FARM CREDIT OF THE VIRGINIAS, ACA

2018 ANNUAL REPORT

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Management

C. Peery Heldreth, III .... Chief Executive Officer
Kelly S. Bohrer .... Chief Operations Officer
A. Katie Frazier .... Director of External Affairs
Teresa A. Harris .... Chief Business Development Officer
Michael S. Jonas .... Director of Sales and Marketing
M. Kay Manchester .... Chief Training and Human Resource Officer
Al P. Saufley .... Chief Lending Officer
Justin J. Weekley .... Chief Financial Officer

Board of Directors

Donna M. Brooke-Alt .... Chairperson
Donald W. Reese .... Vice Chairperson
Ronald L. Bennett .... Director
Kevin C. Craun .... Director
William J. Franklin, Jr. .... Director
Bobby C. Gray .... Director
Charles E. Horn, Jr. .... Director
Paul M. House .... Director
Melody S. Jones .... Director
James F. Kinsey .... Director
Charles B. Leech, IV .... Director
Milton L. McPike, Jr. .... Director
Wallace W. Sanford, III .... Director
Barry W. Shelor .... Director
Alfred W. Stephens, Jr. .... Director
John E. Wells .... Director

Message from the Chief Executive Officer

Looking back at 2018, I'm very pleased to report that Farm Credit of the Virginias (FCV) completed another excellent financial year on behalf of our customer-owners. Continuing the trend of recent years, we again posted positive results in net income which translates to tangible value to our customer-owners, and undertook other initiatives to benefit agriculture and our rural communities.

FCV finished 2018 with net income of $52.6 million, which was $6.5 million above our budget projections. While this overall net income was lower than at year-end 2017 by approximately $4 million, this disparity stems in part from a one-time pension fund adjustment in 2017 of $8.2 million. Excluding this influx to 2017 income, and adjusting for a $1.7 million insurance refund in 2018, our adjusted 2018 net income increased by $2.5 million over the previous year. We also increased total assets to $1.91 billion at year-end 2018, up $6 million from the prior year.

In 2018, the board approved a record level of patronage payments stemming from the previous year's performance. In April 2018, we were pleased to deliver $30 million in patronage payments to our customers, a combination of direct patronage from FCV and a special pass-through patronage payment from AgFirst, our funding bank.

As a cooperative, delivering on our mission goes beyond our financial performance. We strive every day to deliver value in our individual relationships with our customers, and our relationship and customer service teams are dedicated to crafting the best solutions to meet your individual needs. Our consistently high customer satisfaction survey results tell us that these efforts are appreciated, as we appreciate the opportunity to work with you.

FCV also focuses on developing additional value-added resources through our Knowledge Center. In 2018, we introduced QuickBooks for Agriculture. An online course that enables producers to learn from the convenience of their own homes, and launched a Farm Succession Planning webinar series, both of which will also be offered again in 2019. These new resources supplement the already rich Knowledge Center offerings, including AgBiz Planner, the Dairy Management Institute, the Farm Management Institute, a video series on construction financing, and many more. I encourage all our customer-owners to capitalize on these resources to strengthen their business management for further success.

Also to support the broader community, each year we make considered donations to programs and organizations that are dedicated to the future of agriculture and our communities. In 2018, that included donations to the West Virginia University Davis College and the Virginia Tech VALOR (Virginia Agriculture Leaders Obtaining Results) program, for which we provided seed money and have since extended our support. In conjunction with Colonial Farm Credit and MidAtlantic Farm Credit, fellow organizations in the Farm Credit System, we provided funding for the Federation of Virginia food banks" Milk for Good" program, and we continued our commitment to the Blue Ridge Area Food Bank's "Farm Fresh Fund." We also made numerous donations to Ag industry organizations, county fairs, and local 4H and FFA organizations.

To ensure our continued success, FCV also focuses internally, seeking efficiencies in our operation and retooling our processes to continually improve our delivery of services to customers and to respond to changes in the industries we serve. We are proud that for more than 100 years, we have been evolving alongside our customers and our communities, and we will continue to ensure that we consistently enhance our efforts to best serve you.

Critical to these efforts is a highly capable, highly committed staff of employees, many of whom have been with our cooperative for decades. We also attract vibrant, talented new employees to our team at all levels. One key addition in 2018 was Justin Weekley, who came on board in October as our new Chief Financial Officer, replacing David Sauer who retired in early 2019. We thank David for his years of contribution and service, and look forward to working with Justin in the years to come. Also joining our team in 2018 was Katie Frazier, formerly President of the Virginia Agribusiness Council (VAC), as our Director of External Affairs.

The right staff will be critical as we continue to operate in an environment of change and uncertainty that will impact both FCV and our customer-owners. Now into the sixth year of an economic reset, many of our customers have made and may need to continue to make difficult decisions about their operations in the coming year. The ongoing trade war and escalating tariffs, trade agreements including USMCA that have yet to be ratified, and a new Farm Bill with programs that have yet to be explored all offer their own variances into the mix of business considerations.

Through all the coming changes, FCV's strategy will remain the same: deliver outstanding service, carefully manage our financial resources, and most importantly, support our customer-owners.

C. Peery Heldreth, III
Chief Executive Officer

March 13, 2019

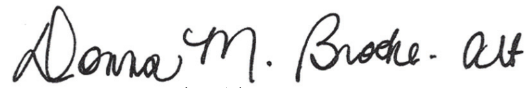
Report of Management

The accompanying consolidated financial statements and related financial information appearing throughout this annual report have been prepared by management of Farm Credit of the Virginias, ACA (Association) in accordance with generally accepted accounting principles appropriate in the circumstances. Amounts which must be based on estimates represent the best estimates and judgments of management. Management is responsible for the integrity, objectivity, consistency, and fair presentation of the consolidated financial statements and financial information contained in this report.

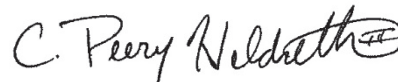
Management maintains and depends upon an internal accounting control system designed to provide reasonable assurance that transactions are properly authorized and recorded, that the financial records are reliable as the basis for the preparation of all financial statements, and that the assets of the Association are safeguarded. The design and implementation of all systems of internal control are based on judgments required to evaluate the costs of controls in relation to the expected benefits and to determine the appropriate balance between these costs and benefits. The Association maintains an internal audit program to monitor compliance with the systems of internal accounting control. Audits of the accounting records, accounting systems and internal controls are performed and internal audit reports, including appropriate recommendations for improvement, are submitted to the Board of Directors.

The consolidated financial statements have been audited by independent auditors, whose report appears elsewhere in this annual report. The Association is also subject to examination by the Farm Credit Administration.

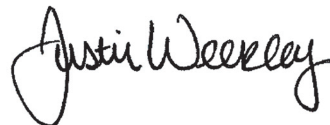
The consolidated financial statements, in the opinion of management, fairly present the financial condition of the Association. The undersigned certify that we have reviewed the 2018 Annual Report of Farm Credit of the Virginias, ACA, that the report has been prepared under the oversight of the audit committee of the Board of Directors and in accordance with all applicable statutory or regulatory requirements, and that the information contained herein is true, accurate, and complete to the best of our knowledge and belief.



Donna M. Brooke-Alt
Chairperson of the Board



C. Peery Heldreth, III
Chief Executive Officer



Justin Weekley
Chief Financial Officer

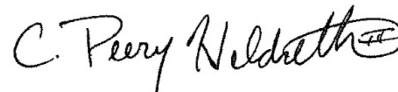
March 13, 2019

Report on Internal Control Over Financial Reporting

The Association's principal executives and principal financial officers, or persons performing similar functions, are responsible for establishing and maintaining adequate internal control over financial reporting for the Association's Consolidated Financial Statements. For purposes of this report, "internal control over financial reporting" is defined as a process designed by, or under the supervision of the Association's principal executives and principal financial officers, or persons performing similar functions, and effected by its Board of Directors, management and other personnel, to provide reasonable assurance regarding the reliability of financial reporting information and the preparation of the Consolidated Financial Statements for external purposes in accordance with accounting principles generally accepted in the United States of America and includes those policies and procedures that: (1) pertain to the maintenance of records that in reasonable detail accurately and fairly reflect the transactions and dispositions of the assets of the Association, (2) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial information in accordance with accounting principles generally accepted in the United States of America, and that receipts and expenditures are being made only in accordance with authorizations of management and directors of the Association, and (3) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use or disposition of the Association's assets that could have a material effect on its Consolidated Financial Statements.

The Association's management has completed an assessment of the effectiveness of internal control over financial reporting as of December 31, 2018. In making the assessment, management used the framework in *Internal Control — Integrated Framework (2013)*, promulgated by the Committee of Sponsoring Organizations of the Treadway Commission, commonly referred to as the "COSO" criteria.

Based on the assessment performed, the Association's management concluded that as of December 31, 2018, the internal control over financial reporting was effective based upon the COSO criteria. Additionally, based on this assessment, the Association determined that there were no material weaknesses in the internal control over financial reporting as of December 31, 2018.



C. Peery Heldreth, III
Chief Executive Officer

Justin Weekley
Chief Financial Officer

March 13, 2019

Consolidated Five - Year Summary of Selected Financial Data

(dollars in thousands)	2018	2017	December 31, 2016	2015	2014
Balance Sheet Data					
Cash	**$ 4,700**	$ 5,082	$ 5,730	$ 2,945	$ 6,038
Loans	**1,850,777**	1,844,949	1,798,996	1,692,633	1,583,241
Allowance for loan losses	**(15,313)**	(17,461)	(14,483)	(14,487)	(12,465)
Net loans	**1,835,464**	1,827,488	1,784,513	1,678,146	1,570,776
Equity investments in other Farm Credit institutions	**20,729**	20,763	19,698	25,330	25,344
Other property owned	**1,477**	1,221	2,467	4,803	2,786
Other assets	**47,281**	49,054	46,125	46,451	49,569
Total assets	**$ 1,909,651**	$1,903,608	$1,858,533	$1,757,675	$1,654,513
Notes payable to AgFirst Farm Credit Bank*	**$ 1,422,676**	$1,437,895	$1,423,922	$1,354,433	$1,275,765
Accrued interest payable and other liabilities with maturities of less than one year	**46,597**	42,892	43,788	38,464	42,521
Total liabilities	**1,469,273**	1,480,787	1,467,710	1,392,897	1,318,286
Capital stock and participation certificates	**10,426**	10,493	10,433	12,606	13,159
Retained earnings					
Allocated	**92,568**	92,568	92,568	92,568	92,568
Unallocated	**337,408**	319,790	287,846	259,626	230,527
Accumulated other comprehensive income (loss)	**(24)**	(30)	(24)	(22)	(27)
Total members' equity	**440,378**	422,821	390,823	364,778	336,227
Total liabilities and members' equity	**$ 1,909,651**	$1,903,608	$1,858,533	$1,757,675	$1,654,513
Statement of Income Data					
Net interest income	**$ 57,070**	$ 54,197	$ 51,160	$ 50,072	$ 47,859
Provision for loan losses	**2,500**	3,250	2,750	2,700	1,200
Noninterest income (expense), net	**(1,949)**	5,997	(5,190)	(3,273)	4,129
Net income	**$ 52,621**	$ 56,944	$ 43,220	$ 44,099	$ 50,788
Key Financial Ratios					
Rate of return on average:					
Total assets	**2.81%**	3.04%	2.43%	2.62%	3.22%
Total members' equity	**11.97%**	13.89%	11.25%	12.40%	15.40%
Net interest income as a percentage of average earning assets	**3.11%**	2.96%	2.95%	3.05%	3.13%
Net (chargeoffs) recoveries to average loans	**(0.254)%**	(0.015)%	(0.159)%	(0.041)%	(0.040)%
Total members' equity to total assets	**23.06%**	22.21%	21.03%	20.75%	20.32%
Debt to members' equity (:1)	**3.34**	3.50	3.76	3.82	3.92
Allowance for loan losses to loans	**0.83%**	0.95%	0.81%	0.86%	0.79%
Permanent capital ratio	**22.48%**	21.09%	20.75%	20.07%	19.91%
Total surplus ratio	**	**	20.08%	19.29%	19.15%
Core surplus ratio	**	**	20.08%	19.29%	19.15%
Common equity tier 1 capital ratio	**22.30%**	20.93%	**	**	**
Tier 1 capital ratio	**22.30%**	20.93%	**	**	**
Total regulatory capital ratio	**23.10%**	21.72%	**	**	**
Tier 1 leverage ratio	**22.84%**	21.41%	**	**	**
Unallocated retained earnings (URE) and URE equivalents leverage ratio	**23.07%**	21.59%	**	**	**
Net Income Distribution					
Estimated patronage refunds:					
Cash	**$ 35,000**	$ 25,000	$ 15,000	$ 15,000	$ 21,000

** General financing agreement is renewable on a one-year cycle. The next renewal date is December 31, 2019.*
*** Not applicable due to changes in regulatory capital requirements effective January 1, 2017.*

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

(dollars in thousands, except as noted)

GENERAL OVERVIEW

The following commentary summarizes the financial condition and results of operations of Farm Credit of the Virginias, ACA, (Association) for the year ended December 31, 2018 with comparisons to the years ended December 31, 2017 and December 31, 2016. This information should be read in conjunction with the Consolidated Financial Statements, Notes to the Consolidated Financial Statements and other sections in this Annual Report. The accompanying consolidated financial statements were prepared under the oversight of the Audit Committee of the Board of Directors. For a list of the Audit Committee members, refer to the "Report of the Audit Committee" reflected in this Annual Report. Information in any part of this Annual Report may be incorporated by reference in answer or partial answer to any other item of the Annual Report.

The Association is an institution of the Farm Credit System (System), which was created by Congress in 1916 and has served agricultural producers for over a 100 years. The System's mission is to maintain and improve the income and well-being of American farmers, ranchers, and producers or harvesters of aquatic products and farm-related businesses. The System is the largest agricultural lending organization in the United States. The System is regulated by the Farm Credit Administration, (FCA), which is an independent safety and soundness regulator.

The Association is a cooperative, which is owned by the members (also referred to throughout this Annual Report as stockholders or shareholders) served. The territory of the Association extends across a diverse agricultural region of Virginia, West Virginia and Maryland. Refer to Note 1, *Organization and Operations*, of the Notes to the Consolidated Financial Statements for counties in the Association's territory. The Association provides credit to farmers, ranchers, rural residents, and agribusinesses. Our success begins with our extensive agricultural experience and knowledge of the market.

The Association obtains funding from AgFirst Farm Credit Bank (AgFirst or Bank). The Association is materially affected and shareholder investment in the Association could be affected by the financial condition and results of operations of the Bank. Copies of the Bank's Annual and Quarterly Reports are on the AgFirst website, ***www.agfirst.com,*** or may be obtained at no charge by calling 1-800-845-1745, extension 2832, or writing Susanne Caughman, AgFirst Farm Credit Bank, P. O. Box 1499, Columbia, SC 29202.

Copies of the Association's Annual and Quarterly reports are also available upon request free of charge on the Association's website, **www.farmcreditofvirginias.com**, or by calling 1-540-886-3435, extension 5040, or writing Justin Weekley, Farm Credit of the Virginias, P.O. Box 899, Staunton, VA 24402-0899. The Association prepares an electronic version of the Annual Report, which is available on the website, within 75 days after the end of the fiscal year and distributes the Annual reports to shareholders within 90 days after the end of the fiscal year. The Association prepares an electronic version of the Quarterly report, which is available on the internet, within 40 days after the end of each fiscal quarter, except that no report needs to be prepared for the fiscal quarter that coincides with the end of the fiscal year of the Association.

FORWARD LOOKING INFORMATION

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

- political, legal, regulatory and economic conditions and developments in the United States and abroad;
- economic fluctuations in the agricultural, rural utility, international, and farm-related business sectors;
- weather-related, disease, and other adverse climatic or biological conditions that periodically occur that impact agricultural productivity and income;
- changes in United States government support of the agricultural industry and the Farm Credit System, as a government-sponsored enterprise, as well as investor and rating-agency reactions to events involving other government-sponsored enterprises and other financial institutions; and
- actions taken by the Federal Reserve System in implementing monetary policy.

CRITICAL ACCOUNTING POLICIES

The financial statements are reported in conformity with accounting principles generally accepted in the United States of America. Our significant accounting policies are critical to the understanding of our results of operations and financial position because some accounting policies require us to make complex or subjective judgments and estimates that may affect the value of certain assets or liabilities. We consider these policies critical because management must make judgments about matters that are inherently uncertain. For a complete discussion of

significant accounting policies, see Note 2, *Summary of Significant Accounting Policies*, of the Notes to the Consolidated Financial Statements. The following is a summary of certain critical policies.

- *Allowance for loan losses* — The allowance for loan losses is maintained at a level considered adequate by management to provide for probable and estimable losses inherent in the loan portfolio. The allowance for loan losses is increased through provisions for loan losses and loan recoveries and is decreased through allowance reversals and loan charge-offs. The allowance for loan losses is determined based on a periodic evaluation of the loan portfolio by management in which numerous factors are considered, including economic and political conditions, loan portfolio composition, credit quality and prior loan loss experience.

  Significant individual loans are evaluated based on the borrower's overall financial condition, resources, and payment record, the prospects for support from any financially responsible guarantor, and, if appropriate, the estimated net realizable value of any collateral. The allowance for loan losses encompasses various judgments, evaluations and appraisals with respect to the loans and their underlying security that, by nature, contains elements of uncertainty and imprecision. Changes in the agricultural economy and their borrower repayment capacity will cause these various judgments, evaluations and appraisals to change over time. Accordingly, actual circumstances could vary from the Association's expectations and predictions of those circumstances.

  Management considers the following factors in determining and supporting the levels of allowance for loan losses: the concentration of lending in agriculture, combined with uncertainties in farmland values, commodity prices, exports, government assistance programs, regional economic effects and weather-related influences. Changes in the factors considered by management in the evaluation of losses in the loan portfolios could result in a change in the allowance for loan losses and could have a direct impact on the provision for loan losses and the results of operations.

- *Valuation methodologies* — Management applies various valuation methodologies to assets and liabilities that often involve a significant degree of judgment, particularly when liquid markets do not exist for the particular items being valued. Quoted market prices are referred to when estimating fair values for certain assets for which an observable liquid market exists, such as most investment securities. Management utilizes significant estimates and assumptions to value items for which an observable liquid market does not exist. Examples of these items include impaired loans, other property owned, pension and other postretirement benefit obligations, and certain other financial instruments. These valuations require the use of various assumptions, including, among others, discount rates, rates of return on assets, repayment rates, cash flows, default rates, costs of servicing and liquidation values. The use of different assumptions could produce significantly different results, which could have material positive or negative effects on the Association's results of operations.

ECONOMIC CONDITIONS

During 2018, the general economy continued to grow. On the strength of the economy, the Federal Reserve increased the federal funds rate a quarter of a point four times during the year, pushing mortgage rates higher. Overall, the real estate market including farms and houses continued to experience growth. Part of the strength in the general economy was the job market, where unemployment continued to remain at historically low levels during the year.

Of the major agricultural commodities served by the Association, some farmers experienced a difficult year. Dairy farmers continued to struggle to be profitable as low milk prices continued throughout 2018 which negatively impacted their income. Cattle prices, which experienced improved pricing late in 2017, declined in 2018 negatively impacting cattle farmers profitability. Another year of good weather in the grain producing parts of the United States, kept grain prices in check during the year. The low grain prices continue to help most of our farmers who use feed grain in their operations. Poultry companies slowed expansion efforts which has started to negatively impact farmers with poultry houses in our territory. For the forestry and timber industry, the industry continued to experience a steady demand for lumber and logs, but this demand was negatively impacted by tariffs impacting the industry as a result of continued international trade negotiations.

LOAN PORTFOLIO

The Association loan volume was $1,850,777 at December 31, 2018 compared to $1,844,949 at December 31, 2017, an increase of $5,828 or 0.32 percent. The increase in loan volume was mainly due to an increase in real estate mortgage loans offset somewhat by a decrease in production and intermediate-term loans.

The Association provides funds to farmers, rural homeowners, and farm-related businesses for financing of short and intermediate-term loans and long-term real estate mortgage loans through numerous product types.

The diversification of the Association loan volume by type for each of the past three years is shown below.

Loan Type	December 31, 2018		2017		2016	
	(dollars in thousands)					
Real estate mortgage	$ 1,371,536	74.11 %	$ 1,354,874	73.44 %	$ 1,307,311	72.67 %
Production and intermediate-term	361,652	19.54	374,931	20.32	387,878	21.56
Rural residential real estate	59,716	3.23	52,045	2.82	46,175	2.57
Processing and marketing	33,143	1.79	35,018	1.90	30,144	1.67
Farm-related business	17,993	0.97	20,829	1.13	17,754	0.99
Communication	6,737	0.36	7,252	0.39	9,670	0.54
Loans to cooperatives	–	–	–	–	64	–
Total	$ 1,850,777	100.00 %	$ 1,844,949	100.00 %	$ 1,798,996	100.00 %

While we make loans and provide financial related services to qualified borrowers in the agricultural and rural sectors and to certain related entities, our loan portfolio is diversified.

The geographic distribution of the loan volume by branch/state for the past three years is as follows:

Branch/State	December 31, 2018	2017	2016
Abingdon, VA	7%	7%	7%
Bedford, VA	3	3	3
Charlottesville, VA	3	3	3
Chatham, VA	3	3	3
Clarksburg, WV	2	2	2
Culpeper, VA	6	5	5
Elkins, WV	2	2	2
Gate City, VA	1	1	1
Halifax, VA	2	2	2
Harrisonburg, VA	13	14	14
Leesburg, VA	10	9	9
Lewisburg, WV	2	3	3
Lexington, VA	3	3	3
Moorefield, WV	4	4	4
Oakland, MD	3	2	3
Orange, VA	5	5	5
Ripley, WV	2	3	3
Roanoke, VA	3	3	3
Rocky Mount, VA	3	3	3
Romney, WV	1	2	1
Verona, VA	6	6	6
Warrenton, VA	5	5	5
Wytheville, VA	4	4	4
Agribusiness	5	4	4
Special Assets Group	1	1	2
Participation Loans Purchased	2	2	1
Participation Loans Sold	(1)	(1)	(1)
	100%	100%	100%

The major commodities in the Association's loan portfolio are shown below. The predominant commodities are livestock, field crops, and timber, which constitute 66 percent of the entire portfolio in 2018.

