



## Farm Credit Services of Mandan, ACA

Quarterly Report  
June 30, 2017

### MANAGEMENT'S DISCUSSION AND ANALYSIS

The following commentary reviews the consolidated financial condition and consolidated results of operations of Farm Credit Services of Mandan, ACA and its subsidiaries Farm Credit Services of Mandan, FLCA and Farm Credit Services of Mandan, PCA. This discussion should be read in conjunction with both the unaudited consolidated financial information and related notes included in this Quarterly Report as well as Management's Discussion and Analysis included in our Annual Report for the year ended December 31, 2016 (2016 Annual Report).

Due to the nature of our financial relationship with AgriBank, FCB (AgriBank), the financial condition and results of operations of AgriBank materially impact our members' investment. To request free copies of the AgriBank or the AgriBank District financial reports or additional copies of our report, contact us at:

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### FORWARD-LOOKING INFORMATION

Any forward-looking statements in this Quarterly Report are based on current expectations and are subject to uncertainty and changes in circumstances. Actual results may differ materially from expectations due to a number of risks and uncertainties. More information about these risks and uncertainties is contained in our 2016 Annual Report. We undertake no duty to update or revise any forward-looking statements, whether as a result of new information, future events, or otherwise.

### AGRICULTURAL AND ECONOMIC CONDITIONS

Early 2017 moisture conditions were sufficient due to significant winter snowfall; however, much of our territory is currently dry due to below average rainfall. This will adversely affect small grain, pasture and hay land production. Recent moderate rainfall will improve the prospects for row and oil crops.

Livestock prices have moderated after experiencing a significant decline during the past two years. Producers with cow/calf operations were able to project modest profitability in 2017; however, current dry conditions are causing some producers to make adjustments. Some are grazing hay land acres where hay production potential was affected, with the plans of being able to buy the needed winter hay supplies. A few producers are reducing herd numbers by selling off older cow/calf pairs. Fortunately, they are able to do so in an improved livestock market. Some feeder operations were able to capitalize with the market improving over the winter and into the spring. This, combined with affordable cost of gains, helped provide feedlots with some profit in early 2017.

Purchases of machinery have continued to be slow, particularly for crop producers. Spring auction sales bids for larger and newer types of machinery were lower, resulting from producers limiting their capital purchases. Real estate sales have softened some but remain strong.

Commodity prices have somewhat improved, but dry conditions in parts of our territory will continue to challenge profitability for producers. Despite these challenges, nearly all producers will continue to obtain financing and continue their farming and ranching operations.

### LOAN PORTFOLIO

#### Loan Portfolio

Total loans were \$1.1 billion at June 30, 2017, an increase of \$62.1 million from December 31, 2016. The increase was primarily due to growth in our agribusiness portfolio from our Commercial Finance Group (CFG) alliance along with traditional real estate loans. There was also increased borrowings in our production and intermediate term loan portfolio due to the seasonal operating needs of producers.

#### Portfolio Credit Quality

The credit quality of our portfolio declined from December 31, 2016. Adversely classified loans increased to 1.8% of the portfolio at June 30, 2017, from 1.1% of the portfolio at December 31, 2016. The increase in adverse loans is due to challenges agricultural producers are experiencing and the resulting trend in the

portfolio to slightly weaker credit performance classifications. Adversely classified loans are loans we have identified as showing some credit weakness outside our credit standards. We have considered portfolio credit quality in assessing the reasonableness of our allowance for loan losses.

In certain circumstances, government guarantee programs are used to reduce the risk of loss. At June 30, 2017, \$23.7 million of our loans were, to some level, guaranteed under these government programs.

## Risk Assets

### Components of Risk Assets

(dollars in thousands)	June 30	December 31
As of:	2017	2016
Loans:		
Nonaccrual	\$ 1,251	\$ 583
Accruing restructured	4	880
Accruing loans 90 days or more past due	2,417	472
Total risk loans	3,672	1,935
Other property owned	--	--
Total risk assets	\$ 3,672	\$ 1,935
Total risk loans as a percentage of total loans	0.3%	0.2%
Nonaccrual loans as a percentage of total loans	0.1%	0.1%
Current nonaccrual loans as a percentage of total nonaccrual loans	23.7%	15.8%
Total delinquencies as a percentage of total loans	0.5%	1.3%

Note: Accruing loans include accrued interest receivable.

