

TEXAS FARM CREDIT SERVICES

2023 Quarterly Report

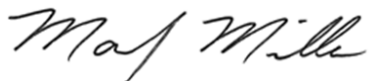


For the Quarter Ended September 30, 2023

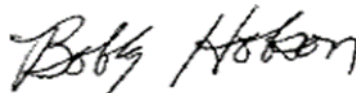
REPORT OF MANAGEMENT

The consolidated financial statements of Texas Farm Credit Services (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.

The undersigned certify that we have reviewed this report, that it has been 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 our knowledge and belief.



Mark Miller, Chief Executive Officer
November 3, 2023



Bobby Hobson, Chairman, Board of Directors
November 3, 2023



Lane Pepper, Chief Financial Officer
November 3, 2023

TEXAS FARM CREDIT SERVICES MANAGEMENT'S DISCUSSION AND ANALYSIS

The following commentary reviews the financial performance of the Texas Farm Credit Services (ACA), referred to as the Association, for the quarter ended September 30, 2023. These comments should be read in conjunction with the accompanying financial statements and the December 31, 2022, Annual Report to Stockholders.

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

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

Loan Portfolio

Total loans outstanding at September 30, 2023, including nonaccrual loans and sales contracts, were \$2,262,819,907 compared to \$2,218,378,245 at December 31, 2022, reflecting an increase of 2.0 percent. Nonaccrual loans as a percentage of total loans outstanding were 0.7 percent at September 30, 2023, compared to 0.5 percent at December 31, 2022.

The Association recorded \$10,509 in recoveries and \$0 in charge-offs for the quarter ended September 30, 2023, and \$0 in recoveries and \$0 in charge-offs for the same period in 2022. The Association's allowance for loan losses was 0.1 percent and 0.1 percent of total loans outstanding as of September 30, 2023, and December 31, 2022, respectively.

Risk Exposure

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

	High-Risk Assets			
	September 30, 2023		December 31, 2022	
	Amount	%	Amount	%
Nonaccrual	\$ 15,649,916	100.0%	\$ 10,503,174	86.8%
90 days past due and still accruing interest	49	0.0%	1,598,991	13.2%
Total	\$ 15,649,965	100.0%	\$ 12,102,165	100.0%

Results of Operations

The Association had net income of \$12,179,532 and \$36,449,233 for the three and nine months ended September 30, 2023, as compared to net income of \$12,128,632 and \$35,728,525 for the same period in 2022, reflecting an increase of 0.4 percent and 2.0 percent. Net interest income was \$15,025,301 and \$44,712,074 for the three and nine months ended September 30, 2023, compared to \$14,115,207 and \$41,654,967 for the same period in 2022.

	Nine Months Ended			
	September 30, 2023		September 30, 2022	
	Average Balance	Interest	Average Balance	Interest
Loans	\$ 2,252,695,648	\$ 94,855,173	\$ 2,138,125,650	\$ 72,933,796
Investments	374,644	20,224	602,783	27,296
Total interest-earning assets	2,253,070,292	94,875,397	2,138,728,433	72,961,092
Interest-bearing liabilities	2,031,656,726	50,163,323	1,928,306,350	31,306,125
Impact of capital	\$ 221,413,566		\$ 210,422,083	
Net interest income		\$ 44,712,074		\$ 41,654,967

	2023	2022
	Average Yield	Average Yield
Yield on loans	5.63%	4.56%
Yield on investments	7.22%	6.05%
Total yield on interest-earning assets	5.63%	4.56%
Cost of interest-bearing liabilities	3.30%	2.17%
Interest rate spread	2.33%	2.39%
Net interest income as a percentage of average earning assets	2.65%	2.60%

Nine months ended:			
September 30, 2023 vs. September 30, 2022			
Increase (decrease) due to			
	Volume	Rate	Total
Interest income - loans	\$ 3,908,073	\$ 18,013,304	\$ 21,921,377
Interest income - investments	(10,331)	3,259	(7,072)
Total interest income	3,897,742	18,016,563	21,914,305
Interest expense	1,677,883	17,179,315	18,857,198
Net interest income	\$ 2,219,859	\$ 837,248	\$ 3,057,107

Interest income for the three and nine months ended September 30, 2023, increased by \$6,528,134 and \$21,914,305, or 24.7 percent and 30.0 percent respectively, from the same period of 2022, primarily due to increases in yields on earning assets and an increase in average loan volume. Interest expense for the three and nine months ended September 30, 2023, increased by \$5,618,040 and \$18,857,198, or 45.5 percent and 60.2 percent, from the same period of 2022 due to an increase in funding rates as well as an increase in average debt volume. Average loan volume, including investments, for the nine months ended September 30, 2023, was \$2,253,070,292, compared to \$2,138,728,433 for the same period of 2022. The average net interest rate spread on the loan portfolio for the nine months ended September 30, 2023, was 2.33 percent, compared to 2.39 percent for the same period of 2022.

Noninterest income for the nine months ended September 30, 2023, decreased by \$3,463,552, or 17.8 percent, compared to the same period of 2022, primarily due to a decrease in loan fees and a reduced accrual of direct note patronage based on guidance provided by the Bank. Noninterest expense for the nine months ended September 30, 2023, increased by \$1,040,180, or 4.1 percent, compared to the same period of 2022, primarily due to an increase in salaries and employee benefits and other miscellaneous expenses.

The Association's annualized return on average assets for the nine months ended September 30, 2023, was 2.08 percent compared to 2.16 percent for the same period in 2022. The Association's annualized return on average equity for the nine months ended September 30, 2023, was 17.50 percent, compared to 18.89 percent for the same period in 2022.

Liquidity and Funding Sources

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

	September 30, 2023	December 31, 2022
Note payable to the Bank	\$ 2,031,721,066	\$ 1,991,062,303
Accrued interest on note payable	5,883,006	4,876,398
Total	\$ 2,037,604,072	\$ 1,995,938,701

The Association operates under a general financing agreement (GFA) with the Bank. The current GFA is effective through September 30, 2026. The primary source of liquidity and funding for the Association is a direct loan from the Bank. The outstanding balance of \$2,031,721,066 as of September 30, 2023, is recorded as a liability on the Association's Consolidated Balance Sheet. The note carried a weighted average interest rate of 3.30 percent at September 30, 2023. The indebtedness is collateralized by a pledge of substantially all of the Association's assets to the Bank and is governed by the general financing agreement. The increase in note payable to the Bank and related accrued interest payable since December 31, 2022, is due to the Association's increase in debt related to its match funding of new loans. The Association's own funds, which represent the amount of the Association's loan portfolio funded by the Association's equity, were \$228,354,507 at September 30, 2023. The maximum amount the Association may borrow from the Bank

as of September 30, 2023, was \$2,274,941,800 as defined by the general financing agreement. The indebtedness continues in effect until the expiration date of the general financing agreement, unless sooner terminated by the Bank upon the occurrence of an event of default, or by the Association, in the event of a breach of this agreement by the Bank, upon giving the Bank 30 calendar days' prior written notice, or in all other circumstances, upon giving the Bank 120 days' prior written notice.

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 in 2023. As borrower payments are received, they are applied to the Association's note payable to the Bank.

Capital Resources

The Association's capital position increased by \$34,660,463 at September 30, 2023, compared to December 31, 2022. The Association's liabilities as a multiple of members' equity was 6.93:1 as of September 30, 2023, compared to 7.75:1 as of December 31, 2022.

Farm Credit Administration regulations require the Association to maintain minimums for various regulatory capital ratios. New regulations became effective January 1, 2017, which replaced the previously required core surplus and total surplus ratios with common equity tier 1, tier 1 capital, and total capital risk-based capital ratios. The new regulations also added tier 1 leverage and unallocated retained earnings and equivalents (UREE) ratios. The permanent capital ratio continues to remain in effect, with some modifications to align with the new regulations. As of September 30, 2023, the Association exceeded all regulatory capital requirements.

Significant Recent Accounting Pronouncements

Refer to Note 1 – "Organization and Significant Accounting Policies" in this quarterly report for disclosures of recent accounting pronouncements which may impact the Association's consolidated financial position and results of operations and for critical accounting policies.

Relationship With the Farm Credit Bank of Texas

The Association's financial condition may be impacted by factors that affect the Bank. The financial condition and results of operations of the Bank may materially affect the stockholder's investment in the Association. The Management's Discussion and Analysis and Notes to Financial Statements contained in the 2022 Annual Report of Association more fully describe the Association's relationship with the Bank.

The annual and quarterly stockholder reports of the Bank can be found at the Bank's website at www.farmcreditbank.com.

The Association's quarterly stockholder reports are also available free of charge, upon request. These reports can be obtained by writing to Association, 545 South Hwy. 77, Robstown, TX 78380 or calling (361) 387-8563. The annual and quarterly stockholder reports for the Association are also available on its website at www.texasfarmcredit.com. Copies of the Association's quarterly stockholder reports can also be requested by e-mailing lpepper@texasfarmcredit.com.

