Cape Fear Farm Credit

2016 ANNUAL REPORT

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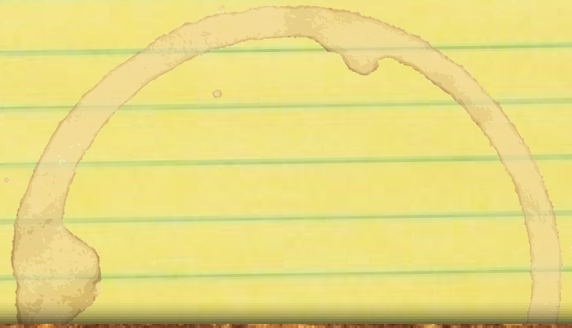


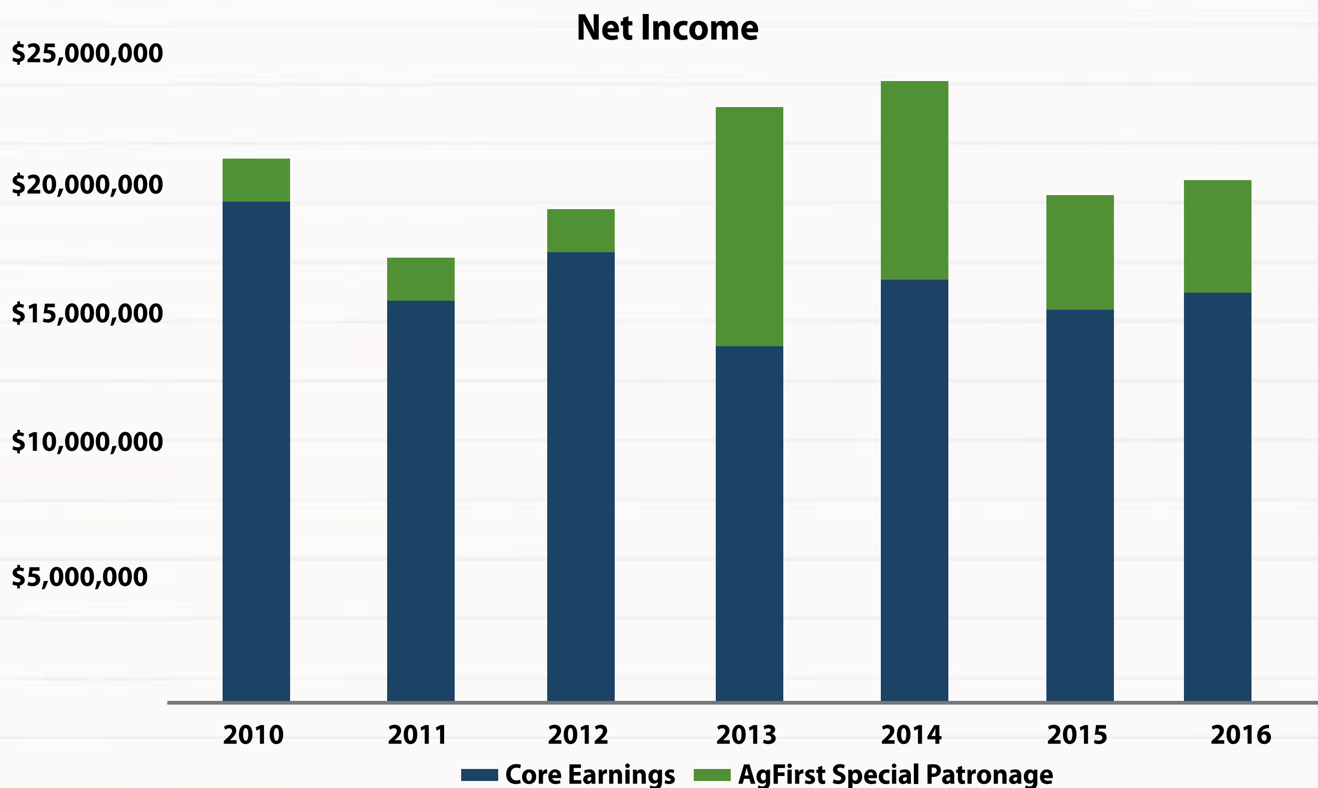
Message from the Chief Executive Officer

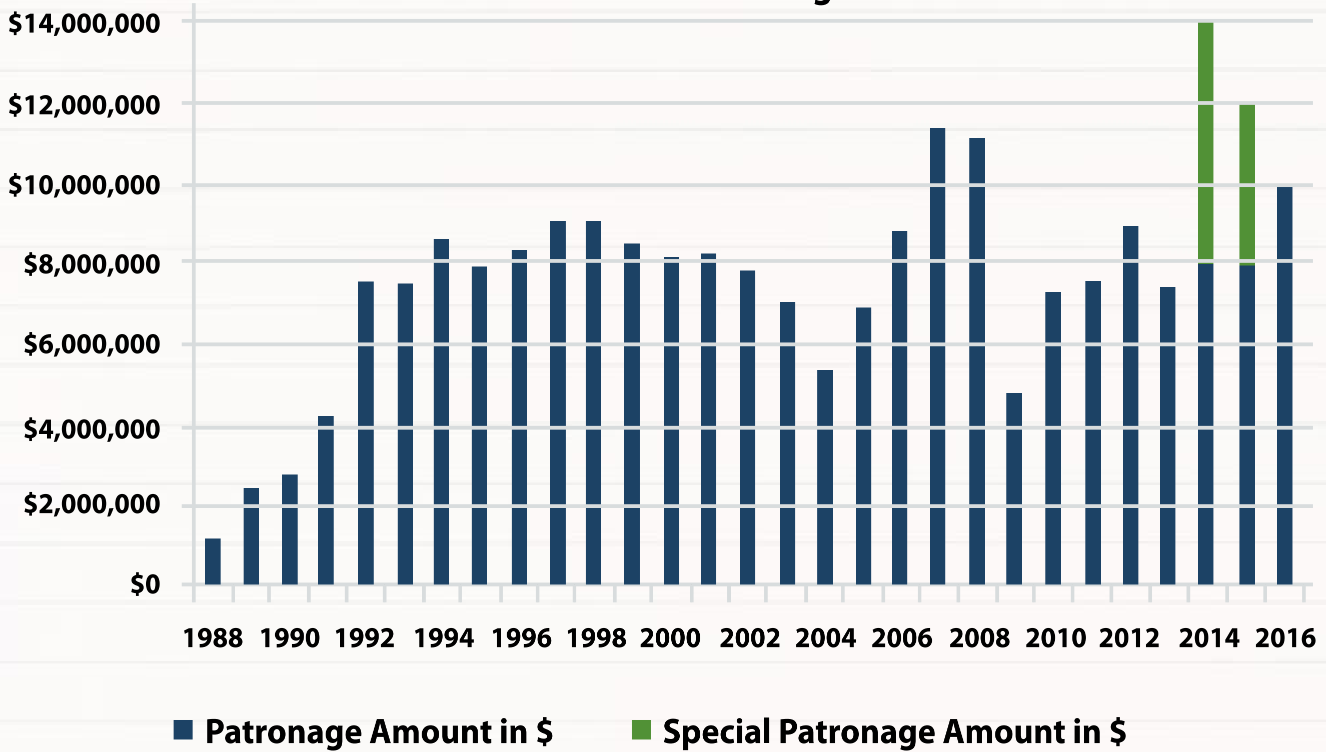
Brad Cornelius

As we reflect on the past year, it presented challenges and opportunities for the Association and southeastern North Carolina. 2016 was another year of depressed commodity prices, and we experienced a major weather event with Hurricane Matthew. On a very positive note, it was a year of celebrating the Farm Credit System's centennial and the long, successful history we have with our customer-owners and their families. Cape Fear Farm Credit has stood the test of time, because we have served the needs of farmers and rural America for 100 years. Celebrating this milestone is a success many organizations never experience, and one that we do not take lightly. We owe all of our success to the customer-owners we serve, with a special thanks to our employees who come to work ready to meet your needs.

The Association experienced another successful year in 2016, and I would like to highlight a few of the accomplishments you will see in this annual report:

- Strong net income of $20.2 million
- Net loan volume grew to approximately $852 million
- Cash patronage of $10 million will be distributed to customer-owners
- Permanent Capital over 22% continues to be strong





We remain an organization committed to serving the needs of our customer-owners and the rural communities we serve. Although some sectors of our portfolio are experiencing stress, as we look to the next 100 years of service, we see a bright future for agriculture, our current customer-owners, and future generations. As always, we appreciate your business and loyalty to Cape Fear Farm Credit, and we continue to be well positioned to meet the challenges and opportunities in partnership with you. As we celebrate our strong past, we look forward to an even stronger future.

Brad Cornelius,
Chief Executive Officer

Strong past. Stronger Future.

The year 2016 marked a monumental accomplishment for Cape Fear Farm Credit and the Farm Credit System. Farm Credit celebrated 100 years of serving agriculture and those involved in this important industry. It was a year of celebration, reflection, and planning for the future.

Take a stroll down memory lane to see the major milestones that have shaped Farm Credit into the organization you know it today.

July 17
1916

President Wilson signed legislation creating the Federal Land Bank System.

March 4
1923

The Agricultural Credit Act of 1923 extended service and provided for short-term and intermediate operating credit, while the System strengthened its funding capability.

June 16
1933

In the midst of the Great Depression, even greater for agriculture, the System was rescued and expanded, which helped save countless farms.

December 10
1941

Three days after Pearl Harbor, officials of the Banks for Cooperatives met to set new priorities – the entire Farm Credit System prepared to fight inflation and feed a nation at war.

December 4
1953

The Farm Credit Act of 1953 made the Farm Credit Administration an agency of the executive branch and set the System on a path toward independence.

December 2

1971

Comprehensive legislation completely updated the charter of the newly borrower-owned system, broadening its lending authority.

December 24

1980

The Farm Credit Act amendments of 1980 broadened the System's lending authority, provided for the creation of service organizations, and recognized the System's commitment to young, beginning, and small farmers.

January 6

1988

In the midst of an extended farm crisis, the Agricultural Credit Act of 1987 provided federal financial assistance and required the System to reorganize.

October 1

1999

After more than a decade of experimentation, the "Parent Agricultural Credit Association" arrangement was developed, setting the pattern for subsequent mergers on the Association level.

June 10

2005

Twenty years after the peak of the farm crisis, the System repaid the last of the federal capital provided during the emergency, returning to fully borrower-owned status.

July 17

2016

Marked the Farm Credit System's centennial of serving agriculture and rural America.

We have seen agriculture change in a dramatic way over the last 100 years. One of the greatest changes has been the improvements in technology related to equipment as well as the plants and animals produced. We have seen row crop farming transition from mules to self-driving tractors. Improved genetics has produced great yields, disease and pest resistance, and an ability to meet consumer demand in an ever-growing world population. We have seen the livestock industry revolutionized from the days when farmers had a few animals on the ground to the vertically integrated system we know today. Tobacco has played a major role in the history of North Carolina agriculture and has been the backbone of our agricultural heritage. The evolution of the blueberry industry in North Carolina happened right in the heart of Cape Fear Farm Credit's territory in the late 1920's, and we have seen that industry expand over time with advances in technology. Farmers are utilizing diversification, business planning, and financial management to allow for greater risk mitigation.

Although there have been many changes over the decades, the agriculture industry is still filled with farmers who love the land, providing for their families, and doing their part to help feed and clothe the world. The next 100 years will look drastically different as well, and Cape Fear Farm Credit is committed to providing support to our farmers to meet the opportunities and challenges that the next century will bring. Together we have celebrated a successful legacy, and we look forward to partnering with you for an even stronger future.

Bringing Value

Loans for Your Farm

- Equipment and vehicles
- Operating expenses
- Poultry and livestock facilities
- Farm improvements
- Barns, stables, sheds

Loans for Your Agribusiness

- Nurseries and greenhouses
- Poultry and livestock operations
- Gins and processing facilities
- Timber and sawmill operations
- Farm-related businesses

Loans for Your Home and Place in the Country

- Lots
- Homes
  - Home construction
  - Purchases and refinancing
  - Remodeling and home improvements
  - Refinances
- Horses, cattle and other livestock
- Livestock and utility trailers

More than just loans...

Cape Fear Farm Credit wants to help you be successful. Cape Fear offers the following services and conveniences:

Financially-Related Services

Mortgage, life and disability insurance — protect what is important to you.

E-Commerce

AccountAccess

Conveniently manage your account information 24/7 from your computer or mobile device.

Money Management Tools

FastCash

Quick and easy fund transfers from your line of credit loan into your personal or business checking account at no cost to you.

AutoDraft

Hassle-free, automatic drafting of your loan payments saves you time and money.

AutoBorrow

A cash management tool that links your Cape Fear Farm Credit loan to your business checking account.

Other Services

Farm Credit *EXPRESS*

Offered at most local equipment dealers.

Leases

Trucks, equipment, buildings and more.

Short and Long-term Group Life Insurance

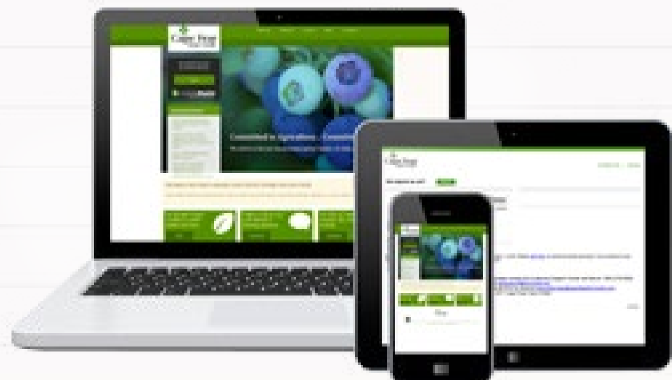
A variety of affordable options.

Educational Programs

Offered throughout the year to our members .

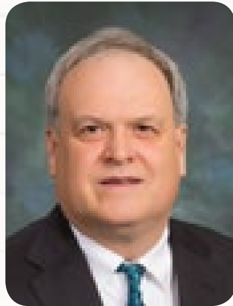
Industry News

Market news, data analysis, and other tools to keep ahead of the curve.



Board of Directors

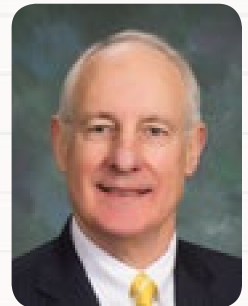
Gary Hendrix
(Vice Chairman)
Raeford, NC



Al Bain
Outside Director
Lillington, NC

David Gooden
Elizabethtown, NC

Tony Grant
Outside Director
Columbia, SC



Glenn Harder
Outside Director
Raleigh, NC

Adrian Locklear
Maxton, NC

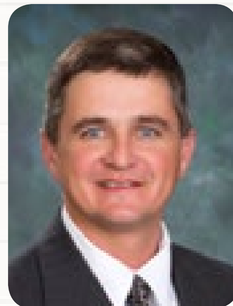
Paul Maguire
Roseboro, NC

Morris Murphy
Albertson, NC

Jon Pope
Coats, NC

Gary Rouse
Outside Director
Clinton, NC

Mitchell Sessoms
Roseboro, NC



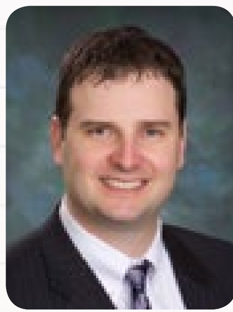
Michael T. (Bo) Stone
Rowland, NC

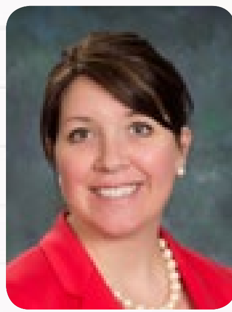
Alfred Wooten
Burgaw, NC

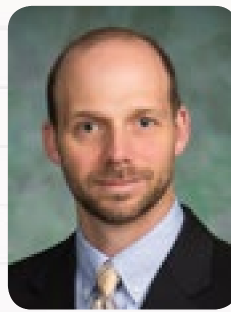
*F.A. (Andy) Lowrey completed his appointed term as an outside director on February 16, 2017.

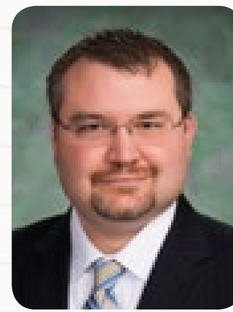
2017 Senior Leadership Team

Brad Cornelius
Chief Executive Officer


Evan Kleinhans
Chief Financial Officer


Skipper Jones
Administrative Officer


Pierce Hodnette
Chief Lending Officer


Geoff Manderewicz
Chief Credit Officer

Cape Fear Farm Credit Employees (as of March 1, 2017)

Burgaw Branch
Cale Horne
Debbie Bradshaw
Gail Lee

Clinton Branch
Mike Carter
Gloria Chalk
Sylvia Fryar
Tonya Hobbs
Dennis Honrine
Gena Tew

Elizabethtown Branch
Glenn Walters
Jeanne Fields
Paula Roberts
Jake Suggs
Linda Wilson

Fayetteville Branch
Brian Johnson
Summer Howard
Ashley Such

Harnett County Branch
Stuart Betts
Tracy Armstrong
Deneice Core
Karen Powell
Denise Stancil
Glenda Tew

Kenansville Branch
Gerald Wilson
Patrick Abrams
Shannon Bell
Kim Hunter
Daniel Outlaw
Debbie Raynor
Shannon Scott

Lumberton Branch
Kevin Kinlaw
Vickie Edwards
T.C. Hall
Carmin Russ
Vickie Walters

Raeford Branch
Brian Johnson
Suzanne Malloy
Sharon Nichols

Whiteville Branch
Kevin Kinlaw
Andy Coates
Ginny Martin
Becky Thompson
Candy Ward

Capital Markets Department
Randy Pope
Brook Gillis
Cliff Kilpatrick
Amy Tyndall

Appraisal Department
John Hales
Amy Capra
Matthew Edwards
Jared Johnson
Graham Smith
Ismael Avila

Administrative
Brad Cornelius
Melissa Boney
Kim Bunce
Nancy Byrd
Elise Canaski
Darryl Carter
Jay Darden
Dana Desien
Chuck Hester
Pierce Hodnette
Ronda Hoffman
Skipper Jones
Cathy Keane
Brandon Kelly
Brentley King
Evan Kleinhans
Will Maxwell
Tina Melvin-Ford
Christy Moore
Katie Neal
John Patterson
Kristina Quinn
Brian Smith
Janet Smith
Jill Smith
Sharon Smith
Courtney Stewart
Sarah Temple
Michael Thomas
Diana Winningham
Geoff Manderewicz

Branch Locations

Burgaw
811 South Walker Street
910-259-5481

Clinton
1780 Southeast Boulevard
910-592-8121

Dunn
400 West Broad Street
910-892-4065

Elizabethtown
108 North Poplar Street
910-862-4536

Fayetteville
333 East Russell Street
910-483-1404

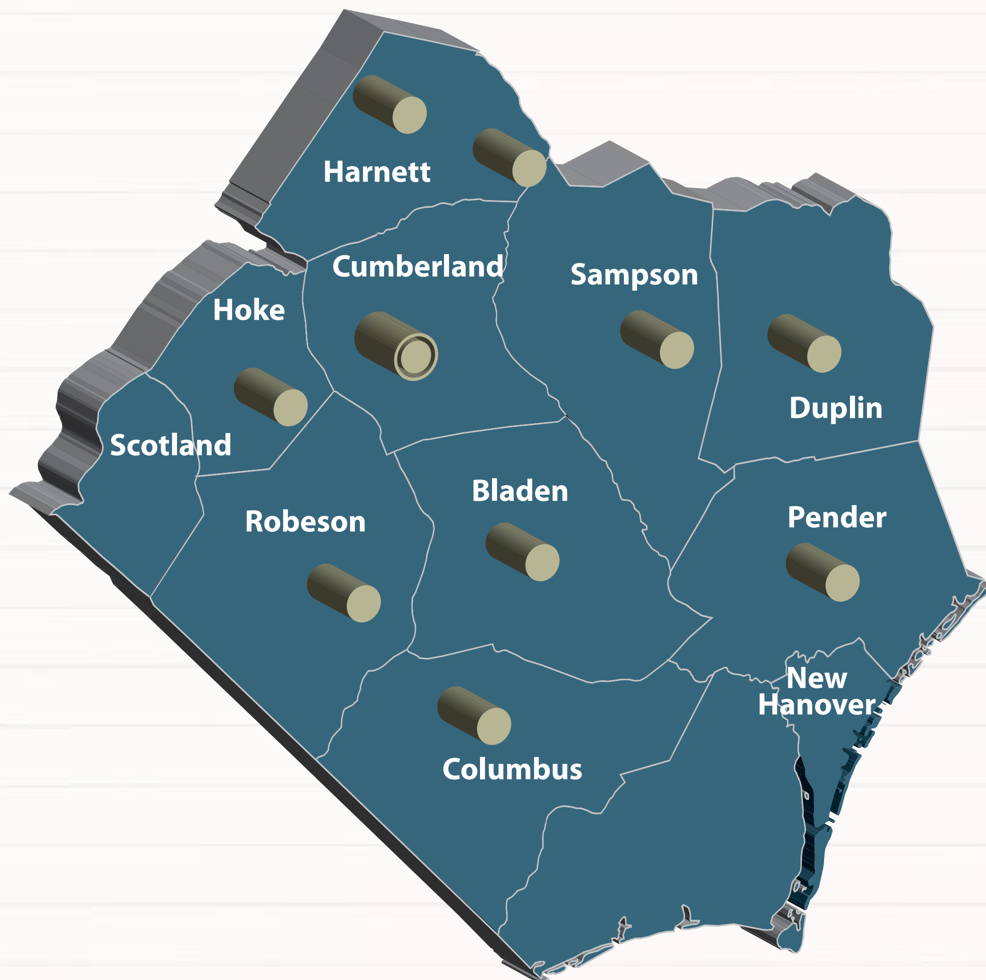
Kenansville
127 Beasley Street
910-296-1776

Lillington
105 East Front Street
910-893-8318

Lumberton
1902 North Cedar Street
910-738-8181

Raeford
331 South Main Street
910-875-6181

Whiteville
300 Liberty Street
910-642-8041



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Report of Management

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

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

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

The consolidated financial statements, in the opinion of management, fairly present the financial condition of the Association. The undersigned certify that we have reviewed the 2016 Annual Report of Cape Fear Farm Credit, ACA, that the report has been prepared under the oversight of the Audit Committee of the Board of Directors and in accordance with all applicable statutory or regulatory requirements, and that the information contained herein is true, accurate, and complete to the best of our knowledge and belief.

Gary Hendrix
Vice Chairman of the Board

Brad Cornelius
Chief Executive Officer

Evan J. Kleinhans
Chief Financial Officer

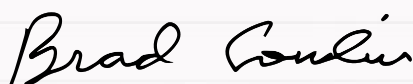
March 13, 2017

Report on Internal Control Over Financial Reporting

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

The Association's management has completed an assessment of the effectiveness of internal control over financial reporting as of December 31, 2016. In making the assessment, management used the framework in *Internal Control — Integrated Framework (2013)*, promulgated by the Committee of Sponsoring Organizations of the Treadway Commission, commonly referred to as the "COSO" criteria.