Our risk assets have increased from December 31, 2016, but remained at acceptable levels. Despite the increase in risk assets, total risk loans as a percentage of total loans were well within our established risk management guidelines.

The increase in nonaccrual loans was primarily due to several customers moving to nonaccrual status in the production and intermediate term loan category during the first half of 2017.

The increase in accruing loans 90 days or more past due was primarily due to a few loans in the production and intermediate term category and one loan in the real estate category becoming more than 90 days past due during the first half of 2017. Our accounting policy requires accruing loans past due 90 days or more to be transferred into nonaccrual status unless adequately secured and in the process of collection. Based on our analysis, all accruing loans 90 days or more past due were eligible to remain in accruing status.

## Allowance for Loan Losses

The allowance for loan losses is an estimate of losses on loans in our portfolio as of the financial statement date. We determine the appropriate level of allowance for loan losses based on periodic evaluation of factors such as loan loss history, estimated probability of default, estimated loss severity, portfolio quality, and current economic and environmental conditions.

### Allowance Coverage Ratios

As of:	June 30	December 31
	2017	2016
Allowance as a percentage of:		
Loans	0.3%	0.3%
Nonaccrual loans	240.8%	475.0%
Total risk loans	82.1%	143.1%

In our opinion, the allowance for loan losses was reasonable in relation to the risk in our loan portfolio at June 30, 2017.

## RESULTS OF OPERATIONS

### Profitability Information

(dollars in thousands)	2017	2016
For the six months ended June 30		
Net income	\$ 9,976	\$ 8,959
Return on average assets	1.8%	1.7%
Return on average members' equity	9.2%	9.0%

Changes in the chart above relate directly to:

- Changes in income discussed below
- Changes in assets discussed in the Loan Portfolio section
- Changes in capital discussed in the Funding, Liquidity, and Capital section

#### Changes in Significant Components of Net Income

(in thousands)			Increase (decrease) in net income
For the six months ended June 30	2017	2016	
Net interest income	\$ 14,996	\$ 14,101	\$ 895
Provision for loan losses	221	836	615
Patronage income	1,502	1,727	(225)
Other income, net	3,240	3,262	(22)
Operating expenses	9,069	8,705	(364)
Provision for income taxes	472	590	118
Net income	<u>\$ 9,976</u>	<u>\$ 8,959</u>	<u>\$ 1,017</u>

#### Changes in Net Interest Income

(in thousands)		
For the six months ended June 30	2017 vs 2016	
Changes in volume	\$	388
Changes in interest rates		466
Changes in nonaccrual income and other		41
Net change	<u>\$</u>	<u>895</u>

The change in the provision for loan losses was primarily related to changes in our portfolio, decreases to specific reserves, and changes in loan volume.

The change in operating expenses was primarily due to an increase in salaries expense.

### FUNDING, LIQUIDITY, AND CAPITAL

We borrow from AgriBank, under a note payable, in the form of a line of credit. Our note payable matures on February 29, 2020, at which time the note will be renegotiated. The repricing attributes of our line of credit generally correspond to the repricing attributes of our loan portfolio which significantly reduces our market interest rate risk. Due to the cooperative structure of the Farm Credit System and as we are a stockholder of AgriBank, we expect this borrowing relationship to continue into the foreseeable future.

The components of cost of funds associated with our note payable include:

- A marginal cost of debt component
- A spread component, which includes cost of servicing, cost of liquidity, and bank profit
- A risk premium component, if applicable

In addition, with approval from AgriBank, on July 24, 2006, we entered into a loan agreement with CoBank, ACB (CoBank) to obtain funding in the amount not to exceed \$20.0 million in connection with specific CoBank related transactions. The interest rate on such indebtedness will be established at the time of the related transactions. There was no outstanding balance on this agreement as of June 30, 2017 or December 31, 2016.

