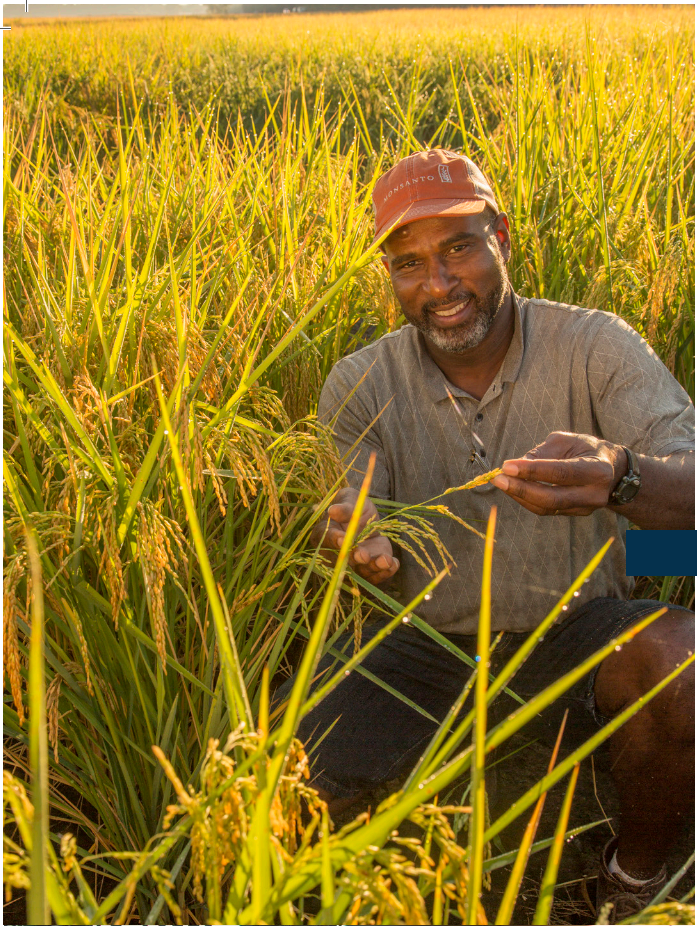
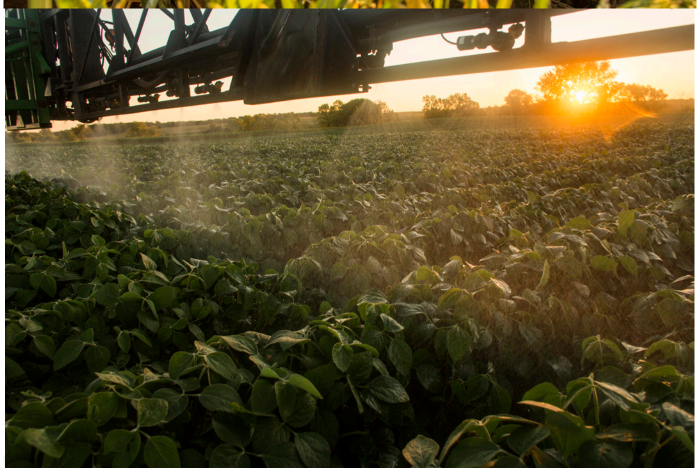

AgHeritage®
Farm Credit Services
2016 ANNUAL REPORT





Over a CENTURY of Support

In 2016, Farm Credit celebrated 100 years of supporting rural communities and agriculture with reliable, consistent credit and financial services. We've been fulfilling our mission of helping these areas grow and thrive by providing farmers with the capital they need to make their businesses successful and by financing vital infrastructure and communication services. Because a steady flow of capital means more jobs and economic growth, Farm Credit is able to invest in the vibrancy of communities throughout rural America.

Farm Credit is the premier funding source for farmers and ranchers throughout the country, because you — our members and owners — dared to plant seeds for the future. Year after year, our national network of borrower-owned lending institutions ensures that customers always stand front and center.

We've seen rural America through good times and tough challenges. Building on our century of experience, we're committed to helping you grow, today and tomorrow. Celebrating our past, preparing for the future.

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AgHeritage Farm Credit Services, ACA

MESSAGE FROM THE CHAIRPERSON OF THE BOARD AND CHIEF EXECUTIVE OFFICER

Dear AgHeritage Farm Credit Services Customer-Owners,

We are pleased to report that AgHeritage Farm Credit Services, ACA has generated some of the top financial ratios in the Farm Credit System in terms of capital, efficiency ratio, credit quality and earnings. Your cooperative has grown to exceed $1 billion in assets and enjoys a strong market share position, which confirms that we are achieving our vision of being the lender of choice in our local marketplace.

