

ALABAMA AG CREDIT, ACA

**2019
Quarterly Report
Third Quarter**



For the Quarter Ended September 30, 2019

REPORT OF MANAGEMENT

The consolidated financial statements of Alabama Ag Credit, ACA (Association) are prepared by management, who are responsible for the statements' integrity and objectivity, including amounts that must necessarily be based on judgments and estimates. The consolidated financial statements have been prepared in conformity with accounting principles generally accepted in the United States of America appropriate in the circumstances. Other financial information included in the quarterly report is consistent with that in the consolidated financial statements.

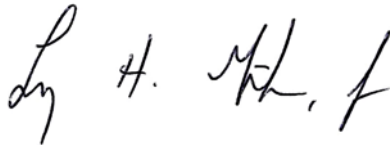
To meet its responsibility for reliable financial information, management depends on the Farm Credit Bank of Texas' (Bank) and the Association's accounting and internal control systems, which have been designed to provide reasonable, but not absolute, assurance that assets are safeguarded and transactions are properly authorized and recorded. The systems have been designed to recognize that the cost of controls must be related to the benefits derived. The annual financial statements are audited by PricewaterhouseCoopers LLP, independent accountants, who conduct a review of internal controls solely for the purpose of establishing a basis for reliance thereon in determining the nature, extent and timing of audit tests applied in the audit of the financial statements in accordance with auditing standards generally accepted in the United States of America. The Association is also examined by the Farm Credit Administration.

The audit committee of the board of directors has oversight responsibility for the Association's system of internal controls and financial reporting. The audit committee consults regularly with management and meets periodically with the independent auditors and the internal auditor to review the scope and results of their work. The independent auditors and internal auditor have direct access to the audit committee.

The undersigned certify that, to the best of our knowledge and belief, the consolidated financial statements and other financial information included in this quarterly report reliably present the financial condition of Alabama Ag Credit, ACA and the results of its operations for the periods shown.



Douglas Thiessen, President/Chief Executive Officer
November 4, 2019



Larry H. Gibson, Jr., Chairman, Board of Directors
November 4, 2019



M. Scott Sellers, CPA, Sr. VP/Chief Financial Officer
November 4, 2019



J.K. Love, CPA (retired), Chairman, Audit Committee
November 4, 2019

**ASSOCIATION NEW MODEL
MANAGEMENT'S DISCUSSION AND ANALYSIS**

The following commentary reviews the financial performance of the Alabama Ag Credit, ACA (Agricultural Credit Association), referred to as the Association, for the quarter and nine months ended September 30, 2019. These comments should be read in conjunction with the accompanying financial statements and the December 31, 2018 Annual Report to Stockholders.

The Association is a member of the Farm Credit System (System), a nationwide network of cooperatively owned financial institutions established by and subject to the provisions of the Farm Credit Act of 1971, as amended, and the regulations of the Farm Credit Administration (FCA) promulgated thereunder.

The consolidated financial statements comprise the operations of the ACA and its wholly-owned subsidiaries. The consolidated financial statements were prepared under the oversight of the Association's audit committee.

Results of Operations

The Association had net income of \$4,146,302 and \$12,631,643 for the three and nine months ended September 30, 2019, as compared to net income of \$3,792,954 and \$12,743,698 for the same period in 2018, reflecting an increase of 9.3 percent and a decrease of 0.9 percent, respectively. Net interest income was \$7,113,525 and \$21,335,756 for the three and nine months ended September 30, 2019, compared to \$6,928,962 and \$20,734,221 for the same period in 2018.

	Nine Months Ended			
	September 30, 2019		September 30, 2018	
	Average Balance	Interest	Average Balance	Interest
Loans	\$ 1,037,438,126	\$ 41,362,782	\$ 974,721,001	\$ 36,934,903
Interest-bearing liabilities	867,469,144	20,027,026	814,513,874	16,200,682
Impact of capital	\$ 169,968,982		\$ 160,207,127	
Net interest income		\$ 21,335,756		\$ 20,734,221
	2019		2018	
	Average Yield		Average Yield	
Yield on loans	5.33%		5.07%	
Cost of interest-bearing liabilities	3.09%		2.66%	
Interest rate spread	2.24%		2.41%	
Impact of capital	0.51%		0.44%	
Net interest income as a percentage of average earning assets	2.75%		2.85%	

	Nine months ended:		
	September 30, 2019 vs. September 30, 2018		
	Increase (decrease) due to		
	Volume	Rate	Total
Interest income - loans	\$ 2,376,549	\$ 2,051,330	\$ 4,427,879
Interest expense	1,053,286	2,773,058	3,826,344
Net interest income	\$ 1,323,263	\$ (721,728)	\$ 601,535

Interest income for the three and nine months ended September 30, 2019, increased by \$1,275,188 and \$4,427,879, or 10.0 and 12.0 percent respectively, from the same period of 2018, primarily due to increases in yields on earning assets and an increase in average loan volume. Interest expense for the three and nine months ended September 30, 2019, increased by \$1,090,625 and \$3,826,344, or 18.7 and 23.6 percent, from the same period of 2018 due to an increase in average debt volume and an increase in the cost of debt. Average loan volume for the third quarter of 2019 was \$1,057,724,423, compared to \$989,699,953 in the third quarter of 2018.

Noninterest income for the three months ended September 30, 2019, increased by \$11,125, or 2.3 percent, over the same period of 2018. The increase is due primarily to an increase in net loan fees in 2019 compared to 2018. In addition, the Association recognized

gains on sales of premises and equipment in 2019 as compared to a loss in 2018. Noninterest income for the nine months ended September 30, 2019, decreased by \$190,445, or 9.9 percent, over the same period of 2018. The decrease is due primarily to Insurance Fund refunds from the Farm Credit System Insurance Corporation (FCSIC) that were received in the first quarter of 2019 and 2018. The 2018 refund was significantly larger than the 2019 refund.

Noninterest expenses for the three months ended September 30, 2019 increased by \$173,751, or 5.5 percent, as compared to the same period in 2018. The increase is primarily due to increases in salaries and benefits. The increase in salaries and benefits is primarily due to a larger workforce and normal increase in compensation rates. Noninterest expenses for the nine months ended September 30, 2019 increased by \$561,790, or 5.9 percent, as compared to the same period in 2018. The increase is primarily due to increases in salaries and benefits. The increase in salaries and benefits is primarily due to a larger workforce and normal increase in compensation rates.

The Association's return on average assets for the nine months ended September 30, 2019, was 1.58 percent compared to 1.70 percent for the same period in 2018. The Association's return on average equity for the nine months ended September 30, 2019, was 8.96 percent, compared to 9.58 percent for the same period in 2018.

Loan Portfolio

The Association makes and services loans to farmers, ranchers, rural homeowners and certain farm-related businesses. The Association's loan volume consists of long-term farm mortgage loans, production and intermediate-term loans, and farm-related business loans. These loans are available to eligible borrowers with competitive prime- and LIBOR-based, fixed and adjustable interest rates and loan maturities ranging up to 40 years. Loans serviced by the Association offer several installment payment cycles, the timing of which usually coincides with seasonal cash-flow capabilities of the borrower.

