



PART OF THE FARM CREDIT SYSTEM

Quarterly Report To Stockholders

Quarter Ended September 30, 2016

REPORT OF MANAGEMENT

The consolidated financial statements of Capital Farm Credit, ACA (the Association) are prepared by management, who is responsible for the statements' integrity and objectivity, including amounts that must necessarily be based on judgments and estimates. The consolidated financial statements have been prepared in conformity with accounting principles generally accepted in the United States of America appropriate in the circumstances. Other financial information included in the quarterly report is consistent with that in the consolidated financial statements and there are no significant changes in the Association's internal controls or in other factors that could significantly affect such controls during the year.

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

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

The undersigned certify that this quarterly report has been reviewed and prepared in accordance with all applicable statutory or regulatory requirements, and that the information contained herein is true, accurate and complete to the best of his knowledge and belief.



Ben R. Novosad,
Chief Executive Officer



Phillip Munden,
Chairman, Board of Directors



Don VandeVanter,
Chief Financial Officer

November 4, 2016

**MANAGEMENT'S DISCUSSION AND ANALYSIS
OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS
(Dollars in thousands)**

The following commentary explains management's assessment of the principal aspects of the consolidated financial condition and results of operations of Capital Farm Credit, ACA including its wholly-owned subsidiaries, Capital Farm Credit, PCA and Capital Farm Credit, FLCA, (collectively referred to as the Association) for the quarter ended September 30, 2016. These comments should be read in conjunction with the accompanying consolidated financial statements and the December 31, 2015 Annual Report of the Association. Results for interim periods are not necessarily indicative of results to be expected for future periods.

Rainfall during the third quarter was detrimental for dryland crops in some regions, but very beneficial for range and pasture conditions. Cattle prices are significantly lower than in the last few years. This, along with lower crop prices may continue to reduce farmer revenues in 2016, creating market strain and possibly resulting in operating losses for some producers. Oil prices have stabilized some and show a slightly positive improvement when compared to the last 18 months. The housing market has experienced mixed growth in Texas' major metropolitan areas. The Texas economic outlook reflects continued moderate growth in the coming months.

Patronage Refunds by Association

In September 2016, the board of directors approved a resolution to retire \$36,783 in nonqualified allocated equities which are to be paid to the recipients in November 2016. The retirement is a distribution of 50 percent of the earnings allocated in 2010.

The Association distributed its patronage refund for 2015 in March 2016. \$56,746 of this distribution was paid in cash and \$80,881 was distributed in the form of nonqualified allocated equity. These nonqualified distributions are not taxable to the recipient until the equities are retired. It is the board's intention with these allocations to assign ownership of the earnings of the Association, allowing the stockholders to benefit more fully from the earnings of the Association and to create a method to make future equity distributions in the form of cash. While there is not a planned retirement of the allocated equity, the board of directors will make an annual evaluation of the Association's capital position and determine if some cash retirements of these equities can be made. In November 2015, the Association retired \$39,867 in nonqualified allocated equity, which represented all of the allocated equity issued for 2009. In March 2015, the Association made its patronage distribution for 2014, with cash distribution of \$71,980 and nonqualified allocations of \$70,070.

Loan Portfolio

Total loan volume was \$6,845,854 at September 30, 2016. This compares with loan volume owned by the Association at December 31, 2015 of \$6,483,896. This represents an increase of \$361,958, or approximately 5.6 percent. Most of this increase was realized in the farm-related business and real estate mortgage segments. The Association's loan growth is a result of a stable and growing economy and effective marketing.

The Association's high-risk assets have increased by 42.9 percent in 2016. Most of this increase has been in nonaccrual loans. The following table summarizes the Association's components and trends of high-risk assets:

	<u>September 30, 2016</u>	<u>%</u>	<u>December 31, 2015</u>	<u>%</u>
Nonaccrual loans	\$ 92,420	85.5	\$ 59,966	79.4
Loans 90 days past due and still accruing interest	931	0.9	933	1.2
Formally restructured loans	12,711	11.8	13,522	17.9
Other property owned, net	1,902	1.8	1,109	1.5
Total	<u>\$ 107,964</u>	<u>100.0</u>	<u>\$ 75,530</u>	<u>100.0</u>

Nonaccrual loans increased \$32,454 during the first nine months of 2016. This increase was recognized primarily in the production and real estate mortgage sectors. This increase was a result of operating losses experienced by

producers, driven primarily by drops in commodity prices. The increase in nonaccrual loans for the real estate mortgage sector was due to rules of attribution. Due to the production loans being transferred to nonaccrual, the real estate loans due from the same customers were also required to be transferred to nonaccrual.

Loans that are 90 or more days past due and still accruing interest decreased \$2 in the first nine months of 2016. Loans in this category are to customers that have a documented plan that details how and when the amount owed will be paid.

Formally restructured loans decreased \$811 during the first nine months of 2016 as a result of loan pay offs. The Association is cooperating with distressed borrowers to work through temporary repayment problems, where possible. These restructurings may include a modification of loan terms to accommodate the financial difficulties of the customer.

Other property owned increased \$793 during the first nine months of 2016. The Association is actively working with real estate professionals to ensure properties are accurately valued on the Association's books and that proactive marketing activities are in place.

Management also continues to routinely evaluate and monitor counterparty and collateral risks in an effort to avoid concentrations that could result in excess exposure to a single counterparty or type of collateral. The loan portfolio management practices in place have been designed to ensure loans and industries with actual or potential problems are promptly identified, monitored and addressed in a manner that allows the lending staff to work with problem customers and industries through periods of adversity.

Results of Operations

The Association's net income for the nine months ended September 30, 2016 was \$108,818 as compared to \$98,420 for the nine months ended September 30, 2015, an increase of \$10,398, or 10.6 percent.

