investments decreased \$1.1 million for the nine months ended September 30, 2013 as compared to the same period in 2012. This resulted primarily from improvement in both probability of default and projected credit loss for securities analyzed for impairment.

Gains on investments of \$7.6 million during the nine months ended September 30, 2013 were primarily the result of the sale of U.S. government agency mortgage-backed securities. See discussion of investments in the *Liquidity and Funding Sources* section above and Note 2, *Investment Securities*, in the Notes to the Combined Financial Statements for further information.

Losses on called debt decreased \$11.6 million and \$27.9 million for the three and nine month periods in 2013, respectively, compared to the same periods in 2012. Concession or debt issuance expense is amortized over the life of the underlying debt security. When debt securities are called prior to maturity, any unamortized concession is expensed. Call options were exercised on bonds totaling \$5.611 billion for the nine months ended September 30, 2013 compared to \$18.899 billion for the same period of 2012, as opportunities to call debt were more limited in the 2013 period. The called debt losses are 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 months ended September 30, 2013, gains on other transactions decreased \$1.5 million compared to the same period last year due primarily to \$1.3 million increased losses on the sale of rural home loans for the third quarter 2013 compared to the prior year. For the nine months ended September 30, 2013, gains on other transactions decreased \$179 thousand compared to the same period last year.

*Noninterest Expense*

The following table illustrates the changes in noninterest expense:

Change in Noninterest Expense <i>(dollars in thousands)</i>	For the three months ended September 30,			For the nine months ended September 30,		
	2013	2012	Increase/ (Decrease)	2013	2012	Increase/ (Decrease)
Salaries and employee benefits	\$ 67,100	\$ 64,012	\$ 3,088	\$ 204,114	\$ 193,223	\$ 10,891
Occupancy and equipment	9,528	8,444	1,084	27,550	25,106	2,444
Insurance Fund premiums	5,331	2,848	2,483	14,234	8,363	5,871
Other operating expenses	27,055	24,967	2,088	80,806	75,017	5,789
Losses (gains) from other property owned, net	(4,113)	4,700	(8,813)	9,132	25,917	(16,785)
Total noninterest expense	\$ 104,901	\$ 104,971	\$ (70)	\$ 335,836	\$ 327,626	\$ 8,210

Noninterest expense decreased \$70 thousand for the three months ended and increased \$8.2 million for the nine months ended September 30, 2013, compared to the corresponding periods in 2012. The variances for both periods ended September 30, 2013 were due to decreases in losses from other property owned, offset by increases in all other categories of noninterest expenses.

The increases in salaries and employee benefits of \$3.1 million and \$10.9 million for the three and nine month periods ended September 30, 2013, were due primarily to normal salary administration, an increase in number of employees, and increased employee benefit costs.

Occupancy and equipment expense for the three and nine months ended September 30, 2013 increased \$1.1 million and \$2.4 million, respectively, compared to the corresponding periods in 2012. These increases were due primarily to increases for the cost of space to maintain the building purchased for future Bank occupancy, as referenced above in the *Noninterest Income* section.

Insurance Fund premiums increased \$2.5 million and \$5.9 million for the three and nine month periods ended September 30, 2013. Premium expense increased as a result of an increase in the 2013 base annual premium rate to 10 basis points from the 2012 base annual premium rate of 5 basis points. 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. Offsetting the premium expense increase for the nine month period was a \$1.4 million Insurance Fund premium reimbursement received in May 2013 after FCSIC made a clarification that cash held in a deposit account at the Federal Reserve Bank qualifies as a deduction in the premium calculation. The reimbursement was for the periods July 1, 2008, when the premium methodology initially changed to a debt basis, through December 31, 2012.

Other operating expenses increased \$2.1 million and \$5.8 million for the three and nine months ended September 30, 2013, compared to the prior year. The increases primarily resulted from additional consulting and professional fees required for system enhancements of \$723 thousand and \$3.5 million and operating expenses related to nonaccrual loans of \$836 thousand and \$1.0 million for the three and nine month periods, respectively. Also contributing to the increases was additional fee expense related to the Bank's first lien residential mortgage portfolio of \$330 thousand and \$1.3 million, for the three and nine month periods, respectively, due primarily to increased guarantee fees resulting from higher guarantee fee rates and higher volume in the first lien residential mortgage portfolio.

The increase in gains from other property owned of \$8.8 million for the three months ended September 30, 2013, compared to the prior year resulted primarily from a \$5.2 million gain recorded during the third quarter of 2013 from a sale in the previous year of an ethanol plant, including \$2.3 million which was previously deferred pending settlement of litigation. During the third quarter of 2013, an additional \$1.6 million gain was recognized on a land holding. These gains also contributed to the \$16.8 million decrease in losses from other property owned for the nine months ended September 30, 2013. The remainder of the decrease for the nine month period resulted from lower writedowns recorded during 2013 as real estate values began to stabilize in most areas of the District. See *Other Property Owned* section above.

## **DISTRICT MERGER ACTIVITY**

Please refer to Note 1, *Organization, Significant Accounting Policies, and Recently Issued Accounting Pronouncements*, in the Notes to the Combined Financial Statements for information regarding merger activity in the District.

## **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 2012 Annual Report of AgFirst Farm Credit Bank and District Associations for recently issued accounting pronouncements.

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**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](http://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>	September 30, 2013 <i>(unaudited)</i>	December 31, 2012 <i>(audited)</i>
<b>Assets</b>		
Cash	\$ 810,662	\$ 775,859
Cash equivalents	152,190	149,589
Investment securities:		
Available for sale (amortized cost of \$6,538,257 and \$6,756,026, respectively)	6,630,407	6,936,420
Held to maturity (fair value of \$752,990 and \$774,275, respectively)	734,726	712,997
Total investment securities	7,365,133	7,649,417
Loans held for sale	15,286	18,132
Loans	23,081,744	22,929,205
Allowance for loan losses	(184,693)	(213,500)
Net loans	22,897,051	22,715,705
Accrued interest receivable	215,266	182,472
Accounts receivable	37,750	61,519
Investments in other Farm Credit System institutions	13,993	13,871
Other investments	82,374	163,178
Premises and equipment, net	161,104	156,315
Other property owned	91,367	109,997
Other assets	95,312	103,091
Total assets	<b>\$ 31,937,488</b>	<b>\$ 32,099,145</b>
<b>Liabilities</b>		
Systemwide debt securities	\$ 24,172,054	\$ 24,293,168
Systemwide notes payable	2,010,878	2,195,707
Accrued interest payable	45,948	40,815
Accounts payable	74,137	161,029
Advanced conditional payments	16,699	9,019
Other liabilities	511,439	511,588
Total liabilities	<b>26,831,155</b>	<b>27,211,326</b>
Commitments and contingencies (Note 5)		
<b>Shareholders' Equity</b>		
Perpetual preferred stock	125,250	275,250
Protected borrower equity	1,004	1,351
Capital stock and participation certificates	162,279	157,260
Additional paid-in-capital	60,270	60,270
Retained earnings		
Allocated	1,474,861	1,531,077
Unallocated	3,560,896	3,076,113
Accumulated other comprehensive income (loss)	(278,227)	(213,502)
Total shareholders' equity	<b>5,106,333</b>	<b>4,887,819</b>
Total liabilities and equity	<b>\$ 31,937,488</b>	<b>\$ 32,099,145</b>

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 September 30,		For the nine months ended September 30,	
	2013	2012	2013	2012
<b>Interest Income</b>				
Investment securities	\$ 36,692	\$ 48,736	\$ 119,189	\$ 151,983
Loans	279,233	285,873	825,160	860,355
Total interest income	<b>315,925</b>	334,609	<b>944,349</b>	1,012,338
<b>Interest Expense</b>				
	<b>50,865</b>	51,222	<b>144,413</b>	161,595
Net interest income	<b>265,060</b>	283,387	<b>799,936</b>	850,743
Provision for (reversal of) loan losses	<b>(3,980)</b>	38,163	<b>4,431</b>	63,137
Net interest income after provision for loan losses	<b>269,040</b>	245,224	<b>795,505</b>	787,606
<b>Noninterest Income</b>				
Loan fees	7,545	8,706	25,100	27,981
Fees for financially related services	3,192	3,546	6,371	6,798
Building lease income	1,149	18	3,376	42
Total other-than-temporary impairment losses	109	—	(1,427)	(21,995)
Portion of loss recognized in other comprehensive income	—	(158)	(827)	18,657
Net other-than-temporary impairment losses	109	(158)	(2,254)	(3,338)
Gains (losses) on investments, net	—	—	7,592	—
Gains (losses) on called debt	(115)	(11,675)	(4,117)	(32,044)
Gains (losses) on other transactions	898	2,444	3,445	3,624
Insurance premium refund	—	—	—	33,744
Other noninterest income	800	726	5,596	4,243
Total noninterest income	<b>13,578</b>	3,607	<b>45,109</b>	41,050
<b>Noninterest Expenses</b>				
Salaries and employee benefits	67,100	64,012	204,114	193,223
Occupancy and equipment	9,528	8,444	27,550	25,106
Insurance Fund premiums	5,331	2,848	14,234	8,363
Other operating expenses	27,055	24,967	80,806	75,017
Losses (gains) on other property owned, net	(4,113)	4,700	9,132	25,917
Total noninterest expenses	<b>104,901</b>	104,971	<b>335,836</b>	327,626
Income before income taxes	<b>177,717</b>	143,860	<b>504,778</b>	501,030
Provision for income taxes	<b>349</b>	584	<b>741</b>	1,000
Net income	<b>\$ 177,368</b>	\$ 143,276	<b>\$ 504,037</b>	\$ 500,030

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 September 30,		For the nine months ended September 30,	
	2013	2012	2013	2012
<b>Net income</b>	<b>\$ 177,368</b>	<b>\$ 143,276</b>	<b>\$ 504,037</b>	<b>\$ 500,030</b>
Other comprehensive income net of tax:				
Unrealized gains (losses) on investments:				
Other-than-temporarily impaired	<b>78,329</b>	12,689	<b>14,028</b>	(5,788)
Not other-than-temporarily impaired	<b>(110,864)</b>	34,082	<b>(102,328)</b>	66,987
Change in value of firm commitments - when issued securities	<b>(242)</b>	6,174	<b>(943)</b>	7,384
Employee benefit plans adjustments	<b>8,173</b>	6,391	<b>24,518</b>	20,902
Other comprehensive income (Note 9)	<b>(24,604)</b>	59,336	<b>(64,725)</b>	89,485
Comprehensive income	<b>\$ 152,764</b>	<b>\$ 202,612</b>	<b>\$ 439,312</b>	<b>\$ 589,515</b>

*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, 2011	\$ 400,000	\$ 3,269	\$ 159,334	\$ 7,873	\$ 1,415,359	\$ 2,756,592	\$ (221,248)	\$ 4,521,179
Comprehensive income						500,030	89,485	589,515
Protected borrower equity retired		(194)						(194)
Capital stock/participation certificates issued (retired), net			(1,808)					(1,808)
Dividends declared/paid			323			(472)		(149)
Dividends paid on perpetual preferred stock						(12,012)		(12,012)
Redemption of perpetual preferred stock (Note 8)	(124,750)			36,580				(88,170)
Patronage distribution								
Cash						(9,814)		(9,814)
Retained earnings retired					(52,863)	225		(52,638)
Equity issued as result of merger (Note 14)			3,163	15,817	10,463			29,443
Equity retired as result of merger (Note 14)			(3,163)		(10,463)	(14,509)		(28,135)
Patronage distribution adjustment					1,709	(1,426)		283
Balance at September 30, 2012	\$ 275,250	\$ 3,075	\$ 157,849	\$ 60,270	\$ 1,364,205	\$ 3,218,614	\$ (131,763)	\$ 4,947,500
Balance at December 31, 2012	\$ 275,250	\$ 1,351	\$ 157,260	\$ 60,270	\$ 1,531,077	\$ 3,076,113	\$ (213,502)	\$ 4,887,819
Comprehensive income						504,037	(64,725)	439,312
Protected borrower equity retired		(347)						(347)
Capital stock/participation certificates issued (retired), net			4,702					4,702
Dividends declared/paid			317			(460)		(143)
Dividends paid on perpetual preferred stock						(5,908)		(5,908)
Redemption of perpetual preferred stock (Note 8)	(150,000)							(150,000)
Patronage distribution								
Cash						(7,575)		(7,575)
Nonqualified allocated retained earnings					5,980	(5,980)		—
Retained earnings retired					(63,103)	136		(62,967)
Patronage distribution adjustment					907	533		1,440
Balance at September 30, 2013	\$ 125,250	\$ 1,004	\$ 162,279	\$ 60,270	\$ 1,474,861	\$ 3,560,896	\$ (278,227)	\$ 5,106,333

