



**Yankee Farm Credit, ACA**

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**CONSOLIDATED FINANCIAL STATEMENTS  
THIRD QUARTER ENDED SEPTEMBER 30, 2013**

November 7, 2013

Dear Shareholder:

Enclosed are the Association's consolidated financial statements for the third quarter of 2013. These statements should be read in conjunction with the 2012 Annual Report to Shareholders.

The purpose of these financial statements is to provide timely financial information about your Association's financial condition and results of operations. Should you have any questions about these statements, please call us.

Copies of the Association's annual and quarterly reports are available to members at no charge from any of our local offices or by accessing the Association's website at [www.yankeeaca.com](http://www.yankeeaca.com). The Association's annual reports are available 75 days after year end, and quarterly reports are available 40 days after the end of each calendar quarter. As a shareholder, your investment in the Association is materially affected by the financial condition and results of operations of CoBank, ACB. CoBank's annual and quarterly reports are available at no charge from any of our offices. Our office locations are listed at the end of this report.

The undersigned certify that they have reviewed this report and it has been prepared in accordance with all statutory and regulatory requirements and that the information contained herein is true, accurate, and complete to the best of his or her knowledge and belief. The financial statements, in the opinion of management, fairly present the financial condition of the institution except as noted.

Sincerely,

Rocklyn A. Giroux  
Chairperson, Board of Directors

George S. Putnam  
President and CEO

Rocki-Lee DeWitt  
Chairperson, Audit Committee

Greg M. LeDuc  
Chief Financial Officer

## YANKEE FARM CREDIT, ACA

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

#### Third Quarter Ended September 30, 2013

(Dollars in thousands, except as noted)  
(Unaudited)

#### Results of Operations: Third Quarter

Net income for the third quarter of 2013 was \$2.258 million, up \$382 thousand (20%) from net income of \$1.876 million in the third quarter of 2012.

Net interest income before the provision for loan losses was up \$402 thousand (13%) in 2013 as compared to 2012. The following table shows the components of this increase:

<u>Changes in net interest income due to:</u>	
Changes in volumes of accrual loans & debt	\$ 312
Changes in interest rates on accrual loans & debt	60
Changes in interest income on nonaccrual loans	24
Changes in interest rate swap income	0
Other adjustments	6
Total change in net interest income	<u>\$ 402</u>

Changes in accrual volumes and rates are shown in the following table:

	Three Months Ended September 30,	
	2013	2012
Average accrual loan volume	\$ 387,088	\$ 352,549
Average interest rate on loans	4.19%	4.18%
Average interest rate spread	3.46%	3.39%

Average loan volume was higher in 2013, and this contributed an increase of \$312 thousand and changes in interest rates on accrual loans contributed \$60 thousand to the total change in net interest income as shown in the first table above.

There was a provision for credit losses of \$83 thousand in the third quarter of 2013, as compared to a provision for credit losses of \$264 thousand in the third quarter of 2012.

Other income increased by \$51 thousand (7%) in 2013 as compared to 2012. This increase resulted primarily from an increase of \$71 thousand in patronage refunds from CoBank. The increase in patronage refunds was offset by a decrease of \$25 thousand in fees for financial services.

Other expense increased by \$251 thousand (15%) in 2013 as compared to 2012. Salaries and employee benefits increased by \$53 thousand (5%) and other expenses increased \$149 thousand (52%).

#### Results of Operations: Year-to-Date

Net income through the third quarter of 2013 was \$6.679 million, up \$283 thousand (4%) from net income of \$6.396 million through the third quarter of 2012.

## Management's Discussion & Analysis (cont.)

Net interest income before the provision for loan losses was up \$1.186 million (13%) in 2013 as compared to 2012. The following table shows the components of this increase:

<u>Changes in net interest income due to:</u>	
Changes in volumes of accrual loans & debt	\$ 973
Changes in interest rates on accrual loans & debt	47
Changes in interest income on nonaccrual loans	173
Changes in interest rate swap income	(8)
Other adjustments	1
Total change in net interest income	<u>\$ 1,186</u>

Changes in accrual volumes and rates are shown in the following table:

	Nine Months Ended September 30,	
	<u>2013</u>	<u>2012</u>
Average accrual loan volume	\$ 379,973	\$ 342,796
Average interest rate on loans	4.18%	4.22%
Average interest rate spread	3.45%	3.41%

Average loan volume was higher in 2013, contributing an increase of \$973 thousand, interest recognized upon payouts of nonaccruals loans contributed \$173 thousand, and changes in interest rates contributed \$47 thousand to the total change in net interest income, as shown in the first table above. These increases to net interest income were offset by decreases in swap income of \$8 thousand, as shown in the first table above.