We were not subject to a risk premium at June 30, 2017, or December 31, 2016.

Total members' equity increased \$8.8 million from December 31, 2016, primarily due to net income for the period, which was partially offset by patronage distribution accruals.

Farm Credit Administration (FCA) Regulations require us to maintain minimums for various regulatory capital ratios. New regulations became effective January 1, 2017, which replaced the previously required core surplus and total surplus ratios with common equity tier 1, tier 1 capital, and total capital risk-based capital ratios. The new regulations also added tier 1 leverage and unallocated retained earnings and equivalents ratios. The permanent capital ratio continues to remain in effect, with some modifications to align with the new regulations.

The capital adequacy ratios are directly impacted by the changes in capital as more fully explained in this section and the changes in assets as discussed in the Loan Portfolio section. Refer to Note 4 of the accompanying Consolidated Financial Statements for additional detail regarding the capital ratios effective as of June 30, 2017. Refer to Note 6 in our 2016 Annual Report for a more complete description of the ratios effective as of December 31, 2016.

## RELATIONSHIP WITH AGRIBANK

### Purchased Services

During 2016, District Associations and AgriBank conducted research related to the creation of a separate service entity to provide many of the business services offered by AgriBank. A separate service entity allows District Associations and AgriBank to develop and maintain long-term, cost effective technology and business services. The service entity would be owned by certain District Associations and AgriBank. An application to form the service entity was submitted to the FCA for approval in May 2017.

### Patronage

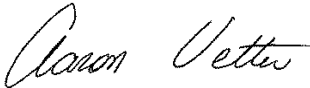
AgriBank has amended its capital plan effective July 1, 2017, to provide for adequate capital at AgriBank under the new capital regulations as well as to create a path to long-term capital optimization within the AgriBank District. The plan optimizes capital at AgriBank; distributing available AgriBank earnings in the form of patronage, either cash or stock. A key part of these changes involves maintaining capital adequacy such that sufficient earnings will be retained in the form of unallocated retained earnings and allocated stock to meet the leverage ratio target and other regulatory or policy constraints prior to any cash patronage distributions.

## CERTIFICATION

The undersigned have reviewed the June 30, 2017, Quarterly Report of Farm Credit Services of Mandan, ACA, which has been prepared under the oversight of the Audit Committee and in accordance with all applicable statutory or regulatory requirements. The information contained herein is true, accurate, and complete to the best of our knowledge and belief.



James Vander Vorst  
Chairperson of the Board  
Farm Credit Services of Mandan, ACA



Aaron Vetter  
Chief Executive Officer  
Farm Credit Services of Mandan, ACA



Sandy Nagel  
Vice President – Corporate Finance  
Farm Credit Services of Mandan, ACA

August 7, 2017

# CONSOLIDATED STATEMENTS OF CONDITION

*Farm Credit Services of Mandan, ACA*

*(in thousands)*

*(Unaudited)*

As of:	June 30 2017	December 31 2016
<b>ASSETS</b>		
Loans	\$ 1,109,866	\$ 1,047,773
Allowance for loan losses	3,013	2,769
Net loans	1,106,853	1,045,004
Investment in AgriBank, FCB	20,903	20,903
Accrued interest receivable	12,005	13,869
Other assets	13,336	11,164
Total assets	\$ 1,153,097	\$ 1,090,940
<b>LIABILITIES</b>		
Note payable to AgriBank, FCB	\$ 922,371	\$ 867,311
Accrued interest payable	3,700	3,116
Deferred tax liabilities, net	782	600
Patronage distribution payable	1,150	2,124
Other liabilities	4,332	5,784
Total liabilities	932,335	878,935
Contingencies and commitments (Note 5)		
<b>MEMBERS' EQUITY</b>		
Capital stock and participation certificates	2,305	2,375
Unallocated surplus	218,457	209,630
Total members' equity	220,762	212,005
Total liabilities and members' equity	\$ 1,153,097	\$ 1,090,940