Total loans outstanding at September 30, 2019, stated at recorded investment (principal less funds held), were \$1,069,554,047 compared to \$997,421,512 at December 31, 2018, reflecting an increase of 7.2 percent. Nonaccrual loans as a percentage of total loans outstanding were 0.8 percent at September 30, 2019 and 0.3 percent at December 31, 2018. The major commodities within the Association's portfolio are timber, poultry, cattle and field crops.

The Association recorded \$19,361 in recoveries and \$6,722 in charge-offs for the quarter ended September 30, 2019 compared to \$38,989 in recoveries and no charge-offs for the same period in 2018. The Association's allowance for loan losses was 0.7 percent of total loans outstanding as of September 30, 2019, and December 31, 2018.

The following table reflects the credit quality of the Association's loan volume as of:

	<u>September 30, 2019</u>		<u>December 31, 2018</u>	
Acceptable	97.0	%	98.1	%
OAEM	1.5		1.0	
Substandard/doubtful	1.5		0.9	
	<u>100.0</u>	%	<u>100.0</u>	%

Risk Exposure

High-risk assets include nonaccrual loans, loans that are past due 90 days or more and still accruing interest, formally restructured loans and other property owned. The following table illustrates the Association's components and trends of high-risk assets.

	<u>September 30, 2019</u>		<u>December 31, 2018</u>	
	Amount	%	Amount	%
Nonaccrual	\$ 8,181,205	85.8%	\$ 2,597,848	64.0%
90 days past due and still accruing interest	-	0.0%	983	0.0%
Formally restructured	1,215,923	12.8%	1,415,001	34.9%
Other property owned, net	133,200	1.4%	45,040	1.1%
Total	<u>\$ 9,530,328</u>	<u>100.0%</u>	<u>\$ 4,058,872</u>	<u>100.0%</u>

Liquidity and Funding Sources

The Association secures the majority of its lendable funds from the Farm Credit Bank of Texas (the Bank), which obtains its funds through the issuance of System-wide obligations. The following schedule summarizes the Association's borrowings.

	September 30, 2019	December 31, 2018
Note payable to the bank	\$ 897,782,763	\$ 825,552,682
Accrued interest on note payable	2,245,705	2,085,861
Total	<u>\$ 900,028,468</u>	<u>\$ 827,638,543</u>

The Association operates under a general financing agreement (GFA) with the Bank. The current GFA is effective through September 30, 2020. The primary source of liquidity and funding for the Association is a direct loan from the Bank. The outstanding balance of \$897,782,763 as of September 30, 2019, is recorded as a liability on the Association's balance sheet. The note carried a weighted average interest rate of 3.01 percent at September 30, 2019. The indebtedness is collateralized by a pledge of substantially all of the Association's assets to the Bank and is governed by the GFA. The increase in note payable to the Bank and related accrued interest payable since December 31, 2018, is due to increased funding needs generated by growth in the Association's loan portfolio. The Association's own funds, which represent the amount of the Association's loan portfolio funded by the Association's equity, were \$172,179,448 at September 30, 2019. The maximum amount the Association may borrow from the Bank as of September 30, 2019, was \$1,076,545,805 as defined by the GFA. The indebtedness continues in effect until the expiration date of the GFA, unless sooner terminated by the Bank upon the occurrence of an event of default, or by the Association, in the event of a breach of this agreement by the Bank, upon giving the Bank 30 calendar days' prior written notice, or in all other circumstances, upon giving the Bank 120 days' prior written notice.

Capital Resources

The Association's capital position increased by \$12,677,815 at September 30, 2019, compared to December 31, 2018. The Association's debt as a ratio of members' equity was 4.66:1 as of September 30, 2019, compared to 4.64:1 as of December 31, 2018.

FCA regulations require the Association to maintain minimums for various regulatory capital ratios. New regulations became effective January 1, 2017, which replaced the previously required core surplus and total surplus ratios with common equity tier 1, tier 1 capital, and total capital risk-based capital ratios. The new regulations also added tier 1 leverage and unallocated retained earnings and equivalents (UREE) ratios. The permanent capital ratio continues to remain in effect, with some modifications to align with the new regulations. As of September 30, 2019, the Association exceeded all regulatory capital requirements.

Significant Recent Accounting Pronouncements

Information regarding significant recent accounting pronouncements, required to be disclosed, is incorporated herein by reference to Note 1 to the consolidated financial statements, "Organization and Significant Accounting Policies," included in this quarterly report.

Relationship With the Farm Credit Bank of Texas

The Association's financial condition may be impacted by factors that affect the Bank. The financial condition and results of operations of the Bank may materially affect the stockholder's investment in the Association. The Management's Discussion and Analysis and Notes to Financial Statements contained in the 2018 Annual Report of Alabama Ag Credit, ACA more fully describe the Association's relationship with the Bank.

The Bank's annual and quarterly stockholder reports are available free of charge, upon request. These reports can be obtained by writing to Farm Credit Bank of Texas, Corporate Communications, P.O. Box 202590, Austin, Texas 78720, or by calling (512) 483-9260. The annual and quarterly stockholder reports for the Bank are also available on its website at www.farmcreditbank.com.

The Association's annual and quarterly stockholder reports are also available free of charge, upon request. The quarterly reports will be available on the Association's website at www.AlabamaAgCredit.com approximately 40 days after quarter end and can also be obtained by writing to Alabama Ag Credit, ACA, 2660 EastChase Lane, Suite 401, Montgomery, Alabama, 36117 or calling (334) 270-8687. Copies of the Association's quarterly stockholder reports can also be requested by e-mailing Info@AlabamaAgCredit.com. The Association's annual stockholder report is available on its website 75 days after the fiscal year end. Copies of the Association's annual stockholder report can also be requested 90 days after the fiscal year end.

ALABAMA AG CREDIT, ACA

CONSOLIDATED BALANCE SHEET

	September 30, 2019 (unaudited)	December 31, 2018
<u>ASSETS</u>		
Cash	\$ 11,822	\$ 10,000
Loans	1,069,554,047	997,421,512
Less: allowance for loan losses	7,628,931	7,359,122
Net loans	1,061,925,116	990,062,390
Accrued interest receivable	11,998,095	9,827,877
Investment in and receivable from the Bank:		
Capital stock	16,322,640	16,322,640
Accrued patronage receivable	702,000	228,574
Other	2,405,709	1,474,469
Other property owned, net	133,200	45,040
Premises and equipment, net	6,347,565	6,439,711
Other assets	1,119,936	509,846
Total assets	\$ 1,100,966,083	\$ 1,024,920,547
<u>LIABILITIES</u>		
Note payable to the Bank	\$ 897,782,763	\$ 825,552,682
Accrued interest payable	2,245,705	2,085,861
Drafts outstanding	823,928	229,909
Patronage distributions payable	92	9,129,719
Other liabilities	5,555,268	6,041,864
Total liabilities	906,407,756	843,040,035
<u>MEMBERS' EQUITY</u>		
Capital stock and participation certificates	4,175,495	4,114,255
Unallocated retained earnings	190,378,019	177,746,279
Accumulated other comprehensive income (loss)	4,813	19,978
Total members' equity	194,558,327	181,880,512
Total liabilities and members' equity	\$ 1,100,966,083	\$ 1,024,920,547

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

ALABAMA AG CREDIT, ACA

CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME

(unaudited)