There was a provision for credit losses of \$244 thousand through the third quarter of 2013, as compared to a provision for credit losses of \$151 thousand for the same period in 2012.

Other income decreased by \$207 thousand (8%) in 2013 as compared to 2012. This decrease resulted primarily from \$393 thousand in refunds received in 2012 from the Farm Credit System Insurance Corporation related to the Farm Credit Insurance Fund. There were no such refunds received in 2013. This was offset by an increase of \$254 thousand (20%) in patronage refunds from CoBank.

Other expense increased by \$602 thousand (12%) in 2013 as compared to 2012. Salaries and employee benefits increased by \$251 thousand (8%) and the FCSIC insurance premium increased \$107 thousand.

### Loan Portfolio and Financial Condition

Loans originated by the Association increased by \$28.2 million (7%) from year-end. Loans purchased increased by \$751 thousand (4%) from year-end, and participations sold increased by \$10.1 million (15%). Loans held by the Association increased by \$18.8 million (5%) from year-end.

The loan portfolio continues to be concentrated in the dairy industry. Farm prices for dairy products increased in the third quarter of 2013. Federal Order 1 prices for the third quarter of 2013 averaged \$20.22/cwt, up \$0.69/cwt (4%) from the second quarter of 2013, and up \$2.81/cwt (16%) from the third quarter of 2012. (Prices quoted do not include the effect of the Milk Income Loss Contract (MILC) program, which began December 1, 2001.) The change in prices received for dairy products has been accompanied by a decrease in the cost of farm inputs, particularly purchased feed. The composite Feed Index published by the USDA was 256 for the third quarter of 2013, down 4% from the second quarter of 2013, and down 8% from the third quarter of 2012. (Feed Index = 100 for 1990-1992)

Loan quality improved slightly and remained strong through the third quarter of 2013. Loans graded Substandard or lower were 3.7% of total loans at September 30, 2013, 0.8% improved from year-end. High risk assets comprised 0.9% of loans and related assets at September 30, 2013, 0.5% improved from year-end. (High risk assets include nonaccrual loans, accrual restructured loans, loans delinquent 90 days or more but not yet classified as nonaccrual, and other property owned.) Repayment performance remained satisfactory. Loans (both accrual and nonaccrual) delinquent 30 days or more were 1.0% at September 30, 2013, 0.4% worse from year-end. The 12-month rolling average for this statistic was 0.8% at September 30, 2013, 0.2% improved from year-end. There were no charge-

### **Management's Discussion & Analysis (cont.)**

offs, but recoveries of \$7 thousand in the first three quarters of 2013. There were no charge-offs, but recoveries of \$6 thousand in the first three quarters of 2012.

As discussed in the 2012 Annual Report to Shareholders, the Association declared a patronage distribution of \$4.918 million based on 2012 earnings, 100% in cash. This was paid on March 25, 2013.

Members' equity as a percentage of assets was 19.8% at September 30, 2013, no change from year-end. The Association's permanent capital ratio was 19.3% at September 30, 2013, down 0.6% from year-end.

These financial statements were prepared under the oversight of the Audit Committee of the Board of Directors.

**YANKEE FARM CREDIT, ACA**  
**CONSOLIDATED BALANCE SHEET**  
(Unaudited)

	September 30, <u>2013</u>	December 31, <u>2012</u>
<b><u>ASSETS</u></b>		
Loans originated by the Association	\$ 461,427	\$ 433,223
Plus loans purchased	19,178	18,427
Less participations sold	<u>76,708</u>	<u>66,550</u>
Loans held by the Association	403,897	385,100
Less allowance for loan losses	<u>5,082</u>	<u>4,788</u>
Net loans	398,815	380,312
Cash	763	2,522
Accrued interest receivable	1,207	1,072
Patronage refunds due from CoBank, ACB	1,526	1,833
Investment in CoBank, ACB	13,722	13,583
Mission related investment	673	751
Premises and equipment, less accumulated depreciation	1,065	1,022
Other assets	1,436	1,459
Total assets	<u>\$ 419,207</u>	<u>\$ 402,554</u>
<b><u>LIABILITIES</u></b>		
Note payable to CoBank, ACB	\$ 330,545	\$ 316,179
Patronage distribution payable	3,206	4,918
Reserve for unfunded commitments	207	251
Other liabilities	<u>2,137</u>	<u>1,595</u>
Total liabilities	<u>336,095</u>	<u>322,943</u>
<b><u>MEMBERS' EQUITY</u></b>		
Capital stock and participation certificates	1,058	1,030
Unallocated surplus	84,024	80,551
Accumulated other comprehensive income	<u>(1,970)</u>	<u>(1,970)</u>
Total members' equity	83,112	79,611
Total liabilities and members' equity	<u>\$ 419,207</u>	<u>\$ 402,554</u>