Based on the assessment performed, the Association's management concluded that as of December 31, 2016, the internal control over financial reporting was effective based upon the COSO criteria. Additionally, based on this assessment, the Association determined that there were no material weaknesses in the internal control over financial reporting as of December 31, 2016.



Brad Cornelius
Chief Executive Officer

Evan J. Kleinhans
Chief Financial Officer

March 13, 2017

Consolidated Five-Year Summary Of Selected Financial Data

(dollars in thousands)	December 31, 2016	2015	2014	2013	2012
Balance Sheet Data					
Cash	**$ 3,063**	$ 3,882	$ 3,107	$ 4,567	$ 3,959
Investment securities	**4,209**	7,366	4,647	7,220	5,556
Loans	**859,557**	830,254	789,693	762,528	761,424
Allowance for loan losses	**(7,738)**	(7,117)	(5,378)	(6,057)	(7,425)
Net loans	**851,819**	823,137	784,315	756,471	753,999
Investments in other Farm Credit institutions	**9,951**	9,592	9,360	9,396	9,418
Other property owned	**1,876**	1,356	4,976	4,931	7,484
Other assets	**24,605**	25,090	27,180	33,420	31,093
Total assets	**$ 895,523**	$ 870,423	$ 833,585	$ 816,005	$ 811,509
Notes payable to AgFirst Farm Credit Bank*	**$ 683,642**	$ 667,938	$ 636,579	$ 633,872	$ 646,145
Accrued interest payable and other liabilities with maturities of less than one year	**24,214**	25,062	27,222	22,325	20,819
Total liabilities	**707,856**	693,000	663,801	656,197	666,964
Protected borrower stock	**3**	3	3	4	34
Capital stock and participation certificates	**2,454**	2,411	2,406	2,433	2,445
Retained earnings					
Allocated	**90,846**	83,467	77,931	69,210	55,494
Unallocated	**94,664**	91,849	89,784	88,459	86,915
Accumulated other comprehensive income (loss)	**(300)**	(307)	(340)	(298)	(343)
Total members' equity	**187,667**	177,423	169,784	159,808	144,545
Total liabilities and members' equity	**$ 895,523**	$ 870,423	$ 833,585	$ 816,005	$ 811,509
Statement of Income Data					
Net interest income	**$ 24,604**	$ 24,693	$ 24,336	$ 24,466	$ 25,546
Provision for loan losses	**892**	622	174	1,367	1,247
Noninterest income (expense), net	**(3,516)**	(4,469)	(75)	(103)	(5,202)
Net income	**$ 20,196**	$ 19,602	$ 24,087	$ 22,996	$ 19,097
Key Financial Ratios					
Rate of return on average:					
Total assets	**2.31%**	2.30%	2.95%	2.86%	2.39%
Total members' equity	**10.83%**	10.96%	14.16%	14.99%	13.28%
Net interest income as a percentage of average earning assets	**2.89%**	3.00%	3.09%	3.14%	3.34%
Net (chargeoffs) recoveries to average loans	**(0.032)%**	0.136%	(0.109)%	(0.357)%	(0.097)%
Total members' equity to total assets	**20.96%**	20.38%	20.37%	19.58%	17.81%
Debt to members' equity (:1)	**3.77**	3.91	3.91	4.11	4.61
Allowance for loan losses to loans	**0.90%**	0.86%	0.68%	0.79%	0.98%
Permanent capital ratio	**22.23%**	22.23%	23.30%	22.25%	20.66%
Total surplus ratio	**21.93%**	21.91%	22.96%	21.88%	20.41%
Core surplus ratio	**21.93%**	21.91%	22.96%	21.88%	20.41%
Net Income Distribution					
Estimated patronage refunds:					
Cash	**$ 10,000**	$ 12,000	$ 14,000	$ 7,500	$ 8,722
Nonqualified retained earnings	**7,807**	5,944	8,890	14,303	11,435

** General financing agreement is renewable on a one-year cycle. The next renewal date is December 31, 2017.*

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

(dollars in thousands, except as noted)

GENERAL OVERVIEW

The following commentary summarizes the financial condition and results of operations of Cape Fear Farm Credit, ACA, (Association) for the year ended December 31, 2016 with comparisons to the years ended December 31, 2015 and December 31, 2014. This information should be read in conjunction with the Consolidated Financial Statements, Notes to the Consolidated Financial Statements and other sections in this Annual Report. The accompanying Consolidated Financial Statements were prepared under the oversight of the Audit Committee of the Board of Directors. For a list of the Audit Committee members, refer to the "Report of the Audit Committee" reflected in this Annual Report. Information in any part of this Annual Report may be incorporated by reference in answer or partial answer to any other item of the Annual Report.

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

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

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

Copies of the Association's Annual and Quarterly reports are also available upon request free of charge on the Association's website, ***www.capefearfarmcredit.com***, or by calling 1-800-368-5819, extension 3243, or writing Evan J. Kleinhans, Cape Fear Farm Credit, P.O. Box 2405, Fayetteville, NC, 28302. The Association prepares an electronic version of the Annual Report, which is available on the website, within 75 days after the end of the fiscal year and distributes the Annual Reports to shareholders within 90 days after the end of the fiscal year. The Association prepares an electronic version of the Quarterly Report, which is available on the internet, within 40 days after the end of each fiscal quarter, except that no report needs to be prepared for the fiscal quarter that coincides with the end of the fiscal year of the Association.

FORWARD LOOKING INFORMATION

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

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

AGRICULTURAL OUTLOOK

The following United States Department of Agriculture (USDA) analysis provides a general understanding of the U.S. agricultural economic outlook. However, this outlook does not take into account all aspects of the Association's business. References to USDA information in this section refer to the U.S. agricultural market data and are not limited to information/data for the Association.

The February 2017 USDA forecast estimates 2016 farmers' net cash income, which is a measure of the cash income after payment of business expenses, at $91.9 billion, down $12.8 billion from 2015 and down $11.3 billion from its 10-year average of $103.2 billion. The decline in net cash income in 2016 was primarily due to decreases in livestock receipts of $21.7 billion and cash farm-related income of $3.7 billion, partially offset by a decrease in cash expenses of $8.3 billion.

The February 2017 USDA forecast for the farm economy, as a whole, forecasts 2017 farmers' net cash income to increase to $93.5 billion, a $1.6 billion increase from 2016, but $9.7 billion below the 10-year average. The forecasted increase in farmers' net cash income for 2017 is primarily due to an expected increase in cash farm-related income of $3.7 billion, partially offset by a decrease in crop receipts of $1.0 billion and an increase in cash expenses of $700 million.

The following table sets forth the commodity prices per bushel for certain crops, by hundredweight for hogs, milk, and beef cattle, and by pound for broilers and turkeys from December 31, 2013 to December 31, 2016:

Commodity	12/31/16	12/31/15	12/31/14	12/31/13
Hogs	$43.10	$42.80	$64.30	$61.50
Milk	$18.80	$17.30	$20.40	$22.00
Broilers	$0.48	$0.47	$0.58	$0.56
Turkeys	$0.74	$0.89	$0.73	$0.69
Corn	$3.33	$3.65	$3.79	$4.41
Soybeans	$9.64	$8.76	$10.30	$13.00
Wheat	$3.91	$4.75	$6.14	$6.73
Beef Cattle	$111.00	$122.00	$164.00	$130.00

The USDA's income outlook varies depending on farm size and commodity specialties. The USDA classifies all farms into four primary categories: small family farms (gross cash farm income (GCFI) less than $350 thousand), midsize family farms (GCFI between $350 thousand and under $1 million), large-scale family farms (GCFI of $1 million or more), and nonfamily farms (principal operator or individuals related to the operator do not own a majority of the business). Approximately 99 percent of U.S. farms are family farms and the remaining 1 percent are nonfamily farms. The family farms produce 89 percent of the value of agricultural output and the nonfamily farms produce the remaining 11 percent of agricultural output. The small family farms represent about 90 percent of all U.S. farms, hold 57 percent of farm assets and account for 24 percent of the value of production. Approximately 65 percent of production occurs on 9 percent of family farms classified as midsize or large-scale.

According to the USDA February 2017 forecast, farm sector equity (assets minus debt) is expected to decline 2.1 percent in 2017 to $2.44 trillion, the third consecutive year of declining equity after a record $2.60 trillion in 2014. Farm sector debt is expected to rise 5.2 percent to $395 billion in 2017, while a 1.1 percent decline is anticipated in the market value of farm sector assets to $2.84 trillion. Farm real estate accounts for about 84 percent of farm sector assets and the 2017 forecast anticipates a slight decline in real estate values. This reflects falling farm profit margins, increased interest rates, and more restrictive debt terms.

Two measures of the financial health of the agricultural sector used by the USDA are the farm sector's debt-to-asset and debt-to-equity ratios. As a result of the decline in farm assets and continued increase in farm debt, these ratios are forecast to rise in 2017 to 13.9 percent and 16.2 percent from 13.1 percent and 15.1 percent in 2016. The debt-to-asset ratio has increased for the fifth straight year but is still well below the all-time highs of over 20 percent in the 1980s.

As estimated by the USDA in February 2017, the System's market share of farm business debt (defined as debt incurred by those involved in on-farm agricultural production) increased to 40.6 percent at December 31, 2015 (the latest available data), as compared with 39.6 percent at December 31, 2014.

In general, agriculture, during the past several years, experienced favorable economic conditions driven by high commodity and livestock prices and increased farmland values during this period. To date, the Association's financial results have remained favorable as a result of these favorable agricultural conditions. Production agriculture; however, remains a cyclical business that is heavily influenced by commodity prices and various other factors. In an environment of less favorable economic conditions in agriculture, including extensive and extended drought conditions, and without sufficient government support programs, including USDA-sponsored crop insurance programs, the Association's financial performance and credit quality measures would likely be negatively impacted. Conditions in the general economy remain more volatile given the state of the global economy. Certain agriculture sectors, as described more fully in this *Management's Discussion and Analysis*, recently have experienced significant financial stress and could experience additional financial stress in the near future, which could have a negative financial impact on the Association. Any negative impact from these less favorable conditions should be lessened by geographic and commodity diversification and the influence of off-farm income sources supporting agricultural-related debt. However, agricultural borrowers who are more reliant on off-farm income sources may be more adversely impacted by a weakened general economy.

CRITICAL ACCOUNTING POLICIES

The consolidated financial statements are reported in conformity with accounting principles generally accepted in the United States of America. Our significant accounting policies are critical to the understanding of our results of operations and financial position because some accounting policies require us to make complex or subjective judgments and estimates that may affect the value of certain assets or liabilities. We consider these policies critical because management must make judgments about matters that are inherently uncertain. For a complete discussion of significant accounting policies, see Note 2, *Summary of Significant Accounting Policies*, of the Notes to the Consolidated Financial Statements. The following is a summary of certain critical policies.

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

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

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

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

- *Pensions* — The Bank and its related Associations participate in defined benefit retirement plans. These plans are noncontributory and benefits are based on salary and years of service. In addition, the Bank and its related Associations also participate in defined contribution retirement savings plans. Pension expense for all plans is recorded as part of salaries and employee benefits. Pension expense for the defined benefit retirement plans is determined by actuarial valuations based on certain assumptions, including expected long-term rate of return on plan assets and discount rate. The expected return on plan assets for the year is calculated based on the composition of assets at the beginning of the year and the expected long-term rate of return on that portfolio of assets. The discount rate is used to determine the present value of our future benefit obligations. The discount rate for 2016 was selected by reference to analysis and yield curves of the plans' actuary and industry norms.

ECONOMIC CONDITIONS

North Carolina's economy continues to improve as labor markets have strengthened, household conditions have improved, and housing market indicators have moved in a positive direction. The Cape Fear region continues to have slower economic growth in comparison to other parts of the state and country. North Carolina's unemployment rate decreased from 5.7% in December 2015 to 5.1% in December 2016 and is above the national rate of 4.7%. The unemployment rate in Southeastern North Carolina is higher than the state average. Of the 12 counties in Southeastern North Carolina that the Association serves, 33.3% are ranked by the North Carolina Department of Commerce as Tier 1, or most distressed in terms of economic wellbeing, 41.7% are ranked as Tier 2, or moderately distressed, and 25.0% are ranked as Tier 3, or least distressed.

Overall, the farm sector profitability is expected to decline in 2016 caused by modest commodity prices, weather conditions including Hurricane Matthew, livestock disease outbreaks, and farm expenses falling more slowly than commodity prices. Liquidity in the balance sheet has eroded for many farmers and created the need for debt restructuring by some.

The swine and poultry segments, the largest commodity exposures in our portfolio, are profitable due to lower feed costs, strong domestic demand, and sizable exports. Significant poultry sector expansion is occurring in the Cape Fear region. Disease outbreaks have caused production interruptions for livestock farmers and are being managed by proper biosecurity. Production levels have created large supplies of hogs and poultry. A strong US dollar is a potential threat as the export market plays a significant role in maintaining current price levels.

Crop production, the third largest portion of the loan portfolio, has suffered from adverse weather conditions, modest commodity prices, and farm expenses falling slower than commodity prices during 2016. Input costs are high for most crops. Commodity prices are forecast to remain near current levels in 2017 with peanuts being an exception. Tobacco production contracts are expected to be cut again in 2017.

Farm real estate values declined approximately 1% during 2016, and farm asset values have the potential to decrease further in 2017 with more farm equipment and real estate offered for sale.

Credit quality reflects the challenges facing our customer-owners with 91.18% rated acceptable, which is a slight decline from last year. Loans classified as other assets especially mentioned, currently collectible but exhibiting some potential weakness, increased from last year to 5.32%, while loans classified as substandard, those exhibiting serious weaknesses in repayment capacity, equity and/or loan performance, improved slightly from last year to 3.50%. Although management expects credit quality to remain stressed during 2017, Cape Fear Farm Credit's financial performance continues to be strong.

Our Association's loan officers, with the support and direction of our senior leadership team, have successfully navigated the challenges of operating in difficult economic conditions. We continue to adhere to our mission to be the lender of choice to all of agriculture and our rural communities. Our expertise in agricultural and rural lending allows us to help our customer-owners through the fluctuations and uncertainties that are prevalent in the agricultural industry today.

LOAN PORTFOLIO

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

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

Loan Type	December 31, 2016		2015		2014	
	(dollars in thousands)					
Real estate mortgage	$ 527,783	61.40%	$ 526,365	63.40%	$ 502,448	63.63%
Production and intermediate-term	287,275	33.42	259,901	31.31	247,835	31.39
Processing and marketing	21,776	2.53	28,833	3.47	25,853	3.27
Loans to Cooperatives	6,376	0.74	249	0.03	250	0.03
Rural residential real estate	4,877	0.57	5,503	0.66	4,267	0.54
Farm related business	4,023	0.47	6,376	0.77	5,641	0.71
International	3,257	0.38	–	–	–	–
Lease Receivable	2,962	0.35	–	–	–	–
Communication	952	0.11	2,751	0.33	3,123	0.40
Power and water/waste disposal	276	0.03	276	0.03	276	0.03
	$ 859,557	100.00%	$ 830,254	100.00%	$ 789,693	100.00%

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

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

Branch/State	December 31, 2016	2015	2014
Burgaw	6.36%	5.30%	5.21%
Clinton	14.48	14.37	16.66
Dunn	6.09	6.24	6.88
Elizabethtown	9.91	10.40	9.74
Fayetteville	3.04	2.90	3.35
Kenansville	21.24	20.65	20.78
Lillington	3.77	3.59	3.37
Lumberton	8.36	9.33	9.14
Raeford	5.78	5.37	5.75
Shallotte*	–	1.47	1.16
Whiteville	5.20	4.63	4.28
Capital Markets	6.48	5.52	4.34
Commercial	6.70	7.22	7.71
Bonds & Investments	0.03	.04	0.05
Special Asset Management	2.56	2.97	1.58
	100.00%	100.00%	100.00%

**Upon closure of the Shallotte branch office in September 2016, all loan assets were transferred to the Whiteville and Burgaw branch offices.*

Commodity and industry categories are based upon the Standard Industrial Classification system published by the federal government. The system is used to assign commodity or industry categories based upon the largest agricultural commodity of the customer.

The major commodities in the Association's loan portfolio are shown below. The predominant commodities are Swine, Chickens, and Field & Row Crops, which constitute 66 percent of the entire portfolio.

Commodity Group	December 31, 2016		2015		2014	
	(dollars in thousands)					
Swine	$ 255,024	30%	$ 247,738	30%	$ 241,697	31%
Chickens	194,295	23	180,155	22	172,480	22
Field & Row Crops	110,968	13	109,047	13	101,804	13
Landlords	51,474	6	55,929	7	56,250	7
Timber, Sawmills, & Paper	46,928	5	42,895	5	34,349	4
Tobacco	46,672	5	51,578	6	43,435	6
Fruits, Vegetables, & Nuts	42,554	5	39,328	5	34,717	4
Other	34,459	4	27,369	3	22,495	3
Turkeys	24,623	3	18,215	2	19,308	2
Livestock	21,367	2	22,230	3	24,598	3
Cotton	19,356	2	21,926	2	25,779	3
Rural Home	6,611	1	6,750	1	5,873	1
Non-Farm & Miscellaneous	5,226	1	7,094	1	6,908	1
Total	$ 859,557	100%	$ 830,254	100%	$ 789,693	100%

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

The Association had a 5.47% increase in gross loan volume for the twelve months ended December 31, 2016, in comparison with the same period of 2015. Purchased accruing loans increased by $11,269 or 24.33% in 2016 from 2015. The Association had a $24,241 increase in sold volume which

equated to a 3.75% increase in net accruing volume in 2016 in comparison with 2015.

During 2016, the Association continued activity in the selling of loan participations within the System. Selling participation loans provides a means for the Association to spread credit concentration risk and realize interest and fee income which may strengthen our capital position. The Association continued strict guidelines for purchases in 2016.

Loan Participations:	December 31, 2016	2015	2014
	(dollars in thousands)		
Participations Purchased – FCS Institutions	$ 51,673	$ 45,898	$ 33,734
Participations Purchased – Non-FCS Institutions	5,849	520	621
Participations Sold	(213,714)	(188,279)	(173,542)
Total	$ (156,192)	$ (141,861)	$ (139,187)

The Association did not have any loans sold with recourse, retained subordinated participation interests in loans sold, or interests in pools of subordinated participation interests for the period ended December 31, 2016.

The Association continued to sell qualified long-term mortgage loans into the secondary market in 2016. For the period ended December 31, 2016, the Association originated loans for resale totaling $1,861 which is a decrease of $614 or 24.81% from the 2015 amount of $2,475 originated. Of the $1,861 originated in 2016, $1,861 was sold into the secondary market and no loans were held for sale at year end waiting processing and funding. The Association originated $2,475 loans for resale in 2015, $2,475 was sold into the secondary market, and no loans were held for sale at year end waiting processing and funding. The Association originated $2,179 loans for resale in 2014, $2,179 was sold into the secondary market, and no loans were held for sale at year end waiting processing and funding.

MISSION RELATED INVESTMENTS

During 2005, the FCA initiated an investment program to stimulate economic growth and development in rural areas. The FCA outlined a program to allow System institutions to hold such investments, subject to approval by the FCA on a case-by-case basis. FCA approved the Rural America Bonds pilot program and the Tobacco Buyout Program under the Mission Related Investments umbrella, as described in the following.

Effective December 31, 2014, the FCA concluded each pilot program approved as part of the Investment in Rural America program. Each institution participating in such programs may continue to hold its investment through the maturity dates for the investments, provided the institution continues to meet all approval conditions. Although the pilot programs have concluded, the FCA can consider future requests on a case-by-case basis.

In October 2005, the FCA authorized AgFirst and the Associations to make investments in Rural America Bonds under a three-year pilot period. Rural America Bonds may include debt obligations issued by public and private enterprises, corporations, cooperatives, other financing institutions, or rural lenders where the proceeds would be used to support agriculture, agribusiness, rural housing, or economic development, infrastructure, or community development and revitalization projects in rural areas. Examples include investments that fund value-added food and fiber processors and marketers, agribusinesses, commercial enterprises that create and maintain employment opportunities in rural areas, community services, such as schools, hospitals, and government facilities, and other activities that sustain or revitalize rural communities and their economies. The objective of this pilot program was to help meet the growing and diverse financing needs of agricultural enterprises, agribusinesses, and rural communities by providing a flexible flow of money to rural areas through bond financing. These bonds are classified as Loans or Investments on the Consolidated Balance Sheets depending on the nature of the investment. As of December 31, 2016, the Association had $4,444 in Rural America Bonds of which $235 of these instruments were classified as Loans on the Consolidated Balance Sheets and the other $4,209 were classified as Investment Securities. As of December 31, 2015, the Association had $7,697 in Rural America Bonds of which $331 of these instruments were classified as Loans and the other $7,366 were classified as Investment Securities. As of December 31, 2014, the Association had $5,026 in Rural America Bonds of which $379 of these instruments were classified as Loans and the other $4,647 were classified as Investment Securities.

On October 22, 2004, Congress enacted the "Fair and Equitable Tobacco Reform Act of 2004" (Tobacco Act) as part of the "American Jobs Creation Act of 2004." The Tobacco Act repealed the Federal tobacco price support and quota programs, provided for payments to tobacco "quota owners" and producers for the elimination of the quota and included an assessment mechanism for tobacco manufacturers and importers to pay for the buyout. Tobacco quota holders and producers received equal annual payments through 2014 under a contract with the Secretary of Agriculture. The Tobacco Act also included a provision that allowed the quota holders and producers to assign to a "financial institution" the right to receive the contract payments (Successor-in-Interest Contracts (SIIC)) so that they may obtain a lump sum or other payment. On April 4, 2005, the United States Department of Agriculture (USDA) issued a Final Rule implementing the "Tobacco Transition Payment Program" (Tobacco Buyout). At December 31, 2016, 2015, and 2014 the Association had $0 in SIIC outstanding. The final payment under this program was received in January 2014.

CREDIT RISK MANAGEMENT

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

- Character – borrower integrity and credit history
- Capacity – repayment capacity of the borrower based on cash flows from operations or other sources of income
- Collateral – protection for the lender in the event of default and a potential secondary source of repayment

- Capital – ability of the operation to survive unanticipated risks
- Conditions – intended use of the loan funds

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

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

- Acceptable – Assets are expected to be fully collectible and represent the highest quality.
- Other Assets Especially Mentioned (OAEM) – Assets are currently collectible but exhibit some potential weakness.
- Substandard – Assets exhibit some serious weakness in repayment capacity, equity, and/or collateral pledged on the loan.
- Doubtful – Assets exhibit similar weaknesses to substandard assets. However, doubtful assets have additional weaknesses in existing facts, conditions and values that make collection in full highly questionable.
- Loss – Assets are considered uncollectible.