Commodity Group	December 31, 2018		2017		2016	
	(dollars in thousands)					
Livestock	$ 669,272	36%	$ 681,879	37%	$ 655,549	36%
Field Crops	350,015	19	354,285	19	342,287	19
Timber	207,478	11	193,239	11	187,522	11
Dairy	181,696	10	191,616	10	192,293	10
Poultry	171,119	9	167,032	9	156,896	9
Rural Home	61,746	3	54,494	3	47,873	3
Tobacco	20,084	1	23,190	1	22,446	1
Other	189,367	11	179,214	10	194,130	11
Total	$ 1,850,777	100%	$ 1,844,949	100%	$ 1,798,996	100%

Repayment ability is closely related to the commodities produced by our borrowers, and increasingly, the off-farm income of borrowers. The Association's loan portfolio contains a concentration of livestock producers. Although a large percentage of the loan portfolio is concentrated in these commodities, many of these operations are diversified within their enterprise and/or with crop production that reduces overall risk exposure. Demand for beef, prices of field grains, and international trade are some of the factors affecting the prices of these commodities. To proactively reduce overall risk exposure, the concentration of large loans has decreased over the past few years. The agricultural enterprise mix of these loans is diversified and similar to that of the overall portfolio. The risk in the portfolio associated with commodity concentration and large loans is reduced by the range of diversity of enterprises in the Association's territory.

During 2018, the Association continued to buy and sell loan participations within the System. Loan participations provide a means for the Association to spread credit concentration risk and realize non-patronage sourced interest and fee income, which may strengthen its capital position.

Loan Participations:	December 31, 2018	2017	2016
	(dollars in thousands)		
Participations Purchased – FCS Institutions	$ 37,322	$ 31,739	$ 30,091
Participations Sold	(21,261)	(12,662)	(14,897)
Total	$ 16,061	$ 19,077	$ 15,194

The Association did not have any loans sold with recourse, retained subordinated participation interests in loans sold, or interests in pools of subordinated participation interests for the period ended December 31, 2018.

The Association sells qualified long-term mortgage loans into the secondary market. For the period ended December 31, 2018, the Association originated loans for resale totaling $39,672, which were all sold into the secondary market.

MISSION RELATED INVESTMENTS

In October 2005, the FCA authorized AgFirst and the associations to make investments in Rural America Bonds under a three-year pilot period. Rural America Bonds may include debt obligations issued by public and private enterprises, corporations, cooperatives, other financing institutions, or rural lenders where the proceeds would be used to support agriculture, agribusiness, rural housing, or economic

development, infrastructure, or community development and revitalization projects in rural areas. Examples include investments that fund value-added food and fiber processors and marketers, agribusinesses, commercial enterprises that create and maintain employment opportunities in rural areas, community services, such as schools, hospitals, and government facilities, and other activities that sustain or revitalize rural communities and their economies. The objective of this pilot program is to help meet the growing and diverse financing needs of agricultural enterprises, agribusinesses, and rural communities by providing a flexible flow of money to rural areas through bond financing. Effective December 31, 2014, the FCA concluded each pilot program approved as part of the Investment in Rural America Bonds program. Each System institution participating in such programs may continue to hold its investment through the maturity dates for the investments, provided the institution continues to meet all approval conditions. Although the pilot programs ended, the FCA can consider future requests on a case-by-case basis.

The Association did not hold any Rural American Bonds during the period of January 1, 2016, thru December 31, 2018.

CREDIT RISK MANAGEMENT

Credit risk arises from the potential inability of an obligor to meet its repayment obligation. As part of the process to evaluate the success of a loan, the Association continues to review the credit quality of the loan portfolio on an ongoing basis. With the approval of the Association Board of Directors, the Association establishes underwriting standards and lending policies that provide direction to loan officers. Underwriting standards include, among other things, an evaluation of:

- Character – borrower integrity and credit history
- Capacity – repayment capacity of the borrower based on cash flows from operations or other sources of income
- Collateral – protection for the lender in the event of default and a potential secondary source of repayment
- Capital – ability of the operation to survive unanticipated risks
- Conditions – intended use of the loan funds

The credit risk management process begins with an analysis of the borrower's credit history, repayment capacity, and financial position. Repayment capacity focuses on the borrower's ability to repay the loan based upon cash flows from operations or other sources of income, including non-farm income. Real estate loans must be collateralized by first liens on the real estate (collateral). As required by FCA regulations, each institution that makes loans on a collateralized basis must have collateral evaluation policies and procedures. Real estate mortgage loans may be made only in amounts up to 85 percent of the original appraised value of the property taken as collateral or up to 97 percent of the appraised value if guaranteed by a state, federal, or other governmental agency. The actual loan to appraised value when loans are made is generally lower than the statutory maximum percentage. Appraisals are required for loans of more than $250. In addition, each loan is assigned a credit risk rating based upon the underwriting standards. This credit risk rating process incorporates objective and subjective criteria to identify inherent strengths, weaknesses, and risks in a particular relationship.

We review the credit quality of the loan portfolio on an ongoing basis as part of our risk management practices. Each loan is classified according to the Uniform Classification System, which is used by all Farm Credit System institutions. Below are the classification definitions.

- Acceptable – Assets are expected to be fully collectible and represent the highest quality.
- Other Assets Especially Mentioned (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 facts, conditions and values that make collection in full highly questionable.
- Loss – Assets are considered uncollectible.

The following table presents selected statistics related to the credit quality of loans including accrued interest at December 31.

Credit Quality	2018	2017	2016
Acceptable & OAEM	97.67%	97.54%	97.29%
Substandard	2.30%	2.43%	2.68%
Doubtful	0.03%	0.03%	0.03%
Total	100.00%	100.00%	100.00%

Nonperforming Assets

The Association's loan portfolio is divided into performing and high-risk categories. A Special Assets Group is responsible for servicing loans classified as high-risk. The high-risk assets, including accrued interest, are detailed below:

	December 31,		
High-risk Assets	**2018**	**2017**	**2016**
	(dollars in thousands)		
Nonaccrual loans	$ 22,412	$ 31,927	$ 33,578
Restructured loans	1,883	1,649	1,442
Accruing loans 90 days past due	–	55	114
Total high-risk loans	24,295	33,631	35,134
Other property owned	1,477	1,221	2,467
Total high-risk assets	$ 25,772	$ 34,852	$ 37,601
Ratios			
Nonaccrual loans to total loans	1.21%	1.73%	1.87%
High-risk assets to total assets	1.35%	1.83%	2.02%

Nonaccrual loans represent all loans where there is a reasonable doubt as to the collection of principal and/or future interest accruals, under the contractual terms of the loan. In substance, nonaccrual loans reflect loans where the accrual of interest has been suspended. Nonaccrual loans decreased $9,515 or 29.80 percent in 2018. The decrease was mainly due to payments received on loans and loans being reinstated into accruing status offset somewhat by loans being downgrade to nonaccrual status during the year. Of the $22,412 in nonaccrual volume at December 31, 2018, $12,433 or 55.47 percent, compared to 53.45 percent and 63.07 percent at December 31, 2017 and 2016, respectively, was current as to scheduled principal and

interest payments, but did not meet all regulatory requirements to be transferred into accrual status.

Loan restructuring is available to financially distressed borrowers. Restructuring of loans occurs when the Association grants a concession to a borrower based on either a court order or good faith in a borrower's ability to return to financial viability. The concessions can be in the form of a modification of terms or rates, a compromise of amounts owed, or deed in lieu of foreclosure. Other receipts of assets and/or equity to pay the loan in full or in part are also considered restructured loans. The type of alternative financing structure chosen is based on minimizing the loss incurred by both the Association and the borrower.

Other property owned totaled $1,477 at December 31, 2018. This was an increase of $256 as compared to December 31, 2017. The increase was mainly due to several properties being acquired during the year and fewer properties being sold during the year. The Association actively markets these properties in order to sell them.

Allowance for Loan Losses

The allowance for loan losses at each period end was considered by Association management to be adequate to absorb probable losses existing in and inherent to its loan portfolio. The following table presents the activity in the allowance for loan losses for the most recent three years:

	Year Ended December 31,		
Allowance for Loan Losses Activity:	**2018**	**2017**	**2016**
	(dollars in thousands)		
Balance at beginning of year	$ 17,461	$ 14,483	$ 14,487
Charge-offs:			
Real estate mortgage	(225)	(138)	(1,005)
Production and intermediate-term	(4,699)	(492)	(1,677)
Agribusiness	(99)	–	(222)
Rural residential real estate	(12)	–	(80)
Total charge-offs	(5,035)	(630)	(2,984)
Recoveries:			
Real estate mortgage	221	73	147
Production and intermediate-term	163	181	83
Agribusiness	–	104	–
Rural residential real estate	3	–	–
Total recoveries	387	358	230
Net (charge-offs) recoveries	(4,648)	(272)	(2,754)
Provision for (reversal of allowance for) loan losses	2,500	3,250	2,750
Balance at end of year	$ 15,313	$ 17,461	$ 14,483
Ratio of net (charge-offs) recoveries during the period to average loans outstanding during the period	(0.254)%	(0.015)%	(0.159)%

The allowance for loan losses decreased during 2018 which was mainly due to an increase in loans charged off during the year. The 2018 provision for loan losses was recorded in response to an increase in loan volume and financial stress on some accounts in the cattle and dairy sector.

The allowance for loan losses by loan type for the most recent three years is as follows:

	December 31,		
Allowance for Loan Losses by Type	**2018**	**2017**	**2016**
	(dollars in thousands)		
Real estate mortgage	$ 6,142	$ 6,160	$ 6,472
Production and intermediate-term	7,822	10,296	6,989
Agribusiness	980	575	697
Communication	54	80	–
Rural residential real estate	315	350	325
Total Allowance	$ 15,313	$ 17,461	$ 14,483

The allowance for loan losses as a percentage of loans outstanding and as a percentage of certain other credit quality indicators is shown below:

Allowance for Loan Losses	December 31,		
as a Percentage of:	**2018**	**2017**	**2016**
Total loans	0.83%	0.95%	0.81%
Nonaccrual loans	68.33%	54.69%	43.13%

Please refer to Note 3, *Loans and Allowance for Loan Losses*, of the Notes to the Consolidated Financial Statements, for further information concerning the allowance for loan losses and prior years reclassification of loan types as defined by FCA.

RESULTS OF OPERATIONS

The Association's net income was $52,621 for 2018, $56,944 for 2017, and $43,220 for 2016. The decrease in net income for 2018 compared to 2017 was mainly due to an accounting adjustment in postretirement benefits in 2017 that did not reoccur in 2018, and a decrease in the AgFirst patronage refund. The increase in net income for 2017 compared to 2016 was mainly due to an accounting adjustment in postretirement benefits and an increase in the AgFirst patronage refund.

Interest income was $103,008 for 2018, $96,455 for 2017, and $88,990 for 2016. The increase in interest income for 2018 compared to 2017 was mainly due to an increase in loan volume and as a result of the Federal Reserve increasing interest rates, higher interest rates on loans. The increase in interest income for 2017 compared to 2016 was also primarily due to an increase in loan volume during 2017.

Net Interest Income

Net interest income was $57,070 for 2018, $54,197 for 2017 and $51,160 for 2016. Net interest income is the difference between interest income and interest expense. Net interest income is the principal source of earnings for the Association and is impacted by volume, yields on assets and cost of debt. Net interest income increased during 2018 compared to 2017 mainly due to an increase in loan volume and interest rates. The effects of changes in average volume and interest rates on net interest income over the past three years are presented in the following table:

Change in Net Interest Income:

	Volume*	Rate	Nonaccrual Income	Total
	(dollars in thousands)			
12/31/18 - 12/31/17				
Interest income	$ 428	$ 4,162	$ 1,963	$ 6,553
Interest expense	(731)	4,411	–	3,680
Change in net interest income	$ 1,159	$ (249)	$ 1,963	$ 2,873
12/31/17 - 12/31/16				
Interest income	$ 3,062	$ 3,840	$ 563	$ 7,465
Interest expense	1,839	2,589	–	4,428
Change in net interest income	$ 1,223	$ 1,251	$ 563	$ 3,037

* *Volume variances can be the result of increased/decreased loan volume or from changes in the percentage composition of assets and liabilities between periods.*

Noninterest Income

Total noninterest income for the period ended December 31, 2018, totaled $26,063, a decrease of $487 or 1.83 percent, as compared to $26,550 for 2017.

Noninterest income for each of the three years ended December 31 is shown in the following table:

	For the Year Ended December 31,			Increase/(Decrease)	
Noninterest Income	**2018**	**2017**	**2016**	**2018/ 2017**	**2017/ 2016**
	(dollars in thousands)				
Loan fees	$ 822	$ 612	$ 745	$ 210	$ (133)
Fees for financially related services	140	57	68	83	(11)
Patronage refund from other Farm Credit Institutions	22,432	24,833	21,860	(2,401)	2,973
FCS Insurance Corporation Refund	1,673	–	–	1,673	–
Gains (losses) on sales of rural home loans	619	801	851	(182)	(50)
Gains (losses) on sales of premises and equipment, net	301	86	55	215	31
Gains (losses) on other transactions	4	61	55	(57)	6
Other noninterest income	72	100	81	(28)	19
Total noninterest income	$ 26,063	$ 26,550	$ 23,715	$ (487)	$ 2,835

Income from loan fees decreased during 2018 compared to 2017 mainly due to a decrease in loan fees on loans sold into the secondary mortgage market.

The patronage refund from other Farm Credit Institutions decreased 10% for 2018 when compared to 2017. The patronage refund, which was from AgFirst, decreased $2,401 compared to last year. The decrease was due to AgFirst decreasing its special additional patronage refund paid to the Association. For 2018, the special patronage refund was $11,666. For 2017 and 2016, special patronage refund was $13,811 and $8,943, respectively. AgFirst paid the special patronage refunds due to its strong financial position.

Noninterest Expense

Total noninterest expense increased $7,468 or 36.42 percent for the year ended December 31, 2018, as compared to the same period for 2017.

Noninterest expense for each of the three years ended December 31 is shown in the following table:

	For the Year Ended December 31,			Increase/(Decrease)	
Noninterest Expense	**2018**	**2017**	**2016**	**2018/ 2017**	**2017/ 2016**
	(dollars in thousands)				
Salaries and employee benefits	$ 13,269	$ 13,757	$ 13,337	$ (488)	$ 420
Postretirement benefits	4,510	(4,114)	5,086	8,624	(9,200)
Occupancy and equipment	1,369	1,408	1,369	(39)	39
Insurance Fund premiums	1,272	2,143	2,316	(871)	(173)
(Gains) losses on other property owned, net	71	615	286	(544)	329
Other operating expenses	7,481	6,695	6,473	786	222
Total noninterest expense	$ 27,972	$ 20,504	$ 28,867	$ 7,468	$ (8,363)

Salaries and employee benefits decreased for 2018 compared to 2017 mainly due to decreases in discretionary compensation and increases in deferred origination costs, offset by an increase in employees' salaries. Postretirement benefits increased by $8,624. The increase in postretirement benefits was due to a one time adjustment recorded in 2017. Refer to Note 9, *Employee Benefit Plans*, for more information concerning the adjustment.

Insurance Fund premiums decreased $871 for 2018 compared to 2017 primarily due to lower premium assessment rate for 2018 compared to 2017.

Income Taxes

The Association recorded a provision for income taxes of $40 for the year ended December 31, 2018, as compared to a provision for income taxes of $49 for 2017 and a provision of $38 for 2016. Refer to Note 2, *Summary of Significant Accounting Policies*, and Note 12, *Income Taxes*, of the Notes to the Consolidated Financial Statements, for more information concerning Association income taxes.

Key Results of Operations Comparisons

Key results of operations comparisons for each of the twelve months ended December 31 are shown in the following table:

Key Results of	For the 12 Months Ended		
Operations Comparisons	**12/31/18**	**12/31/17**	**12/31/16**
Return on average assets	2.81%	3.04%	2.43%
Return on average members' equity	11.97%	13.89%	11.25%
Net interest income as a percentage of average earning assets	3.11%	2.96%	2.95%
Net (charge-offs) recoveries to average loans	(0.254)%	(0.015)%	(0.159)%

The decrease in net income for 2018 drove the return on average assets and return on average members' equity lower when compared to last year.

LIQUIDITY AND FUNDING SOURCES

Liquidity and Funding

The principal source of funds for the Association is the borrowing relationship established with the Bank through a General Financing Agreement (GFA). The GFA utilizes the Association's credit and fiscal performance as criteria for establishing a line of credit on which the Association may draw funds. The Bank advances the funds to the Association, creating notes payable (or direct loans) to the Bank. The Bank manages interest rate risk through direct loan pricing and asset/liability management. The notes payable are segmented into variable rate and fixed rate components. The variable rate note is utilized by the Association to fund variable rate loan advances and operating funds requirements. The fixed rate note is used specifically to fund fixed rate loan advances made by the Association. Association capital levels effectively create a borrowing margin between the amount of loans outstanding and the amount of notes payable outstanding. This margin is commonly referred to as "Loanable Funds."

Total notes payable to the Bank at December 31, 2018, was $1,422,676 as compared to $1,437,895 at December 31, 2017 and $1,423,922 at December 31, 2016. The average volume of outstanding notes payable to the Bank was $1,410,860 and $1,435,700 for the years ended December 31, 2018 and 2017, respectively. Refer to Note 6, *Notes Payable to AgFirst Farm Credit Bank*, of the Notes to the Consolidated Financial Statements, for weighted average interest rates and maturities, and additional information concerning the Association's notes payable.

Liquidity management is the process whereby funds are made available to meet all financial commitments including the extension of credit, payment of operating expenses and payment of debt obligations. The Association receives access to funds through its borrowing relationship with the Bank and from income generated by operations. The liquidity policy of the Association is to manage cash balances to maximize debt reduction and to increase loan volume. As borrower payments are received, they are applied to the Association's note payable to the Bank. The Association's participation in the Farmer Mac, investments, and other secondary market programs provides additional liquidity. Sufficient liquid funds have been available to meet all financial obligations. There are no known trends likely to result in a liquidity deficiency for the Association. The Association did not have any lines of credit from third party financial institutions as of December 31, 2018.

On January 16, 2019, the Bank approved a waiver of the Association's event of default under the GFA.

Funds Management

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

Demand for loan types is a driving force in establishing a funds management strategy. The Association offers fixed, adjustable and variable rate loan products that are marginally priced according to financial market rates. Variable rate loans may be indexed to market indices such as the Prime Rate or the 90-day London Interbank Offered Rate (LIBOR). Adjustable rate mortgages are indexed to U.S. Treasury Rates. Fixed rate loans are priced based on the current cost of System debt of similar terms to maturity.

The majority of the interest rate risk in the Association's Consolidated Balance Sheets is transferred to the Bank through the notes payable structure. The Bank, in turn, actively utilizes funds management techniques to identify, quantify and control risk associated with the loan portfolio.

Relationship with the Bank

The Association's statutory obligation to borrow only from the Bank is discussed in Note 6, *Notes Payable to AgFirst Farm Credit Bank*, of the Notes to the Consolidated Financial Statements in this Annual Report.

The Bank's ability to access capital of the Association is discussed in Note 4, *Investment in Other Farm Credit Institutions*, of the Notes to the Consolidated Financial Statements in this Annual Report.

The Bank's role in mitigating the Association's exposure to interest rate risk is described in the "Liquidity and Funding" section of this Management's Discussion and Analysis and in Note 6, *Notes Payable to AgFirst Farm Credit Bank*, included in this Annual Report.

CAPITAL RESOURCES

Capital serves to support asset growth and provide protection against unexpected credit and interest rate risk and operating losses. Capital is also needed for future growth and investment in new products and services.

The Association Board of Directors establishes, adopts, and maintains a formal written capital adequacy plan to ensure that adequate capital is maintained for continued financial viability, to provide for growth necessary to meet the needs of members/borrowers, and to ensure that all stockholders are treated equitably. There were no material changes to the capital plan for 2018 that would affect minimum stock purchases or would have an effect on the Association's ability to retire stock and distribute earnings.

Members' equity at December 31, 2018, totaled $440,378, an increase of $17,557 or 4.15 percent compared to $422,821 at December 31, 2017. At December 31, 2017, total members' equity increased 8.19 percent from the December 31, 2016 total of $390,823. The increase was primarily attributed to the earnings of the Association offset by the cash profit-sharing distribution (patronage dividend) to the Association's member-stockholders. The Association plans to distribute approximately $30 million of its 2018 net income in cash to its member-stockholders during the second quarter of 2019.

Total capital stock and participation certificates were $10,426 on December 31, 2018, compared to $10,493 on December 31, 2017 and $10,433 on December 31, 2016.

FCA sets minimum regulatory capital requirements for System Banks and associations. Capital adequacy is evaluated using a number of regulatory ratios. Effective January 1, 2017, the regulatory capital requirements for System Banks and associations were modified. The new regulations ensure that the System's capital requirements are comparable to the Basel III framework and the standardized approach that the federal banking regulatory agencies have adopted. New regulations replaced core surplus and total surplus ratios with common equity tier 1 (CET1) capital, tier 1 capital, and total capital risk-based capital ratios. The new regulations also include a tier 1 leverage ratio and an unallocated retained earnings equivalents (UREE) leverage ratio. The permanent capital ratio (PCR) remains in effect.

Risk-adjusted assets have been defined by FCA Regulations as the Balance Sheet assets and off-balance-sheet commitments adjusted by various percentages, depending on the level of risk inherent in the various types of assets. The primary changes which generally have the effect of increasing risk-adjusted assets (decreasing risk-based regulatory capital ratios) were as follows:

- Inclusion of off-balance-sheet commitments less than 14 months
- Increased risk-weighting of most loans 90 days past due or in nonaccrual status

Calculation of PCR risk-adjusted assets includes the allowance for loan losses as a deduction from risk-adjusted assets. This differs from the other risk-based capital calculations.

The ratios are calculated using three-month average daily balances, in accordance with FCA regulations, as follows:

- The CET1 capital ratio is the sum of statutory minimum purchased borrower stock, other required borrower stock held for a minimum of 7 years, allocated equities held for a minimum of 7 years or not subject to revolvement, unallocated retained earnings, paid-in capital, less certain regulatory required deductions including the amount of investments in other System institutions, divided by average risk-adjusted assets.
- The tier 1 capital ratio is CET1 capital plus non-cumulative perpetual preferred stock, divided by average risk-adjusted assets.
- The total capital ratio is tier 1 capital plus other required borrower stock held for a minimum of 5 years, subordinated debt and limited-life preferred stock greater than 5 years to maturity at issuance subject to certain limitations, allowance for loan losses and reserve for unfunded commitments under certain limitations less certain investments in other System institutions under the corresponding deduction approach, divided by average risk-adjusted assets.
- The permanent capital ratio is all at-risk borrower stock, any allocated excess stock, unallocated retained earnings, paid-in capital, subordinated debt and preferred stock subject to certain limitations, less certain investments in other System institutions, divided by PCR risk-adjusted assets.
- The tier 1 leverage ratio is tier 1 capital, divided by average assets less regulatory deductions to tier 1 capital.
- The UREE leverage ratio is unallocated retained earnings, paid-in capital, and allocated surplus not subject to revolvement less certain regulatory required deductions including the amount of allocated investments in other System institutions divided by average assets less regulatory deductions to tier 1 capital.