The increase in net income was affected by an increase in net interest income and in noninterest income, offset somewhat by an increase in the provision for loan losses. Net interest income increased by \$11,745 during the first nine months of 2016 compared to the same time period for 2015. An increase in average loan volume and higher average capital was the catalyst for the improvement in net interest income. The effects of changes in average volume and interest rates on net interest income in the nine months ended September 30, 2016, as compared with the corresponding period of the prior year, are presented in the following tables:

	For the nine months ended September 30, 2016		For the nine months ended September 30, 2015	
	Average Balance	Interest	Average Balance	Interest
Accrual loans and investments	\$ 6,618,593	\$ 246,426	\$ 5,950,957	\$ 220,846
Interest-bearing liabilities	5,688,033	86,197	5,069,967	72,362
Impact of capital	\$ 930,560		\$ 880,990	
Net interest income		\$ 160,229		\$ 148,484

	Average Yield	Average Yield
Yield on loans	4.97%	4.96%
Cost of interest-bearing Liabilities	2.02%	1.91%
Net interest margin	2.95%	3.05%

	2016 vs. 2015		
	Increase (decrease) due to		
	Volume	Rate	Total
Interest income	\$ 24,799	\$ 781	\$ 25,580
Interest expense	8,830	5,005	13,835
Net interest income	\$ 15,969	\$ (4,224)	\$ 11,745

Provision for loan losses was \$7,657 for the period ended September 30, 2016, as compared to \$5,268 for the same period in 2015. The Association added to its allowance for losses as loan volume continues to increase and credit quality continues to decline slightly during the period. The Association's noninterest income increased from \$23,281 in the first nine months of 2015 to \$24,966 in the first nine months of 2016. The Association has received a patronage refund over the last several years from the Farm Credit Bank of Texas (Bank). This refund is paid annually to the Association in December by a direct reduction in its Note Payable to Bank. In accordance with the Bank's 2016 Capital Plan declaration the Association is accruing 0.40 percent of its average Note Payable during 2016. For the first nine months, the patronage income accrued is \$2,110 more in 2016 than for the same period in 2015 because of the higher Note Payable balance.

Noninterest expenses increased \$646, or 0.9 percent in the first nine months of 2016 as compared to the same time period in 2015. This increase is primarily attributable to an increase of \$2,019 in the Farm Credit Insurance Corporation (FCSIC) expense, and an increase of \$731 in salaries and benefits expense, offset by a decrease of \$1,086 in purchased services and a decrease of \$1,886 in other expenses. The increase in the FCSIC was due to increased premiums paid on accrual loans from 13 basis points in September 2015 to 16 basis points for the first half of 2016 and to 18 basis points for the second half of 2016. The increase in salary and benefits expense is due to an increase of 16 full-time employees as compared to the same time period in 2015, as the Association hires staff in anticipation of pending retirements, new business initiatives to support future business growth and additional regulatory compliance. Other expenses and purchased services decreased as the Association experienced lower legal expenses in the current year versus those incurred in the prior year.

Liquidity and Funding Sources

The interest rate risk inherent in the Association's loan portfolio is substantially mitigated through the funding relationship with the Bank. The Bank manages interest rate risk through its direct loan pricing and asset/liability management process.

The primary source of liquidity and funding for the Association is its direct loan from the Bank. The Association had an outstanding balance of \$5,815,138 at September 30, 2016, as compared to \$5,474,595 at December 31, 2015. This increase in note payable to the Bank since December 2015 is the result of the increase in the Association's loan portfolio. The direct loan carried a weighted average interest rate of 2.02 percent for the nine months ended September 30, 2016, compared to 1.92 percent for the year ended December 31, 2015. The indebtedness is collateralized by a pledge of substantially all of the Association's assets to the Bank and is governed by a financing agreement.

The Association is obligated to borrow only from the Bank unless the Bank approves borrowing from other funding sources. The Bank and FCA regulations have 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 September 30, 2016 the Association's note payable was within the specified limitations. The maximum amount the Association could borrow from the Bank as of September 30, 2016, was \$6,773,858, as defined by the general financing agreement. This borrowing limit changes as the borrowing base increases or decreases. In general the Bank funds 100 percent of all eligible acceptable and special mention loans and 75 percent of all eligible substandard loans.

The liquidity policy of the Association is to manage cash balances to maximize debt reduction, and to increase accrual loan volume. This policy will continue to be pursued during 2016. As borrower payments are received they are applied to the Association's note payable with the Bank.

The Association will continue to fund its operations through direct borrowings from the Bank, retained earnings, member stock and funds held in trust. It is management's opinion that funds available to the Association are sufficient to fund its operations for the next twelve months.

Capital Resources and Regulatory Matters

The Association's capital position remains strong, with total capital of \$1,138,668 at September 30, 2016. This represents an increase of \$72,289 from the December 31, 2015 total capital level of \$1,066,379. This increase in capital is a direct result of the Association's net income for the period, offset by a reduction of non-qualified retained earnings as the board of directors approved a resolution to retire \$36,783 in non-qualified allocated equities to be paid to stockholders in November 2016. Under current regulations governing minimum permanent capital adequacy and other capitalization issues, the Association is required to maintain a minimum adjusted permanent capital of 7.0 percent of risk-adjusted assets as defined by the FCA. The Association's permanent capital ratio at September 30, 2016 was 14.82 percent. The Association's core surplus ratio and total surplus ratio at September 30, 2016 were 14.56 percent and 14.56 percent, respectively, which is in compliance with the FCA's minimum ratio requirements of 3.5 percent and 7.0 percent, respectively.

On March 10, 2016, the Farm Credit Administration approved a final rule to modify the regulatory capital requirements for System banks and associations. The final rule will be effective January 1, 2017. The stated objectives of the final rule are as follows:

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

The final rule replaces existing core surplus and total surplus requirements with common equity tier 1, tier 1, and total capital (tier 1 plus tier 2) risk-based capital ratio requirements. It also adds a tier 1 leverage ratio, which requires at least 1.5 percent of risk-adjusted assets to be capitalized with unallocated retained earnings. In addition, the final rule establishes a capital conservation buffer and a leverage buffer that will need to be maintained in order to make any capital distributions, such as patronage refunds.

The effects of the final rule have been evaluated by the Association. In general, the capital requirements will cause the Association to hold greater levels of capital relative to its assets for longer periods of time. The Association anticipates being in full compliance with the new capital ratio requirements when the new rule becomes effective.

Relationship with the Farm Credit Bank of Texas

The Association's statutory obligation to borrow only from the Bank is described in the section "Liquidity and Funding Sources" of the Management's Discussion and Analysis, included in this quarterly report.

The Bank's role in mitigating the Association's exposure to interest rate risk is described in the section "Liquidity and Funding Sources" of Management's Discussion and Analysis, included in this quarterly report.

The Bank provides computer systems to support the critical operations of the Association. The Association also has operating systems and facility-based systems that are not supported by the Bank. The Bank also provides other services the Association can utilize.