*The accompanying notes are an integral part of these Consolidated Financial Statements.*

# CONSOLIDATED STATEMENTS OF INCOME

Farm Credit Services of Mandan, ACA

(in thousands)

(Unaudited)

For the period ended June 30	Three Months Ended		Six Months Ended	
	2017	2016	2017	2016
<b>Interest income</b>	\$ 11,365	\$ 10,135	\$ 21,867	\$ 19,853
<b>Interest expense</b>	3,700	2,952	6,871	5,752
Net interest income	7,665	7,183	14,996	14,101
<b>Provision for loan losses</b>	261	790	221	836
Net interest income after provision for loan losses	7,404	6,393	14,775	13,265
<b>Other income</b>				
Patronage income	763	882	1,502	1,727
Financially related services income	1,203	1,375	2,520	2,648
Fee income	322	310	649	610
Miscellaneous income (loss), net	26	(9)	71	4
Total other income	2,314	2,558	4,742	4,989
<b>Operating expenses</b>				
Salaries and employee benefits	3,038	2,986	6,105	5,855
Other operating expenses	1,399	1,339	2,964	2,850
Total operating expenses	4,437	4,325	9,069	8,705
Income before income taxes	5,281	4,626	10,448	9,549
<b>Provision for income taxes</b>	212	279	472	590
Net income	\$ 5,069	\$ 4,347	\$ 9,976	\$ 8,959

The accompanying notes are an integral part of these Consolidated Financial Statements.

## CONSOLIDATED STATEMENTS OF CHANGES IN MEMBERS' EQUITY

*Farm Credit Services of Mandan, ACA*

*(in thousands)*

*(Unaudited)*

		Capital Stock and Participation Certificates	Unallocated Surplus		Total Members' Equity
Balance at December 31, 2015	\$	2,435	\$ 192,970	\$	195,405
Net income		--	8,959		8,959
Unallocated surplus designated for patronage distributions		--	(1,063)		(1,063)
Capital stock and participation certificates issued		66	--		66
Capital stock and participation certificates retired		(90)	--		(90)
<b>Balance at June 30, 2016</b>	<b>\$</b>	<b>2,411</b>	<b>\$ 200,866</b>	<b>\$</b>	<b>203,277</b>
Balance at December 31, 2016	\$	2,375	\$ 209,630	\$	212,005
Net income		--	9,976		9,976
Unallocated surplus designated for patronage distributions		--	(1,149)		(1,149)
Capital stock and participation certificates issued		42	--		42
Capital stock and participation certificates retired		(112)	--		(112)
<b>Balance at June 30, 2017</b>	<b>\$</b>	<b>2,305</b>	<b>\$ 218,457</b>	<b>\$</b>	<b>220,762</b>

*The accompanying notes are an integral part of these Consolidated Financial Statements.*

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## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

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### NOTE 1: ORGANIZATION AND SIGNIFICANT ACCOUNTING POLICIES

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The Consolidated Financial Statements contain all adjustments necessary for a fair presentation of the interim consolidated financial condition and consolidated results of operations. Our accounting policies conform to accounting principles generally accepted in the United States of America (GAAP) and the prevailing practices within the financial services industry. This interim Quarterly Report is prepared based upon statutory and regulatory requirements and in accordance with GAAP. However, certain disclosures required by GAAP are omitted. The results of the six months ended June 30, 2017, are not necessarily indicative of the results to be expected for the year ending December 31, 2017. The interim financial statements and the related notes in this Quarterly Report should be read in conjunction with the Consolidated Financial Statements and related notes included in our Annual Report for the year ended December 31, 2016 (2016 Annual Report).

The Consolidated Financial Statements present the consolidated financial results of Farm Credit Services of Mandan, ACA and its subsidiaries Farm Credit Services of Mandan, FLCA and Farm Credit Services of Mandan, PCA (the subsidiaries). All material intercompany transactions and balances have been eliminated in consolidation.