	Quarter Ended September 30,		Nine Months Ended September 30,	
	2019	2018	2019	2018
<u>INTEREST INCOME</u>				
Loans	\$ 14,032,750	\$ 12,757,562	\$ 41,362,782	\$ 36,934,903
<u>INTEREST EXPENSE</u>				
Note payable to the Bank	6,919,225	5,828,600	20,027,026	16,200,682
Net interest income	7,113,525	6,928,962	21,335,756	20,734,221
<u>PROVISION FOR LOAN LOSSES</u>				
Provision for loan losses	118,263	449,674	298,838	337,483
Net interest income after	6,995,262	6,479,288	21,036,918	20,396,738
<u>NONINTEREST INCOME</u>				
Patronage income from the Bank	359,930	413,976	1,076,500	1,061,214
Loan fees	99,560	66,190	298,120	227,785
Gain (loss) on sale of premises and equipment, net	31,799	(110)	117,889	70,575
Other noninterest income	556	664	246,525	569,905
Total noninterest income	491,845	480,720	1,739,034	1,929,479
<u>NONINTEREST EXPENSES</u>				
Salaries and employee benefits	2,115,385	1,948,668	6,285,196	5,959,038
Directors' expense	78,716	31,242	256,451	208,981
Purchased services	159,198	141,097	339,219	321,976
Travel	209,924	224,263	579,818	582,429
Occupancy and equipment	171,585	186,986	579,666	548,734
Communications	71,288	68,672	217,437	209,171
Advertising	49,396	69,334	195,687	212,643
Public and member relations	74,471	94,226	323,087	310,731
Supervisory and exam expense	95,238	90,156	275,551	249,292
Insurance Fund premiums	184,063	169,845	690,029	644,337
Other components of net periodic postretirement benefit cost	24,320	33,358	72,960	100,072
Loss on other property owned, net	24,150	35,425	77,948	37,057
Other noninterest expense	83,071	73,782	251,260	198,058
Total noninterest expenses	3,340,805	3,167,054	10,144,309	9,582,519
NET INCOME	4,146,302	3,792,954	12,631,643	12,743,698
Other comprehensive (loss) income:				
Change in postretirement benefit plans	(5,055)	3,894	(15,165)	11,682
COMPREHENSIVE INCOME	\$ 4,141,247	\$ 3,796,848	\$ 12,616,478	\$ 12,755,380

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

ALABAMA AG CREDIT, ACA

CONSOLIDATED STATEMENT OF CHANGES IN MEMBERS' EQUITY

(unaudited)

	<u>Capital Stock/ Participation Certificates</u>	<u>Unallocated Retained Earnings</u>	<u>Accumulated Other Comprehensive Income (Loss)</u>	<u>Total Members' Equity</u>
Balance at December 31, 2017	\$ 4,004,710	\$ 167,430,087	\$ (582,234)	\$ 170,852,563
Net income	-	12,743,698	-	12,743,698
Other comprehensive income	-	-	11,682	11,682
Capital stock/participation certificates issued	419,195	-	-	419,195
Capital stock/participation certificates retired	(337,025)	-	-	(337,025)
Patronage refunds:				
Change in patronage declared and paid	-	(1,395)	-	(1,395)
Balance at September 30, 2018	<u>\$ 4,086,880</u>	<u>\$ 180,172,390</u>	<u>\$ (570,552)</u>	<u>\$ 183,688,718</u>
Balance at December 31, 2018	\$ 4,114,255	\$ 177,746,279	\$ 19,978	\$ 181,880,512
Net income	-	12,631,643	-	12,631,643
Other comprehensive income	-	-	(15,165)	(15,165)
Capital stock/participation certificates issued	460,895	-	-	460,895
Capital stock/participation certificates retired	(399,655)	-	-	(399,655)
Patronage refunds:				
Change in patronage declared and paid	-	97	-	97
Balance at September 30, 2019	<u>\$ 4,175,495</u>	<u>\$ 190,378,019</u>	<u>\$ 4,813</u>	<u>\$ 194,558,327</u>

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

ALABAMA AG CREDIT, ACA
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
(UNAUDITED)

NOTE 1 — ORGANIZATION AND SIGNIFICANT ACCOUNTING POLICIES

Alabama Ag Credit, ACA (Agricultural Credit Association), referred to as the Association, is a member-owned cooperative that provides credit and credit-related services to or for the benefit of eligible borrowers/stockholders for qualified agricultural purposes. The Association serves the counties of Autauga, Baldwin, Barbour, Bibb, Bullock, Butler, Chambers, Chilton, Choctaw, Clarke, Coffee, Conecuh, Coosa, Covington, Crenshaw, Dale, Dallas, Elmore, Escambia, Geneva, Greene, Hale, Henry, Houston, Lee, Lowndes, Macon, Marengo, Mobile, Monroe, Montgomery, Perry, Pickens, Pike, Russell, Sumter, Tallapoosa, Tuscaloosa, Washington and Wilcox in the state of Alabama. The Association is a lending institution of the Farm Credit System (the System), which was established by Acts of Congress to meet the needs of American agriculture.

The accompanying unaudited financial statements have been prepared in accordance with accounting principles generally accepted in the U.S. (GAAP) for interim financial information. Accordingly, they do not include all of the disclosures required by GAAP for annual financial statements and should be read in conjunction with the audited financial statements as of and for the year ended December 31, 2018, as contained in the 2018 Annual Report to Stockholders.

In the opinion of management, the accompanying consolidated financial statements contain all adjustments necessary for a fair presentation of the interim financial condition and results of operations and conform with GAAP, except for the inclusion of a statement of cash flows. GAAP require a business enterprise that provides a set of financial statements reporting both financial position and results of operations to also provide a statement of cash flows for each period for which results of operations are provided. In regulations issued by the Farm Credit Administration (FCA), associations have the option to exclude statements of cash flows in interim financial statements. Therefore, the Association has elected not to include a statement of cash flows in these consolidated financial statements. These interim financial statements should be read in conjunction with the audited financial statements as of and for the year ended December 31, 2018, as contained in the 2018 Annual Report to Stockholders. The preparation of financial statements in accordance with GAAP requires management to make estimates and assumptions that affect the amounts reported in the financial statements and accompanying notes. Actual results could differ from those estimates. The results of operations for interim periods are not necessarily indicative of the results to be expected for the full year. Descriptions of the significant accounting policies are included in the 2018 Annual Report to Stockholders. In the opinion of management, these policies and the presentation of the interim financial condition and results of operations conform with GAAP and prevailing practices within the banking industry.

In August 2018, the Financial Accounting Standards Board (FASB) issued guidance entitled “Customer’s Accounting for Implementation Costs Incurred in a Cloud Computing Arrangement That Is a Service Cost.” The guidance aligns the requirements for capitalizing implementation costs incurred in a hosting arrangement that is a service contract with the requirements for capitalizing implementation costs incurred to develop or obtain internal-use software (and hosting arrangements that include an internal-use software license). The accounting for the service element of a hosting arrangement that is a service contract is not affected by this guidance. This guidance becomes effective for interim and annual periods beginning after December 15, 2019. The guidance also requires an entity (customer) to expense the capitalized implementation costs of a hosting arrangement that is a service contract over the term of the hosting arrangement. It further specifies where to present expense and payments in the financial statements. Early adoption is permitted. The guidance is to be applied on a retrospective or prospective basis to all implementation costs incurred after the date of adoption. The Association is evaluating the impact of adoption on the Association’s financial condition and its results of operations.