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

# Combined Statements of Cash Flows

(unaudited)

<i>(dollars in thousands)</i>	For the nine months ended September 30,	
	2013	2012
<b>Cash flows from operating activities:</b>		
Net income	\$ 504,037	\$ 500,030
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation on premises and equipment	12,762	12,502
Amortization of net deferred loan origination (fees) costs	(6,492)	(7,039)
Premium amortization (discount accretion) on investment securities	7,700	2,903
(Premium amortization) discount accretion on bonds and notes	5,075	2,675
Amortization (accretion) of yield mark resulting from merger	(4,111)	(6,329)
Provision for loan losses	4,431	63,137
(Gains) losses on other property owned	7,319	23,382
Net impairment losses on investments	2,254	3,338
(Gains) losses on investments, net	(7,592)	—
(Gains) losses on other transactions	(3,445)	(3,624)
Net change in loans held for sale	15,524	23,470
Changes in operating assets and liabilities:		
(Increase) decrease in accrued interest receivable	(32,794)	(26,221)
(Increase) decrease in accounts receivable	23,769	(1,426)
(Increase) decrease in other assets	(3,232)	(4,774)
Increase (decrease) in accrued interest payable	5,133	(6,587)
Increase (decrease) in accounts payable	3,997	(23,796)
Increase (decrease) in other liabilities	26,537	4,460
Total adjustments	56,835	56,071
Net cash provided by (used in) operating activities	560,872	556,101
<b>Cash flows from investing activities:</b>		
Investment securities purchased	(1,507,572)	(977,379)
Proceeds from investment securities sold or matured	1,697,118	1,280,447
Net (increase) decrease in loans	(230,047)	(385,299)
(Increase) decrease in investments in other Farm Credit System institutions	(122)	(165)
Purchases of other investments	—	(475)
Proceeds from payments received on other investments	83,954	83,683
Purchase of premises and equipment, net	(18,184)	(12,277)
Proceeds from sale of premises and equipment, net	1,341	1,347
Proceeds from sale of other property owned	53,340	50,759
Net cash provided by (used in) investing activities	79,828	40,641
<b>Cash flows from financing activities:</b>		
Bonds and notes issued	16,649,595	33,100,092
Bonds and notes retired	(16,948,884)	(33,921,986)
Net increase (decrease) in advanced conditional payments	7,680	4,786
Protected borrower equity retired	(347)	(194)
Capital stock and participation certificates issued/retired, net	4,702	(1,808)
Patronage refunds and dividends paid	(97,167)	(89,431)
Redemption of perpetual preferred stock (Note 8)	(150,000)	(88,170)
Dividends paid on perpetual preferred stock	(5,908)	(12,012)
Retained earnings retired	(62,967)	(52,638)
Net cash provided by (used in) financing activities	(603,296)	(1,061,361)
Net increase (decrease) in cash and cash equivalents	37,404	(464,619)
Cash and cash equivalents, beginning of period	925,448	1,340,167
Cash and cash equivalents, end of period	\$ 962,852	\$ 875,548
<b>Supplemental schedule of non-cash investing and financing activities:</b>		
Financed sales of other property owned	\$ 7,084	\$ 17,479
Receipt of property in settlement of loans	49,113	58,346
Change in unrealized gains (losses) on investments, net	(88,300)	61,199
Employee benefit plans adjustments	(24,518)	(20,902)
<b>Non-cash changes related to interest rate hedging activities:</b>		
Increase (decrease) in bonds and notes	\$ (11,011)	\$ (6,520)
Decrease (increase) in other assets	11,011	6,520
<b>Supplemental information:</b>		
Interest paid	\$ 134,205	\$ 165,510
Taxes paid, net	514	564

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, 2012 are contained in the 2012 Annual Report to Shareholders. These unaudited interim financial statements should be read in conjunction with the latest Annual Report to Shareholders.

Effective July 1, 2012, Chattanooga, ACA, merged with and into Jackson Purchase, ACA, which then changed its name to River Valley AgCredit, ACA, reducing the number of Associations to nineteen.

### Basis of Presentation

In the opinion of management, the accompanying financial statements contain all adjustments necessary for a fair presentation of the interim financial condition and results of operations and conform with generally accepted accounting principles (GAAP) and prevailing practices within the banking industry. All significant transactions and balances between AgFirst and the District Associations have been eliminated in combination.

Certain amounts in the prior period 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 for any interim period are not necessarily indicative of the results to be expected for a full year.

### Significant Accounting Policies

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. The allowance for loan losses is a valuation account used to reasonably estimate loan losses as of the financial statement date. Determining the appropriate allowance for loan losses balance involves significant judgment about when a loss has been incurred and the amount of that loss. The District considers factors such as credit risk classifications, collateral values, risk concentrations, weather related conditions, current production and economic conditions, and prior loan loss experience, among others, when determining the allowance for loan losses.

A specific allowance may be established for impaired loans under Financial Accounting Standards Board (FASB) guidance on accounting by creditors for impairment of a loan. Impairment of these loans is measured based on the present value of expected future cash flows discounted at the loan's effective interest rate, or at the loan's observable market price, or fair value of the collateral if the loan is collateral dependent.

A general allowance may also be established under FASB guidance on accounting for contingencies to reflect estimated probable credit losses incurred in the remainder of the loan portfolio at the financial statement date. The general allowance excludes loans included under the specific allowance discussed above, unless specific characteristics of the loan indicate that it is probable that there would be an incurred loss in a group of loans with those characteristics. The level of the general allowance may be based on management's best estimate of the likelihood of default adjusted for other relevant factors reflecting the current environment.

The credit risk rating methodology is a key component of the District's allowance for loan losses evaluation, and is generally incorporated into the institution's loan underwriting standards and internal lending limit. The District uses a two-dimensional loan rating model based on internally generated combined system risk rating guidance that incorporates a 14-point risk rating scale to identify and track the probability of borrower default and a separate scale addressing loss given default over a period of time. Probability of default is the probability that a borrower will experience a default within 12 months from the date of the determination of the risk rating. A default is considered to have occurred if the lender believes the borrower will not be able to pay its obligation in full or the borrower is past due more than 90 days. The loss given default is management's estimate as to the anticipated economic loss on a specific loan assuming default has occurred or is expected to occur within the next 12 months.

Each of the 14 categories carries a distinct percentage of default probability. The 14-point risk rating scale provides for granularity of the probability of default, especially in the acceptable ratings. There are nine acceptable categories that range from a borrower of the highest quality to a borrower of minimally acceptable quality. The probability of default between 1 and 9 is very narrow and would reflect almost no default to a minimal default percentage. The probability of default grows more rapidly as a loan moves from a "9" to other assets especially mentioned and grows significantly as a loan moves to a substandard (viable) level. A substandard (non-viable) rating indicates that the probability of default is almost certain.

### **Recently Issued Accounting Pronouncements**

In July 2013, the FASB issued Accounting Standards Update (ASU) 2013-10, "Derivatives and Hedging (Topic 815): Inclusion of the Fed Funds Effective Swap Rate for Hedge Accounting Purposes." As a result of the financial crisis in 2008, the exposure to and the demand for hedging the Fed Funds rate have increased significantly. That demand has been driven by an increased focus by banks on their sources of funding (including an increased focus on overnight interbank borrowings of surplus balances held at the Federal Reserve), the greater (and sometimes volatile) spread between LIBOR and OIS ("Overnight Index Swap Rate" or also referred to as the "Fed Funds Effective Swap Rate"), and new regulatory measures to curb systemic risks (such as increased collateralization of derivatives). Considering the increased importance of OIS, the objective of this ASU is to provide for the inclusion of the Fed Funds Effective Swap Rate (OIS) as a U.S. benchmark interest rate for hedge accounting purposes, in addition to UST (U.S. Treasuries) and LIBOR. The amendments are effective prospectively for qualifying new or redesignated hedging relationships entered into on or after July 17, 2013. Adoption of this guidance did not impact the District's financial condition or its results of operations.

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

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

reporting periods beginning after December 15, 2013. Early application is permitted. The District elected early adoption of this guidance for 2012. This election had no effect on the District's financial condition or results of operations.

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

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

Other recently issued accounting pronouncements are discussed in the 2012 Annual Report to Shareholders.

## **NOTE 2 — 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 Farm Credit Administration (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 the AAA/Aaa credit rating criteria and requires System institutions to provide notification to the FCA. Non-agency CMO and ABS securities not rated in the top category by at least one of the NRSROs at September 30, 2013 had a fair value of \$178.2 million and \$31.0 million, respectively. For each of these investment securities in the District's portfolio rated below AAA/Aaa, the FCA has approved, with conditions, for the District to continue to hold these investments.

Held-to-maturity Mission Related Investments consist primarily of Rural America Bonds, which are private placement securities purchased under the Mission Related Investment Program approved by the FCA. In its Conditions of Approval for the program, the FCA considers a Rural America Bond ineligible if its investment rating, based on the internal 14-point risk rating scale used to also grade loans, falls below 9. FCA approval has been obtained to allow the District to continue to hold eight Rural America Bonds whose credit quality has deteriorated beyond the program limits.

**Available-for-sale**

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

	<b>September 30, 2013</b>				
<i>(dollars in thousands)</i>	<b>Amortized Cost</b>	<b>Gross Unrealized Gains</b>	<b>Gross Unrealized Losses</b>	<b>Fair Value</b>	<b>Yield</b>
U.S. Govt. GNMA MBS/CMOs	\$ 4,460,821	\$ 113,150	\$ (11,232)	\$ 4,562,739	1.97%
U.S. Govt. Agency MBS/CMOs	1,800,254	19,652	(14,257)	1,805,649	0.97
Non-Agency CMOs (a)	209,667	18	(30,092)	179,593	0.58
Asset-Backed Securities (a)	22,325	15,449	(820)	36,954	0.78
Mission Related Investments (a)	45,190	1,753	(1,471)	45,472	6.00
<b>Total</b>	<b>\$ 6,538,257</b>	<b>\$ 150,022</b>	<b>\$ (57,872)</b>	<b>\$ 6,630,407</b>	<b>1.67%</b>

	<b>December 31, 2012</b>				
<i>(dollars in thousands)</i>	<b>Amortized Cost</b>	<b>Gross Unrealized Gains</b>	<b>Gross Unrealized Losses</b>	<b>Fair Value</b>	<b>Yield</b>
U.S. Govt. GNMA MBS/CMOs	\$ 4,814,556	\$ 198,488	\$ (12,431)	\$ 5,000,613	2.18%
U.S. Govt. Agency MBS/CMOs	1,621,428	30,002	(7,203)	1,644,227	1.17
Non-Agency CMOs (b)	246,179	27	(41,507)	204,699	0.63
Asset-Backed Securities (b)	26,219	8,236	(1,065)	33,390	0.75
Mission Related Investments	47,644	6,103	(256)	53,491	5.96
<b>Total</b>	<b>\$ 6,756,026</b>	<b>\$ 242,856</b>	<b>\$ (62,462)</b>	<b>\$ 6,936,420</b>	<b>1.90%</b>

(a) Gross unrealized losses include non-credit related other-than-temporary impairment included in AOCI of \$21.0 million for Non-Agency CMOs, \$0 for Asset-Backed Securities, and \$3 thousand for Mission Related Investments.

(b) Gross unrealized losses include non-credit related other-than-temporary impairment included in AOCI of \$27.9 million for Non-Agency CMOs and \$0 for Asset-Backed Securities.