AgHeritage FCS is proud to be your lending cooperative providing both customer and stockholder value to our members. AgHeritage FCS supports our rural communities and agriculture with reliable, consistent credit and financial services, today and tomorrow.

We are pleased to announce that we have continued the patronage program with $3.6 million of 2016 earnings paid to eligible customer-owners in February 2017. This is part of the Board's commitment to our customer-owners in sharing the success of your cooperative. The $3.6 million patronage program represents approximately 16.9 percent of net earnings. This payout allows retention of a portion of earnings to provide for future growth and capital stability. This patronage distribution represents the eleventh consecutive year your cooperative has distributed a portion of its annual earnings to its customer-owners. To date, AgHeritage has distributed $32.4 million to customer-owners like you and plans to continue patronage distributions well into the future.

The Annual Report provides detailed documentation supporting the financial results of the Association. We encourage you to review it carefully, and if you have any questions, contact our corporate office or any branch location.

While the U.S. economy continues along its slow and delicate recovery, the crop sector enters its fourth year of a down cycle. This cycle is characterized by a dramatic decline in crop prices, with inputs decreasing at a much slower rate. This disparity is magnified by relatively flat demand, a strong dollar and large carryover stocks in need of supply adjustments. Short of a significant event in the marketplace, this cycle could last for an extended period of time. Though the crop sector is stressed, the protein sector continues to experience modest profitability with lower feed costs offsetting declining meat prices. Despite the situation, your Association remains a financially strong organization. AgHeritage FCS and the Farm Credit System are well capitalized and are in a strong financial position to meet the needs of our customer-owners during these turbulent times.

We recognize that our success is a result of the hard work and dedication of our staff. We want to thank our staff for their dedication and hard work. We want to also thank you, our customer-owners, for your loyalty and for allowing us to serve your credit and financial service needs.

Sincerely,

Michael D. Taylor
Chairperson of the Board
AgHeritage Farm Credit Services, ACA

Gregory W. Cole
President and Chief Executive Officer
AgHeritage Farm Credit Services, ACA

March 14, 2017

CONSOLIDATED FIVE-YEAR SUMMARY OF SELECTED FINANCIAL DATA

AgHeritage Farm Credit Services, ACA

(dollars in thousands)

	2016	2015	2014	2013	2012
Statement of Condition Data					
Loans	**$ 1,073,202**	$ 977,289	$ 965,083	$ 892,163	$ 820,028
Allowance for loan losses	**5,307**	1,520	981	1,002	1,033
Net loans	**1,067,895**	975,769	964,102	891,161	818,995
Investment in AgriBank, FCB	**22,219**	21,439	21,493	22,738	21,871
Investment securities	**6,004**	8,610	11,663	14,806	19,057
Other property owned	**--**	--	--	--	142
Other assets	**26,510**	23,474	21,699	19,833	20,070
Total assets	**$ 1,122,628**	$ 1,029,292	$ 1,018,957	$ 948,538	$ 880,135
Obligations with maturities of one year or less	**$ 866,727**	$ 791,141	$ 799,399	$ 748,574	$ 698,887
Total liabilities	**866,727**	791,141	799,399	748,574	698,887
Protected members' equity	**1**	1	1	4	4
Capital stock and participation certificates	**2,875**	2,877	2,909	2,896	2,791
Unallocated surplus	**253,025**	235,273	216,648	197,064	178,453
Total members' equity	**255,901**	238,151	219,558	199,964	181,248
Total liabilities and members' equity	**$ 1,122,628**	$ 1,029,292	$ 1,018,957	$ 948,538	$ 880,135
Statement of Income Data					
Net interest income	**$ 32,259**	$ 31,965	$ 30,033	$ 28,268	$ 26,838
Provision for loan losses	**3,764**	1,360	--	--	325
Other expenses, net	**7,188**	8,504	7,060	6,374	4,837
Net income	**$ 21,307**	$ 22,101	$ 22,973	$ 21,894	$ 21,676
Key Financial Ratios					
Return on average assets	**1.9%**	2.1%	2.3%	2.4%	2.6%
Return on average members' equity	**8.6%**	9.7%	11.0%	11.5%	12.6%
Net interest income as a percentage of average earning assets	**3.0%**	3.2%	3.2%	3.3%	3.3%
Members' equity as a percentage of total assets	**22.8%**	23.1%	21.6%	21.1%	20.6%
Net (recoveries) charge-offs as a percentage of average loans	**(0.0%)**	0.1%	0.0%	0.0%	0.0%
Allowance for loan losses as a percentage of loans	**0.5%**	0.2%	0.1%	0.1%	0.1%
Permanent capital ratio	**20.0%**	19.9%	18.9%	18.1%	17.9%
Total surplus ratio	**19.8%**	19.6%	18.6%	17.8%	17.5%
Core surplus ratio	**19.8%**	19.6%	18.6%	17.8%	17.5%
Net Income Distributed					
Patronage distributions:					
Cash	**$ 3,455**	$ 3,376	$ 3,289	$ 3,183	$ 3,076