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

**YANKEE FARM CREDIT, ACA**  
**CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME**  
(Unaudited)

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2013	2012	2013	2012
	(in thousands)			
<b><u>INTEREST INCOME</u></b>				
Loans	\$ 4,115	\$ 3,704	\$ 12,044	\$ 10,832
Total interest income	4,115	3,704	12,044	10,832
<b><u>INTEREST EXPENSE</u></b>				
Note payable to CoBank, ACB	586	577	1,714	1,688
Total interest expense	586	577	1,714	1,688
Net interest income	3,529	3,127	10,330	9,144
Provision for credit losses	83	264	244	151
Net interest income after provision for credit losses	3,446	2,863	10,086	8,993
<b><u>OTHER INCOME</u></b>				
Patronage refunds from CoBank, ACB	518	447	1,530	1,276
Fees for financial services	195	220	771	835
Loan fees and other income	32	27	62	459
Total other income	745	694	2,363	2,570
<b><u>OTHER EXPENSE</u></b>				
Salaries and employee benefits	1,090	1,037	3,382	3,131
Occupancy and equipment	85	85	270	251
Farm Credit Insurance Fund premium	69	30	196	89
Fees paid to Farm Credit Financial Partners, Inc.	248	238	744	714
Other expenses	436	287	1,165	970
Total other expense	1,928	1,677	5,757	5,155
Income before income taxes	2,263	1,880	6,692	6,408
Provision for income taxes	5	4	13	12
Net income	\$ 2,258	\$ 1,876	\$ 6,679	\$ 6,396
<b><u>OTHER COMPREHENSIVE (LOSS) INCOME</u></b>				
OCI related to swaps	-	-	-	(8)
Comprehensive income	\$ 2,258	\$ 1,876	\$ 6,679	\$ 6,388

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

**YANKEE FARM CREDIT, ACA**  
**CONSOLIDATED STATEMENT OF CHANGES IN MEMBERS' EQUITY**  
(Unaudited)

	Capital Stock and Participation Certificates	Surplus		Accumulated Other Comprehensive Income	Total Members' Equity
		Allocated	Unallocated (in thousands)		
Balance at December 31, 2011	\$ 993	\$ -	\$ 76,798	\$ (1,975)	\$ 75,816
Comprehensive income					
Net income	-	-	6,396	-	6,396
Other comprehensive income					
Net unrealized gains (losses) on interest rate swaps	-	-	-	(8)	(8)
Change in minimum pension liability	-	-	-	-	-
Total comprehensive income	<u>-</u>	<u>-</u>	<u>6,396</u>	<u>(8)</u>	<u>6,388</u>
Capital stock/PCs issued	127	-	-	-	127
Capital stock/PCs retired	(100)	-	-	-	(100)
Patronage distribution accrued					
Cash	-	-	(2,584)	-	(2,584)
Adjustment for Rounding	-	-	1	-	1
Balance at September 30, 2012	<u>\$ 1,020</u>	<u>\$ -</u>	<u>\$ 80,611</u>	<u>\$ (1,983)</u>	<u>\$ 79,648</u>
Balance at December 31, 2012	\$ 1,030	\$ -	\$ 80,551	\$ (1,970)	\$ 79,611
Comprehensive income					
Net income	-	-	6,679	-	6,679
Other comprehensive income					
Net unrealized gains (losses) on interest rate swaps	-	-	-	-	-
Change in minimum pension liability	-	-	-	-	-
Total comprehensive income	<u>-</u>	<u>-</u>	<u>6,679</u>	<u>-</u>	<u>6,679</u>
Capital stock/PCs issued	150	-	-	-	150
Capital stock/PCs retired	(122)	-	-	-	(122)
Patronage distribution accrued					
Cash	-	-	(3,206)	-	(3,206)
Adjustment for rounding	-	-	-	-	-
Balance at September 30, 2013	<u>\$ 1,058</u>	<u>\$ -</u>	<u>\$ 84,024</u>	<u>\$ (1,970)</u>	<u>\$ 83,112</u>