In August 2018, the FASB issued guidance entitled “Disclosure Framework — Changes to the Disclosure Requirements for Defined Benefit Plans.” The guidance modifies the disclosure requirements for employers that sponsor defined benefit pension or other postretirement plans. This guidance becomes effective for fiscal years ending after December 15, 2020. Early adoption is permitted. The guidance is to be applied on a retrospective basis for all periods. The adoption of this guidance will not impact the Association’s financial condition or its results of operations but will impact the employee benefit plan disclosures.

In August 2018, the FASB issued guidance entitled “Disclosure Framework — Changes to the Disclosure Requirements for Fair Value Measurement.” The guidance modifies the requirements on fair value measurements by removing, modifying or adding to the disclosures. This guidance becomes effective for interim and annual periods beginning after December 15, 2019. Early adoption is permitted, and an entity is permitted to early adopt any removal or modified disclosures and delay adoption of the additional disclosures until their effective date. The adoption of this guidance did not impact the Association’s financial condition or its results of operations but did impact the fair value disclosure.

In August 2017, the FASB issued guidance entitled “Targeted Improvements to Accounting for Hedging Activities.” The guidance better aligns an entity’s risk management activities and financial reporting for hedging relationships through changes to both the designation and measurement guidance for qualifying hedging relationships and the presentation of hedge results. The amendments in this guidance require an entity to present the earnings effect of the hedging instrument in the same income statement line item in

which the earnings effect of the hedged item is reported. This guidance also addresses the timing of effectiveness testing, qualitative and quantitative effectiveness testing and components that can be excluded from effectiveness testing. This guidance became effective for interim and annual periods beginning after December 15, 2018. The adoption of this guidance did not impact the Association's financial condition or its results of operations.

In June 2016, the FASB issued guidance entitled "Measurement of Credit Losses on Financial Instruments." The guidance replaces the current incurred loss impairment methodology with a methodology that reflects expected credit losses and requires consideration of a broader range of reasonable and supportable information to inform credit loss estimates. Credit losses relating to available-for-sale securities would also be recorded through an allowance for credit losses. For public business entities that are not U.S. Securities and Exchange Commission filers this guidance becomes effective for interim and annual periods beginning after December 15, 2020, with early application permitted. The Association is evaluating the impact of adoption on its financial condition and results of operations.

In February 2016, the FASB issued guidance entitled "Leases." The guidance requires the recognition by lessees of lease assets and lease liabilities on the balance sheet for the rights and obligations created by those leases. Leases with lease terms of more than 12 months are impacted by this guidance. The guidance and related amendments in this update became effective for interim and annual periods beginning after December 15, 2018, with early application permitted. The adoption of this guidance did not materially impact the Association's financial condition and results of operations. The Association adopted this guidance on January 1, 2019 and upon adoption, recorded a \$613,317 right of use asset and a \$613,317 lease liability.

The consolidated financial statements comprise the operations of the ACA and its wholly-owned subsidiaries. The preparation of these consolidated financial statements requires the use of management's estimates. The results for the quarter ended September 30, 2019, are not necessarily indicative of the results to be expected for the year ended December 31, 2019. Certain amounts in the prior period's financial statements have been reclassified to conform to current financial statement presentation.

NOTE 2 — LOANS AND ALLOWANCE FOR LOAN LOSSES

A summary of loans follows:

Loan Type	September 30,	December 31,
	2019	2018
	Amount	Amount
Production agriculture:		
Real estate mortgage	\$ 880,723,261	\$ 828,054,658
Production and intermediate term	116,851,375	109,967,257
Agribusiness:		
Loans to cooperatives	6,731,167	2,127,764
Processing and marketing	30,716,749	29,920,600
Farm-related business	15,959	143,110
Communication	2,701,247	2,767,256
Energy	398,786	-
Rural residential real estate	31,415,503	24,440,867
Total	<u>\$ 1,069,554,047</u>	<u>\$ 997,421,512</u>

The Association purchases or sells participation interests with other parties in order to diversify risk, manage loan volume and comply with FCA regulations. The following table presents information regarding the balances of participations purchased and sold at September 30, 2019:

	Other Farm Credit Institutions		Non-Farm Credit Institutions		Total	
	Participations Purchased	Participations Sold	Participations Purchased	Participations Sold	Participations Purchased	Participations Sold
Real estate mortgage	\$ 12,741,322	\$ 32,727,483	\$ -	\$ -	\$ 12,741,322	\$ 32,727,483
Production and intermediate term	11,355,214	4,973,933	-	-	11,355,214	4,973,933
Agribusiness	34,206,440	7,677,562	-	-	34,206,440	7,677,562
Communication	2,701,247	-	-	-	2,701,247	-
Energy	398,786	-	-	-	398,786	-
Total	<u>\$ 61,403,009</u>	<u>\$ 45,378,978</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 61,403,009</u>	<u>\$ 45,378,978</u>

The Association is authorized under the Farm Credit Act to accept “advance conditional payments” (ACPs) from borrowers. To the extent the borrower’s access to such ACPs is restricted and the legal right of setoff exists, the ACPs are netted against the borrower’s related loan balance. Unrestricted ACPs are included in other liabilities. ACPs are not insured, and interest is generally paid by the Association on such balances. Balances of ACPs were \$32,036,664 and \$26,916,674 at September 30, 2019, and December 31, 2018, respectively.

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

	September 30, 2019	December 31, 2018
Nonaccrual loans:		
Real estate mortgage	\$ 7,614,636	\$ 2,325,499
Production and intermediate term	509,098	208,811
Agribusiness	15,959	24,110
Rural residential real estate	41,512	39,428
Total nonaccrual loans	<u>8,181,205</u>	<u>2,597,848</u>
Accruing restructured loans:		
Real estate mortgage	1,189,603	1,363,583
Production and intermediate term	26,320	51,418
Total accruing restructured loans	<u>1,215,923</u>	<u>1,415,001</u>
Accruing loans 90 days or more past due:		
Production and intermediate term	-	983
Total accruing loans 90 days or more past due	<u>-</u>	<u>983</u>
Total nonperforming loans	9,397,128	4,013,832
Other property owned	133,200	45,040
Total nonperforming assets	<u>\$ 9,530,328</u>	<u>\$ 4,058,872</u>

One credit quality indicator utilized by the Association is the FCA Uniform Loan Classification System that categorizes loans into five categories. The categories are defined as follows:

- Acceptable – assets are expected to be fully collectible and represent the highest quality;
- OAEM – assets are currently collectible but exhibit some potential weakness;
- Substandard – assets exhibit some serious weakness in repayment capacity, equity and/or collateral pledged on the loan;
- Doubtful – assets exhibit similar weaknesses to substandard assets; however, doubtful assets have additional weaknesses in existing factors, conditions and values that make collection in full highly questionable; and
- Loss – assets are considered uncollectible.