The following sets forth the regulatory capital ratios which were effective January 1, 2017:

Ratio	Minimum Requirement	Capital Conservation Buffer*	Minimum Requirement with Capital Conservation Buffer	Capital Ratios as of December 31, 2018	Capital Ratios as of December 31, 2017
Risk-adjusted ratios:					
CET1 Capital Ratio	4.5%	1.25%	5.75%	22.30%	20.93%
Tier 1 Capital Ratio	6.0%	1.25%	7.25%	22.30%	20.93%
Total Capital Ratio	8.0%	1.25%	9.25%	23.10%	21.72%
Permanent Capital Ratio	7.0%	0.0%	7.0%	22.48%	21.09%
Non-risk-adjusted:					
Tier 1 Leverage Ratio	4.0%	1.0%	5.0%	22.84%	21.41%
UREE Leverage Ratio	1.5%	0.0%	1.5%	23.07%	21.59%

** The capital conservation buffers have a 3 year phase-in period and will become fully effective January 1, 2020. Risk-adjusted ratio minimums will increase 0.625% each year until fully phased in. There is no phase-in period for the tier 1 leverage ratio.*

If the capital ratios fall below the minimum regulatory requirements, including the buffer amounts, capital distributions (equity redemptions, dividends, and patronage) and discretionary senior executive bonuses are restricted or prohibited without prior FCA approval.

The following sets forth regulatory Capital ratios as previously reported:

	Regulatory Minimum	2016	2015	2014	2013	2012
Permanent Capital Ratio	7.00%	20.75%	20.07%	19.91%	19.88%	16.95%
Total Surplus Ratio	7.00%	20.08%	19.29%	19.15%	18.68%	15.73%
Core Surplus Ratio	3.50%	20.08%	19.29%	19.15%	18.68%	15.73%

There are no trends, commitments, contingencies, or events that are likely to affect the Association's ability to meet regulatory minimum capital standards and capital adequacy requirements. See Note 7, *Members' Equity*, of the Notes to the Consolidated Financial Statements, for further information concerning capital resources.

PATRONAGE PROGRAM

Prior to the beginning of any fiscal year, the Association's Board of Directors, by adoption of a resolution, may establish a Patronage Allocation Program to distribute its available consolidated net earnings. This resolution provides for the application of net earnings in the manner described in the Association's Bylaws. This includes the setting aside of funds to increase surplus to meet minimum capital adequacy standards established by FCA Regulations, to increase surplus to meet Association capital adequacy standards to a level necessary to support competitive pricing at targeted earnings levels, and for reasonable reserves for necessary purposes of the Association. After excluding net earnings attributable to (a) the portion of loans participated to another institution, and (b) participation loans purchased, remaining consolidated net earnings are eligible for allocation to borrowers. Refer to Note 7, *Members' Equity*, of the Notes to the Consolidated Financial Statements, for more information concerning the patronage distributions.

YOUNG, BEGINNING AND SMALL (YBS) FARMERS AND RANCHERS PROGRAM

The Association's mission is to provide financial services to agriculture and the rural community, which includes providing credit to Young*, Beginning** and Small*** farmers. Because of the unique needs of these individuals, and their importance to the future growth of the Association, the Association has established annual marketing goals to increase our market share of loans to YBS farmers. Specific marketing plans have been developed to target these groups, and resources have been designated to help ensure YBS borrowers have access to a stable source of credit.

The following table outlines the loan volume and number of YBS loans in the loan portfolio for the Association.

	As of December 31, 2018	
(dollars in thousands)	Number of Loans	Amount of Loans
Young	2,480	$251,598
Beginning	4,042	$470,624
Small	10,953	$1,077,946

Note: For purposes of the above table, a loan could be classified in more than one category, depending upon the characteristics of the underlying borrower.

The 2012 USDA Ag census data has been used as a benchmark to measure penetration of the Association's marketing efforts. The Association currently has a high penetration in the Young, Beginning, and Small farm market. As of December 31, 2018, the Association was doing business with 83 percent of the Young farmers, 36 percent of the Beginning farmers, and 17 percent of Small farmers identified by the 2012 Ag census.

The following strategies and outreach programs have been conducted which allowed the Association to meet its objectives and goals in the young, beginning, and small farmer program:

- Began in 2011, the sponsorship of the Ag Biz Planner financial training program for YBS farmers. This has continued each year through 2018 with a total of 106 participants completing the program since its inception. In 2018, sponsored trip for 3 participants to visit Congress in Washington D.C.

- Began in 2014, the initiation of a Knowledge Center. This provides educational opportunities and resources for all farmers including YBS farmers.
- In 2015, initiate new "Farm Launch" program that is designed primarily for YBS farmers.
- Support of 4-H, FFA, and Young farmer organizations through sponsorships and donations.
- Sponsor and host, two, one-day, Farm Management Institute seminars; these are facilitated by nationally recognized agricultural business consultant, Dr. David Kohl. Total attendance was 127 in 2018.
- Sponsor and host, online Farm Transition and Succession Planning Webinar Series; this series was facilitated by university professors throughout the association footprint.
- Support Young and Beginning farmers through many youth programs including a Youth Loan program.
- Support numerous trade shows and conferences that benefit YBS borrowers.

The Association is committed to the future success of Young, Beginning and Small farmers.

* Young farmers are defined as those farmers, ranchers, producers or harvesters of aquatic products who are age 35 or younger as of the date the loan is originally made.

** Beginning farmers are defined as those farmers, ranchers, producers or harvesters of aquatic products who have 10 years or less farming or ranching experience as of the date the loan is originally made.

*** Small farmers are defined as those farmers, ranchers, producers or harvesters of aquatic products who normally generate less than $250 in annual gross sales of agricultural or aquatic products at the date the loan is originally made.

REGULATORY MATTERS

On May 10, 2018, the Farm Credit Administration adopted a final rule that amends the regulations governing investments of System banks and associations. The final rule strengthens eligibility criteria for the investments the banks may purchase and hold. It also implements Section 939A of the Dodd-Frank Act by removing references to and requirements for credit ratings and substitutes the eligibility requirement with other appropriate standards of credit worthiness. In addition, it grants associations greater flexibility regarding the risk management purposes for investments and limits the type and amount of investments that an association may hold. Only securities that are issued by, or are unconditionally guaranteed or insured as to the timely payment of principal and interest by, the U.S. government or its agencies are eligible for association risk management purposes. An association may purchase and hold investments not to exceed 10 percent of its 90-day average daily balance of outstanding loans on the last business day of the quarter. The final rule became effective January 1, 2019.

Farm Bill

The Agricultural Improvement Act of 2018 (Farm Bill) was signed into law on December 20, 2018. This new Farm Bill will govern an array of federal farm and food programs, including commodity price support payments, farm credit, conservation programs, research, rural development and foreign and domestic food programs for five years through 2023. The new Farm Bill continues to provide support for crop insurance and commodity support programs, strengthen livestock disaster programs, and provides dairy producers with an updated voluntary margin protection program that will provide additional risk management options to dairy operations.

The Farm Bill also clarifies and updates the Insurance Corporation's authorities to act as conservator or receiver of a System institution. The Congressional Conference Committee report states that Congress intends "for the authorities of the Corporation to be functionally equivalent to the parallel authorities of the Federal Deposit Insurance Corporation." In addition, the Farm Bill provides, among other authorities, the Insurance Corporation with the authority to organize, and the Farm Credit Administration to charter, a System bridge bank, which has all the powers of a System bank with a maximum life span of five years.

Many provisions of the Farm Bill will require the United States Department of Agriculture to develop rules and procedures to fully implement these authorities. The timing for the issuance of those rules is uncertain.

LIBOR TRANSITION

On July 27, 2017, the United Kingdom Financial Conduct Authority (the Conduct Authority) announced that it will no longer persuade or compel such banks to submit rates for the calculation of the LIBOR rates after 2021. The Conduct Authority regulates the panel banks that submit quotes for the purpose of calculating LIBOR to the Intercontinental Exchange (ICE) Benchmark Administration (the entity that is responsible for calculating LIBOR). Accordingly, it is uncertain whether the ICE Benchmark Administration will continue to quote LIBOR after 2021. Furthermore, in the United States, efforts to identify a set of alternative U.S. dollar reference interest rates include proposals by the Alternative Reference Rates Committee (ARRC) of the Federal Reserve Board and the Federal Reserve Bank of New York. Specifically, the ARRC has proposed the Secured Overnight Financing Rate (SOFR) as the recommended alternative to LIBOR and the Federal Reserve Bank of New York began publishing SOFR in April of 2018. SOFR is based on a broad segment of the overnight Treasury repurchase market and is a broad measure of the cost of borrowing cash overnight collateralized by Treasury securities.

At this time, it is not possible to predict, among other uncertainties, whether (i) LIBOR will be discontinued, (ii) the effect of any changes to the methodology for calculating LIBOR, or (iii) any establishment of alternative reference rates or any other reforms to LIBOR that may be enacted in the United Kingdom, in the United States or elsewhere. Uncertainty as to the nature of such potential changes, alternative reference rates or other reforms may adversely affect the trading market for LIBOR based instruments, including certain of the Systemwide Debt Securities, System borrowings, loans, investments, derivatives, other System assets and liabilities and preferred stock that are indexed to LIBOR. Accordingly, reform of, or the replacement or disappearance of, LIBOR and the proposed regulation of LIBOR and other "benchmarks" may adversely affect the rates of interest the System pays on its

Systemwide Debt Securities (including changes to their value and liquidity, return, and usefulness for intended purpose), on other borrowings and preferred stock, as well as the value of and return on loans and investments and the value and effectiveness of derivatives. This could adversely affect the System's cash flows. Moreover, if LIBOR is replaced, System institutions will need to take steps to restructure their debt and derivatives, which could adversely affect operations.

The System institutions are currently evaluating the potential impact of the eventual replacement of the LIBOR benchmark interest rate, including the possibility of using SOFR as the alternative to LIBOR. While each system institution is required by the regulator to have a transition plan, the transition from LIBOR to SOFR is expected to be complex and to include the development of term and credit adjustments to minimize, to the extent possible, discrepancies between LIBOR and SOFR. Accordingly, the transition may introduce additional basis risk for market participants, including when an alternative index, e.g., SOFR, exists in conjunction with LIBOR. There can be no guarantee that SOFR will become the dominant alternative to U.S. dollar LIBOR or that SOFR will be widely used. In addition, other alternatives may or may not be developed with additional complications.

Changes in LIBOR may result in interest rates and/or payments that are higher or lower than, or that do not otherwise correlate over time with, the interest rates and/or payments that would have been associated with LIBOR-based Systemwide Debt Securities, or loans or investments that are based on LIBOR, which may increase or decrease the payments to be made on such LIBOR-based Systemwide Debt Securities, or loans or investments that are based on LIBOR.

RECENTLY ISSUED ACCOUNTING PRONOUNCEMENTS

The following Accounting Standards Updates (ASUs) were issued by the Financial Accounting Standards Board (FASB) but have not yet been adopted:

The following Accounting Standards Updates (ASUs) were issued by the Financial Accounting Standards Board (FASB) but have not yet been adopted:

Summary of Guidance	Adoption and Potential Financial Statement Impact
ASU 2016-13 – Financial Instruments – Credit Losses (Topic 326): Measurement of Credit Losses on Financial Instruments	
• Replaces multiple existing impairment standards by establishing a single framework for financial assets to reflect management's estimate of current expected credit losses (CECL) over the complete remaining life of the financial assets. • Changes the present incurred loss impairment guidance for loans to a CECL model. • The Update also modifies the other-than-temporary impairment model for debt securities to require an allowance for credit impairment instead of a direct write-down, which allows for reversal of credit impairments in future periods based on improvements in credit. • Eliminates existing guidance for purchased credit impaired (PCI) loans, and requires recognition of an allowance for expected credit losses on these financial assets. • Requires a cumulative-effect adjustment to retained earnings as of the beginning of the reporting period of adoption. • Effective for fiscal years beginning after December 15, 2020, and interim periods within those fiscal years. Early application will be permitted for fiscal years, and interim periods within those fiscal years, beginning after December 15, 2018.	• The Association has begun implementation efforts by establishing a cross-discipline governance structure and will implement a third-party model. The Association is currently identifying key interpretive issues and assessing processes against the new guidance to determine what modifications may be required. • The Association expects that the new guidance will result in an increase in its allowance for credit losses due to several factors, including: 1. The allowance related to loans and commitments will most likely increase to cover credit losses over the full remaining expected life of the portfolio, and will consider expected future changes in macroeconomic conditions, 2. An allowance will be established for estimated credit losses on any debt securities, 3. The nonaccretable difference on any PCI loans will be recognized as an allowance, offset by an increase in the carrying value of the related loans. • The extent of the increase is under evaluation, but will depend upon the nature and characteristics of the Association's portfolio at the adoption date, and the macroeconomic conditions and forecasts at that date. • The Association expects to adopt the guidance in first quarter 2021.
ASU 2016-02 – Leases (Topic 842)	
• Requires lessees to recognize leases on the balance sheet with lease liabilities and corresponding right-of-use assets based on the present value of lease payments. • Lessor accounting activities are largely unchanged from existing lease accounting. • The Update also eliminates leveraged lease accounting but allows existing leveraged leases to continue their current accounting until maturity, termination or modification. • Also, expands qualitative and quantitative disclosures of leasing arrangements. • Requires adoption using a modified cumulative-effect approach wherein the guidance is applied to all periods presented. A recent amendment provides an additional (and optional) transition method to adopt the new leases standard. Under this new transition method, an entity initially applies the new leases standard at the adoption date and recognizes a cumulative-effect adjustment to the opening balance of retained earnings in the period of adoption. • Effective for fiscal years beginning after December 15, 2018, including interim periods within those fiscal years. Early adoption is permitted.	• The practical expedients allow entities to largely account for existing leases consistent with current guidance, except for the incremental balance sheet recognition for lessees. • The Association completed its evaluation of leasing contracts and activities and developed its methodology to estimate the right-of-use assets and lease liabilities, which is based on the present value of lease payments. There will not be a material change to the timing of expense recognition. • Given the limited changes to lessor accounting, there were no material changes to recognition or measurement for the Association. • The Association will need to provide additional disclosure information as a result of adopting the Update. • The Association will adopt the guidance in first quarter 2019 using the optional modified retrospective method and practical expedients for transition. • Upon adoption, the Association will record a cumulative-effect adjustment of approximately $0. In addition, a Right of Use Asset in the amount of $287 and Lease Liability in the amount of $287 will be recorded.

Disclosure Required by Farm Credit Administration Regulations

Description of Business

Descriptions of the territory served, persons eligible to borrow, types of lending activities engaged in, financial services offered and related Farm Credit organizations are incorporated herein by reference to Note 1, *Organization and Operations*, of the Consolidated Financial Statements included in this Annual Report to shareholders.

The description of significant developments that had or could have a material impact on earnings or interest rates to borrowers, acquisitions or dispositions of material assets, material changes in the manner of conducting the business, seasonal characteristics, and concentrations of assets, if any, is incorporated in "Management's Discussion and Analysis of Financial Condition and Results of Operations" included in this Annual Report.

Description of Property

The following table sets forth certain information regarding the properties of the reporting entity, all of which are located in Virginia, West Virginia and Maryland:

Location	Description	Form of Ownership
106 Sangers Lane Staunton, VA	Administrative	Owned
19292 Lee Highway Abingdon, VA	Branch	Owned
1356-B American Way Court Bedford, VA	Branch	Rented *($1,600 per month)*
1445 E. Rio Road Suite 103 Charlottesville, VA	Branch	Rented *($2,262 per month)*
19651 US Highway 29 Chatham, VA	Branch	Owned
4579 Buckhannon Pike Suite 102 Clarksburg, WV	Branch	Rented *($2,586 per month)*
15574 Ira Hoffman Lane Culpeper, VA	Branch	Owned
308 Railroad Avenue Elkins, WV	Branch	Rented *($650 per month)*
268 E. Jackson Street Gate City, VA	Branch	Owned
161 South Main Street Halifax, VA	Branch	Rented *($531 per month)*
4646 South Valley Pike Harrisonburg, VA	Branch	Owned
306 East Market Street Harrisonburg, VA	Processing Center	Owned
27 Fort Evans Road, NE Leesburg, VA	Branch	Owned
880 North Jefferson Street Lewisburg, WV	Branch	Owned
152 Maury River Road Lexington, VA	Branch	Owned
550 South Main Street Moorefield, WV	Branch	Owned
13195 Garrett Highway Oakland, MD	Branch	Owned
13284 James Madison Hwy Orange, VA	Branch	Rented *($1,575 per month)*
2112 Ripley Road Ripley, WV	Branch	Rented *($3,150 per month)*
38 Murray Farm Road Roanoke, VA	Branch	Owned
670 Old Franklin Turnpike Rocky Mount, VA	Branch	Owned
452 North High Street Romney, WV	Branch	Owned
1557 Commerce Road Suite 202 Verona, VA	Branch	Rented *($1,850 per month)*
516 Fauquier Road Warrenton, VA	Branch	Owned
660 Pepper's Ferry Road Wytheville, VA	Branch	Owned

Legal Proceedings

Information, if any, to be disclosed in this section is incorporated herein by reference to Note 11, *Commitments and Contingencies*, of the Consolidated Financial Statements included in this Annual Report.

Description of Capital Structure

Information to be disclosed in this section is incorporated herein by reference to Note 7, *Members' Equity*, of the Consolidated Financial Statements included in this Annual Report.

Description of Liabilities

The description of liabilities, contingent liabilities and intrasystem financial assistance rights and obligations to be disclosed in this section is incorporated herein by reference to Notes 2, 6, 9 and 11 of the Consolidated Financial Statements included in this Annual Report.

Description of Unincorporated Business Entities

The Association holds an equity investment at December 31 2018, in the following Unincorporated Business Entity (UBE) as an equity interest holder of the limited liability company (LLC). The LLC was organized for the stated purpose of holding and managing unusual or complex collateral associated with former loans, until such time as the assets may be sold or otherwise disposed of pursuant to the terms of the Operating Agreements of the respective LLC.

Entity Name	Entity Purpose
Ethanol Holdings, LLC	Manage Acquired Property

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

"Management's Discussion and Analysis of Financial Condition and Results of Operations," which appears in this Annual Report and is to be disclosed in this section, is incorporated herein by reference.

Senior Officers

The following represents certain information regarding the senior officers of the Association at December 31, 2018 and their business experience for the past 5 years.

Senior Officer	Position
C. Peery Heldreth, III	*Chief Executive Officer,* since January, 2017. He had previously served as Chief Relationship Officer since 2012 and as Regional Sales and Lending Manager. He serves on the Virginia Agribusiness Council Board, Virginia Tech's VALOR Advisory Council, and the West Virginia University's Board of Visitors for the Davis College of Agriculture, Natural Resources and Design.
Kelly S. Bohrer	*Chief Operations Officer,* since November, 2016. She had previously served at MidAtlantic Farm Credit as their Senior Vice President of Loan Operations since November, 2014, adding role of Chief Credit Officer, in March 2016. Prior roles included Senior Vice President and Regional Lending Manager, and Credit Analyst for MidAtlantic Farm Credit.
A. Katie Frazier	*Director of External Affairs,* since May 2018. She has 14 years of public affairs experience at the state and federal level.
Teresa A. Harris	*Business Development Officer* since January, 2017. She had previously served as Regional Sales and Lending Officer.
Michael S. Jonas	*Director of Sales and Marketing* since January, 2017. He had previously served as Regional Sales and Lending Officer and as Business Line Leader.
M. Kay Manchester	*Chief Training and Human Resource Officer* since 2006.
Al P. Saufley	*Chief Lending Officer* since 2012 and had previously served as Business Line Leader and as Director of Risk Management and Underwriting.
Justin J. Weekley	*Chief Financial Officer* since October 2018. He previously spent 9 years in public accounting.

Compensation Overview

The Association's compensation philosophy is to pay for performance that supports the Association's short-term and long-term business strategies and enhances the member-shareholders' value in the Association. The overall compensation programs which include base salary, incentive compensation and retirement benefits, are designed to offer competitive pay opportunities to employees and enable the Association to effectively attract, retain and motivate highly qualified employees.

The compensation programs for senior officers include both fixed and variable compensation components. The mix of fixed and variable components is designed to balance the need to motivate senior management and employees to find new business opportunities and to promote the Association's mission to ensure a safe, sound, and dependable source of credit for agriculture and rural America. The fixed component of compensation is the annual salary. The variable component of compensation is an incentive program. The incentive program is designed to promote pay for performance while balancing the needs of the Association to manage risk and promote sound credit decisions. The incentive compensation is paid in two parts. Part of the incentive is paid to employees shortly after the end of the year. This part is referred to as the short-term incentive. The remaining component of the incentive is paid after the completion of three more years and this is the long-term incentive.

The Chief Executive Officer (CEO) and the Internal Audit employees do not participate in the incentive program. Instead the Board of Directors, at its discretion, may award a bonus. Historically, the Board of Directors has used the results of the senior officers' short-term and long-term incentive plan to determine the payout amount.

Salary. The CEO, senior officers and all employees of the Association have a base salary as part of their compensation program. The base salary is determined based on position, responsibilities and performance. The Association strives to provide employees with base salaries that are competitive with respect to the position, as identified in compensation surveys conducted by external compensation consultants, and the need to maintain careful control of salaries and benefits expense. The Board of Directors has delegated the base salaries administration for senior officers to the CEO. The CEO's base salary is reviewed and approved by the Board of Directors.

Short-Term Incentives. The Association provides short-term incentive programs for senior officers and eligible employees. The short-term incentive programs are designed to promote new business development, increased loan volume and revenue growth, and increased Association's net income. These financial measures were selected since they align with our mission and enhance the Association's ability to pay a patronage refund to our member-stockholders. The senior officers' short-term incentive is based on the performance of the sales and lending team. Performance of the sales and lending team is based on the production of loans made during the year and the number of new customers who joined the Association. The senior officers' short term incentive is reduced if key financial business goals are below established targets. The short-term incentive programs are reviewed and approved annually by the Board of Directors.

The short-term incentive for 2018 was expensed during 2018 with the payment to be made in the first quarter of 2019.

Long-term Incentives. The Association provides a long-term incentive program for senior officers. The long-term incentive plan is designed to motivate and reward the senior officers to meet and exceed financial and performance goals of the Association. The financial and performance goals are return on equity, return on assets, loan portfolio credit quality, loan delinquency rate, and level of nonaccrual loan volume. These performance areas are weighted equally. A target goal is set for each financial and performance goal. The incentive amount is determined by the Association's performance compared to the goals. The long-term incentive for 2018 will be paid during the first quarter of 2022. The payment can be reduced if the financial and performance results for the last year, 2021, are less than the target goals in the 2017 long-term incentive program. Since the 2018 long-term incentive will be paid out after three years, it will be expensed equally over the next three years. The long-term incentive program is reviewed and approved by the Board of Directors.