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

Credit Quality	2016	2015	2014
Acceptable & OAEM	96.50%	96.06%	96.37%
Substandard	3.50%	3.94%	3.63%
Doubtful	–%	–%	–%
Loss	–%	–%	–%
Total	100.00%	100.00%	100.00%

The Association monitors and manages risk concentrations to safeguard the investment of its stockholders. Risk concentrations can arise from:

- the collective exposure of loan(s) to a single obligor or group of obligors;
- a group of loans in which the primary repayment source is dependent upon a common affiliated party such as a livestock integrator, a marketing cooperative, a specialized buying station, etc.;
- a group of loans whose primary repayment source is dependent upon a specific commodity or industry;
- financial entities failing to meet their contractual obligations to the Association, referred to as financial counterparty risk.

The tools for managing these risks include financial monitoring of the risk source, proper reserve and capital levels, loan participations and cooperative lending, government guarantees, standby loan guarantees issued by other financial institutions, and periodic stress testing of the Association's portfolio.

The Association maintains a standby loan guarantee agreement with Farmer Mac, a separate entity of the Farm Credit System, to guarantee a pool of loans. Under the terms of the agreement, Farmer Mac is obligated to purchase loans that default and limit the Association's maximum loss potential to $4,000. During 2016, the Association added 163 additional loans totaling $39,765 to this guarantee pool. This standby guarantee agreement reduced the Association's risk caused by concentrations in certain industries and certain affiliated parties. As of December 31, 2016, the balance of loans guaranteed in this pool was $58,123. The balance of loans guaranteed in this pool for years ended in 2015 and 2014 was $40,982 and $62,056, respectively. No losses have been recognized on the Farmer Mac pool in 2016, 2015 or 2014.

The Association also utilizes government guarantees to help reduce risk on individual loan relationships and to help manage concentration risk. As of the year ended December 31, 2016, the balance of loans secured by a government guarantee was $64,498. The balance of loans secured by a government guarantee for the years ended in 2015 and 2014 was $70,905 and $75,962, respectively.

Nonperforming Assets

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

	December 31,		
High-risk Assets	**2016**	**2015**	**2014**
	(dollars in thousands)		
Nonaccrual loans	$ 19,662	$ 20,702	$ 11,240
Accruing restructured loans	3,546	3,448	1,283
Accruing bankruptcy loans	258	921	1,128
Accruing loans 90 days past due	–	–	–
Total high-risk loans	23,466	25,071	13,651
Other property owned	1,876	1,356	4,976
Total high-risk assets	$ 25,342	$ 26,427	$ 18,627
Ratios			
Nonaccrual loans to total loans	2.29%	2.49%	1.42%
High-risk assets to total assets	2.83%	3.04%	2.23%

Nonaccrual loans represent all loans where there is a reasonable doubt as to the collection of principal and/or future interest accruals, under the contractual terms of the loan. In substance, nonaccrual loans reflect loans where the accrual of interest has been suspended. Nonaccrual loans decreased $1,040 or 5.02% percent in 2016 in comparison with 2015. The contraction in nonaccrual volume is primarily attributed to payoffs, booking charge-offs, and transfers to other property

owned. Of the $19,662 in nonaccrual volume at December 31, 2016, $2,124 or 10.80%, compared to $2,574 or 12.43% and $4,388 or 39.04% at December 31, 2015 and 2014, respectively, was current as to scheduled principal and interest payments but did not meet all regulatory requirements to be transferred into accrual status.

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

Allowance for Loan Losses

The allowance for loan losses at each period end was considered by Association management to be adequate to absorb probable losses existing in and inherent to its loan portfolio.

The following table presents the activity in the allowance for loan losses for the most recent three years:

Allowance for Loan Losses Activity:	Year Ended December 31, 2016	2015	2014
	(dollars in thousands)		
Balance at beginning of year	$ 7,117	$ 5,378	$ 6,057
Charge-offs:			
Real estate mortgage	(551)	(13)	(150)
Production and intermediate-term	(136)	(59)	(955)
Energy	–	–	–
Agribusiness	–	(49)	–
Rural Residential Real Estate	–	–	–
Total charge-offs	(687)	(121)	(1,105)
Recoveries:			
Real estate mortgage	250	1,232	112
Production and intermediate-term	166	6	140
Energy	–	–	–
Agribusiness	–	–	–
Rural Residential Real Estate	–	–	–
Total recoveries	416	1,238	252
Net (charge-offs) recoveries	(271)	1,117	(853)
Provision for (reversal of allowance for) loan losses	892	622	174
Balance at end of year	$ 7,738	$ 7,117	$ 5,378
Ratio of net (charge-offs) recoveries during the period to average loans outstanding during the period	(0.032)%	0.136%	(0.109)%

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

Allowance for Loan Losses by Type	December 31, 2016	2015	2014
	(dollars in thousands)		
Production and intermediate-term	$ 3,386	$ 2,600	$ 2,032
Real estate mortgage	4,048	4,202	3,087
Agribusiness	217	227	184
Energy	2	2	2
Rural residential real estate	34	68	55
Communication	18	18	18
International	24	–	–
Lease Receivable	9	–	–
Total allowance	$ 7,738	$ 7,117	$ 5,378

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

Allowance for Loan Losses as a Percentage of:	December 31, 2016	2015	2014
Total loans	0.90%	0.86%	0.68%
Nonperforming loans	33.34%	29.47%	42.95%
Nonaccrual loans	39.36%	34.38%	47.85%

Please refer to Note 3, *Loans and Allowance for Loan Losses*, of the Notes to the Consolidated Financial Statements, for further information concerning the allowance for loan losses.

RESULTS OF OPERATIONS

Net Interest Income

Net interest income was $24.6 million, $24.7 million, and $24.3 million in 2016, 2015 and 2014, respectively. Net interest income is the difference between interest income and interest expense. Net interest income is the principal source of earnings for the Association and is impacted by volume, yields on assets and cost of debt. The effects of changes in average volume and interest rates on net interest income over the past three years are presented in the following table:

Change in Net Interest Income:

	Volume*	Rate	Nonaccrual Income	Total
	(dollars in thousands)			
12/31/16 - 12/31/15				
Interest income	$ 1,064	$ 179	$ (50)	$ 1,193
Interest expense	(291)	(990)	–	(1,281)
Change in net interest income	$ 773	$ (811)	$ (50)	$ (88)
12/31/15 - 12/31/14				
Interest income	$ 2,347	$ (1,079)	$ 414	$ 1,682
Interest expense	(778)	(548)	–	(1,326)
Change in net interest income	$ 1,569	$ (1,627)	$ 414	$ 356

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

Noninterest Income

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

Noninterest Income	For the Year Ended December 31, 2016	2015	2014	Percentage Increase/(Decrease) 2016/2015	2015/2014
	(dollars in thousands)				
Loan fees	$ 2,415	$ 2,130	$ 2,110	13.38%	1.00%
Fees for financially related services	124	141	50	(12.06)	182.00
Patronage refund from other Farm Credit Institutions	9,898	9,917	12,995	(0.19)	(23.69)
Insurance Fund refund	–	–	–	–	–
Other noninterest income	89	137	288	(35.04)	(52.43)
Total noninterest income	$ 12,526	$ 12,325	$ 15,443	1.63%	(20.19)%

Noninterest income increased $201 or 1.63% when comparing 2016 to 2015 and decreased $3,118 or 20.19% when comparing 2015 to 2014. The increase from 2015 to 2016 is primarily attributed to an increase in loan fees from $2,130 in 2015 to $2,415 in 2016. The decrease from 2014 to 2015 is primarily attributed to a decrease in the special patronage distribution from $7,532 in 2014 to $4,336 in 2015. The Association had a $133 decrease in special patronage from 2015 to 2016. This special patronage is nonrecurring and was declared by the AgFirst Board of Directors in 2014, 2015 and 2016 due to their very strong earnings and high capital levels. The Association had a $17 decrease in Fees for Financially Related Services from 2015 to 2016. Other noninterest income decreased to $89 in 2016 from $137 in 2015.

Noninterest Expense

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

Noninterest Expense	For the Year Ended December 31, 2016	2015	2014	Percentage Increase/(Decrease) 2016/2015	2015/2014
	(dollars in thousands)				
Salaries and employee benefits	$ 10,387	$ 10,269	$ 9,790	1.15%	4.89%
Occupancy and equipment	683	719	796	(5.10)	(9.67)
Insurance Fund premiums	1,074	782	690	37.34	13.33
(Gains) losses on other property owned, net	222	1,074	487	(79.33)	120.53
Other operating expenses	3,533	3,788	3,592	(6.73)	5.46
Total noninterest expense	$ 15,899	$ 16,632	$ 15,355	(4.41)%	8.32%

Salaries and employee benefits increased by $118 or 1.15% in 2016 as compared with 2015. Insurance Fund premiums increased 37.34% percent for the twelve months ended December 31, 2016 compared to the same period of 2015. The FCSIC set premiums at 16 basis points on adjusted insured debt outstanding for the first half of 2016 and 18 basis points on adjusted insured debt outstanding for the second half of 2016. In addition, there was a 10 basis point premium on the average principal outstanding of nonaccrual loans and any other-than-temporarily impaired investments. The Association recognized losses on Other Property Owned of $222 in 2016 compared to $1,074 for 2015 and $487 for 2014. The decrease in losses on Other Property Owned is primarily attributed to the loss associated with the sale of one large property in the fourth quarter of 2015. Please refer to Note 5, *Other Property Owned*, of the Notes to the Consolidated Financial Statements, for more information concerning Association Other Property Owned. Other Operating Expenses decreased by 6.73% in 2016 from 2015. The total decrease in noninterest expense in 2016 in comparision with 2015 is primarily a result of the decrease in losses on Other Property Owned. Total noninterest expense decreased $733 or 4.41% when comparing 2016 to 2015 and increased $1,277 or 8.32% when comparing 2015 to 2014.

Income Taxes

The Association recorded a provision for income taxes of $143 for the year ended December 31, 2016 as compared to a provision of $150 for 2015 and a provision of $150 for 2014. Refer to Note 2, *Summary of Significant Accounting Policies, Income Taxes*, and Note 12, *Income Taxes* of the Notes to the Consolidated Financial Statements, for more information concerning Association income taxes.

Key Results of Operations Comparisons

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

Key Results of Operations Comparisons	For the 12 Months Ended 12/31/16	12/31/15	12/31/14
Return on average assets	2.31%	2.30%	2.95%
Return on average members' equity	10.83%	10.96%	14.16%
Net interest income as a percentage of average earning assets	2.89%	3.00%	3.09%
Net (charge-offs) recoveries to average loans	(0.032)%	0.136%	(0.109)%

Cape Fear Farm Credit has enjoyed robust earnings in recent years with strong interest income as well as noninterest income. The Association has also experienced moderate and manageable loan volume growth over the last three years. Net charge-offs as a percentage of average loans have remained less than (1.0)% over the last three years, and the Association's net interest margin, while contracting slightly, has remained strong.

Our goal is to generate earnings sufficient to fund operations, adequately capitalize the Association, and achieve an adequate rate of return for our members. We also seek to attract and maintain high quality loan volume priced at competitive rates and to manage credit risk in our entire portfolio, while efficiently meeting the credit needs of our members.

LIQUIDITY AND FUNDING SOURCES

Liquidity and Funding

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

Total notes payable to the Bank at December 31, 2016, was $683,642 as compared to $667,938 at December 31, 2015 and $636,579 at December 31, 2014. The increase of 2.35% compared to December 31, 2015 is attributed to an increase in loan volume year over year. The increase of 4.93% as of December 31, 2015 compared to December 31, 2014 is attributable to an increase in loan volume year over year. The average volume of outstanding notes payable to the Bank was $674,591 for the year ended December 31, 2016. For the year ended December 31, 2015 and 2014, the average volume outstanding notes payable to the Bank was $656,724 and $633,180, respectively. Refer to Note 6, *Notes Payable to AgFirst Farm Credit Bank*, of the Notes to the Consolidated Financial Statements, for weighted average interest rates and maturities, and additional information concerning the Association's notes payable.

Liquidity management is the process whereby funds are made available to meet all financial commitments including the extension of credit, payment of operating expenses and payment of debt obligations. The Association receives access to funds through its borrowing relationship with the Bank and from income generated by operations. The liquidity policy of the Association is to manage cash balances to maximize debt reduction and to increase loan volume. As borrower payments are received, they are applied to the Association's note payable to the Bank. Sufficient liquid funds have been available to meet all financial obligations. There are no known trends likely to result in a liquidity deficiency for the Association.

The Association had no lines of credit available from third party financial institutions as of December 31, 2016.

Funds Management

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

Demand for loan types is a driving force in establishing a funds management strategy. The Association offers fixed, adjustable and variable rate loan products that are marginally priced according to financial market rates. Variable rate loans may be indexed to market indices such as the Prime Rate or the 30 or 90-day London Interbank Offered Rate (LIBOR). Adjustable rate mortgages are indexed to U.S. Treasury Rates. Fixed rate loans are priced based on the current cost of System debt of similar terms to maturity.

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

Relationship with the Bank

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

The Bank's ability to access capital of the Association is discussed in Note 7, *Members' Equity*, of the Notes to the Consolidated Financial Statements.

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

CAPITAL RESOURCES

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

The Association Board of Directors establishes, adopts, and maintains a formal written capital adequacy plan to ensure that adequate capital is maintained for continued financial viability, to provide for growth necessary to meet the needs of members/borrowers, and to ensure that all stockholders are treated equitably. There were no material changes to the capital plan for 2016 that would affect minimum stock purchases or would have an effect on the Association's ability to retire stock and distribute earnings.

Total members' equity at December 31, 2016, increased 5.77% percent to $187,667 from the December 31, 2015 total of $177,423. At December 31, 2015, total members' equity increased 4.50% from the December 31, 2014 total of $169,784. The increase was primarily attributed to the increase in retained surplus due to the amount of net income being greater than any surplus amounts revolved or redeemed in 2016.

Total capital stock and participation certificates were $2,457 on December 31, 2016, compared to $2,414 on December 31, 2015, and $2,409 on December 31, 2014.

FCA sets minimum regulatory capital requirements for System banks and associations. Capital adequacy is evaluated using a number of regulatory ratios. According to the FCA regulations, each institution's permanent capital ratio is calculated by dividing permanent capital by a risk-adjusted asset base. Risk adjusted assets mean the total dollar amount of the institution's assets adjusted by an appropriate credit conversion factor as defined by regulation. For all periods represented, the Association exceeded minimum regulatory standards for all the ratios.

The Association's capital ratios as of December 31 and the FCA minimum requirements follow:

	2016	2015	2014	Regulatory Minimum
Permanent capital ratio	22.23%	22.23%	23.30%	7.00%
Total surplus ratio	21.93%	21.91%	22.96%	7.00%
Core surplus ratio	21.93%	21.91%	22.96%	3.50%

The Association's permanent capital, total surplus, and core surplus ratios for December 31, 2016 were essentially unchanged from December 31, 2015. The total and core surplus ratios are exactly the same because the Association no longer has any allocated surplus that is scheduled to be revolved. There are no trends, commitments, contingencies, or events that are likely to affect the Association's ability to meet regulatory minimum capital standards and capital adequacy requirements.

See Note 7, *Members' Equity*, of the Consolidated Financial Statements, for further information concerning capital resources.

PATRONAGE PROGRAM

Prior to the beginning of any fiscal year, the Association's Board of Directors, by adoption of a resolution, may establish a Patronage Allocation Program to distribute its available consolidated net earnings. This resolution provides for the application of net earnings in the manner described in the Association's Bylaws. This program includes the setting aside of funds to increase surplus to meet minimum capital adequacy standards established by FCA Regulations, to increase surplus to meet Association capital adequacy standards to a level necessary to support competitive pricing at targeted earnings levels, and for reasonable reserves for necessary purposes of the Association. After excluding net earnings attributable to (a) the portion of loans participated to another institution, and (b) participation loans purchased, remaining consolidated net earnings are eligible for allocation to borrowers. Refer to Note 7, *Members' Equity*, of the Notes to the Consolidated Financial Statements, for more information concerning the patronage distributions. The Association declared patronage distributions of $10,000 in 2016, $12,000 in 2015, and $14,000 in 2014.

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

The Association's mission is to be the lender of choice to all of agriculture and our rural communities, which includes providing credit to Young*, Beginning** and Small*** farmers. We recognize these farmers are vital to the future growth of the Association and our ability to meet our mission. Demographic data indicates that the average age of a farmer is increasing, making it even more important for the Association to be committed to attracting, growing and retaining the YBS volume in our territory.

For these reasons, the Association has established annual business goals to ensure we meet the financial needs of these farmers and increase our market share of loans to these farmers. Our business goals include both specific marketing plans to target these groups and designated resources to help ensure YBS borrowers have access to a stable source of credit. The Association met its 2016 goals and will continue to strive to build its YBS portfolio.

The following table outlines the loan volume and number of YBS loans originated by the Association in 2016.

	As of December 31, 2016	
	Number of Loans	Amount of Loans
Young	237	$71,023
Beginning	308	$63,071
Small	628	$41,787

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

The 2012 USDA Ag Census data has been used as a benchmark to measure the Association's market share to this group of farmers. The census indicated there were 6,348 farmers within the Association's chartered territory (counties). Of these reported farmers, the following were classified as Young, Beginning or Small Farmers:

- 378 or 6.0% of the total – Young;
- 1,265 or 19.90% of the total – Beginning; and
- 4,724 or 74.40% of the total – Small.

The Ag Census does not collect data on how many of these farmers borrow money, thus a fair comparison of market percentage is not possible. However, as of December 31, 2016, the demographics of the Association's agricultural portfolio contained 5,410 loans to farmers. Of that total, the following were classified as Young, Beginning or Small Farmers:

- 802 or 15% of the total were Young Farmers;
- 1,083 or 20% of the total were Beginning Farmers; and
- 2,080 or 38% of the total were to Small Farmers.

The Association recognizes these farmers have unique credit and business needs to be successful. Through marketing, outreach and financial support programs, we maintained a three-pronged approach to help young, beginning and small farmers in 2016. These initiatives and outreach programs included:

- Support of 4-H, FFA, and young farmer organizations through sponsorships and donations.
- Involvement of at least one Young, Beginning, or Small (YBS) Farmer on each Branch Advisory Committee.
- Implementation of streamlined loans with reduced cost.

- Sponsorship of Ag Biz Planner – an e-learning course focused on helping young, beginning, small or minority farmers develop a business plan and learn to be successful business owners. At the conclusion of the online portion, all participants come together for a day and a half conference to hear expert speakers and engage in network activities to put in practice the principles learned in the course.
- Sponsorship of an Emerging Entrepreneurs' Conference – a three day conference focused on young, beginning, small and minority farmers. Topics include farm transition, farm management, issues facing agriculture, and strategic planning all delivered by expert speakers. The conference is designed to create an interactive environment for emerging entrepreneurs to network and share ideas.
- Advertising, including radio and use of the Association's internet site to reach YBS Farmers.

The Chief Lending Officer coordinates the Association's YBS efforts. The Association includes YBS goals in the annual strategic plan and reports on those goals and achievements to the Board of Directors on a quarterly basis.

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

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

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

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

REGULATORY MATTERS

New regulatory capital requirements for System banks and associations became effective January 1, 2017 and were adopted to:

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

These new requirements replace the core surplus and total surplus requirements with Common Equity Tier 1 (CET1), Tier 1 and Total Capital risk-based capital ratio requirements. The new requirements also replace the existing net collateral ratio with a Tier 1 Leverage ratio which is applicable to all banks and associations. The Permanent Capital Ratio remains in effect.

The following sets forth the new regulatory capital ratios:

Ratio	Primary Components of Numerator	Denominator	Minimum Requirement	Minimum Requirement with Conservation Buffer
CET1 Capital	Unallocated retained earnings/surplus (URE), Common Stock (subject to certain conditions)	Risk-weighted assets	4.5%	7.0%
Tier 1 Capital	CET1 Capital, Non-cumulative perpetual preferred stock	Risk-weighted assets	6.0%	8.5%
Total Capital	Tier 1 Capital, Allowance for Loan Losses, other equity securities not included in Tier 1 Capital	Risk-weighted assets	8.0%	10.5%
Tier 1 Leverage	Tier 1 Capital (1.5% must be URE or URE equivalents)	Total assets	4.0%	5.0%

The new capital requirements have a three-year phase-in of the capital conservation buffer applied to the risk-adjusted capital ratios. Based on analysis, the Association is positioned to be in compliance with the new requirements.

On November 30, 2015, the FCA, along with four other federal agencies, published in the Federal Register a final rule to establish capital and margin requirements for covered swap entities as required by the Dodd-Frank Act. See below for further information regarding the Dodd-Frank Act.

On July 25, 2014, the FCA published a proposed rule in the Federal Register to revise the requirements governing the eligibility of investments for System banks and associations. The public comment period ended on October 23, 2014. The FCA expects to issue a final regulation in 2017. The stated objectives of the proposed rule are as follows:

- To strengthen the safety and soundness of System banks and associations,
- To ensure that System banks hold sufficient liquidity to continue operations and pay maturing obligations in the event of market disruption,
- To enhance the ability of the System banks to supply credit to agricultural and aquatic producers,
- To comply with the requirements of section 939A of the Dodd-Frank Act,
- To modernize the investment eligibility criteria for System banks, and
- To revise the investment regulation for System associations to improve their investment management practices so they are more resilient to risk.

FINANCIAL REGULATORY REFORM

The Dodd-Frank Act was signed into law on July 21, 2010. While the Dodd-Frank Act represents a significant overhaul of many aspects of the regulation of the financial services industry, many of the statutory provisions of the Dodd-Frank Act are not applicable to the Farm Credit System.

The provisions of the Dodd-Frank Act pertaining to the regulation of derivatives transactions require, among other things, more of these transactions to be cleared through a third-party central clearinghouse and traded on regulated exchanges or other multilateral platforms. Margin is required for these transactions. Derivative transactions that are not subject to mandatory trading and clearing requirements may be subject to minimum margin and capital requirements. The Commodity Futures Trading Commission and other federal banking regulators have exempted System institutions from certain, but not all, of these new requirements, including, for swaps with members, mandatory clearing and minimum margin for noncleared swaps.

Notwithstanding the above-mentioned exemptions from clearing and margin requirements for System institutions, counterparties of System institutions may require margin or other forms of credit support as a condition to entering into noncleared transactions because such transactions may subject these counterparties to more onerous capital, liquidity and other requirements absent such margin or credit support. Alternatively, these counterparties may pass on the capital and other costs associated with entering into transactions if insufficient margin or if other credit support is not provided.

The Dodd-Frank Act also created a new federal agency called the Consumer Financial Protection Bureau (CFPB). The CFPB is responsible for regulating the offering of consumer financial products or services under federal consumer financial laws. The Farm Credit Administration retains the responsibility to oversee and enforce compliance by System institutions with relevant rules adopted by the CFPB.

In light of the foregoing, it is difficult to predict at this time the extent to which the Dodd-Frank Act or the forthcoming implementing rules and regulations will have an impact on the System. However, it is possible they could affect funding and hedging strategies and increase funding and hedging costs.

RECENTLY ISSUED ACCOUNTING PRONOUNCEMENTS

Please refer to Note 2, *Summary of Significant Accounting Policies*, in the Notes to the Consolidated Financial Statements for recently issued accounting pronouncements.