The following table shows loans and related accrued interest as a percentage of total loans and related accrued interest receivable by loan type as of:

	September 30, 2019	December 31, 2018
Real estate mortgage		
Acceptable	97.6 %	98.1 %
OAEM	0.8	0.8
Substandard/doubtful	1.6	1.1
	100.0	100.0
Production and intermediate term		
Acceptable	96.3	97.1
OAEM	2.3	2.6
Substandard/doubtful	1.4	0.3
	100.0	100.0
Agribusiness		
Acceptable	83.5	99.9
OAEM	16.5	-
Substandard/doubtful	-	0.1
	100.0	100.0
Energy and water/waste water		
Acceptable	100.0	-
OAEM	-	-
Substandard/doubtful	-	-
	100.0	-
Communication		
Acceptable	100.0	100.0
OAEM	-	-
Substandard/doubtful	-	-
	100.0	100.0
Rural residential real estate		
Acceptable	99.6	99.8
OAEM	-	-
Substandard/doubtful	0.4	0.2
	100.0	100.0
Total loans		
Acceptable	97.0	98.1
OAEM	1.5	1.0
Substandard/doubtful	1.5	0.9
	100.0 %	100.0 %

The following tables provide an age analysis of past due loans (including accrued interest) as of:

<u>September 30, 2019</u>	<u>30-89 Days Past Due</u>	<u>90 Days or More Past Due</u>	<u>Total Past Due</u>	<u>Not Past Due or Less Than 30 Days Past Due</u>	<u>Total Loans</u>	<u>Recorded Investment >90 Days and Accruing</u>
Real estate mortgage	\$ 2,612,687	\$ 1,377,655	\$ 3,990,342	\$ 886,685,959	\$ 890,676,301	\$ -
Production and intermediate term	468,768	325,926	794,694	117,871,006	118,665,700	-
Loans to cooperatives	-	-	-	6,790,650	6,790,650	-
Processing and marketing	-	-	-	30,760,804	30,760,804	-
Farm-related business	-	-	-	15,959	15,959	-
Communication	-	-	-	2,710,193	2,710,193	-
Energy	-	-	-	400,161	400,161	-
Rural residential real estate	502,058	-	502,058	31,030,316	31,532,374	-
Total	\$ 3,583,513	\$ 1,703,581	\$ 5,287,094	\$ 1,076,265,048	\$ 1,081,552,142	\$ -

<u>December 31, 2018</u>	<u>30-89 Days Past Due</u>	<u>90 Days or More Past Due</u>	<u>Total Past Due</u>	<u>Not Past Due or Less Than 30 Days Past Due</u>	<u>Total Loans</u>	<u>Recorded Investment >90 Days and Accruing</u>
Real estate mortgage	\$ 3,215,620	\$ 1,315,735	\$ 4,531,355	\$ 831,458,373	\$ 835,989,728	\$ -
Production and intermediate term	644,096	1,983	646,079	111,064,600	111,710,679	983
Loans to cooperatives	-	-	-	2,136,305	2,136,305	-
Processing and marketing	-	-	-	29,974,158	29,974,158	-
Farm-related business	-	-	-	143,692	143,692	-
Communication	-	-	-	2,767,257	2,767,257	-
Rural residential real estate	94,945	-	94,945	24,432,625	24,527,570	-
Total	\$ 3,954,661	\$ 1,317,718	\$ 5,272,379	\$ 1,001,977,010	\$ 1,007,249,389	\$ 983

Note: The recorded investment in the 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.

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. TDRs are undertaken in order to improve the likelihood of recovery on the loan and may include, but are not limited to, forgiveness of principal or interest, interest rate reductions that are lower than the current market rate for new debt with similar risk, or significant term or payment extensions.

As of September 30, 2019, the total recorded investment of TDR loans was \$1,419,620, including \$203,697 classified as nonaccrual and \$1,215,923 classified as accrual, with specific allowance for loan losses of \$526,782. All loans classified as TDRs were individually evaluated to determine the need for allowance for loan losses. As of September 30, 2019, the Association had no commitments to lend funds to borrowers whose loan terms have been modified in a TDR.

The following tables present additional information regarding troubled debt restructurings, which includes both accrual and nonaccrual loans with troubled debt restructuring designation, that occurred during the three months and nine months ended September 30, 2019. The premodification outstanding recorded investment represents the recorded investment of the loans as of the quarter end prior to the restructuring. The postmodification outstanding recorded investment represents the recorded investment of the loans as of the quarter end the restructuring occurred. Loans formally restructured prior to January 1, 2019 were \$1,273,709.

<u>For the Three Months Ended September 30, 2019</u>	<u>Premodification Outstanding Recorded Investment</u>	<u>Postmodification Outstanding Recorded Investment</u>
Troubled debt restructurings:		
Production and intermediate term	\$ 163,863	\$ 145,911
Total	\$ 163,863	\$ 145,911

<u>For the Nine Months Ended September 30, 2019</u>	<u>Premodification Outstanding Recorded Investment</u>	<u>Postmodification Outstanding Recorded Investment</u>
Troubled debt restructurings:		
Production and intermediate term	\$ 163,863	\$ 145,911
Total	\$ 163,863	\$ 145,911

In restructurings where principal is forgiven, the amount of the forgiveness is immediately charged off. In restructurings where accrued interest is forgiven, the interest is reversed (if current year interest) or charged off (if prior year interest).

The predominant form of concession granted for TDRs includes extension of the term and/or delayed payments. Other types of modifications include principal or accrued interest reductions and interest rate decreases, among others. At times, these terms might

be offset with incremental payments, collateral or new borrower guarantees, in which case we assess all of the modified terms to determine if the overall modification qualifies as a TDR. No loans modified in the last 12 months have subsequently defaulted as of September 30, 2019.

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

	Loans Modified as TDRs		TDRs in Nonaccrual Status	
	September 30, 2019	December 31, 2018	September 30, 2019	December 31, 2018
Real estate mortgage	\$ 1,210,128	\$ 1,555,714	\$ 20,525	\$ 192,131
Production and intermediate term	209,492	95,366	183,172	43,948
Total	\$ 1,419,620	\$ 1,651,080	\$ 203,697	\$ 236,079

Additional impaired loan information is as follows:

	September 30, 2019			December 31, 2018		
	Recorded Investment	Unpaid Principal Balance ^a	Related Allowance	Recorded Investment	Unpaid Principal Balance ^a	Related Allowance
Impaired loans with a related allowance for credit losses:						
Real estate mortgage	\$ 3,049,046	\$ 3,090,499	\$ 901,678	\$ 1,464,953	\$ 1,472,467	\$ 524,234
Production and intermediate term	145,911	145,911	144,911	207,811	207,811	171,620
Farm-related business	-	-	-	-	-	-
Rural residential real estate	-	-	-	-	-	-
Total	\$ 3,194,957	\$ 3,236,410	\$ 1,046,589	\$ 1,672,764	\$ 1,680,278	\$ 695,854
Impaired loans with no related allowance for credit losses:						
Real estate mortgage	\$ 5,755,194	\$ 5,968,204	\$ -	\$ 2,224,129	\$ 2,427,675	\$ -
Production and intermediate term	389,507	390,357	-	53,401	140,547	-
Farm-related business	15,959	15,959	-	24,110	24,110	-
Rural residential real estate	41,512	41,512	-	39,428	39,428	-
Total	\$ 6,202,172	\$ 6,416,032	\$ -	\$ 2,341,068	\$ 2,631,760	\$ -
Total impaired loans:						
Real estate mortgage	\$ 8,804,240	\$ 9,058,703	\$ 901,678	\$ 3,689,082	\$ 3,900,142	\$ 524,234
Production and intermediate term	535,418	536,268	144,911	261,212	348,358	171,620
Farm-related business	15,959	15,959	-	24,110	24,110	-
Rural residential real estate	41,512	41,512	-	39,428	39,428	-
Total	\$ 9,397,129	\$ 9,652,442	\$ 1,046,589	\$ 4,013,832	\$ 4,312,038	\$ 695,854

^a Unpaid principal balance represents the recorded principal balance of the loan.