Retirement benefits. The Association provides retirement benefits to the CEO, senior management and employees to offer a competitive compensation program.

Employees hired before January 1, 2003, participate in the AgFirst Farm Credit Retirement Plan. The plan is an employer-funded qualified defined benefit pension plan. Benefits under this plan are determined by a formula based on years of service and eligible compensation. Employees are eligible to retire and begin receiving unreduced pension benefits at age 65 or when years of service plus age equal "85". Upon retirement, annual payout is equal to 2.0 percent of the highest three years of average salary, not including incentives, times years of credited service, subject to the Internal Revenue Code limitations.

Employees hired on or after January 1, 2003, but prior to November 4, 2014, participated in the AgFirst Farm Credit Cash Balance Retirement Plan. This plan was a qualified defined contribution pension plan. The plan was terminated as of December 31, 2017 and vested benefits of the plan were distributed to plan participants in 2017.

All employees may participate in the Farm Credit Benefits Alliance 401(k) Plan, a qualified 401(k) defined contribution plan that has employer matching contribution determined by the employee's date of hire. Employees hired prior to January 1, 2003 receive a maximum employer matching contribution equal to $0.50 for each $1.00 of employee compensation contributed up to 6.0 percent, subject to the Internal Revenue Code limitation on compensation. Employees hired on or after January 1, 2003, receive a maximum employer matching contribution equal to $1.00 for each $1.00 of employee compensation contributed up to 6.0 percent, and employer nonelective contribution equal to 3.0 percent of employee compensation, subject to the Internal Revenue Code limitation on compensation.

Senior officers and other highly compensated employees may participate in the Farm Credit Benefits Alliance Nonqualified Supplemental 401(k) plan, a non-qualified deferred compensation plan. The purpose of the plan is to allow these employees to defer income taxes on a portion of their compensation until retirement or separation from the Association and to restore benefits limited in the qualified 401(k) plan as a result of restrictions in the Internal Revenue Code. The plan includes a provision for discretionary contributions by the Association.

Employees who choose to defer a portion of their compensation may defer part or all of their base salary, short term incentive, and long term incentive and or bonus. This is shown under the deferred compensation column in the Summary of Compensation table below.

The following Summary of Compensation table includes compensation paid to the CEO and the senior officers and highly compensated individuals as a group, excluding the CEO, during the years ended December 31, 2018, 2017 and 2016:

Name of CEO	Year	Salary	Bonus Short Term	Bonus Long term	Deferred Comp.	Change in Pension Value (1)	Perq/ Other(2)	Total
C. Peery Heldreth, III, CEO	2018	$ 367,500	$ –	$ 73,500	$ –	$ 48,164	$ 12,609	$ 501,773
C. Peery Heldreth, III, CEO	2017	$ 317,929	$ 31,793	$ 63,586	$ –	$ 282,859	$ 6,082	$ 702,249
David E. Lawrence, CEO	2017	$ 102,838	$ 28,606	$ –	$ –	$ 466,778	$ 400,207	$ 998,429
David E. Lawrence, CEO	2016	$ 402,466	$ –	$ –	$ 80,490	$ 441,317	$ 15,615	$ 939,888

Aggregate No. of Senior Officers and Highly Compensated Individuals	Year	Salary	Short Term Incentive	Long Term Incentive	Deferred Comp.	Change in Pension Value (1)	Perq/ Other(2)	Total
9	2018	$ 1,317,071	$ 20,000	$ 221,783	$ 38,553	$ 87,746	$ 26,612	$ 1,711,765
9	2017	$ 1,410,830	$ 355,215	$ 305,690	$ 84,632	$ 1,121,626	$ 34,540	$ 3,312,533
9	2016	$ 1,130,025	$ 190,164	$ 141,981	$ 64,219	$ 1,039,272	$ 27,775	$ 2,593,436

(1) The change in pension values in 2018 as reflected in the table above, was primarily due to a decrease due to assumption changes, primarily an increase in the discount rate, offset by an increase due to benefit accruals and the passage of time. The change in pension values in 2016 and 2017 was primarily from changes in the actuarial assumptions for discount rate. See further discussion in Note 9, Employee Benefit Plans, of the Financial Statements.

(2) The Perquisites/Other amount disclosed in the above chart include group life insurance, automobile compensation, spousal expense reimbursements for attendance at Association meetings and for David E. Lawrence retirement, a payment into his nonqualified supplemental (401)k plan.

Pension Benefits for the year ended December 31, 2018,

Pension Benefits Table
As of December 31, 2018

Name of CEO	Year	Plan Name	Number of Years Credited Service	Actuarial Present Value of Accumulated Benefits	Payments During 2018
C. Peery Heldreth, III, CEO	2018	AgFirst Retirement Plan	18	$ 869,573	$ –
				$ 869,573	$ –
Aggregate No. of Senior Officers and Highly Compensated Individuals					
9	2018	AgFirst Retirement Plans	27*	$ 7,660,679	$ –
				$ 7,660,679	$ –

**Represents the average years of credit service for the group*

The disclosure of information on the total compensation paid during 2018 to any senior officer as reported in the table above is available and will be disclosed to the shareholders of the institution upon request.

On February 4, 2015, the FCA Board approved the final rule, "Disclosure to Shareholders; Pension Benefit Disclosures". The rule amends FCA regulations to exclude employee compensation from being reported in the Summary Compensation Table if the employee would be considered a "highly compensated employee" solely because of payments related to or change(s) in value of the employee's qualified pension plan provided that the plan was available to all similarly situated employees on the same basis at the time the employee joined the plan. The Association was required to comply with the rule for compensation reported in the table for fiscal year 2015.

Employee Travel Reimbursement

All employees are reimbursed for all direct travel expenses incurred when traveling on Association business. A copy of the travel policy is available to shareholders upon written request.

Defined Benefit-Type Plans

The Association sponsors a non-qualified defined benefit supplemental executive retirement plan for Donald L. Shiflet, retired CEO. The purpose of the non-qualified plan is to provide benefits that supplement the qualified defined benefit plan in which the Association's employees participate. For Mr. Shiflet, compensation in excess of the 401(a)(17) limit and benefits in excess of the 415(b) limit in the qualified defined benefit plan will be made up through the non-qualified plan. As a non-qualified plan, assets have been allocated and separately invested for this plan, but are not isolated from the general creditors of the Association.

Directors

The following chart details the current term of each director and total cash compensation paid for 2018:

DIRECTOR	CURRENT TERM	TOTAL COMPENSATION PAID DURING 2018
Donna M. Brooke-Alt, **Chairperson**	2018-2021	$ 31,600
Donald W. Reese, **Vice Chairperson**	2018-2021	22,150
Melody S. Jones, **Chairperson of Audit Committee**	2015-2018	23,050
Ronald L. Bennett	2018-2021	17,000
Kevin C. Craun	2017-2020	18,450
William J. Franklin, Jr.	2015-2018	21,050
Bobby C. Gray	2015-2018	23,950
Charles E. Horn, Jr.	2016-2019	20,250
Paul M. House	2017-2020	15,850
James F. Kinsey	2018-2021	20,350
Charles B. Leech, IV	2016-2019	16,400
Milton L. McPike, Jr.	2017-2020	20,350
Wallace W. Sanford, III	2015-2018	16,600
Barry W. Shelor	2017-2020	17,950
Alfred W. Stephens, Jr.	2017-2020	23,050
John E. Wells	2016-2019	19,100
		$ 327,150

The following represents certain information regarding the directors of the Association, including their principal occupation for the past five years:

Donna M. Brooke-Alt, ***Chairperson*****,** is owner/operator and president of Brookedale Farms, LLC which is a greenhouse, event building and Agri-tainment operation. She serves on the Mineral County FSA Board and the Mineral County Family Resource Network Board. Ms. Brooke-Alt also serves on the Potomac State College Ag Advisory Committee and the Potomac State College Gerstell Ag Development Award Committee.

Donald W. Reese, Vice Chairperson, is a partner in Reese's Farm Fresh Produce, a retail produce operation in Halifax County, VA. Mr. Reese also teaches agriculture at Halifax County High School.

Ronald L. Bennett operates a dairy farm. Mr. Bennett serves on the Alleghany County Farm Bureau Board and on the Virginia Farm Bureau Dairy Advisory Board.

Kevin C. Craun owns and operates, with his brother, a 900-acre operation supporting 190 dairy cows, 100 cow/calf pairs and dairy steers. Mr. Craun is a director and president of Rockingham Cooperative, a director and vice chairman of the Shenandoah Valley Soil and Water Conservation District, and a member of the Rockingham County Agriculture Stewardship Committee.

William J. Franklin, Jr., is a livestock producer in Scott County, Va. He also produces hay and corn for his 165 beef cows. Mr. Franklin is employed off the farm at Scott County Telephone Cooperative where he serves as the Chief Executive Officer. He serves on the Carolina-Virginia's Telephone Membership Association Board; the PAC Board of the National Rural Broadband Association; the IRIS Board, which is a Tennessee LLC regional network provider; and the LIT Board, which is a Virginia LLC regional network provider; the Scott County Cattle Association Board and the Southwest Virginia Workforce Development Board. Mr. Franklin also serves on the National Rural Broadband Association's Membership Committee and is a member of the Scott County Rotary Club. Mr. Franklin is a director on the AgFirst Farm Credit Bank Board.

Bobby C. Gray operates a diversified farm operation, which includes raising dairy heifers, a beef cow herd, growing corn and hay on 1400 acres in Washington County, VA. Mr. Gray serves on the Advisory Committee for the Washington County School System.

Charles E. Horn, Jr. owns and operates Delta Springs LLC, a poultry and replacement dairy heifer farm in Mt. Solon, VA. Mr. Horn currently serves on the Valley Conservation Council board of directors, and has been a member of the North River Ruritan Club for 30 years, currently serving as treasurer.

Paul M. House is president of Kettle Wind Farm, LLC, a grain and sod farm. Mr. House is also a shareholder in Dutchland Farm Inc., a family dairy farm.

Melody S. Jones is an outside director and is chairman of the Audit Committee. She is a self-employed sole practitioner Certified Public Accountant. Ms. Jones is a financial partner of Philippi Women's Investment Club.

James F. Kinsey is owner/manager of Kinsey's Oak Front Farms, which is a 200 head seed stock Angus farm. He is a board member of the West Virginia Cattlemen's Association and serves as vice president. Mr. Kinsey is a member of the WVU Davis College Visiting Committee and serves on the Wardensville Bull Test Committee. Mr. Kinsey is also a member of the West Virginia Farm Bureau, West Virginia Angus Association, American Angus Association, and Bridgeport United Methodist Church.

Charles B. Leech, IV, is an owner/operator of the family's dairy farm. Mr. Leech serves as a director on the Rockbridge Farmers' Cooperative Board and a director of Virginia State Dairyman's Association.

Milton L. McPike, Jr., is an outside director. He is a retired Operations Manager for Cargill, Inc. in Wichita, KS.

Wallace W. Sanford, III, is a dairy and beef farmer in partnership with his family. Mr. Sanford serves on the Maryland-Virginia Milk Producers Board and is a director for the VA State Dairymen Association.

Barry W. Shelor operates a dairy farm. He serves on the Board of Directors for Shelor's Dairy, Inc. and Mountain Meadows Dairy, LLC. Mr. Shelor also serves on the Patrick County Farm Bureau Board as vice-president.

Alfred W. Stephens, Jr, is a dairy and beef cow/calf farmer and has a small produce business. Mr. Stephens serves as secretary-treasurer on the Wythe/Bland DHIA.

John E. Wells is a full-time beef farmer. He is a member of the West Virginia Cattlemen's Association, Wirt County Farm Bureau, and is vice president of the Jackson County Calf Pool Cooperative and serves on the AgFirst Farm Credit Council Board. Mr. Wells also serves as director for the Wirt County Group, Inc.

Subject to approval by the board, the Association may allow directors honorarium of $500 for attendance at meetings, committee meetings, or special assignments, and $100 for telephone conferences. In addition to the honoraria, the board chairperson was paid a quarterly retainer fee of $1,500, the audit committee chairperson was paid a quarterly retainer fee of $1,375 and the directors were paid a quarterly retainer fee of $1,250.

The following chart details the number of meetings, other activities and additional compensation paid for other activities (if applicable) for each director:

Name of Director	Days Served: Regular Board Meetings	Days Served: Other Official Activities*	Committee Assignments	Compensation Paid For Other Activities**
Donna M. Brooke-Alt, **Chairperson**	13	41	Chairperson of Compensation Committee and Governance Committee	$ 18,050
Donald W. Reese, **Vice Chairperson**	11	25	Compensation Committee and Governance Committee	10,500
Melody S. Jones, **Chairperson of Audit Committee**	11	31	Chairperson of Audit Committee	10,400
Ronald L. Bennett	13	13	Risk Management Committee	4,450
Kevin C. Craun	13	18	Audit Committee	6,300
William J. Franklin, Jr.	13	20	Chairperson of Governance Committee and Compensation Committee	7,300
Bobby C. Gray	13	24	Audit Committee	10,500
Charles E. Horn, Jr.	13	18	Communication Advocacy Program/Sales Committee	8,100
Paul M. House	11	17	Audit Committee	4,400
James F. Kinsey	13	17	Communication Advocacy Program/Sales Committee	7,000
Charles B. Leech, IV	13	11	Compensation Committee and Governance Committee	4,250
Milton L. McPike, Jr.	13	18	Chairperson of Risk Management Committee	7,200
Wallace W. Sanford, III	13	13	Risk Management Committee	4,450
Barry W. Shelor	13	14	Risk Management Committee	5,000
Alfred W. Stephens, Jr.	13	20	Chairperson of Communication Advocacy Program/Sales Committee	10,100
John E. Wells	13	13	Compensation Committee and Governance Committee	5,350
				$ 123,350

** Includes board committee meetings and other board activities other than regular board meetings.*

Directors and senior officers are reimbursed on an actual cost basis for all expenses incurred in the performance of official duties. Such expenses may include transportation, lodging, meals, tips, tolls, parking of cars, laundry, registration fees, and other expenses associated with travel on official business. A copy of the policy is available to shareholders of the Association upon request.

The aggregate amount of reimbursement for travel, subsistence and other related expenses for all directors as a group was $221,668 for 2018, $210,674 for 2017, and $202,958 for 2016.

Transactions with Senior Officers and Directors

The reporting entity's policies on loans to and transactions with its officers and directors, to be disclosed in this section are incorporated herein by reference to Note 10, *Related Party Transactions*, of the Notes to the Consolidated Financial Statements in this Annual Report.

Transactions Other Than Loans

There have been no transactions that occurred at any time during the year ended December 31, 2018, between the Association and senior officers or directors, their immediate family members or any organizations with which they are affiliated, which require reporting per FCA regulations. There were no transactions with any senior officer or director related to the purchase or retirement of preferred stock of the Association, for the year ended December 31, 2018.

Involvement in Certain Legal Proceedings

There were no other transactions which came to the attention of management or the board of directors regarding involvement of current directors or senior officers in specified legal proceedings which should be disclosed in this section. No directors or senior officers have been involved in any legal proceedings during the last five years which require reporting per FCA regulations.

Relationship with Independent Auditors

There were no changes in or material disagreements with our independent auditors on any matter of accounting principles or financial statement disclosure during this period.

Aggregate fees incurred by the Association for services rendered by its independent auditors for the year ended December 31, 2018 were as follows:

(dollars in thousands)	2018
Independent Auditors	
PricewaterhouseCoopers LLP Audit services	$ 67
Total	$ 67

Audit fees were for the annual audit of the consolidated financial statements.

Consolidated Financial Statements

The consolidated financial statements, together with the report thereon of PricewaterhouseCoopers LLP dated March 13, 2019, and the report of management, which appear in this Annual Report, are incorporated herein by reference.

Copies of the Association's Annual and unaudited Quarterly reports are available upon request free of charge by calling 1-540-886-3435, extension 5040, or writing Justin Weekley, Farm Credit of the Virginias, P.O. Box 899, Staunton, VA 24402-0899 or accessing the web site, **www.farmcreditofvirginias.com**. The Association prepares an electronic version of the Annual Report which is available on the Association's web site within 75 days after the end of the fiscal year and distributes the Annual Reports

to shareholders within 90 days after the end of the fiscal year. The Association prepares an electronic version of the Quarterly report which is available on the Association's website within 40 days after the end of each fiscal quarter, except that no report need be prepared for the fiscal quarter that coincides with the end of the fiscal year of the Association.

Borrower Information Regulations

Since 1972, Farm Credit Administration (FCA) regulations have required that borrower information be held in strict confidence by Farm Credit System (FCS) institutions, their directors, officers and employees. These regulations provide Farm Credit institutions clear guidelines for protecting their borrowers' nonpublic personal information.

On November 10, 1999, the FCA Board adopted a policy that requires FCS institutions to formally inform new borrowers at loan closing of the FCA regulations on releasing borrower information and to address this information in the Annual Report. The implementation of these measures ensures that new and existing borrowers are aware of the privacy protections afforded them through FCA regulations and Farm Credit System institution efforts.

Credit and Services to Young, Beginning, and Small Farmers and Ranchers and Producers or Harvesters of Aquatic Products

Information to be disclosed in this section is incorporated herein by reference to the similarly named section in the Management's Discussion and Analysis of Financial Condition and Results of Operations section included in this annual report to the shareholders.

Shareholder Investment

Shareholder investment in the Association could be materially affected by the financial condition and results of operations of AgFirst Farm Credit Bank (Bank or AgFirst). Copies of the Bank's Annual and Quarterly reports are available upon request free of charge by calling 1-800-845-1745, ext. 2832, or writing Susanne Caughman, AgFirst Farm Credit Bank, P. O. Box 1499, Columbia, SC 29202. Information concerning AgFirst Farm Credit Bank can also be obtained by going to AgFirst's web site at ***www.agfirst.com.*** The Bank prepares an electronic version of the Annual Report, which is available on the website, within 75 days after the end of the fiscal year. The Bank prepares an electronic version of the Quarterly report within 40 days after the end of each fiscal quarter, except that no report needs to be prepared for the fiscal quarter that coincides with the end of the fiscal year of the Bank.

Report of the Audit Committee

The Audit Committee of the Board of Directors (Committee) is comprised of the directors named below. None of the directors who serve on the Committee is an employee of Farm Credit of the Virginias, ACA (Association) and in the opinion of the Board of Directors, each is free of any relationship with the Association or management that would interfere with the director's independent judgment on the Committee.

The Committee has adopted a written charter that has been approved by the Board of Directors. The Committee has reviewed and discussed the Association's audited financial statements with management, which has primary responsibility for the financial statements.

PricewaterhouseCoopers LLP (PwC), the Association's independent auditors for 2018, is responsible for expressing an opinion on the conformity of the Association's audited financial statements with accounting principles generally accepted in the United States of America. The Committee has discussed with PwC the matters that are required to be discussed by Statement on Auditing Standards No. 114 *(The Auditor's Communication With Those Charged With Governance)*. The Committee discussed with PwC its independence from Farm Credit of the Virginias, ACA. The Committee also reviewed the non-audit services provided by PwC and concluded that these services were not incompatible with PwC's independence.

Based on the considerations referred to above, the Committee recommended to the Board of Directors that the audited financial statements be included in the Association's Annual Report for 2018. The foregoing report is provided by the following independent directors, who constitute the Committee:

Melody S. Jones
Chairperson of the Audit Committee

Members of Audit Committee

Kevin C. Craun
Bobby C. Gray
Paul M. House

March 13, 2019

Report of Independent Auditors

To the Board of Directors and Management of
Farm Credit of the Virginias, ACA

We have audited the accompanying consolidated financial statements of Farm Credit of the Virginias, ACA and its subsidiaries (the "Association"), which comprise the consolidated balance sheets as of December 31, 2018, 2017 and 2016, and the related consolidated statements of income, comprehensive income, changes in members' equity and cash flows for the years then ended.

Management's Responsibility for the Consolidated Financial Statements

Management is responsible for the preparation and fair presentation of the consolidated financial statements in accordance with accounting principles generally accepted in the United States of America; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of consolidated financial statements that are free from material misstatement, whether due to fraud or error.