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

## YANKEE FARM CREDIT, ACA

### Notes To Consolidated Financial Statements

#### Third Quarter Ended September 30, 2013

(Dollars in thousands, except as noted)  
(Unaudited)

#### **NOTE 1 - ORGANIZATION AND SIGNIFICANT ACCOUNTING POLICIES**

Yankee Farm Credit, ACA (the Association) is a member-owned cooperative within the Farm Credit System. A description of the organization and operations of the Association, the significant accounting policies followed, and the financial condition and results of operations as of and for the year ended December 31, 2012 are contained in the 2012 Annual Report to Shareholders. These unaudited third quarter 2013 financial statements should be read in conjunction with the 2012 Annual Report to Shareholders.

In December 2011, the Financial Accounting Standards Board (FASB) issued guidance entitled, "Balance Sheet – Disclosures about Offsetting Assets and Liabilities." The guidance requires an entity to disclose information about offsetting and related arrangements to enable users of its financial statements to understand the effect of those arrangements on its financial position. This includes the effect or potential effect of rights of setoff associated with an entity's recognized assets and recognized liabilities. The requirements apply to recognized financial instruments and derivative instruments that are offset in accordance with the rights of offset set forth in accounting guidance and for those recognized financial instruments and derivative instruments that are subject to an enforceable master netting arrangement or similar agreement, irrespective of whether they are offset or not. This guidance is to be applied retrospectively for all comparative periods and is effective for annual reporting periods beginning on or after January 1, 2013, and interim periods within those annual periods. The adoption of this guidance did not impact the financial condition or results of operations, but resulted in additional disclosures.

In February 2013, the FASB issued guidance entitled, "Reporting of Amounts Reclassified Out of Accumulated Other Comprehensive Income". The guidance requires entities to present either parenthetically on the face of the financial statements or in the notes to the financial statements, significant amounts reclassified from each component of accumulated other comprehensive income and the income statement line items affected by the reclassification. The guidance is effective for public entities for annual periods beginning after December 15, 2012 and for non-public entities for annual periods beginning after December 15, 2013. The adoption of this guidance did not impact the financial condition or results of operations, but resulted in additional disclosures.

The accompanying financial statements contain all adjustments necessary for a fair presentation of the interim financial condition and results of operations and conform to generally accepted accounting principles and prevailing practices within the banking industry. The results of operations for the nine month period ended September 30, 2013 are not necessarily indicative of the results to be expected for the full year.

#### **NOTE 2 - LOANS AND ALLOWANCE FOR LOAN LOSSES**

A summary of loans follows:

	Value at	
	September 30, 2013	December 31, 2012
Long-term farm mortgage	\$ 154,641	\$ 143,535
Country home	2,215	1,813
Farm related business	40,903	24,198
Production and intermediate term	206,138	215,554
Total loans	<u>\$ 403,897</u>	<u>\$ 385,100</u>

The Association purchases and sells participation interests with other parties in order to diversify risk, manage loan volume and comply with FCA regulations. All of the Association's loan purchases and sales are with other Farm Credit institutions. The following table presents information regarding the balances of participations purchased and sold:



	Value at			
	September 30, 2013		December 31, 2012	
	Participations Purchased	Participations Sold	Participations Purchased	Participations Sold
Long-term farm mortgage	\$ 1,300	\$ 6,893	\$ 1,283	\$ 7,876
Farm related business	17,464	578	16,752	410
Production and intermediate term	414	69,237	392	58,264
Total	\$ 19,178	\$ 76,708	\$ 18,427	\$ 66,550

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

	Value at	
	September 30, 2013	December 31, 2012
<u>Nonaccrual Loans:</u>		
Long-term farm mortgage	\$ 1,584	\$ 3,263
Farm related business	641	760
Production and intermediate term	691	908
Total nonaccrual loans	\$ 2,916	\$ 4,931
<u>Troubled Debt Restructured Loans:</u>		
Long-term farm mortgage	\$ 567	\$ 628
Total troubled debt restructured loans	\$ 567	\$ 628
<u>Accrual Loans ≥ 90 Days Past Due:</u>		
Production and intermediate term	\$ -	\$ -
Total accrual loans ≥ 90 days past due	\$ -	\$ -
Total impaired assets	\$ 3,483	\$ 5,559

The following table provides an age analysis of past due loans (including accrued interest) as of September 30, 2013:

	Past Due		
	30 – 89 Days	≥ 90 Days	Total
Long-term farm mortgage	\$ 1,267	\$ 21	\$ 1,288
Country home	78	-	78
Farm related business	277	579	856
Production and intermediate term	1,423	288	1,711
Total loans past due	\$ 3,045	\$ 888	\$ 3,933

There were no loans that were 90 days or more past due but still classified as accrual at September 30, 2013.