**Held-to-maturity**

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

	<b>September 30, 2013</b>				
<i>(dollars in thousands)</i>	<b>Amortized Cost</b>	<b>Gross Unrealized Gains</b>	<b>Gross Unrealized Losses</b>	<b>Fair Value</b>	<b>Yield</b>
U.S. Govt. Agency MBS	\$ 483,753	\$ 24,185	\$ (11,870)	\$ 496,068	4.26%
Asset-Backed Securities	56,853	1,429	(156)	58,126	1.48
Mission Related Investments (a)	194,120	9,238	(4,562)	198,796	5.92
<b>Total</b>	<b>\$ 734,726</b>	<b>\$ 34,852</b>	<b>\$ (16,588)</b>	<b>\$ 752,990</b>	<b>4.49%</b>

	<b>December 31, 2012</b>				
<i>(dollars in thousands)</i>	<b>Amortized Cost</b>	<b>Gross Unrealized Gains</b>	<b>Gross Unrealized Losses</b>	<b>Fair Value</b>	<b>Yield</b>
U.S. Govt. Agency MBS	\$ 442,031	\$ 38,420	\$ (148)	\$ 480,303	5.51%
Asset-Backed Securities	68,554	1,454	(340)	69,668	1.58
Mission Related Investments	202,412	22,055	(163)	224,304	6.04
<b>Total</b>	<b>\$ 712,997</b>	<b>\$ 61,929</b>	<b>\$ (651)</b>	<b>\$ 774,275</b>	<b>5.28%</b>

(a) Gross unrealized losses include non-credit related other-than-temporary impairment included in AOCI of \$56 thousand for Rural America Bonds.

During the first nine months of 2013, proceeds from sales of investments were \$122.2 million and realized gains were \$7.6 million. During the first nine months of 2012, proceeds from sales of investments were \$486 thousand, and there were no realized gain on investments.

A summary of the contractual maturity, estimated fair value and amortized cost of investment securities at September 30, 2013 follows:

**Available-for-sale**

	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
<i>(dollars in thousands)</i>										
U.S. Govt. GNMA MBS/CMOs	\$ —	— %	\$ 58	0.39 %	\$ 7,595	1.28 %	\$ 4,555,086	1.97 %	\$ 4,562,739	1.97 %
U.S. Govt. Agency MBS/CMOs	18	0.68	8,366	2.47	38,863	2.48	1,758,402	0.93	1,805,649	0.97
Non-Agency CMOs	—	—	—	—	1,390	1.05	178,203	0.57	179,593	0.58
Asset-Backed Securities	—	—	—	—	—	—	36,954	0.78	36,954	0.78
Mission Related Investments	—	—	925	6.00	1,431	6.00	43,116	6.00	45,472	6.00
Total fair value	\$ 18	0.68 %	\$ 9,349	2.82 %	\$ 49,279	2.37 %	\$ 6,571,761	1.67 %	\$ 6,630,407	1.67 %
Total amortized cost	\$ 18		\$ 9,147		\$ 49,070		\$ 6,480,022		\$ 6,538,257	

**Held-to-maturity**

	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
<i>(dollars in thousands)</i>										
U.S. Govt. Agency MBS	\$ —	— %	\$ —	— %	\$ 628	4.75 %	\$ 483,125	4.26 %	\$ 483,753	4.26 %
Asset-Backed Securities	150	0.79	10,420	0.88	25,200	1.57	21,083	1.68	56,853	1.48
Mission Related Investments	1,800	5.00	34,929	6.39	15,431	5.93	141,960	5.82	194,120	5.92
Total amortized cost	\$ 1,950	4.68 %	\$ 45,349	5.12 %	\$ 41,259	3.25 %	\$ 646,168	4.52 %	\$ 734,726	4.49 %
Total fair value	\$ 1,954		\$ 47,536		\$ 43,152		\$ 660,348		\$ 752,990	

Substantially all of these securities have 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 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 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.

	September 30, 2013					
	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. GNMA MBS/CMOs	\$ 941,931	\$ (9,614)	\$ 166,977	\$ (1,618)	\$ 1,108,908	\$ (11,232)
U.S. Govt. Agency MBS/CMOs	1,036,130	(19,244)	326,978	(6,883)	1,363,108	(26,127)
Non-Agency CMOs	—	—	179,389	(30,092)	179,389	(30,092)
Asset-Backed Securities	1,746	(7)	15,361	(969)	17,107	(976)
Mission Related Investments	87,019	(4,224)	7,365	(1,809)	94,384	(6,033)
Total	\$ 2,066,826	\$ (33,089)	\$ 696,070	\$ (41,371)	\$ 2,762,896	\$ (74,460)

	December 31, 2012					
	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. GNMA MBS/CMOs	\$ 318,804	\$ (10,537)	\$ 183,098	\$ (1,894)	\$ 501,902	\$ (12,431)
U.S. Govt. Agency MBS/CMOs	98,792	(410)	446,896	(6,941)	545,688	(7,351)
Non-Agency CMOs	—	—	204,459	(41,507)	204,459	(41,507)
Asset-Backed Securities	665	(10)	9,526	(1,065)	10,191	(1,075)
Mortgage-Backed Securities	—	—	13,557	(330)	13,557	(330)
Mission Related Investments	10,190	(249)	2,517	(170)	12,707	(419)
Total	\$ 428,451	\$ (11,206)	\$ 860,053	\$ (51,907)	\$ 1,288,504	\$ (63,113)

FASB guidance contemplates numerous factors in determining whether an impairment is other-than-temporary. These factors include: (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 non-credit 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 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 credit worthiness 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.

Based on the results of all analyses, the District has recognized \$2.3 million of credit-related other-than-temporary impairment for 2013, which is included in Impairment Losses on Investments 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 other-than temporary impairment 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.

Following are the assumptions used at:

Assumptions Used	September 30, 2013	
	Mortgage-backed Securities	Asset-backed Securities
	Default rate by range	1.12% to 33.34%
Prepayment rate by range	4.73% to 9.68%	3.08% to 10.13%
Loss severity by range	4.08% to 75.94%	64.01% to 100.00%

Assumptions Used	December 31, 2012	
	Mortgage-backed Securities	Asset-backed Securities
	Default rate by range	0.53% to 32.62%
Prepayment rate by range	7.07% to 19.62%	5.65% to 17.57%
Loss severity by range	3.88% to 71.36%	56.22% to 100.00%

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. For the nine months ended September 30, 2013, net unrealized losses of \$102.3 million were recognized in other comprehensive income for 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 September 30,		For the nine months ended September 30,	
	2013	2012	2013	2012
<b>Cumulative Losses Beginning of Period</b>	\$ 38,866	\$ 36,879	\$ 38,217	\$ 36,542
Additions for initial credit impairments	—	—	631	1,768
Additions for subsequent credit impairments	—	158	1,732	1,570
Reductions for increases in expected cash flows	(235)	(253)	(813)	(787)
Reductions for securities sold	—	(432)	—	(432)
Reductions for losses incurred	(684)	1,964	(1,820)	(345)
<b>Cumulative Losses End of Period</b>	\$ 37,947	\$ 38,316	\$ 37,947	\$ 38,316

### NOTE 3 — LOANS AND ALLOWANCE FOR LOAN LOSSES

For a complete description of the District's accounting for loans (including impaired loans and the allowance for loan losses) and definitions of loan types, see the 2012 Annual Report to Shareholders.

Credit risk arises from the potential inability of an obligor to meet its repayment obligation. The 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.

The credit risk management process begins with an analysis of the obligor's credit history, repayment capacity and financial position. Repayment capacity focuses on the obligor's ability to repay the obligation based on cash flows from operations or other sources of income, including non-farm income. Real estate mortgage loans must be secured by first liens on the real estate collateral. As required by FCA regulations, each institution that makes loans on a secured basis must have collateral evaluation policies and procedures.

The credit risk rating process for loans uses a two-dimensional structure, incorporating a 14-point probability of default scale (as discussed in Note 1 above) and a separate scale addressing estimated percentage loss in the event of default. The loan rating structure incorporates borrower risk and transaction risk. Borrower risk is the risk of loss driven by factors intrinsic to the borrower. The transaction risk is related to the structure of a credit (tenor, terms, and collateral).

A summary of loans outstanding at period end follows:

<i>(dollars in thousands)</i>	September 30, 2013	December 31, 2012
Real estate mortgage	\$ 10,142,047	\$ 9,921,750
Production and intermediate-term	7,408,367	7,760,377
Loans to cooperatives	251,225	235,703
Processing and marketing	1,115,607	1,053,247
Farm-related business	372,910	354,039
Communication	353,074	319,320
Energy/water and waste disposal	495,454	525,070
Rural residential real estate	2,792,634	2,634,609
Lease receivables	5,079	2,880
Loans to other financial institutions (OFIs)	85,066	60,479
Other (including mission-related)	60,281	61,731
Total Loans	<u>\$ 23,081,744</u>	<u>\$ 22,929,205</u>

The District may purchase or sell participation interests with other parties in order to diversify risk, manage loan volume, and comply with FCA regulations. The following tables present the principal balance of participation loans, including loans to OFIs, at periods ended:

<i>(dollars in thousands)</i>	September 30, 2013					
	Within Farm Credit System		Outside Farm Credit System		Total	
	Participations Purchased	Participations Sold	Participations Purchased	Participations Sold	Participations Purchased	Participations Sold
Real estate mortgage	\$ 163,189	\$ 35,424	\$ 82,445	\$ 18,082	\$ 245,634	\$ 53,506
Production and intermediate-term	470,231	321,052	582,537	4,283	1,052,768	325,335
Loans to cooperatives	211,065	-	22,149	-	233,214	-
Processing and marketing	400,488	47,897	572,857	2,802	973,345	50,699
Farm-related business	140,824	490	50,093	-	190,917	490
Communication	339,475	-	10,000	-	349,475	-
Energy/water and waste disposal	490,497	-	6,953	-	497,450	-
Rural residential real estate	-	-	49	-	49	-
Lease receivables	2,432	-	-	-	2,432	-
Loans to OFIs	-	-	85,066	-	85,066	-
Other (including mission-related)	10,000	-	3,790	-	13,790	-
Total	<u>\$ 2,228,201</u>	<u>\$ 404,863</u>	<u>\$ 1,415,939</u>	<u>\$ 25,167</u>	<u>\$ 3,644,140</u>	<u>\$ 430,030</u>

<i>(dollars in thousands)</i>	December 31, 2012					
	Within Farm Credit System		Outside Farm Credit System		Total	
	Participations Purchased	Participations Sold	Participations Purchased	Participations Sold	Participations Purchased	Participations Sold
Real estate mortgage	\$ 143,204	\$ 51,816	\$ 94,815	\$ 20,537	\$ 238,019	\$ 72,353
Production and intermediate-term	434,656	233,016	391,410	4,434	826,066	237,450
Loans to cooperatives	199,342	-	17,173	-	216,515	-
Processing and marketing	418,060	48,556	591,669	4,052	1,009,729	52,608
Farm-related business	128,279	630	37,373	817	165,652	1,447
Communication	354,180	-	-	-	354,180	-
Energy/water and waste disposal	530,641	-	7,204	-	537,845	-
Rural residential real estate	-	-	51	-	51	-
Lease receivables	861	-	-	-	861	-
Loans to OFIs	-	-	60,479	-	60,479	-
Other (including mission-related)	-	19,776	5,673	2,910	5,673	22,686
Total	<u>\$ 2,209,223</u>	<u>\$ 353,794</u>	<u>\$ 1,205,847</u>	<u>\$ 32,750</u>	<u>\$ 3,415,070</u>	<u>\$ 386,544</u>

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

<i>(dollars in thousands)</i>	September 30, 2013			
	Due less than 1 year	Due 1 through 5 years	Due after 5 years	Total
Real estate mortgage	\$ 616,536	\$ 2,426,214	\$ 7,099,297	\$ 10,142,047
Production and intermediate-term	2,052,052	3,159,487	2,196,828	7,408,367
Loans to cooperatives	58,498	129,620	63,107	251,225
Processing and marketing	218,025	592,617	304,965	1,115,607
Farm-related business	53,345	223,779	95,786	372,910
Communication	99,083	144,421	109,570	353,074
Energy/water and waste disposal	28,581	178,210	288,663	495,454
Rural residential real estate	27,129	66,780	2,698,725	2,792,634
Lease receivables	2,467	2,612	-	5,079
Loans to OFIs	-	83,866	1,200	85,066
Other (including mission-related)	7,198	10,646	42,437	60,281
Total Loans	<u>\$ 3,162,914</u>	<u>\$ 7,018,252</u>	<u>\$ 12,900,578</u>	<u>\$ 23,081,744</u>
Percentage	13.70%	30.41%	55.89%	100.00%