Auditors' Responsibility

Our responsibility is to express an opinion on the consolidated financial statements based on our audits. We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statements. The procedures selected depend on our judgment, including the assessment of the risks of material misstatement of the consolidated financial statements, whether due to fraud or error. In making those risk assessments, we consider internal control relevant to the Association's preparation and fair presentation of the consolidated financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Association's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the consolidated financial statements. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of Farm Credit of the Virginias, ACA and its subsidiaries as of December 31, 2018, 2017 and 2016, and the results of their operations and their cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

PricewaterhouseCoopers LLP
Miami, Florida

March 13, 2019

PricewaterhouseCoopers LLP, 333 SE 2nd Avenue, Suite 3000, Miami, FL 33131
T: (305) 375 7400, F: (305) 375 6221, www.pwc.com/us

Consolidated Balance Sheets

(dollars in thousands)	December 31, 2018	2017	2016
Assets			
Cash	**$ 4,700**	$ 5,082	$ 5,730
Loans	**1,850,777**	1,844,949	1,798,996
Allowance for loan losses	**(15,313)**	(17,461)	(14,483)
Net loans	**1,835,464**	1,827,488	1,784,513
Loans held for sale	**349**	1,388	1,317
Accrued interest receivable	**10,518**	10,127	9,352
Equity investments in other Farm Credit institutions	**20,729**	20,763	19,698
Premises and equipment, net	**11,552**	10,142	10,228
Other property owned	**1,477**	1,221	2,467
Accounts receivable	**22,716**	25,059	22,046
Other assets	**2,146**	2,338	3,182
Total assets	**$ 1,909,651**	$ 1,903,608	$ 1,858,533
Liabilities			
Notes payable to AgFirst Farm Credit Bank	**$ 1,422,676**	$ 1,437,895	$ 1,423,922
Accrued interest payable	**4,033**	3,634	3,265
Patronage refunds payable	**30,303**	25,254	15,230
Accounts payable	**2,279**	3,146	3,380
Other liabilities	**9,982**	10,858	21,913
Total liabilities	**1,469,273**	1,480,787	1,467,710
Commitments and contingencies (Note 11)			
Members' Equity			
Capital stock and participation certificates	**10,426**	10,493	10,433
Retained earnings			
Allocated	**92,568**	92,568	92,568
Unallocated	**337,408**	319,790	287,846
Accumulated other comprehensive income (loss)	**(24)**	(30)	(24)
Total members' equity	**440,378**	422,821	390,823
Total liabilities and members' equity	**$ 1,909,651**	$ 1,903,608	$ 1,858,533

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

Consolidated Statements of Income

(dollars in thousands)	For the year ended December 31, 2018	2017	2016
Interest Income			
Loans	**$ 103,008**	$ 96,455	$ 88,990
Interest Expense			
Notes payable to AgFirst Farm Credit Bank	**45,938**	42,258	37,830
Net interest income	**57,070**	54,197	51,160
Provision for loan losses	**2,500**	3,250	2,750
Net interest income after provision for loan losses	**54,570**	50,947	48,410
Noninterest Income			
Loan fees	**822**	612	745
Fees for financially related services	**140**	57	68
Patronage refunds from other Farm Credit institutions	**22,432**	24,833	21,860
Gains (losses) on sales of rural home loans, net	**619**	801	851
Gains (losses) on sales of premises and equipment, net	**301**	86	55
Gains (losses) on other transactions	**4**	61	55
Insurance Fund refunds	**1,673**	—	—
Other noninterest income	**72**	100	81
Total noninterest income	**26,063**	26,550	23,715
Noninterest Expense			
Salaries and employee benefits	**17,779**	17,827	18,417
Occupancy and equipment	**1,369**	1,408	1,369
Insurance Fund premiums	**1,272**	2,143	2,316
(Gains) losses on other property owned, net	**71**	615	286
Other operating expenses	**7,481**	(1,489)	6,479
Total noninterest expense	**27,972**	20,504	28,867
Income before income taxes	**52,661**	56,993	43,258
Provision for income taxes	**40**	49	38
Net income	**$ 52,621**	$ 56,944	$ 43,220

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

Consolidated Statements of Comprehensive Income

(dollars in thousands)	For the year ended December 31, 2018	2017	2016
Net income	**$ 52,621**	$ 56,944	$ 43,220
Other comprehensive income net of tax			
Employee benefit plans adjustments	**6**	(6)	(2)
Comprehensive income	**$ 52,627**	$ 56,938	$ 43,218

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

Consolidated Statements of Changes in Members' Equity

(dollars in thousands)	Capital Stock and Participation Certificates	Retained Earnings Allocated	Retained Earnings Unallocated	Accumulated Other Comprehensive Income (Loss)	Total Members' Equity
Balance at December 31, 2015	$ 12,606	$ 92,568	$ 259,626	$ (22)	$ 364,778
Comprehensive income			43,220	(2)	43,218
Capital stock/participation certificates issued/(retired), net	(2,173)				(2,173)
Patronage distribution					
Cash			(15,000)		(15,000)
Balance at December 31, 2016	$ 10,433	$ 92,568	$ 287,846	$ (24)	$ 390,823
Comprehensive income			56,944	(6)	56,938
Capital stock/participation certificates issued/(retired), net	60				60
Patronage distribution					
Cash			(25,000)		(25,000)
Balance at December 31, 2017	$ 10,493	$ 92,568	$ 319,790	$ (30)	$ 422,821
Comprehensive income			**52,621**	**6**	**52,627**
Capital stock/participation certificates issued/(retired), net	**(67)**				**(67)**
Patronage distribution					
Cash			**(35,000)**		**(35,000)**
Patronage distribution adjustment			**(3)**		**(3)**
Balance at December 31, 2018	**$ 10,426**	**$ 92,568**	**$ 337,408**	**$ (24)**	**$ 440,378**

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

Consolidated Statements of Cash Flows

(dollars in thousands)	For the year ended December 31, 2018	2017	2016
Cash flows from operating activities:			
Net income	**$ 52,621**	$ 56,944	$ 43,220
Adjustments to reconcile net income to net cash provided by (used in) operating activities:			
Depreciation on premises and equipment	**850**	822	814
Amortization (accretion) of net deferred loan costs (fees)	**322**	307	200
Provision for loan losses	**2,500**	3,250	2,750
(Gains) losses on other property owned	**52**	588	180
(Gains) losses on sales of premises and equipment, net	**(301)**	(86)	(55)
(Gains) losses on sales of rural home loans, net	**(619)**	(801)	(851)
(Gains) losses on other transactions	**(4)**	(61)	(55)
Changes in operating assets and liabilities:			
Origination of loans held for sale	**(39,672)**	(42,887)	(43,170)
Proceeds from sales of loans held for sale, net	**41,330**	43,617	44,973
(Increase) decrease in accrued interest receivable	**(391)**	(775)	(672)
(Increase) decrease in accounts receivable	**2,343**	(3,013)	193
(Increase) decrease in other assets	**192**	844	2,046
Increase (decrease) in accrued interest payable	**399**	369	205
Increase (decrease) in accounts payable	**(867)**	(234)	917
Increase (decrease) in other liabilities	**(860)**	(10,994)	4,290
Total adjustments	**5,274**	(9,054)	11,765
Net cash provided by (used in) operating activities	**57,895**	47,890	54,985
Cash flows from investing activities:			
Net (increase) decrease in loans	**(11,536)**	(47,429)	(110,745)
(Increase) decrease in equity investments in other Farm Credit institutions	**34**	(1,065)	5,632
Purchases of premises and equipment	**(2,331)**	(751)	(3,014)
Proceeds from sales of premises and equipment	**372**	101	62
Proceeds from sales of other property owned	**424**	1,549	3,578
Net cash provided by (used in) investing activities	**(13,037)**	(47,595)	(104,487)
Cash flows from financing activities:			
Advances on (repayment of) notes payable to AgFirst Farm Credit Bank, net	**(15,219)**	13,973	69,489
Capital stock and participation certificates issued/(retired), net	**(67)**	60	(2,173)
Patronage refunds and dividends paid	**(29,954)**	(14,976)	(15,029)
Net cash provided by (used in) financing activities	**(45,240)**	(943)	52,287
Net increase (decrease) in cash	**(382)**	(648)	2,785
Cash, beginning of period	**5,082**	5,730	2,945
Cash, end of period	**$ 4,700**	$ 5,082	$ 5,730
Supplemental schedule of non-cash activities:			
Receipt of property in settlement of loans	**$ 738**	$ 897	$ 1,428
Estimated cash dividends or patronage distributions declared or payable	**35,000**	25,000	15,000
Employee benefit plans adjustments (Note 9)	**(6)**	6	2
Supplemental information:			
Interest paid	**45,539**	41,889	37,625
Taxes (refunded) paid, net	**48**	25	37

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

Notes to the Consolidated Financial Statements

(dollars in thousands, except as noted)

Note 1 — Organization and Operations

A. **Organization:** Farm Credit of the Virginias, ACA (Association) is a member-owned cooperative that provides credit and credit-related services to qualified borrowers in forty-six counties in the state of Virginia, forty-eight counties in the state of West Virginia, and two counties in the state of Maryland as follows:

Virginia: Counties of Albemarle, Alleghany, Arlington, Augusta, Bath, Bedford, Bland, Botetourt, Buchanan, Carroll, Craig, Culpeper, Dickenson, Fairfax, Fauquier, Floyd, Franklin, Giles, Grayson, Greene, Halifax, Henry, Highland, Lee, Loudoun, Madison, Montgomery, Nelson, Orange, Patrick, Pittsylvania, Prince William, Pulaski, Rappahannock, Roanoke, Rockbridge, Rockingham, Russell, Scott, Smyth, Spotsylvania, Stafford, Tazewell, Washington, Wise, and Wythe;

West Virginia: Counties of Barbour, Boone, Braxton, Cabell, Calhoun, Clay, Doodridge, Fayette, Gilmer, Grant, Greenbrier, Hampshire, Hardy, Harrison, Jackson, Kanawha, Lewis, Lincoln, Logan, Marion, Mason, McDowell, Mercer, Mineral, Mingo, Monongalia, Monroe, Nicholas, Pendleton, Pleasants, Pocahontas, Preston, Putnam, Raleigh, Randolph, Ritchie, Roane, Summers, Taylor, Tucker, Tyler, Upshur, Wayne, Webster, Wetzel, Wirt, Wood, and Wyoming; and

Maryland: Counties of Allegany and Garrett.

The Association is a lending institution in the Farm Credit System (System), a nationwide network of cooperatively owned banks and associations. It was established by Acts of Congress and is subject to the provisions of the Farm Credit Act of 1971, as amended (Farm Credit Act). The System specializes in providing financing and related services to qualified borrowers for agricultural and rural purposes.

The nation is served by three Farm Credit Banks (FCBs) and one Agricultural Credit Bank (ACB), (collectively, the System Banks) each of which has specific lending authorities within its chartered territory. The ACB also has additional specific nationwide lending authorities.

Each System Bank serves one or more Agricultural Credit Associations (ACAs) that originate long-term, short-term and intermediate-term loans, Production Credit Associations (PCAs) that originate and service short- and intermediate-term loans, and/or Federal Land Credit Associations (FLCAs) that originate and service long-term real estate mortgage loans. These associations borrow a majority of the funds for their lending activities from their related bank. System Banks are also responsible for supervising the activities of associations within their districts. AgFirst (Bank) and its related associations (Associations or District Associations) are collectively referred to as the AgFirst District. The District Associations jointly own substantially all of AgFirst's voting stock. As of year end, the AgFirst District consisted of the Bank and nineteen District Associations. All nineteen were structured as ACA holding companies, with PCA and FLCA subsidiaries. FLCAs are tax-exempt while ACAs and PCAs are taxable.

The Farm Credit Administration (FCA) is delegated authority by Congress to regulate the System banks and associations. The FCA examines the activities of the associations and certain actions by the associations are subject to the prior approval of the FCA and the supervising bank.

The Farm Credit Act also established the Farm Credit System Insurance Corporation (Insurance Corporation) to administer the Farm Credit Insurance Fund (Insurance Fund). The Insurance Fund is required to be used (1) to ensure the timely payment of principal and interest on Systemwide debt obligations (Insured Debt), (2) to ensure the retirement of protected borrower capital at par or stated value, and (3) for other specified purposes. The Insurance Fund is also available for discretionary uses by the Insurance Corporation to provide assistance to certain troubled System institutions and to cover the operating expenses of the Insurance Corporation. Each System bank has been required to pay premiums, which may be passed on to the Association, into the Insurance Fund, based on its average adjusted outstanding Insured Debt until the assets in the Insurance Fund reach the "secure base amount." The secure base amount is defined in the Farm Credit Act as 2.0 percent of the aggregate insured obligations (adjusted to reflect the reduced risk on loans or investments guaranteed by federal or state governments) or such other percentage of the aggregate obligations as the Insurance Corporation at its sole discretion determines to be actuarially sound. When the amount in the Insurance Fund exceeds the secure base amount, the Insurance Corporation is required to reduce premiums and may return excess funds above the secure base amount to System institutions. However it must still ensure that reduced premiums are sufficient to maintain the level of the Insurance Fund at the secure base amount.

B. **Operations:** The Farm Credit Act sets forth the types of authorized lending activity and financial services that can be offered by the Association, and the persons eligible to borrow.

The Associations borrow from the Bank and in turn may originate and service short- and intermediate-term loans to their members, as well as long-term real estate mortgage loans.

The Bank primarily lends to the District Associations in the form of a line of credit to fund the Associations' earning assets. These lines of credit (or Direct Notes) are collateralized by a pledge of substantially all of each Association's assets. The terms of the Direct Notes are governed by a lending agreement between the Bank and Association. Each advance is structured such that the principal cash flow, repricing characteristics, and underlying

index (if any) of the advance match those of the assets being funded. By match-funding the Association loans, the Associations' exposure to interest rate risk is minimized.

In addition to providing funding for earning assets, the Bank provides District Associations with banking and support services such as accounting, human resources, information systems, and marketing. The costs of these support services are included in the cost of the Direct Note, or in some cases billed directly to certain Associations that use a specific service.

The Association is authorized to provide, either directly or in participation with other lenders, credit, credit commitments, and related services to eligible borrowers. Eligible borrowers include farmers, ranchers, producers or harvesters of aquatic products, rural residents, and farm-related businesses.

The Association may sell to any System borrowing member, on an optional basis, credit or term life insurance appropriate to protect the loan commitment in the event of death of the debtor(s). The sale of other insurance necessary to protect a member's farm or aquatic unit is permitted, but limited to hail and multi-peril crop insurance, and insurance necessary to protect the facilities and equipment of aquatic borrowers.

Note 2 — Summary of Significant Accounting Policies

The accounting and reporting policies of the Association conform with accounting principles generally accepted in the United States of America (GAAP) and prevailing practices within the banking industry. The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the amounts reported in the Consolidated Financial Statements and accompanying notes. Significant estimates are discussed in these footnotes, as applicable. Actual results may differ from these estimates.

The accompanying consolidated financial statements include the accounts of the ACA, PCA and FLCA.

Certain amounts in the prior year financial statements have been reclassified to conform to the current period presentation. Such reclassifications had no effect on net income or total members' equity of prior years.

A. **Cash:** Cash represents cash on hand and on deposit at banks.

B. **Loans and Allowance for Loan Losses:** The Association is authorized to make long-term real estate loans with maturities of 5 to 40 years and certain short- and intermediate-term loans for agricultural production or operating purposes with maturities of not more than 10 years.

   Loans are carried at their principal amount outstanding adjusted for charge-offs, premiums, discounts, deferred loan fees or costs, and derivative instruments and hedging valuation adjustments, if any. Interest on loans is accrued and credited to interest income based upon the daily principal amount outstanding. The difference in the total investment in a loan and its principal amount may be deferred as part of the carrying amount of the loan and the net difference amortized over the life of the related loan as an adjustment to interest income using the effective interest method.

   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 and are generally considered substandard or doubtful, which is in accordance with the loan rating model, as described below. Impaired loans include nonaccrual loans, restructured loans, and loans past due 90 days or more and still accruing interest. A loan is considered contractually past due when any principal repayment or interest payment required by the loan instrument is not received on or before the due date. A loan remains contractually past due until the entire amount past due, including principal, accrued interest, and penalty interest incurred as the result of past due status, is collected or otherwise discharged in full. A formal restructuring may also cure a past due status.

   Loans are generally classified as nonaccrual when principal or interest is delinquent for 90 days (unless adequately collateralized and in the process of collection) or circumstances indicate that collection of principal and/or interest is in doubt. When a loan is placed in nonaccrual status, accrued interest deemed uncollectible is reversed (if accrued in the current year) or charged against the allowance for loan losses (if accrued in the prior year).

   When loans are in nonaccrual status, payments are applied against the recorded investment in the loan asset. If collection of the recorded investment in the loan is fully expected and the loan does not have a remaining unrecovered prior charge-off associated with it, the interest portion of payments received in cash may be recognized as interest income. Nonaccrual loans may be returned to accrual status when principal and interest are current, prior charge-offs have been recovered, the ability of the borrower to fulfill the contractual repayment terms is fully expected, and the loan is not classified "doubtful" or "loss." Loans are charged off at the time they are determined to be uncollectible.

   In cases where a borrower experiences financial difficulties and the Association makes certain monetary concessions to the borrower through modifications to the contractual terms of the loan, the loan is classified as a restructured loan. A restructured loan constitutes a troubled debt restructuring (TDR) if for economic or legal reasons related to the debtor's financial difficulties the Association grants a concession to the debtor that it would not otherwise consider. If the borrower's ability to meet the revised payment schedule is uncertain, the loan is classified as a nonaccrual loan.

   The allowance for loan losses is maintained at a level considered adequate by management to provide for probable and estimable losses inherent in the loan portfolio as of the report date. The allowance for loan losses is increased through provisions for loan losses and loan recoveries and is decreased through loan charge-offs and allowance reversals. A review of individual loans in each respective portfolio is

performed periodically to determine the appropriateness of risk ratings and to ensure loss exposure to the Association has been identified. 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 Association considers the following factors, among others, when determining the allowance for loan losses:

- Changes in credit risk classifications
- Changes in collateral values
- Changes in risk concentrations
- Changes in weather-related conditions
- Changes in economic conditions

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, as practically expedient, 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 inherent in the remainder of the loan portfolio which excludes impaired loans considered under the specific allowance discussed above. A general allowance can be evaluated on a pool basis for those loans with similar 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 Association's allowance for loan losses evaluation, and is generally incorporated into the institution's loan underwriting standards and internal lending limit. The Association 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.

C. **Loans Held for Sale:** Loans are classified as held for sale when there is intent to sell the loans within a reasonable period of time. Loans intended for sale are carried at the lower of cost or fair value.

D. **Other Property Owned (OPO):** Other property owned, consisting of real estate, personal property, and other assets acquired through a collection action, is recorded upon acquisition at fair value less estimated selling costs. Any initial reduction in the carrying amount of a loan to the fair value of the collateral received is charged to the allowance for loan losses. Revised estimates to the fair value less cost to sell are reported as adjustments to the carrying amount of the asset, provided that such adjusted value is not in excess of the carrying amount at acquisition. Income, expenses, and carrying value adjustments related to other property owned are included in Gains (Losses) from Other Property Owned, Net in the Consolidated Statements of Income.

E. **Premises and Equipment:** Land is carried at cost. Premises and equipment are carried at cost less accumulated depreciation. Depreciation is provided on the straight-line method over the estimated useful lives of the assets. Gains and losses on dispositions are reflected in current earnings. Maintenance and repairs are charged to expense and improvements are capitalized. Premises and equipment are evaluated for impairment whenever events or circumstances indicate that the carrying value of the asset may not be recoverable.

From time to time, assets classified as premises and equipment are transferred to held for sale for various reasons. These assets are carried in Other Assets at the lower of the recorded investment in the asset or fair value less estimated cost to sell based upon the property's appraised value at the date of transfer. Any write-down of property held for sale is recorded as a loss in the period identified.

F. **Investments:** The Association may hold investments as described below.

Equity Investments in Other Farm Credit System Institutions

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

Investment Income

Dividends from Investments in Other Farm Credit Institutions are generally recorded as patronage income and included in Noninterest Income.

Other Investments
As discussed in Note 8, certain investments, consisting primarily of mutual funds, are held in trust and investment accounts and are reported at fair value. Holding period gains and losses are included within Noninterest Income on the Consolidated Statements of Income and the balance of these investments, totaling $1,964, is included in Other Assets on the accompanying Consolidated Balance Sheets as of December 31, 2018.

G. **Voluntary Advance Conditional Payments:** The Association is authorized under the Farm Credit Act to accept advance payments from borrowers. To the extent the borrower's access to such advance payments is restricted, the advanced conditional payments are netted against the borrower's related loan balance. Amounts in excess of the related loan balance and amounts to which the borrower has unrestricted access are presented as other liabilities in the accompanying Consolidated Balance Sheets. Advanced conditional payments are not insured. Interest is generally paid by the Association on such accounts.

H. **Employee Benefit Plans:** The Association participates in District and multi-District sponsored benefit plans. These plans may include defined benefit final average pay retirement, defined benefit cash balance retirement, defined benefit other postretirement benefits, and defined contribution plans.

Defined Contribution Plans
Substantially all employees are eligible to participate in the defined contribution Farm Credit Benefit Alliance (FCBA) 401(k) Plan, subsequently referred to as the 401(k) Plan, which qualifies as a 401(k) plan as defined by the Internal Revenue Code. Employee deferrals are not to exceed the maximum deferral as determined and adjusted by the Internal Revenue Service. Company contributions to the 401(k) Plan are expensed as funded.

Additional information may be found in Note 9.

Multi-Employer Defined Benefit Plans
Substantially all employees hired before January 1, 2003 may participate in the AgFirst Farm Credit Retirement Plan (Plan), which is a defined benefit plan and considered multi-employer under FASB accounting guidance. The Plan is noncontributory and includes eligible Association and District employees. The "Projected Unit Credit" actuarial method is used for financial reporting purposes.

In addition to pension benefits, the Association provides certain health care and life insurance benefits for retired employees (other postretirement benefits) through a multi-District sponsored retiree healthcare plan. Substantially all employees are eligible for those benefits when they reach early retirement age while working for the Association. Authoritative accounting guidance requires the accrual of the expected cost of providing these benefits to an employee, their beneficiaries and covered dependents during the years the employee renders service necessary to become eligible for benefits.

Since the foregoing plans are multiemployer, the Association does not apply the provisions of FASB guidance on employers' accounting for defined benefit pension and other postretirement plans in its stand-alone financial statements. Rather, the effects of this guidance are reflected in the Annual Information Statement of the Farm Credit System.

Additional information may be found in Note 9 and in the Notes to the Annual Information Statement of the Farm Credit System.

Single Employer Defined Benefit Plans
The Association also sponsors a single employer defined benefit supplemental retirement plan and offers a FCBA supplemental 401(k) plan for certain key employees. These plans are nonqualified; therefore, the associated liabilities are included in the Association's Consolidated Balance Sheets in Other Liabilities.

The foregoing defined benefit plan is considered single employer, therefore the Association applies the provisions of FASB guidance on employers' accounting for defined benefit pension and other postretirement plans in its stand-alone financial statements. See Note 9 for additional information.

I. **Income Taxes:** The Association evaluates tax positions taken in previous and current years according to FASB guidance. A tax position can result in a permanent reduction of income taxes payable, a deferral of income taxes otherwise currently payable to future years, or a change in the expected realizability of deferred tax assets. The term tax position also encompasses, but is not limited to, an entity's status, including its status as a pass-through entity or tax-exempt entity.

The Association is generally subject to Federal and certain other income taxes. As previously described, the ACA holding company has two wholly-owned subsidiaries, a PCA and a FLCA. The FLCA subsidiary is exempt from federal and state income taxes as provided in the Farm Credit Act. The ACA holding company and the PCA subsidiary are subject to federal, state and certain other income taxes.

The Association is eligible to operate as a cooperative that qualifies for tax treatment under Subchapter T of the Internal Revenue Code. Accordingly, under specified conditions, the Association 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 refunds. The Association distributes patronage on the basis of book income.

The Association accounts for income taxes under the asset and liability method, recognizing deferred tax assets and liabilities for the expected future tax consequences of the temporary differences between the carrying amounts and tax bases of assets and liabilities. Deferred tax assets and liabilities are measured using enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be realized or settled.

The Association records a valuation allowance at the balance sheet dates against that portion of the Association's deferred

tax assets that, based on management's best estimates of future events and circumstances, more likely than not (a likelihood of more than 50 percent) will not be realized. The consideration of valuation allowances involves various estimates and assumptions as to future taxable earnings, including the effects of the expected patronage program, which reduces taxable earnings.

J. **Due from AgFirst Farm Credit Bank:** The Association records patronage refunds from the Bank and certain District Associations on an accrual basis.

K. **Valuation Methodologies:** FASB guidance defines fair value 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. This guidance also 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. It prescribes three levels of inputs that may be used to measure fair value.

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

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 3 inputs to the valuation methodology are unobservable and supported by little or no market activity. Valuation is determined using pricing models, discounted cash flow methodologies, or similar techniques, and could include significant management judgment or estimation. Level 3 assets and liabilities also could include instruments whose price has been adjusted based on dealer quoted pricing that is different than a third-party valuation or internal model pricing. The Association may use the Bank, internal resources or third parties to obtain fair value prices. Quoted market prices are generally used when estimating fair values of any assets or liabilities for which observable, active markets exist.