#### Recently Issued or Adopted Accounting Pronouncements

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We have assessed the potential impact of accounting standards that have been issued by the Financial Accounting Standards Board (FASB) and have determined the following standards to be applicable to our business:

Standard	Description	Effective date and financial statement impact
In June 2016, the FASB issued Accounting Standards Update (ASU) 2016-13 "Financial Instruments – Credit Losses."	The guidance replaces the current incurred loss impairment methodology with a methodology that reflects expected credit losses and requires consideration of a broader range of reasonable and supportable information to inform credit loss estimates. Credit losses relating to available-for-sale securities would also be recorded through an allowance for credit losses.	The guidance is effective for nonpublic entities for annual reporting periods beginning after December 15, 2020, and interim periods within annual periods beginning after December 15, 2021. Early adoption is permitted as of annual reporting periods beginning after December 15, 2018, including interim periods within those annual periods. We are currently evaluating the impact of the guidance on our financial condition, results of operations, cash flows, and financial statement disclosures.
In February 2016, the FASB issued ASU 2016-02 "Leases."	The guidance modifies the recognition and accounting for lessees and lessors and requires expanded disclosures regarding assumptions used to recognize revenue and expenses related to leases.	The guidance is effective for nonpublic entities for annual reporting periods beginning after December 15, 2019, and interim periods the subsequent year. Early adoption is permitted and modified retrospective adoption is required. We are currently evaluating the impact of the guidance on our financial condition, results of operations, cash flows, and financial statement disclosures.
In January 2016, the FASB issued ASU 2016-01 "Recognition and Measurement of Financial Assets and Financial Liabilities."	The guidance is intended to enhance the reporting model for financial instruments to provide users of financial statements with more decision-useful information. The amendments address certain aspects of recognition, measurement, presentation, and disclosure of financial statements.	The guidance is effective for nonpublic entities for annual reporting periods beginning after December 15, 2018, and interim periods with annual periods beginning after December 15, 2019. Certain disclosure changes are permitted to be immediately adopted for annual reporting periods that have not yet been made available for issuance. Nonpublic entities are no longer required to include certain fair value of financial instruments disclosures as part of these disclosure changes. We have immediately adopted this guidance and have excluded such disclosures from our Notes to Consolidated Financial Statements. Early adoption is permitted for interim and annual reporting periods beginning after December 15, 2017, for other applicable sections of the guidance. We are currently evaluating the impact of the remaining guidance on our financial condition, results of operations, cash flows, and financial statement disclosures.

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Standard	Description	Effective date and financial statement impact
In May 2014, the FASB issued ASU 2014-09 "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 our contracts would be excluded from the scope of this new guidance.	The guidance is effective for nonpublic entities for annual reporting periods beginning after December 15, 2017, and interim periods within annual periods beginning after December 15, 2018. In March 2016, the FASB issued ASUs 2016-08 and 2016-10, which provided further clarifying guidance on the previously issued standard. We are in the process of reviewing contracts to determine the effect, if any, on our financial condition and results of operations.

## NOTE 2: LOANS AND ALLOWANCE FOR LOAN LOSSES

### Loans by Type

(dollars in thousands)

As of:	June 30, 2017		December 31, 2016	
	Amount	%	Amount	%
Real estate mortgage	\$ 366,002	33.0%	\$ 347,677	33.2%
Production and intermediate term	442,019	39.8%	429,190	41.0%
Agribusiness	200,057	18.0%	171,558	16.4%
Other	101,788	9.2%	99,348	9.4%
Total	\$ 1,109,866	100.0%	\$ 1,047,773	100.0%

The other category is primarily comprised of energy, communication, and agricultural export finance loans and certain assets originated under the Mission Related Investment authority, as well as finance leases.