MANAGEMENT'S DISCUSSION AND ANALYSIS

AgHeritage Farm Credit Services, ACA

The following commentary reviews the consolidated financial condition and consolidated results of operations of AgHeritage Farm Credit Services, ACA (the Association) and its subsidiaries, AgHeritage Farm Credit Services, FLCA and AgHeritage Farm Credit Services, PCA (subsidiaries) and provides additional specific information. The accompanying Consolidated Financial Statements and Notes to the Consolidated Financial Statements also contain important information about our financial condition and results of operations.

The Farm Credit System (System) is a nationwide system of cooperatively owned banks and associations established by Congress to meet the credit needs of American agriculture. As of January 1, 2017, the System consisted of three Farm Credit Banks, one Agricultural Credit Bank and 73 customer-owned cooperative lending institutions (associations). The System serves all 50 states, Washington D.C. and Puerto Rico. This network of financial cooperatives is owned and governed by the rural customers the System serves.

AgriBank, FCB (AgriBank), a System bank and its affiliated Associations are collectively referred to as the AgriBank Farm Credit District (AgriBank District or the District). We are an affiliated Association in the District.

The Farm Credit Administration (FCA) is authorized by Congress to regulate the System. The Farm Credit System Insurance Corporation (FCSIC) ensures the timely payment of principal and interest on Systemwide debt obligations and the retirement of protected borrower capital at par or stated value.

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

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St. Paul, MN 55101
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www.agribank.com
financialreporting@agribank.com

Our Annual Report is available on our website no later than 75 days after the end of the calendar year and members are provided a copy of such report no later than 90 days after the end of the calendar year. The Quarterly Reports are available on our website no later than 40 days after the end of each calendar quarter. To request free copies of our Annual or Quarterly Reports, contact us as stated above.

FORWARD-LOOKING INFORMATION

This Annual Report includes 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 "anticipate", "believe", "estimate", "may", "expect", "intend", "outlook" and similar expressions are used to identify such forward-looking statements. These statements reflect our current views with respect to future events. However, actual results may differ materially from our expectations due to a number of risks and uncertainties which may be beyond our control. These risks and uncertainties include, but are not limited to:

- Political, legal, regulatory, financial markets, international and economic conditions and developments in the United States (U.S.) and abroad
- Economic fluctuations in the agricultural and farm-related business sectors
- Unfavorable weather, disease and other adverse climatic or biological conditions that periodically occur and impact agricultural productivity and income
- Changes in U.S. government support of the agricultural industry and the System as a government-sponsored enterprise, as well as investor and rating agency actions relating to events involving the U.S. government, other government-sponsored enterprises and other financial institutions
- Actions taken by the Federal Reserve System in implementing monetary policy
- Credit, interest rate and liquidity risks inherent in our lending activities
- Changes in our assumptions for determining the allowance for loan losses, other-than-temporary impairment and fair value measurements

AGRICULTURAL AND ECONOMIC CONDITIONS

For the 2016 crop, average yields were generally somewhat lower than the prior year due to unfavorable weather conditions late in the growing season. Commodity prices have been falling due to large supplies and weakness in export markets. We expect that many of our crop borrowers experienced negative cash flow margins for the 2016 crop; however, negative margins were reduced due to farm program payments received, particularly for rice producers. Due to customers' strong profitability in recent years and generally strong balance sheets, we do not expect significant changes in credit quality in the short term. We could see a more material decline in credit quality if lower commodity prices remain in place. Our poultry portfolio is performing well. Land values in our portfolio are stable to slightly increasing.

LOAN PORTFOLIO

Loan Portfolio

Total loans were $1.1 billion at December 31, 2016, an increase of $95.9 million from December 31, 2015.

Components of Loans

(in thousands) As of December 31	2016	2015	2014
Accrual loans:			
Real estate mortgage	**$ 550,293**	$ 514,074	$ 504,303
Production and intermediate term	**368,519**	364,171	366,457
Agribusiness	**98,428**	59,994	52,677
Other	**45,179**	36,596	37,070
Nonaccrual loans	**10,783**	2,454	4,576
Total loans	**$ 1,073,202**	$ 977,289	$ 965,083

The other category is primarily comprised of rural residential real estate loans and certain assets originated under the Mission Related Investment authority.