A number of methodologies may be employed to value items for which an observable active market does not exist. Examples of these items include: impaired loans, other property owned, and certain derivatives, investment securities and other financial instruments. Inputs to these valuations can involve estimates and assumptions that require a substantial degree of judgment. Some of the assumptions used include, among others, discount rates, rates of return on assets, repayment rates, cash flows, default rates, costs of servicing, and liquidation values. The use of different assumptions could produce significantly different asset or liability values, which could have material positive or negative effects on results of operations.

Additional information may be found in Note 8.

L. **Off-Balance-Sheet Credit Exposures:** The credit risk associated with commitments to extend credit and letters of credit is essentially the same as that involved with extending loans to customers and is subject to normal credit policies. Collateral may be obtained based on management's assessment of the customer's creditworthiness.

Commitments to extend credit are agreements to lend to customers, generally having fixed expiration dates or other termination clauses that may require payment of a fee.

Letters of credit are commitments issued to guarantee the performance of a customer to a third party. These letters of credit are issued to facilitate commerce and typically result in the commitment being funded when the underlying transaction is consummated between the customer and third party.

M. **Revenue Recognitio**n: The Association generates income from multiple sources.

Financial Instruments
The largest source of revenue for the Association is Interest Income. Interest income is recognized on an accrual basis driven by nondiscretionary formulas based on written contracts, such as loan agreements or securities contracts. Credit-related fees, including letter of credit fees, finance charges and other fees are recognized in Noninterest Income when earned. Other types of noninterest revenues, such as service charges, professional services and broker fees, are accrued and recognized into income as services are provided and the amount of fees earned is reasonably determinable.

Contracts with Customers
In May 2014, the FASB issued ASU 2014-09 Revenue from Contracts with Customers (Topic 606). This guidance, which became effective January 1, 2018, changed the recognition of revenue from contracts with customers. The core principle of the guidance is that an entity should recognize revenue to reflect the transfer of goods and services to customers in an amount equal to the consideration the entity receives or expects to receive. The guidance also included expanded disclosure requirements that result in an entity providing users of financial statements with comprehensive information about the nature, amount, timing, and uncertainty of revenue and cash flows arising from the entity's contracts with customers. Based on input received from stakeholders, the FASB issued several additional Updates that generally provided clarifying guidance where there was the potential for diversity in practice, or address the cost and complexity of applying Topic 606.

The Association maintains contracts with customers to provide support services in various areas such as accounting, lending transactions, consulting, insurance, and information technology. The Association does not generally incur costs to obtain contracts. As most of the contracts are to provide access to expertise or system capacity that the Association maintains, there are no material incremental costs to fulfill these contracts that should be capitalized.

Transition Information

- The Association identified ancillary revenues affected by this Update and adopted the guidance on January 1, 2018.
- The amendments were applied using the modified retrospective approach.
- The Association elected to only apply the guidance to contracts that were not completed at the date of initial application.
- Subtopics 610-20 on gains and losses from the derecognition of nonfinancial assets, and 340-40 on other assets and deferred costs-contracts with customers were adopted using the same transition options.
- Adoption did not have an impact on the Association's financial condition or results of operations.

Gains and Losses from Nonfinancial Assets
Any gains or losses on sales of Premises and Equipment and OPO are included as part of Other Noninterest Income. These gains and losses are recognized, and the nonfinancial asset is derecognized, when the Association has entered into a valid contract with a noncustomer and transferred control of the asset. If the criteria to meet the definition of a contract have not been met, the Association does not derecognize the nonfinancial asset and any consideration received is recognized as a liability. If the criteria for a contract are subsequently met, or if the consideration received is or becomes nonrefundable, a gain or loss may be recognized at that time.

N. **Accounting Standards Updates (ASUs):** In August 2018, the FASB issued ASU 2018-15 Intangibles—Goodwill and Other—Internal-Use Software (Subtopic 350-40): Customer's Accounting for Implementation Costs Incurred in a Cloud Computing Arrangement That Is a Service Contract. The amendments align 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 the amendments in this Update. The guidance is effective for public business entities for fiscal years beginning after December 15, 2019, and interim periods within those fiscal years. Early adoption is permitted, including adoption in any interim period, for all entities. The amendments should be applied either retrospectively or prospectively to all implementation costs incurred after the date of adoption.Adoption of the guidance will have no impact on the statements of financial condition and results of operations.

In August 2018, the FASB issued ASU 2018-13 Disclosure Framework—Changes to the Disclosure Requirements for Fair Value Measurement. The amendments are part of the FASB's disclosure framework project. The project's objective and primary focus are to improve the effectiveness of disclosures in the notes to financial statements by facilitating clear communication of the information required by GAAP that is most important to users of each entity's financial statements. The amendments remove, modify or add certain disclosures contained in the financial statement footnotes related to fair value. Additionally, the guidance is intended to promote the appropriate exercise of discretion by entities when considering fair value measurement disclosures and to clarify that materiality is an appropriate consideration of entities and their auditors when evaluating disclosure requirements. The amendments are effective for all entities for fiscal years, and interim periods within those fiscal years, beginning after December 15, 2019. Certain amendments should be applied prospectively for only the most recent interim or annual period presented in the initial fiscal year of adoption. All other amendments should be applied retrospectively to all periods presented upon their effective date. Entities may early adopt the provisions in whole upon issuance or may early adopt any removed or modified disclosures upon issuance and delay adoption of the additional disclosures until their effective date. The Association has adopted the removed disclosures effective with the 2018 Annual Report.

In July 2018, the FASB issued ASU 2018-09 Codification Improvements. The amendments affect a wide variety of Topics in the Codification. They apply to all reporting entities within the scope of the affected accounting guidance. The Board has an ongoing project on its agenda about improvements to clarify the Codification or to correct unintended application of guidance. Those items generally are not expected to have a significant effect on current accounting practice. The transition and effective date guidance is based on the facts and circumstances of each amendment.

In February 2018, the FASB issued ASU 2018-02 Income Statement—Reporting Comprehensive Income (Topic 220): Reclassification of Certain Tax Effects from Accumulated Other Comprehensive Income. The guidance allows a reclassification from accumulated other comprehensive income to retained earnings for stranded tax effects resulting from the Tax Cuts and Jobs Act. The amendments eliminate the stranded tax effects resulting from the Tax Cuts and Jobs Act and are intended to improve the usefulness of information reported to financial statement users. However, because the amendments only relate to the reclassification of the income tax effects of the Tax Cuts and Jobs Act, the underlying guidance that requires that the effect of a change in tax laws or rates be included in income from continuing operations is not affected. The Update also requires certain disclosures about stranded tax effects. The guidance is effective for all entities for fiscal years beginning after December 15, 2018, and interim periods within those fiscal years. The Associaation is in the process of evaluating what effects the guidance may have on the statements of financial condition and results of operations.

In March 2017, the FASB issued ASU 2017-08 Receivables—Nonrefundable Fees and Other Costs (Subtopic 310-20): Premium Amortization on Purchased Callable Debt Securities. The guidance relates to certain callable debt securities and shortens the amortization period for any premium to the earliest call date. The Update will be effective for interim and annual periods beginning after December 15, 2018 for public business entities. The Association is in the process of evaluating what effects the guidance may have on the statements of financial condition and results of operations.

In March 2017, the FASB issued ASU 2017-07 Compensation—Retirement Benefits (Topic 715): Improving the Presentation of Net Periodic Pension Cost and Net Periodic Postretirement Benefit Cost related to the income statement presentation of the components of net periodic benefit cost for an entity's sponsored defined benefit pension and other postretirement plans. The amendments were effective January 1, 2018 for the Association. Adoption in 2018 did not have a material effect on the Association's financial statements, but did require reclassification of certain periodic pension costs to Other Operating Expenses.

In January 2017, the FASB issued ASU 2017-01 Business Combinations (Topic 805): Clarifying the Definition of a Business. The amendments provide a more robust framework to use in determining when a set of assets and activities is a business. They also support more consistency in applying the guidance, reduce the costs of application, and make the definition of a business more operable. The ASU was effective January 1, 2018 for the Association. The amendments were applied prospectively. Adoption of the guidance in 2018 had no impact on the statements of financial condition and results of operations of the Association.

In June 2016, the FASB issued ASU 2016-13 Financial Instruments—Credit Losses (Topic 326): Measurement of Credit Losses on Financial Instruments. This Update, and subsequent clarifying guidance issued, is intended to improve financial reporting by requiring timelier recording of credit losses on financial instruments. It requires an organization to measure all expected credit losses for financial assets held at the reporting date. Financial institutions and other organizations will use forward-looking information to better estimate their credit losses. Additionally, the ASU amends the accounting for credit losses on available-for-sale debt securities and purchased financial assets with credit deterioration. For public companies that are not SEC filers, it will take effect for fiscal years beginning after December 15, 2020, and interim periods within those fiscal years. Early application will be permitted for all organizations for fiscal years, and interim periods within those fiscal years, beginning after December 15, 2018. The Association is in the process of evaluating what effects the guidance may have on the statements of financial condition and results of operations.

In February 2016, the FASB issued ASU 2016-02 Leases (Topic 842). This Update, and subsequent clarifying guidance issued, requires organizations that lease assets to recognize on the balance sheet the assets and liabilities for the rights and obligations created by those leases. Leases will be classified as either finance leases or operating leases. This distinction will be relevant for the pattern of expense recognition in the income statement. The amendments will be effective for fiscal years beginning after December 15, 2018, including interim periods within those fiscal years for public business entities. The Association will implement the guidance in first quarter 2019 using the practical expedients and does not expect a material impact to the financial statements.

In January 2016, the FASB issued ASU 2016-01 Financial Instruments—Overall (Subtopic 825-10): Recognition and Measurement of Financial Assets and Financial Liabilities. The Update, and subsequent clarifying guidance issued, was intended to improve the recognition and measurement of financial instruments. The new guidance makes targeted improvements to existing GAAP.

Transition Information

- The Association identified investment securities affected by this Update and adopted the guidance on January 1, 2018.
- The amendments related to equity securities without readily determinable fair values were applied prospectively to equity investments that existed as of the date of adoption.
- Application of the amendments did not require a cumulative effect adjustment.
- Adoption did not have an impact on the Association's financial condition or results of operations.
- The new standard did result in changes to certain disclosures.

Note 3 — Loans and Allowance for Loan Losses

For a description of the Association's accounting for loans, including impaired loans, and the allowance for loan losses, see Note 2 subsection B above.

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

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 (see further discussion in Note 2 subsection B 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 or facility risk is related to the structure of a credit (tenor, terms, and collateral).

The Association's loan portfolio, which includes purchased interests in loans, has been segmented by the following loan types as defined by the FCA:

- Real estate mortgage loans — loans made to full-time or part-time farmers secured by first lien real estate mortgages with maturities from five to thirty years. These loans may be made only in amounts up to 85 percent of the appraised value of the property taken as security or up to 97 percent of the appraised value if guaranteed by a federal, state, or other governmental agency. The actual percentage of loan-to-appraised value when loans are made is generally lower than the statutory required percentage.
- Production and intermediate-term loans — loans to full-time or part-time farmers that are not real estate mortgage loans. These loans fund eligible financing needs including operating inputs (such as labor, feed, fertilizer, and repairs), livestock, living expenses, income taxes, machinery or equipment, farm buildings, and other business-related expenses. Production loans may be made on a secured or unsecured basis and are most often made for a period of time that matches the borrower's normal production and marketing cycle, which is typically one year or less. Intermediate-term loans are made for a specific term, generally greater than one year and less than or equal to ten years.
- Loans to cooperatives — loans for any cooperative purpose other than for communication, power, and water and waste disposal.
- Processing and marketing loans — loans for operations to process or market the products produced by a farmer, rancher, or producer or harvester of aquatic products, or by a cooperative.
- Farm-related business loans — loans to eligible borrowers that furnish certain farm-related business services to farmers or ranchers that are directly related to their agricultural production.
- Rural residential real estate loans — loans made to individuals, who are not farmers, to purchase a single-family dwelling that will be the primary residence in open country, which may include a town or village that has a population of not more than 2,500 persons. In addition, the loan may be to remodel, improve, or repair a rural home, or to refinance existing debt. These loans are generally secured by a first lien on the property.
- Communication loans — loans primarily to finance rural communication providers.
- Power loans — loans primarily to finance electric generation, transmission and distribution systems serving rural areas.
- Water and waste disposal loans — loans primarily to finance water and waste disposal systems serving rural areas.
- International loans — primarily loans or credit enhancements to other banks to support the export of U.S. agricultural commodities or supplies. The federal government guarantees a substantial portion of these loans.
- Lease receivables — the net investment for all finance leases such as direct financing leases, leveraged leases, and sales-type leases.
- Other (including Mission Related) — additional investments in rural America approved by the FCA on a program or a case-by-case basis. Examples of such investments include partnerships with agricultural and rural community lenders, investments in rural economic development and infrastructure, and investments in obligations and mortgage securities that increase the availability of affordable housing in rural America.

A summary of loans outstanding at period end follows:

	December 31,		
	2018	2017	2016
Real estate mortgage	$ 1,371,535	$ 1,354,874	$ 1,307,311
Production and intermediate-term	361,653	374,931	387,878
Loans to cooperatives	–	–	64
Processing and marketing	33,143	35,018	30,144
Farm-related business	17,993	20,829	17,754
Communication	6,737	7,252	9,670
Rural residential real estate	59,716	52,045	46,175
Total loans	$ 1,850,777	$ 1,844,949	$ 1,798,996

A substantial portion of the Association's lending activities is collateralized and the Association's exposure to credit loss associated with lending activities is reduced accordingly.

The amount of collateral obtained, if deemed necessary upon extension of credit, is based on management's credit evaluation of the borrower. Collateral held varies, but typically includes farmland and income-producing property, such as crops and livestock, as well as receivables. Long-term real estate loans are collateralized by the first liens on the underlying real property. Federal regulations state that long-term real estate loans are not to exceed 85 percent (97 percent if guaranteed by a government agency) of the property's appraised value. However, a decline in a property's market value subsequent to loan origination or advances, or other actions necessary to protect the financial interest of the Association in the collateral, may result in loan to value ratios in excess of the regulatory maximum.

The Association may purchase or sell participation interests with other parties in order to diversify risk, manage loan volume, and comply with FCA regulations. During 2016, the Association canceled its participation in the Capitalized Participation Pool program with the Bank. As a result, the Association repurchased $73,558 of participations previously sold to AgFirst. The following tables present the principal balance of participation loans at periods ended:

December 31, 2018	Within AgFirst District		Within Farm Credit System		Outside Farm Credit System		Total	
	Participations Purchased	Participations Sold	Participations Purchased	Participations Sold	Participations Purchased	Participations Sold	Participations Purchased	Participations Sold
Real estate mortgage	$ 10,075	$ 16,412	$ –	$ –	$ –	$ –	$ 10,075	$ 16,412
Production and intermediate-term	13,870	4,849	305	–	–	–	14,175	4,849
Processing and marketing	5,464	–	21	–	–	–	5,485	–
Farm-related business	836	–	–	–	–	–	836	–
Communication	6,751	–	–	–	–	–	6,751	–
Total	$ 36,996	$ 21,261	$ 326	$ –	$ –	$ –	$ 37,322	$ 21,261

December 31, 2017	Within AgFirst District		Within Farm Credit System		Outside Farm Credit System		Total	
	Participations Purchased	Participations Sold	Participations Purchased	Participations Sold	Participations Purchased	Participations Sold	Participations Purchased	Participations Sold
Real estate mortgage	$ 5,501	$ 9,714	$ –	$ –	$ –	$ –	$ 5,501	$ 9,714
Production and intermediate-term	9,595	2,948	360	–	–	–	9,955	2,948
Processing and marketing	8,476	–	147	–	–	–	8,623	–
Farm-related business	389	–	–	–	–	–	389	–
Communication	7,271	–	–	–	–	–	7,271	–
Total	$ 31,232	$ 12,662	$ 507	$ –	$ –	$ –	$ 31,739	$ 12,662

December 31, 2016	Within AgFirst District		Within Farm Credit System		Outside Farm Credit System		Total	
	Participations Purchased	Participations Sold	Participations Purchased	Participations Sold	Participations Purchased	Participations Sold	Participations Purchased	Participations Sold
Real estate mortgage	$ 3,961	$ 10,312	$ –	$ –	$ –	$ –	$ 3,961	$ 10,312
Production and intermediate-term	9,540	4,585	415	–	–	–	9,955	4,585
Processing and marketing	6,204	–	189	–	–	–	6,393	–
Farm-related business	110	–	–	–	–	–	110	–
Communication	9,672	–	–	–	–	–	9,672	–
Total	$ 29,487	$ 14,897	$ 604	$ –	$ –	$ –	$ 30,091	$ 14,897

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

December 31, 2018	Due less than 1 year	Due 1 Through 5 years	Due after 5 years	Total
Real estate mortgage	$ 2,113	$ 53,495	$ 1,315,927	$ 1,371,535
Production and intermediate-term	159,844	148,194	53,615	361,653
Processing and marketing	22,120	2,053	8,970	33,143
Farm-related business	5,454	3,922	8,617	17,993
Communication	–	2,127	4,610	6,737
Rural residential real estate	6,707	3,412	49,597	59,716
Total loans	$ 196,238	$ 213,203	$ 1,441,336	$ 1,850,777
Percentage	10.60%	11.52%	77.88%	100.00%

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.

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:

	December 31,		
	2018	2017	2016
Real estate mortgage:			
Acceptable	94.24%	95.84%	95.55%
OAEM	3.49	1.96	1.79
Substandard/doubtful/loss	2.27	2.20	2.66
	100.00%	100.00%	100.00%
Production and intermediate-term:			
Acceptable	90.86%	92.26%	94.44%
OAEM	6.06	3.70	2.21
Substandard/doubtful/loss	3.08	4.04	3.35
	100.00%	100.00%	100.00%
Loans to cooperatives:			
Acceptable	–%	–%	100.00%
OAEM	–	–	–
Substandard/doubtful/loss	–	–	–
	–%	–%	100.00%
Processing and marketing:			
Acceptable	81.83%	100.00%	100.00%
OAEM	18.17	–	–
Substandard/doubtful/loss	–	–	–
	100.00%	100.00%	100.00%

	December 31,		
	2018	2017	2016
Farm-related business:			
Acceptable	99.09%	99.32%	97.43%
OAEM	–	–	–
Substandard/doubtful/loss	0.91	0.68	2.57
	100.00%	100.00%	100.00%
Communication:			
Acceptable	100.00%	100.00%	100.00%
OAEM	–	–	–
Substandard/doubtful/loss	–	–	–
	100.00%	100.00%	100.00%
Rural residential real estate:			
Acceptable	96.18%	97.50%	97.08%
OAEM	2.49	1.98	2.09
Substandard/doubtful/loss	1.33	0.52	0.83
	100.00%	100.00%	100.00%
Total loans:			
Acceptable	93.49%	95.29%	95.46%
OAEM	4.18	2.25	1.83
Substandard/doubtful/loss	2.33	2.46	2.71
	100.00%	100.00%	100.00%

The following tables provide an aging analysis of past due loans and related accrued interest as of:

	December 31, 2018				
	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
Real estate mortgage	$ 8,658	$ 3,446	$ 12,104	$ 1,366,093	$ 1,378,197
Production and intermediate-term	3,679	3,946	7,625	357,527	365,152
Processing and marketing	–	–	–	33,191	33,191
Farm-related business	150	15	165	17,921	18,086
Communication	–	–	–	6,738	6,738
Rural residential real estate	1,626	82	1,708	58,223	59,931
Total	$ 14,113	$ 7,489	$ 21,602	$ 1,839,693	$ 1,861,295

	December 31, 2017				
	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
Real estate mortgage	$ 11,111	$ 5,692	$ 16,803	$ 1,344,425	$ 1,361,228
Production and intermediate-term	3,892	6,900	10,792	367,597	378,389
Processing and marketing	117	–	117	34,944	35,061
Farm-related business	109	192	301	20,608	20,909
Communication	–	–	–	7,254	7,254
Rural residential real estate	897	25	922	51,313	52,235
Total	$ 16,126	$ 12,809	$ 28,935	$ 1,826,141	$ 1,855,076

	December 31, 2016				
	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
Real estate mortgage	$ 6,995	$ 4,936	$ 11,931	$ 1,301,054	$ 1,312,985
Production and intermediate-term	2,511	5,405	7,916	383,408	391,324
Loans to cooperatives	–	–	–	64	64
Processing and marketing	139	–	139	30,009	30,148
Farm-related business	–	193	193	17,615	17,808
Communication	–	–	–	9,672	9,672
Rural residential real estate	129	–	129	46,218	46,347
Total	$ 9,774	$ 10,534	$ 20,308	$ 1,788,040	$ 1,808,348

Nonperforming assets (including related accrued interest) and related credit quality statistics at period end were as follows:

	December 31,		
	2018	2017	2016
Nonaccrual loans:			
Real estate mortgage	$ 13,875	$ 17,906	$ 20,813
Production and intermediate-term	8,260	12,009	9,963
Farm-related business	165	1,932	2,657
Rural residential real estate	112	80	145
Total	$ 22,412	$ 31,927	$ 33,578
Accruing restructured loans:			
Real estate mortgage	$ 1,364	$ 1,101	$ 976
Production and intermediate-term	519	548	466
Total	$ 1,883	$ 1,649	$ 1,442
Accruing loans 90 days or more past due:			
Real estate mortgage	$ –	$ –	$ 114
Production and intermediate-term	–	55	–
Total	$ –	$ 55	$ 114
Performing impaired loans:			
Real estate mortgage	$ 983	$ 1,931	$ 2,175
Production and intermediate-term	956	1,969	712
Total	$ 1,939	$ 3,900	$ 2,887
Total nonperforming loans	$ 26,234	$ 37,531	$ 38,021
Other property owned	1,477	1,221	2,467
Total nonperforming assets	$ 27,711	$ 38,752	$ 40,488
Nonaccrual loans as a percentage of total loans	1.21%	1.73%	1.87%
Nonperforming assets as a percentage of total loans and other property owned	1.50%	2.10%	2.25%
Nonperforming assets as a percentage of capital	6.29%	9.17%	10.36%

The following table presents information relating to impaired loans (including accrued interest) as defined in Note 2:

	December 31,		
	2018	2017	2016
Impaired nonaccrual loans:			
Current as to principal and interest	$ 12,433	$ 17,065	$ 21,177
Past due	9,979	14,862	12,401
Total	$ 22,412	$ 31,927	$ 33,578
Impaired accrual loans:			
Performing	$ 1,939	$ 3,900	$ 2,887
Restructured	1,883	1,649	1,442
90 days or more past due	–	55	114
Total	$ 3,822	$ 5,604	$ 4,443
Total impaired loans	$ 26,234	$ 37,531	$ 38,021
Additional commitments to lend	$ 16	$ 150	$ 191

The following tables present additional impaired loan information at period end. Unpaid principal balance represents the contractual principal balance of the loan.