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

	September 30, 2013	December 31, 2012		September 30, 2013	December 31, 2012
<b>Real estate mortgage:</b>			<b>Energy/water and waste disposal:</b>		
Acceptable	91.08%	89.50%	Acceptable	99.95%	99.99%
OAEM	4.00	4.79	OAEM	-	0.01
Substandard/doubtful/loss	4.92	5.71	Substandard/doubtful/loss	0.05	-
	<u>100.00%</u>	<u>100.00%</u>		<u>100.00%</u>	<u>100.00%</u>
<b>Production and intermediate-term:</b>			<b>Rural residential real estate:</b>		
Acceptable	88.52%	86.80%	Acceptable	99.03%	98.81%
OAEM	5.27	5.09	OAEM	0.32	0.45
Substandard/doubtful/loss	6.21	8.11	Substandard/doubtful/loss	0.65	0.74
	<u>100.00%</u>	<u>100.00%</u>		<u>100.00%</u>	<u>100.00%</u>
<b>Loans to cooperatives:</b>			<b>Lease receivables:</b>		
Acceptable	99.94%	96.45%	Acceptable	96.39%	91.42%
OAEM	0.03	2.90	OAEM	3.10	7.47
Substandard/doubtful/loss	0.03	0.65	Substandard/doubtful/loss	0.51	1.11
	<u>100.00%</u>	<u>100.00%</u>		<u>100.00%</u>	<u>100.00%</u>
<b>Processing and marketing:</b>			<b>Loans to OFIs:</b>		
Acceptable	94.53%	89.13%	Acceptable	100.00%	100.00%
OAEM	2.22	3.05	OAEM	-	-
Substandard/doubtful/loss	3.25	7.82	Substandard/doubtful/loss	-	-
	<u>100.00%</u>	<u>100.00%</u>		<u>100.00%</u>	<u>100.00%</u>
<b>Farm-related business:</b>			<b>Other (including mission-related):</b>		
Acceptable	97.49%	94.45%	Acceptable	85.27%	86.61%
OAEM	1.35	3.10	OAEM	0.07	-
Substandard/doubtful/loss	1.16	2.45	Substandard/doubtful/loss	14.66	13.39
	<u>100.00%</u>	<u>100.00%</u>		<u>100.00%</u>	<u>100.00%</u>
<b>Communication:</b>			<b>Total Loans:</b>		
Acceptable	100.00%	100.00%	Acceptable	91.92%	90.19%
OAEM	-	-	OAEM	3.62	4.07
Substandard/doubtful/loss	-	-	Substandard/doubtful/loss	4.46	5.74
	<u>100.00%</u>	<u>100.00%</u>		<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:

September 30, 2013

<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	\$ 87,578	\$ 113,309	\$ 200,887	\$ 10,041,397	\$ 10,242,284	\$ 45
Production and intermediate-term	37,383	97,643	135,026	7,353,253	7,488,279	254
Loans to cooperatives	13	—	13	252,452	252,465	—
Processing and marketing	246	18,026	18,272	1,101,050	1,119,322	—
Farm-related business	474	139	613	374,121	374,734	—
Communication	—	—	—	353,411	353,411	—
Energy/water and waste disposal	—	—	—	497,108	497,108	—
Rural residential real estate	40,504	6,909	47,413	2,756,639	2,804,052	2,754
Lease receivables	—	26	26	5,058	5,084	—
Loans to OFIs	—	—	—	85,178	85,178	—
Other (including mission-related)	238	4,779	5,017	55,874	60,891	—
Total	\$ 166,436	\$ 240,831	\$ 407,267	\$ 22,875,541	\$ 23,282,808	\$ 3,053

December 31, 2012

<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	\$ 81,839	\$ 153,406	\$ 235,245	\$ 9,766,477	\$ 10,001,722	\$ 786
Production and intermediate-term	40,946	141,898	182,844	7,644,134	7,826,978	148
Loans to cooperatives	—	1,548	1,548	234,922	236,470	—
Processing and marketing	618	25,234	25,852	1,030,716	1,056,568	—
Farm-related business	186	417	603	355,252	355,855	—
Communication	—	—	—	319,726	319,726	—
Energy/water and waste disposal	—	—	—	526,263	526,263	—
Rural residential real estate	51,050	7,853	58,903	2,587,098	2,646,001	2,313
Lease receivables	40	32	72	2,810	2,882	—
Loans to OFIs	—	—	—	60,544	60,544	—
Other (including mission-related)	117	7,446	7,563	54,804	62,367	478
Total	\$ 174,796	\$ 337,834	\$ 512,630	\$ 22,582,746	\$ 23,095,376	\$ 3,725

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

Nonperforming assets (including related accrued interest) and related credit quality statistics are summarized as follows:

<i>(dollars in thousands)</i>	<b>September 30, 2013</b>	<b>December 31, 2012</b>
<b>Nonaccrual loans:</b>		
Real estate mortgage	\$ 247,771	\$ 266,827
Production and intermediate-term	193,126	249,086
Loans to cooperatives	8	1,545
Processing and marketing	18,030	40,526
Farm-related business	3,976	4,575
Energy/water and waste disposal	235	-
Rural residential real estate	9,622	11,364
Lease receivables	26	32
Other (including mission-related)	4,757	6,953
Total nonaccrual loans	<u>\$ 477,551</u>	<u>\$ 580,908</u>
<b>Accruing restructured loans:</b>		
Real estate mortgage	\$ 61,035	\$ 50,338
Production and intermediate-term	51,001	50,269
Farm-related business	825	867
Rural residential real estate	1,817	1,793
Total accruing restructured loans	<u>\$ 114,678</u>	<u>\$ 103,267</u>
<b>Accruing loans 90 days or more past due:</b>		
Real estate mortgage	\$ 45	\$ 786
Production and intermediate-term	254	148
Rural residential real estate	2,754	2,313
Other (including mission-related)	-	478
Total accruing loans 90 days or more past due	<u>\$ 3,053</u>	<u>\$ 3,725</u>
Total nonperforming loans	\$ 595,282	\$ 687,900
Other property owned	91,367	109,997
Total nonperforming assets	<u>\$ 686,649</u>	<u>\$ 797,897</u>
Nonaccrual loans as a percentage of total loans	2.07%	2.53%
Nonperforming assets as a percentage of total loans and other property owned	2.96%	3.46%
Nonperforming assets as a percentage of capital	<u>13.45%</u>	<u>16.32%</u>

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

<i>(dollars in thousands)</i>	<b>September 30, 2013</b>	<b>December 31, 2012</b>
<b>Impaired nonaccrual loans:</b>		
Current as to principal and interest	\$ 187,858	\$ 200,430
Past due	289,693	380,478
Total impaired nonaccrual loans	<u>477,551</u>	<u>580,908</u>
<b>Impaired accrual loans:</b>		
Restructured	114,678	103,267
90 days or more past due	3,053	3,725
Total impaired accrual loans	<u>117,731</u>	<u>106,992</u>
Total impaired loans	<u>\$ 595,282</u>	<u>\$ 687,900</u>

Additional impaired loan information at period end is summarized as follows:

	September 30, 2013			Quarter Ended September 30, 2013		Nine Months Ended September 30, 2013	
	Recorded Investment	Unpaid Principal Balance	Related Allowance	Average Impaired Loans	Interest Income Recognized on Impaired Loans	Average Impaired Loans	Interest Income Recognized on Impaired Loans
<i>(dollars in thousands)</i>							
<b>Impaired loans with a related allowance for credit losses:</b>							
Real estate mortgage	\$ 91,582	\$ 109,511	\$ 22,601	\$ 99,394	\$ 496	\$ 112,289	\$ 1,584
Production and intermediate-term	100,834	128,328	33,165	109,698	500	136,073	1,916
Loans to cooperatives	—	—	—	—	—	—	—
Processing and marketing	355	560	85	396	(132)	16,242	8
Farm-related business	3,888	4,223	548	4,240	35	4,106	82
Communication	—	—	—	—	—	—	—
Energy/water and waste disposal	236	241	236	263	1	321	5
Rural residential real estate	4,630	5,392	1,620	5,021	45	5,380	95
Lease receivables	—	—	—	—	—	—	—
Other (including mission-related)	3,207	3,262	78	3,577	30	4,598	72
Total	<u>\$ 204,732</u>	<u>\$ 251,517</u>	<u>\$ 58,333</u>	<u>\$ 222,589</u>	<u>\$ 975</u>	<u>\$ 279,009</u>	<u>\$ 3,762</u>
<b>Impaired loans with no related allowance for credit losses:</b>							
Real estate mortgage	\$ 217,269	\$ 286,470	\$ —	\$ 223,020	\$ 1,487	\$ 205,402	\$ 3,840
Production and intermediate-term	143,547	188,335	—	165,995	1,276	152,498	2,960
Loans to cooperatives	8	41	—	9	—	539	—
Processing and marketing	17,675	33,657	—	16,060	143	13,501	238
Farm-related business	913	1,689	—	996	8	963	19
Communication	—	—	—	—	—	9	—
Energy/water and waste disposal	(1)	—	—	(1)	—	(2)	—
Rural residential real estate	9,563	11,525	—	8,901	36	9,635	188
Lease receivables	26	78	—	29	—	29	1
Other (including mission-related)	1,550	1,861	—	1,730	(7)	2,112	35
Total	<u>\$ 390,550</u>	<u>\$ 523,656</u>	<u>\$ —</u>	<u>\$ 416,739</u>	<u>\$ 2,943</u>	<u>\$ 384,686</u>	<u>\$ 7,281</u>
<b>Total impaired loans:</b>							
Real estate mortgage	\$ 308,851	\$ 395,981	\$ 22,601	\$ 322,414	\$ 1,983	\$ 317,691	\$ 5,424
Production and intermediate-term	244,381	316,663	33,165	275,693	1,776	288,571	4,876
Loans to cooperatives	8	41	—	9	—	539	—
Processing and marketing	18,030	34,217	85	16,456	11	29,743	246
Farm-related business	4,801	5,912	548	5,236	43	5,069	101
Communication	—	—	—	—	—	9	—
Energy/water and waste disposal	235	241	236	262	1	319	5
Rural residential real estate	14,193	16,917	1,620	13,922	81	15,015	283
Lease receivables	26	78	—	29	—	29	1
Other (including mission-related)	4,757	5,123	78	5,307	23	6,710	107
Total	<u>\$ 595,282</u>	<u>\$ 775,173</u>	<u>\$ 58,333</u>	<u>\$ 639,328</u>	<u>\$ 3,918</u>	<u>\$ 663,695</u>	<u>\$ 11,043</u>

<i>(dollars in thousands)</i>	December 31, 2012			Year Ended December 31, 2012	
	Recorded Investment	Unpaid Principal Balance	Related Allowance	Average Impaired Loans	Interest Income Recognized on Impaired Loans
<b>Impaired loans with a related allowance for credit losses:</b>					
Real estate mortgage	\$ 110,633	\$ 140,657	\$ 29,578	\$ 121,051	\$ 2,703
Production and intermediate-term	149,996	190,301	50,839	150,439	3,476
Processing and marketing	25,846	26,797	8,755	16,164	487
Farm-related business	4,407	5,260	770	5,321	131
Rural residential real estate	5,309	7,764	1,433	5,508	157
Other (including mission-related)	6,409	6,360	627	2,603	211
Total	<u>\$ 302,600</u>	<u>\$ 377,139</u>	<u>\$ 92,002</u>	<u>\$ 301,086</u>	<u>\$ 7,165</u>
<b>Impaired loans with no related allowance for credit losses:</b>					
Real estate mortgage	\$ 207,318	\$ 269,787	\$ —	\$ 207,079	\$ 6,551
Production and intermediate-term	149,507	201,879	—	165,107	5,423
Loans to cooperatives	1,545	1,564	—	1,553	50
Processing and marketing	14,680	21,134	—	21,367	1,314
Farm-related business	1,035	1,922	—	2,132	30
Rural residential real estate	10,161	11,877	—	11,794	347
Lease receivables	32	83	—	76	1
Other (including mission-related)	1,022	995	—	6,424	70
Total	<u>\$ 385,300</u>	<u>\$ 509,241</u>	<u>\$ —</u>	<u>\$ 415,532</u>	<u>\$ 13,786</u>
<b>Total impaired loans:</b>					
Real estate mortgage	\$ 317,951	\$ 410,444	\$ 29,578	\$ 328,130	\$ 9,254
Production and intermediate-term	299,503	392,180	50,839	315,546	8,899
Loans to cooperatives	1,545	1,564	—	1,553	50
Processing and marketing	40,526	47,931	8,755	37,531	1,801
Farm-related business	5,442	7,182	770	7,453	161
Rural residential real estate	15,470	19,641	1,433	17,302	504
Lease receivables	32	83	—	76	1
Other (including mission-related)	7,431	7,355	627	9,027	281
Total	<u>\$ 687,900</u>	<u>\$ 886,380</u>	<u>\$ 92,002</u>	<u>\$ 716,618</u>	<u>\$ 20,951</u>