The increase in total loans from December 31, 2015, was primarily due to loan participations purchased during the year as well as retail mortgage growth at year end.

We offer variable, fixed, capped, indexed and adjustable interest rate loan and lease programs to our borrowers. We also partner with Farm Credit Leasing to offer fixed rate lease programs to our borrowers. We determine interest margins charged on each lending program based on cost of funds, credit risk, market conditions and the need to generate sufficient earnings.

As part of the AgriBank Asset Pool program, we have sold participation interests in real estate loans to AgriBank. The total participation interests in this program were $31.1 million, $36.7 million and $41.4 million at December 31, 2016, 2015 and 2014, respectively.

Portfolio Distribution

We are chartered to serve certain counties in Arkansas. Approximately 54.6% of our total loan portfolio was in Lawrence, Lonoke, Monroe, Arkansas, Randolph and Jackson counties at December 31, 2016.

Agricultural Concentrations

As of December 31	2016	2015	2014
Rice	**42.1%**	44.6%	41.7%
Other livestock	**11.1%**	10.7%	10.8%
Soybeans	**7.7%**	8.2%	8.3%
Processing and marketing	**9.0%**	8.3%	7.9%
Corn	**4.3%**	4.8%	4.8%
Timber	**3.4%**	4.4%	5.0%
Poultry and eggs	**3.7%**	4.6%	4.5%
Cotton	**2.1%**	2.5%	3.9%
Other row crops	**3.7%**	2.9%	3.1%
Other	**12.9%**	9.0%	10.0%
Total	**100.0%**	100.0%	100.0%

Commodities are based on the borrower’s primary intended commodity at the time of loan origination and may change due to borrower business decisions as a result of changes in weather, prices, input costs and other circumstances.

Our production and intermediate term loan portfolio shows some seasonality. Borrowings increase throughout the planting and growing seasons to meet farmers’ operating and capital needs. These loans are normally at their lowest levels following the harvest and then increase in the spring and throughout the rest of the year as borrowers fund operating needs. In addition, the loan portfolio increased temporarily in December, followed by significant repayments in January, as borrowers increased their operating lines to purchase 2017 production inputs, primarily as part of tax-planning strategies.

Portfolio Credit Quality

The credit quality of our portfolio declined from December 31, 2015. Adversely classified loans increased to 2.4% of the portfolio at December 31, 2016, from 0.7% of the portfolio at December 31, 2015. Adversely classified loans are loans we have identified as showing some credit weakness outside our credit standards. We have considered portfolio credit quality in assessing the reasonableness of our allowance for loan losses.

In certain circumstances, government guarantee programs are used to reduce the risk of loss. At December 31, 2016, $25.9 million of our loans were, to some level, guaranteed under these government programs.

Risk Assets

Components of Risk Assets

(dollars in thousands)

As of December 31	**2016**	2015	2014
Loans:			
Nonaccrual	**$ 10,783**	$ 2,454	$ 4,576
Accruing restructured	**--**	--	--
Accruing loans 90 days or more past due	**--**	130	645
Total risk loans	**10,783**	2,584	5,221
Other property owned	**--**	--	--
Total risk assets	**$ 10,783**	$ 2,584	$ 5,221
Total risk loans as a percentage of total loans	**1.0%**	0.3%	0.5%
Nonaccrual loans as a percentage of total loans	**1.0%**	0.2%	0.5%
Current nonaccrual loans as a percentage of total nonaccrual loans	**61.6%**	45.7%	24.3%
Total delinquencies as a percentage of total loans	**0.6%**	0.9%	0.9%

Note: Accruing loans include accrued interest receivable.

Our risk assets have increased from December 31, 2015, but remained at acceptable levels. Despite the increase in risk assets, total risk loans as a percentage of total loans were well within our established risk management guidelines.

The increase in nonaccrual loans was primarily due to several real estate mortgage and production and intermediate term loans transferred to nonaccrual status during the year ended December 31, 2016. Nonaccrual loans remained at an acceptable level at December 31, 2016, 2015 and 2014.

Allowance for Loan Losses

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

Allowance Coverage Ratios

As of December 31	**2016**	2015	2014
Allowance as a percentage of:			
Loans	**0.5%**	0.2%	0.1%
Nonaccrual loans	**49.2%**	61.9%	21.4%
Total risk loans	**49.2%**	58.8%	18.8%
Net (recoveries) charge-offs as a percentage of average loans	**(0.0%)**	0.1%	0.0%
Adverse assets to risk funds	**10.8%**	3.0%	8.9%

In our opinion, the allowance for loan losses was reasonable in relation to the risk in our loan portfolio at December 31, 2016.