The Association's financial condition may be impacted by factors that affect the Bank as discussed in Note 1 to the consolidated financial statements, "Organization and Significant Accounting Policies," included in this quarterly report. The financial condition and results of operations of the Bank may materially affect the stockholders' investment in the Association.

The Tenth Farm Credit District's (District) annual and quarterly stockholder reports are available free of charge, upon request. These reports can be obtained by writing to Farm Credit Bank of Texas, The Ag Agency, P. O. Box 202590, Austin, Texas 78720-2590 or calling (512) 483-9204. Copies of the District's annual and quarterly stockholder reports can also be requested by e-mailing Bank@farmcreditBank.com. The District's annual and quarterly stockholder reports are also available on its Website at www.farmcreditBank.com.

The Association's annual and quarterly stockholder reports are also available free of charge, upon request. These reports can be obtained by writing to Capital Farm Credit, ACA, P.O. Box 488, Hondo, Texas 78861 or calling (830) 426-4589. Copies of the Association's quarterly and annual stockholder reports are also available on its Website at www.capitalfarmcredit.com or can be requested by e-mailing isela.morales@capitalfarmcredit.com.

CAPITAL FARM CREDIT, ACA
CONSOLIDATED BALANCE SHEETS
(Dollars in thousands)

	September 30, 2016	December 31, 2015
	(Unaudited)	(Audited)
<u>ASSETS</u>		
Loans	\$ 6,845,854	\$ 6,483,896
Less: Allowance for losses	<u>(30,766)</u>	<u>(23,328)</u>
Net Loans	6,815,088	6,460,568
Cash	38	52
Accrued interest receivable - loans	67,952	52,669
Accrued interest receivable - investments	118	92
Investment - held-to-maturity	7,283	8,098
Investment in and receivable from the Bank:		
Capital stock	102,014	102,014
Receivable	22,781	12,716
Investments in other Farm Credit Institutions	7,407	6,414
Other property owned, net	1,902	1,109
Premises and equipment, net	15,452	16,603
Other assets	<u>18,497</u>	<u>16,525</u>
Total assets	<u>\$ 7,058,532</u>	<u>\$ 6,676,860</u>
<u>LIABILITIES</u>		
Note payable to the Bank	\$ 5,815,138	\$ 5,474,595
Advanced conditional payments	5,546	6,214
Accrued interest payable	9,717	9,018
Drafts outstanding	771	4,397
Patronage distributions payable	36,789	56,746
Unfunded post retirement medical obligation	22,454	21,870
Other liabilities	<u>29,449</u>	<u>37,641</u>
Total liabilities	<u>5,919,864</u>	<u>5,610,481</u>
<u>MEMBERS' EQUITY</u>		
Capital stock and participation certificates	24,956	24,419
Non-qualified allocated retained earnings	450,702	487,489
Unallocated retained earnings	663,874	555,052
Accumulated other comprehensive loss	<u>(864)</u>	<u>(581)</u>
Total members' equity	<u>1,138,668</u>	<u>1,066,379</u>
Total liabilities and members' equity	<u>\$ 7,058,532</u>	<u>\$ 6,676,860</u>

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

CAPITAL FARM CREDIT, ACA
CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME
(Dollars in thousands)
(UNAUDITED)

	For the three months ended September 30, 2016	For the three months ended September 30, 2015	For the nine months ended September 30, 2016	For the nine months ended September 30, 2015
<u>INTEREST INCOME</u>				
Loans	\$ 82,733	\$ 75,701	\$ 246,138	\$ 220,483
Investments	92	108	288	363
Total interest income	<u>82,825</u>	<u>75,809</u>	<u>246,426</u>	<u>220,846</u>
<u>INTEREST EXPENSE</u>				
Note payable to the Bank and others	29,697	25,334	86,197	72,362
Net interest income	<u>53,128</u>	<u>50,475</u>	<u>160,229</u>	<u>148,484</u>
<u>PROVISION FOR LOAN LOSSES</u>				
Provision for loan losses	3,368	1,468	7,657	5,268
Net interest income after provision for losses	<u>49,760</u>	<u>49,007</u>	<u>152,572</u>	<u>143,216</u>
<u>NONINTEREST INCOME</u>				
Patronage income from the FCB	6,322	5,672	18,616	16,506
Loan fees	1,084	1,071	2,876	2,802
Other income	636	1,326	3,474	3,973
Total noninterest income	<u>8,042</u>	<u>8,069</u>	<u>24,966</u>	<u>23,281</u>
<u>NONINTEREST EXPENSES</u>				
Salaries and employee benefits	15,081	14,855	43,606	42,875
Farm Credit System insurance premium	2,450	1,587	6,635	4,616
Occupancy and equipment	994	1,025	3,248	3,245
Advertising	993	962	2,980	2,771
Travel	789	734	2,176	1,959
Purchased services and allocations	493	461	1,703	2,789
Public and member relations	478	534	2,094	2,114
FCA supervisory and exam expense	368	259	1,105	932
Communications	266	302	873	899
Directors' expense	220	209	632	662
Loss (Gain) on other property owned, net	74	(188)	64	(278)
Other expenses	1,023	1,521	3,599	5,485
Total noninterest expenses	<u>23,229</u>	<u>22,261</u>	<u>68,715</u>	<u>68,069</u>
Income before federal income tax	34,573	34,815	108,823	98,428
Provision for (Benefit from) federal income tax	2	(15)	5	8
NET INCOME	<u>\$ 34,571</u>	<u>\$ 34,830</u>	<u>\$ 108,818</u>	<u>\$ 98,420</u>
Other comprehensive loss:				
Change in postretirement benefit plans	(94)	(28)	(283)	(84)
Income tax expense related items of other comprehensive income	-	-	-	-
Other comprehensive loss, net of tax	<u>(94)</u>	<u>(28)</u>	<u>(283)</u>	<u>(84)</u>
COMPREHENSIVE INCOME	<u>\$ 34,477</u>	<u>\$ 34,802</u>	<u>\$ 108,535</u>	<u>\$ 98,336</u>

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

CAPITAL FARM CREDIT, ACA
CONSOLIDATED STATEMENT OF CHANGES IN MEMBERS' EQUITY
(Dollars in thousands)
(UNAUDITED)