TEXAS FARM CREDIT SERVICES
CONSOLIDATED BALANCE SHEET

	September 30, 2023 (unaudited)	December 31, 2022
<u>ASSETS</u>		
Cash	\$ 23,438	\$ 26,159
Investments	321,486	424,737
Loans	2,262,819,907	2,218,378,245
Less: allowance for loan losses	2,410,387	3,051,962
Net loans	2,260,409,520	2,215,326,283
Accrued interest receivable	23,204,599	18,151,458
Investment in and receivable from the Farm Credit Bank of Texas:		
Capital stock	38,497,285	38,519,130
Other	9,933,760	563,151
Deferred taxes, net	69,386	163,570
Premises and equipment, net	18,260,272	17,895,655
Other assets	5,088,572	3,363,181
Total assets	\$ 2,355,808,318	\$ 2,294,433,324
<u>LIABILITIES</u>		
Note payable to the Farm Credit Bank of Texas	\$ 2,031,721,066	\$ 1,991,062,303
Advance conditional payments	4,584,047	2,136,930
Accrued interest payable	5,883,006	4,876,398
Drafts outstanding	372,940	150,749
Dividends payable	-	20,539,000
Other liabilities	16,284,316	13,365,464
Total liabilities	2,058,845,375	2,032,130,844
<u>MEMBERS' EQUITY</u>		
Capital stock and participation certificates	4,602,750	4,580,185
Additional paid-in capital	47,596,495	47,596,495
Allocated retained earnings	53,219,859	53,219,859
Unallocated retained earnings	190,739,737	156,044,338
Accumulated other comprehensive income (loss)	804,102	861,603
Total members' equity	296,962,943	262,302,480
Total liabilities and members' equity	\$ 2,355,808,318	\$ 2,294,433,324

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

TEXAS FARM CREDIT SERVICES

CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME

(unaudited)

	Quarter Ended		Nine Months Ended	
	September 30,		September 30,	
	2023	2022	2023	2022
<u>INTEREST INCOME</u>				
Loans	\$ 32,987,839	\$ 26,457,306	\$ 94,855,173	\$ 72,933,796
Investments	6,295	8,694	20,224	27,296
Total interest income	<u>32,994,134</u>	<u>26,466,000</u>	<u>94,875,397</u>	<u>72,961,092</u>
<u>INTEREST EXPENSE</u>				
Note payable to the Farm Credit Bank of Texas	17,949,611	12,346,650	50,141,248	31,301,874
Advance conditional payments	19,222	4,143	22,075	4,251
Total interest expense	<u>17,968,833</u>	<u>12,350,793</u>	<u>50,163,323</u>	<u>31,306,125</u>
Net interest income	<u>15,025,301</u>	<u>14,115,207</u>	<u>44,712,074</u>	<u>41,654,967</u>
Reversal of provision for loan losses and other property owned	<u>(2,280,842)</u>	<u>(255,096)</u>	<u>(2,474,569)</u>	<u>(253,120)</u>
Net interest income after provision for loan losses	<u>17,306,143</u>	<u>14,370,303</u>	<u>47,186,643</u>	<u>41,908,087</u>
<u>NONINTEREST INCOME</u>				
Income from the Farm Credit Bank of Texas:				
Patronage income	777,533	4,073,004	9,108,413	11,922,827
Loan fees	1,180,069	1,479,439	2,693,336	3,533,211
Financially related services income	850,552	638,682	3,505,002	3,317,291
Gain (loss) on sale of premises and equipment, net	90,860	196,864	308,967	356,842
Other noninterest income	33,015	102,240	414,714	363,813
Total noninterest income	<u>2,932,029</u>	<u>6,490,229</u>	<u>16,030,432</u>	<u>19,493,984</u>
<u>NONINTEREST EXPENSES</u>				
Salaries and employee benefits	4,405,627	4,917,919	14,741,338	13,784,554
Directors' expense	237,501	236,978	542,564	441,643
Purchased services	183,734	345,502	643,280	1,011,804
Travel	442,554	461,999	1,245,957	1,186,966
Occupancy and equipment	550,650	569,731	2,687,596	2,621,332
Communications	94,925	123,841	336,668	348,827
Advertising	76,707	87,627	260,603	231,677
Public and member relations	159,662	284,160	800,422	846,031
Supervisory and exam expense	141,681	-	425,043	387,301
Insurance fund premiums	895,504	953,418	2,619,549	2,743,683
Other noninterest expense	737,546	679,106	2,328,688	1,987,710
Total noninterest expenses	<u>7,926,091</u>	<u>8,660,281</u>	<u>26,631,708</u>	<u>25,591,528</u>
Income before income taxes	<u>12,312,081</u>	<u>12,200,251</u>	<u>36,585,367</u>	<u>35,810,543</u>
Provision for (benefit from) income taxes	<u>132,549</u>	<u>71,619</u>	<u>136,134</u>	<u>82,018</u>
NET INCOME	<u>12,179,532</u>	<u>12,128,632</u>	<u>36,449,233</u>	<u>35,728,525</u>
Other comprehensive income:				
Change in postretirement benefit plans	<u>(19,167)</u>	<u>(5,430)</u>	<u>(57,501)</u>	<u>(16,290)</u>
COMPREHENSIVE INCOME	<u>\$ 12,160,365</u>	<u>\$ 12,123,202</u>	<u>\$ 36,391,732</u>	<u>\$ 35,712,235</u>

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

TEXAS FARM CREDIT SERVICES

CONSOLIDATED STATEMENT OF CHANGES IN MEMBERS' EQUITY

(unaudited)

	Capital Stock/ Participation Certificates	Additional Paid-in-Capital	Retained Earnings		Accumulated Other Comprehensive Income (Loss)	Total Members' Equity
			Allocated	Unallocated		
Balance at December 31, 2021	\$ 4,364,895	\$ 47,596,495	\$ 54,627,414	\$ 129,133,773	\$ (315,716)	\$ 235,406,861
Comprehensive income	-	-	-	35,728,525	(16,290)	35,712,235
Capital stock/participation certificates and allocated retained earnings issued	447,180	-	-	-	-	447,180
Capital stock/participation certificates and allocated retained earnings retired	(234,845)	-	-	-	-	(234,845)
Patronage refunds:						
Cash	-	-	-	630,865	-	630,865
Capital stock/participation certificates and allocated retained earnings	-	-	(109,463)	-	-	(109,463)
Balance at September 30, 2022	\$ 4,577,230	\$ 47,596,495	\$ 54,517,951	\$ 165,493,163	\$ (332,006)	\$ 271,852,833
Balance at December 31, 2022	\$ 4,580,185	\$ 47,596,495	\$ 53,219,859	\$ 156,044,338	\$ 861,603	\$ 262,302,480
Comprehensive income	-	-	-	36,449,233	(57,501)	36,391,732
Capital stock/participation certificates and allocated retained earnings issued	221,960	-	-	-	-	221,960
Capital stock/participation certificates and allocated retained earnings retired	(199,395)	-	-	-	-	(199,395)
Adjustment due to CECL adoption	-	-	-	(1,786,948)	-	(1,786,948)
Patronage refunds:						
Cash	-	-	-	33,114	-	33,114
Balance at September 30, 2023	\$ 4,602,750	\$ 47,596,495	\$ 53,219,859	\$ 190,739,737	\$ 804,102	\$ 296,962,943

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

TEXAS FARM CREDIT SERVICES
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

Unaudited

NOTE 1 — ORGANIZATION AND SIGNIFICANT ACCOUNTING POLICIES:

The Texas Farm Credit Services (Agricultural Credit Association), referred to as the Association, is a member-owned cooperative that provides credit and credit-related services to or for the benefit of eligible borrowers/stockholders for qualified agricultural purposes. The Association serves the counties of Anderson, Angelina, Aransas, Atascosa, Austin, Bandera, Bee, Bexar, Bowie, Brooks, Cameron, Camp, Cass, Chambers, Cherokee, Collin, Cook, Dallas, Delta, Denton, DeWitt, Dimmit, Duval, Edwards, Fannin, Fayette, Franklin, Freestone, Frio, Goliad, Gonzales, Grayson, Gregg, Guadalupe, Hardin, Harrison, Henderson, Hidalgo, Hopkins, Houston, Hunt, Jasper, Jefferson, Jim Hogg, Jim Wells, Karnes, Kaufman, Kenedy, Kerr, Kinney, Kleberg, Lamar, LaSalle, Lavaca, Leon, Liberty, Limestone, Live Oak, Marion, Maverick, McMullen, Medina, Montgomery, Morris, Nacogdoches, Newton, Nueces, Orange, Panola, Polk, Rains, Real, Red River, Rockwall, Rusk, Sabine, San Augustine, San Jacinto, San Patricio, Shelby, Smith, Starr, Titus, Trinity, Tyler, Upshur, Uvalde, Val Verde, Van Zandt, Walker, Waller, Washington, Webb, Willacy, Wilson, Wood, Zapata, and Zavala, parts of Refugio, and the lower half of Lee in the State of Texas. The Association is a lending association of the Farm Credit System (the System), which was established by Acts of Congress to meet the needs of American agriculture.