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

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

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

<i>(dollars in thousands)</i>	Real Estate Mortgage	Production and Intermediate-term	Agribusiness*	Communication	Energy/Water and Waste Disposal	Rural Residential Real Estate	Lease Receivables	Other Loans (including mission related)	Total
<b>Allowance for credit losses:</b>									
Balance at June 30, 2013	\$ 74,723	\$ 116,754	\$ 12,338	\$ 810	\$ 1,604	\$ 4,494	\$ 89	\$ 557	\$ 211,369
Charge-offs	(2,952)	(20,435)	(4,243)	—	—	(542)	—	(398)	(28,570)
Recoveries	4,678	667	230	—	—	20	—	279	5,874
Provision for loan losses	(6,545)	827	1,330	134	(38)	739	9	(436)	(3,980)
Loan type reclassification	(1,205)	318	439	—	(2)	—	—	450	—
Balance at September 30, 2013	\$ 68,699	\$ 98,131	\$ 10,094	\$ 944	\$ 1,564	\$ 4,711	\$ 98	\$ 452	\$ 184,693
Balance at December 31, 2012	\$ 76,832	\$ 110,409	\$ 18,990	\$ 863	\$ 1,364	\$ 3,968	\$ 40	\$ 1,034	\$ 213,500
Charge-offs	(10,408)	(27,726)	(8,878)	—	—	(824)	(5)	(398)	(48,239)
Recoveries	10,023	3,467	755	—	—	430	—	326	15,001
Provision for loan losses	(6,990)	11,663	(1,212)	81	263	1,137	63	(574)	4,431
Loan type reclassification	(758)	318	439	—	(63)	—	—	64	—
Balance at September 30, 2013	\$ 68,699	\$ 98,131	\$ 10,094	\$ 944	\$ 1,564	\$ 4,711	\$ 98	\$ 452	\$ 184,693
Balance at June 30, 2012	\$ 65,804	\$ 89,817	\$ 13,251	\$ 731	\$ 1,110	\$ 3,619	\$ 17	\$ 740	\$ 175,089
Charge-offs	(8,420)	(9,693)	(2,287)	—	—	(592)	—	(1)	(20,993)
Recoveries	1,312	4,770	13	—	—	17	—	6	6,118
Provision for loan losses	12,135	18,505	7,046	52	35	691	31	(332)	38,163
Adjustment due to merger	(440)	(702)	(235)	—	—	(32)	—	—	(1,409)
Loan type reclassification	—	—	(1)	—	—	—	—	1	—
Balance at September 30, 2012	\$ 70,391	\$ 102,697	\$ 17,787	\$ 783	\$ 1,145	\$ 3,703	\$ 48	\$ 414	\$ 196,968
Balance at December 31, 2011	\$ 65,951	\$ 89,155	\$ 14,050	\$ 482	\$ 672	\$ 4,015	\$ 20	\$ 631	\$ 174,976
Charge-offs	(34,371)	(21,720)	(2,305)	—	—	(1,729)	—	(366)	(60,491)
Recoveries	5,962	14,626	85	—	—	76	—	6	20,755
Provision for loan losses	35,072	19,461	6,230	301	473	1,429	28	143	63,137
Adjustment due to merger	(440)	(702)	(235)	—	—	(32)	—	—	(1,409)
Loan type reclassification	(1,783)	1,877	(38)	—	—	(56)	—	—	—
Balance at September 30, 2012	\$ 70,391	\$ 102,697	\$ 17,787	\$ 783	\$ 1,145	\$ 3,703	\$ 48	\$ 414	\$ 196,968
Loans individually evaluated for impairment	\$ 22,562	\$ 33,085	\$ 633	\$ —	\$ 236	\$ 1,620	\$ —	\$ 78	\$ 58,214
Loans collectively evaluated for impairment	46,098	64,966	9,461	944	1,328	3,091	98	374	126,360
Loans acquired with deteriorated credit quality	39	80	—	—	—	—	—	—	119
Balance at September 30, 2013	\$ 68,699	\$ 98,131	\$ 10,094	\$ 944	\$ 1,564	\$ 4,711	\$ 98	\$ 452	\$ 184,693
Loans individually evaluated for impairment	\$ 29,124	\$ 50,786	\$ 9,499	\$ —	\$ —	\$ 1,365	\$ —	\$ 627	\$ 91,401
Loans collectively evaluated for impairment	47,254	59,570	9,465	863	1,364	2,535	40	407	121,498
Loans acquired with deteriorated credit quality	454	53	26	—	—	68	—	—	601
Balance at December 31, 2012	\$ 76,832	\$ 110,409	\$ 18,990	\$ 863	\$ 1,364	\$ 3,968	\$ 40	\$ 1,034	\$ 213,500
<b>Recorded investment in loans outstanding:</b>									
Loans individually evaluated for impairment	\$ 337,288	\$ 201,159	\$ 22,852	\$ —	\$ 236	\$ 2,287,873	\$ —	\$ 3,747	\$ 2,853,155
Loans collectively evaluated for impairment	9,895,814	7,281,395	1,723,669	353,411	496,872	515,987	5,084	142,322	20,414,554
Loans acquired with deteriorated credit quality	9,182	5,725	—	—	—	192	—	—	15,099
Ending balance at September 30, 2013	\$ 10,242,284	\$ 7,488,279	\$ 1,746,521	\$ 353,411	\$ 497,108	\$ 2,804,052	\$ 5,084	\$ 146,069	\$ 23,282,808
Loans individually evaluated for impairment	\$ 373,848	\$ 258,994	\$ 51,473	\$ —	\$ —	\$ 2,182,310	\$ —	\$ —	\$ 2,866,625
Loans collectively evaluated for impairment	9,611,337	7,561,221	1,597,150	319,726	526,263	462,283	2,882	122,911	20,203,773
Loans acquired with deteriorated credit quality	16,537	6,763	270	—	—	1,408	—	—	24,978
Ending balance at December 31, 2012	\$ 10,001,722	\$ 7,826,978	\$ 1,648,893	\$ 319,726	\$ 526,263	\$ 2,646,001	\$ 2,882	\$ 122,911	\$ 23,095,376

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

A restructuring of a debt constitutes a troubled debt restructuring (TDR) if the creditor for economic or legal reasons related to the debtor's financial difficulties grants a concession to the debtor that it would not otherwise consider. The following tables present additional information about activity that occurred during the periods presented related to TDRs. The tables do not include purchased credit impaired loans.

Three months ended September 30, 2013				
Pre-modification Outstanding Recorded Investment				
	Interest Concessions	Principal Concessions	Other Concessions	Total
<b>Troubled debt restructurings:</b>				
Real estate mortgage	\$ 22,101	\$ 3,915	\$ 5,754	\$ 31,770
Production and intermediate-term	23,584	9,817	679	34,080
Rural residential real estate	635	—	—	635
Total	\$ 46,320	\$ 13,732	\$ 6,433	\$ 66,485

Three months ended September 30, 2013					
Post-modification Outstanding Recorded Investment					Effects of Modification
	Interest Concessions	Principal Concessions	Other Concessions	Total	Charge-offs
<b>Troubled debt restructurings:</b>					
Real estate mortgage	\$ 12,223	\$ 3,745	\$ 5,815	\$ 21,783	\$ (7,824)
Production and intermediate-term	17,922	9,858	470	28,250	(7,260)
Rural residential real estate	615	—	—	615	—
Total	\$ 30,760	\$ 13,603	\$ 6,285	\$ 50,648	\$ (15,084)

Nine months ended September 30, 2013				
Pre-modification Outstanding Recorded Investment				
	Interest Concessions	Principal Concessions	Other Concessions	Total
<b>Troubled debt restructurings:</b>				
Real estate mortgage	\$ 30,783	\$ 18,340	\$ 6,931	\$ 56,054
Production and intermediate-term	23,862	26,452	1,868	52,182
Rural residential real estate	904	—	—	904
Total	\$ 55,549	\$ 44,792	\$ 8,799	\$ 109,140

Nine months ended September 30, 2013					
Post-modification Outstanding Recorded Investment					Effects of Modification
	Interest Concessions	Principal Concessions	Other Concessions	Total	Charge-offs
<b>Troubled debt restructurings:</b>					
Real estate mortgage	\$ 20,909	\$ 18,358	\$ 6,984	\$ 46,251	\$ (7,835)
Production and intermediate-term	18,200	26,527	1,653	46,380	(8,155)
Rural residential real estate	885	—	—	885	—
Total	\$ 39,994	\$ 44,885	\$ 8,637	\$ 93,516	\$ (15,990)

Three months ended September 30, 2012				
Pre-modification Outstanding Recorded Investment				
	Interest Concessions	Principal Concessions	Other Concessions	Total
<b>Troubled debt restructurings:</b>				
Real estate mortgage	\$ 3,587	\$ 21,336	\$ 1,196	\$ 26,119
Production and intermediate-term	67	30,184	51	30,302
Farm related business	—	24	—	24
Rural residential real estate	—	63	—	63
Total	\$ 3,654	\$ 51,607	\$ 1,247	\$ 56,508

Three months ended September 30, 2012

	Post-modification Outstanding Recorded Investment				Effects of Modification
	Interest Concessions	Principal Concessions	Other Concessions	Total	Charge-offs
<b>Troubled debt restructurings:</b>					
Real estate mortgage	\$ 3,588	\$ 20,132	\$ 1,180	\$ 24,900	\$ (877)
Production and intermediate-term	67	29,745	50	29,862	(381)
Farm related business	–	25	–	25	–
Rural residential real estate	–	63	–	63	(65)
Total	\$ 3,655	\$ 49,965	\$ 1,230	\$ 54,850	\$ (1,323)

Nine months ended September 30, 2012

	Pre-modification Outstanding Recorded Investment			
	Interest Concessions	Principal Concessions	Other Concessions	Total
<b>Troubled debt restructurings:</b>				
Real estate mortgage	\$ 8,796	\$ 52,528	\$ 2,205	\$ 63,529
Production and intermediate-term	2,622	59,091	118	61,831
Farm related business	694	3,979	321	4,994
Rural residential real estate	4	670	78	752
Total	\$ 12,116	\$ 116,268	\$ 2,722	\$ 131,106

Nine months ended September 30, 2012

	Post-modification Outstanding Recorded Investment				Effects of Modification
	Interest Concessions	Principal Concessions	Other Concessions	Total	Charge-offs
<b>Troubled debt restructurings:</b>					
Real estate mortgage	\$ 8,790	\$ 51,186	\$ 2,144	\$ 62,120	\$ (1,260)
Production and intermediate-term	1,831	58,959	118	60,908	(386)
Farm related business	692	3,980	321	4,993	–
Rural residential real estate	4	674	78	756	(129)
Total	\$ 11,317	\$ 114,799	\$ 2,661	\$ 128,777	\$ (1,775)

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

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

	Three months ended September 30,		Nine months ended September 30,	
	2013	2012	2013	2012
<b>Defaulted troubled debt restructurings:</b>				
Real estate mortgage	\$ 3,920	\$ 6,431	\$ 4,983	\$ 11,548
Production and intermediate-term	3,851	6,461	8,877	16,787
Processing and marketing	7,456	–	27,042	–
Farm-related business	–	–	–	8
Rural residential real estate	–	41	–	66
Total	\$ 15,227	\$ 12,933	\$ 40,902	\$ 28,409

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

	Total TDRs		Nonaccrual TDRs	
	September 30, 2013	December 31, 2012	September 30, 2013	December 31, 2012
Real estate mortgage	\$ 145,439	\$ 128,399	\$ 84,404	\$ 78,061
Production and intermediate-term	126,942	115,933	75,941	65,664
Processing and marketing	17,399	24,930	17,399	24,930
Farm-related business	4,185	4,449	3,360	3,582
Rural residential real estate	3,344	3,583	1,527	1,790
Total Loans	\$ 297,309	\$ 277,294	\$ 182,631	\$ 174,027
Additional commitments to lend	\$ 8,569	\$ 17,444		

### Purchased Credit Impaired Loans

District entities acquire loans individually and in groups or portfolios. For certain acquired loans that experienced deterioration in credit quality between origination and acquisition, the amount paid for the loan will reflect this fact. At acquisition, each loan is reviewed to determine whether there is evidence of deterioration of credit quality since origination and if it is probable that the holder would be unable to collect all amounts due according to the loan's contractual terms. If both conditions exist, the purchaser determines whether each such loan is to be accounted for individually or whether such loans would be assembled into pools of loans based on common risk characteristics (credit score, loan type, and date of origination, for example). Considerations of value should include expected prepayments, the estimated amount and timing of undiscounted expected principal, interest, and other cash flows (expected at acquisition) for each loan and the subsequently aggregated pool of loans. Any excess of the loan's or pool's scheduled contractual principal and contractual interest payments over all of the cash flows expected at acquisition is an amount that should not be accreted to income (nonaccretable difference). The remaining amount, representing the excess of the loan's cash flows expected to be collected over the amount paid, is accreted into interest income over the remaining life of the loan or pool (accretable yield).