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

	September 30, 2013	December 31, 2012
Long-term farm mortgage		
Acceptable	34.3%	33.4%
OAEM*	2.2%	1.0%
Substandard/doubtful	1.4%	2.0%
	<u>37.9%</u>	<u>36.4%</u>
Country home		
Acceptable	0.5%	0.4%
OAEM*	0.1%	0.1%
Substandard/doubtful	0.0%	0.0%
	<u>0.6%</u>	<u>0.5%</u>
Farm related business		
Acceptable	15.4%	14.1%
OAEM*	0.1%	0.1%
Substandard/doubtful	0.4%	0.5%
	<u>15.9%</u>	<u>14.7%</u>
Production and intermediate term		
Acceptable	41.7%	43.3%
OAEM*	2.0%	3.1%
Substandard/doubtful	1.9%	2.0%
	<u>45.6%</u>	<u>48.4%</u>
Total Loans		
Acceptable	91.9%	91.2%
OAEM*	4.4%	4.3%
Substandard/doubtful	3.7%	4.5%
	<u>100.0%</u>	<u>100.0%</u>

\*Other Assets Especially Mentioned

The following tables present information on impaired loans and related amounts in the Allowance for Loan Losses:

	At September 30, 2013		
	Recorded Investment	Unpaid Principal Balance*	Related Allowance
<b>Impaired Loans with a related allowance for loan losses:</b>			
Long-term farm mortgage	\$ 2,139	\$ 2,276	\$ 219
Farm related business	508	681	36
Production and intermediate term	812	1,258	222
Total	<u>\$ 3,459</u>	<u>\$ 4,215</u>	<u>\$ 477</u>
<b>Impaired Loans with no related allowance for loan losses:</b>			
Long-term farm mortgage	\$ 12	\$ 26	\$ -
Production and intermediate term	12	33	-
Total	<u>\$ 24</u>	<u>\$ 59</u>	<u>\$ -</u>
<b>Total Impaired Loans:</b>			
Long-term farm mortgage	\$ 2,151	\$ 2,302	\$ 219
Farm related business	508	681	36
Production and intermediate term	824	1,291	222
Total	<u>\$ 3,483</u>	<u>\$ 4,274</u>	<u>\$ 477</u>

	At December 31, 2012		
	Recorded Investment	Unpaid Principal Balance*	Related Allowance
<b>Impaired Loans with a related allowance for loan losses:</b>			
Long-term farm mortgage	\$ 3,860	\$ 4,452	\$ 312
Farm related business	849	1,116	94
Production and intermediate term	760	1,020	143
Total	<u>\$ 5,469</u>	<u>\$ 6,588</u>	<u>\$ 549</u>
<b>Impaired Loans with no related allowance for loan losses:</b>			
Long-term farm mortgage	\$ 31	\$ 105	\$ -
Production and intermediate term	59	149	-
Total	<u>\$ 90</u>	<u>\$ 254</u>	<u>\$ -</u>
<b>Total Impaired Loans:</b>			
Long-term farm mortgage	\$ 3,891	\$ 4,557	\$ 312
Farm related business	908	1,265	94
Production and intermediate term	760	1,020	143
Total	<u>\$ 5,559</u>	<u>\$ 6,842</u>	<u>\$ 549</u>

\*Unpaid principal balance represents the borrower's contractual balance of the loan.

The following tables present additional information on impaired loans:

	Three Months Ended			
	September 30, 2013		September 30, 2012	
	Average Impaired Loans	Interest Income Recognized	Average Impaired Loans	Interest Income Recognized
<b>Impaired Loans with a related allowance for loan losses:</b>				
Long-term farm mortgage	\$ 2,186	\$ 32	\$ 4,011	\$ 12
Farm related business	127	-	919	-
Production and intermediate term	722	14	972	2
Total	<u>\$ 3,035</u>	<u>\$ 46</u>	<u>\$ 5,902</u>	<u>\$ 14</u>
<b>Impaired Loans with no related allowance for loan losses:</b>				
Long-term farm mortgage	\$ 13	\$ -	\$ 39	\$ -
Production and intermediate term	12	-	59	-
Total	<u>\$ 25</u>	<u>\$ -</u>	<u>\$ 98</u>	<u>\$ -</u>
<b>Total Impaired Loans:</b>				
Long-term farm mortgage	\$ 2,199	\$ 32	\$ 4,050	\$ 12
Farm related business	127	-	919	-
Production and intermediate term	734	14	1,031	2
Total	<u>\$ 3,060</u>	<u>\$ 46</u>	<u>\$ 6,000</u>	<u>\$ 14</u>