Disclosure Required by Farm Credit Administration Regulations

Description of Business

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

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

Unincorporated Business Entities

The Association holds an equity ownership in the following Unincorporated Business Entities (UBEs) as an equity interest holder of the limited liability company (LLC). The LLCs were organized for the stated purpose of acquiring and managing unusual or complex collateral associated with former loans until such time as the assets may be sold or otherwise disposed of pursuant to the terms of the Operating Agreements of the respective LLCs.

Entity Name	Entity Type	Entity Purpose
Cape Fear Acquisitions	LLC	Manage Acquired Property
CBF Holdings	LLC	Manage Acquired Property
Ethanol Holding Company	LLC	Manage Acquired Property
A1 Ledges Wilder	LLC	Manage Acquired Property
A1 Sequatchie Point	LLC	Manage Acquired Property

Description of Property

The following table sets forth certain information regarding the properties of the reporting entity, all of which are located in North Carolina:

Location	Description	Form of Ownership
333 East Russell Street Fayetteville	Administrative/ Branch	Owned
105 East Front Street Lillington	Branch	Owned
400 West Broad Street Dunn	Branch	Owned
1780 Southeast Boulevard Clinton	Branch	Owned
127 Beasley Street Kenansville	Branch	Owned
811 South Walker Street Burgaw	Branch	Owned
108 North Poplar Street Elizabethtown	Branch	Owned
331 South Main Street Raeford	Branch	Owned
1902 North Cedar Street Lumberton	Branch	Owned
300 Liberty Street Whiteville	Branch	Owned
4631 Main Street Shallotte	Branch	Owned*

**Shallotte branch was sold 1/23/2017*

Legal Proceedings

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

Description of Capital Structure

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

Description of Liabilities

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

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

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

Senior Officers

The following represents certain information regarding the senior officers of the Association and their business experience for the past five years:

Senior Officer	Position & Other Business Interests
Bradford (Brad) Cornelius	*President and Chief Executive Officer* since January 2016. He previously served as Chief Credit Officer at AgChoice Farm Credit for five years. Prior, he spent eighteen years in various lending and credit roles at AgGeorgia Farm Credit.
Pierce R. Hodnette	*Senior Vice President / Chief Lending Officer* since May 2016. He previously served as Chief Credit Officer at Ag Credit Agricultural Credit Association for two years. Prior, he spent nine years in various lending and credit roles at AgFirst Farm Credit Bank.
Laura (Skipper) Jones	*Senior Vice President / Administrative Officer* since July 2014. She previously served as Marketing Manager from September 2008 to July 2014.
Evan J. Kleinhans	*Senior Vice President / Chief Financial Officer* since November 2011. Mr. Kleinhans serves as the Treasurer of CBF Holdings, LLC which is an Unincorporated Business Entity created for the purpose of acquiring and managing unusual or complex collateral associated with former loans that Cape Fear Farm Credit has an equity ownership in.
Brian J. Smith	*Senior Vice President / Chief Risk Officer* since May 2011. Served as Interim President & Chief Executive Officer between January 2013 and July 2013. He also served as Senior Vice President and Senior Credit Analyst at Four Oaks Bank from June 2008 through May 2011 and prior to that served as Vice President – Credit at AgCarolina Farm Credit. Mr. Smith serves as a Member Manager of CBF Holdings, LLC which is an Unincorporated Business Entity created for the purpose of acquiring and managing unusual or complex collateral associated with former loans that Cape Fear Farm Credit has an equity ownership in.
Betty Kay Williams	*Senior Vice President / Director of Project Management* since May 2016. She previously served as Chief Credit Operations Officer from April 2011 to May 2016. Prior, she served the Association as a Vice President and Senior Credit Administrator from November 2010 to April 2011 and she also served the Association as Vice President and Branch Manager.

The total amount of compensation earned by the Chief Executive Officer (CEO) and the senior officers and other highly compensated employees as a group during the years ended December 31, 2016, 2015 and 2014, is as follows:

Name of Individual or Number in Group	Year	Salary	Bonus	Deferred Comp.	Change in Pension Value*	Perq/ Other**	Total
Bradford Cornelius	2016	$ 250,010	$ 45,627	$ –	$ 366,196	$ 15,987	$ 677,819
William L. Melton	2016	$ 26,251	$ –	$ –	$ 1,376	$ –	$ 27,627
William L. Melton	2015	$ 310,012	$ 135,000	$ –	$ 108	$ –	$ 445,120
William L. Melton	2014	$ 290,845	$ –	$ –	$ 8,300	$ –	$ 299,145
8	2016	$ 879,649	114,340	$ –	$ 293,388	$ 72,239	$ 1,359,617
6	2015	$ 746,459	$ 128,929	$ –	$ 4,145	$ –	$ 879,533
7 (a)	2014	$ 747,686	$ 135,935	$ 10,851	$ 559,282	$ 9,516	$ 1,463,270

All amounts are in actual dollars

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

*** The Perquisites/Other amount disclosed in the above chart includes club memberships, automobile allowance, deferred compensation, life insurance, and relocation reimbursement.*

(a) The changes in pension values in 2014 as reflected in the table above resulted primarily from changes in the actuarial assumptions for mortality and discount rate. See further discussion in Note 9, Employee Benefit Plans, of the Financial Statement.

The disclosure of information on the total compensation paid during 2016 to any senior officer or to any other employee included in the aggregate group total as reported in the table above is available and will be disclosed to the shareholders of the institution upon request.

On March 31, 2014, the FCA published an interim final rule rescinding all requirements for nonbinding advisory votes on senior officer compensation at System banks and associations. The comment period for the interim rule ended on April 30, 2014 and the final rule became effective on June 18, 2014.

For the year ended December 31, 2016, no advisory votes were held. On October 3, 2012, FCA adopted a regulation that requires all System institutions to hold advisory votes on the compensation for all senior officers and/or the CEO when the compensation of either the CEO or the senior officer group increases by 15 percent or more from the previous reporting period. In addition, the regulation requires associations to hold an advisory vote on CEO and/or senior officer compensation when 5 percent of the voting stockholders petition for the vote and to disclose the petition authority in the annual report to shareholders. The regulation became effective December 17, 2012, and the base year for determining whether there is a 15 percent or greater increase was 2013. No District Association held an advisory vote based on a stockholder petition in 2013.

On January 17, 2014, the President signed into law the Consolidated Appropriations Act, which includes language

prohibiting the FCA from using any funds available to "implement or enforce" the regulation. In addition, on February 7, 2014, the President signed into law the Agricultural Act of 2014. Section 5404 of the law directs FCA, within 60 days of enactment of the law, to "review its rules to reflect the Congressional intent that a primary responsibility of boards of directors of Farm Credit System institutions, as elected representatives of their stockholders, is to oversee compensation practices." FCA has not yet taken any action with respect to their regulation in response to these actions. Regulatory reporting changes have affected the content of the compensation reported for 2014, 2015, and 2016.

Amounts in the above table classified as Perquisites include travel incentives, group life insurance, automobile compensation, purchased automobile, spousal travel, relocation and tuition reimbursement. Amounts in the above table classified as Other include amounts contributed by the Association on behalf of the senior officer to a defined contribution plan unless the plan is made available to all employees on the same basis.

In addition to a base salary, senior officers earn additional compensation under a profit sharing plan. The Association profit sharing plan is designed to motivate employees to maximize the return to Association stockholders. The profit sharing plan has positive and negative adjustments for loan volume growth, earnings, efficiencies, and credit quality factors. All Association employees are covered by the plan. Bonuses shown in previous years are shown in the year earned which may be different than the year of payment.

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

Pension Benefits Table
As of December 31, 2016

Name of Individual or Number in Group	Year	Plan Name	Number of Years Credited Service	Actuarial Present Value of Accumulated Benefits	Payments During 2016
CEO:					
Bradford Cornelius (1)	2016	AgFirst Retirement Plan	25.83	$ 1,447,621	$ –
				$ 1,447,621	$ –
Senior Officers and Highly Compensated Employees:					
3 Officers, excluding the CEO	2016	AgFirst Retirement Plan	33.47*	$ 3,293,334	$ –
5 Officers, excluding the CEO	2016	AgFirst Cash Balance Retirement Plan	6.18	69,703	–
				$ 3,363,037	$ –

All amounts are in actual dollars
* *Represents the average years of credited service for the group*

Retirement and Deferred Compensation Plans

The Association's compensation programs include retirement and deferred compensation plans designed to provide income following an employee's retirement. Although retirement benefits are paid following an employee's retirement, the benefits are earned while employed. The objective of the Association is to offer benefit plans that are market competitive and aligned with the Association's strategic objectives. The plans are designed to enable the Association to proactively attract, retain, recognize and reward a highly skilled, motivated and diverse staff that supports the Association's mission and that allows the Association to align the human capital needs with the Association's overall strategic plan.

Employees participate in one of two qualified defined benefit retirement plans.

Employees hired prior to January 1, 2003 participate in the AgFirst Farm Credit Retirement Plan. Employees are eligible to retire and begin drawing unreduced pension benefits at age 65 or when years of credited service plus age equal "85." Upon retirement, annual payout is equal to 2 percent of the highest three years average compensation times years of credited service, subject to the Internal Revenue Code limitations. For purposes of determining the payout, "average compensation" is defined as regular salary (i.e., does not include incentive awards compensation). At the election of the retiree, benefits are paid based upon various annuity terms or on a lump sum basis. Benefits under the plan are not subject to an offset for Social Security.

Employees hired on or after January 1, 2003 participate in the AgFirst Farm Credit Cash Balance Retirement Plan. Employees are eligible to retire and begin drawing unreduced pension benefits at age 65 with a minimum of 5 years of credited service or at age 55 with a minimum of 10 years of credited service. Upon retirement, payout is determined using a percent of eligible compensation formula, subject to the Internal Revenue Code limitation on compensation, and regular interest credits. For purposes of determining the payout, "compensation" is defined as regular salary (i.e., does not include incentive awards compensation). At the election of the retiree, benefits are paid based upon various annuity terms or on a lump sum basis. Benefits under the plan are not subject to an offset for Social Security.

Employees participate in the Farm Credit Benefits Alliance 401(k) Plan, a qualified 401(k) defined contribution plan which has an employer matching contribution determined by the employee's date of hire. Employees hired prior to January 1, 2003 receive a maximum employer matching contribution equal to $0.50 for each $1.00 of employee compensation contributed up to 6 percent, subject to the Internal Revenue Code limitation on compensation. Employees hired on or after January 1, 2003 receive a maximum employer matching contribution equal to $1.00 for each $1.00 of employee

compensation contributed up to 6 percent, subject to the Internal Revenue Code limitation on compensation.

Senior officers and other highly compensated employees may participate in the Farm Credit Benefits Alliance Nonqualified Supplemental 401(k) Plan, a nonqualified deferred compensation plan that allows certain key employees to defer compensation and which restores the benefits limited in the qualified 401(k) plan as a result of restrictions in the Internal Revenue Code. The plan also includes a provision for discretionary contributions to be made by the Association.

Chief Executive Officer

Mr. Cornelius participates in the AgFirst Farm Credit Retirement Plan. Mr. Melton participated in the AgFirst Farm Credit Cash Balance Retirement Plan.

Mr. Cornelius participates in the Farm Credit Benefits Alliance 401(k) Plan. Mr. Melton did not participate in the Farm Credit Benefits Alliance 401(k) Plan.

Mr. Cornelius does not participate in the Farm Credit Benefits Alliance Nonqualified Supplemental 401(k) Plan. Mr. Melton did not participate in the Farm Credit Benefits Alliance Nonqualified Supplemental 401(k) Plan.

Directors

The following chart details the year the director began serving on the board, the current term of expiration, and total cash compensation paid:

DIRECTOR & TITLE*	ORIGINAL YEAR OF ELECTION OR APPOINTMENT	CURRENT TERM EXPIRATION**	TOTAL COMP. PAID DURING 2016
F.A. Lowrey, *Chairman, Outside Director*	2013	2017	$40,000
Gary A. Hendrix, *Vice Chairman*	2007	2018	25,625
Alton D. Bain, *Outside Director*	2014	2017	28,750
Anthony E. Darden (1)	2014	2016	5,000
David R. Gooden (2)	2014	2018	23,750
Anthony T. Grant, *Outside Director*	2013	2019	35,375
Glenn E. Harder, *Outside Director*	2013	2018	35,375
P. Jart Hudson (3)	2003	2020	8,778
Adrian B. Locklear (4)	2016	2017	8,899
Paul M. Maguire	2014	2018	23,750
T. Morris Murphy	2016	2020	18,063
Jonathan A. Pope	2009	2017	23,750
Gary L. Rouse, *Outside Director*	2014	2017	28,750
Mitchell S. Sessoms	2014	2017	23,750
Michael T. (Bo) Stone (5)	2015	2019	23,750
Alfred K. Wooten	2004	2019	25,625
Total			$378,990

All amounts are in actual dollars

** Position Title as of 12/31/2016*
*** Term expires on the Annual Meeting Date of corresponding year unless otherwise noted*

(1) Mr. Anthony E. Darden's term expired in 2016.
(2) Mr. David R. Gooden previously served from 2005-2008
(3) Mr. P. Jart Hudson resigned in 2016.
(4) Mr. Adrian B. Locklear was appointed to vacant seat until 2017 Annual Meeting.
(5) Mr. Michael T. Stone previously served from 2007-2014.

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

Mr. F. A. Lowrey, *Chairman***,** was appointed as an Association outside director in 2013. His principal occupation and employment for the past five years was as the CEO of AgFirst Farm Credit Bank. He retired from this position in June 2012. Mr. Lowrey serves on the boards of the South Carolina Jobs & Economic Development Authority, a SC statewide conduit bond issuer, and the Business Partnership Foundation of the Darla Moore School of Business at the University of South Carolina, an educational institution. Mr. Lowrey is Chairman of the Audit Committee of The National 4-H Council. He also serves as an elder at Eastminster Presbyterian Church, a religious organization. *Mr. Lowrey completed his appointed term as an outside director February 16, 2017.*

Mr. Gary A. Hendrix, *Vice Chairman***,** is a row crop, cotton, and peanut farmer. His principal occupation and employment for the past five years was self-employed farming. Mr. Hendrix also serves on the boards of FCI (agricultural services), the North Carolina Soybean Growers Association (crop promotion) and the Hoke County Soil & Water Conservation District (conservation).

Mr. Alton D. Bain, was appointed as an Association outside director in 2014. He is a Partner in Bain & McRae, LLP, a law firm. His principal occupation and employment for the past five years was practicing law with Bain & McRae, LLP. Mr. Bain also serves on the board of the Harnett County Community Foundation (civic organization), as president of the Harnett County Historical Society (historic preservation), and also as an elder at Lillington Presbyterian Church, a religious organization.

Mr. Anthony E. Darden is a poultry and swine farmer. His principal occupation and employment for the past five years was self-employed farming. Mr. Darden also serves on the board of the Sampson Regional Medical Center (hospital). *Mr. Darden completed his elected term as a director April 11, 2016.*

Mr. David R. Gooden is a row crop, hay, strawberry, cattle, timber, swine, poultry and sweet corn farmer. His principal occupation and employment for the past five years was self-employed farming. Mr. Gooden serves on the Bladen County Board of Commissioners (political), and also on the board of the Bladen County Livestock Association (livestock promotion).

Mr. Anthony T. Grant was appointed as an Association outside director in 2013. He is the CEO and owner of Grant Business Strategies, Inc., a financial advisory and business strategies firm. His principal occupation and employment for the past five years was as a business consultant with Grant Business Strategies, Inc. Mr. Grant also serves on the board of the Columbia Urban League (multi-service non-profit agency).

Mr. Glenn E. Harder was appointed as an Association outside director in 2013. He is the President and owner of GEH Advisory Services, LLC, a strategic advisory services firm. His principal occupation and employment for the past five years was as a business consultant with GEH Advisory Services, LLC. Mr. Harder also served on the board of DPL, Inc., an Ohio based public utility, as Board Chairman, prior to 2012.

Mr. P. Jart Hudson, Jr. is a row crop, peanut, tobacco and contract swine farmer. His principal occupation and employment for the past five years was self-employed farming. Mr. Hudson also serves on the board of the Tobacco Growers Association of NC (crop promotion association,). *Mr. Hudson resigned from the Board of Directors effective May 25, 2016.*

Mr. Adrian Locklear is a row crop, rapeseed, sweet corn and yellow field pea farmer. His principal occupation the past five years was self-employed farming.

Mr. Paul M. Maguire is a cattle, poultry, hay and timber farmer. His principal occupation and employment for the past five years was self-employed farming. Mr. Maguire also serves as on the Cumberland County Extension Advisory Board (agricultural advisory board), and as an officer of the Cumberland County Livestock Association (livestock promotion).

Mr. T. Morris Murphy is a tobacco, corn, soybeans, cotton, sweet potatoes, cucumbers, hay, swine and poultry farmer. His principal occupation for the past five years was self-employed farming. Mr. Murphy also serves on the board of the Jones County Cotton Gin, Albertson Volunteer Fire Department, as FSA County Committee chairman, and also as assistant treasurer at Friendship F.W.B. Church, a religious organization.

Mr. Jonathan (Jon) A. Pope is a row crop, cattle, contract poultry and hay farmer. His principal occupation and employment for the past five years was self-employed farming. Mr. Pope also serves on the board of the Harnett County Farm Bureau (insurance).

Mr. Gary L. Rouse was appointed as an Association outside director in 2014. He is the President, Stockholder and Firm Manager of Rouse & Peterson, P.A a public accounting firm. His principal occupation and employment for the last five years was practicing as a Certified Public Accountant at Rouse & Peterson, P.A.

Mr. Mitchell S. Sessoms is a poultry and hay farmer. His principal occupation and employment for the last five years was working for Tyson Foods (poultry integrator) and self-employed farming.

Mr. Michael T. (Bo) Stone is a row crop, hay, cattle, contract swine, produce and strawberry farmer. His principal occupation and employment for the past five years was self-employed farming. Mr. Stone also serves on the board of Southeastern Regional Medical Center (hospital), Dillon Christian School (private school), and AgFirst Farm Credit Bank (financial institution).

Mr. Alfred K. Wooten is a turf grass, blueberry and row crop farmer. His principal occupation and employment for the past five years was self-employed farming. Mr. Wooten also serves as President of the North Carolina Sod Producers Association (crop promotion association) and on the board of the Green Industry Council (crop promotion association), and the Pender County Farm Bureau (insurance).

Subject to approval by the board, the Association may allow the outside Directors a quarterly retainer of $7,500, elected Directors a quarterly retainer of $6,250, Board Chairman a $1,250 quarterly stipend, and other Committee Chairs a $625 quarterly stipend. Total compensation paid to directors as a group during 2016 was $378,990.

The following chart details the number of meetings and other activities as well as committee assignments during 2016 for each director:

	Days Served		
Name of Director	**Regular Board Meetings**	**Other Official Activities***	**Committee Assignments****
F.A. Lowrey, *Chairman, Outside Director (1)*	12	23	Compensation, Compliance, Governance
Gary A. Hendrix *Vice Chairman (4)*	12	23	Audit, Compliance, Governance
Alton D. Bain, *Outside Director*	12	9	Compensation
Anthony E. Darden	3	3	Risk Management
David R. Gooden	12	8	Audit
Anthony T. Grant, *Outside Director (2)*	10	20	Governance, Risk Management
Glenn E. Harder, *Outside Director (3)*	11	14	Audit, Compliance, Governance
P. Jart Hudson	4	3	Compensation
Adrian B. Locklear	4	2	Compensation
Paul M. Maguire	10	8	Compliance, Risk Management
T. Morris Murphy	9	5	Risk Management
Jonathan A. Pope	10	8	Compliance, Risk Management
Gary L. Rouse, *Outside Director*	10	11	Audit
Mitchell S. Sessoms	12	4	Risk Management
Michael T. (Bo) Stone	12	10	Compensation
Alfred K. Wooten *(5)*	12	21	Compensation, Governance

* *Includes board committee meetings and other board activities other than regular board meetings including training.*
** *Committee Assignments as of 12/31/2016*

(1) Chairman of the Governance Committee
(2) Chairman of the Risk Committee
(3) Chairman of the Compliance Committee
(4) Chairman of the Audit Committee
(5) Chairman of the Compensation Committee

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

The aggregate amount of reimbursement for travel, subsistence and other related expenses for all directors as a group was $87,465 for 2016, $101,703 for 2015, and $79,429 for 2014.

Transactions with Senior Officers and Directors

The reporting entity's policies on loans to and transactions with its officers and directors, to be disclosed in this section are incorporated herein by reference to Note 10, *Related Party Transactions*, of the Consolidated Financial Statements included in this Annual Report. There have been no transactions between the Association and senior officers or directors which require reporting per FCA regulations.

Involvement in Certain Legal Proceedings

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

Relationship with Independent Certified Public Accountants

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

Aggregate fees paid by the Association for services rendered by its independent certified public accountants for the year ended December 31, 2016 were as follows:

	2016
Independent Certified Public Accountants	
Pricewaterhouse Coopers LLP	
Audit services	$ 64,620
Total	$ 64,620

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

Consolidated Financial Statements

The Consolidated Financial Statements, together with the report thereon of PricewaterhouseCoopers LLP dated March 13, 2017 and the report of management, which appear in this Annual Report, are incorporated herein by reference.

Copies of the Association's Annual and Quarterly reports are available upon request free of charge by calling 1-800-368-5819, extension 3243 or writing Evan J. Kleinhans, Chief Financial Officer, Cape Fear Farm Credit, PO Box 2405, Fayetteville, NC, 28302 or by accessing the web site, ***www.capefearfarmcredit.com***. The Association prepares an electronic version of the Annual Report which is available on the Association's web site within 75 days after the end of the fiscal year and distributes the Annual Reports to shareholders within 90 days after the end of the fiscal year. The Association prepares an electronic version of the Quarterly report within 40 days after the end of each fiscal quarter, except that no report need be prepared for the fiscal quarter that coincides with the end of the fiscal year of the institution.

Borrower Information Regulations

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

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

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

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

Shareholder Investment

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

Report of the Audit Committee

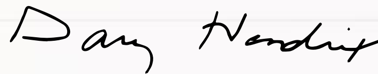
The Audit Committee of the Board of Directors (Committee) is comprised of the directors named below. None of the directors who serve on the Committee is an employee of Cape Fear Farm Credit (Association) and in the opinion of the Board of Directors, each is free of any relationship with the Association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

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

PricewaterhouseCoopers LLP (PwC), the Association's independent certified public accountants for 2016, is responsible for expressing an opinion on the conformity of the Association's audited consolidated financial statements with accounting principles generally accepted in the United States of America. The Committee has discussed with PwC the matters that are required to be discussed by Statement on Auditing Standards No. 114 *(The Auditor's Communication With Those Charged With Governance)*. The Committee discussed with PwC its independence from Cape Fear Farm Credit. The Committee also reviewed the non-audit services provided by PwC and concluded that these services were not incompatible with maintaining PwC's independence.

The Committee has also concluded that PwC's provision of non-audit services, if any, to the Association is compatible with PwC's independence.