	Capital Stock/ Participation Certificates	Retained Earnings		Accumulated Other Comprehensive Income (Loss)	Total Members' Equity
		Non-qualified Allocated	Unallocated		
Balance at December 31, 2014	\$ 23,417	\$ 446,477	\$ 553,366	\$ (3,028)	\$ 1,020,232
Net income	-	-	98,420	-	98,420
Other comprehensive loss	-	-	-	(84)	(84)
Capital stock/participation certificates issued	3,096	-	-	-	3,096
Capital stock/participation certificates/ allocated equities retired	(2,307)	(39,867)	-	-	(42,174)
Other adjustments	-	(3)	16	-	13
Balance at September 30, 2015	24,206	406,607	651,802	(3,112)	1,079,503
Net income	-	-	40,882	-	40,882
Other comprehensive gain	-	-	-	2,531	2,531
Capital stock/participation certificates issued	972	-	-	-	972
Capital stock/participation certificates/ allocated equities retired	(759)	-	-	-	(759)
Patronage distributions declared:	-	-	-	-	-
Cash	-	-	(56,746)	-	(56,746)
Nonqualified allocations	-	80,885	(80,885)	-	-
Other adjustments	-	(3)	(1)	-	(4)
Balance at December 31, 2015	24,419	487,489	555,052	(581)	1,066,379
Net income	-	-	108,818	-	108,818
Other comprehensive loss	-	-	-	(283)	(283)
Capital stock/participation certificates issued	3,001	-	-	-	3,001
Capital stock/participation certificates/ allocated equities retired	(2,464)	(36,783)	-	-	(39,247)
Other adjustments	-	(4)	4	-	-
Balance at September 30, 2016	\$ 24,956	\$ 450,702	\$ 663,874	\$ (864)	\$ 1,138,668

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

CAPITAL FARM CREDIT, ACA
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
(Dollars in thousands)
(UNAUDITED)

NOTE 1 — ORGANIZATION AND SIGNIFICANT ACCOUNTING POLICIES:

Capital Farm Credit, ACA including its wholly owned subsidiaries, Capital Farm Credit, PCA and Capital Farm Credit, FLCA, (collectively called the “Association”), is a member-owned cooperative which provides credit and credit-related services to, or for the benefit of, eligible borrowers/stockholders for qualified agricultural purposes in 192 counties in the state of Texas.

The Association is a lending institution of the Farm Credit System (System) which was established by acts of Congress and is subject to the provisions of the Farm Credit Act of 1971, as amended (Act.)

A description of the organization and operations of the Association, the significant accounting policies followed, and the financial condition and results of operations as of December 31, 2015 are contained in the 2015 Annual Report to Stockholders.

The accompanying unaudited financial statements have been prepared in accordance with accounting principles generally accepted in the U.S. (GAAP) for interim financial information. Accordingly, they do not include all of the disclosures required by GAAP for annual financial statements and should be read in conjunction with the audited financial statements as of and for the year ended December 31, 2015 as contained in the 2015 Annual Report to Stockholders.

The Bank and its related Associations are collectively referred to as the “District.” The Association’s financial condition may be affected by factors that affect the Bank. The financial condition and results of operations of the Bank may materially affect stockholders’ investment in the Association. Upon request, stockholders of the Association will be provided the Tenth Farm Credit District’s Annual Report to Stockholders, which includes the combined financial statements of the Bank and all of the District Associations. The District’s annual report discusses the material aspects of the financial condition, changes in financial condition, and results of operations for the Bank and the District. In addition, the District’s annual report identifies favorable and unfavorable trends, significant events, uncertainties and the impact of activities of the Farm Credit System Insurance Corporation.

In the opinion of management, the unaudited financial information is complete and reflects, all adjustments, consisting of normal recurring adjustments, necessary for a fair statement of results for the interim periods. The preparation of financial statements in accordance with GAAP requires management to make estimates and assumptions that affect the amounts reported in the financial statements and accompanying notes. Actual results could differ from those estimates. The results of operations for interim periods are not necessarily indicative of the results to be expected for the full year ending December 31, 2016. Descriptions of the significant accounting policies are included in the 2015 Annual Report to Stockholders. In the opinion of management, these policies and the presentation of the interim financial condition and results of operations conform with GAAP and prevailing practices within the Banking industry.

In August 2016, the Financial Accounting Standards Board (FASB) issued guidance entitled “Classification of Certain Cash Receipts and Cash Payments.” The guidance addresses specific cash flow issues with the objective of reducing the diversity in the classification of these cash flows. Included in the cash flow issues are debt prepayment or debt extinguishment costs and settlement of zero-coupon debt instruments or other debt instruments with coupon interest rates that are insignificant in relation to the effective interest rate of the borrowing. This guidance becomes effective for interim and annual periods beginning after December 15, 2017. The adoption of this guidance is not expected to impact the Association’s financial condition or its results of operations but could change the classification of certain items in the statement of cash flows.

In June 2016, the FASB issued guidance entitled “Measurement of Credit Losses on Financial Instruments.” The guidance replaces the current incurred loss impairment methodology with a methodology that reflects expected credit losses and requires consideration of a broader range of reasonable and supportable information to estimate credit losses. Credit losses relating to available-for-sale securities would also be recorded through an allowance for credit

losses. For public business entities that are not U.S. Securities and Exchange Commission filers, this guidance becomes effective for interim and annual periods beginning after December 15, 2020, with early application permitted. The Association is currently evaluating the impact of adoption on its financial condition and results of operations.

In February 2016, the FASB issued guidance entitled “Leases.” The guidance requires the recognition by lessees of lease assets and lease liabilities on the balance sheet for the rights and obligations created by those leases. Leases with lease terms of more than 12 months are impacted by this guidance. This guidance becomes effective for interim and annual periods beginning after December 15, 2018, with early application permitted. The Association is currently evaluating the impact of adoption on its financial condition and results of operations.

In January 2016, the FASB issued guidance entitled “Recognition and Measurement of Financial Assets and Liabilities.” The guidance affects, among other things, the presentation and disclosure requirements for financial instruments. For public entities, the guidance eliminates the requirement to disclose the methods and significant assumptions used to estimate the fair value of financial instruments carried at amortized cost. This guidance becomes effective for interim and annual periods beginning after December 15, 2017. The adoption of this guidance is not expected to impact the Association’s financial condition or its results of operations.

In August 2014, the FASB issued guidance entitled “Presentation of Financial Statements — Going Concern.” The guidance governs management’s responsibility to evaluate whether there is substantial doubt about an entity’s ability to continue as a going concern and to provide related footnote disclosures. This guidance requires management to perform interim and annual assessments of an entity’s ability to continue as a going concern within one year after the date the financial statements are issued or within one year after the financial statements are available to be issued, when applicable. Substantial doubt exists if it is probable that the entity will be unable to meet its obligations for the assessed period. This guidance becomes effective for interim and annual periods ending after December 15, 2016, and early application is permitted. Management will be required to make its initial assessment as of December 31, 2016, and expects the Association to continue as a going concern.