### Delinquency

#### Aging Analysis of Loans

(in thousands) As of June 30, 2017	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	90 Days or More Past Due and Accruing
	Real estate mortgage	\$ 559	\$ 1,235	\$ 1,794	\$ 370,055	\$ 371,849
Production and intermediate term	1,076	2,120	3,196	444,378	447,574	1,395
Agribusiness	96	--	96	200,420	200,516	--
Other	--	--	--	101,929	101,929	--
Total	\$ 1,731	\$ 3,355	\$ 5,086	\$ 1,116,782	\$ 1,121,868	\$ 2,417

As of December 31, 2016	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	90 Days or More Past Due and Accruing
	Real estate mortgage	\$ 3,426	\$ --	\$ 3,426	\$ 350,970	\$ 354,396
Production and intermediate term	8,011	962	8,973	426,651	435,624	472
Agribusiness	1,180	--	1,180	170,880	172,060	--
Other	--	--	--	99,558	99,558	--
Total	\$ 12,617	\$ 962	\$ 13,579	\$ 1,048,059	\$ 1,061,638	\$ 472

Note: Accruing loans include accrued interest receivable.

## Risk Loans

Risk loans are loans for which it is probable that all principal and interest will not be collected according to the contractual terms.

### Risk Loan Information

(in thousands)	June 30	December 31
As of:	2017	2016
Volume with specific allowance	\$ 1,475	\$ 164
Volume without specific allowance	2,197	1,771
Total risk loans	\$ 3,672	\$ 1,935
Total specific allowance	\$ 452	\$ 145
For the six months ended June 30	2017	2016
Income on accrual risk loans	\$ 31	\$ 13
Income on nonaccrual loans	123	82
Total income on risk loans	\$ 154	\$ 95
Average risk loans	\$ 1,837	\$ 2,861

Note: Accruing loans include accrued interest receivable.

We did not have any material commitments to lend additional money to borrowers whose loans were at risk at June 30, 2017.

### Troubled Debt Restructurings (TDRs)

In situations where, for economic or legal reasons related to the borrower's financial difficulties, we grant a concession for other than an insignificant period of time to the borrower that we would not otherwise consider, the related loan is classified as a troubled debt restructuring, also known as a restructured loan. A concession is generally granted in order to minimize economic loss and avoid foreclosure. Concessions vary by program and borrower and may include interest rate reductions, term extensions, payment deferrals, or an acceptance of additional collateral in lieu of payments. In limited circumstances, principal may be forgiven. Loans classified as TDRs are considered risk loans. All risk loans are analyzed within our allowance for loan losses. We record a specific allowance to reduce the carrying amount of the restructured loan to the lower of book value or net realizable value of collateral.

We completed TDRs of certain production and intermediate loans during the six months ended June 30, 2017. Our recorded investment in these loans just prior to restructuring was \$53 thousand during the six months ended June 30, 2017. Our recorded investment in these loans immediately following the restructuring was \$52 thousand during the six months ended June 30, 2017. There were no TDRs that occurred during the six months ended June 30, 2016. The recorded investment of the loan is the unpaid principal amount of the receivable increased or decreased by applicable accrued interest and unamortized premium, discount, finance charges, and acquisition costs and may also reflect a previous direct charge-off.

The primary type of modification was extension of maturity.

We had TDRs in the production and intermediate term loan category of \$2 thousand and \$8 thousand that defaulted during the six months ended June 30, 2017, and 2016, respectively in which the modifications were within twelve months of the respective reporting period.

### TDRs Outstanding

(in thousands)	June 30	December 31
As of:	2017	2016
Accrual status:		
Real estate mortgage	\$ --	\$ --
Production and intermediate term	4	2
Other	--	878
Total TDRs in accrual status	\$ 4	\$ 880
Nonaccrual status:		
Real estate mortgage	\$ 26	\$ 35
Production and intermediate term	85	33
Other	--	--
Total TDRs in nonaccrual status	\$ 111	\$ 68
Total TDRs:		
Real estate mortgage	\$ 26	\$ 35
Production and intermediate term	89	35
Other	--	878
Total TDRs	\$ 115	\$ 948

The decrease in TDRs outstanding from December 31, 2016, was primarily due to communication loans, which are included in the other loan category, being refinanced at market terms during the first quarter of 2017.

There were no material commitments to lend to borrowers whose loans have been modified in a TDR at June 30, 2017.