Based on the considerations referred to above, the Committee recommended to the Board of Directors that the audited consolidated financial statements be included in the Association's Annual Report for 2016. The foregoing report is provided by the following independent directors, who constitute the Committee:



Gary A. Hendrix
Chairman of the Audit Committee

Members of Audit Committee

David R. Gooden
Glenn E. Harder
Gary L. Rouse

March 13, 2017

Report of Independent Certified Public Accountants

To the Board of Directors and Members of
Cape Fear Farm Credit, ACA

We have audited the accompanying consolidated financial statements of Cape Fear Farm Credit, ACA and its subsidiaries (the "Association"), which comprise the consolidated balance sheets as of December 31, 2016, 2015 and 2014, and the related consolidated statements of income, comprehensive income, changes in members' equity and cash flows for the years then ended.

Management's Responsibility for the Consolidated Financial Statements

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

Certified Public Accountants' Responsibility

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

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

Opinion

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of Cape Fear Farm Credit, ACA and its subsidiaries as of December 31, 2016, 2015 and 2014, and the results of their operations and their cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

PricewaterhouseCoopers LLP

March 13, 2017

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

Consolidated Balance Sheets

(dollars in thousands)	December 31, 2016	2015	2014
Assets			
Cash	**$ 3,063**	$ 3,882	$ 3,107
Investment securities:			
Held to maturity (fair value of $3,961, $7,087, and $4,312, respectively)	**4,209**	7,366	4,647
Loans	**859,557**	830,254	789,693
Allowance for loan losses	**(7,738)**	(7,117)	(5,378)
Net loans	**851,819**	823,137	784,315
Accrued interest receivable	**7,938**	7,327	7,108
Investments in other Farm Credit institutions	**9,951**	9,592	9,360
Premises and equipment, net	**3,191**	3,354	3,081
Other property owned	**1,876**	1,356	4,976
Accounts receivable	**10,307**	10,340	13,111
Other assets	**3,169**	4,069	3,880
Total assets	**$ 895,523**	$ 870,423	$ 833,585
Liabilities			
Notes payable to AgFirst Farm Credit Bank	**$ 683,642**	$ 667,938	$ 636,579
Accrued interest payable	**1,394**	1,310	1,186
Patronage refunds payable	**10,026**	12,008	14,007
Accounts payable	**2,541**	1,070	2,143
Other liabilities	**10,253**	10,674	9,886
Total liabilities	**707,856**	693,000	663,801
Commitments and contingencies (Note 11)			
Members' Equity			
Protected borrower stock	**3**	3	3
Capital stock and participation certificates	**2,454**	2,411	2,406
Retained earnings			
Allocated	**90,846**	83,467	77,931
Unallocated	**94,664**	91,849	89,784
Accumulated other comprehensive income (loss)	**(300)**	(307)	(340)
Total members' equity	**187,667**	177,423	169,784
Total liabilities and members' equity	**$ 895,523**	$ 870,423	$ 833,585

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

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

Consolidated Statements of Income

(dollars in thousands)	For the year ended December 31, 2016	2015	2014
Interest Income			
Loans	**$ 40,511**	$ 39,318	$ 37,535
Investments	**263**	264	364
Total interest income	**40,774**	39,582	37,899
Interest Expense			
Notes payable to AgFirst Farm Credit Bank	**16,170**	14,889	13,563
Net interest income	**24,604**	24,693	24,336
Provision for loan losses	**892**	622	174
Net interest income after provision for loan losses	**23,712**	24,071	24,162
Noninterest Income			
Loan fees	**2,415**	2,130	2,110
Fees for financially related services	**124**	141	50
Patronage refunds from other Farm Credit institutions	**9,898**	9,917	12,995
Gains (losses) on sales of rural home loans, net	**42**	60	52
Gains (losses) on sales of premises and equipment, net	**14**	55	89
Gains (losses) on other transactions	**2**	—	7
Other noninterest income	**31**	22	140
Total noninterest income	**12,526**	12,325	15,443
Noninterest Expense			
Salaries and employee benefits	**10,387**	10,269	9,790
Occupancy and equipment	**683**	719	796
Insurance Fund premiums	**1,074**	782	690
(Gains) losses on other property owned, net	**222**	1,074	487
Other operating expenses	**3,533**	3,800	3,605
Total noninterest expense	**15,899**	16,644	15,368
Income before income taxes	**20,339**	19,752	24,237
Provision for income taxes	**143**	150	150
Net income	**$ 20,196**	$ 19,602	$ 24,087

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

Consolidated Statements of Comprehensive Income

(dollars in thousands)	For the year ended December 31, 2016	2015	2014
Net income	**$ 20,196**	$ 19,602	$ 24,087
Other comprehensive income net of tax			
Employee benefit plans adjustments	**7**	33	(42)
Comprehensive income	**$ 20,203**	$ 19,635	$ 24,045

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

Consolidated Statements of Changes in Members' Equity

(dollars in thousands)	Protected Borrower Stock	Capital Stock and Participation Certificates	Retained Earnings Allocated	Retained Earnings Unallocated	Accumulated Other Comprehensive Income (Loss)	Total Members' Equity
Balance at December 31, 2013	$ 4	$ 2,433	$ 69,210	$ 88,459	$ (298)	$ 159,808
Comprehensive income				24,087	(42)	24,045
Protected borrower stock issued/(retired), net	(1)					(1)
Capital stock/participation certificates issued/(retired), net		(27)				(27)
Patronage distribution						
Cash				(14,000)		(14,000)
Nonqualified retained earnings			8,890	(8,890)		—
Patronage distribution adjustment			(169)	128		(41)
Balance at December 31, 2014	$ 3	$ 2,406	$ 77,931	$ 89,784	$ (340)	$ 169,784
Comprehensive income				19,602	33	19,635
Capital stock/participation certificates issued/(retired), net		5				5
Patronage distribution						
Cash				(12,000)		(12,000)
Nonqualified retained earnings			5,944	(5,944)		—
Patronage distribution adjustment			(408)	407		(1)
Balance at December 31, 2015	$ 3	$ 2,411	$ 83,467	$ 91,849	$ (307)	$ 177,423
Comprehensive income				**20,196**	**7**	**20,203**
Capital stock/participation certificates issued/(retired), net		**43**				**43**
Patronage distribution						
Cash				**(10,000)**		**(10,000)**
Nonqualified retained earnings			**7,807**	**(7,807)**		**—**
Patronage distribution adjustment			**(428)**	**426**		**(2)**
Balance at December 31, 2016	**$ 3**	**$ 2,454**	**$ 90,846**	**$ 94,664**	**$ (300)**	**$ 187,667**

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

Consolidated Statements of Cash Flows

(dollars in thousands)	For the year ended December 31, 2016	2015	2014
Cash flows from operating activities:			
Net income	**$ 20,196**	$ 19,602	$ 24,087
Adjustments to reconcile net income to net cash provided by (used in) operating activities:			
Depreciation on premises and equipment	**486**	429	355
Amortization (accretion) of net deferred loan costs (fees)	**(39)**	(32)	(22)
Premium amortization (discount accretion) on investments	**—**	(9)	(11)
Provision for loan losses	**892**	622	174
(Gains) losses on other property owned	**64**	1,177	139
(Gains) losses on sales of premises and equipment, net	**(14)**	(55)	(89)
(Gains) losses on sales of rural home loans, net	**(42)**	(60)	(52)
(Gains) losses on other transactions	**(2)**	—	(7)
Changes in operating assets and liabilities:			
Origination of loans held for sale	**(1,861)**	(2,475)	(2,179)
Proceeds from sales of loans held for sale, net	**1,903**	2,535	2,231
(Increase) decrease in accrued interest receivable	**(611)**	(219)	(1,243)
(Increase) decrease in accounts receivable	**33**	2,771	1,406
(Increase) decrease in other assets	**900**	(189)	894
Increase (decrease) in accrued interest payable	**84**	124	5
Increase (decrease) in accounts payable	**1,471**	(1,073)	596
Increase (decrease) in other liabilities	**(321)**	836	(2,290)
Total adjustments	**2,943**	4,382	(93)
Net cash provided by (used in) operating activities	**23,139**	23,984	23,994
Cash flows from investing activities:			
Purchases of investment securities, held to maturity	**(163)**	(2,934)	—
Proceeds from maturities of or principal payments received on investment securities, held to maturity	**3,320**	224	2,573
Net (increase) decrease in loans	**(31,147)**	(39,125)	(31,034)
(Increase) decrease in investment in other Farm Credit institutions	**(359)**	(232)	36
Proceeds from payments received on other investments	**—**	—	5,523
Purchases of premises and equipment	**(350)**	(695)	(699)
Proceeds from sales of premises and equipment	**41**	48	104
Proceeds from sales of other property owned	**937**	2,141	2,960
Net cash provided by (used in) investing activities	**(27,721)**	(40,573)	(20,537)
Cash flows from financing activities:			
Advances on (repayment of) notes payable to AgFirst Farm Credit Bank, net	**15,704**	31,359	2,707
Protected borrower stock retired	**—**	—	(1)
Capital stock and participation certificates issued/(retired), net	**43**	5	(27)
Patronage refunds and dividends paid	**(11,984)**	(14,000)	(7,596)
Net cash provided by (used in) financing activities	**3,763**	17,364	(4,917)
Net increase (decrease) in cash	**(819)**	775	(1,460)
Cash, beginning of period	**3,882**	3,107	4,567
Cash, end of period	**$ 3,063**	$ 3,882	$ 3,107
Supplemental schedule of non-cash activities:			
Financed sales of other property owned	**$ 85**	$ 287	$ 65
Receipt of property in settlement of loans	**1,697**	—	3,103
Estimated cash dividends or patronage distributions declared or payable	**10,000**	12,000	14,000
Employee benefit plans adjustments (Note 9)	**(7)**	(33)	42
Supplemental information:			
Interest paid	**16,086**	14,765	13,558
Taxes (refunded) paid, net	**25**	67	192

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

Notes to the Consolidated Financial Statements

(dollars in thousands, except as noted)

Note 1 — Organization and Operations

A. **Organization:** Cape Fear Farm Credit, ACA (Association) is a member-owned cooperative that provides credit and credit-related services to qualified borrowers in the counties of Bladen, Brunswick, Columbus, Cumberland, Duplin, Harnett, Hoke, New Hanover, Pender, Robeson, Sampson, and Scotland in the state of North Carolina.

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

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

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

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

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

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

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

The Bank primarily lends to the District Associations in the form of a line of credit to fund the Associations' earning assets. These lines of credit (or Direct Notes) are collateralized by a pledge of substantially all of each Association's assets. The terms of the Direct Notes are governed by a General Financing Agreement (GFA) between the Bank and Association. Each advance is structured such that the principal cash flow, repricing characteristics, and underlying index (if any) of the advance match those of the assets being funded. By match-funding the Association loans, the Associations' exposure to interest rate risk is minimized.

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

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

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

Note 2 — Summary of Significant Accounting Policies

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

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

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

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

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

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

Impaired loans are loans for which it is probable that not all principal and interest will be collected according to the contractual terms of the loan. Impaired loans include nonaccrual loans, restructured loans, and could include loans past due 90 days or more and still accruing interest. A loan is considered contractually past due when any principal repayment or interest payment required by the loan instrument is not received on or before the due date. A loan shall remain contractually past due until it is formally restructured 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.

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

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

Loans are charged off, wholly or partially, as appropriate, at the time they are determined to be uncollectible.

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

The allowance for loan losses is maintained at a level considered adequate by management to provide for probable and estimable losses inherent in the loan portfolio as of the report date. The allowance for loan losses is increased through provisions for loan losses and loan recoveries and is decreased through loan charge-offs and allowance reversals. A review of individual loans in each respective portfolio is performed periodically to determine the appropriateness of risk ratings and to ensure loss exposure to the Association has been identified. The allowance for loan losses is a valuation account used to reasonably estimate loan losses as of the financial statement date. Determining the appropriate allowance for loan losses balance involves significant judgment about when a loss has been incurred and the amount of that loss.

The Association considers the following factors, among others, when determining the allowance for loan losses:

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

A specific allowance may be established for impaired loans under Financial Accounting Standards Board (FASB) guidance on accounting by creditors for impairment of a loan. Impairment of these loans is measured based on the

present value of expected future cash flows discounted at the loan's effective interest rate or, as practically expedient, at the loan's observable market price or fair value of the collateral if the loan is collateral dependent.

A general allowance may also be established under FASB guidance on accounting for contingencies, to reflect estimated probable credit losses inherent in the remainder of the loan portfolio which excludes impaired loans considered under the specific allowance discussed above. A general allowance can be evaluated on a pool basis for those loans with similar characteristics. The level of the general allowance may be based on management's best estimate of the likelihood of default adjusted for other relevant factors reflecting the current environment.

The credit risk rating methodology is a key component of the Association's allowance for loan losses evaluation, and is generally incorporated into the institution's loan underwriting standards and internal lending limit. The Association uses a two-dimensional loan rating model based on internally generated combined system risk rating guidance that incorporates a 14-point risk rating scale to identify and track the probability of borrower default and a separate scale addressing loss given default over a period of time. Probability of default is the probability that a borrower will experience a default within 12 months from the date of the determination of the risk rating. A default is considered to have occurred if the lender believes the borrower will not be able to pay its obligation in full or the borrower is past due more than 90 days. The loss given default is management's estimate as to the anticipated economic loss on a specific loan assuming default has occurred or is expected to occur within the next 12 months.

Each of the 14 categories carries a distinct percentage of default probability. The 14-point risk rating scale provides for granularity of the probability of default, especially in the acceptable ratings. There are nine acceptable categories that range from a borrower of the highest quality to a borrower of minimally acceptable quality. The probability of default between 1 and 9 is very narrow and would reflect almost no default to a minimal default percentage. The probability of default grows more rapidly as a loan moves from a "9" to other assets especially mentioned and grows significantly as a loan moves to a substandard (viable) level. A substandard (non-viable) rating indicates that the probability of default is almost certain.

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

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

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

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

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

Investment Securities
The Association holds certain investment securities, as permitted under the FCA regulations. These investments are classified based on management's intention on the date of purchase and are generally recorded in the Consolidated Balance Sheets as securities on the trade date.

Securities for which the Association has the intent and ability to hold to maturity are classified as held-to-maturity (HTM) and carried at amortized cost. Investment securities classified as available-for-sale (AFS) are carried at fair value with net unrealized gains and losses included as a component of Other Comprehensive Income (OCI). Purchase premiums and discounts are amortized or accreted ratably over the term of the respective security using the interest method.

The Association reviews all investments that are in a loss position in order to determine whether the unrealized loss, which is considered an impairment, is temporary or other-than-temporary. As mentioned above, changes in the fair value of AFS investments are reflected in OCI, unless the investment is deemed to be other-than-temporarily impaired (OTTI). Impairment is considered to be other-than-temporary if the present value of cash flows expected to be collected from the debt security is less than the amortized cost basis of the security (any such shortfall is referred to as a "credit loss"). If the Association intends to sell an impaired debt security or is more likely than not to be required to sell the security before recovery of its amortized cost basis less any current-period credit loss, the impairment is other-than-temporary and recognized currently in earnings in an amount equal to the entire difference between fair value and amortized cost. If a credit loss exists, but the Association does not intend to sell the impaired debt security and is not more likely than not to be required to sell before recovery, the impairment is other-than-temporary and is separated into (i) the estimated amount relating to credit loss, and (ii) the amount relating to all other factors. Only the estimated credit loss amount is charged to current earnings, with the

remainder of the loss amount recognized in other comprehensive income.

In subsequent periods, if the present value of cash flows expected to be collected is less than the amortized cost basis, the Association will record additional OTTI and adjust the yield of the security prospectively. The amount of total OTTI for an AFS security that previously was impaired is determined as the difference between its carrying amount prior to the determination of OTTI and its fair value.

Interest on investment securities, including amortization of premiums and accretion of discounts, is included in Interest Income. Realized gains and losses from the sales of investment securities are recognized in current earnings using the specific identification method.

Other Investments
As discussed in Note 8, certain investments, consisting primarily of mutual funds, are held in trust and investment accounts and are reported at fair value. Holding period gains and losses are included within other noninterest income on the Consolidated Statements of Income and the balance of these investments, totaling $66, is included in Other Assets on the accompanying Consolidated Balance Sheet as of December 31, 2016.

Investment in Other Farm Credit Institutions
The Association is required to maintain ownership in the Bank in the form of Class B and Class C stock, as presented on the Consolidated Balance Sheet as Investments in Other Farm Credit Institutions. Accounting for this investment is on the cost plus allocated equities basis.

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

H. **Employee Benefit Plans:** The Association participates in District and multi-District sponsored benefit plans. These plans include a defined benefit final average pay retirement plan, a defined benefit cash balance retirement plan, a defined benefit other postretirement benefits plan, and a defined contribution 401(k) plan.

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

Additional information for the above may be found in Note 9 and the Notes to the Combined Financial Statements of AgFirst Farm Credit Bank and District Associations' Annual Report.

Multi-Employer Defined Benefit Plans
Substantially all employees hired before November 4, 2014 may participate in either the AgFirst Farm Credit Retirement Plan or the AgFirst Farm Credit Cash Balance Retirement Plan (collectively referred to as the "Plans"), which are defined benefit plans and considered multi-employer under FASB accounting guidance. The Plans are noncontributory and include eligible Association and District employees. The "Projected Unit Credit" actuarial method is used for financial reporting purposes. The actuarially-determined costs of the Plans are allocated to each participating entity by multiplying the Plans' net pension expense by each institution's eligible service cost and accumulated benefit obligation as a percentage of the total eligible service cost and total accumulated benefit obligation for all Plan participants. The cumulative excess of amounts funded by the Association over the cost allocated to the Association is reflected as prepaid retirement expense, a component of Other Assets in the Association's Consolidated Balance Sheets.

In addition to pension benefits, the Association provides certain health care and life insurance benefits for retired employees (other postretirement benefits) through a multi-District sponsored retiree healthcare plan. Substantially all employees are eligible for those benefits when they reach early retirement age while working for the Association. Certain charges related to this plan are an allocation of District charges based on the Association's proportional share of the plan liability. Authoritative accounting guidance requires the accrual of the expected cost of providing these benefits to an employee, their beneficiaries and covered dependents during the years the employee renders service necessary to become eligible for benefits. The cumulative excess of cost allocated to the Association over the amounts funded by the Association is reflected as postretirement benefits other than pensions, a component of Other Liabilities in the Association's Consolidated Balance Sheets.

Since the foregoing plans are multi-employer, the Association does not apply the provisions of FASB guidance on employers' accounting for defined benefit pension and other postretirement plans in its stand-alone financial statements. Rather, the effects of this guidance are reflected in the Combined Financial Statements of AgFirst Farm Credit Bank and District Associations.

Additional information for the above may be found in Note 9 and the Notes to the Combined Financial Statements of AgFirst Farm Credit Bank and District Associations' Annual Report.

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

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

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

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

The Association is eligible to operate as a cooperative that qualifies for tax treatment under Subchapter T of the Internal Revenue Code. Accordingly, under specified conditions, the Association can exclude from taxable income amounts distributed as qualified patronage refunds in the form of cash, stock or allocated surplus. Provisions for income taxes are made only on those taxable earnings that will not be distributed as qualified patronage refunds. The Association distributes patronage on the basis of book income.

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

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

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

K. **Valuation Methodologies:** FASB guidance defines fair value as the exchange price that would be received for an asset or paid to transfer a liability in an orderly transaction between market participants in the principal or most advantageous market for the asset or liability. This guidance also establishes a fair value hierarchy, which requires an entity to maximize the use of observable inputs and minimize the use of unobservable inputs when measuring fair value. It prescribes three levels of inputs that may be used to measure fair value.

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

Level 2 inputs to the valuation methodology include quoted prices for similar assets and liabilities in active markets; quoted prices in markets that are not active; and inputs that are observable, or can be corroborated, for substantially the full term of the asset or liability.

Level 3 inputs to the valuation methodology are unobservable and supported by little or no market activity. Valuation is determined using pricing models, discounted cash flow methodologies, or similar techniques, and could include significant management judgment or estimation. Level 3 assets and liabilities also could include instruments whose price has been adjusted based on dealer quoted pricing that is different than a third-party valuation or internal model pricing.

The Association may use the Bank, internal resources or third parties to obtain fair value prices. Quoted market prices are generally used when estimating fair values of any assets or liabilities for which observable, active markets exist.

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

Please see further discussion in Note 8.

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

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

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

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

N. **Accounting Standards Updates (ASUs):** In January, 2017, the FASB issued ASU 2017-01 Business Combinations (Topic 805): Clarifying the Definition of a Business. The amendments provide a more robust framework to use in determining when a set of assets and activities is a business. They also support more consistency in applying the guidance, reduce the costs of application, and make the definition of a business more operable. For public business entities, the ASU is effective for annual periods beginning after December 15, 2017, including interim periods within those periods. The amendments should be applied prospectively. Application of this guidance is not expected to have a material impact on the Association's financial condition or results of operations.

In November, 2016, the FASB issued ASU 2016-18 Statement of Cash Flows (Topic 230): Restricted Cash. The Update clarifies that amounts generally described as restricted cash and restricted cash equivalents should be included with cash and cash equivalents when reconciling the beginning-of-period and end-of-period total amounts shown on the statement of cash flows. The amendments are effective for public business entities for fiscal years beginning after December 15, 2017, and interim periods within those fiscal years. Early adoption is permitted using a retrospective transition method to each period presented. Application of this guidance is not expected to have a material impact on the Association's financial condition or results of operations.

In October, 2016, the FASB issued ASU 2016-17 Consolidation (Topic 810): Interests Held through Related Parties That Are under Common Control. If a reporting entity satisfies the first characteristic of a primary beneficiary of a variable interest entity (VIE), the amendments in this Update require that reporting entity, in determining whether it satisfies the second characteristic of a primary beneficiary, to include all of its direct variable interests in a VIE and, on a proportionate basis, its indirect variable interests in a VIE held through related parties, including related parties that are under common control with the reporting entity. That is, a single decision maker is not required to consider indirect interests held through related parties that are under common control with the single decision maker to be the equivalent of direct interests in their entirety. Instead, a single decision maker is required to include those interests on a proportionate basis consistent with indirect interests held through other related parties. The amendments are effective for public business entities for fiscal years beginning after December 15, 2016, including interim periods within those fiscal years. Application of this guidance is not expected to have a material impact on the Association's financial condition or results of operations.

In October, 2016, the FASB issued ASU 2016-16 Income Taxes (Topic 740): Intra-Entity Transfers of Assets Other Than Inventory. The Update requires an entity to recognize the income tax consequences of an intra-entity transfer of an asset other than inventory when the transfer occurs. Consequently, the amendments in this Update eliminate the exception for an intra-entity transfer of an asset other than inventory. The amendments in this Update align the recognition of income tax consequences for intra-entity transfers of assets other than inventory with International Financial Reporting Standards (IFRS). For public business entities, the amendments are effective, on a modified retrospective basis, for annual reporting periods beginning after December 15, 2017, including interim reporting periods within those annual reporting periods. Application of this guidance is not expected to have a material impact on the Association's financial condition or results of operations.