	Nine Months Ended			
	September 30, 2013		September 30, 2012	
	Average Impaired Loans	Interest Income Recognized	Average Impaired Loans	Interest Income Recognized
<b>Impaired Loans with a related allowance for loan losses:</b>				
Long-term farm mortgage	\$ 2,303	\$ 123	\$ 4,124	\$ 27
Farm related business	120	-	943	-
Production and intermediate term	844	90	1,040	3
Total	<u>\$ 3,267</u>	<u>\$ 213</u>	<u>\$ 6,107</u>	<u>\$ 30</u>
<b>Impaired Loans with no related allowance for loan losses:</b>				
Long-term farm mortgage	\$ 14	\$ -	\$ 42	\$ -
Production and intermediate term	12	-	59	-
Total	<u>\$ 26</u>	<u>\$ -</u>	<u>\$ 101</u>	<u>\$ -</u>
<b>Total Impaired Loans:</b>				
Long-term farm mortgage	\$ 2,317	\$ 123	\$ 4,166	\$ 27
Farm related business	120	-	943	-
Production and intermediate term	856	90	1,099	3
Total	<u>\$ 3,293</u>	<u>\$ 213</u>	<u>\$ 6,208</u>	<u>\$ 30</u>

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

	Long-term Farm Mortgage	Country Home	Farm Related Business	Production & Intermediate Term	Total
<b>Allowance for Loan Losses:</b>					
Balance at June 30, 2013	\$ 3,064	\$ 71	\$ 312	\$ 1,590	\$ 5,037
Charge-offs	-	-	-	-	-
Recoveries	-	-	-	-	-
Provision for (reversal of provision for) loan losses	(8)	(35)	53	35	45
Balance at September 30, 2013	<u>\$ 3,056</u>	<u>\$ 36</u>	<u>\$ 365</u>	<u>\$ 1,625</u>	<u>\$ 5,082</u>
Balance at December 31, 2012	\$ 2,586	\$ 67	\$ 238	\$ 1,897	\$ 4,788
Charge-offs	-	-	-	-	-
Recoveries	-	-	7	-	7
Provision for (reversal of provision for) loan losses	470	(31)	120	(272)	287
Balance at September 30, 2013	<u>\$ 3,056</u>	<u>\$ 36</u>	<u>\$ 365</u>	<u>\$ 1,625</u>	<u>\$ 5,082</u>
Ending Balance: individually evaluated for impairment	\$ 219	\$ -	\$ 36	\$ 222	\$ 477
Ending Balance: collectively evaluated for impairment	<u>2,837</u>	<u>36</u>	<u>329</u>	<u>1,403</u>	<u>4,605</u>
Balance at September 30, 2013	<u>\$ 3,056</u>	<u>\$ 36</u>	<u>\$ 365</u>	<u>\$ 1,625</u>	<u>\$ 5,082</u>
Balance at June 30, 2012	\$ 2,784	\$ 26	\$ 393	\$ 1,490	\$ 4,693
Charge-offs	-	-	-	-	-
Recoveries	-	-	-	-	-
Provision for (reversal of provision for) loan losses	(161)	1	18	358	216
Balance at September 30, 2012	<u>\$ 2,623</u>	<u>\$ 27</u>	<u>\$ 411</u>	<u>\$ 1,848</u>	<u>\$ 4,909</u>
Balance at December 31, 2011	\$ 2,818	\$ 18	\$ 240	\$ 1,808	\$ 4,884
Charge-offs	-	-	-	-	-
Recoveries	-	-	6	-	6
Provision for (reversal of provision for) loan losses	(195)	9	165	40	19
Balance at September 30, 2012	<u>\$ 2,623</u>	<u>\$ 27</u>	<u>\$ 411</u>	<u>\$ 1,848</u>	<u>\$ 4,909</u>
Ending Balance: individually evaluated for impairment	\$ 394	\$ -	\$ 36	\$ 305	\$ 735
Ending Balance: collectively evaluated for impairment	<u>2,229</u>	<u>27</u>	<u>375</u>	<u>1,543</u>	<u>4,174</u>
Balance at September 30, 2012	<u>\$ 2,623</u>	<u>\$ 27</u>	<u>\$ 411</u>	<u>\$ 1,848</u>	<u>\$ 4,909</u>