Accounting guidance requires that the purchaser continue to estimate cash flows expected to be collected over the life of the loan or pool. It then evaluates at the balance sheet date whether the present value of its loans, determined using the effective interest rate, has decreased and if so, recognizes a loss. For loans or pools that are not accounted for as debt securities, the present value of any subsequent increase in the loan's or pool's actual cash flows or cash flows expected to be collected is used first to reverse any existing valuation allowance for that loan or pool. For any remaining increases in cash flows expected to be collected, or for loans or pools accounted for as debt securities, a purchaser adjusts the amount of accretable yield recognized on a prospective basis over the loan's or pool's remaining life.

Valuation allowances for all purchased impaired loans reflect only those losses incurred after acquisition, that is, the present value of cash flows expected at acquisition that are not expected to be collected. Valuation allowances are established only subsequent to acquisition of the loans.

As discussed in Note 14:

- i. Effective January 1, 2011, Farm Credit of North Florida, ACA, and Farm Credit of Southwest Florida, ACA, merged with and into Farm Credit of South Florida, ACA, which then changed its name to Farm Credit of Florida, ACA.
- ii. Effective July 1, 2012, Chattanooga, ACA, merged with and into Jackson Purchase, ACA, which then changed its name to River Valley AgCredit, ACA (River Valley).

The mergers were accounted for under the acquisition method.

In connection with the mergers, the acquirers 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 September 30, 2013, were as follows.

<i>(dollars in thousands)</i>	Loans Acquired During	
	2012	2011
Real estate mortgage	\$ 1,508	\$ 7,674
Production and intermediate-term	2,696	3,029
Farm-related business	—	—
Rural residential real estate	90	102
Total Loans	\$ 4,294	\$ 10,805

At September 30, 2013, the allowance for loan losses related to these loans was \$119 thousand compared with \$601 thousand at December 31, 2012. During the three and nine month periods ended September 30, 2013, provision for loan losses on these loans was \$301 thousand and a reversal of \$567 thousand, respectively, compared with expense of \$570 thousand and \$875 thousand for the three and nine month periods ended September 30, 2012, respectively. See above for a summary of changes in the total allowance for loan losses for the period ended September 30, 2013.

The total of loans acquired during 2011 and 2012 for which it was probable at acquisition that all contractually required payments would not be collected are as follows. None were acquired in 2013.

<i>(dollars in thousands)</i>	2012	2011
Real estate mortgage	\$ 3,488	\$ 57,735
Production and intermediate-term	4,105	18,862
Processing and marketing	—	2,196
Farm-related business	—	1,734
Rural residential real estate	236	1,769
Total Loans	\$ 7,829	\$ 82,296

Certain of the loans acquired in the business combinations 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 merger, the real estate markets were very unpredictable. These settings made 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 4 — 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 of the District's assets and liabilities within the fair value hierarchy are as follows:

### **Level 1**

Level 1 inputs to the valuation methodology are unadjusted quoted prices for identical assets or liabilities in active markets. 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 1 assets consist of assets held in trust funds related to deferred compensation and supplemental retirement plans. The trust funds include investments in securities that are actively traded and have quoted net asset value prices that are directly observable in the marketplace.

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

### **Level 2**

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

The fair value of substantially all investment securities is determined from third-party valuation services that estimate current market prices. Inputs and assumptions related to third-party market valuation services are typically observable in the marketplace. Such services incorporate prepayment assumptions and underlying mortgage- or asset-backed collateral information to generate cash flows that are discounted using appropriate benchmark interest rate curves and volatilities. Third-party valuations also incorporate information regarding broker/dealer quotes, available trade information, historical cash flows, credit ratings, and other market information. Such valuations represent an estimated exit price, or price to be received by a seller in active markets to sell the investment securities to a willing participant.

Level 2 assets include investments in U.S. government and agency mortgage-backed securities and U.S. agency debt securities, all of which use unadjusted values from third parties or internal pricing models. The underlying loans for these investment securities are residential mortgages. Also included are federal funds sold, securities purchased under resale agreements, and other highly-liquid funds, all of which are non-exchange-traded instruments. The market value of these federal funds sold and other instruments is generally their face value, plus accrued interest, as these instruments are highly-liquid, readily convertible to cash, and short-term in nature.

The fair value of derivative financial instruments is the estimated amount to be received to sell a derivative asset or paid to transfer a derivative liability in active markets among willing participants at the reporting date. Estimated fair values are determined through internal market valuation models which use an income approach. These models incorporate benchmark interest rate curves (primarily the LIBOR swap curve), potential volatilities of future interest rate movements, and other inputs which are observable directly or indirectly in the marketplace. The District compares internally calculated derivative valuations to broker/dealer quotes to substantiate the results.

Collateral liabilities are also considered Level 2. The majority of derivative contracts are supported by bilateral collateral agreements with counterparties requiring the posting of collateral in the event certain dollar thresholds of credit exposure are reached. Face value plus accrued interest approximates the fair value of collateral liabilities.

### **Level 3**

Level 3 inputs to the valuation methodology 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.

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

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

The District's non-agency ABS and CMO investment portfolios are also considered Level 3. The underlying loans for the ABSs are mortgage related. The underlying loans for the CMO securities are residential mortgages. Based on the currently illiquid marketplace for these investments and the lack of marketplace information available as inputs and assumptions to the valuation process, the District classified the non-agency ABS and CMO investment portfolios as Level 3 assets. Fair value estimates are obtained from third-party valuation services.

For other investments, fair value is estimated by discounting estimated future cash flows using prevailing rates for similar instruments at the measurement date.

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

Systemwide Debt Securities are not all traded in the secondary market and those that are traded may not have readily available quoted market prices. Therefore, the fair value of the instruments is estimated by calculating the discounted value of the expected future cash flows. The discount rates used are based on the sum of quoted market yields for the Treasury yield curve and an estimated yield-spread relationship between Systemwide Debt Securities and Treasury securities. An appropriate yield-spread is estimated, taking into consideration selling group member (banks and securities dealers) yield indications, observed new GSE debt security pricing, and pricing levels in the related U.S. Dollar (USD) interest rate swap market.

The following tables present the changes in Level 3 assets and liabilities measured at fair value on a recurring basis for the periods presented. Effective March 31, 2012, in tandem with the latest guidance on fair value measurement and disclosure and movement to available for sale classification, \$51.9 million of Mission Related Investments was transferred from Level 2 to Level 3 status. The District had no transfers of assets or liabilities into or out of Level 1 during the reporting period.

<i>(dollars in thousands)</i>	<b>Asset- Backed Securities</b>	<b>Non- Agency CMOs</b>	<b>Mission Related Investments</b>	<b>Standby Letters of Credit</b>
Balance at January 1, 2013	\$ 33,390	\$ 204,699	\$ 53,491	\$ 2,046
Total gains or (losses) realized/unrealized:				
Included in earnings	(28)	(1,705)	(292)	-
Included in other comprehensive income	7,457	11,407	(5,565)	-
Purchases	-	-	313	-
Issuances	-	-	-	-
Settlements	(3,865)	(34,808)	(2,475)	(416)
Transfers in and/or out of Level 3	-	-	-	-
Balance at September 30, 2013	<u>\$ 36,954</u>	<u>\$ 179,593</u>	<u>\$ 45,472</u>	<u>\$ 1,630</u>

<i>(dollars in thousands)</i>	Asset- Backed Securities	Non- Agency CMOs	Mission Related Investments	Standby Letters of Credit
Balance at January 1, 2012	\$ 30,324	\$ 241,756	\$ —	\$ 3,073
Total gains or (losses) realized/unrealized:				
Included in earnings	—	(3,167)	—	—
Included in other comprehensive income	8,971	4,505	2,003	—
Purchases	—	—	431	—
Sales	—	—	—	—
Issuances	—	—	—	—
Settlements	(7,232)	(30,993)	(232)	(807)
Transfers in and/or out of Level 3	—	—	51,885	—
Balance at September 30, 2012	\$ 32,063	\$ 212,101	\$ 54,087	\$ 2,266

## 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.

### Other Property Owned/Impaired Loans

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

### Inputs to Valuation Techniques

Management determines the 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
Firm commitments-when issued securities	\$ —	Broker/Consensus pricing	Offered quotes	None outstanding
Mission Related Investments	\$ 45,472	Discounted cash flow	Risk adjusted spread	0.01% – 99.61%
Non-agency securities	\$ 216,547	Vendor priced	**	
Impaired loans and other property owned	\$ 637,753	Appraisal	Income and expense Comparable sales Replacement cost Comparability adjustments	* * * *

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

\*\* The significant unobservable inputs used to estimate fair value for Level 3 assets and liabilities that are obtained from third party vendors are not included in the table as the specific inputs applied are not provided by the vendor.

#### 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 Loss severity Price for similar security
	Quoted prices Vendor priced	***
Federal funds sold, securities purchased under resale agreements and other	Carrying value	Par/principal and appropriate interest yield
Interest rate swaps	Discounted cash flow	Annualized volatility Counterparty credit risk Own credit risk

\*\*\* The inputs used to estimate fair value for assets and liabilities that are obtained from third party vendors are not included in the table as the specific inputs applied are not provided by the vendor.

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

	<b>Valuation Technique(s)</b>	<b>Input</b>
Loans	Discounted cash flow	Prepayment forecasts Probability of default Loss severity
Cash and cash equivalents	Carrying value	Par/principal and appropriate interest yield
Mission Related Investments	Discounted cash flow	Risk adjusted spread
Other investments	Discounted cash flow	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

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

**At or for the Nine Months Ended September 30, 2013**

<i>(dollars in thousands)</i>	<b>Total Carrying Amount</b>	<b>Level 1</b>	<b>Level 2</b>	<b>Level 3</b>	<b>Total Fair Value</b>	<b>Fair Value Effects On Earnings</b>
<b><u>Recurring Measurements</u></b>						
<b>Assets:</b>						
Investments available-for-sale:						
U.S. Govt. GNMA MBS/CMOs	\$ 4,562,739	\$ —	\$ 4,562,739	\$ —	\$ 4,562,739	
U.S. Govt. Agency MBS/CMOs	1,805,649	—	1,805,649	—	1,805,649	
Non-Agency CMOs	179,593	—	—	179,593	179,593	
Asset-backed securities	36,954	—	—	36,954	36,954	
Mission Related Investments	45,472	—	—	45,472	45,472	
Total investments available-for-sale	6,630,407	—	6,368,388	262,019	6,630,407	
Federal funds sold, securities purchased under resale agreements, and other	152,190	—	152,190	—	152,190	
Interest rate swaps and other derivative instruments	30,373	—	30,373	—	30,373	
Assets held in trust funds	15,503	15,503	—	—	15,503	
Recurring Assets	\$ 6,828,473	\$ 15,503	\$ 6,550,951	\$ 262,019	\$ 6,828,473	
<b>Liabilities:</b>						
Interest rate swaps and other derivative instruments	\$ —	\$ —	\$ —	\$ —	\$ —	
Collateral liabilities	—	—	—	—	—	
Standby letters of credit	1,630	—	—	1,630	1,630	
Recurring Liabilities	\$ 1,630	\$ —	\$ —	\$ 1,630	\$ 1,630	
<b><u>Nonrecurring Measurements</u></b>						
<b>Assets:</b>						
Impaired loans	\$ 536,949	\$ —	\$ —	\$ 536,949	\$ 536,949	\$ 430
Other property owned	91,367	—	—	100,804	100,804	(7,319)
Nonrecurring Assets	\$ 628,316	\$ —	\$ —	\$ 637,753	\$ 637,753	\$ (6,889)
<b><u>Other Financial Instruments</u></b>						
<b>Assets:</b>						
Cash	\$ 810,662	\$ 810,662	\$ —	\$ —	\$ 810,662	
Investments held to maturity	734,726	—	554,194	198,796	752,990	
Loans	22,375,388	—	—	21,736,604	21,736,604	
Other investments	82,374	—	—	83,624	83,624	
Other Assets	\$ 24,003,150	\$ 810,662	\$ 554,194	\$ 22,019,024	\$ 23,383,880	
<b>Liabilities:</b>						
Systemwide debt securities	\$ 26,182,932	\$ —	\$ —	\$ 25,998,550	\$ 25,998,550	
Other Liabilities	\$ 26,182,932	\$ —	\$ —	\$ 25,998,550	\$ 25,998,550	