In August, 2016, the FASB issued ASU 2016-15 Statement of Cash Flows (Topic 230): Classification of Certain Cash Receipts and Cash Payments (a consensus of the Emerging Issues Task Force). Stakeholders had indicated there was diversity in practice in how certain cash receipts and cash payments are presented and classified in the statement of cash flows. The Update addresses eight specific cash flow issues with the objective of reducing the existing diversity in practice. The amendments are effective for public business entities for fiscal years beginning after December 15, 2017, and interim periods within those fiscal years. Early adoption is permitted, including adoption in an interim period. An entity that elects early adoption must adopt all of the amendments in the same period. The amendments are to be applied using a retrospective transition method to each period presented. Application of this guidance is not expected to have a material impact on the Association's financial condition or results of operations.

In June, 2016, the FASB issued ASU 2016-13 Financial Instruments—Credit Losses (Topic 326): Measurement of Credit Losses on Financial Instruments. The Update improves financial reporting by requiring timelier recording of credit losses on financial instruments. It requires an organization to measure all expected credit losses for financial assets held at the reporting date. Financial institutions and other organizations will use forward-looking information to better estimate their credit losses. Many of the loss estimation techniques applied today will still be permitted, although the inputs to those techniques will change to reflect the full amount of expected credit losses. Organizations will continue to use judgment to determine which loss estimation method is appropriate for their circumstances. The ASU requires enhanced disclosures to help investors and other financial statement users better understand significant estimates and judgments used in estimating credit losses, as well as the credit quality and underwriting standards of an organization's portfolio. Additionally, the ASU amends the accounting for credit losses on available-for-sale debt securities and purchased financial assets with credit deterioration. The Update will take effect for U.S. Securities and Exchange Commission (SEC) filers for fiscal years, and interim periods within those fiscal years, beginning after December 15, 2019. For public business entities that are not SEC filers, it will take effect for fiscal years beginning after December 15, 2020,

and interim periods within those fiscal years. For all other organizations, the ASU will take effect for fiscal years beginning after December 15, 2020, and for interim periods within fiscal years beginning after December 15, 2021. Early application will be permitted for all organizations for fiscal years, and interim periods within those fiscal years, beginning after December 15, 2018. The Association will apply the ASU guidance as a public business entity that is not a SEC filer. The Association is in the process of evaluating what effects the guidance may have on the statements of financial condition and results of operations.

In February, 2016, the FASB issued ASU 2016-02 Leases (Topic 842). The Update is intended to improve financial reporting about leasing transactions. The ASU affects all companies and other organizations that lease assets such as real estate, airplanes, and manufacturing equipment. The ASU will require organizations that lease assets—referred to as “lessees”—to recognize on the balance sheet the assets and liabilities for the rights and obligations created by those leases. A lessee will be required to recognize assets and liabilities for leases with lease terms of more than 12 months. Consistent with current guidance, the recognition, measurement, and presentation of expenses and cash flows arising from a lease by a lessee primarily will depend on its classification as a finance or operating lease. However, the new ASU will require both types of leases to be recognized on the balance sheet. The Update also will require disclosures to help investors and other financial statement users better understand the amount, timing, and uncertainty of cash flows arising from leases. These disclosures include qualitative and quantitative requirements, providing additional information about the amounts recorded in the financial statements. The accounting by organizations that own the assets leased by the lessee—also known as lessor accounting—will remain largely unchanged from current guidance. However, the ASU contains some targeted improvements that are intended to align, where necessary, lessor accounting with the lessee accounting model and with the updated revenue recognition guidance issued in 2014. The amendments are effective for public business entities for fiscal years, and interim periods within those fiscal years, beginning after December 15, 2018. Early application will be permitted for all organizations. The Association is in the process of evaluating what effects the guidance may have on the statements of financial condition and results of operations.

In January, 2016, the FASB issued Accounting Standards Update (ASU) 2016-01 Financial Instruments—Overall (Subtopic 825-10): Recognition and Measurement of Financial Assets and Financial Liabilities. The amendments are intended to improve the recognition and measurement of financial instruments. The Update affects public and private companies, not-for-profit organizations, and employee benefit plans that hold financial assets or owe financial liabilities. The new guidance makes targeted improvements to existing GAAP by requiring equity investments (except those accounted for under the equity method of accounting, or those that result in consolidation of the investee) to be measured at fair value with changes in fair value recognized in net income, requiring public business entities to use the exit price notion when measuring the fair value of financial instruments for disclosure purposes, requiring separate presentation of financial assets and financial liabilities by measurement category and form of financial asset (that is, securities or loans and receivables) on the balance sheet or the accompanying notes to the financial statements, eliminating the requirement to disclose the fair value of financial instruments measured at amortized cost for organizations that are not public business entities, eliminating the requirement for public business entities to disclose the method(s) and significant assumptions used to estimate the fair value that is required to be disclosed for financial instruments measured at amortized cost on the balance sheet, and requiring a reporting organization to present separately in other comprehensive income the portion of the total change in the fair value of a liability resulting from a change in the instrument-specific credit risk (also referred to as “own credit”) when the organization has elected to measure the liability at fair value in accordance with the fair value option for financial instruments. The ASU is effective for public business entities for fiscal years beginning after December 15, 2017, including interim periods within those fiscal years. The Association is in the process of evaluating what effects the guidance may have on the statements of financial condition and results of operations.

In September, 2015, the FASB issued ASU 2015-16 Business Combinations (Topic 805): Simplifying the Accounting for Measurement-Period Adjustments. The amendments in this Update require that an acquirer recognize adjustments to provisional amounts that are identified during the measurement period in the reporting period in which the adjustment amounts are determined and to present separately on the face of the income statement or disclose in the notes the portion of the amount recorded in current-period earnings by line item that would have been recorded in previous reporting periods if the adjustment to the provisional amounts had been recognized as of the acquisition date. For public business entities, the amendments were effective for fiscal years beginning after December 15, 2015, including interim periods within those fiscal years. Adoption of this guidance was applied prospectively and did not have an impact on the Association’s financial condition or results of operations.

In February, 2015, the FASB issued ASU 2015-02, Consolidation (Topic 810): Amendments to the Consolidation Analysis. The amendments affect reporting entities that are required to evaluate whether they should consolidate certain legal entities. All legal entities are subject to reevaluation under the revised consolidation model. Specifically, the amendments modify the evaluation of whether limited partnerships and similar legal entities are VIEs or voting interest entities, eliminate the presumption that a general partner should consolidate a limited partnership, affect the consolidation analysis of reporting entities that are involved with VIEs, particularly those that have fee arrangements and related party relationships, and provide a scope exception from consolidation guidance for reporting entities with interests in legal entities that are required to comply with or operate in accordance with requirements that are similar to those in Rule 2a-7 of the Investment Company Act of 1940 for registered money market funds. The amendments in this Update were effective for public business entities for fiscal years, and for interim periods within those fiscal years, beginning after December 15, 2015. Adoption of this guidance was applied on a modified retrospective basis and

did not have an impact on the Association's financial condition or results of operations.

In August, 2014, the FASB issued ASU 2014-15, Presentation of Financial Statements—Going Concern (Subtopic 205-40): Disclosure of Uncertainties about an Entity's Ability to Continue as a Going Concern. The Update is intended to define management's responsibility to evaluate whether there is substantial doubt about an organization's ability to continue as a going concern and to provide related footnote disclosures. Under GAAP, financial statements are prepared under the presumption that the reporting organization will continue to operate as a going concern, except in limited circumstances. Financial reporting under this presumption is commonly referred to as the going concern basis of accounting. The going concern basis of accounting is critical to financial reporting because it establishes the fundamental basis for measuring and classifying assets and liabilities. Currently, GAAP lacks guidance about management's responsibility to evaluate whether there is substantial doubt about the organization's ability to continue as a going concern or to provide related footnote disclosures. The Update provides guidance to an organization's management, with principles and definitions that are intended to reduce diversity in the timing and content of disclosures that are commonly provided by organizations today in the financial statement footnotes. The amendments in this Update apply to all companies and not-for-profit organizations and became effective in the annual period ended after December 15, 2016, with early application permitted. Adoption of this guidance was applied prospectively and did not have a material impact on the Association's financial condition or results of operations.

In May 2014, the FASB, responsible for U.S. Generally Accepted Accounting Principles (U.S. GAAP), and the International Accounting Standards Board (IASB), responsible for International Financial Reporting Standards (IFRS), jointly issued converged standards on the recognition of revenue from contracts with customers. ASU 2014-09, Revenue from Contracts with Customers (Topic 606) and IFRS 15 "Revenue from Contracts with Customers" are intended to improve the financial reporting of revenue and comparability of the top line in financial statements globally and supersede substantially all previous revenue recognition guidance. The core principle of the new standards is for companies to recognize revenue to depict the transfer of goods or services to customers in amounts that reflect the consideration (that is, payment) to which the company expects to be entitled in exchange for those goods or services. The new standards also will result in enhanced disclosures about revenue, provide guidance for transactions that were not previously addressed comprehensively (for example, service revenue and contract modifications) and improve guidance for multiple-element arrangements. Because of the pervasive nature of the new guidance, the boards have established a joint transition resource group (TRG) in order to aid transition to the new standard. Based on input received from its stakeholders and Revenue Recognition TRG, the FASB has issued five Updates related to this ASU. The Updates generally provided clarifying guidance where there was the potential for diversity in practice, or to address the cost and complexity of applying Topic 606. Collectively, the Updates are not expected to have a significant effect on implementation of the guidance. For public business entities, the amendments in the Update are effective for annual reporting periods beginning after December 15, 2017, including interim periods within that reporting period. Early application is not permitted. The amendments are to be applied retrospectively. The Association has identified ancillary revenues that will be affected by this Update. However, because financial instruments are not within the scope of the guidance, it is expected that adoption will not have a material impact on the Association's financial condition or results of operations, but may result in additional disclosures.

Note 3 — Loans and Allowance for Loan Losses

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

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

The credit risk management process begins with an analysis of the obligor's credit history, repayment capacity and financial position. Repayment capacity focuses on the obligor's ability to repay the obligation based on cash flows from operations or other sources of income, including non-farm income. Real estate mortgage loans must be secured by first liens on the real estate collateral. As required by FCA regulations, each institution that makes loans on a secured basis must have collateral evaluation policies and procedures.

The credit risk rating process for loans uses a two-dimensional structure, incorporating a 14-point probability of default scale (see further discussion in Note 2 subsection B above) and a separate scale addressing estimated percentage loss in the event of default. The loan rating structure incorporates borrower risk and transaction risk. Borrower risk is the risk of loss driven by factors intrinsic to the borrower. The transaction risk or facility risk is related to the structure of a credit (tenor, terms, and collateral).

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

- Real estate mortgage loans — loans made to full-time or part-time farmers secured by first lien real estate mortgages with maturities from five to thirty years. These loans may be made only in amounts up to 85 percent of the appraised value of the property taken as security or up to 97 percent of the appraised value if guaranteed by a federal, state, or other governmental agency. The actual percentage of loan-to-appraised value when loans are made is generally lower than the statutory required percentage.

- Production and intermediate-term loans — loans to full-time or part-time farmers that are not real estate mortgage loans. These loans fund eligible financing needs including

operating inputs (such as labor, feed, fertilizer, and repairs), livestock, living expenses, income taxes, machinery or equipment, farm buildings, and other business-related expenses. Production loans may be made on a secured or unsecured basis and are most often made for a period of time that matches the borrower's normal production and marketing cycle, which is typically one year or less. Intermediate-term loans are made for a specific term, generally greater than one year and less than or equal to ten years.

- Loans to cooperatives — loans for any cooperative purpose other than for communication, power, and water and waste disposal.
- Processing and marketing loans — loans for operations to process or market the products produced by a farmer, rancher, or producer or harvester of aquatic products, or by a cooperative.
- Farm-related business loans — loans to eligible borrowers that furnish certain farm-related business services to farmers or ranchers that are directly related to their agricultural production.
- Rural residential real estate loans — loans made to individuals, who are not farmers, to purchase a single-family dwelling that will be the primary residence in open country, which may include a town or village that has a population of not more than 2,500 persons. In addition, the loan may be to remodel, improve, or repair a rural home, or to refinance existing debt. These loans are generally secured by a first lien on the property.
- Communication loans — loans primarily to finance rural communication providers.
- Power loans — loans primarily to finance electric generation, transmission and distribution systems serving rural areas.
- Water and waste disposal loans — loans primarily to finance water and waste disposal systems serving rural areas.
- International loans — primarily loans or credit enhancements to other banks to support the export of U.S. agricultural commodities or supplies. The federal government guarantees a substantial portion of these loans.
- Lease receivables — the net investment for all finance leases such as direct financing leases, leveraged leases, and sales-type leases.
- Other (including Mission Related) — additional investments in rural America approved by the FCA on a program or a case-by-case basis. Examples of such investments include partnerships with agricultural and rural community lenders, investments in rural economic development and infrastructure, and investments in obligations and mortgage securities that increase the availability of affordable housing in rural America.

A summary of loans outstanding at period end follows:

	December 31,		
	2016	2015	2014
Real estate mortgage	$ 527,783	$ 526,365	$ 502,448
Production and intermediate-term	287,275	259,901	247,835
Loans to cooperatives	6,376	249	250
Processing and marketing	21,776	28,833	25,853
Farm-related business	4,023	6,376	5,641
Communication	952	2,751	3,123
Power and water/waste disposal	276	276	276
Rural residential real estate	4,877	5,503	4,267
International	3,257	–	–
Lease receivables	2,962	–	–
Total Loans	$ 859,557	$ 830,254	$ 789,693

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

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

The Association may purchase or sell participation interests with other parties in order to diversify risk, manage loan volume, and comply with FCA regulations. The following tables present the principal balance of participation loans at periods ended:

	December 31, 2016							
	Within AgFirst District		Within Farm Credit System		Outside Farm Credit System		Total	
	Participations Purchased	Participations Sold	Participations Purchased	Participations Sold	Participations Purchased	Participations Sold	Participations Purchased	Participations Sold
Real estate mortgage	$ 2,170	$ 59,066	$ –	$ –	$ –	$ 7,083	$ 2,170	$ 66,149
Production and intermediate-term	23,977	131,621	–	–	5,849	–	29,826	131,621
Loans to cooperatives	6,383	–	–	–	–	–	6,383	–
Processing and marketing	10,436	15,944	–	–	–	–	10,436	15,944
Farm-related business	1,253	–	–	–	–	–	1,253	–
Communication	953	–	–	–	–	–	953	–
Power and water/waste disposal	276	–	–	–	–	–	276	–
Lease receivables	–	–	2,962	–	–	–	2,962	–
International	3,263	–	–	–	–	–	3,263	–
Total	$ 48,711	$ 206,631	$ 2,962	$ –	$ 5,849	$ 7,083	$ 57,522	$ 213,714

	December 31, 2015							
	Within AgFirst District		Within Farm Credit System		Outside Farm Credit System		Total	
	Participations Purchased	Participations Sold	Participations Purchased	Participations Sold	Participations Purchased	Participations Sold	Participations Purchased	Participations Sold
Real estate mortgage	$ 356	$ 110,056	$ –	$ –	$ –	$ 12,369	$ 356	$ 122,425
Production and intermediate-term	16,756	64,987	735	–	520	–	18,011	64,987
Loans to cooperatives	251	–	–	–	–	–	251	–
Processing and marketing	20,222	867	–	–	–	–	20,222	867
Farm-related business	4,546	–	–	–	–	–	4,546	–
Communication	2,756	–	–	–	–	–	2,756	–
Power and water/waste disposal	276	–	–	–	–	–	276	–
Total	$ 45,163	$ 175,910	$ 735	$ –	$ 520	$ 12,369	$ 46,418	$ 188,279

	December 31, 2014							
	Within AgFirst District		Within Farm Credit System		Outside Farm Credit System		Total	
	Participations Purchased	Participations Sold	Participations Purchased	Participations Sold	Participations Purchased	Participations Sold	Participations Purchased	Participations Sold
Real estate mortgage	$ 57	$ 69,675	$ –	$ –	$ –	$ 17,655	$ 57	$ 87,330
Production and intermediate-term	13,370	85,279	–	–	621	–	13,991	85,279
Loans to cooperatives	251	–	–	–	–	–	251	–
Processing and marketing	13,214	933	–	–	–	–	13,214	933
Farm-related business	3,442	–	–	–	–	–	3,442	–
Communication	3,124	–	–	–	–	–	3,124	–
Power and water/waste disposal	276	–	–	–	–	–	276	–
Total	$ 33,734	$ 155,887	$ –	$ –	$ 621	$ 17,655	$ 34,355	$ 173,542

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

	December 31, 2016			
	Due less than 1 year	Due 1 Through 5 years	Due after 5 years	Total
Real estate mortgage	$ 11,076	$ 89,096	$ 427,611	$ 527,783
Production and intermediate-term	100,803	101,020	85,452	287,275
Loans to cooperatives	–	3,907	2,469	6,376
Processing and marketing	5,119	11,798	4,859	21,776
Farm-related business	1,102	2,491	430	4,023
Communication	–	952	–	952
Power and water/waste disposal	–	276	–	276
Rural residential real estate	14	666	4,197	4,877
International	–	2,507	750	3,257
Lease receivables	–	16	2,946	2,962
Total Loans	$ 118,114	$ 212,729	$ 528,714	$ 859,557
Percentage	13.74%	24.75%	61.51%	100.00%

The recorded investment in a receivable is the face amount increased or decreased by applicable accrued interest and unamortized premium, discount, finance charges, or acquisition costs and may also reflect a previous direct write-down of the investment.

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

	December 31, 2016	2015	2014
Real estate mortgage:			
Acceptable	92.30%	93.72%	94.25%
OAEM	4.76	3.21	2.78
Substandard/doubtful/loss	2.94	3.07	2.97
	100.00%	100.00%	100.00%
Production and intermediate-term:			
Acceptable	89.47%	89.79%	90.02%
OAEM	7.04	4.96	5.60
Substandard/doubtful/loss	3.49	5.25	4.38
	100.00%	100.00%	100.00%
Loans to cooperatives:			
Acceptable	100.00%	100.00%	100.00%
OAEM	–	–	–
Substandard/doubtful/loss	–	–	–
	100.00%	100.00%	100.00%
Processing and marketing:			
Acceptable	79.37%	80.46%	86.37%
OAEM	–	11.80	2.77
Substandard/doubtful/loss	20.63	7.74	10.86
	100.00%	100.00%	100.00%
Farm-related business:			
Acceptable	100.00%	100.00%	100.00%
OAEM	–	–	–
Substandard/doubtful/loss	–	–	–
	100.00%	100.00%	100.00%

	December 31, 2016	2015	2014
Communication:			
Acceptable	100.00%	100.00%	100.00%
OAEM	–	–	–
Substandard/doubtful/loss	–	–	–
	100.00%	100.00%	100.00%
Power and water/waste disposal:			
Acceptable	100.00%	100.00%	100.00%
OAEM	–	–	–
Substandard/doubtful/loss	–	–	–
	100.00%	100.00%	100.00%
Rural residential real estate:			
Acceptable	92.59%	95.18%	91.93%
OAEM	5.63	3.22	5.51
Substandard/doubtful/loss	1.78	1.60	2.56
	100.00%	100.00%	100.00%
International:			
Acceptable	100.00%	–%	–%
OAEM	–	–	–
Substandard/doubtful/loss	–	–	–
	100.00%	–%	–%
Lease receivables:			
Acceptable	99.46%	–%	–%
OAEM	0.54	–	–
Substandard/doubtful/loss	–	–	–
	100.00%	–%	–%
Total Loans:			
Acceptable	91.18%	92.11%	92.72%
OAEM	5.32	4.02	3.65
Substandard/doubtful/loss	3.50	3.87	3.63
	100.00%	100.00%	100.00%

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

December 31, 2016	30 Through 89 Days Past Due	90 Days or More Past Due	Total Past Due	Not Past Due or Less Than 30 Days Past Due	Total Loans	Recorded Investment 90 Days or More Past Due and Accruing Interest
Real estate mortgage	$ 2,441	$ 6,050	$ 8,491	$ 523,831	$ 532,322	$ –
Production and intermediate-term	1,671	6,177	7,848	282,685	290,533	–
Loans to cooperatives	–	–	–	6,381	6,381	–
Processing and marketing	–	4,502	4,502	17,317	21,819	–
Farm-related business	–	–	–	4,033	4,033	–
Communication	–	–	–	952	952	–
Power and water/waste disposal	–	–	–	276	276	–
Rural residential real estate	–	9	9	4,882	4,891	–
International	–	–	–	3,288	3,288	–
Lease receivables	–	–	–	2,973	2,973	–
Total	$ 4,112	$ 16,738	$ 20,850	$ 846,618	$ 867,468	$ –

December 31, 2015	30 Through 89 Days Past Due	90 Days or More Past Due	Total Past Due	Not Past Due or Less Than 30 Days Past Due	Total Loans	Recorded Investment 90 Days or More Past Due and Accruing Interest
Real estate mortgage	$ 5,666	$ 6,192	$ 11,858	$ 518,853	$ 530,711	$ –
Production and intermediate-term	2,224	4,084	6,308	256,423	262,731	–
Loans to cooperatives	–	–	–	250	250	–
Processing and marketing	1,500	–	1,500	27,402	28,902	–
Farm-related business	–	–	–	6,402	6,402	–
Communication	–	–	–	2,751	2,751	–
Power and water/waste disposal	–	–	–	276	276	–
Rural residential real estate	–	56	56	5,464	5,520	–
Total	$ 9,390	$ 10,332	$ 19,722	$ 817,821	$ 837,543	$ –

	December 31, 2014					
	30 Through 89 Days Past Due	90 Days or More Past Due	Total Past Due	Not Past Due or Less Than 30 Days Past Due	Total Loans	Recorded Investment 90 Days or More Past Due and Accruing Interest
Real estate mortgage	$ 1,886	$ 2,093	$ 3,979	$ 502,596	$ 506,575	$ –
Production and intermediate-term	2,037	3,777	5,814	244,747	250,561	–
Loans to cooperatives	–	–	–	250	250	–
Processing and marketing	–	–	–	26,055	26,055	–
Farm-related business	–	–	–	5,648	5,648	–
Communication	–	–	–	3,123	3,123	–
Power and water/waste disposal	–	–	–	276	276	–
Rural residential real estate	46	63	109	4,172	4,281	–
Total	$ 3,969	$ 5,933	$ 9,902	$ 786,867	$ 796,769	$ –

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

	December 31,		
	2016	2015	2014
Nonaccrual loans:			
Real estate mortgage	$ 7,714	$ 11,264	$ 6,330
Production and intermediate-term	7,391	7,882	4,847
Processing and marketing	4,502	1,500	–
Rural residential real estate	55	56	63
Total	$ 19,662	$ 20,702	$ 11,240
Accruing restructured loans:			
Real estate mortgage	$ 1,170	$ 1,304	$ 712
Production and intermediate-term	2,376	2,144	571
Total	$ 3,546	$ 3,448	$ 1,283
Total nonperforming loans	$ 23,208	$ 24,150	$ 12,523
Other property owned	1,876	1,356	4,976
Total nonperforming assets	$ 25,084	$ 25,506	$ 17,499
Nonaccrual loans as a percentage of total loans	2.29%	2.49%	1.42%
Nonperforming assets as a percentage of total loans and other property owned	2.91%	3.07%	2.20%
Nonperforming assets as a percentage of capital	13.37%	14.38%	10.31%

There were no loans accruing and 90 days past due at December 31, 2016, 2015 and 2014.