In May 2014, the FASB issued guidance entitled, “Revenue from Contracts with Customers.” The guidance governs revenue recognition from contracts with customers and requires an entity to recognize revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. Financial instruments and other contractual rights within the scope of other guidance issued by the FASB are excluded from the scope of this new revenue recognition guidance. In this regard, a majority of the Association’s contracts would be excluded from the scope of this new guidance. In August 2015, the FASB issued an update that defers this guidance by one year, which results in the new revenue standard becoming effective for interim and annual reporting periods beginning after December 15, 2017. The Association is in the process of reviewing contracts to determine the effect, if any, on their financial condition or results of operations. Management anticipates the adoption of this guidance to have very little impact to the financial condition or results of operations for the Association.

Certain amounts in the prior period’s financial statements have been reclassified to conform to the current period’s financial statement presentation.

NOTE 2 — INVESTMENTS:

Investments Held-to-Maturity

The Association's held-to-maturity investment consists of Farmer Mac guaranteed agricultural mortgage-backed securities (AMBS). A summary of the amortized cost and fair value of investment securities held-to-maturity is as follows:

	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value	Weighted Average Yield	Weighted Average Life (Years)
September 30, 2016						
Agricultural mortgage-backed securities	\$ 7,283	\$ 120	\$ -	\$ 7,403	4.91%	3.21
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value	Weighted Average Yield	Weighted Average Life (Years)
December 31, 2015						
Agricultural mortgage-backed securities	\$ 8,098	\$ 43	\$ -	\$ 8,141	4.93%	2.82

The Farmer Mac AMBS were received in exchange for mortgage loans which were previously covered under the long-term standby commitment to purchase agreement with Farmer Mac. No gain or loss was recognized in the financial statements upon completion of the exchange transactions. The Association continues to service the loans included in the transaction.

NOTE 3 — LOANS AND ALLOWANCE FOR LOAN LOSSES:

A summary of loans follows:

Industry	September 30 2016	%	December 31 2015	%
Real estate mortgage	\$ 5,109,214	74.7	\$ 4,853,855	74.9
Production and intermediate term	836,527	12.2	827,061	12.8
Farm-related business	609,474	8.9	543,010	8.4
Rural residential real estate	153,166	2.2	144,470	2.2
Energy	70,716	1.0	46,489	0.7
Communication	51,418	0.8	53,063	0.8
Mission-related investments	7,910	0.1	8,127	0.1
Lease receivables	6,353	0.1	6,028	0.1
Water and waste disposal	1,076	0.0	1,793	0.0
Total	\$ 6,845,854	100.0	\$ 6,483,896	100.0

At September 30, 2016, the Association held five transactions, which are reported as loans on the consolidated balance sheet totaling \$6,478 and with \$44 in remaining commitments extended under the Rural America Bond Program approved by the FCA. The program is designed to meet the growing and changing needs of agricultural enterprises, agribusinesses and rural communities by providing investment in rural areas.

The Association purchases or sells participation interests with other parties in order to diversify risk, manage loan volume and comply with Farm Credit Administration regulations. The following table presents information regarding the balances of participations purchased and sold as of September 30, 2016:

	Other Farm Credit Institutions		Non-Farm Credit Institutions		Total	
	Participations	Participations	Participations	Participations	Participations	Participations
	<u>Purchased</u>	<u>Sold</u>	<u>Purchased</u>	<u>Sold</u>	<u>Purchased</u>	<u>Sold</u>
Real estate mortgage	\$ 101,985	\$ 398,221	\$ 9,015	\$ -	\$ 111,000	\$ 398,221
Production and Intermediate-term	153,280	317,582	-	-	153,280	317,582
Farm-related business	442,888	63,643	4,025	-	446,913	63,643
Energy	70,716	-	-	-	70,716	-
Communication	51,418	-	-	-	51,418	-
Mission-related investments	2,208	-	4,270	-	6,478	-
Lease receivables	6,004	-	-	-	6,004	-
Water and waste disposal	1,076	-	-	-	1,076	-
Total	<u>\$ 829,575</u>	<u>\$ 779,446</u>	<u>\$ 17,310</u>	<u>\$ -</u>	<u>\$ 846,885</u>	<u>\$ 779,446</u>

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

	<u>September 30, 2016</u>	<u>December 31, 2015</u>
Nonaccrual loans:		
Real estate mortgage	\$ 61,340	\$ 47,524
Production and intermediate-term	28,774	10,947
Farm-related business	1,642	1,011
Rural residential real estate	660	468
Lease receivable	4	16
Total nonaccrual loans	<u>\$ 92,420</u>	<u>\$ 59,966</u>
Accruing restructured loans:		
Real estate mortgage	\$ 7,944	\$ 4,642
Production and intermediate-term	2,612	6,542
Rural residential real estate	-	155
Mission-related investments	2,264	2,282
Total accruing restructured loans	<u>\$ 12,820</u>	<u>\$ 13,621</u>
Accruing loans 90 days or more past due:		
Real estate mortgage	\$ 142	\$ 295
Production and intermediate-term	810	583
Rural residential real estate	-	92
Total accruing loans 90 days or more past due	<u>\$ 952</u>	<u>\$ 970</u>
Total nonperforming loans	<u>\$ 106,192</u>	<u>\$ 74,557</u>
Other property owned	1,902	1,109
Total nonperforming assets	<u>\$ 108,094</u>	<u>\$ 75,666</u>

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

- Acceptable – assets are expected to be fully collectible and represent the highest quality,
- 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 factors, conditions and values that make collection in full highly questionable, and
- Loss – assets are considered uncollectible.