The accompanying unaudited financial statements have been prepared in accordance with accounting principles generally accepted in the U.S. (GAAP) for interim financial information. Accordingly, they do not include all of the disclosures required by GAAP for annual financial statements and should be read in conjunction with the audited financial statements as of and for the year ended December 31, 2022, as contained in the 2022 Annual Report to Stockholders.

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 and conform with GAAP, except for the exclusion of a statement of cash flows. GAAP require a business enterprise that provides a set of financial statements reporting both financial position and results of operations to also provide a statement of cash flows for each period for which results of operations are provided. In regulations issued by FCA, associations have the option to exclude statements of cash flows in interim financial statements. Therefore, the Association has elected not to include a statement of cash flows in these consolidated financial statements. These interim financial statements should be read in conjunction with the audited financial statements as of and for the year ended December 31, 2022, as contained in the 2022 Annual Report to Stockholders. The preparation of financial statements in accordance with GAAP requires management to make estimates and assumptions that affect the amounts reported in the financial statements and accompanying notes. Actual results could differ from those estimates. The results of operations for interim periods are not necessarily indicative of the results to be expected for the full year ending December 31, 2023. Descriptions of the significant accounting policies are included in the 2022 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.

Recently Adopted Accounting Pronouncements

On January 1, 2023, the Association adopted the Financial Accounting Standards Board (FASB) guidance entitled “Measurement of Credit Losses on Financial Instruments” and other subsequently issued accounting standards updates related to credit losses. This guidance replaced the current incurred loss impairment methodology with a single allowance framework that estimates the current expected credit losses (CECL) over the remaining contractual life for all financial assets measured at amortized cost and certain off-balance-sheet credit exposures. This guidance is applied on a modified retrospective basis. This framework requires management to consider in its estimate of the allowance for credit losses (ACL) relevant historical events, current conditions and reasonable and supportable forecasts that consider macroeconomic conditions. In addition, the guidance amends existing impairment guidance for held-to-maturity and available-for-sale investments to incorporate an allowance for credit losses related to these securities, which will allow for the reversal of credit impairments in the event that the credit of an issuer improves.

Also adopted effective January 1, 2023, was the updated guidance entitled “Financial Instruments – Credit Losses: Troubled Debt Restructurings and Vintage Disclosure.” This guidance requires the creditor to determine whether a modification results in a new loan or a continuation of an existing loan, among other disclosures specific to modifications with borrowers that are experiencing financial difficulties. The update eliminated the accounting guidance for troubled debt restructurings by creditors. The update also requires disclosure of current period gross write-offs by year of origination for financing receivables and net investments in leases on a prospective basis.

The following table presents the impact to the allowance for credit losses and retained earnings upon adoption of this guidance on January 1, 2023:

	<u>December 31, 2022</u>	<u>CECL adoption impact</u>	<u>January 1, 2023</u>
Assets:			
Allowance for credit losses on loans	\$ (3,051,962)	\$ (1,735,440)	\$ (4,787,402)
Deferred tax assets	\$ 163,570	\$ (81,212)	\$ 82,358
Liabilities:			
Allowance for credit losses on unfunded commitments	\$ (203,392)	\$ 29,704	\$ (173,688)
Retained earnings:			
Unallocated retained earnings, net of tax	\$ 156,044,338	\$ (1,786,948)	\$ 154,257,390

Investments

The Association's investments include mortgage-backed securities issued by Federal Agricultural Mortgage Corporation (Farmer Mac) for which the Association has the intent and ability to hold to maturity and which are consequently classified as held-to-maturity. As more fully described in the 2022 Annual Report, the Association may hold additional investments in accordance with other investment programs approved by the FCA. These programs allow the Association to make investments that further the mission to support rural America.

Upon adoption of CECL guidance, the investments held-to-maturity are presented net of an allowance for credit losses on investments. The guidance also amended the previous other-than-temporary impairment (OTTI) model for investments available-for-sale to incorporate an allowance for credit losses.

Impairment may result from credit deterioration of the issuer or collateral underlying the security. In performing an assessment of whether any decline in fair value is due to a credit loss, all relevant information is considered at the individual security level. For mortgage-backed and asset-backed securities, performance indicators considered relate to the underlying assets include default rates, delinquency rates, percentage of nonperforming assets, debt-to-collateral ratios, third-party guarantees, current levels of subordination, vintage, geographic concentration, analyst reports and forecasts, credit ratings and other market data.

With respect to certain classes of debt securities, primarily U.S. Treasuries and government guaranteed agency securities, management considers the history of credit losses, current conditions and reasonable and supportable forecasts, which may indicate that the expectation that nonpayment of the amortized cost basis is or continues to be zero, even if the U.S. government were to technically default. Therefore, for those securities, System associations do not record expected credit losses.

Available-for-sale debt securities in unrealized loss positions are evaluated for impairment related to credit losses at least quarterly. For available-for-sale debt securities, a decline in fair value due to estimated credit loss results in recording an allowance for credit losses to the extent the fair value is less than the amortized cost basis. Declines in fair value that have not been recorded through an allowance for credit losses, such as declines due to changes in market interest rates, are recorded through other comprehensive income, net of applicable taxes.

In assessing whether a credit loss exists for held-to-maturity investments, the present value of cash flows expected to be collected from the security is compared to the amortized cost basis of the security. If the present value of cash flows expected to be collected is less than the amortized cost basis for the security, a credit loss exists and an allowance for credit losses is recorded, limited to the amount the fair value is less than amortized cost basis.

If the intention is to sell a debt security or it is more likely than not to be required to sell the security before recovery of its amortized cost basis, the debt security is written down to its fair value and the write down is charged against the allowance for credit losses with any incremental impairment reported in earnings.

To the extent that debt securities in the held-to-maturity portfolio share common risk characteristics, estimated expected credit losses are calculated in a manner like that used for loans held for investment. That is, for pools of such securities with common risk characteristics, the historical lifetime probability of default and severity of loss in the event of default is derived or obtained from external sources and adjusted for the expected effects of reasonable and supportable forecasts over the expected lives of the securities on those historical credit losses.

Expected credit loss on each security in the held-to-maturity portfolio that do not share common risk characteristics with any of the pools of debt securities is individually measured based on net realizable value, or the difference between the discounted value of the expected future cash flows, based on the original effective interest rate, and the recorded amortized cost basis of the security.

Loans and Allowance for Credit Losses

Loans are generally carried at their principal amount outstanding adjusted for charge-offs, deferred loan fees or costs, and valuation adjustments relating to hedging activities. Loan origination fees and direct loan origination costs are netted and capitalized and the net fee or cost is amortized over the average life of the related loan as an adjustment to interest income. Loan prepayment fees are reported in interest income. Interest on loans is accrued and credited to interest income based on the daily principal amount outstanding.

Nonaccrual Loans

Nonaccrual loans are loans for which there is reasonable doubt that all principal and interest will be collected according to the original contractual terms and are generally considered substandard or doubtful, which is in accordance with the loan rating model, as described below. A loan is considered contractually past due when any principal repayment or interest payment required by the loan instrument is not received on or before the due date. A loan shall remain contractually past due until it is modified or until the entire amount past due, including principal, accrued interest, and penalty interest incurred as the result of past due status, is collected or otherwise discharged in full.

Consistent with prior practice, loans are generally placed in nonaccrual status when principal or interest is delinquent for 90 days (unless adequately secured and in the process of collection), circumstances indicate that collection of principal and interest is in doubt or legal action, including foreclosure or other forms of collateral conveyance, has been initiated to collect the outstanding principal and interest. At the time a loan is placed in nonaccrual status, accrued interest that is considered uncollectible is reversed (if accrued in the current year) or charged against the allowance for loan losses (if accrued in prior years). Loans are charged-off at the time they are determined to be uncollectible.

When loans are in nonaccrual status, interest payments received in cash are generally recognized as interest income if the collectability of the loan principal is fully expected and certain other criteria are met. Otherwise, payments received on nonaccrual loans are applied against the recorded investment in the loan asset. Nonaccrual loans are returned to accrual status if all contractual principal and interest is current, the borrower is fully expected to fulfill the contractual repayments terms and after remaining current as to principal and interest for a sustained period or have a recent repayment pattern demonstrating future repayment capacity to make on-time payments. If previously unrecognized interest income exists at the time the loan is transferred to accrual status, cash received at the time of or subsequent to the transfer should first be recorded as interest income until such time as the recorded balance equals the contractual indebtedness of the borrower.