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

	December 31,		
	2016	2015	2014
Impaired nonaccrual loans:			
Current as to principal and interest	$ 2,124	$ 2,523	$ 4,388
Past due	17,538	18,179	6,852
Total	19,662	20,702	11,240
Impaired accrual loans:			
Restructured	3,546	3,448	1,283
90 days or more past due	–	–	–
Total	3,546	3,448	1,283
Total impaired loans	$ 23,208	$ 24,150	$ 12,523
Additional commitments to lend	$ 3	$ 179	$ 3

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

	December 31, 2016			Year Ended December 31, 2016	
Impaired loans:	Recorded Investment	Unpaid Principal Balance	Related Allowance	Average Impaired Loans	Interest Income Recognized on Impaired Loans
With a related allowance for credit losses:					
Real estate mortgage	$ 1,622	$ 1,549	$ 233	$ 1,622	$ 61
Production and intermediate-term	3,805	3,885	1,380	3,805	143
Processing and marketing	–	–	–	–	–
Rural residential real estate	–	–	–	–	–
Total	$ 5,427	$ 5,434	$ 1,613	$ 5,427	$ 204
With no related allowance for credit losses:					
Real estate mortgage	$ 7,262	$ 7,687	$ –	$ 7,260	$ 273
Production and intermediate-term	5,962	6,480	–	5,961	225
Processing and marketing	4,502	4,679	–	4,501	169
Rural residential real estate	55	112	–	55	2
Total	$ 17,781	$ 18,958	$ –	$ 17,777	$ 669
Total impaired loans:					
Real estate mortgage	$ 8,884	$ 9,236	$ 233	$ 8,882	$ 334
Production and intermediate-term	9,767	10,365	1,380	9,766	368
Processing and marketing	4,502	4,679	–	4,501	169
Rural residential real estate	55	112	–	55	2
Total	$ 23,208	$ 24,392	$ 1,613	$ 23,204	$ 873

	December 31, 2015			Year Ended December 31, 2015	
Impaired loans:	Recorded Investment	Unpaid Principal Balance	Related Allowance	Average Impaired Loans	Interest Income Recognized on Impaired Loans
With a related allowance for credit losses:					
Real estate mortgage	$ 6,076	$ 6,073	$ 754	$ 3,516	$ 211
Production and intermediate-term	5,497	5,573	919	3,180	190
Processing and marketing	1,500	1,500	–	868	52
Rural residential real estate	56	89	32	33	2
Total	$ 13,129	$ 13,235	$ 1,705	$ 7,597	$ 455
With no related allowance for credit losses:					
Real estate mortgage	$ 6,492	$ 6,954	$ –	$ 3,757	$ 225
Production and intermediate-term	4,529	4,983	–	2,620	158
Processing and marketing	–	–	–	–	–
Rural residential real estate	–	–	–	–	–
Total	$ 11,021	$ 11,937	$ –	$ 6,377	$ 383
Total impaired loans:					
Real estate mortgage	$ 12,568	$ 13,027	$ 754	$ 7,273	$ 436
Production and intermediate-term	10,026	10,556	919	5,800	348
Processing and marketing	1,500	1,500	–	868	52
Rural residential real estate	56	89	32	33	2
Total	$ 24,150	$ 25,172	$ 1,705	$ 13,974	$ 838

	December 31, 2014			Year Ended December 31, 2014	
Impaired loans:	Recorded Investment	Unpaid Principal Balance	Related Allowance	Average Impaired Loans	Interest Income Recognized on Impaired Loans
With a related allowance for credit losses:					
Real estate mortgage	$ 1,656	$ 1,674	$ 208	$ 1,859	$ 46
Production and intermediate-term	2,696	2,808	618	3,026	76
Farm-related business	–	–	–	–	–
Rural residential real estate	60	91	31	67	2
Total	$ 4,412	$ 4,573	$ 857	$ 4,952	$ 124
With no related allowance for credit losses:					
Real estate mortgage	$ 5,386	$ 6,655	$ –	$ 6,045	$ 151
Production and intermediate-term	2,722	4,827	–	3,056	77
Farm-related business	–	–	–	–	–
Rural residential real estate	3	5	–	3	–
Total	$ 8,111	$ 11,487	$ –	$ 9,104	$ 228
Total impaired loans:					
Real estate mortgage	$ 7,042	$ 8,329	$ 208	$ 7,904	$ 197
Production and intermediate-term	5,418	7,635	618	6,082	153
Farm-related business	–	–	–	–	–
Rural residential real estate	63	96	31	70	2
Total	$ 12,523	$ 16,060	$ 857	$ 14,056	$ 352

The following table summarizes interest income on nonaccrual and accruing restructured loans that would have been recognized under the original terms of the loans:

	Year Ended December 31,		
	2016	2015	2014
Interest income which would have been recognized under the original loan terms	$ 1,851	$ 1,380	$ 1,051
Less: interest income recognized	873	837	352
Foregone interest income	$ 978	$ 543	$ 699

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

	Real Estate Mortgage	Production and Intermediate-term	Agribusiness*	Communication	Power and Water/Waste Disposal	Rural Residential Real Estate	International	Lease receivables	Total
Activity related to the allowance for credit losses:									
Balance at December 31, 2015	$ 4,202	$ 2,600	$ 227	$ 18	$ 2	$ 68	$ –	$ –	$ 7,117
Charge-offs	(551)	(136)	–	–	–	–	–	–	(687)
Recoveries	250	166	–	–	–	–	–	–	416
Provision for loan losses	147	756	(10)	–	–	(34)	24	9	892
Balance at December 31, 2016	$ 4,048	$ 3,386	$ 217	$ 18	$ 2	$ 34	$ 24	$ 9	$ 7,738
Balance at December 31, 2014	$ 3,087	$ 2,032	$ 184	$ 18	$ 2	$ 55	$ –	$	$ 5,378
Charge-offs	(13)	(59)	(49)	–	–	–	–		(121)
Recoveries	1,232	6	–	–	–	–	–		1,238
Provision for loan losses	(104)	621	92	–	–	13	–		622
Balance at December 31, 2015	$ 4,202	$ 2,600	$ 227	$ 18	$ 2	$ 68	$ –	$	$ 7,117
Balance at December 31, 2013	$ 3,213	$ 2,615	$ 149	$ 21	$ 2	$ 57	$ –	$	$ 6,057
Charge-offs	(150)	(955)	–	–	–	–	–		(1,105)
Recoveries	112	140	–	–	–	–	–		252
Provision for loan losses	(88)	232	35	(3)	–	(2)	–		174
Balance at December 31, 2014	$ 3,087	$ 2,032	$ 184	$ 18	$ 2	$ 55	$ –	$	$ 5,378
Allowance on loans evaluated for impairment:									
Individually	$ 233	$ 1,380	$ –	$ –	$ –	$ –	$ –	$ –	$ 1,613
Collectively	3,815	2,006	217	18	2	34	24	9	6,125
Balance at December 31, 2016	$ 4,048	$ 3,386	$ 217	$ 18	$ 2	$ 34	$ 24	$ 9	$ 7,738
Individually	$ 754	$ 919	$ –	$ –	$ –	$ 32	$ –	$	$ 1,705
Collectively	3,448	1,681	227	18	2	36	–		5,412
Balance at December 31, 2015	$ 4,202	$ 2,600	$ 227	$ 18	$ 2	$ 68	$ –	$	$ 7,117
Individually	$ 208	$ 618	$ –	$ –	$ –	$ 31	$ –	$	$ 857
Collectively	2,879	1,414	184	18	2	24	–		4,521
Balance at December 31, 2014	$ 3,087	$ 2,032	$ 184	$ 18	$ 2	$ 55	$ –	$	$ 5,378
Recorded investment in loans evaluated for impairment:									
Individually	$ 8,883	$ 9,767	$ 4,502	$ –	$ –	$ 55	$ –	$ –	$ 23,207
Collectively	523,439	280,766	27,731	952	276	4,836	3,288	2,973	844,261
Balance at December 31, 2016	$ 532,322	$ 290,533	$ 32,233	$ 952	$ 276	$ 4,891	$ 3,288	$ 2,973	$ 867,468
Individually	$ 12,584	$ 10,082	$ 1,500	$ –	$ –	$ 56	$ –	$	$ 24,222
Collectively	518,135	252,641	34,054	2,751	276	5,464	–		813,321
Balance at December 31, 2015	$ 530,719	$ 262,723	$ 35,554	$ 2,751	$ 276	$ 5,520	$ –	$	$ 837,543
Individually	$ 7,195	$ 5,277	$ –	$ –	$ –	$ 109	$ –	$	$ 12,581
Collectively	499,380	245,284	31,953	3,123	276	4,172	–		784,188
Balance at December 31, 2014	$ 506,575	$ 250,561	$ 31,953	$ 3,123	$ 276	$ 4,281	$ –	$	$ 796,769

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

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

	Year Ended December 31, 2016				
Outstanding Recorded Investment	Interest Concessions	Principal Concessions	Other Concessions	Total	Charge-offs
Pre-modification:					
Real estate mortgage	$ –	$ 74	$ –	$ 74	
Production and intermediate-term	–	866	–	866	
Rural residential real estate	–	103	–	103	
Total	$ –	$ 1,043	$ –	$ 1,043	
Post-modification:					
Real estate mortgage	$ –	$ 74	$ –	$ 74	$ –
Production and intermediate-term	–	871	–	871	–
Rural residential real estate	–	103	–	103	–
Total	$ –	$ 1,048	$ –	$ 1,048	$ –

	Year Ended December 31, 2015				
Outstanding Recorded Investment	Interest Concessions	Principal Concessions	Other Concessions	Total	Charge-offs
Pre-modification:					
Real estate mortgage	$ –	$ 1,707	$ –	$ 1,707	
Production and intermediate-term	–	2,046	–	2,046	
Total	$ –	$ 3,753	$ –	$ 3,753	
Post-modification:					
Real estate mortgage	$ –	$ 1,715	$ –	$ 1,715	$ –
Production and intermediate-term	–	2,046	–	2,046	–
Total	$ –	$ 3,761	$ –	$ 3,761	$ –

	Year Ended December 31, 2014				
Outstanding Recorded Investment	Interest Concessions	Principal Concessions	Other Concessions	Total	Charge-offs
Pre-modification:					
Real estate mortgage	$ –	$ 60	$ –	$ 60	
Production and intermediate-term	–	1,320	–	1,320	
Total	$ –	$ 1,380	$ –	$ 1,380	
Post-modification:					
Real estate mortgage	$ –	$ 60	$ –	$ 60	$ –
Production and intermediate-term	–	1,321	–	1,321	–
Total	$ –	$ 1,381	$ –	$ 1,381	$ –

Interest concessions may include interest forgiveness and interest deferment. Principal concessions may include principal forgiveness, principal deferment, and maturity extension. Other concessions may include additional compensation received which might be in the form of cash or other assets.

There were no TDRs that occurred during the previous twelve months and for which there was a subsequent payment default during the periods presented. Payment default is defined as a payment that was thirty days or more past due.

The following table provides information at period end on outstanding loans restructured in troubled debt restructurings. These loans are included as impaired loans in the impaired loan table:

	Total TDRs			Nonaccrual TDRs		
	December 31,			December 31,		
	2016	2015	2014	2016	2015	2014
Real estate mortgage	$ 1,351	$ 1,725	$ 3,027	$ 181	$ 421	$ 2,314
Production and intermediate-term	3,183	2,774	1,665	807	630	1,095
Rural residential real estate	46	–	–	46	–	–
Total Loans	$ 4,580	$ 4,499	$ 4,692	$ 1,034	$ 1,051	$ 3,409
Additional commitments to lend	$ –	$ 178	$ –			

The following table presents information as of period end:

	December 31, 2016
Carrying amount of foreclosed residential real estate properties held as a result of obtaining physical possession	$ –
Recorded investment of consumer mortgage loans secured by residential real estate for which formal foreclosure proceedings are in process	$ –

Note 4 — Investments

Investment Securities

The Association's investments consist primarily of Rural America Bonds (RABs), which are private placement securities purchased under the Mission Related Investment program approved by the FCA. In its Conditions of Approval for the program, the FCA considers a RAB ineligible if its investment rating, based on the internal 14-point risk rating scale used to also grade loans, falls below 9 and requires System institutions to provide notification to FCA when a security becomes ineligible. At December 31, 2016, the Association held no RABs whose credit quality had deteriorated beyond the program limits.

A summary of the amortized cost and fair value of investment securities held-to-maturity follows:

December 31, 2016	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value	Yield
RABs	$ 4,209	$ –	$ (248)	$ 3,961	4.91%

December 31, 2015	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value	Yield
RABs	$ 7,366	$ –	$ (279)	$ 7,087	4.40%

December 31, 2014	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value	Yield
RABs	$ 4,647	$ –	$ (335)	$ 4,312	4.89%

A summary of the contractual maturity, amortized cost and estimated fair value of investment securities held-to-maturity follows:

December 31, 2016	Amortized Cost	Fair Value	Weighted Average Yield
In one year or less	$ –	$ –	– %
After one year through five years	–	–	–
After five years through ten years	1,270	1,229	2.49
After ten years	2,939	2,732	5.95
Total	$ 4,209	$ 3,961	4.91%

A portion of these investments has contractual maturities in excess of ten years. However, expected maturities for these types of securities can differ from contractual maturities because borrowers may have the right to prepay obligations with or without prepayment penalties.

An investment is considered impaired if its fair value is less than its cost. The following tables show the fair value and gross unrealized losses for investments that were in a continuous unrealized loss position aggregated by investment category at each reporting period. A continuous unrealized loss position for an investment is measured from the date the impairment was first identified.

December 31, 2016	Less than 12 Months		12 Months or Greater	
	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
RABs	$ –	$ –	$ 3,961	$ (248)

December 31, 2015	Less than 12 Months		12 Months or Greater	
	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
RABs	$ 2,929	$ (5)	$ 4,158	$ (274)

December 31, 2014	Less than 12 Months		12 Months or Greater	
	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
RABs	$ –	$ –	$ 4,312	$ (335)

The recording of an impairment loss is predicated on: (1) whether or not management intends to sell the security, (2) whether it is more likely than not that management would be required to sell the security before recovering its costs, and (3) whether management expects to recover the security's entire amortized cost basis (even if there is no intention to sell). If the Association intends to sell the security or it is more likely than not that it would be required to sell the security, the impairment loss equals the full difference between amortized cost and fair value of the security. When the Association does not intend to sell securities in an unrealized loss position and it is not more likely than not that it would be required to sell the securities, other-than-temporary impairment loss is separated into credit loss and non-credit loss. Credit loss is defined as the shortfall of the present value of the cash flows expected to be collected in relation to the amortized cost basis.

The Association performs periodic credit reviews, including other-than-temporary impairment analyses, on its investment securities portfolio. The objective is to quantify future possible loss of principal or interest due on securities in the portfolio. Factors considered in determining whether an impairment is other-than-temporary include among others: (1) the length of time and the extent to which the fair value is less than cost, (2) adverse conditions specifically related to the industry, (3) geographic area and the condition of the underlying collateral, (4) payment structure of the security, (5) ratings by rating agencies, (6) the credit worthiness of bond insurers, and (7) volatility of the fair value changes.

The Association uses the present value of cash flows expected to be collected from each debt security to determine the amount of credit loss. This technique requires assumptions related to the underlying collateral, including default rates, amount and timing of prepayments, and loss severity. Assumptions can vary widely from security to security and are influenced by such factors as loan interest rate, geographical location of the borrower, borrower characteristics, and collateral type.

Significant inputs used to estimate the amount of credit loss include, but are not limited to, performance indicators of the underlying assets in the security (including default rates, delinquency rates, and percentage of nonperforming assets), loan-to-collateral value ratios, third-party guarantees, current levels of subordination, vintage, geographic concentration, and credit ratings. The Association may obtain assumptions for the default rate, prepayment rate, and loss severity rate from an independent third party, or generate the assumptions internally.

The Association has not recognized any credit losses in 2016 or prior years as any impairments were deemed temporary and resulted from non-credit related factors. The Association has the ability and intent to hold these temporarily impaired investments until a recovery of unrealized losses occurs, which may be at maturity, and at this time expects to collect the full principal amount and interest due on these securities, especially after considering credit enhancements.

Investments in Other Farm Credit Institutions
Investments in other Farm Credit System institutions are generally nonmarketable investments consisting of stock and participation certificates, allocated surplus, and reciprocal investments in other institutions regulated by the FCA. The Association is required to maintain ownership in the Bank in the form of Class B or Class C stock as determined by the Bank. The Bank may require additional capital contributions to maintain its capital requirements. Accounting for this investment is on the cost plus allocated equities basis.

The Association's investment in the Bank totaled $9,416 for 2016, $9,083 for 2015 and $8,890 for 2014. The Association owns 3.72 percent of the issued stock of the Bank as of December 31, 2016 net of any reciprocal investment. As of that date, the Bank's assets totaled $32.1 billion and shareholders' equity totaled $2.2 billion. The Bank's earnings were $342 million for 2016. In addition, the Association had an investment of $535 related to other Farm Credit institutions at December 31, 2016.

Note 5 — Real Estate and Other Property

Premises and Equipment
Premises and equipment consists of the following:

	December 31,		
	2016	2015	2014
Land	$ 1,032	$ 1,031	$ 978
Buildings and improvements	3,872	3,834	3,773
Furniture and equipment	2,991	2,944	2,667
	7,895	7,809	7,418
Less: accumulated depreciation	4,704	4,455	4,337
Total	$ 3,191	$ 3,354	$ 3,081

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

	December 31,		
	2016	2015	2014
(Gains) losses on sale, net	$ (91)	$ (1)	$ (128)
Carrying value unrealized (gains) losses	155	1,178	267
Operating (income) expense, net	158	(103)	348
(Gains) losses on other property owned, net	$ 222	$ 1,074	$ 487

OPO consisted of 7, 4, and 10 properties with book values of $1,876, $1,356 and $4,976 at December 31, 2016, 2015 and 2014, respectively. At December 31, 2016, OPO included 4 properties with a book value of $649 that were added to the portfolio before 2016. During 2016, 4 properties (including parcels) were sold, representing a book value of $1,021.

Gains on sales of other property owned were deferred if the sales involved financing from the Association and did not meet the criteria for immediate recognition. Deferred gains totaled $0, $91, and $106 at December 31, 2016, 2015, and 2014, respectively.

Note 6 — Debt

Notes Payable to AgFirst Farm Credit Bank
Under the Farm Credit Act, the Association is obligated to borrow only from the Bank, unless the Bank approves borrowing from other funding sources. The borrowing relationship is established with the Bank through a GFA. The GFA utilizes the Association's credit and fiscal performance as criteria for establishing a line of credit on which the Association may draw funds. The GFA has a one year term which expires on December 31 and is renewable each year. The Association has no reason to believe the GFA will not be renewed upon expiration. The Bank, consistent with FCA regulations, has established limitations on the Association's ability to borrow funds based on specified factors or formulas relating primarily to credit quality and financial condition. At December 31, 2016, the Association's notes payable were within the specified limitations.

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

The weighted average interest rates on the variable rate advances were 1.86 percent for LIBOR-based loans and 1.82 percent for Prime-based loans, and the weighted average remaining maturities were 3.1 years and 3.4 years, respectively, at December 31, 2016. The weighted-average interest rate on the fixed rate and adjustable rate mortgage (ARM) loans which are match funded by the Bank was 2.57 percent, and the

weighted average remaining maturity was 7.9 years at December 31, 2016. The weighted-average interest rate on all interest-bearing notes payable was 2.43 percent and the weighted-average remaining maturity was 6.9 years at December 31, 2016. Variable rate and fixed rate notes payable represent approximately 0.60 percent and 99.40 percent, respectively, of total notes payable at December 31, 2016. The weighted average maturities described above are related to matched-funded loans. The direct note itself has an annual maturity as prescribed in the GFA.

Note 7 — Members' Equity

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

A. **Protected Borrower Stock:** Protection of certain borrower stock is provided under the Farm Credit Act which requires the Association, when retiring protected borrower stock, to retire such stock at par or stated value regardless of its book value. Protected borrower stock includes capital stock and participation certificates which were outstanding as of January 6, 1988, or were issued or allocated prior to October 6, 1988. If an Association is unable to retire protected borrower stock at par value or stated value, amounts required to retire this equity would be obtained from the Insurance Fund.

B. **Capital Stock and Participation Certificates:** In accordance with the Farm Credit Act and the Association's capitalization bylaws, each borrower is required to invest in Class C stock for agricultural loans, or participation certificates in the case of rural home and farm related business loans, as a condition of borrowing. The initial borrower investment, through either purchase or transfer, must be in an amount equal to 200 shares ($1,000.00) or one (1) share for each $250.00 (or fraction thereof) of the amount of the loan. The Board of Directors may increase the amount of investment if necessary to meet the Association's capital needs. Loans designated for sale or sold into the Secondary Market on or after April 16, 1996 will have no voting stock or participation certificate purchase requirement if sold within 180 days following the date of designation.

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

C. **Regulatory Capitalization Requirements and Restrictions:** FCA regulations require that certain minimum standards for capital be achieved and maintained. These standards are measured based on capital as a percentage of risk-adjusted assets and off-balance-sheet commitments and surplus levels as a percentage of risk-adjusted assets.

Failure to meet the capital requirements can initiate certain mandatory and possibly additional discretionary actions by FCA that, if undertaken, could have a direct material effect on the Association's consolidated financial statements. The Association is prohibited from reducing permanent capital by retiring stock or making certain other distributions to shareholders unless prescribed capital standards are met.

The Association's capital ratios as of December 31 and the FCA minimum requirements follow:

	2016	2015	2014	Regulatory Minimum
Permanent capital ratio	22.23%	22.23%	23.30%	7.00%
Total surplus ratio	21.93%	21.91%	22.96%	7.00%
Core surplus ratio	21.93%	21.91%	22.96%	3.50%

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

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

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

The Association had the following shares outstanding at December 31, 2016:

		Shares Outstanding	
Class	Protected	Number	Aggregate Par Value
B Common/Nonvoting	Yes	580	$ 3
C Common/Voting	No	474,547	2,373
C Participation Certificates/Nonvoting	No	16,236	81
Total Capital Stock and Participation Certificates		491,363	$ 2,457

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

Retained Earnings

The Association maintains an unallocated retained earnings account and an allocated retained earnings account. The minimum aggregate amount of these two accounts is

determined by the Board. At the end of any fiscal year, if the retained earnings accounts otherwise would be less than the minimum amount determined by the Board as necessary to maintain adequate capital reserves to meet the commitments of the Association, the Association shall apply earnings for the year to the unallocated retained earnings account in such amounts as may be determined necessary by the Board. Unallocated retained earnings are maintained for each borrower to permit liquidation on a patronage basis.