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

	<u>September 30, 2016</u>	<u>December 31, 2015</u>
Real estate mortgage		
Acceptable	96.9%	97.1%
OAEM	1.4%	1.4%
Substandard/doubtful	1.7%	1.5%
	<u>100.0%</u>	<u>100.0%</u>
Production and intermediate-term		
Acceptable	88.2%	93.6%
OAEM	5.2%	2.9%
Substandard/doubtful	6.6%	3.5%
	<u>100.0%</u>	<u>100.0%</u>
Farm-related business		
Acceptable	97.3%	95.2%
OAEM	0.8%	3.1%
Substandard/doubtful	1.9%	1.7%
	<u>100.0%</u>	<u>100.0%</u>
Rural residential real estate		
Acceptable	97.6%	97.7%
OAEM	1.5%	1.3%
Substandard/doubtful	0.9%	1.0%
	<u>100.0%</u>	<u>100.0%</u>
Energy		
Acceptable	81.9%	100.0%
OAEM	18.1%	-
Substandard/doubtful	-	-
	<u>100.0%</u>	<u>100.0%</u>
Communication		
Acceptable	100.0%	100.0%
OAEM	-	-
Substandard/doubtful	-	-
	<u>100.0%</u>	<u>100.0%</u>
Mission-related investments		
Acceptable	100.0%	100.0%
OAEM	-	-
Substandard/doubtful	-	-
	<u>100.0%</u>	<u>100.0%</u>
Lease receivables		
Acceptable	99.9%	99.7%
OAEM	-	-
Substandard/doubtful	0.1%	0.3%
	<u>100.0%</u>	<u>100.0%</u>
Water and waste disposal		
Acceptable	100.0%	100.0%
OAEM	-	-
Substandard/doubtful	-	-
	<u>100.0%</u>	<u>100.0%</u>
Total Loans		
Acceptable	95.7%	96.6%
OAEM	2.0%	1.7%
Substandard/doubtful	2.3%	1.7%
	<u>100.0%</u>	<u>100.0%</u>

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

	30-89 Days Past Due	90 Days or More Past Due	Total Past Due	Not Past Due or less than 30 Days Past Due	Total Loans	Loans > 90 Days and Accruing
September 30, 2016						
Real estate mortgage	\$31,649	\$ 25,538	\$ 57,187	\$ 5,100,612	\$ 5,157,799	\$ 142
Production and intermediate-term	16,442	7,072	23,514	828,822	852,336	810
Farm-related business	756	-	756	611,191	611,947	-
Rural residential real estate	1,263	-	1,263	152,572	153,835	-
Energy	-	-	-	70,847	70,847	-
Communication	-	-	-	51,492	51,492	-
Mission-related investments	-	-	-	8,072	8,072	-
Lease receivables	-	-	-	6,400	6,400	-
Water and waste disposal	-	-	-	1,078	1,078	-
Total	\$50,110	\$ 32,610	\$ 82,720	\$ 6,831,086	\$ 6,913,806	\$ 952
December 31, 2015						
Real estate mortgage	\$25,908	\$ 16,812	\$ 42,720	\$ 4,850,922	\$ 4,893,642	\$ 295
Production and intermediate-term	14,549	6,349	20,898	816,438	837,336	583
Farm-related business	6,633	-	6,633	538,129	544,762	-
Rural residential real estate	300	92	392	144,695	145,087	92
Energy	-	-	-	46,543	46,543	-
Communication	-	-	-	53,104	53,104	-
Mission-related investments	-	-	-	8,189	8,189	-
Lease receivables	-	-	-	6,108	6,108	-
Water and waste disposal	-	-	-	1,794	1,794	-
Total	\$47,390	\$ 23,253	\$ 70,643	\$ 6,465,922	\$ 6,536,565	\$ 970

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

As of September 30, 2016 the total troubled debt restructured loans was \$14,547, including \$1,727 classified as nonaccrual and \$12,820 classified as accrual, with specific allowance for loan losses of \$158. As of September 30, 2016 commitments to lend funds to borrowers whose loan terms have been modified in a troubled debt restructuring were \$12.

The following table presents additional information regarding troubled debt restructurings, which includes both accrual and nonaccrual loans with troubled debt restructuring designation that occurred. Balance of Pre-TDR designation represents quarter-end loans just prior to restructuring and post-TDR represents the quarter-end loans immediately following the restructuring. The Association had no loans that met the accounting criteria as a troubled debt restructuring and that occurred during the quarter ended September 2016 and 2015.

	Troubled Debt Restructuring Activity			
	2016		2015	
	Pre-TDR Designation Balance	Post-TDR Designation Balance	Pre-TDR Designation Balance	Post-TDR Designation Balance
Nine months ended September 30:				
Real estate mortgage	\$ -	\$ -	\$ 71	\$ 70
Production and intermediate-term	-	-	880	447
Rural residential real estate	-	-	161	159
Total	\$ -	\$ -	\$ 1,112	\$ 676

The Association had one loan that met the accounting criteria as troubled debt restructuring and that occurred during the previous twelve months, and for which there was an extension of term during that same period.

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

Additional impaired loan information is as follows:

	At September 30, 2016			At December 31, 2015		
	Loan Balance	Unpaid Principal Balance	Related Specific Allowance	Loan Balance	Unpaid Principal Balance	Related Specific Allowance
Impaired loans with a related allowance for loan losses:						
Real estate mortgage	\$ 6,000	\$ 6,080	\$ 772	\$ 1,425	\$ 1,456	\$ 259
Production and intermediate-term	12,955	13,184	2,421	5,649	5,650	1,881
Farm-related business	735	735	115	-	-	-
Mission-related investments	2,208	2,208	86	2,258	2,258	84
Total	<u>\$ 21,898</u>	<u>\$ 22,207</u>	<u>\$ 3,394</u>	<u>\$ 9,332</u>	<u>\$ 9,364</u>	<u>\$ 2,224</u>
Impaired loans with no related allowance for loan losses:						
Real estate mortgage	\$ 63,409	\$ 66,326	\$ -	\$ 51,019	\$ 54,505	\$ -
Production and intermediate-term	19,184	21,684	-	12,330	15,228	-
Farm-related business	907	15,233	-	1,011	20,083	-
Rural residential real estate	660	768	-	713	857	-
Lease receivables	4	4	-	16	16	-
Total	<u>\$ 84,164</u>	<u>\$ 104,015</u>	<u>\$ -</u>	<u>\$ 65,089</u>	<u>\$ 90,689</u>	<u>\$ -</u>
Total impaired loans:						
Real estate mortgage	\$ 69,409	\$ 72,406	\$ 772	\$ 52,444	\$ 55,961	\$ 259
Production and intermediate-term	32,139	34,868	2,421	17,979	20,878	1,881
Farm-related business	1,642	15,968	115	1,011	20,083	-
Rural residential real estate	660	768	-	713	857	-
Mission-related investments	2,208	2,208	86	2,258	2,258	84
Lease receivables	4	4	-	16	16	-
Total	<u>\$ 106,062</u>	<u>\$ 126,222</u>	<u>\$ 3,394</u>	<u>\$ 74,421</u>	<u>\$ 100,053</u>	<u>\$ 2,224</u>