Accrued interest receivable

The Association elected to continue classifying accrued interest on loans and investment securities in accrued interest receivable and not as part of loans or investments on the Consolidated Balance Sheet. The Association also elected to not estimate an allowance on interest receivable balances because the nonaccrual policies in place provide for the accrual of interest to cease on a timely basis when all contractual amounts are not expected.

Loan Modifications to Borrowers Experiencing Financial Difficulty

Loan modifications may be granted to borrowers experiencing financial difficulty. Modifications can be in the form of one or a combination of principal forgiveness, interest rate reduction, other-than-insignificant payment delay or a term extension. Covenant waivers and modifications of contingent acceleration clauses are not considered term extensions.

Collateral dependent loans

Collateral dependent loans are loans secured by collateral, including but not limited to agricultural real estate, crop inventory, equipment and livestock. CECL requires the Association to measure the expected credit losses based on fair value of the collateral at the reporting date when the Association determines that foreclosure is probable. Additionally, CECL allows a fair value practical expedient as a measurement approach for loans when the repayment is expected to be provided substantially through the operation or sale of the collateral when the borrower is experiencing financial difficulties. Under the practical expedient measurement approach, the expected credit losses is based on the difference between the fair value of the collateral less estimated costs to sell and the amortized cost basis of the loan.

Allowance for Credit Losses

Effective January 1, 2023, the allowance for credit losses (ACL) represents the estimated current expected credit losses over the remaining contractual life of financial assets measured at amortized cost and certain off-balance sheet credit exposures. The ACL takes into consideration relevant information about past events, current conditions and reasonable and supportable macroeconomic forecasts of future conditions. The contractual term excludes expected extensions, renewals and modifications unless the extension or renewal options are not unconditionally cancellable. The ACL comprises:

- the allowance for credit losses on loans (ACLL)
- the allowance for credit losses on unfunded commitments, which is presented on the Consolidated Balance Sheet in other liabilities, and

- the allowance for credit losses on investment securities, which covers held-to-maturity and available-for-sale securities and is recognized within each investment securities classification on the Consolidated Balance Sheet.

Determining the appropriateness of the allowance is complex and requires judgment by management about the effect of matters that are inherently uncertain. Subsequent evaluations of the loan portfolio, considering macroeconomic conditions, forecasts and other factors prevailing at the time, may result in significant changes in the ACL in those future periods.

Methodology for Allowance for Credit Losses on Loans

The ACLL represents management's estimate of credit losses over the remaining expected life of loans. Loans are evaluated on the amortized cost basis, including premiums, discounts and fair value hedge accounting adjustments.

The Association employs a disciplined process and methodology to establish its ACLL that has two basic components: first, an asset-specific component involving individual loans that do not share risk characteristics with other loans and the measurement of expected credit losses for such individual loans; and second, a pooled component for estimated expected credit losses for pools of loans that share similar risk characteristics.

Asset-specific loans are generally collateral-dependent loans (including those loans for which foreclosure is probable) and nonaccrual loans. For an asset-specific loan, expected credit losses are measured as the difference between the amortized cost basis in the loan and the present value of expected future cash flows discounted at the loan's effective interest rate except that, for collateral-dependent loans, credit loss is measured as the difference between the amortized cost basis in the loan and the fair value of the underlying collateral. The fair value of the collateral is adjusted for the estimated cost to sell if repayment or satisfaction of a loan is dependent on the sale (rather than only on the operation) of the collateral. In accordance with the Association's appraisal policy, the fair value of collateral-dependent loans is based upon independent third-party appraisals. When an updated appraisal or collateral valuation is received, management reassesses the need for adjustments to the loan's expected credit loss measurements and, where appropriate, records an adjustment. If the calculated expected credit loss is determined to be permanent, fixed or non-recoverable, the credit loss portion of the loan will be charged off against the allowance for credit losses.

In estimating the component of the ACLL that share common risk characteristics, loans are evaluated collectively and segregated into loan pools considering the risk associated with the specific pool. Relevant risk characteristics include loan type, commodity, credit quality rating, delinquency category or business segment or a combination of these classes. The allowance is determined based on a quantitative calculation of the expected life-of-loan loss percentage for each loan category by considering the probability of default, based on the migration of loans from performing to loss by credit quality rating or delinquency buckets using historical life-of-loan analysis periods for loan types, and the severity of loss, based on the aggregate net lifetime losses incurred per loan pool.

The component of the ACLL also considers factors for each loan pool to adjust for differences between the historical period used to calculate historical default and loss severity rates and expected conditions over the remaining lives of the loans in the portfolio related to:

- Lending policies and procedures;
- National, regional and local economic business conditions and developments that affect the collectability of the portfolio, including the condition of various markets;
- Nature of the loan portfolio, including the terms of the loans;
- Experience, ability and depth of the lending management and other relevant staff;
- Volume and severity of past due and adversely classified or graded loans and the volume of nonaccrual loans;
- Quality of the loan review and process;
- Value of underlying collateral for collateral-dependent loans;
- Existence and effect of any concentrations of credit and changes in the level of such concentrations; and
- Effect of external factors such as competition and legal and regulatory requirements on the level of estimated credit losses in the existing portfolio.

The Association uses multiple scenarios over a reasonable and supportable forecast period of two years. Subsequent to the forecast period, the Association reverts to long run historical loss experience beyond the two years on a straight-line basis over a one year reversion period to inform the estimate of losses for the remaining contractual life of the loan portfolio.

The economic forecasts incorporate numerous macroeconomic variables, some of which include unemployment rates, real gross domestic product levels and corporate bond spreads. Also considered are loan and borrower characteristics, such as internal risk ratings, delinquency status, collateral type, and the remaining term of the loan, adjusted for expected prepayments.

In addition to the quantitative calculation, the Association considers the imprecision inherent in the process and methodology, emerging risk assessments and other subjective factors, which may lead to a management adjustment to the modeled ACLL results. Expected credit loss estimates also include consideration of expected cash recoveries on loans previously charged-off or expected recoveries on collateral dependent loans where recovery is expected through sale of the collateral. The economic forecasts are updated on a quarterly basis.

Prior to January 1, 2023, the allowance for loan losses was maintained at a level considered adequate to provide for probable losses existing in and inherent in the loan portfolio. The allowance was based on a periodic evaluation of the loan portfolio in which numerous factors are considered, including economic conditions, collateral values, borrowers' financial conditions, loan portfolio composition and prior loan loss experience. The allowance for loan losses encompassed various judgments, evaluations and appraisals with respect to the loans and their underlying collateral that, by their nature, contain elements of uncertainty and imprecision. Changes in the agricultural economy and their impact on borrower repayment capacity would cause these various judgments, evaluations and appraisals to change over time. Management considered a number of factors in determining and supporting the levels of the allowances for loan losses, which include, but are not limited to, the concentration of lending in agriculture, combined with uncertainties associated with farmland values, commodity prices, exports, government assistance programs, regional economic effects and weather-related influences.

Allowance for Credit Losses on Unfunded Commitments

The Association evaluates the need for an allowance for credit losses on unfunded commitments under CECL and, if required, an amount is recognized and included in other liabilities on the Combined Statement of Condition. The amount of expected losses is determined by calculating a commitment usage factor over the contractual period for exposures that are not unconditionally cancellable by the Association and applying the loss factors used in the ACLL methodology to the results of the usage calculation. No allowance for credit losses are recorded for commitments that are unconditionally cancellable.

NOTE 2 — INVESTMENTS:

The Association holds Farmer Mac agricultural mortgage-backed securities. The following is a summary of these holdings:

	September 30, 2023				
	Amortized Cost	Gross Unrealized Losses	Fair Value	Weighted Average Yield	Weighted Average Life
Agricultural mortgage-backed securities	\$ 321,486	\$ (14,554)	\$ 306,932	6.13%	4.01 Years
	December 31, 2022				
	Amortized Cost	Gross Unrealized Losses	Fair Value	Weighted Average Yield	Weighted Average Life
Agricultural mortgage-backed securities	\$ 424,737	\$ (16,159)	\$ 408,578	5.80%	4.64 Years

NOTE 3 — LOANS AND ALLOWANCE FOR LOAN LOSSES:

A summary of loans follows:

Loan Type	September 30,	December 31,
	2023	2022
	Amount	Amount
Production agriculture:		
Real estate mortgage	\$ 1,841,079,805	\$ 1,801,949,287
Production and intermediate-term	241,061,415	257,966,403
Agribusiness:		
Processing and marketing	76,604,998	69,301,464
Farm-related business	40,922,001	36,011,762
Loans to cooperatives	19,446,517	22,640,041
Communication	22,484,104	16,267,788
Water and waste-water	8,249,048	7,073,081
Agricultural export finance	6,030,210	3,440,131
Energy	5,171,524	1,858,635
Rural residential real estate	1,019,850	1,070,269
Mission-related investments	750,435	799,384
Total	\$ 2,262,819,907	\$ 2,218,378,245