	Long-term Farm Mortgage	Country Home	Farm Related Business	Production & Intermediate Term	Total
<b>Recorded Investment in Loans Outstanding:</b>					
At September 30, 2013					
Ending Balance for loans individually evaluated for impairment	\$ 2,149	\$ -	\$ 508	\$ 824	\$ 3,481
Ending Balance for loans collectively evaluated for impairment	<u>152,949</u>	<u>2,215</u>	<u>4,330</u>	<u>240,922</u>	<u>400,416</u>
Ending Balance at September 30, 2013	<u>\$ 155,098</u>	<u>\$ 2,215</u>	<u>\$ 4,838</u>	<u>\$ 241,746</u>	<u>\$ 403,897</u>
At December 31, 2012					
Ending Balance for loans individually evaluated for impairment	\$ 3,891	\$ -	\$ 760	\$ 908	\$ 5,559
Ending Balance for loans collectively evaluated for impairment	<u>138,576</u>	<u>1,813</u>	<u>24,506</u>	<u>214,646</u>	<u>379,541</u>
Ending Balance at December 31, 2012	<u>\$ 152,467</u>	<u>\$ 1,813</u>	<u>\$ 25,266</u>	<u>\$ 215,554</u>	<u>\$ 385,100</u>

In 2011, we revised our methodology for determining the Allowance for Credit Losses. The new methodology takes into consideration potential losses related to unfunded commitments, and as a result, we have established a separate Reserve for Unfunded Commitments, which is included in Other Liabilities on the Association's balance sheet.

The provision for the Reserve for Unfunded Commitments is part of the Provision for Credit Losses on the income statement. The components of the Provision for Credit Losses are presented in the table below:

	Nine Months Ended September 30,	
	2013	2012
Provision for loan losses	\$ 288	\$ 19
Provision for unfunded commitments	(44)	132
Total provision for credit losses	<u>\$ 244</u>	<u>\$ 151</u>

A restructuring of a debt constitutes as troubled debt restructuring (TDR) if the Association, for economic or legal reasons related to the member's financial difficulties, grants a concession to the member that it would not otherwise consider. The Association had no new TDR loans through the period ending September 30, 2013.

The following table provides information on outstanding loans restructured in troubled debt restructurings as of September 30, 2013:

	Loans Modified as TDRs		TDRs in Nonaccrual Status*	
	September 30, 2013	December 31, 2012	September 30, 2013	December 31, 2012
Long-term farm mortgage	\$ 853	\$ 1,063	\$ 289	\$ 435
Production and intermediate term	12	23	12	23
Total	<u>\$ 865</u>	<u>\$ 1,086</u>	<u>\$ 301</u>	<u>\$ 458</u>

\*represents the portion of loans modified as TDRs (first two columns) that are in nonaccrual status

There were no additional commitments to lend additional funds to members whose loans were classified as troubled debts restructured at September 30, 2013.

### **NOTE 3 - CAPITAL**

Please see the 2012 Annual Report to Shareholders, particularly Note 7 to the Financial Statements, for a description of the Association's capitalization policies. The Association's requirement for purchased equities (stock and participation certificates) is presently the legal minimum of 2.0% of the loan with a cap of \$1 thousand.

The patronage distribution for 2012 was \$4.918 million and was distributed 100% in cash on March 25, 2013. A patronage distribution program is also in effect for 2013. The amount of the patronage distribution for 2013 will depend on financial results for the year as a whole and is therefore not known with certainty at this time. However, management estimates that the patronage distribution attributable to the first three quarters of 2013 is approximately \$3.206 million. Management believes it is probable that the 2013 patronage distribution will be paid 100% in cash. Therefore, the accompanying financial statements show an interim accrual at the end of the third quarter of 2013 for patronage distribution payable of \$3.206 million. The corresponding interim accrual at the end of the first three quarters of 2012 for patronage distribution payable was \$2.584 million (also 100% cash).

The Association's regulatory capital ratios were:

	Value At		Regulatory Minimum
	September 30, 2013	December 31, 2012	
Core surplus ratio	19.0%	19.4%	3.5%
Total surplus ratio	19.0%	19.6%	7.0%
Permanent capital ratio	19.3%	19.9%	7.0%

Additionally, for 2013, the Association has established an internal minimum of 16.0% for the permanent capital ratio and a goal of 19.3%. The ratio at September 30, 2013, as indicated above, is not indicative of the full year.