	At or for the Year Ended December 31, 2012						
(dollars in thousands)	Total Carrying Amount	Level 1	Level 2	Level 3	Total Fair Value	Fair Value Effects On Earnings	
<b>Recurring Measurements</b>							
<b>Assets:</b>							
Investments available-for-sale:							
U.S. Govt. GNMA MBS/CMOs	\$ 5,000,613	\$ —	\$ 5,000,613	\$ —	\$ 5,000,613		
U.S. Govt. Agency MBS/CMOs	1,644,227	—	1,644,227	—	1,644,227		
Non-Agency CMOs	204,699	—	—	204,699	204,699		
Asset-backed securities	33,390	—	—	33,390	33,390		
Mission related securities	53,491	—	—	53,491	53,491		
Total investments available-for-sale	6,936,420	—	6,644,840	291,580	6,936,420		
Federal funds sold, securities purchased under resale agreements, and other	149,589	—	149,589	—	149,589		
Interest rate swaps and other derivative instruments	41,384	—	41,384	—	41,384		
Assets held in trust funds	14,562	14,562	—	—	14,562		
Recurring Assets	\$ 7,141,955	\$ 14,562	\$ 6,835,813	\$ 291,580	\$ 7,141,955		
<b>Liabilities:</b>							
Interest rate swaps and other derivative instruments	\$ —	\$ —	\$ —	\$ —	\$ —		
Collateral liabilities	—	—	—	—	—		
Standby letters of credit	2,046	—	—	2,046	2,046		
Recurring Liabilities	\$ 2,046	\$ —	\$ —	\$ 2,046	\$ 2,046		
<b>Nonrecurring Measurements</b>							
<b>Assets:</b>							
Impaired loans	\$ 595,898	\$ —	\$ —	\$ 595,898	\$ 595,898	\$ (86,423)	
Other property owned	109,997	—	—	119,851	119,851	(30,181)	
Nonrecurring Assets	\$ 705,895	\$ —	\$ —	\$ 715,749	\$ 715,749	\$ (116,604)	
<b>Other Financial Instruments</b>							
<b>Assets:</b>							
Cash	\$ 775,859	\$ 775,859	\$ —	\$ —	\$ 775,859		
Investments held to maturity	712,997	—	549,971	224,304	774,275		
Loans	22,137,939	—	—	22,409,374	22,409,374		
Other investments	163,178	—	—	166,557	166,557		
Other Assets	\$ 23,789,973	\$ 775,859	\$ 549,971	\$ 22,800,235	\$ 24,126,065		
<b>Liabilities:</b>							
Systemwide debt securities	\$ 26,488,875	\$ —	\$ —	\$ 26,578,330	\$ 26,578,330		
Other Liabilities	\$ 26,488,875	\$ —	\$ —	\$ 26,578,330	\$ 26,578,330		

## NOTE 5 — COMMITMENTS AND CONTINGENT LIABILITIES

Under the Farm Credit Act of 1971, each Farm Credit System (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 Allocation 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 Insurance Corporation 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 Farm Credit Administration 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 the aggregate of the banks’ 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 Farm Credit Administration is required to appoint the Insurance Corporation as the receiver for the defaulting bank. The receiver would be required to expeditiously liquidate the bank.

AgFirst did not anticipate making any payments on behalf of its co-obligors under the Joint and Several Liability Allocation Agreement for any of the periods presented.

<i>(dollars in billions)</i>	<b>9/30/2013</b>	<b>12/31/2012</b>
Total System bonds and notes	\$ 200.888	\$ 197.966
AgFirst bonds and notes	\$ 25.982	\$ 26.287

Legal actions are pending against the District in which claims for money damages are asserted. 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 combined financial position of AgFirst and District Associations.

#### **NOTE 6 — EMPLOYEE BENEFIT PLANS**

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

<i>(dollars in thousands)</i>	<b>For the three months ended September 30,</b>		<b>For the nine months ended September 30,</b>	
	<b>2013</b>	<b>2012</b>	<b>2013</b>	<b>2012</b>
Pension	\$ 12,390	\$ 11,797	\$ 37,170	\$ 35,392
401k	1,748	1,621	5,348	4,990
Other postretirement benefits	2,524	2,101	7,570	6,199
Total	\$ 16,662	\$ 15,519	\$ 50,088	\$ 46,581

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, 2012.

<i>(dollars in thousands)</i>	<b>Actual YTD Through 9/30/13</b>	<b>Projected Contributions for Remainder of 2013</b>	<b>Projected Total Contributions 2013</b>
Pensions	\$ 699	\$ 59,277	\$ 59,976
Other postretirement benefits	5,226	2,154	7,380
Total	\$ 5,925	\$ 61,431	\$ 67,356

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, 2013.

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

#### **NOTE 7 — 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 lower cost of funding or to reduce interest rate risk. 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 instrument used and the amount of activity for the periods presented is summarized in the following table:

Notional Amounts (dollars in millions)	For the Nine Months Ended September 30,			
	2013		2012	
	Receive- Fixed Swaps	Forward Contracts	Receive- Fixed Swaps	Forward Contracts
Balance at beginning of period	\$ 360	\$ —	\$ 535	\$ 66
Additions	—	—	—	542
Maturities/amortization	(50)	—	—	(493)
Terminations	—	—	—	—
Balance at end of period	\$ 310	\$ —	\$ 535	\$ 115

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. The District does not anticipate nonperformance by any of these counterparties. A number of swaps are supported by collateral arrangements with counterparties. Accounting guidance requires a pledgee to reflect as a liability the value of any cash collateral held in its statement of condition. However, securities held as collateral are not reported in the pledgee's statement of condition, even though in the custody of the pledgee.

At September 30, 2013, the District had not posted collateral with respect to any of these arrangements.

Counterparty exposure related to derivatives at:

(dollars in millions)	September 30, 2013	December 31, 2012
Estimated Gross Credit Risk	\$30.4	\$41.4
Percent of Notional	9.80%	11.50%
Cash Collateral Held (on balance sheet)	\$—	\$—
Securities Collateral Held (off balance sheet)	\$10.5	\$19.6

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 Bank 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 nine months ended September 30, 2013 was \$11.0 million, while the amount of the gain on the Systemwide Debt Securities was \$11.0 million. The amount of the loss on interest rate swaps recognized in interest expense for the nine months ended September 30, 2012 was \$4.8 million, while the amount of the gain on the Systemwide Debt Securities was \$4.8 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 Other Comprehensive Income (OCI), and Other Liabilities or Other Assets as appropriate, as firm commitments in the District's Balance Sheet for each period end. At September 30, 2013 and December 31, 2012, 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 for the periods presented:

<i>(dollars in thousands)</i>	Balance Sheet Classification – Assets	9/30/13 Fair Value	Balance Sheet Classification - Liabilities	9/30/13 Fair Value
<b>Derivatives designated as hedging instruments:</b>				
Receive-fixed swaps	Other Assets	\$ 30,373	Other Liabilities	\$ –
Forward contracts	Other Assets	–	Other Liabilities	–
Total		\$ 30,373		\$ –

<i>(dollars in thousands)</i>	Balance Sheet Classification - Assets	12/31/12 Fair Value	Balance Sheet Classification – Liabilities	12/31/12 Fair Value
<b>Derivatives designated as hedging instruments:</b>				
Receive-fixed swaps	Other Assets	\$ 41,384	Other Liabilities	\$ –
Forward contracts	Other Assets	–	Other Liabilities	–
Total		\$ 41,384		\$ –

The following tables set forth the amount of net gain (loss) recognized in the Statements of Income and, for cash flow hedges, the amount of net gain (loss) recognized in the Balance Sheets for the periods presented.

	Location of Gain or (Loss) Recognized in the Statements of Income	Amount of Gain or (Loss) Recognized in the Statements of Income	
		2013	2012
<i>(dollars in thousands)</i>			
<b>Derivatives – Fair Value</b>			
<b>Hedging Relationships:</b>			
Receive-fixed swaps	Noninterest Income	\$ –	\$ –

	Amount of Gain or (Loss) Recognized in OCI on Derivative (Effective Portion)		Location of Gain or (Loss) Reclassified from AOCI into Income (Effective Portion)		Amount of Gain or (Loss) Reclassified from AOCI into Income (Effective Portion)		Location of Gain or (Loss) Recognized in Income on Derivative (Ineffective Portion and Amount Excluded from Effectiveness Testing)		Amount of Gain or (Loss) Recognized in Income on Derivative (Ineffective Portion and Amount Excluded from Effectiveness Testing)	
	2013	2012	2013	2012	2013	2012	2013	2012	2013	2012
<i>(dollars in thousands)</i>										
<b>Derivatives – Cash Flow</b>										
<b>Hedging Relationships:</b>										
Firm Commitments	\$ –	\$ 7,864	Interest Income	\$ 943	\$ 480	Interest Income	\$ –	\$ –	\$ –	\$ –

#### NOTE 8 — 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.

On May 15, 2013, the Bank redeemed and cancelled the entire \$150.0 million of Perpetual Non-cumulative Preferred Stock issued October 14, 2003. The stock was redeemed at its par value together with accrued and unpaid dividends.

During 2012, the Bank repurchased, through privately negotiated transactions, and cancelled Class B Perpetual Non-Cumulative Fixed-to-Floating Rate Subordinated Preferred Stock with a par value of \$124.8 million. The effect of the repurchases on shareholders' equity was to reduce preferred stock outstanding by \$124.8 million and record \$36.6 million of additional paid-in-capital. See additional information about this preferred stock issuance in the 2012 Annual Report to Shareholders.

**NOTE 9 — ACCUMULATED OTHER COMPREHENSIVE INCOME**

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

<i>(dollars in thousands)</i>	<b>Changes in Accumulated Other Comprehensive Income by Component (a)</b>			
	<b>Three Months</b>		<b>Year to Date</b>	
	<b>2013</b>	<b>2012</b>	<b>2013</b>	<b>2012</b>
<b>Unrealized Gains (Losses) on Investments:</b>				
Balance at beginning of period	\$ 124,629	\$ 153,795	\$ 180,394	\$ 139,367
Other comprehensive income before reclassifications	(32,426)	46,613	(82,962)	57,861
Amounts reclassified from AOCI	(109)	158	(5,338)	3,338
Net current period other comprehensive income	(32,535)	46,771	(88,300)	61,199
Balance at end of period	<u>\$ 92,094</u>	<u>\$ 200,566</u>	<u>\$ 92,094</u>	<u>\$ 200,566</u>
<b>Firm Commitments:</b>				
Balance at beginning of period	\$ 813	\$ (4,356)	\$ 1,514	\$ (5,566)
Other comprehensive income before reclassifications	—	6,355	—	7,864
Amounts reclassified from AOCI	(242)	(181)	(943)	(480)
Net current period other comprehensive income	(242)	6,174	(943)	7,384
Balance at end of period	<u>\$ 571</u>	<u>\$ 1,818</u>	<u>\$ 571</u>	<u>\$ 1,818</u>
<b>Employee Benefit Plans:</b>				
Balance at beginning of period	\$ (379,065)	\$ (340,538)	\$ (395,410)	\$ (355,049)
Other comprehensive income before reclassifications	—	(4,454)	—	—
Amounts reclassified from AOCI	8,173	10,845	24,518	20,902
Net current period other comprehensive income	8,173	6,391	24,518	20,902
Balance at end of period	<u>\$ (370,892)</u>	<u>\$ (334,147)</u>	<u>\$ (370,892)</u>	<u>\$ (334,147)</u>
<b>Total Accumulated Other Comprehensive Income:</b>				
Balance at beginning of period	\$ (253,623)	\$ (191,099)	\$ (213,502)	\$ (221,248)
Other comprehensive income before reclassifications	(32,426)	48,514	(82,962)	65,725
Amounts reclassified from AOCI	7,822	10,822	18,237	23,760
Net current period other comprehensive income	(24,604)	59,336	(64,725)	89,485
Balance at end of period	<u>\$ (278,227)</u>	<u>\$ (131,763)</u>	<u>\$ (278,227)</u>	<u>\$ (131,763)</u>

<i>(dollars in thousands)</i>	<b>Reclassifications Out of Accumulated Other Comprehensive Income (b)</b>				
	<b>Three Months</b>		<b>Year to Date</b>		<b>Income Statement Line Item</b>
	<b>2013</b>	<b>2012</b>	<b>2013</b>	<b>2012</b>	
<b>Investment Securities:</b>					
Sales gains & losses	\$ —	\$ —	\$ 7,592	\$ —	Gains (losses) on investments, net
Holding gains & losses	109	(158)	(2,254)	(3,338)	Net other-than-temporary impairment
Net amounts reclassified	<u>109</u>	<u>(158)</u>	<u>5,338</u>	<u>(3,338)</u>	
<b>Cash Flow Hedges:</b>					
Interest income	242	181	943	480	See footnote 7.
Net amounts reclassified	<u>242</u>	<u>181</u>	<u>943</u>	<u>480</u>	
<b>Defined Benefit Pension Plans:</b>					
Periodic pension costs	(8,173)	(10,845)	(24,518)	(20,902)	See footnote 6.
Net amounts reclassified	<u>(8,173)</u>	<u>(10,845)</u>	<u>(24,518)</u>	<u>(20,902)</u>	
Total reclassifications for period	<u>\$ (7,822)</u>	<u>\$ (10,822)</u>	<u>\$ (18,237)</u>	<u>\$ (23,760)</u>	

(a) Amounts in parentheses indicate debits to AOCI.