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 at September 30, 2023:

	Other Farm Credit Institutions		Non-Farm Credit Institutions		Total	
	Participations Purchased	Participations Sold	Participations Purchased	Participations Sold	Participations Purchased	Participations Sold
	Real estate mortgage	\$ 61,116,574	\$ 85,939,945	\$ 12,213,411	\$ -	\$ 73,329,985
Production and intermediate-term	28,961,812	12,191,017	-	-	28,961,812	12,191,017
Agribusiness	82,706,096	10,145,274	-	-	82,706,096	10,145,274
Communication	22,484,104	-	-	-	22,484,104	-
Water and waste-water	8,249,048	-	-	-	8,249,048	-
Agricultural export finance	6,030,210	-	-	-	6,030,210	-
Energy	5,171,524	-	-	-	5,171,524	-
Total	\$ 214,719,368	\$ 108,276,236	\$ 12,213,411	\$ -	\$ 226,932,779	\$ 108,276,236

The Association is authorized under the Farm Credit Act to accept “advance conditional payments” (ACPs) from borrowers. To the extent the borrower’s access to such ACPs is restricted and the legal right of setoff exists, the ACPs are netted against the borrower’s related loan balance. Unrestricted advance conditional payments are included in other liabilities. ACPs are not insured, and interest is generally paid by the Association on such balances. Balances of ACPs were \$4,584,047 and \$2,136,930 at September 30, 2023, and December 31, 2022, respectively.

Credit Quality

Credit risk arises from the potential inability of an obligor to meet its payment obligation and exists in our outstanding loans, letters of credit and unfunded loan commitments. The Association manages credit risk associated with the retail lending activities through an analysis of the credit risk profile of an individual borrower using its own set of underwriting standards and lending policies, approved by its board of directors, which provides direction to its loan officers. The retail credit risk management process begins with an analysis of the borrower’s credit history, repayment capacity, financial position and collateral, which includes an enhanced focus on credit scores for smaller loans. Repayment capacity focuses on the borrower’s ability to repay the loan based on cash flows from operations or other sources of income, including off-farm income. Real estate mortgage loans must be secured by first liens on the real estate (collateral). As required by Farm Credit Administration regulations, associations that make loans on a secured basis must have collateral evaluation policies and procedures. Real estate mortgage loans may be made only in amounts up to 85 percent of the original appraised value of the property taken as security or up to 97 percent of the appraised value if guaranteed by a state, federal, or other governmental agency. The actual loan to appraised value when loans are made is generally lower than the statutory maximum percentage. Loans other than real estate mortgage may be made on a secured or unsecured basis.

The Association uses a two-dimensional risk rating model based on an internally generated combined System risk rating guidance that incorporates a 14-point probability of default rating scale to identify and track the probability of borrower default and a separate scale addressing loss given default. Probability of default is the probability that a borrower will experience a default during the life of the loan. The loss given default is management's estimate as to the anticipated principal loss on a specific loan assuming default occurs during the remaining life of the loan. A default is considered to have occurred if the lender believes the borrower will not be able to pay its obligation in full or the loan is classified nonaccrual. This credit risk rating process incorporates objective and subjective criteria to identify inherent strengths, weaknesses and risks in a particular relationship.

Each of the probability of default categories carries a distinct percentage of default probability. The probability of default rate between one and nine of the acceptable categories is very narrow and would reflect almost no default to a minimal default percentage. The probability of default rate grows more rapidly as a loan moves from acceptable to other assets especially mentioned and grows significantly as a loan moves to a substandard (viable) level. A substandard (non-viable) rating indicates that the probability of default is almost certain. These 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 that if not cured jeopardizes repayment;
- Doubtful — assets exhibit similar weaknesses to substandard assets; however, doubtful assets have additional weaknesses in existing facts, conditions and values that make collection in full highly questionable; and
- Loss — assets are considered uncollectible.

The following table presents credit quality indicators by loan type and the related principal balance as of September 30, 2023:

	Term Loans Amortized Cost by Origination Year						Revolving Loans Amortized Cost Basis	Revolving Loans Converted to Term Loans Amortized Cost	Total
	2023	2022	2021	2020	2019	Prior			
Real estate mortgage									
Acceptable	\$ 190,143,803	\$ 389,865,889	\$ 578,272,295	\$ 287,503,593	\$ 104,167,933	\$ 277,150,623	\$ -	\$ 3,477,731	\$ 1,830,581,867
OAEM	-	-	775,591	846,430	1,474,788	1,495,960	-	-	4,592,769
Substandard/Doubtful	-	-	2,530,314	670,308	258,150	2,446,397	-	-	5,905,169
	<u>190,143,803</u>	<u>389,865,889</u>	<u>581,578,200</u>	<u>289,020,331</u>	<u>105,900,871</u>	<u>281,092,980</u>	<u>-</u>	<u>3,477,731</u>	<u>1,841,079,805</u>
Current period gross charge-offs	-	-	-	-	-	-	-	-	-
Production and intermediate-term									
Acceptable	17,803,503	71,166,212	15,717,460	19,060,761	1,504,870	4,306,679	-	104,145,651	233,705,136
OAEM	3,703,040	11,898	-	-	75,025	38,857	-	673,350	4,502,170
Substandard/Doubtful	1,477,587	290,467	1,075,352	-	-	10,703	-	-	2,854,109
	<u>22,984,130</u>	<u>71,468,577</u>	<u>16,792,812</u>	<u>19,060,761</u>	<u>1,579,895</u>	<u>4,356,239</u>	<u>-</u>	<u>104,819,001</u>	<u>241,061,415</u>
Current period gross charge-offs	-	-	-	-	-	-	-	-	-
Agribusiness									
Acceptable	12,160,422	44,087,962	13,099,056	11,413,659	4,858,051	8,738,429	-	27,171,672	121,529,251
OAEM	-	1,875,259	-	-	-	-	-	1,420,466	3,295,725
Substandard/Doubtful	-	-	-	4,533,639	-	7,614,901	-	-	12,148,540
	<u>12,160,422</u>	<u>45,963,221</u>	<u>13,099,056</u>	<u>15,947,298</u>	<u>4,858,051</u>	<u>16,353,330</u>	<u>-</u>	<u>28,592,138</u>	<u>136,973,516</u>
Current period gross charge-offs	-	-	-	-	-	-	-	-	-
Communications									
Acceptable	8,902,843	-	-	12,395,679	-	-	-	89,409	21,387,931
OAEM	-	-	-	1,096,173	-	-	-	-	1,096,173
Substandard/Doubtful	-	-	-	-	-	-	-	-	-
	<u>8,902,843</u>	<u>-</u>	<u>-</u>	<u>13,491,852</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>89,409</u>	<u>22,484,104</u>
Current period gross charge-offs	-	-	-	-	-	-	-	-	-
Energy									
Acceptable	3,495,468	-	-	-	-	1,340,246	-	-	4,835,714
OAEM	-	-	-	-	-	-	-	-	-
Substandard/Doubtful	-	-	-	-	-	335,810	-	-	335,810
	<u>3,495,468</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>1,676,056</u>	<u>-</u>	<u>-</u>	<u>5,171,524</u>
Current period gross charge-offs	-	-	-	-	-	-	-	-	-
Water/waste disposal									
Acceptable	2,727,757	2,944,480	2,496,810	-	-	-	-	80,001	8,249,048
OAEM	-	-	-	-	-	-	-	-	-
Substandard/Doubtful	-	-	-	-	-	-	-	-	-
	<u>2,727,757</u>	<u>2,944,480</u>	<u>2,496,810</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>80,001</u>	<u>8,249,048</u>
Current period gross charge-offs	-	-	-	-	-	-	-	-	-
Rural residential real estate									
Acceptable	-	-	-	86,076	-	511,975	-	-	598,051
OAEM	-	-	-	-	-	341,137	-	-	341,137
Substandard/Doubtful	-	-	-	-	-	80,662	-	-	80,662
	<u>-</u>	<u>-</u>	<u>-</u>	<u>86,076</u>	<u>-</u>	<u>933,774</u>	<u>-</u>	<u>-</u>	<u>1,019,850</u>
Current period gross charge-offs	-	-	-	-	-	-	-	-	-
Agricultural export finance									
Acceptable	5,587,582	-	-	-	-	-	-	442,628	6,030,210
OAEM	-	-	-	-	-	-	-	-	-
Substandard/Doubtful	-	-	-	-	-	-	-	-	-
	<u>5,587,582</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>442,628</u>	<u>6,030,210</u>
Current period gross charge-offs	-	-	-	-	-	-	-	-	-
Mission-related									
Acceptable	-	-	-	-	-	750,435	-	-	750,435
OAEM	-	-	-	-	-	-	-	-	-
Substandard/Doubtful	-	-	-	-	-	-	-	-	-
	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>750,435</u>	<u>-</u>	<u>-</u>	<u>750,435</u>
Current period gross charge-offs	-	-	-	-	-	-	-	-	-
Total Loans									
Acceptable	240,821,378	508,064,543	609,585,621	330,459,768	110,530,854	292,798,387	-	135,407,092	2,227,667,643
OAEM	3,703,040	1,887,157	775,591	1,942,603	1,549,813	1,875,954	-	2,093,816	13,827,974
Substandard/Doubtful	1,477,587	290,467	3,605,666	5,203,947	258,150	10,488,473	-	-	21,324,290
	<u>\$ 246,002,005</u>	<u>\$ 510,242,167</u>	<u>\$ 613,966,878</u>	<u>\$ 337,606,318</u>	<u>\$ 112,338,817</u>	<u>\$ 305,162,814</u>	<u>\$ -</u>	<u>\$ 137,500,908</u>	<u>\$ 2,262,819,907</u>
Total current period gross charge-offs	<u>\$ -</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ -</u>