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

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

Allocated equities shall be retired solely at the discretion of the Board, provided that minimum capital standards established by the FCA and the Board are met. All nonqualified distributions are tax deductible only when redeemed.

At December 31, 2016, allocated members' equity consisted of $90,846 of nonqualified retained surplus.

Dividends

The Association may declare noncumulative dividends on its capital stock and participation certificates provided the dividend rate does not exceed 20 percent of the par value of the respective capital stock and participation certificates. Such dividends may be paid solely on Classes D Preferred Stock or on all classes of stock and participation certificates.

The rate of dividends paid on Class D Preferred Stock for any fiscal year may not be less than the rate of dividends paid on Classes A, B or C Common Stock or participation certificates for such year. The rate of dividends on Classes A, B and C Common Stock and participation certificates shall be at the same rate per share.

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

Patronage Distributions

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

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

Transfer

Class D Preferred, Classes A, B and C Common Stocks, and Classes B and C Participation Certificates may be transferred to persons or entities eligible to purchase or hold such equities.

Impairment

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

(a) ***First,*** allocated surplus evidenced by nonqualified written notices of allocation, in its entirety, with application to most recent allocation first and then in reverse order until all such allocated surplus has been exhausted;

(b) ***Second,*** allocated surplus evidenced by qualified written notices of allocation, in its entirety, with application to most recent allocation first and then in reverse order until all such allocated surplus has been exhausted;

(c) ***Third,*** Class A Common Stock, Class B Common Stock, Class C Common Stock and Class C Participation Certificates issued and outstanding, pro rata until such stock is fully impaired; and

(d) ***Fourth,*** Class D Preferred Stock issued and outstanding, if any.

Impairments shall be considered as being applied pro rata to each share and/or unit outstanding in the class.

Liquidation

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

(a) ***First,*** to the holders of Class D Preferred Stock until an amount equal to the aggregate par value of all shares of said stock then issued and outstanding has been distributed to such holders;

(b) ***Second,*** to the holders of Class A Common, Class B Common, Class C Common, Class B Participation Certificates and Class C Participation Certificates, pro rata in proportion to the number of shares or units of each such class of stock or participation certificates then issued and outstanding, until an amount equal to the aggregate par value or face amount of all such shares or units has been distributed to such holders;

(c) ***Third,*** to the holders of allocated surplus evidenced by qualified written notices of allocation, in the order of year of issuance and pro rata by year of issuance, until the total amount of such allocated surplus has been distributed;

(d) ***Fourth,*** to the holders of allocated surplus evidenced by nonqualified written notices of allocation, in the order of year of issuance and pro rata by year of issuance, until the total amount of such allocated surplus has been distributed; and

(e) ***Fifth,*** any remaining assets of the Association after such distributions shall be distributed to past and present Patrons on a patronage basis, to the extent practicable.

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

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

	For the years ended December 31,		
	2016	**2015**	**2014**
Employee Benefit Plans:			
Balance at beginning of period	$ (307)	$ (340)	$ (298)
Other comprehensive income before reclassifications	(8)	17	(57)
Amounts reclassified from AOCI	15	16	15
Net current period OCI	7	33	(42)
Balance at end of period	$ (300)	$ (307)	$ (340)

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

	2016	**2015**	**2014**	**Income Statement Line Item**
Defined Benefit Pension Plans:				
Periodic pension costs	$ (15)	$ (16)	$ (15)	See Note 9.
Amounts reclassified	$ (15)	$ (16)	$ (15)	

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

Note 8 — Fair Value Measurement

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

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

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

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

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

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

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

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

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

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

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

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

For investment securities held to maturity, which consists of RABs, fair value is determined by discounting the expected future cash flows using prevailing rates for similar assets.

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

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

At or for the Year ended December 31, 2016

	Total Carrying Amount	Level 1	Level 2	Level 3	Total Fair Value	Fair Value Effects On Earnings
Recurring Measurements						
Assets:						
Assets held in Trust funds	$ 66	$ 66	$ –	$ –	$ 66	
Recurring Assets	$ 66	$ 66	$ –	$ –	$ 66	
Liabilities:						
Recurring Liabilities	$ –	$ –	$ –	$ –	$	
Nonrecurring Measurements						
Assets:						
Impaired loans	$ 21,595	$ –	$ –	$ 21,595	$ 21,595	$ (179)
Other property owned	1,876	–	–	2,119	2,119	(64)
Nonrecurring Assets	$ 23,471	$ –	$ –	$ 23,714	$ 23,714	$ (243)
Other Financial Instruments						
Assets:						
Cash	$ 3,063	$ 3,063	$ –	$ –	$ 3,063	
Investment securities, held-to-maturity	4,209	–	–	3,961	3,961	
Loans	830,224	–	–	819,458	819,458	
Other Financial Assets	$ 837,496	$ 3,063	$ –	$ 823,419	$ 826,482	
Liabilities:						
Notes payable to AgFirst Farm Credit Bank	$ 683,642	$ –	$ –	$ 674,231	$ 674,231	
Other Financial Liabilities	$ 683,642	$ –	$ –	$ 674,231	$ 674,231	

	At or for the Year ended December 31, 2015					
	Total Carrying Amount	Level 1	Level 2	Level 3	Total Fair Value	Fair Value Effects On Earnings
Recurring Measurements						
Assets:						
Assets held in Trust funds	$ 91	$ 91	$ –	$ –	$ 91	
Recurring Assets	$ 91	$ 91	$ –	$ –	$ 91	
Liabilities:						
Recurring Liabilities	$ –	$ –	$ –	$ –	$ –	
Nonrecurring Measurements						
Assets:						
Impaired loans	$ 22,445	$ –	$ –	$ 22,445	$ 22,445	$ 270
Other property owned	1,356	–	–	1,485	1,485	(1,177)
Nonrecurring Assets	$ 23,801	$ –	$ –	$ 23,930	$ 23,930	$ (907)
Other Financial Instruments						
Assets:						
Cash	$ 3,882	$ 3,882	$ –	$ –	$ 3,882	
Investment securities, held-to-maturity	7,366	–	–	7,087	7,087	
Loans	800,692	–	–	804,157	804,157	
Other Financial Assets	$ 811,940	$ 3,882	$ –	$ 811,244	$ 815,126	
Liabilities:						
Notes payable to AgFirst Farm Credit Bank	$ 667,938	$ –	$ –	$ 667,143	$ 667,143	
Other Financial Liabilities	$ 667,938	$ –	$ –	$ 667,143	$ 667,143	

	At or for the Year ended December 31, 2014					
	Total Carrying Amount	Level 1	Level 2	Level 3	Total Fair Value	Fair Value Effects On Earnings
Recurring Measurements						
Assets:						
Assets held in Trust funds	$ 107	$ 107	$ –	$ –	$ 107	
Recurring Assets	$ 107	$ 107	$ –	$ –	$ 107	
Liabilities:						
Recurring Liabilities	$ –	$ –	$ –	$ –	$ –	
Nonrecurring Measurements						
Assets:						
Impaired loans	$ 11,666	$ –	$ –	$ 11,666	$ 11,666	$ (122)
Other property owned	4,976	–	–	5,319	5,319	(139)
Nonrecurring Assets	$ 16,642	$ –	$ –	$ 16,985	$ 16,985	$ (261)
Other Financial Instruments						
Assets:						
Cash	$ 3,107	$ 3,107	$ –	$ –	$ 3,107	
Investment securities, held-to-maturity	4,647	–	–	4,312	4,312	
Loans	772,649	–	–	766,846	766,846	
Other Financial Assets	$ 780,403	$ 3,107	$ –	$ 771,158	$ 774,265	
Liabilities:						
Notes payable to AgFirst Farm Credit Bank	$ 636,579	$ –	$ –	$ 628,738	$ 628,738	
Other Financial Liabilities	$ 636,579	$ –	$ –	$ 628,738	$ 628,738	

SENSITIVITY TO CHANGES IN SIGNIFICANT UNOBSERVABLE INPUTS

Discounted cash flow or similar modeling techniques are generally used to determine the recurring fair value measurements for Level 3 assets and liabilities. Use of these techniques requires determination of relevant inputs and assumptions, some of which represent significant unobservable inputs as indicated in the tables that follow. Accordingly, changes in these unobservable inputs may have a significant impact on fair value.

Certain of these unobservable inputs will (in isolation) have a directionally consistent impact on the fair value of the instrument for a given change in that input. Alternatively, the fair value of the instrument may move in an opposite direction for a given change in another input. Where multiple inputs are used within the valuation technique of an asset or liability, a change in one input in a certain direction may be offset by an opposite change in another input having a potentially muted impact to the overall fair value of that particular instrument. Additionally, a change in one unobservable input may result in a change to another unobservable input (that is, changes in certain inputs are interrelated with one another), which may counteract or magnify the fair value impact.

Investment Securities
The fair values of predominantly all Level 3 investment securities have consistent inputs, valuation techniques and correlation to changes in underlying inputs. The models used to determine fair value for these instruments use certain significant unobservable inputs within a discounted cash flow or market comparable pricing valuation technique. Such inputs generally include discount rate components including risk premiums, prepayment estimates, default estimates and loss severities.

These Level 3 assets would decrease (increase) in value based upon an increase (decrease) in discount rates, defaults, or loss severities. Conversely, the fair value of these assets would generally increase (decrease) in value if the repayment input were to increase (decrease).

Generally, a change in the assumption used for defaults is accompanied by a directionally similar change in the risk premium component of the discount rate (specifically, the portion related to credit risk) and a directionally opposite change in the assumption used for prepayments. Unobservable inputs for loss severities do not normally increase or decrease based on movements in the other significant unobservable inputs for these Level 3 assets.

Inputs to Valuation Techniques

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

Quoted market prices are generally not available for the instruments presented below. Accordingly fair values are based on judgments regarding anticipated cash flows, future expected loss experience, current economic conditions, risk characteristics of various financial instruments, and other factors. These estimates involve uncertainties and matters of judgment, and therefore cannot be determined with precision. Changes in assumptions could significantly affect the estimates.

Quantitative Information about Recurring and Nonrecurring Level 3 Fair Value Measurements

	Fair Value	Valuation Technique(s)	Unobservable Input	Range
Impaired loans and other property owned	$ 23,714	Appraisal	Income and expense	*
			Comparable sales	*
			Replacement costs	*
			Comparability adjustments	*

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

Information about Other Financial Instrument Fair Value Measurements

	Valuation Technique(s)	Input
Cash	Carrying Value	Par/Principal and appropriate interest yield
Loans	Discounted cash flow	Prepayment forecasts
		Probability of default
		Loss severity
Investment securities, held-to-maturity	Discounted cash flow	Prepayment rates
		Risk adjusted discount rate
Notes payable to AgFirst Farm Credit Bank	Discounted cash flow	Prepayment forecasts
		Probability of default
		Loss severity

Note 9 — Employee Benefit Plans

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

1. Assets contributed to multiemployer plans by one employer may be used to provide benefits to employees of other participating employers.

2. If a participating employer stops contributing to the plan, the unfunded obligations of the plan may be borne by the remaining participating employers.

3. If the Association chooses to stop participating in some of its multiemployer plans, the Association may be required to contribute to eliminate the underfunded status of the plan.

In November 2014, the AgFirst Plan Sponsor Committee approved and executed amendments to the CB Plan that included the following changes:

1. The CB Plan was closed to new participants effective as of December 31, 2014. Based on the plan's eligibility provisions, this change affected employees hired on or after November 4, 2014.

2. Employer contributions were discontinued effective as of January 1, 2015.

3. All participants who were not already fully vested in the CB Plan became fully vested as of December 31, 2014.

4. The CB Plan was terminated effective as of December 31, 2015.

A favorable determination letter was received from the Internal Revenue Service, and as a result of the termination of the CB Plan, vested benefits will be distributed to participants in 2017. Participants will continue to receive interest credits to their hypothetical cash balance accounts following the termination of the plan through the month immediately preceding the

month in which the vested benefits are distributed from the plan.

Curtailment accounting, as prescribed in ASC 715 "Compensation – Retirement Benefits", was initiated upon execution of the plan amendments and did not have a material impact on the Association's financial condition or results of operations.

Beginning on January 1, 2015, for participants in the CB Plan and eligible employees hired on or after November 4, 2014, additional employer contributions are made to the 401(k) Plan equal to 3.00 percent of the participants' eligible compensation.

The Association's participation in the multiemployer defined benefit plans for the annual periods ended December 31, is outlined in the table below. The "Percentage Funded to Projected Benefit Obligation" or "Percentage Funded to Accumulated Postretirement Benefit Obligation" represents the funded amount for the entire plan and the "Contributions" and "Percentage of Total Contributions" columns represent the Association's respective amounts.

Pension Plan	Percentage Funded to Projected Benefit Obligation			Contributions			Percentage of Total Contributions		
	2016	2015	2014	2016	2015	2014	2016	2015	2014
AgFirst Farm Credit Retirement Plan	86.96%	85.73%	84.56%	$1,204	$2,346	$1,588	4.22%	4.06%	4.18%
AgFirst Farm Credit Cash Balance Retirement Plan	100.21%	102.72%	100.07%	$–	$–	$138	0.00%	0.00%	2.77%

Other Postretirement Benefit Plan	Percentage Funded to Accumulated Postretirement Benefit Obligation			Contributions			Percentage of Total Contribution		
	2016	2015	2014	2016	2015	2014	2016	2015	2014
Farm Credit Benefits Alliance Retiree and Disabled Medical and Dental Plans	0.00%	0.00%	0.00%	$256	$235	$247	3.56%	3.46%	3.19%

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

1. The Employee Identification Number (EIN) and three-digit Pension Plan Number

2. The most recent Pension Protection Act (PPA) zone status. Among other factors, plans in the red zone are generally less than 65 percent funded, plans in the yellow zone are less than 80 percent funded, and plans in the green zone are at least 80 percent funded.

3. The "FIP/RP Status" indicating whether a financial improvement plan (FIP) or a rehabilitation plan (RP) is either pending or has been implemented.

4. The expiration date(s) of collective-bargaining agreement(s).

Substantially all employees of the Association hired before November 4, 2014 are eligible to participate in either the FAP Plan or the CB Plan. These two plans are noncontributory and include eligible Association and other District employees. For participants hired prior to January 1, 2003, benefits are provided under the FAP Plan and are based on eligible compensation and years of service. For participants hired on or after January 1, 2003 through November 3, 2014, benefits are provided under the CB Plan and are determined using a percent of eligible compensation formula. Prior to January 1, 2015, when employer contributions were discontinued as discussed above, the employer contribution into the CB Plan was based on a formula of 3.00-5.00 percent of eligible compensation (depending on years of service) and interest credits as allocated to an employee's theoretical account balance. The actuarially-determined costs of these plans are allocated to each participating entity, including the Association, by multiplying the plans' net pension expense by each institution's eligible service cost and accumulated benefit obligation as a percentage of the total eligible service cost and total accumulated benefit obligation for all plan participants. Plan expenses included in employee benefit costs were $2,207 for 2016, $2,159 for 2015, and $2,318 for 2014. The cumulative excess of amounts funded by the Association over the cost allocated to the Association is reflected as prepaid retirement expense, a component of Other Assets in the Consolidated Balance Sheets.

In addition to providing pension benefits, the Association provides certain medical and dental benefits for eligible retired employees through the OPEB Plan. Substantially all of the Association employees may become eligible for the benefits if they reach early retirement age while working for the Association. Early retirement age is defined as a minimum of age 55 and 10 years of service. Employees hired after December 31, 2002, and employees who separate from service between age 50 and age 55, are required to pay the full cost of their retiree health insurance coverage. Employees who retire subsequent to December 1, 2007 are no longer provided retiree life insurance benefits. Certain Association charges related to this plan are an allocation of District charges based on the Association's proportional share of the plan liability. This plan is unfunded with expenses paid as incurred. Postretirement benefits other than pensions included in employee benefit costs were $473 for 2016, $625 for 2015, and $355 for 2014. The cumulative excess of cost allocated to the Association over the amounts funded by the Association is reflected as postretirement benefits other than pensions, a component of Other Liabilities in the Association's Consolidated Balance Sheets.

The Association also participates in a defined contribution Farm Credit Benefits Alliance (FCBA) 401(k) Plan (401(k) Plan), which qualifies as a 401(k) plan as defined by the Internal Revenue Code. For employees hired on or prior to December 31, 2002, the Association contributes $0.50 for each $1.00 of the employee's first 6.00 percent of contribution (based on total

compensation) up to the maximum employer contribution of 3.00 percent of total compensation. For employees hired on or after January 1, 2003, the Association contributes $1.00 for each $1.00 of the employee's first 6.00 percent of contribution up to the maximum employer contribution of 6.00 percent of total compensation. Employee deferrals are not to exceed the maximum deferral as determined and adjusted by the Internal Revenue Service. The 401(k) Plan costs are expensed as funded. Employer contributions to this plan included in salaries and employee benefit costs were $333, $298, and $205 for the years ended December 31, 2016, 2015, and 2014, respectively. Beginning in 2015, contributions include additional amounts related to the discontinuation of the CB Plan as discussed above.

FASB guidance further requires the determination of the fair value of plan assets and recognition of actuarial gains and losses, prior service costs or credits, and transition assets or obligations as a component of AOCI. Under the guidance, these amounts are subsequently recognized as components of net periodic benefit costs over time. For 2016, 2015, and 2014, $7, $33 and $(42), respectively, has been recognized as net credits, and a net debit to AOCI to reflect these elements.

The supplemental retirement plan is unfunded and had a projected benefit obligation of $397 and a net under-funded status of $397 at December 31, 2016. Net periodic pension cost was $33, $34, and $33 for 2016, 2015, and 2014, respectively. Assumptions used to determine the projected benefit obligation as of December 31, 2016 included a discount rate of 4.35 percent.

Additional information can be found in Note 9 of the Notes to the Combined Financial Statements of AgFirst Farm Credit Bank and District Associations' Annual Report.

Note 10 — Related Party Transactions

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

Total loans to such persons at December 31, 2016 amounted to $11,213. During 2016, $6,477 of new loans were made and repayments totaled $3,022. In the opinion of management, none of these loans outstanding at December 31, 2016 involved more than a normal risk of collectability.

Note 11 — Commitments and Contingencies

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

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

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

Since many of these commitments are expected to expire without being drawn upon, the total commitments do not necessarily represent future cash requirements. However, these credit-related financial instruments have off-balance-sheet credit risk because their amounts are not reflected on the Consolidated Balance Sheets until funded or drawn upon. The credit risk associated with issuing commitments and letters of credit is substantially the same as that involved in extending loans to borrowers and management applies the same credit policies to these commitments. Upon fully funding a commitment, the credit risk amounts are equal to the contract amounts, assuming that borrowers fail completely to meet their obligations and the collateral or other security is of no value. The amount of collateral obtained, if deemed necessary upon extension of credit, is based on management's credit evaluation of the borrower. At December 31, 2016, $155,859 of commitments to extend credit and no commercial letters of credit were outstanding. There was no reserve for unfunded commitments included in Other Liabilities in the Consolidated Balance Sheets at December 31, 2016.

The Association also participates in standby letters of credit to satisfy the financing needs of its borrowers. These letters of credit are irrevocable agreements to guarantee payments of specified financial obligations. At December 31, 2016, standby letters of credit outstanding totaled $335 with expiration dates ranging from January 1, 2017 to January 14, 2019. The maximum potential amount of future payments that may be required under these guarantees was $335.

Note 12 — Income Taxes

The provision (benefit) for income taxes follows:

	Year Ended December 31,		
	2016	2015	2014
Current:			
Federal	$ 143	$ 150	$ 198
State	–	–	(48)
Total provision (benefit) for income taxes	$ 143	$ 150	$ 150

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

	December 31,		
	2016	2015	2014
Federal tax at statutory rate	$ 7,119	$ 6,913	$ 8,483
State tax, net	–	–	(31)
Patronage distributions	(3,500)	(4,200)	(4,900)
Tax-exempt FLCA earnings	(3,810)	(3,440)	(3,583)
Change in valuation allowance	259	1,082	(169)
Adjustment to deferred-prior period	–	(62)	96
Other	75	(143)	254
Provision (benefit) for income taxes	$ 143	$ 150	$ 150

Deferred tax assets and liabilities are comprised of the following at:

	December 31,		
	2016	2015	2014
Deferred income tax assets:			
Allowance for loan losses	$ 1,987	$ 1,608	$ 1,353
Net operating loss – carryforward	1,996	2,140	1,396
Nonaccrual loan interest	670	646	563
Gross deferred tax assets	4,653	4,394	3,312
Less: valuation allowance	(4,653)	(4,394)	(3,312)
Gross deferred tax assets, net of valuation allowance	–	–	–
Deferred income tax liabilities:			
Future Bank equity redemption	–	–	–
Loan fees	–	–	–
Gross deferred tax liability	–	–	–
Net deferred tax asset (liability)	$ –	$ –	$ –

At December 31, 2016, deferred income taxes have not been provided by the Association on approximately $3.6 million of patronage refunds received from the Bank prior to January 1, 1993. Such refunds, distributed in the form of stock, are subject to tax only upon conversion to cash. The tax liability related to future conversions is not expected to be material.

The Association recorded a valuation allowance of $4,653, $4,394, and $3,312 as of December 31, 2016, 2015 and 2014, respectively. The Association will continue to evaluate the realizability of these deferred tax assets and adjust the valuation allowance accordingly.

There were no uncertain tax positions identified related to the current year and the Association has no unrecognized tax benefits at December 31, 2016 for which liabilities have been established. The Association recognizes interest and penalties, if any, related to unrecognized tax benefits as a component of income tax expense.

The tax years that remain open for federal and major state income tax jurisdictions are 2013 and forward.

Note 13 — Additional Financial Information

Quarterly Financial Information (Unaudited)

	2016				
	First	Second	Third	Fourth	Total
Net interest income	$ 6,135	$ 6,176	$ 6,136	$ 6,157	$ 24,604
Provision for (reversal of allowance for) loan losses	225	702	242	(277)	892
Noninterest income (expense), net	(1,559)	(1,895)	(2,140)	2,078	(3,516)
Net income	$ 4,351	$ 3,579	$ 3,754	$ 8,512	$ 20,196

	2015				
	First	Second	Third	Fourth	Total
Net interest income	$ 6,077	$ 6,234	$ 6,265	$ 6,117	$ 24,693
Provision for (reversal of allowance for) loan losses	278	299	95	(50)	622
Noninterest income (expense), net	(1,822)	(2,100)	(1,951)	1,404	(4,469)
Net income	$ 3,977	$ 3,835	$ 4,219	$ 7,571	$ 19,602

	2014				
	First	Second	Third	Fourth	Total
Net interest income	$ 6,008	$ 6,112	$ 6,203	$ 6,013	$ 24,336
Provision for (reversal of allowance for) loan losses	110	241	(57)	(120)	174
Noninterest income (expense), net	(1,477)	(1,528)	(2,031)	4,961	(75)
Net income	$ 4,421	$ 4,343	$ 4,229	$ 11,094	$ 24,087

Note 14 — Subsequent Events

The Association evaluated subsequent events and determined that there were none requiring disclosure through March 13, 2017, which was the date the financial statements were issued.

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