	December 31, 2018			Year Ended December 31, 2018	
Impaired loans:	**Recorded Investment**	**Unpaid Principal Balance**	**Related Allowance**	**Average Impaired Loans**	**Interest Income Recognized on Impaired Loans**
With a related allowance for credit losses:					
Real estate mortgage	$ 4,136	$ 4,362	$ 501	$ 4,896	$ 516
Production and intermediate-term	6,091	7,482	1,085	7,210	759
Farm-related business	16	15	16	18	2
Rural residential real estate	83	83	31	98	10
Total	$ 10,326	$ 11,942	$ 1,633	$ 12,222	$ 1,287
With no related allowance for credit losses:					
Real estate mortgage	$ 12,086	$ 14,667	$ –	$ 14,305	$ 1,505
Production and intermediate-term	3,644	6,136	–	4,312	454
Farm-related business	149	292	–	177	19
Rural residential real estate	29	158	–	34	4
Total	$ 15,908	$ 21,253	$ –	$ 18,828	$ 1,982
Total impaired loans:					
Real estate mortgage	$ 16,222	$ 19,029	$ 501	$ 19,201	$ 2,021
Production and intermediate-term	9,735	13,618	1,085	11,522	1,213
Farm-related business	165	307	16	195	21
Rural residential real estate	112	241	31	132	14
Total	$ 26,234	$ 33,195	$ 1,633	$ 31,050	$ 3,269

	December 31, 2017			Year Ended December 31, 2017	
Impaired loans:	**Recorded Investment**	**Unpaid Principal Balance**	**Related Allowance**	**Average Impaired Loans**	**Interest Income Recognized on Impaired Loans**
With a related allowance for credit losses:					
Real estate mortgage	$ 1,930	$ 2,070	$ 138	$ 1,804	$ 71
Production and intermediate-term	10,412	11,051	4,182	9,735	380
Farm-related business	–	–	–	–	–
Rural residential real estate	–	–	–	–	–
Total	$ 12,342	$ 13,121	$ 4,320	$ 11,539	$ 451
With no related allowance for credit losses:					
Real estate mortgage	$ 19,008	$ 22,508	$ –	$ 17,772	$ 694
Production and intermediate-term	4,169	7,746	–	3,897	153
Farm-related business	1,932	2,934	–	1,806	71
Rural residential real estate	80	208	–	75	3
Total	$ 25,189	$ 33,396	$ –	$ 23,550	$ 921
Total impaired loans:					
Real estate mortgage	$ 20,938	$ 24,578	$ 138	$ 19,576	$ 765
Production and intermediate-term	14,581	18,797	4,182	13,632	533
Farm-related business	1,932	2,934	–	1,806	71
Rural residential real estate	80	208	–	75	3
Total	$ 37,531	$ 46,517	$ 4,320	$ 35,089	$ 1,372

	December 31, 2016			Year Ended December 31, 2016	
Impaired loans:	**Recorded Investment**	**Unpaid Principal Balance**	**Related Allowance**	**Average Impaired Loans**	**Interest Income Recognized on Impaired Loans**
With a related allowance for credit losses:					
Real estate mortgage	$ 2,593	$ 2,753	$ 218	$ 2,579	$ 80
Production and intermediate-term	4,940	5,698	513	4,912	152
Farm-related business	2,465	3,229	92	2,451	76
Rural residential real estate	–	–	–	–	–
Total	$ 9,998	$ 11,680	$ 823	$ 9,942	$ 308
With no related allowance for credit losses:					
Real estate mortgage	$ 21,485	$ 24,460	$ –	$ 21,364	$ 661
Production and intermediate-term	6,201	9,596	–	6,166	191
Farm-related business	192	430	–	191	6
Rural residential real estate	145	292	–	144	4
Total	$ 28,023	$ 34,778	$ –	$ 27,865	$ 862
Total impaired loans:					
Real estate mortgage	$ 24,078	$ 27,213	$ 218	$ 23,943	$ 741
Production and intermediate-term	11,141	15,294	513	11,078	343
Farm-related business	2,657	3,659	92	2,642	82
Rural residential real estate	145	292	–	144	4
Total	$ 38,021	$ 46,458	$ 823	$ 37,807	$ 1,170

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*	Communication	Rural Residential Real Estate	Total
Activity related to the allowance for credit losses:						
Balance at December 31, 2017	$ 6,160	$ 10,296	$ 575	$ 80	$ 350	$ 17,461
Charge-offs	(225)	(4,699)	(99)	–	(12)	(5,035)
Recoveries	221	163	–	–	3	387
Provision for loan losses	(14)	2,062	504	(26)	(26)	2,500
Balance at December 31, 2018	$ 6,142	$ 7,822	$ 980	$ 54	$ 315	$ 15,313
Balance at December 31, 2016	$ 6,472	$ 6,989	$ 697	$ –	$ 325	$ 14,483
Charge-offs	(138)	(492)	–	–	–	(630)
Recoveries	73	181	104	–	–	358
Provision for loan losses	(247)	3,618	(226)	80	25	3,250
Balance at December 31, 2017	$ 6,160	$ 10,296	$ 575	$ 80	$ 350	$ 17,461
Balance at December 31, 2015	$ 6,920	$ 6,594	$ 613	$ –	$ 360	$ 14,487
Charge-offs	(1,005)	(1,677)	(222)	–	(80)	(2,984)
Recoveries	147	83	–	–	–	230
Provision for loan losses	410	1,989	306	–	45	2,750
Balance at December 31, 2016	$ 6,472	$ 6,989	$ 697	$ –	$ 325	$ 14,483
Allowance on loans evaluated for impairment:						
Individually	$ 501	$ 1,085	$ 16	$ –	$ 31	$ 1,633
Collectively	5,641	6,737	964	54	284	13,680
Balance at December 31, 2018	$ 6,142	$ 7,822	$ 980	$ 54	$ 315	$ 15,313
Individually	$ 138	$ 4,182	$ –	$ –	$ –	$ 4,320
Collectively	6,022	6,114	575	80	350	13,141
Balance at December 31, 2017	$ 6,160	$ 10,296	$ 575	$ 80	$ 350	$ 17,461
Individually	$ 218	$ 513	$ 92	$ –	$ –	$ 823
Collectively	6,254	6,476	605	–	325	13,660
Balance at December 31, 2016	$ 6,472	$ 6,989	$ 697	$ –	$ 325	$ 14,483
Recorded investment in loans evaluated for impairment:						
Individually	$ 16,222	$ 9,735	$ 165	$ –	$ 112	$ 26,234
Collectively	1,361,975	355,417	51,112	6,738	59,819	1,835,061
Balance at December 31, 2018	$ 1,378,197	$ 365,152	$ 51,277	$ 6,738	$ 59,931	$ 1,861,295
Individually	$ 20,938	$ 14,581	$ 1,932	$ –	$ 80	$ 37,531
Collectively	1,340,290	363,808	54,038	7,254	52,155	1,817,545
Balance at December 31, 2017	$ 1,361,228	$ 378,389	$ 55,970	$ 7,254	$ 52,235	$ 1,855,076
Individually	$ 24,078	$ 11,141	$ 2,657	$ –	$ 145	$ 38,021
Collectively	1,288,907	380,183	45,363	9,672	46,202	1,770,327
Balance at December 31, 2016	$ 1,312,985	$ 391,324	$ 48,020	$ 9,672	$ 46,347	$ 1,808,348

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

To mitigate risk of loan losses, the Association may enter into guarantee arrangements with certain GSEs, including the Federal Agricultural Mortgage Corporation (Farmer Mac), and state or federal agencies. These guarantees generally remain in place until the loans are paid in full or expire and give the Association the right to be reimbursed for losses incurred or to sell designated loans to the guarantor in the event of default (typically four months past due), subject to certain conditions. The guaranteed balance of designated loans under these agreements was $37,559, $46,005, and $44,334 at December 31, 2018, 2017, and 2016, respectively. Fees paid for such guarantee commitments totaled $29, $38, and $54 for 2018, 2017, and 2016, respectively. These amounts are classified as noninterest expense.

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

	Year Ended December 31, 2018				
Outstanding Recorded Investment	**Interest Concessions**	**Principal Concessions**	**Other Concessions**	**Total**	**Charge-offs**
Pre-modification:					
Real estate mortgage	$ 2,003	$ 910	$ –	$ 2,913	
Production and intermediate-term	1,934	1,016	–	2,950	
Total	$ 3,937	$ 1,926	$ –	$ 5,863	
Post-modification:					
Real estate mortgage	$ 2,003	$ 870	$ –	$ 2,873	$ (6)
Production and intermediate-term	1,934	743	–	2,677	–
Total	$ 3,937	$ 1,613	$ –	$ 5,550	$ (6)

Outstanding Recorded Investment	Year Ended December 31, 2017 Interest Concessions	Principal Concessions	Other Concessions	Total	Charge-offs
Pre-modification:					
Real estate mortgage	$ –	$ 151	$ –	$ 151	
Production and intermediate-term	–	616	–	616	
Total	$ –	$ 767	$ –	$ 767	
Post-modification:					
Real estate mortgage	$ –	$ 151	$ –	$ 151	$ –
Production and intermediate-term	–	616	–	616	–
Total	$ –	$ 767	$ –	$ 767	$ –

Outstanding Recorded Investment	Year Ended December 31, 2016 Interest Concessions	Principal Concessions	Other Concessions	Total	Charge-offs
Pre-modification:					
Real estate mortgage	$ –	$ 1,324	$ –	$ 1,324	
Production and intermediate-term	1,112	1,091	–	2,203	
Total	$ 1,112	$ 2,415	$ –	$ 3,527	
Post-modification:					
Real estate mortgage	$ –	$ 988	$ –	$ 988	$ –
Production and intermediate-term	1,112	1,091	–	2,203	–
Total	$ 1,112	$ 2,079	$ –	$ 3,191	$ –

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.

Defaulted troubled debt restructurings	Year Ended December 31, 2018	2017	2016
Real estate mortgage	$ –	$ –	$ 60
Production and intermediate-term	131	216	78
Total	$ 131	$ 216	$ 138

The following table provides information at each 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		
	December 31,			December 31,		
	2018	2017	2016	2018	2017	2016
Real estate mortgage	$ 4,776	$ 2,492	$ 2,526	$ 3,412	$ 1,391	$ 1,550
Production and intermediate-term	4,796	4,318	5,190	4,277	3,770	4,724
Farm related business	–	1,740	2,465	–	1,740	2,465
Rural residential real estate	18	25	29	18	25	29
Total loans	$ 9,590	$ 8,575	$ 10,210	$ 7,707	$ 6,926	$ 8,768
Additional commitments to lend	$ –	$ 130	$ –			

The following table presents information as of period end:

	December 31, 2018
Carrying amount of foreclosed residential real estate properties held as a result of obtaining physical possession	$ –
Recorded investment of consumer mortgage loans secured by residential real estate for which formal foreclosure proceedings are in process	$ –

Note 4 — Investments

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

The Association is required to maintain ownership in the Bank in the form of Class B or Class C stock as determined by the Bank. The Bank may require additional capital contributions to maintain its capital requirements. The Association's investment in the Bank totaled $19,874 for 2018, $19,885 for 2017 and $18,878 for 2016. The Association owns 7.27 percent of the issued stock of the Bank as of December 31, 2018 net of any reciprocal investment. As of that date, the Bank's assets totaled $33.1 billion and shareholders' equity totaled $2.2 billion. The Bank's earnings were $306 million for 2018. In addition, the Association had $854 investments related to other Farm Credit institutions at December 31, 2018.

Note 5 — Real Estate and Other Property

Premises and Equipment
Premises and equipment consists of the following:

	December 31,		
	2018	2017	2016
Land	$ 4,151	$ 3,842	$ 3,828
Buildings and improvements	9,706	8,556	8,516
Furniture and equipment	5,914	5,609	5,685
	19,771	18,007	18,029
Less: accumulated depreciation	8,219	7,865	7,801
Total	$ 11,552	$ 10,142	$ 10,228

Other Property Owned
Net (gains) losses on other property owned consist of the following:

	December 31,		
	2018	2017	2016
(Gains) losses on sale, net	$ 51	$ 655	$ 188
Carrying value unrealized (gains) losses	1	(67)	(8)
Operating (income) expense, net	19	27	106
(Gains) losses on other property owned, net	$ 71	$ 615	$ 286

Gains on sales of other property owned were deferred if the sales involved financing from the Association and did not meet the criteria for immediate recognition. Deferred gains totaled $139, $145, and $150 at December 31, 2018, 2017, and 2016, respectively.

Note 6 — Debt

Notes Payable to AgFirst Farm Credit Bank
Under the Farm Credit Act, the Association is obligated to borrow only from the Bank, unless the Bank approves borrowing from other funding sources. The borrowing relationship is established with the Bank through a General Financing Agreement (GFA). The GFA utilizes the Association's credit and fiscal performance as criteria for establishing a line of credit on which the Association may draw funds. The GFA has a one year term which expires on December 31 and is renewable each year. The Association has no reason to believe the GFA will not be renewed upon expiration. The Bank, consistent with FCA regulations, has established limitations on the Association's ability to borrow funds based on specified factors or formulas relating primarily to credit quality and financial condition. At December 31, 2018, the Association's notes payable were within the specified limitations.

The Association's indebtedness to the Bank represents borrowings by the Association to fund its earning assets. This indebtedness is collateralized by a pledge of substantially all of the Association's assets and the terms of the revolving lines of credit are governed by the GFA. Interest rates on both variable and fixed rate advances are generally established loan-by-loan, based on the Bank's marginal cost of funds, capital position, operating costs and return objectives. In the event of prepayment of any portion of a fixed rate advance, the Association may incur a prepayment penalty in accordance with the terms of the GFA, which will be included in interest expense. The interest rate is periodically adjusted by the Bank based upon an agreement between the Bank and the Association.

The weighted average interest rates on the variable rate advances were 3.41 percent for LIBOR-based loans and 3.45 percent for Prime-based loans, and the weighted average remaining maturities were 4.8 years and 4.0 years, respectively, at December 31, 2018. The weighted-average interest rate on the fixed rate and adjustable rate mortgage (ARM) loans which are match funded by the Bank was 3.43 percent, and the weighted average remaining maturity was 13.1 years at December 31, 2018. The weighted-average interest rate on all interest-bearing notes payable was 3.42 percent and the weighted-average remaining maturity was 11.5 years at December 31, 2018. Gross notes payable consists of approximately 81.10 percent fixed rate and 18.90 percent variable rate portions, representing a match-funding of the Association's loan volume at December 31, 2018. Notes payable to the Bank, as reflected on the Consolidated Balance Sheets, also includes a credit which reduces the note payable and corresponding interest expense. The weighted average maturities described above are related to matched-funded loans. The direct note itself has an annual maturity as prescribed in the GFA.

On January 16, 2019, the Bank approved a waiver of the Association's events of default under the GFA.

Note 7 — Members' Equity

A description of the Association's capitalization requirements, protection mechanisms, regulatory capitalization requirements and restrictions, and equities are provided below:

A. **Capital Stock and Participation Certificates:** In accordance with the Farm Credit Act and the Association's capitalization bylaws, each borrower is required to invest in Class C Common Stock for agricultural loans or Participation Certificates in the case of rural home and farm-related business loans, as a condition of borrowing.

The initial borrower investment, through either purchase or transfer, must be a minimum of 2 percent of the loan amount or $1 thousand, or such higher amount as determined by the Board. The Board of Directors may increase the amount of investment if necessary to meet the Association's capital needs. Loans designated for sale or sold into the Secondary Market on or after April 16, 1996 will have no voting stock or participation certificate purchase requirement if sold within 180 days following the date of designation.

The borrower acquires ownership of the capital stock or participation certificates at the time the loan is made, but usually does not make a cash investment. The aggregate par value is generally added to the principal amount of the related loan obligation. The Association retains a first lien on the stock or participation certificates owned by borrowers. Retirement of such equities will generally be at the lower of par or book value, and repayment of a loan does not automatically result in retirement of the corresponding stock or participation certificates.

B. **Regulatory Capitalization Requirements and Restrictions:** An FCA regulation empowers it to direct a transfer of funds or equities by one or more System institutions to another System institution under specified circumstances. The Association has not been called upon to initiate any transfers and is not aware of any proposed action under this regulation.

There are currently no prohibitions in place that would prevent the Association from retiring stock, distributing earnings, or paying dividends per the statutory and regulatory restrictions, and the Association has no reason to believe any such restrictions may apply in the future.

Effective January 1, 2017, the regulatory capital requirements for System Banks and associations were modified. The new regulations ensure that the System's capital requirements are comparable to the Basel III framework and the standardized approach that the federal banking regulatory agencies have adopted. New regulations replaced core surplus and total surplus ratios with common equity tier 1 (CET1) capital, tier 1 capital, and total capital risk-based ratios. The new regulations also include a tier 1 leverage ratio and an unallocated retained earnings (URE) and URE equivalents (UREE) leverage ratio. The permanent capital ratio (PCR) remains in effect.

The ratios are calculated using three-month average daily balances, in accordance with FCA regulations, as follows:

- The CET1 capital ratio is the sum of statutory minimum purchased borrower stock, other required borrower stock held for a minimum of 7 years, allocated equities held for a minimum of 7 years or not subject to revolvement, unallocated retained earnings, paid-in capital, less certain regulatory required deductions including the amount of investments in other System institutions, divided by average risk-adjusted assets.
- The tier 1 capital ratio is CET1 capital plus non-cumulative perpetual preferred stock, divided by average risk-adjusted assets.
- The total capital ratio is tier 1 capital plus other required borrower stock held for a minimum of 5 years, subordinated debt and limited-life preferred stock greater than 5 years to maturity at issuance subject to certain limitations, allowance for loan losses and reserve for unfunded commitments under certain limitations less certain investments in other System institutions under the corresponding deduction approach, divided by average risk-adjusted assets.
- The permanent capital ratio is all at-risk borrower stock, any allocated excess stock, unallocated retained earnings, paid-in capital, subordinated debt and preferred stock subject to certain limitations, less certain investments in other System institutions, divided by PCR risk-adjusted assets.
- The tier 1 leverage ratio is tier 1 capital, divided by average assets less regulatory deductions to tier 1 capital.
- The URE and UREE leverage ratio is unallocated retained earnings, paid-in capital, and allocated surplus not subject to revolvement less certain regulatory required deductions including the amount of allocated investments in other System institutions divided by average assets less regulatory deductions to tier 1 capital.

The following sets forth the regulatory capital ratios which were effective January 1, 2017:

Ratio	Minimum Requirement	Capital Conservation Buffer*	Minimum Requirement with Capital Conservation Buffer	Capital Ratios as of December 31, 2018	2017
Risk-adjusted ratios:					
CET1 Capital	4.5%	1.25%	5.75%	22.30%	20.93%
Tier 1 Capital	6.0%	1.25%	7.25%	22.30%	20.93%
Total Capital	8.0%	1.25%	9.25%	23.10%	21.72%
Permanent Capital	7.0%	0.0%	7.0%	22.48%	21.09%
Non-risk-adjusted ratios:					
Tier 1 Leverage	4.0%	1.0%	5.0%	22.84%	21.41%
URE and UREE Leverage	1.5%	0.0%	1.5%	23.07%	21.59%

** The capital conservation buffers have a 3 year phase-in period and will become fully effective January 1, 2020. Risk-adjusted ratio minimums will increase 0.625% each year until fully phased in. There is no phase-in period for the tier 1 leverage ratio.*

If the capital ratios fall below the minimum regulatory requirements, including the buffer amounts, capital distributions (equity redemptions, dividends, and patronage) and discretionary senior executive bonuses are restricted or prohibited without prior FCA approval.

C. **Description of Equities:** The Association is authorized to issue or have outstanding Class D Preferred Stock, Classes A and C Common Stock, Participation Certificates and such other classes of equity as may be provided for in amendments to the bylaws in such amounts as may be necessary to conduct the Association's business. All stock and participation certificates have a par or face value of five dollars ($5.00) per share.

The Association had the following shares outstanding at December 31, 2018:

		Shares Outstanding	
Class	Protected	Number	Aggregate Par Value
C Common/Voting	No	1,931,845	$ 9,659
Participation Certificates/Nonvoting	No	153,421	767
Total Capital Stock and Participation Certificates		2,085,266	$ 10,426

At-risk common stock and participation certificates are retired at the sole discretion of the Board at book value not to exceed par or face amounts, provided the minimum capital adequacy standards established by the Board are met.

Retained Earnings

The Association maintains an unallocated retained earnings account and an allocated retained earnings account. The minimum aggregate amount of these two accounts is determined by the Board. At the end of any fiscal year, if the retained earnings accounts otherwise would be less than the minimum amount determined by the Board as necessary to maintain adequate capital reserves to meet the commitments of the Association, the Association shall apply earnings for the year to the unallocated retained earnings account in such amounts as may be determined necessary by the Board.

The Association maintains an allocated retained earnings account consisting of earnings held and allocated to borrowers on a patronage basis. In the event of a net loss for any fiscal year, such allocated retained earnings account will be subject to full impairment in the order specified in the bylaws beginning with the most recent allocation.

The Association has a first lien and security interest on all retained earnings account allocations owned by any borrowers, and all distributions thereof, as additional collateral for their indebtedness to the Association. When the debt of a borrower is in default or is in the process of final liquidation by payment or otherwise, the Association, upon approval of the Board, may order any and all retained earnings account allocations owned by such borrower to be applied on the indebtedness.

Allocated equities shall be retired solely at the discretion of the Board provided that minimum capital standards established by the FCA and the Board are met. Nonqualified retained surplus is considered to be permanently invested in the Association and as such, there is no plan to revolve or retire this surplus. All nonqualified distributions are tax deductible only when redeemed.

At December 31, 2018, allocated members' equity consisted of $92,568 of nonqualified retained surplus.

Patronage Distributions

Prior to the beginning of any fiscal year, the Board, by adoption of a resolution, may obligate the Association to distribute to borrowers on a patronage basis all or any portion of available net earnings for such fiscal year or for that and subsequent fiscal years. Patronage distributions are based on the proportion of the borrower's interest to the amount of interest earned by the Association on its total loans unless another proportionate patronage basis is approved by the Board.

If the Association meets its capital adequacy standards after making the patronage distributions, the patronage distributions may be in cash, authorized stock of the Association, allocations of earnings retained in an allocated members' equity account, or any one or more of such forms of distribution. Patronage distributions of the Association's earnings may be paid on either a qualified or nonqualified basis, or a combination of both, as determined by the Board. A minimum of 20 percent of the total qualified patronage distribution to any borrower for any fiscal year shall always be paid in cash.