The following table shows loans under the Farm Credit Administration Uniform Loan Classification System as a percentage of total loans by loan type:

	September 30, 2023	December 31, 2022
Real estate mortgage		
Acceptable	99.4 %	99.4 %
OAEM	0.3 %	0.2 %
Substandard/doubtful	0.3 %	0.4 %
	100.0 %	100.0 %
Production and intermediate-term		
Acceptable	96.9 %	97.8 %
OAEM	1.9 %	1.3 %
Substandard/doubtful	1.2 %	0.9 %
	100.0 %	100.0 %
Loans to cooperatives		
Acceptable	100.0 %	100.0 %
OAEM	- %	- %
Substandard/doubtful	- %	- %
	100.0 %	100.0 %
Processing and marketing		
Acceptable	95.7 %	92.1 %
OAEM	4.3 %	1.7 %
Substandard/doubtful	- %	6.2 %
	100.0 %	100.0 %
Farm-related business		
Acceptable	70.3 %	63.6 %
OAEM	- %	- %
Substandard/doubtful	29.7 %	36.4 %
	100.0 %	100.0 %
Communication		
Acceptable	95.1 %	100.0 %
OAEM	4.9 %	- %
Substandard/doubtful	- %	- %
	100.0 %	100.0 %
Energy		
Acceptable	93.5 %	76.0 %
OAEM	- %	- %
Substandard/doubtful	6.5 %	24.0 %
	100.0 %	100.0 %
Water and waste water		
Acceptable	100.0 %	100.0 %
OAEM	- %	- %
Substandard/doubtful	- %	- %
	100.0 %	100.0 %
Rural residential real estate		
Acceptable	58.7 %	58.1 %
OAEM	33.4 %	33.6 %
Substandard/doubtful	7.9 %	8.3 %
	100.0 %	100.0 %
Agricultural export finance		
Acceptable	100.0 %	100.0 %
OAEM	- %	- %
Substandard/doubtful	- %	- %
	100.0 %	100.0 %
Mission-related investments		
Acceptable	100.0 %	100.0 %
OAEM	- %	- %
Substandard/doubtful	- %	- %
	100.0 %	100.0 %
Total loans		
Acceptable	98.4 %	98.4 %
OAEM	0.7 %	0.4 %
Substandard/doubtful	0.9 %	1.2 %
	100.0 %	100.0 %

Accrued interest receivable on loans of \$23,198,970 and \$18,146,963 at September 30, 2023, and December 31, 2022, have been excluded from the amortized cost of loans and reported separately in the Consolidated Balance Sheet. The Association wrote off accrued interest receivable of \$226 and \$272,262 during the three months and nine months ended September 30, 2023.

The following table reflects nonperforming assets, which consist of nonaccrual loans, accruing loans 90 days or more delinquent, and other property owned, and related credit quality statistics:

	<u>September 30, 2023</u>	<u>December 31, 2022</u>
Nonaccrual loans:		
Real estate mortgage	\$ 2,226,158	\$ 4,577,106
Production and intermediate-term	939,408	1,174,329
Agribusiness	12,148,540	4,306,286
Energy	335,810	445,453
Total nonaccrual loans	<u>15,649,916</u>	<u>10,503,174</u>
Accruing loans 90 days or more past due:		
Real estate mortgage	-	144,591
Production and intermediate-term	49	31
Agribusiness	-	1,454,369
Total accruing loans 90 days or more past due	<u>49</u>	<u>1,598,991</u>
Other property owned	-	-
Total nonperforming assets	<u>\$ 15,649,965</u>	<u>\$ 12,102,165</u>
Nonaccrual loans as a percentage of total loans	0.69%	0.47%
Nonperforming assets as a percentage of total loans and other property owned	0.69%	0.55%
Nonperforming assets as a percentage of capital	5.27%	4.61%

The following table provides the amortized cost for nonaccrual loans with and without a related allowance for loan losses, as well as, interest income recognized on nonaccrual loans during the period:

	<u>September 30, 2023</u>			<u>Interest Income Recognized</u>	
	<u>Amortized Cost with Allowance</u>	<u>Amortized Cost without Allowance</u>	<u>Total</u>	<u>For the Three Months Ended September 30,</u>	<u>For the Nine Months Ended September 30,</u>
Nonaccrual loans:					
Real estate mortgage	\$ -	\$ 2,226,158	\$ 2,226,158	\$ 35,202	\$ 50,620
Production and intermediate-term	-	939,408	939,408	-	38,393
Agribusiness	-	12,148,540	12,148,540	-	-
Energy and Water/waste disposal	335,810	-	335,810	-	-
Total nonaccrual loans	<u>\$ 335,810</u>	<u>\$ 15,314,106</u>	<u>\$ 15,649,916</u>	<u>\$ 35,202</u>	<u>\$ 89,013</u>

The following tables provide an aging analysis of past due loans at amortized cost by portfolio segment as of:

September 30, 2023	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	Recorded Investment >90 Days and Accruing
Real estate mortgage	\$ 5,610,631	\$ -	\$ 5,610,631	\$ 1,835,469,174	\$ 1,841,079,805	\$ -
Production and intermediate term	865,510	10,752	876,262	240,185,153	241,061,415	49
Processing and marketing	-	-	-	76,604,998	76,604,998	-
Farm-related business	-	-	-	40,922,001	40,922,001	-
Loans to cooperatives	-	-	-	19,446,517	19,446,517	-
Communication	-	-	-	22,484,104	22,484,104	-
Water and waste-water	-	-	-	8,249,048	8,249,048	-
Agricultural export finance	-	-	-	6,030,210	6,030,210	-
Energy	-	-	-	5,171,524	5,171,524	-
Rural residential real estate	97,541	-	97,541	922,309	1,019,850	-
Mission-related investments	-	-	-	750,435	750,435	-
Total	\$ 6,573,682	\$ 10,752	\$ 6,584,434	\$ 2,256,235,473	\$ 2,262,819,907	\$ 49

Prior to the adoption of CECL, the aging analysis of past due loans reported included accrued interest and was as follows:

December 31, 2022	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	Recorded Investment >90 Days and Accruing
Real estate mortgage	\$ 6,483,859	\$ 156,780	\$ 6,640,639	\$ 1,807,972,579	\$ 1,814,613,218	\$ 144,591
Production and intermediate term	619,803	31	619,834	261,172,301	261,792,135	31
Processing and marketing	1,301,882	334,156	1,636,038	67,964,141	69,600,179	-
Farm-related business	-	-	-	36,747,924	36,747,924	-
Loans to cooperatives	-	1,454,368	1,454,368	21,695,143	23,149,511	1,454,369
Communication	-	-	-	16,324,645	16,324,645	-
Water and waste-water	-	-	-	7,080,959	7,080,959	-
Agricultural export finance	-	-	-	3,472,533	3,472,533	-
Energy	-	-	-	1,866,118	1,866,118	-
Rural residential real estate	89,670	-	89,670	984,652	1,074,322	-
Mission-related investments	-	-	-	803,664	803,664	-
Total	\$ 8,495,214	\$ 1,945,335	\$ 10,440,549	\$ 2,226,084,659	\$ 2,236,525,208	\$ 1,598,991

A loan is considered collateral dependent when the borrower is experiencing financial difficulty and repayment is expected to be provided substantially through the sale of the collateral. The collateral dependent loans are primarily real estate mortgage and rural residential real estate loans.

Allowance for Credit Losses

The credit risk rating methodology is a key component of the Association's allowance for credit losses evaluation and is incorporated into the Association's loan underwriting standards. In addition, borrower and commodity concentration lending and leasing limits have been established by the Association to manage credit exposure. The regulatory limit to a single borrower or lessee is 15 percent of the Association's lending and leasing limit base but the Association's boards of directors has established more restrictive lending limits.