#### Allowance for Loan Losses

##### Changes for Allowance for Loan Losses

(in thousands)		
Six months ended June 30	2017	2016
Balance at beginning of period	\$ 2,769	\$ 2,057
Provision for loan losses	221	836
Loan recoveries	80	34
Loan charge-offs	(57)	(91)
Balance at end of period	\$ 3,013	\$ 2,836

#### NOTE 3: INVESTMENT IN AGRIBANK, FCB

Effective July 1, 2017, we were required by AgriBank to maintain an investment equal to 2.25% of the average quarterly balance of our note payable, with an additional amount required on Association growth in excess of a targeted growth rate, if the District is also growing above a targeted growth rate. From January 1 to June 30, 2017, we were required by AgriBank to maintain an investment equal to 2.25% of the average quarterly balance of our note payable, with an additional amount required on growth in excess of a sustainable growth rate. Previously, the required investment was equal to 2.25% of the average quarterly balance of our note payable to AgriBank plus an additional 1.0% on growth that exceeded a targeted rate.

##### Investment in AgriBank

(in thousands)		
As of:	June 30 2017	December 31 2016
Required stock investment	\$ 20,133	\$ 20,461
Purchased excess stock investment	770	442
Total investment	\$ 20,903	\$ 20,903

#### NOTE 4: MEMBERS' EQUITY

##### Regulatory Capitalization Requirements

##### Select Capital Ratios

	As of June 30, 2017	Regulatory Minimums	Capital Conservation Buffer	Total
Risk-adjusted:				
Common equity tier 1 ratio	15.9%	4.5%	2.5%*	7.0%
Tier 1 capital ratio	15.9%	6.0%	2.5%*	8.5%
Total capital ratio	16.1%	8.0%	2.5%*	10.5%
Permanent capital ratio	15.9%	7.0%	0.0%	7.0%
Non-risk-adjusted:				
Tier 1 leverage ratio	18.2%	4.0%	1.0%	5.0%
Unallocated retained earnings and equivalents leverage ratio	18.6%	1.5%	0.0%	1.5%

\*The 2.5% capital conservation buffer over risk-adjusted ratio minimums will be phased in over three years under the FCA capital requirements.

Effective January 1, 2017, the regulatory capital requirements for Farm Credit System Banks and associations were modified. The new regulations replaced existing core surplus and total surplus ratios with common equity tier 1, tier 1 capital, and total capital risk-based capital ratios. The new regulations also added a tier 1 leverage ratio and an unallocated retained earnings equivalents (UREE) leverage ratio. The permanent capital ratio continues to remain in effect, with some modifications, to align with the new regulations.

Risk-adjusted assets have been defined by Farm Credit Administration (FCA) Regulations as the Statement of Condition 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 impact of increasing risk-adjusted assets (decreasing risk-based regulatory capital ratios) were as follows:

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

Risk-adjusted assets is calculated differently for the permanent capital ratio (referred herein as PCR risk-adjusted assets) compared to the other risk-based capital ratios. The primary difference is the inclusion of the allowance for loan losses as a deduction to risk-adjusted assets for the permanent capital ratio.

These ratios are based on a three-month average daily balance in accordance with FCA Regulations and are calculated as follows (not all items below may be applicable to our Association):

- Common equity tier 1 ratio is statutory minimum purchased member stock, other required member stock held for a minimum of 7 years, allocated equities held for a minimum of 7 years or not subject to retirement, unallocated retained earnings, paid-in capital, less certain regulatory required deductions including the amount of allocated investments in other System institutions, and the amount of purchased investments in other System institutions under the corresponding deduction approach, divided by average risk-adjusted assets.
- Tier 1 capital ratio is common equity tier 1 plus non-cumulative perpetual preferred stock, divided by average risk-adjusted assets.
- Total capital is tier 1 capital plus other required member stock held for a minimum of 5 years, allocated equities 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 credit losses subject to certain limitations, less certain investments in other System institutions under the corresponding deduction approach, divided by average risk-adjusted assets.
- 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 allocated and purchased investments in other System institutions divided by PCR risk-adjusted assets.
- Tier 1 leverage ratio is tier 1 capital, including regulatory deductions, divided by average assets less regulatory deductions subject to tier 1 capital.
- UREE leverage ratio is unallocated retained earnings, paid-in capital, allocated surplus not subject to retirement less certain regulatory required deductions including the amount of allocated investments in other System institutions divided by average assets less regulatory deductions subject to tier 1 capital.