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

	For the Three Months Ended				For the Nine Months Ended			
	September 30, 2016		September 30, 2015		September 30, 2016		September 30, 2015	
	Average	Interest	Average	Interest	Average	Interest	Average Impaired	Interest Income
	Impaired	Income	Impaired	Income	Impaired	Income	Loans	Recognized
Loans	Recognized	Loans	Recognized	Loans	Recognized	Loans	Recognized	
Impaired loans with a related allowance for loan losses:								
Real estate mortgage	\$ 6,125	\$ -	\$ 1,272	\$ -	\$ 4,130	\$ 79	\$ 1,170	\$ 4
Production and intermediate-term	15,381	21	3,740	-	12,683	102	3,601	6
Farm-related business	741	-	-	-	330	19	334	-
Rural residential real estate	-	-	1	-	-	-	4	-
Mission-related investments	2,208	34	2,260	35	2,230	104	2,282	106
Total	<u>\$ 24,455</u>	<u>\$ 55</u>	<u>\$ 7,273</u>	<u>\$ 35</u>	<u>\$ 19,373</u>	<u>\$ 304</u>	<u>\$ 7,391</u>	<u>\$ 116</u>
Impaired loans with no related allowance for loan losses:								
Real estate mortgage	\$ 62,263	\$ 275	\$ 67,993	\$ 81	\$ 58,619	\$ 2,289	\$ 69,020	\$ 408
Production and intermediate-term	17,836	72	12,803	158	14,802	368	12,607	705
Farm-related business	907	2	2,462	-	918	3	2,816	-
Rural residential real estate	624	2	657	2	595	11	519	16
Mission-related investments	-	-	-	-	-	-	48	-
Lease receivables	6	-	21	-	10	-	25	-
Total	<u>\$ 81,636</u>	<u>\$ 351</u>	<u>\$ 83,936</u>	<u>\$ 241</u>	<u>\$ 74,944</u>	<u>\$ 2,671</u>	<u>\$ 85,035</u>	<u>\$ 1,129</u>
Total impaired loans:								
Real estate mortgage	\$ 68,388	\$ 275	\$ 69,265	\$ 81	\$ 62,749	\$ 2,368	\$ 70,190	\$ 412
Production and intermediate-term	33,217	93	16,543	158	27,485	470	16,208	711
Farm-related business	1,648	2	2,462	-	1,248	22	3,150	-
Rural residential real estate	624	2	658	2	595	11	523	16
Mission-related investments	2,208	34	2,260	35	2,230	104	2,330	106
Lease receivables	6	-	21	-	10	-	25	-
Total	<u>\$ 106,091</u>	<u>\$ 406</u>	<u>\$ 91,209</u>	<u>\$ 276</u>	<u>\$ 94,317</u>	<u>\$ 2,975</u>	<u>\$ 92,426</u>	<u>\$ 1,245</u>

A summary of changes in the allowance for loan losses and the ending balance including accrued interest of loans outstanding are as follows:

	Real Estate Mortgage	Production and Intermediate Term	Farm related business	Rural Residential Real Estate	Energy	Communication	Mission Related Investments	Lease Receivable	Total
Allowance for credit losses:									
Balance at									
June 30, 2016	\$ 10,186	\$ 12,735	\$ 3,719	\$ 303	\$ 654	\$ 175	\$ 89	\$ 23	\$ 27,884
Charge-offs	-	(30)	-	-	-	-	-	-	(30)
Recoveries	7	1	24	2	-	336	-	-	370
Provision for loan losses	(647)	3,754	366	(25)	251	(329)	(1)	(1)	3,368
Other *	(19)	(605)	(193)	(1)	(7)	(1)	-	-	(826)
Balance at September 30, 2016	<u>\$ 9,527</u>	<u>\$ 15,855</u>	<u>\$ 3,916</u>	<u>\$ 279</u>	<u>\$ 898</u>	<u>\$ 181</u>	<u>\$ 88</u>	<u>\$ 22</u>	<u>\$ 30,766</u>
Balance at									
December 31, 2015	\$ 10,053	\$ 10,465	\$ 2,023	\$ 289	\$ 247	\$ 141	\$ 89	\$ 21	\$ 23,328
Charge-offs	(49)	(448)	-	-	-	-	-	-	(497)
Recoveries	469	103	177	6	-	349	-	-	1,104
Provision for loan losses	(927)	6,340	1,909	(15)	658	(308)	(1)	1	7,657
Other *	(19)	(605)	(193)	(1)	(7)	(1)	-	-	(826)
Balance at September 30, 2016	<u>\$ 9,527</u>	<u>\$ 15,855</u>	<u>\$ 3,916</u>	<u>\$ 279</u>	<u>\$ 898</u>	<u>\$ 181</u>	<u>\$ 88</u>	<u>\$ 22</u>	<u>\$ 30,766</u>
Allowance for loan losses:									
Ending Balance at September 30 2016									
Individually evaluated for impairment	\$ 772	\$ 2,421	\$ 115	\$ -	\$ -	\$ -	\$ 86	\$ -	\$ 3,394
Collectively evaluated for impairment	\$ 8,755	\$ 13,434	\$ 3,801	\$ 279	\$ 898	\$ 181	\$ 2	\$ 22	\$ 27,372
Balance at									
June 30, 2015	\$ 8,280	\$ 6,852	\$ 1,763	\$ 212	\$ 194	\$ 136	\$ 83	\$ 24	\$ 17,544
Charge-offs	-	(297)	-	-	-	-	-	-	(297)
Recoveries	19	52	219	-	-	-	-	-	290
Provision for loan losses	533	1,323	(404)	22	6	(15)	1	2	1,468
Other	-	-	83	-	-	-	-	-	83
Balance at September 30, 2015	<u>\$ 8,832</u>	<u>\$ 7,930</u>	<u>\$ 1,661</u>	<u>\$ 234</u>	<u>\$ 200</u>	<u>\$ 121</u>	<u>\$ 84</u>	<u>\$ 26</u>	<u>\$ 19,088</u>
Balance at									
December 31, 2014	\$ 6,993	\$ 6,662	\$ 1,511	\$ 191	\$ 178	\$ 133	\$ 82	\$ 23	\$ 15,773
Charge-offs	(478)	(378)	-	(7)	-	-	-	-	(863)
Recoveries	26	166	395	-	-	36	-	-	623
Provision for loan losses	2,291	1,480	1,468	50	22	(48)	2	3	5,268
Other	-	-	(1,713)	-	-	-	-	-	(1,713)
Balance at September 30, 2015	<u>\$ 8,832</u>	<u>\$ 7,930</u>	<u>\$ 1,661</u>	<u>\$ 234</u>	<u>\$ 200</u>	<u>\$ 121</u>	<u>\$ 84</u>	<u>\$ 26</u>	<u>\$ 19,088</u>
Allowance for loan losses:									
Ending Balance at December 31, 2015									
individually evaluated for impairment	\$ 259	\$ 1,881	\$ -	\$ -	\$ -	\$ -	\$ 84	\$ -	\$ 2,224
collectively evaluated for impairment	\$ 9,794	\$ 8,584	\$ 2,023	\$ 289	\$ 247	\$ 141	\$ 5	\$ 21	\$ 21,104
Recorded Investments in Loans Outstanding:									
Ending Balance at									
September 30, 2016	\$ 5,157,797	\$ 852,337	\$ 611,948	\$ 153,835	\$ 71,925	\$ 51,492	\$ 8,072	\$ 6,400	\$ 6,913,806
Individually evaluated for impairment	\$ 69,409	\$ 32,139	\$ 1,642	\$ 660	\$ -	\$ -	\$ 2,208	\$ 4	\$ 106,062
Collectively evaluated for impairment	\$ 5,088,388	\$ 820,198	\$ 610,306	\$ 153,175	\$ 71,925	\$ 51,492	\$ 5,864	\$ 6,396	\$ 6,807,744
Ending Balance at									
December 31, 2015	\$ 4,893,644	\$ 837,335	\$ 544,762	\$ 145,087	\$ 48,336	\$ 53,104	\$ 8,189	\$ 6,108	\$ 6,536,565
Individually evaluated for impairment	\$ 52,444	\$ 17,979	\$ 1,011	\$ 713	\$ -	\$ -	\$ 2,258	\$ 16	\$ 74,421
Collectively evaluated for impairment	\$ 4,841,200	\$ 819,356	\$ 543,751	\$ 144,374	\$ 48,336	\$ 53,104	\$ 5,931	\$ 6,092	\$ 6,462,144