The patronage distributions accrued at year-end are based on estimates. The actual amounts distributed may vary from these estimates. Differences are reflected as distribution adjustments in the Consolidated Statements of Changes in Members' Equity.

Dividends

Dividends may be paid on stock and participation certificates as determined by the Board's resolution. Dividends may not be paid on common stock and participation certificates during any fiscal year with respect to which the Association has obligated itself to distribute earnings on a patronage basis pursuant to the bylaws. The rate of dividend paid on Class D Preferred Stock for any fiscal year may not be less than the rate of dividend paid on common stock or participation certificates for such year. All dividends shall be paid on a per share basis. Dividends on common stock and participation certificates shall be noncumulative without preference between classes.

Dividends may not be declared if, after recording the liability, the Association would not meet its capital adequacy standards. No dividends were declared by the Association for any of the periods included in these Consolidated Financial Statements.

Transfer

Common stocks and participation certificates may be transferred to persons or entities eligible to purchase or hold such equities under the bylaws. Class D Preferred Stock may be transferred in the manner set forth in the resolution authorizing its issuance.

Impairment

Any net losses recorded by the Association shall first be applied against unallocated members' equity. To the extent that such losses would exceed unallocated members' equity, such losses would be applied consistent with the Association's bylaws and distributed pro rata to each share and/or unit outstanding in the class, in the following order:

1. Nonqualified allocated members equity beginning with the most recent allocation
2. Qualified allocated members equity beginning with the most recent allocation
3. Classes A and C Common Stock and Participation Certificates
4. Class D Preferred Stock

Liquidation

In the event of liquidation or dissolution of the Association, any assets of the Association remaining after payment or retirement of all liabilities should be distributed to the holders of the outstanding stock and participation certificates in the following order:

1. Holders of Class D Preferred Stock until an amount equal to the aggregate par value of shares of Class D Preferred Stock then outstanding has been distributed to the holders;
2. Holders of Class A Stock, Class C Stock, and Participation Certificates pro rata in proportion to the number of shares or units each such class of stock and participation certificates then outstanding until an amount equal to the aggregate par value (or face value) of such shares or units has been distributed to the holders;
3. Holders of Allocated Surplus to the extent evidenced by qualified written notices of allocation, pro rata, on the basis of the oldest allocations first, until an amount equal to the total account has been distributed to such holders;
4. Holders of Allocated Surplus to the extent evidenced by nonqualified written notice of allocation, pro rata, on the basis of the oldest allocations first, until an amount equal the total account has been distributed to such holders;
5. Any remaining assets of the Association after such distributions shall be distributed to Patrons, past and present, in proportion to which the aggregate patronage of each such Patron bears to the total patronage of all such parties insofar as practicable, unless as otherwise provided by law.

D. **Accumulated Other Comprehensive Income (AOCI):**

Changes in Accumulated Other Comprehensive Income by Component *(a)*

	For the Years Ended December 31,		
	2018	2017	2016
Employee Benefit Plans:			
Balance at beginning of period	$ (30)	$ (24)	$ (22)
Other comprehensive income before reclassifications	5	(7)	(3)
Amounts reclassified from AOCI	1	1	1
Net current period OCI	6	(6)	(2)
Balance at end of period	$ (24)	$ (30)	$ (24)

Reclassifications Out of Accumulated Other Comprehensive Income *(b)*

	Year to Date			
	2018	2017	2016	Income Statement Line Item
Defined Benefit Pension Plans:				
Periodic pension costs	$ (1)	$ (1)	$ (1)	See Note 9.
Amounts reclassified	$ (1)	$ (1)	$ (1)	

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

Note 8 — Fair Value Measurement

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

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

Estimating the fair value of the Association's equity investments in the Bank and Other Farm Credit Institutions is not practicable because the stock is not traded. The net investment is a requirement of borrowing from the Bank and is carried at cost.

The classifications within the fair value hierarchy (See Note 2) are as follows:

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

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

Level 2
The Association had no Level 2 assets and liabilities measured at fair value on a recurring basis.

Level 3
Because no active market exists for the Association's accruing loans, fair value is estimated by discounting the expected future cash flows using the Association's current interest rates at which similar loans currently would be made to borrowers with similar credit risk. The loan portfolio is segregated into pools of loans with homogeneous characteristics based upon repricing and credit risk. Expected future cash flows and interest rates reflecting appropriate credit risk are separately determined for each individual pool.

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

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

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

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

There were no Level 3 assets and liabilities measured at fair value on a recurring basis for the periods presented. The Association had no transfers of assets or liabilities into or out of Level 1 or Level 2 during the periods presented.

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

	December 31, 2018				
	Total Carrying Amount	Level 1	Level 2	Level 3	Total Fair Value
Recurring Measurements					
Assets:					
Assets held in trust funds	$ 1,964	$ 1,964	$ –	$ –	$ 1,964
Recurring Assets	$ 1,964	$ 1,964	$ –	$ –	$ 1,964
Liabilities:					
Recurring Liabilities	$ –	$ –	$ –	$ –	$ –
Nonrecurring Measurements					
Assets:					
Impaired loans	$ 8,693	$ –	$ –	$ 8,693	$ 8,693
Other property owned	1,477	–	–	1,625	1,625
Nonrecurring Assets	$ 10,170	$ –	$ –	$ 10,318	$ 10,318
Other Financial Instruments					
Assets:					
Cash	$ 4,700	$ 4,700	$ –	$ –	$ 4,700
Loans	1,827,120	–	–	1,793,940	1,793,940
Other Financial Assets	$ 1,831,820	$ 4,700	$ –	$ 1,793,940	$ 1,798,640
Liabilities:					
Notes payable to AgFirst Farm Credit Bank	$ 1,422,676	$ –	$ –	$ 1,397,861	$ 1,397,861
Other Financial Liabilities	$ 1,422,676	$ –	$ –	$ 1,397,861	$ 1,397,861

	December 31, 2017									
		Total Carrying Amount		Level 1		Level 2		Level 3		Total Fair Value
Recurring Measurements										
Assets:										
Assets held in trust funds	$	2,183	$	2,183	$	–	$	–	$	2,183
Recurring Assets	$	2,183	$	2,183	$	–	$	–	$	2,183
Liabilities:										
Recurring Liabilities	$	–	$	–	$	–	$	–	$	–
Nonrecurring Measurements										
Assets:										
Impaired loans	$	8,022	$	–	$	–	$	8,022	$	8,022
Other property owned		1,221		–		–		1,354		1,354
Nonrecurring Assets	$	9,243	$	–	$	–	$	9,376	$	9,376
Other Financial Instruments										
Assets:										
Cash	$	5,082	$	5,082	$	–	$	–	$	5,082
Loans		1,820,854		–		–		1,805,958		1,805,958
Other Financial Assets	$	1,825,936	$	5,082	$	–	$	1,805,958	$	1,811,040
Liabilities:										
Notes payable to AgFirst Farm Credit Bank	$	1,437,895	$	–	$	–	$	1,425,367	$	1,425,367
Other Financial Liabilities	$	1,437,895	$	–	$	–	$	1,425,367	$	1,425,367

	December 31, 2016									
		Total Carrying Amount		Level 1		Level 2		Level 3		Total Fair Value
Recurring Measurements										
Assets:										
Assets held in trust funds	$	1,611	$	1,611	$	–	$	–	$	1,611
Recurring Assets	$	1,611	$	1,611	$	–	$	–	$	1,611
Liabilities:										
Recurring Liabilities	$	–	$	–	$	–	$	–	$	–
Nonrecurring Measurements										
Assets:										
Impaired loans	$	9,175	$	–	$	–	$	9,175	$	9,175
Other property owned		2,467		–		–		2,735		2,735
Nonrecurring Assets	$	11,642	$	–	$	–	$	11,910	$	11,910
Other Financial Instruments										
Assets:										
Cash	$	5,730	$	5,730	$	–	$	–	$	5,730
Loans		1,776,655		–		–		1,759,497		1,759,497
Other Financial Assets	$	1,782,385	$	5,730	$	–	$	1,759,497	$	1,765,227
Liabilities:										
Notes payable to AgFirst Farm Credit Bank	$	1,423,922	$	–	$	–	$	1,404,483	$	1,404,483
Other Financial Liabilities	$	1,423,922	$	–	$	–	$	1,404,483	$	1,404,483

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.

Inputs to Valuation Techniques

Management determines the Association's valuation policies and procedures. The Bank performs the majority of the Association's valuations, and its valuation processes are calibrated annually by an independent consultant. The fair value measurements are analyzed on a quarterly basis. For other valuations, documentation is obtained for third party information, such as pricing, and periodically evaluated alongside internal information and pricing that is available.

Quoted market prices are generally not available for the 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
Impaired loans and other property owned	$ 10,318	Appraisal	Income and expense	*
			Comparable sales	*
			Replacement costs	*
			Comparability adjustments	*

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

Information about Other Financial Instrument Fair Value Measurements

	Valuation Technique(s)	Input
Cash	Carrying Value	Par/Principal and appropriate interest yield
Loans	Discounted cash flow	Prepayment forecasts
		Probability of default
		Loss severity
Notes payable to AgFirst Farm Credit Bank	Discounted cash flow	Prepayment rates
		Probability of default
		Loss severity

Note 9 — Employee Benefit Plans

The Association participates in three District sponsored benefit plans. These plans include a multi-employer defined benefit pension plan, the AgFirst Farm Credit Retirement Plan which is a final average pay plan (FAP Plan). In addition, the Association participates in a multi-employer defined benefit other postretirement benefits plan (OPEB Plan), the Farm Credit Benefits Alliance Retiree and Disabled Medical and Dental Plan, and a defined contribution 401(k) plan. The risks of participating in these multi-employer plans are different from single-employer plans in the following aspects:

1. Assets contributed to multi-employer plans by one employer may be used to provide benefits to employees of other participating employers.
2. If a participating employer stops contributing to the plan, the unfunded obligations of the plan may be borne by the remaining participating employers.
3. If the Association chooses to stop participating in some of its multi-employer plans, the Association may be required to contribute to eliminate the underfunded status of the plan.

The District's multiemployer plans are not subject to ERISA and no Form 5500 is required to be filed. As such, the following information is neither available for nor applicable to the plans:

1. The Employee Identification Number (EIN) and three-digit Pension Plan Number
2. The most recent Pension Protection Act (PPA) zone status. Among other factors, plans in the red zone are generally less than 65 percent funded, plans in the yellow zone are less than 80 percent funded, and plans in the green zone are at least 80 percent funded.
3. The "FIP/RP Status" indicating whether a financial improvement plan (FIP) or a rehabilitation plan (RP) is either pending or has been implemented.
4. The expiration date(s) of collective-bargaining agreement(s).

The FAP Plan covers employees hired prior to January 1, 2003 and includes other District employees that are not employees of the Association. It is accounted for as a multiemployer plan. The related net benefit plan obligations are not included in the Association's Balance Sheets but are included in the Combined Balance Sheets for the AgFirst District. FAP Plan expenses included in employee benefit costs on the Association's Statements of Income were $3,189 for 2018, $2,888 for 2017, and $3,512 for 2016. At December 31, 2018, 2017, and 2016, the total liability balance for the FAP Plan presented in the District Combined Balance Sheets is $94,491, $139,104, and $119,000, respectively. The FAP Plan is 89.56 percent, 86.41 percent, and 86.96 percent funded to the projected benefit obligation as of December 31, 2018, 2017, and 2016, respectively.

In addition to providing pension benefits, the Association provides certain medical and dental benefits for eligible retired employees through the OPEB Plan. Substantially all of the Association employees may become eligible for the benefits if they reach early retirement age while working for the Association. Early retirement age is defined as a minimum of age 55 and 10 years of service. Employees hired after December 31, 2002, and employees who separate from service between age 50 and age 55, are required to pay the full cost of their retiree health insurance coverage. Employees who retire subsequent to December 1, 2007 are no longer provided retiree life insurance benefits. The OPEB Plan includes other Farm Credit System employees that are not employees of the Association or District and is accounted for as a multiemployer plan. The related net benefit plan obligations are not included in the Association's Balance Sheets but are included in the Combined Statement of Condition for the Farm Credit System. The OPEB Plan is unfunded with expenses paid as incurred. Postretirement benefits other than pensions included in employee benefit costs on the Association's Statements of Income were $480 for 2018, $411 for 2017, and $873 for 2016. At December 31, 2018, the total AgFirst District liability balance for the OPEB

Plan presented in the Farm Credit System Combined Statement of Condition is $181,820.

During 2017, the method of recording expenses at participating District entities for the FAP and OPEB Plans was modified. Prior to 2017, expense was recorded based on allocations of actuarially-determined costs and any differences between recorded expense and actual contributions were recorded in Other Assets or Other Liabilities on the Consolidated Balance Sheets. For 2017 and future years, participating entities will record employee benefit costs based on the actual contributions to the Plans. This change caused the Association to modify its accounting estimates recorded in Other Assets and Other Liabilities since the assets and liabilities do not impact future contributions to the Plans. The change in estimate resulted in the reduction of Other Assets by $1,374 and the reduction of Other Liabilities by $9,564 on the Association's Balance Sheets, and a total reduction of noninterest expenses on the Association's Statements of Income of $8,190 during 2017.

The Association also participates in a defined contribution Farm Credit Benefits Alliance (FCBA) 401(k) Plan (401(k) Plan), which qualifies as a 401(k) plan as defined by the Internal Revenue Code. For employees hired on or prior to December 31, 2002, the Association contributes $0.50 for each $1.00 of the employee's first 6.00 percent of contribution (based on total compensation) up to the maximum employer contribution of 3.00 percent of total compensation. For employees hired on or after January 1, 2003, the Association contributes $1.00 for each $1.00 of the employee's first 6.00 percent of contribution up to the maximum employer contribution of 6.00 percent of total compensation. Employee deferrals are not to exceed the maximum deferral as determined and adjusted by the Internal Revenue Service. The 401(k) Plan costs are expensed as funded. Employer contributions to this plan included in salaries and employee benefit costs were $841, $772, and $692 for the years ended December 31, 2018, 2017, and 2016, respectively. Beginning in 2015, contributions include an additional 3.00 percent of eligible compensation for employees hired after December 31, 2002.

FASB guidance further requires the determination of the fair value of plan assets and recognition of actuarial gains and losses, prior service costs or credits, and transition assets or obligations as a component of AOCI. Under the guidance, these amounts are subsequently recognized as components of net periodic benefit costs over time. For 2018, 2017, and 2016, $6, $(6) and $(2), respectively, has been recognized as a net credit and net debits to AOCI to reflect these elements.

In addition to the multi-employer plans described above, the Association sponsors nonqualified supplemental retirement and 401(k) plans. The supplemental retirement plan is unfunded and had a projected benefit obligation of $110 and a net under-funded status of $110 at December 31, 2018. Assumptions used to determine the projected benefit obligation as of December 31, 2018 included a discount rate of 4.40 percent. The expenses of these nonqualified plans included in noninterest expenses were $6, $6, and $9 for 2018, 2017, and 2016, respectively.

Additional information for the above may be found in the Notes to the Annual Information Statement of the Farm Credit System.

Note 10 — Related Party Transactions

In the ordinary course of business, the Association enters into loan transactions with officers and directors of the Association, their immediate families and other organizations with which such persons may be associated. Such loans are subject to special approval requirements contained in the FCA regulations and are made on the same terms, including interest rates, amortization schedule, and collateral, as those prevailing at the time for comparable transactions with unaffiliated borrowers.

Total loans to such persons at December 31, 2018 amounted to $12,130. During 2018, $3,386 of new loans were made and repayments totaled $3,416. In the opinion of management, none of these loans outstanding at December 31, 2018 involved more than a normal risk of collectability.

Note 11 — Commitments and Contingencies

From time to time, legal actions are pending against the Association in which claims for money damages are asserted. On at least a quarterly basis, the Association assesses its liabilities and contingencies in connection with outstanding legal proceedings utilizing the latest information available. While the outcome of legal proceedings is inherently uncertain, on the basis of information presently available, management, after consultation with legal counsel, is of the opinion that the ultimate liability, if any, from these actions, would not be material in relation to the financial position of the Association. Because it is not probable that the Association will incur a loss or the loss is not estimable, no liability has been recorded for any claims that may be pending.

In the normal course of business, the Association may participate in financial instruments with off-balance-sheet risk to satisfy the financing needs of its borrowers. These financial instruments may include commitments to extend credit or letters of credit.

The instruments involve, to varying degrees, elements of credit risk in excess of the amount recognized in the financial statements. Commitments to extend credit are agreements to lend to a borrower as long as there is not a violation of any condition established in the contract. Commercial letters of credit are agreements to pay a beneficiary under conditions specified in the letter of credit. Commitments and letters of credit generally have fixed expiration dates or other termination clauses and may require payment of a fee.

Since many of these commitments are expected to expire without being drawn upon, the total commitments do not necessarily represent future cash requirements. However, these credit-related financial instruments have off-balance-sheet credit risk because their amounts are not reflected on the Consolidated Balance Sheets until funded or drawn upon. The credit risk associated with issuing commitments and letters of credit is substantially the same as that involved in extending loans to borrowers and management applies the same credit policies to these commitments. Upon fully funding a commitment, the credit risk amounts are equal to the contract amounts, assuming that borrowers fail completely to meet their obligations and the collateral or other security is of no value. The amount of collateral obtained, if deemed necessary upon

extension of credit, is based on management's credit evaluation of the borrower. At December 31, 2018, $197,732 of commitments to extend credit and no commercial letters of credit were outstanding. At December 31, 2018, there was no reserve for unfunded commitments included in Other Liabilities in the Consolidated Balance Sheets.

The Association also participates in standby letters of credit to satisfy the financing needs of its borrowers. These letters of credit are irrevocable agreements to guarantee payments of specified financial obligations. At December 31, 2018, standby letters of credit outstanding totaled $375 with expiration dates ranging from January 1, 2019 to September 30, 2022. The maximum potential amount of future payments that may be required under these guarantees was $375.

Note 12 — Income Taxes

The provision (benefit) for income taxes follows:

	Year Ended December 31,		
	2018	2017	2016
Current:			
Federal	$ 34	$ 40	$ 27
State	6	9	11
	40	49	38
Deferred:			
Federal	–	–	–
State	–	–	–
	–	–	–
Total provision (benefit) for income taxes	$ 40	$ 49	$ 38

The provision (benefit) for income tax differs from the amount of income tax determined by applying the applicable U.S. statutory federal income tax rate to pretax income as follows:

	December 31,		
	2018	2017	2016
Federal tax at statutory rate	$ 11,059	$ 19,947	$ 15,140
State tax, net	7	6	7
Patronage distributions	(7,350)	(9,562)	(5,250)
Tax-exempt FLCA earnings	(2,787)	(8,750)	(11,257)
Change in valuation allowance	(1,098)	(3,884)	1,570
Other	209	171	(172)
Deferred tax rate change	–	2,121	–
Provision (benefit) for income taxes	$ 40	$ 49	$ 38

In late December 2017, federal tax legislation was enacted which, among other things, lowered the federal corporate tax rate from 35% to 21% beginning on January 1, 2018. The change to the lower corporate tax rate led to an insignificant remeasurement of the deferred tax liabilities and deferred tax assets in 2017, the period of enactment. Deferred tax assets and liabilities are comprised of the following at:

	December 31,		
	2018	2017	2016
Deferred income tax assets:			
Allowance for loan losses	$ 1,941	$ 2,661	$ 2,955
Annual leave	337	334	542
Nonaccrual loan interest	462	717	870
Pensions and other postretirement benefits	485	539	4,314
Deferred incentive	262	257	399
Gross deferred tax assets	3,487	4,508	9,080
Less: valuation allowance	(3,052)	(4,149)	(8,033)
Gross deferred tax assets, net of valuation allowance	435	359	1,047
Deferred income tax liabilities:			
Loan origination fees	(370)	(297)	(436)
Pensions and other postretirement benefits	–	–	(535)
Depreciation	(65)	(62)	(76)
Gross deferred tax liability	(435)	(359)	(1,047)
Net deferred tax asset (liability)	$ –	$ –	$ –

At December 31, 2018, deferred income taxes have not been provided by the Association on approximately $1.6 million of patronage refunds received from the Bank prior to January 1, 1993. Such refunds, distributed in the form of stock, are subject to tax only upon conversion to cash. The tax liability related to future conversions is not expected to be material.

The Association recorded a valuation allowance of $3,052, $4,149, and $8,033 as of December 31, 2018, 2017 and 2016, respectively. The Association will continue to evaluate the realizability of these deferred tax assets and adjust the valuation allowance accordingly.

There were no uncertain tax positions identified related to the current year and the Association has no unrecognized tax benefits at December 31, 2018 for which liabilities have been established. The Association recognizes interest and penalties, if any, related to unrecognized tax benefits as a component of income tax expense. The tax years that remain open for federal and major state income tax jurisdictions are 2015 and forward.

Note 13 — Additional Financial Information

Quarterly Financial Information (Unaudited)

	2018				
	First	Second	Third	Fourth	Total
Net interest income	$ 13,946	$ 13,902	$ 13,979	$ 15,243	$ 57,070
Provision for (reversal of allowance for) loan losses	500	500	1,000	500	2,500
Noninterest income (expense), net	(2,674)	(4,119)	(3,333)	8,177	(1,949)
Net income	$ 10,772	$ 9,283	$ 9,646	$ 22,920	$ 52,621

	2017				
	First	Second	Third	Fourth	Total
Net interest income	$ 13,328	$ 13,633	$ 13,611	$ 13,625	$ 54,197
Provision for (reversal of allowance for) loan losses	500	250	–	2,500	3,250
Noninterest income (expense), net	(4,586)	(4,275)	(3,512)	18,370	5,997
Net income	$ 8,242	$ 9,108	$ 10,099	$ 29,495	$ 56,944

	2016				
	First	**Second**	**Third**	**Fourth**	**Total**
Net interest income	$ 12,586	$ 12,655	$ 12,882	$ 13,037	$ 51,160
Provision for (reversal of allowance for) loan losses	500	1,000	250	1,000	2,750
Noninterest income (expense), net	(3,483)	(3,617)	(3,201)	5,111	(5,190)
Net income	$ 8,603	$ 8,038	$ 9,431	$ 17,148	$ 43,220

Note 14 — Subsequent Events

The Association evaluated subsequent events and determined there were none requiring disclosure through March 13, 2019, which was the date the financial statements were issued.

Subsequent to December 31, 2018, the Board of Directors at the February 2019 board meeting approved a cash patronage refund to customers in the amount of $40,000. This was an increase of $10,000 from the estimated cash patronage refund of $30,000 accrued at December 31, 2018.