If the capital ratios fall below the total 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.

Effective January 1, 2017, the regulatory capital requirements allow for allotment agreements for only the permanent capital ratio and, as such, any stock in excess of our AgriBank required investment was not included in the common equity tier 1, tier 1 capital, total capital, or leverage ratios. We had no allocated excess stock at June 30, 2017, or December 31, 2016.

Refer to Note 6 in our 2016 Annual Report for a more complete description of the ratios effective as of December 31, 2016.

#### **NOTE 5: CONTINGENCIES AND COMMITMENTS**

In the normal course of business, we have various contingent liabilities and commitments outstanding, primarily commitments to extend credit, which may not be reflected in the Consolidated Financial Statements. We do not anticipate any material losses because of these contingencies or commitments.

We may be named as a defendant in certain lawsuits or legal actions in the normal course of business. At the date of these Consolidated Financial Statements, our management team was not aware of any material actions. However, management cannot ensure that such actions or other contingencies will not arise in the future.

#### **NOTE 6: FAIR VALUE MEASUREMENTS**

Fair value is defined as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date in the principal or most advantageous market for the asset or liability. Accounting guidance also establishes a fair value hierarchy, with three levels of inputs that may be used to measure fair value. Refer to Note 2 in our 2016 Annual Report for a more complete description of the three input levels.

We did not have any assets or liabilities measured at fair value on a recurring basis at June 30, 2017, or December 31, 2016.

## Non-Recurring

We may be required, from time to time, to measure certain assets at fair value on a non-recurring basis.

### Assets Measured at Fair Value on a Non-recurring Basis

(in thousands)

	As of June 30, 2017				Six months ended June 30, 2017	
	Fair Value Measurement Using			Total Fair Value	Total (Losses) Gains	
	Level 1	Level 2	Level 3			
Impaired loans	\$ --	\$ 972	\$ 102	\$ 1,074	\$ (364)	
Other property owned	--	--	--	--	--	

	As of December 31, 2016				Six months ended June 30, 2016	
	Fair Value Measurement Using			Total Fair Value	Total (Losses) Gains	
	Level 1	Level 2	Level 3			
Impaired loans	\$ --	\$ --	\$ 20	\$ 20	\$ (476)	
Other property owned	--	--	--	--	3	

## Valuation Techniques

**Impaired loans:** Represents the carrying amount and related write-downs of loans which were evaluated for individual impairment based on the appraised value of the underlying collateral. When the value of the collateral, less estimated costs to sell, is less than the principal balance of the loan, a specific reserve is established. Costs to sell represent transaction costs and are not included as a component of the asset's fair value. If the process uses independent appraisals and other market-based information, they are classified as Level 2. If the process requires significant input based on management's knowledge of and judgment about current market conditions, specific issues relating to the collateral and other matters, they are classified as Level 3.

**Other property owned:** Represents the fair value and related losses of foreclosed assets that were measured at fair value based on the collateral value, which is generally determined using appraisals, or other indications based on sales of similar properties. Costs to sell represent transaction costs and are not included as a component of the asset's fair value. If the process uses independent appraisals and other market-based information, they are classified as Level 2. If the process requires significant input based on management's knowledge of and judgment about current market conditions, specific issues relating to the property and other matters, they are classified as Level 3.

## NOTE 7: SUBSEQUENT EVENTS

We have evaluated subsequent events through August 7, 2017, which is the date the Consolidated Financial Statements were available to be issued. There have been no material subsequent events that would require recognition in our Quarterly Report or disclosure in the Notes to Consolidated Financial Statements.