*The Association recognized a provision for loan loss of \$826 on unfunded commitments in the third quarter of 2016. Because this loss is recognized on commitments yet to be funded, it is included in Other Liabilities in the Consolidated Balance Sheet as of September 30, 2016.

NOTE 4 — FAIR VALUE MEASUREMENTS:

Accounting 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. See Note 14 “Fair Value Measurements” of the 2015 Annual Report to stockholders for a more complete description.

Assets held in nonqualified benefits trusts related to deferred compensation and supplemental retirement plans are classified as Level 1. Level 1 valuation utilizes quoted prices in active markets for identical assets or liabilities that the reporting entity has the ability to access at the measurement date. The trust funds include investments that are actually traded and have quoted net assets values that are quoted in the marketplace. These assets are measured at fair value on a recurring basis and are summarized below:

	Total Fair Value September 30, 2016	Total Fair Value December 31, 2015
Beginning Balance	\$ 5,496	\$ 5,097
Transfers In	397	351
Other Market Changes	(88)	48
	<u>5,805</u>	<u>5,496</u>
Assets held in non-qualified benefits trusts	<u>\$ 5,805</u>	<u>\$ 5,496</u>

Sensitivity to Changes in Significant Unobservable Inputs

For recurring fair value measurements categorized within Level 3 of the fair value hierarchy, the significant unobservable inputs used in the fair value measurement of the mortgage-backed securities are prepayment rates, probability of default, and loss severity in the event of default. Significant increases (decreases) in any of those inputs in isolation would result in a significantly lower (higher) fair value measurement.

Generally, a change in the assumption used for the probability of default is accompanied by a directionally similar change in the assumption used for the loss severity and a directionally opposite change in the assumption used for prepayment rates.

Quoted market prices are generally not available for the instruments presented below. Accordingly, fair values are based on internal models that consider 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.

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

These assets are measured at fair value on a nonrecurring basis and are summarized below:

	Total Fair Value	Total Fair Value
	September 30, 2016	December 31, 2015
Impaired Loans	\$ 18,504	\$ 7,108
Other property owned	1,902	1,109
Total	<u>\$ 20,406</u>	<u>\$ 8,217</u>

NOTE 5 — MEMBERS EQUITY:

In September 2016, the board of directors approved a resolution to retire \$36,783 in nonqualified allocated equities which are to be paid to the recipients in November 2016. The retirement is a distribution of 50.0 percent of the earnings allocated in 2010.

The board of directors approved a \$137,631 patronage distribution for 2015. \$56,746 of this distribution was paid in cash in March 2016. \$80,885 was to be distributed in the form of nonqualified allocated equity. In March 2016 the Association finalized the computation of these distributions which resulted in a reduction in nonqualified allocations of \$4 resulting in an actual allocation of \$80,881. The owners of these nonqualified distributions will not pay federal income taxes until the equities are retired. It is the board's intention with these allocations to assign ownership of the earnings of the Association, allowing the stockholders to benefit more fully from the earnings of the Association and to create a method to make future equity distributions in the form of cash. While there is not a planned retirement of these allocated equities, the board of directors will make an annual evaluation of the Association's capital position and determine if some cash retirements of these equities can be made. In 2014, the board of directors approved a \$142,065 patronage distribution for 2014, with cash patronage payable of \$71,995 and \$70,070 in nonqualified allocations. In March 2015 the Association finalized the computation of these distributions which resulted in a reduction in cash patronage payable of \$15 for an actual cash distribution of \$71,980, and nonqualified allocations remained unchanged.

NOTE 6 — EMPLOYEE BENEFIT PLANS:

The Association expects to contribute \$4,637 to its pension plan in 2016, which will be \$272 more than the 2015 contribution. Pension plan funding expense was \$3,478 and \$3,274 for the nine months ended September 30, 2016 and 2015 respectively.

NOTE 7 — SUBSEQUENT EVENTS:

The Association has evaluated subsequent events through November 4, 2016 which is the date the financial statements were issued and there are no significant events requiring disclosure as of this date.