Effective January 1, 2023, the Association adopted the CECL accounting guidance as described in Note 1. A summary of changes in the allowance for credit losses by portfolio segment are as follows:

	Real Estate Mortgage	Production and Intermediate- Term	Agribusiness	Communi- cations	Energy	Water and waste water	Rural Residential Real Estate	Agricultural export finance	Mission-related	Total
Allowance for Credit Losses on Loans:										
Balance at June 30, 2023	\$ 1,940,873	\$ 338,610	\$ 2,244,400	\$ 22,480	\$ 109,865	\$ 8,882	\$ 1,105	\$ 6,684	\$ 808	\$ 4,673,707
Recoveries	-	10,509	-	-	-	-	-	-	-	10,509
Provision for credit losses/(Loan loss reversal)	(112,424)	(50,616)	(2,108,487)	(211)	(458)	(748)	(97)	(733)	(55)	(2,273,829)
Balance at September 30, 2023	\$ 1,828,449	\$ 298,503	\$ 135,913	\$ 22,269	\$ 109,407	\$ 8,134	\$ 1,008	\$ 5,951	\$ 753	\$ 2,410,387
Balance at December 31, 2022	\$ 1,579,691	\$ 628,543	\$ 712,761	\$ 14,214	\$ 105,928	\$ 6,166	\$ 935	\$ 3,024	\$ 700	\$ 3,051,962
Cumulative effect of a change in accounting principle	2,027,349	(291,909)	-	-	-	-	-	-	-	1,735,440
Balance at January 1, 2023	3,607,040	336,634	712,761	14,214	105,928	6,166	935	3,024	700	4,787,402
Recoveries	-	10,509	-	-	-	-	-	-	-	10,509
Provision for loan losses (loan loss reversal)	(1,778,591)	(48,640)	(576,848)	8,055	3,479	1,968	73	2,927	53	(2,387,524)
Balance at September 30, 2023	\$ 1,828,449	\$ 298,503	\$ 135,913	\$ 22,269	\$ 109,407	\$ 8,134	\$ 1,008	\$ 5,951	\$ 753	\$ 2,410,387
Balance at June 30, 2022	\$ 2,025,473	\$ 752,601	\$ 159,511	\$ 18,278	\$ 106,566	\$ 8,034	\$ 1,266	\$ 4,674	\$ 930	\$ 3,077,333
Provision for loan losses (loan loss reversal)	(76,025)	(123,522)	(17,608)	(1,120)	(140)	(507)	(102)	(294)	(54)	(219,372)
Balance at September 30, 2022	\$ 1,949,448	\$ 629,079	\$ 141,903	\$ 17,158	\$ 106,426	\$ 7,527	\$ 1,164	\$ 4,380	\$ 876	\$ 2,857,961
Balance at December 31, 2021	\$ 1,899,626	\$ 761,376	\$ 145,857	\$ 18,606	\$ 162,348	\$ 3,577	\$ 1,316	\$ 4,724	\$ 19,106	\$ 3,016,536
Recoveries	20,349	868	-	-	-	-	-	-	-	21,217
Provision for loan losses (loan loss reversal)	29,473	(133,165)	(3,954)	(1,448)	(55,922)	3,950	(152)	(344)	(18,230)	(179,792)
Balance at September 30, 2022	\$ 1,949,448	\$ 629,079	\$ 141,903	\$ 17,158	\$ 106,426	\$ 7,527	\$ 1,164	\$ 4,380	\$ 876	\$ 2,857,961
Allowance for Unfunded Commitments:										
Balance at June 30, 2023	\$ 57,158	\$ 36,498	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ 93,656
Provision for unfunded commitments	(2,418)	(4,595)	-	-	-	-	-	-	-	(7,013)
Balance at September 30, 2023	\$ 54,740	\$ 31,903	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ 86,643
Balance at December 31, 2022	\$ 53,032	\$ 150,360	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ 203,392
Cumulative effect of a change in accounting principle	65,109	(94,813)	-	-	-	-	-	-	-	(29,704)
Balance at January 1, 2023	118,141	55,547	-	-	-	-	-	-	-	173,688
Provision for unfunded commitments	(63,401)	(23,644)	-	-	-	-	-	-	-	(87,045)
Balance at September 30, 2023	\$ 54,740	\$ 31,903	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ 86,643

For periods prior to January 1, 2023, the allowance for loan losses was based on probable and estimable losses inherent in the loan portfolio.

There were no loan modifications granted to borrowers experiencing financial difficulty during the three months ended September 30, 2023.

The following table shows the amortized cost basis at the end of the respective reporting period for loan modifications granted to borrowers experiencing financial difficulty, disaggregated by loan type and type of modification granted.

	Term or Payment Extension	
	September 30, 2023	% of Total Loans
Production and intermediate-term	\$ 296,027	0.01%

Accrued interest receivable related to loan modifications granted to borrowers experiencing financial difficulty as of the nine months ended September 30, 2023 was \$5,560.

There is no financial effect of the modification made to borrowers experiencing financial difficulty during the nine months ended September 30, 2023.

There were no loans to borrowers experiencing financial difficulty that received a modification on or after January 1, 2023, that defaulted as of September 30, 2023.

The following table sets forth an aging analysis of loans to borrowers experiencing financial difficulty that were modified on or after January 1, 2023, the date of the adoption of the guidance noted above, through September 30, 2023:

	Payment Status of Loans Modified in the Past Nine Months		
	Current	30-89 Days Past Due	90 Days or More Past Due
Production and intermediate-term	\$ 296,027	\$ -	\$ -

There were no additional commitments to lend to borrowers experiencing financial difficulty whose loans have been modified at September 30, 2023.

Troubled Debt Restructurings

Prior to January 1, 2023, the adoption of updated FASB guidance on loan modifications, a restructuring of a loan constituted a troubled debt restructuring, also known as formally restructured, if the creditor for economic or legal reasons related to the borrower's financial difficulties granted a concession to the borrower that it would not otherwise consider. Concessions varied by program and were borrower-specific and could include interest rate reductions, term extensions, payment deferrals or the acceptance of additional collateral in lieu of payments. When a restructured loan constituted a troubled debt restructuring, these loans were included within our impaired loans under nonaccrual or accruing restructured loans.

There were no troubled debt restructurings that occurred during the quarter ended September 30, 2022.

There were no troubled debt restructurings that occurred within the previous 12 months and for which there was a payment default during the period.

NOTE 4 —LEASES:

The components of lease expense were as follows:

Classification	For the Three Months Ended		For the Nine Months Ended	
	September 30, 2023	September 30, 2022	September 30, 2023	September 30, 2022
Operating lease cost	\$ 60,678	\$ 103,903	\$ 200,718	\$ 202,941
Short-term lease cost	5,400	3,600	47,450	10,800
Finance lease cost:				
Amortization of right-of-use assets	(4,593)	(49,136)	(32,534)	(62,029)
Net lease cost	<u>\$ 61,485</u>	<u>\$ 58,367</u>	<u>\$ 215,634</u>	<u>\$ 151,712</u>

Other information related to leases was as follows:

	For the Three Months Ended		For the Nine Months Ended	
	September 30, 2023	September 30, 2022	September 30, 2023	September 30, 2022
Cash paid for amounts included in the measurement of lease liabilities:				
Operating cash flows from operating leases	\$ 56,085	\$ 54,767	\$ 168,184	\$ 140,912
Right-of-use assets obtained in exchange for lease obligations:				
Operating leases	\$ 60,678	\$ 103,903	\$ 200,718	\$ 202,941

Lease term and discount rate are as follows:

	September 30, 2023	December 31, 2022
Weighted average remaining lease term in years		
Operating leases	6.99	7.33
Weighted average discount rate		
Operating leases	5.45%	4.01%

Future minimum lease payments under non-cancellable leases as of September 30, 2023, were as follows:

	Operating Leases
2023	\$ 41,374
2024	212,466
2025	165,381
2026	96,646
Thereafter	474,675
Total lease payments	<u>\$ 990,542</u>

NOTE 5 — CAPITAL:

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

Regulatory Capitalization Requirements

Risk-adjusted:	Regulatory Minimums with Buffer	As of September 30, 2023
Common equity tier 1 ratio	7.00%	12.36%
Tier 1 capital ratio	8.50%	12.36%
Total capital ratio	10.50%	12.58%
Permanent capital ratio	7.00%	12.39%
Non-risk-adjusted:		
Tier 1 leverage ratio	5.00%	10.41%
UREE leverage ratio	1.50%	7.91%

The components of the Association's regulatory capital ratios, based on 90 day average balances, were as follows at September 30, 2023:

	Common equity tier 1 ratio	Tier 1 capital ratio	Total capital ratio	Permanent capital ratio
Numerator:				
Unallocated retained earnings	\$ 111,973,075	\$ 111,973,075	\$ 111,973,075	\$ 111,973,075
Paid-in capital	47,596,495	47,596,495	47,596,495	47,596,495
Common Cooperative Equities:				
Statutory minimum purchased borrower stock	4,588,957	4,588,957	4,588,957	4,588,957
Allocated equities:				
Allocated equities held ≥ 7	53,219,859	53,219,859	53,219,859	53,219,859
Nonqualified allocated equities not subject to retirement	64,937,342	64,937,342	64,937,342	64,937,342
Allowance for loan losses and reserve for credit losses subject to certain limitations	-	-	4,272,876	-
Regulatory Adjustments and Deductions:				
Amount of allocated investments in other System institutions	(38,500,345)	(38,500,345)	(38,500,345)	(38,500,345)
Other regulatory required deductions	(2,901,427)	(2,901,427)	(2,901,427)	(2,901,427)
	\$ 240,913,956	\$ 240,913,956	\$ 245,186,832	\$ 240,913,956
Denominator:				
Risk-adjusted assets excluding allowance	\$ 1,990,453,794	\$ 1,990,453,794	\$ 1,990,453,794	\$ 1,990,453,794
Regulatory Adjustments and Deductions:				
Regulatory deductions included in total capital	(41,401,772)	(41,401,772)	(41,401,772)	(41,401,772)
Allowance for loan losses	-	-	-	(4,180,233)
	\$ 1,949,052,022	\$ 1,949,052,022	\$ 1,949,052,022	\$ 1,944,871,789
Calculated Ratio	12.36%	12.36%	12.58%	12.39%

	Tier 1 leverage ratio	UREE leverage ratio
Numerator:		
Unallocated retained earnings	\$ 111,973,075	\$ 111,973,075
Paid-in capital	47,596,495	47,596,495
Common Cooperative Equities:		
Statutory minimum purchased borrower stock	4,588,957	-
Allocated equities:		
Allocated equities held ≥ 7	53,219,859	-
Nonqualified allocated equities not subject to retirement	64,937,342	64,937,342
Regulatory Adjustments and Deductions:		
Amount of allocated investments in other System institutions	(38,500,345)	(38,500,345)
Other regulatory required deductions	(2,901,427)	(2,901,427)
	\$ 240,913,956	\$ 183,105,140
Denominator:		
Total Assets	\$ 2,362,693,047	\$ 2,362,693,047
Regulatory Adjustments and Deductions:		
Regulatory deductions included in tier 1 capital	(49,190,897)	(49,190,897)
	\$ 2,313,502,150	\$ 2,313,502,150
Calculated Ratio	10.41%	7.91%

	<u>September 30, 2023</u>	<u>December 31, 2022</u>
Capital stock and participation certificates	\$ 4,602,750	\$ 4,580,185
Additional paid-in-capital	47,596,495	47,596,495
Accumulated other comprehensive income	804,102	861,603
Retained earnings ¹	243,959,596	209,264,197
Total Capital	\$ 296,962,943	\$ 262,302,480

¹ Retained earnings for the quarter ended September 30, 2023, reflects an increase from the cumulative effect of a change in accounting principle for CECL on January 1, 2023.

The following tables present the activity in the accumulated other comprehensive loss, net of tax by component:

Accum Other Comp Income (Loss)	
September 30, 2023	<u>Net of Tax</u>
Nonpension postretirement benefits	\$ 804,102
September 30, 2022	<u>Net of Tax</u>
Nonpension postretirement benefits	\$ (332,006)

The Association's accumulated other comprehensive income (loss) relates entirely to its non-pension other postretirement benefits. Amortization of prior service (credits) cost and of actuarial (gain) loss are reflected in "Salaries and employee benefits" in the Consolidated Statement of Comprehensive Income. The following table summarizes the change in accumulated other comprehensive income (loss) for the nine months ended September 30:

	<u>2023</u>	<u>2022</u>
Accumulated other comprehensive income (loss) at January 1	\$ 861,603	\$ (315,716)
Amortization of prior service credit included in salaries and employee benefits	(16,287)	(16,290)
Amortization of actuarial gain included in salaries and employee benefits	<u>(41,214)</u>	<u>-</u>
Other comprehensive loss, net of tax	<u>(57,501)</u>	<u>(16,290)</u>
Accumulated other comprehensive income (loss) at September 30	<u>\$ 804,102</u>	<u>\$ (332,006)</u>

NOTE 6 — INCOME TAXES:

The Association conducts its business activities through two wholly-owned subsidiaries. Long-term mortgage lending activities are conducted through a wholly-owned FLCA subsidiary which is exempt from federal and state income tax. Short and intermediate term lending activities are conducted through a wholly-owned PCA subsidiary. The PCA subsidiary and the ACA holding company are subject to income tax. The Association operates as a cooperative that qualifies for tax treatment under Subchapter T of the Internal Revenue Code. Accordingly, under specified conditions, the Association can exclude from taxable income amounts distributed as qualified patronage dividends in the form of cash, stock or allocated retained earnings. Provisions for income taxes are made only on those taxable earnings that will not be distributed as qualified patronage dividends. Deferred taxes are recorded at the tax effect of all temporary differences based on the assumption that such temporary differences are retained by the Association and will therefore impact future tax payments. A valuation allowance is provided against deferred tax assets to the extent that it is more likely than not (more than 50 percent probability), based on management's estimate, that they will not be realized. The Association has no valuation allowance on its deferred tax assets because management estimates full utilization of these assets.

NOTE 7 — 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 the principal or most advantageous market for the asset or liability. See Note 15 in the 2022 Annual Report to Stockholders for a more complete description.

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

September 30, 2023	Fair Value Measurement Using		
	Level 1	Level 2	Level 3
Assets:			
Loans	\$ -	\$ -	\$ 231,507
Other property owned	-	-	-
 December 31, 2022			
	Fair Value Measurement Using		
	Level 1	Level 2	Level 3
Assets:			
Loans	\$ -	\$ -	\$ 4,047,437
Other property owned	-	-	-

Uncertainty of Fair Value Measurements

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

Valuation Techniques

As more fully discussed in Note 15 to the 2022 Annual Report to Stockholders, authoritative guidance establishes a fair value hierarchy, which requires an entity to maximize the use of observable inputs and minimize the use of unobservable inputs when

measuring fair value. The following represent a brief summary of the valuation techniques used for the Association's assets and liabilities. For a more complete description, see the 2022 Annual Report to Stockholders.

Loans Evaluated for Impairment

For certain loans evaluated for impairment under FASB impairment guidance, the fair value is based upon the underlying collateral since the loans are collateral-dependent loans for which real estate is the collateral. The fair value measurement process uses independent appraisals and other market-based information, but in many cases it also requires significant input based on management's knowledge of and judgment about current market conditions, specific issues relating to the collateral and other matters. As a result, a majority of these loans have fair value measurements that fall within Level 3 of the fair value hierarchy. When the value of the real estate, less estimated costs to sell, is less than the principal balance of the loan, a specific reserve is established.

Other Property Owned

Other property owned is generally classified as Level 3 of the fair value hierarchy. The process for measuring the fair value of the other property owned involves the use of independent appraisals and other market-based information. Costs to sell represent transaction costs and are not included as a component of the asset's fair value. As a result, these fair value measurements fall within Level 3 of the hierarchy.

NOTE 8 — EMPLOYEE BENEFIT PLANS:

The following table summarizes the components of net periodic benefit costs for the three and nine months ended September 30:

Three months ended September 30:

	Other Benefits	
	2023	2022
Service cost	\$ 6,897	\$ 11,330
Interest cost	42,828	34,959
Amortization of prior service credits	(5,429)	(5,429)
Amortization of net actuarial gain	(13,737)	-
Net periodic benefit cost	\$ 30,559	\$ 40,860

Nine months ended September 30:

	Other Benefits	
	2023	2022
Service cost	\$ 20,692	\$ 33,990
Interest cost	128,483	104,876
Amortization of prior service credits	(16,287)	(16,290)
Amortization of net actuarial gain	(41,214)	-
Net periodic benefit cost	\$ 91,674	\$ 122,576

The Association's liability for the unfunded accumulated obligation for these benefits at September 30, 2023, was \$3,414,642 and is included in other liabilities on the Consolidated Balance Sheet.

The components of net periodic benefit cost other than the service cost component are included in the line item Salaries and employee benefits in the Consolidated Statement of Comprehensive Income.

The structure of the district's defined benefit pension plan is characterized as multiemployer since the assets, liabilities and cost of the plan are not segregated or separately accounted for by participating employers (Bank and Associations). The Association recognizes its amortized annual contributions to the plan as an expense. The Association previously disclosed in its financial statements for the year ended December 31, 2022, that it expected to contribute \$309,219 to the district's defined benefit pension plan in 2023. As of September 30, 2023, \$231,914 of contributions have been expensed. The Association presently does not anticipate contributions over \$309,219 will be required in 2023.

NOTE 9 — COMMITMENTS AND CONTINGENT LIABILITIES:

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

NOTE 10 — SUBSEQUENT EVENTS:

The Association has evaluated subsequent events through November 3, 2023, which is the date the financial statements were issued. There are no other significant events requiring disclosure as of this date.