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

**NOTE 10 — OFFSETTING OF FINANCIAL AND DERIVATIVE ASSETS**

September 30, 2013						
Gross Amounts Not Offset in the Balance Sheets						
(dollars in thousands)	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	\$ 30,373	\$ —	\$ 30,373	\$ (10,518)	\$ —	\$ 19,855
Reverse repurchase and similar arrangements	152,190	—	152,190	(152,190)	—	—
<b>Total</b>	<b>\$ 182,563</b>	<b>\$ —</b>	<b>\$ 182,563</b>	<b>\$ (162,708)</b>	<b>\$ —</b>	<b>\$ 19,855</b>

December 31, 2012						
Gross Amounts Not Offset in the Balance Sheets						
(dollars in thousands)	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	\$ 41,384	\$ —	\$ 41,384	\$ (19,551)	\$ —	\$ 21,833
Reverse repurchase and similar arrangements	149,589	—	149,589	(149,589)	—	—
<b>Total</b>	<b>\$ 190,973</b>	<b>\$ —</b>	<b>\$ 190,973</b>	<b>\$ (169,140)</b>	<b>\$ —</b>	<b>\$ 21,833</b>

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 7, *Derivative Financial Instruments and Hedging Activities*.

The reverse repurchase agreements are accounted for as collateralized lending.

**NOTE 11 — 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 by the 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.

Each issuance of Systemwide Debt Securities ranks equally, in accordance with the FCA regulations, 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.

**NOTE 12 — BANK ONLY FINANCIAL DATA**

Condensed financial information of AgFirst Farm Credit Bank follows:

<b>Balance Sheets Data</b>		
<i>(dollars in thousands)</i>	<b>September 30, 2013</b>	<b>December 31, 2012</b>
	<i>(unaudited)</i>	<i>(audited)</i>
Cash, cash equivalents and investment securities	\$ 8,145,255	\$ 8,357,576
Loans	20,060,519	20,209,251
Allowance for loan losses	(27,324)	(44,539)
Net loans	20,033,195	20,164,712
Other assets	330,065	368,259
Total assets	\$ 28,508,515	\$ 28,890,547
Bonds and notes	\$ 25,981,533	\$ 26,286,758
Other liabilities	131,342	305,559
Total liabilities	26,112,875	26,592,317
Perpetual preferred stock	125,250	275,250
Capital stock and participation certificates	329,419	332,705
Additional paid-in-capital	36,580	36,580
Retained earnings	1,816,322	1,482,227
Accumulated other comprehensive income (loss)	88,069	171,468
Total shareholders' equity	2,395,640	2,298,230
Total liabilities and equity	\$ 28,508,515	\$ 28,890,547

<b>Statements of Income Data</b>		
<i>(dollars in thousands)</i>	<b>For the nine months ended September 30,</b>	
	<b>2013</b>	<b>2012</b>
	<i>(unaudited)</i>	
Interest income	\$ 551,978	\$ 619,611
Interest expense	143,517	161,260
Net interest income	408,461	458,351
Provision for (reversal of) loan losses	(7,212)	10,943
Net interest income after provision for loan losses	415,673	447,408
Noninterest expense, net	65,589	89,798
Net income	\$ 350,084	\$ 357,610

**NOTE 13 — REGULATORY ENFORCEMENT MATTERS**

At September 30, 2013, the FCA had entered into written supervisory agreements with five District Associations having combined assets of approximately \$3.705 billion. 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 adverse impact on the District's financial condition or results of operations.

**NOTE 14 — DISTRICT MERGER ACTIVITY**

Effective July 1, 2012, Chattanooga, ACA, merged with and into Jackson Purchase, ACA. Jackson Purchase, ACA, then changed its name to River Valley AgCredit, ACA.

Mergers are accounted for under the acquisition method. The accounting acquirer accounts for the transaction by using its historical information and accounting policies and adding the identifiable assets and liabilities of the acquiree as of the acquisition date at their respective fair values.

As cooperative organizations, Farm Credit Associations operate for the mutual benefit of their borrowers and other customers, and not for the benefit of equity investors. As such, their capital stock provides no significant interest in corporate earnings or growth. Specifically, due to restrictions in applicable regulations and the bylaws, the Associations can issue stock only at its par value of \$5 per share, the stock is not tradable, and the stock can be retired only for the lesser of par value or book value. In these and other respects, the shares of the acquiree's stock that were converted in the merger and the shares of the acquirer's stock to which they were converted had identical rights and attributes. For this reason, the conversion of stock pursuant to the mergers occurred at a one-for-one exchange ratio (i.e., each acquiree's share was converted into one share of the acquirer's stock with an equal par value).

Management believes that because the stock in each Association is fixed in value (although subject to impairment), the Association's stock issued pursuant to the merger provides no basis for estimating the fair value of the consideration transferred pursuant to the merger. In the absence of a purchase price determination, the Association identified and estimated the acquisition date fair value of the acquiree's equity interests instead of the fair value of the acquirer's equity interests transferred as consideration. The fair value of the assets acquired, including specific intangible assets and liabilities assumed from the acquiree, was measured based on various estimates using assumptions that the Association's management believes are reasonable utilizing information currently available. Use of different estimates and judgments could yield materially different results. This evaluation produced a fair value of identifiable assets acquired and liabilities assumed that was substantially equal to the fair value of the member interests transferred in the merger. As a result, management recorded no goodwill.

The following table reflects the fair values of the identifiable assets acquired and liabilities assumed from Chattanooga, the acquisition adjustment and the merged entity balances at July 1, 2012:

<b>Consolidation of Assets Acquired and Liabilities Assumed at July 1, 2012</b>					
<i>(dollars in thousands)</i>	<b>Chattanooga</b>	<b>Acquisition Adjustment</b>	<b>Acquisition Values</b>	<b>Jackson Purchase</b>	<b>River Valley</b>
<b>Assets</b>					
Cash	\$ 197	\$ —	\$ 197	\$ 958	\$ 1,155
Investment securities:					
Held to maturity	—	—	—	1,793	1,793
Loans held for sale	—	—	—	139	139
Loans	156,489	(469)	156,020	270,479	426,499
Less: allowance for loan losses	(1,409)	1,409	—	(2,714)	(2,714)
Net loans	155,080	940	156,020	267,765	423,785
Other investments	38	2	40	1,180	1,220
Accrued interest receivable	1,147	—	1,147	2,876	4,023
Investments in other Farm Credit institutions	5,985	—	5,985	5,280	11,265
Premises and equipment, net	709	1,515	2,224	2,708	4,932
Other property owned	4,382	—	4,382	165	4,547
Due from AgFirst Farm Credit Bank	647	(57)	590	1,175	1,765
Other assets	145	—	145	719	864
Total assets	\$ 168,330	\$ 2,400	\$ 170,730	\$ 284,758	\$ 455,488
<b>Liabilities</b>					
Notes payable to AgFirst Farm Credit Bank	\$ 135,322	\$ 952	\$ 136,274	\$ 226,887	\$ 363,161
Subordinated debt payable to other Farm Credit Institutions	2,500	140	2,640	—	2,640
Accrued interest payable	330	—	330	471	801
Patronage refund payable	62	—	62	20	82
Advanced conditional payments	—	—	—	5,894	5,894
Other liabilities	1,981	—	1,981	3,397	5,378
Total liabilities	140,195	1,092	141,287	236,669	377,956
Commitments and contingencies					
<b>Members' Equity</b>					
Capital stock and participation certificates	3,163	—	3,163	2,061	5,224
Additional paid in capital	—	15,817	15,817	—	15,817
Retained earnings					
Allocated	10,463	—	10,463	20,218	30,681
Unallocated	14,509	(14,509)	—	25,810	25,810
Total members' equity	28,135	1,308	29,443	48,089	77,532
Total liabilities and members' equity	\$ 168,330	\$ 2,400	\$ 170,730	\$ 284,758	\$ 455,488

Effective January 1, 2011, Farm Credit of North Florida, ACA, and Farm Credit of Southwest Florida, ACA, merged with and into Farm Credit of South Florida, ACA. Farm Credit of South Florida then changed its name to Farm Credit of Florida, ACA. As part of the merger, those Associations entered into an agreement with the Bank under which the Bank would provide limited financial assistance to the merged Association in the event of substantial further deterioration in the combined high risk asset portfolio of the merged Association. This agreement relates only to a finite pool of high risk assets of the merged Association existing at the merger date, which had a net book value at January 1, 2011 of \$250.0 million. At September 30, 2013, those assets had a net book value of \$84.2 million. This agreement with the Bank does not include losses that are sustained outside of the high risk asset pool. Protection to the Bank, such as limitations on the Association's ability to make patronage distributions and certain other restrictions, is provided in the agreement if certain merged Association capital ratios fail to meet minimum established levels.

Under the financial assistance agreement, if specified minimum levels of capital allocated to the high risk asset pool are not maintained by the merged Association, the Bank would provide financial assistance as stipulated in the agreement. The assistance consists of three components. First, AgFirst would allow the Association to include AgFirst allocated stock owned by the merged Association in its capital ratio computations. This allocated stock, which totals \$10.1 million, has been counted entirely by the Bank in its capital ratio computations under an existing capital sharing arrangement. Second, AgFirst would redeem purchased stock held by the merged Association, up to the total amount outstanding, which was \$1.3 million at December 31, 2012, and the redeemed amount would be included in capital ratio computations by the merged Association. This purchased stock has been counted entirely by the Bank in its capital ratio computations under an existing capital sharing arrangement. The third and final level of assistance, if elected by the Association, would be a purchase by AgFirst of the high risk asset pool from the Association at net book value. There would also be a corresponding repurchase by the merged Association of its previously redeemed stock in AgFirst and a return to the capital sharing arrangement allowing the Bank to count the allocated stock in its capital ratio computations in amounts necessary to satisfy the capitalization requirement under AgFirst's capitalization plan then in effect.

At December 31, 2012, capital allocated to the high risk asset pool failed to meet specified minimum levels due to losses in the pool from resolution efforts, provisions, and write-downs subsequent to the merger date. This resulted in the Bank providing assistance under the agreement by allowing the merged Association to include in its capital ratio computations \$3.3 million of the total \$10.1 million of AgFirst allocated stock owned by the merged Association. At September 30, 2013, the amount of assistance increased to \$7.2 million of allocated stock.

The high risk asset pool may continue to experience additional losses. Assistance provided under the agreement did not have a material impact on the financial condition and results of operations of the Bank or District at September 30, 2013 and additional assistance in the future likely would not have a material adverse impact on either the financial condition or future operating results of the Bank or District.

Disclosures related to acquired impaired loans are contained in Note 3, *Loans and Allowance for Loan Losses*.

The acquisition method of accounting requires the financial statement presentation of combined balances as of the date of the merger, but of only the acquirer for previous periods.

#### **NOTE 15 — SUBSEQUENT EVENTS**

The District has evaluated subsequent events and has determined that, except as described below, there are none requiring disclosure through November 8, 2013, which is the date the financial statements were issued.

On October 21, 2013, the Bank's Board of Directors declared a special cash patronage distribution totaling \$200.0 million to be paid primarily to District Associations on January 1, 2014.