For the Three Months Ended

	September 30, 2019		September 30, 2018	
	Average Impaired Loans	Interest Income Recognized	Average Impaired Loans	Interest Income Recognized
Impaired loans with a related allowance for credit losses:				
Real estate mortgage	\$ 3,050,521	\$ 16,645	\$ 3,793,042	\$ 17,235
Production and intermediate term	158,064	-	397,419	4,927
Farm-related business	-	-	-	-
Rural residential real estate	-	-	31,807	-
Total	\$ 3,208,585	\$ 16,645	\$ 4,222,268	\$ 22,162
Impaired loans with no related allowance for credit losses:				
Real estate mortgage	\$ 5,822,532	\$ 2,902	\$ 2,164,807	\$ 4,938
Production and intermediate term	409,270	327	143,823	632
Farm-related business	15,959	-	24,110	-
Rural residential real estate	41,841	-	42,026	-
Total	\$ 6,289,602	\$ 3,229	\$ 2,374,766	\$ 5,570
Total impaired loans:				
Real estate mortgage	\$ 8,873,053	\$ 19,547	\$ 5,957,849	\$ 22,173
Production and intermediate term	567,334	327	541,242	5,559
Farm-related business	15,959	-	24,110	-
Rural residential real estate	41,841	-	73,833	-
Total	\$ 9,498,187	\$ 19,874	\$ 6,597,034	\$ 27,732

For the Nine Months Ended

	September 30, 2019		September 30, 2018	
	Average Impaired Loans	Interest Income Recognized	Average Impaired Loans	Interest Income Recognized
Impaired loans with a related allowance for credit losses:				
Real estate mortgage	\$ 2,226,328	\$ 38,149	\$ 4,041,869	\$ 55,411
Production and intermediate term	200,582	793	325,449	9,800
Farm-related business	-	-	-	-
Rural residential real estate	7,357	185	24,974	272
Total	\$ 2,434,267	\$ 39,127	\$ 4,392,292	\$ 65,483
Impaired loans with no related allowance for credit losses:				
Real estate mortgage	\$ 5,066,197	\$ 51,822	\$ 2,183,581	\$ 30,689
Production and intermediate term	314,913	5,482	323,470	7,053
Farm-related business	16,831	-	25,535	-
Rural residential real estate	46,902	390	43,587	-
Total	\$ 5,444,843	\$ 57,694	\$ 2,576,173	\$ 37,742
Total impaired loans:				
Real estate mortgage	\$ 7,292,525	\$ 89,971	\$ 6,225,450	\$ 86,100
Production and intermediate term	515,495	6,275	648,919	16,853
Farm-related business	16,831	-	25,535	-
Rural residential real estate	54,259	575	68,561	272
Total	\$ 7,879,110	\$ 96,821	\$ 6,968,465	\$ 103,225

A summary of changes in the allowance for loan losses and period end recorded investment in loans is as follows:

	Real Estate Mortgage	Production and Intermediate Term	Agribusiness	Communications	Energy and Water/Waste Water	Rural Residential Real Estate	Total
Allowance for Credit Losses:							
Balance at June 30, 2019	\$ 6,977,622	\$ 378,812	\$ 52,856	\$ 2,213	\$ 329	\$ 100,337	\$ 7,512,169
Charge-offs	-	-	-	-	-	(6,722)	(6,722)
Recoveries	19,361	-	-	-	-	-	19,361
Provision for loan losses	106,374	4,532	17,257	(5)	-	(9,895)	118,263
Other	(176)	(11,306)	(2,568)	-	879	(969)	(14,140)
Balance at September 30, 2019	<u>\$ 7,103,181</u>	<u>\$ 372,038</u>	<u>\$ 67,545</u>	<u>\$ 2,208</u>	<u>\$ 1,208</u>	<u>\$ 82,751</u>	<u>\$ 7,628,931</u>
Balance at December 31, 2018	\$ 6,910,644	\$ 364,699	\$ 43,021	\$ 2,268	\$ -	\$ 38,490	\$ 7,359,122
Charge-offs	(28,202)	-	-	-	-	(6,722)	(34,924)
Recoveries	34,594	-	-	-	-	-	34,594
Provision for loan losses	186,017	31,714	29,953	(60)	-	51,214	298,838
Other	128	(24,375)	(5,429)	-	1,208	(231)	(28,699)
Balance at September 30, 2019	<u>\$ 7,103,181</u>	<u>\$ 372,038</u>	<u>\$ 67,545</u>	<u>\$ 2,208</u>	<u>\$ 1,208</u>	<u>\$ 82,751</u>	<u>\$ 7,628,931</u>
Ending Balance:							
Individually evaluated for impairment	\$ 1,275,178	\$ 144,911	\$ -	\$ -	\$ -	\$ 31,683	\$ 1,451,772
Collectively evaluated for impairment	<u>5,828,003</u>	<u>227,127</u>	<u>67,545</u>	<u>2,208</u>	<u>1,208</u>	<u>51,068</u>	<u>6,177,159</u>
Balance at September 30, 2019	<u>\$ 7,103,181</u>	<u>\$ 372,038</u>	<u>\$ 67,545</u>	<u>\$ 2,208</u>	<u>\$ 1,208</u>	<u>\$ 82,751</u>	<u>\$ 7,628,931</u>
Balance at June 30, 2019	\$ 6,096,697	\$ 236,025	\$ 64,877	\$ 3,855	\$ -	\$ 53,065	\$ 6,454,519
Charge-offs	-	-	-	-	-	-	-
Recoveries	38,989	-	-	-	-	-	38,989
Provision for loan losses	471,188	(10,441)	(14,720)	(46)	-	3,693	449,674
Other	15	(7,831)	(1,320)	-	-	(618)	(9,754)
Balance at September 30, 2018	<u>\$ 6,606,889</u>	<u>\$ 217,753</u>	<u>\$ 48,837</u>	<u>\$ 3,809</u>	<u>\$ -</u>	<u>\$ 56,140</u>	<u>\$ 6,933,428</u>
Balance at December 31, 2017	\$ 6,293,569	\$ 248,540	\$ 58,177	\$ 3,601	\$ -	\$ 28,589	\$ 6,632,476
Charge-offs	-	(88,888)	-	-	-	-	(88,888)
Recoveries	42,387	-	-	-	-	-	42,387
Provision for loan losses	266,629	55,935	(16,820)	208	3,640	27,891	337,483
Other	4,304	2,166	7,480	-	(3,640)	(340)	9,970
Balance at September 30, 2018	<u>\$ 6,606,889</u>	<u>\$ 217,753</u>	<u>\$ 48,837</u>	<u>\$ 3,809</u>	<u>\$ -</u>	<u>\$ 56,140</u>	<u>\$ 6,933,428</u>
Ending Balance:							
Individually evaluated for impairment	\$ 928,562	\$ 52,597	\$ -	\$ -	\$ -	\$ 22,807	\$ 1,003,966
Collectively evaluated for impairment	<u>5,678,327</u>	<u>165,156</u>	<u>48,837</u>	<u>3,809</u>	<u>-</u>	<u>33,333</u>	<u>5,929,462</u>
Balance at September 30, 2018	<u>\$ 6,606,889</u>	<u>\$ 217,753</u>	<u>\$ 48,837</u>	<u>\$ 3,809</u>	<u>\$ -</u>	<u>\$ 56,140</u>	<u>\$ 6,933,428</u>
Recorded Investments in Loans Outstanding:							
Ending Balance at							
September 30, 2019	<u>\$ 890,676,301</u>	<u>\$ 118,665,700</u>	<u>\$ 37,567,413</u>	<u>\$ 2,710,193</u>	<u>\$ 400,161</u>	<u>\$ 31,532,374</u>	<u>\$ 1,081,552,142</u>
Individually evaluated for impairment	<u>\$ 14,376,251</u>	<u>\$ 1,658,716</u>	<u>\$ 15,959</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 137,895</u>	<u>\$ 16,188,821</u>
Collectively evaluated for impairment	<u>\$ 876,300,050</u>	<u>\$ 117,006,984</u>	<u>\$ 37,551,454</u>	<u>\$ 2,710,193</u>	<u>\$ 400,161</u>	<u>\$ 31,394,479</u>	<u>\$ 1,065,363,321</u>
Ending Balance at							
December 31, 2018	<u>\$ 835,989,728</u>	<u>\$ 111,710,679</u>	<u>\$ 32,254,155</u>	<u>\$ 2,767,257</u>	<u>\$ -</u>	<u>\$ 24,527,570</u>	<u>\$ 1,007,249,389</u>
Individually evaluated for impairment	<u>\$ 8,432,927</u>	<u>\$ 345,255</u>	<u>\$ 24,110</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 39,428</u>	<u>\$ 8,841,720</u>
Collectively evaluated for impairment	<u>\$ 827,556,801</u>	<u>\$ 111,365,424</u>	<u>\$ 32,230,045</u>	<u>\$ 2,767,257</u>	<u>\$ -</u>	<u>\$ 24,488,142</u>	<u>\$ 998,407,669</u>