### **NOTE 4 - INCOME TAXES**

Please see the 2012 Annual Report to Shareholders, particularly Note 8 to the Financial Statements, for a description of the Association's deferred tax assets and liabilities and the corresponding valuation allowance. There were no significant changes in the composition or valuation of tax assets/liabilities during the first three quarters of 2013.

### **NOTE 5 - 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. Please see the 2012 Annual Report to Shareholders, particularly Note 2L and Note 11 to the Financial Statements, for a more complete description.

The Association had no assets measured at a fair value on a recurring basis at September 30, 2013 or at December 31, 2012.

Assets measured at a fair value on a non-recurring basis at September 30, 2013 are summarized below:

Assets:	Fair Value Measurement Using		
	Level 1	Level 2	Level 3
Impaired loans	\$ -	\$ -	\$ 2,916
Total Assets	\$ -	\$ -	\$ 2,916

Assets measured at a fair value on a non-recurring basis at December 31, 2012 are summarized below:

Assets:	Fair Value Measurement Using		
	Level 1	Level 2	Level 3
Impaired loans	\$ -	\$ -	\$ 5,432
Total Assets	\$ -	\$ -	\$ 5,432

There were no liabilities measured at fair value on a recurring or non-recurring basis at September 30, 2013.

As more fully discussed in Note 2L and Note 11 of the 2012 Annual Report to Shareholders, accounting 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 Associations' assets.

*Impaired Loans:* For certain loans evaluated for impairment, the fair value is based upon the underlying collateral since the loans were collateral dependent loans. 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 results, these fair value measurements fall within Level 3 of the hierarchy. 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.

Financial assets and financial liabilities measured at carrying amounts and not measured at fair value on the Balance Sheet for each of the fair value hierarchy values are summarized as follows:

	September 30, 2013		December 31, 2012	
	Carrying Amount	Fair Value	Carrying Amount	Fair Value
<b>Financial Assets:</b>				
Loans, net	\$ 398,815	\$ 398,462	\$ 380,312	\$ 380,514
Cash	763	763	2,522	2,522
<b>Financial Liabilities:</b>				
Notes payable to CoBank, ACB	\$ 330,545	\$ 330,388	\$ 316,179	\$ 316,942

A description of the methods and assumptions used to estimate the fair value of the Association's financial instruments for which it is practicable to estimate that value follows:

*Loans:* Fair value is estimated by discounting the expected future cash flows using the Association's and/or CoBank's current interest rates at which similar loans would be made to borrowers with similar credit risk. As discount rates are based on the Association's current loan rates as well as management estimates, management has no basis to determine whether the estimated fair values presented would be indicative of assumptions and adjustments that a purchaser of the Association's loans would see in an actual sale, which could be less.

*Cash:* The carrying value is a reasonable estimate of the fair value.

*Note Payable to CoBank, ACB:* The note payable is segregated into pricing pools according to the types and terms of the loans (or other assets) which it funds. Fair value of the note payable is estimated by discounting the anticipated cash flows of each pricing pool using the current rate that would be charged for additional borrowings. For purposes of this estimate it is assumed the cash flow on the note is equal to the principal payments on the



Association's loan receivables plus accrued interest on the note payable. This assumption implies that earnings on the Association's interest margin are used to fund operating expenses and capital expenditures.

**NOTE 6 - DERIVATIVE FINANCIAL INSTRUMENTS**

The Association enters into derivative financial instruments known as "received fixed" interest rate swaps. The counterparty to the Association's swaps is CoBank. Please see the 2012 Annual Report to Shareholders, particularly Note 2K and Note 15 to the Financial Statements, for a more complete description.

Derivatives had no impact on the balance sheet for the quarter end. The following table shows the impact of these derivatives on the income statement as of quarter end:

	<u>Nine Months Ended September 30,</u>	
	<u>2013</u>	<u>2012</u>
<u>Statement of income:</u>		
(Decreased) increased interest expense	\$ -	\$ (8)
 <u>Other comprehensive income:</u>		
Net unrealized gains (losses) on Interest rate swaps	\$ -	\$ (8)

As of June 2012, the Association had suspended the current interest rate swap program.

**NOTE 7 - SUBSEQUENT EVENTS**

The Association has evaluated subsequent events through November 7, 2013, which is the date the financial statements were available to be issued. No subsequent events were identified that would require additional disclosures or adjustments to the financial statements.

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