NOTE 3 — CAPITAL

The Association's board of directors has established a Capital Adequacy Plan (Plan) that includes the capital targets that are necessary to achieve the institution's capital adequacy goals as well as the minimum permanent capital standards. The Plan monitors projected dividends, equity retirements and other actions that may decrease the Association's permanent capital. In addition to factors that must be considered in meeting the minimum standards, the board of directors also monitors the following factors: capability of management; quality of operating policies, procedures and internal controls; quality and quantity of earnings; asset quality and the adequacy of the allowance for losses to absorb potential loss within the loan portfolio; sufficiency of liquid funds; needs of an institution's customer base; and any other risk-oriented activities, such as funding and interest rate risk, potential obligations under joint and several liability, contingent and off-balance-sheet liabilities or other conditions warranting additional capital. At least quarterly, management reviews the Association's goals and objectives with the board.

Regulatory Capitalization Requirements

Risk-adjusted:	Regulatory Minimums	Conservation Buffer	Total	As of September 30, 2019
Common equity tier 1 ratio	4.50%	2.50%	7.00%	16.25%
Tier 1 capital ratio	6.00%	2.50%	8.50%	16.25%
Total capital ratio	8.00%	2.50%	10.50%	16.95%
Permanent capital ratio	7.00%	0.00%	7.00%	16.36%
Non-risk-adjusted:				
Tier 1 leverage ratio	4.00%	1.00%	5.00%	16.43%
UREE leverage ratio	1.50%	0.00%	1.50%	17.57%

Risk-adjusted Capital Ratios

	Common equity tier 1 ratio	Tier 1 capital ratio	Total capital ratio	Permanent capital ratio
Numerator:				
Unallocated retained earnings	188,111,370	188,111,370	188,111,370	188,111,370
Common Cooperative Equities:				
Statutory minimum purchased borrower stock	4,173,379	4,173,379	4,173,379	4,173,379
Allowance for loan losses and reserve for credit losses subject to certain limitations	-	-	7,625,987	-
Regulatory Adjustments and Deductions:				
Amount of allocated investments in other System institutions	(16,322,640)	(16,322,640)	(16,322,640)	(16,322,640)
	175,962,109	175,962,109	183,588,096	175,962,109
Denominator:				
Risk-adjusted assets excluding allowance	1,099,132,360	1,099,132,360	1,099,132,360	1,099,132,360
Regulatory Adjustments and Deductions:				
Regulatory deductions included in total capital	(16,322,640)	(16,322,640)	(16,322,640)	(16,322,640)
Allowance for loan losses	-	-	-	(7,535,934)
	1,082,809,720	1,082,809,720	1,082,809,720	1,075,273,786

Non-risk-adjusted Capital Ratios

	Tier 1 leverage ratio	UREE leverage ratio
Numerator:		
Unallocated retained earnings	188,111,370	188,111,370
Common Cooperative Equities:		
Statutory minimum purchased borrower stock	4,173,379	-
Regulatory Adjustments and Deductions:		
Amount of allocated investments in other System institutions	(16,322,640)	-
	175,962,109	188,111,370
Denominator:		
Total Assets	1,091,943,740	1,091,943,740
Regulatory Adjustments and Deductions:		
Regulatory deductions included in tier 1 capital	(21,001,561)	(21,001,561)
	1,070,942,179	1,070,942,179

An additional component of equity is accumulated other comprehensive income. The Association's accumulated other comprehensive income (loss) relates entirely to its nonpension other postretirement benefits. Amortization of prior service (credits) cost and of actuarial (gain) loss are reflected in "Other components of net periodic postretirement benefit cost" in the Consolidated Statement of Comprehensive Income. The following table summarizes the changes in accumulated other comprehensive income (loss) for the nine months ended September 30:

	<u>2019</u>	<u>2018</u>
Accumulated other comprehensive income (loss) at January 1	\$ 19,978	\$ (582,234)
Amortization of prior service (credit) costs included		
in salaries and employee benefits	(15,165)	(12,974)
Amortization of actuarial (gain) loss included		
in salaries and employee benefits	-	24,656
Other comprehensive income (loss), net of tax	<u>(15,165)</u>	<u>11,682</u>
Accumulated other comprehensive income at September 30	<u>\$ 4,813</u>	<u>\$ (570,552)</u>

NOTE 4 — INCOME TAXES

Alabama Ag Credit, ACA and its PCA subsidiary, Alabama Ag Credit, PCA (Associations) are subject to federal and certain other income taxes. The Associations are eligible to operate as cooperatives that qualify for tax treatment under Subchapter T of the Internal Revenue Code. Under specified conditions, the Associations can exclude from taxable income amounts distributed as qualified patronage refunds in the form of cash, stock or allocated surplus. Provisions for income taxes are made only on those taxable earnings that will not be distributed as qualified patronage dividends. Deferred taxes are recorded at the tax effect of all temporary differences based on the assumption that such temporary differences are retained by the institution and will therefore impact future tax payments. A valuation allowance is provided against deferred tax assets to the extent that it is more likely than not (more than 50 percent probability), based on management's estimate, that they will not be realized. The Association has recorded a full valuation allowance against its deferred tax asset as of September 30, 2019 based on management's estimate that it is more likely than not that the deferred tax asset will not be realized. For the three and nine months ended September 30, 2019 and 2018, the Associations had no taxable income. The subsidiary, Alabama Ag Credit, FLCA, is exempt from federal and other income taxes as provided in the Farm Credit Act of 1971.

NOTE 5 — FAIR VALUE MEASUREMENTS

FASB guidance defines fair value as the exchange price that would be received for an asset or paid to transfer a liability in the principal or most advantageous market for the asset or liability. See Note 13 to the 2018 Annual Report to Stockholders for a more complete description.

Assets and liabilities measured at fair value on a recurring basis are summarized below:

<u>September 30, 2019</u>	<u>Fair Value Measurement Using</u>			<u>Total Fair Value</u>
	<u>Level 1</u>	<u>Level 2</u>	<u>Level 3</u>	
Assets:				
Assets held in nonqualified benefit trusts	\$ 94,271	\$ -	\$ -	\$ 94,271
<u>December 31, 2018</u>	<u>Fair Value Measurement Using</u>			<u>Total Fair Value</u>
	<u>Level 1</u>	<u>Level 2</u>	<u>Level 3</u>	
Assets:				
Assets held in nonqualified benefit trusts	\$ 72,879	\$ -	\$ -	\$ 72,879

Assets and liabilities measured at fair value on a nonrecurring basis for each of the fair value hierarchy values are summarized below:

<u>September 30, 2019</u>	<u>Fair Value Measurement Using</u>			<u>Total Fair Value</u>
	<u>Level 1</u>	<u>Level 2</u>	<u>Level 3</u>	
Assets:				
Loans*	\$ -	\$ -	\$4,173,154	\$4,173,154
Other property owned	-	-	149,850	149,850
<u>December 31, 2018</u>	<u>Fair Value Measurement Using</u>			<u>Total Fair Value</u>
	<u>Level 1</u>	<u>Level 2</u>	<u>Level 3</u>	
Assets:				
Loans*	\$ -	\$ -	\$ 3,059,213	\$ 3,059,213
Other property owned	-	-	50,670	50,670

*Represents the fair value of certain loans that were evaluated for impairment under authoritative guidance “Accounting by Creditors for Impairment of a Loan.” The fair value was based upon the underlying collateral since these were collateral-dependent loans for which real estate is the collateral.

Information About Nonrecurring Level 3 Fair Value Measurements

With regard to nonrecurring measurements for impaired loans and other property owned, it is not practicable to provide specific information on inputs, as each collateral property is unique. System institutions utilize appraisals to value these loans and other property owned and take into account unobservable inputs, such as income and expense, comparable sales, replacement cost and comparability adjustments.

Valuation Techniques

As more fully discussed in Note 13 to the 2018 Annual Report to Stockholders, authoritative guidance establishes a fair value hierarchy, which requires an entity to maximize the use of observable inputs and minimize the use of unobservable inputs when measuring fair value. The following represent a brief summary of the valuation techniques used for the Association’s assets and liabilities.

Assets Held in Nonqualified Benefits Trusts

Assets held in trust funds related to deferred compensation and supplemental retirement plans are classified within Level 1. The trust funds include investments that are actively traded and have quoted net asset values that are observable in the marketplace.

Loans Evaluated for Impairment

For certain loans evaluated for impairment under FASB impairment guidance, the fair value is based upon the underlying real estate collateral since the loans were collateral-dependent. 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. As a result, a majority of these loans have fair value measurements that fall within Level 3 of the fair value hierarchy. When the value of the real estate, less estimated costs to sell, is less than the principal balance of the loan, a specific reserve is established.

Other Property Owned

Other property owned is generally classified as Level 3 of the fair value hierarchy. The process for measuring the fair value of the other property owned involves the use of independent appraisals and other market-based information. Costs to sell represent transaction costs and are not included as a component of the asset’s fair value. As a result, these fair value measurements fall within Level 3 of the hierarchy. As of September 30, 2019, other property owned, net is reported at \$133,200 in the consolidated balance sheet.

NOTE 6 — EMPLOYEE BENEFIT PLANS

Employee Retirement Plans: As discussed in Note 2 and Note 11 to the 2018 Annual Report to Stockholders, employees of the Association participate in either the Texas Farm Credit District’s (District) defined benefit pension plan (DB Plan) or the District’s defined contribution plan (DC Plan).

The structure of the DB Plan is characterized as multi-employer since the assets, liabilities and cost of the plan are not segregated or separately accounted for by participating employers (Bank and associations). The Association recognizes its amortized annual contributions to the plan as an expense. The annual contribution is paid in January of each year and amortized into expense on a monthly basis; unamortized contributions are included in “Other Assets” in the consolidated balance sheet. The following table represents DB contributions made, amounts amortized into expense, and the remaining unamortized contributions amounts as of September 30:

	<u>2019</u>	<u>2018</u>
DB contribution	\$ 522,220	\$ 572,482
YTD amortization	\$ 391,665	\$ 429,361
Net periodic benefit	<u>\$ 130,555</u>	<u>\$ 143,121</u>

Association contributions to the DC Plan are expensed as incurred. For the nine months ended September 30, 2019 and 2018, the Association recognized pension costs for the DC Plan of \$248,424 and \$225,332, respectively.

Employees are also eligible to participate in the Farm Credit Benefits Alliance 401(k) Plan. Contributions to the 401(k) plan are expensed as incurred. The Association’s contributions to the 401(k) plan were \$177,822 and \$184,525 for the nine months ended September 30, 2019 and 2018, respectively.

Other Postretirement Benefits: In addition to pension benefits, the Association provides certain health care benefits to qualifying retired employees (other postretirement benefits). These benefits are not characterized as multi-employer, and consequently, the liability for these benefits is included in the consolidated balance sheet. The following table summarizes the components of net periodic benefit costs of nonpension other postretirement employee benefits for the nine months ended September 30:

	<u>Other Benefits</u>	
	<u>2019</u>	<u>2018</u>
Service cost	\$ 39,129	\$ 53,109
Interest cost	88,125	88,390
Expected return on plan assets	-	-
Amortization of prior service (credits) costs	(15,165)	(12,974)
Amortization of net actuarial (gain) loss	-	24,656
Total non-service cost	<u>72,960</u>	<u>100,072</u>
Net periodic benefit cost	<u>\$ 112,089</u>	<u>\$ 153,181</u>

The Association’s liability for the unfunded accumulated obligation for these benefits at September 30, 2019, was \$2,589,577 and is included in “Other Liabilities” in the balance sheet.

NOTE 7 — COMMITMENTS AND CONTINGENT LIABILITIES

The Association is involved in various legal proceedings in the normal course of business. In the opinion of legal counsel and management, there are no legal proceedings at this time that are likely to materially affect the Association.

NOTE 8 — SUBSEQUENT EVENTS

The Association has evaluated subsequent events through November 4, 2019 which is the date the financial statements were issued. There are no other significant events requiring disclosure as of November 4, 2019.