Additional loan information is included in Notes 3, 10, 11 and 12 to the accompanying Consolidated Financial Statements.

INVESTMENT SECURITIES

In addition to loans, we held investment securities which totaled $6.0 million, $8.6 million and $11.7 million at December 31, 2016, 2015 and 2014, respectively. Our investment securities consisted of our share of securities made up of loans guaranteed by the Small Business Administration.

The investment portfolio is evaluated for other-than-temporary impairment. To date, we have not recognized any impairment on our investment portfolio.

Additional investment securities information is included in Note 5 to the accompanying Consolidated Financial Statements.

RESULTS OF OPERATIONS

Profitability Information

(dollars in thousands) For the year ended December 31	2016	2015	2014
Net income	**$ 21,307**	$ 22,101	$ 22,973
Return on average assets	**1.9%**	2.1%	2.3%
Return on average members' equity	**8.6%**	9.7%	11.0%

Changes in the chart above relate directly to:

- Changes in income discussed below
- Changes in assets discussed in the Loan Portfolio and Investment Securities sections
- Changes in capital discussed in the Capital Adequacy section

Changes in Significant Components of Net Income

	For the year ended December 31			Increase (decrease) in net income	
(in thousands)	2016	2015	2014	2016 vs 2015	2015 vs 2014
Net interest income	**$ 32,259**	$ 31,965	$ 30,033	**$ 294**	$ 1,932
Provision for loan losses	**3,764**	1,360	--	**(2,404)**	(1,360)
Patronage income	**3,900**	3,205	3,900	**695**	(695)
Other income, net	**2,751**	2,091	2,334	**660**	(243)
Operating expenses	**13,621**	12,953	11,821	**(668)**	(1,132)
Provision for income taxes	**218**	847	1,473	**629**	626
Net income	**$ 21,307**	$ 22,101	$ 22,973	**$ (794)**	$ (872)

Net Interest Income

Changes in Net Interest Income

(in thousands) For the year ended December 31	2016 vs 2015	2015 vs 2014
Changes in volume	**$ 1,611**	$ 2,161
Changes in interest rates	**(1,119)**	(654)
Changes in nonaccrual income and other	**(198)**	425
Net change	**$ 294**	$ 1,932

Net interest income included income on nonaccrual loans that totaled $379 thousand, $577 thousand and $152 thousand in 2016, 2015 and 2014, respectively. Nonaccrual income is recognized when received in cash, collection of the recorded investment is fully expected and prior charge-offs have been recovered.

Net interest margin (net interest income as a percentage of average earning assets) was 3.0%, 3.2% and 3.2% in 2016, 2015 and 2014, respectively. We expect margins to further compress in the future if interest rates continue to rise and competition increases.

Provision for Loan Losses

The fluctuation in the provision for loan losses was related to our estimate of losses in our portfolio for the applicable years. Additional discussion is included in Note 3 to the accompanying Consolidated Financial Statements.

Patronage Income

We received patronage income based on the average balance of our note payable to AgriBank. The patronage rates were 25.6 basis points, 26.0 basis points and 33.5 basis points in 2016, 2015 and 2014, respectively. We recorded patronage income of $2.2 million, $2.1 million and $2.6 million in 2016, 2015 and 2014, respectively.

Since 2008, we have participated in the AgriBank Asset Pool program in which we sell participation interests in certain real estate loans to AgriBank. As part of this program, we received patronage income in an amount that approximated the net earnings of the loans. Net earnings represents the net interest income associated with these loans adjusted for certain fees and costs specific to the related loans as well as adjustments deemed appropriate by AgriBank related to the credit performance of the loans, as applicable. In addition, we received patronage income in an amount that approximated the wholesale patronage had we retained the volume. We recorded asset pool patronage income of $877 thousand, $1.0 million and $1.3 million in 2016, 2015 and 2014, respectively.

We also received patronage related to an increase in the wholesale spread on our note payable.

Patronage and equalization distributions for the programs discussed above are declared solely at the discretion of AgriBank's Board of Directors.

Operating Expenses

Components of Operating Expenses

(dollars in thousands) For the year ended December 31	2016	2015	2014
Salaries and employee benefits	**$ 7,978**	$ 8,186	$ 7,358
Purchased and vendor services	**1,336**	1,114	1,067
Communications	**270**	201	213
Occupancy and equipment	**690**	716	665
Advertising and promotion	**380**	366	402
Examination	**355**	282	283
Farm Credit System insurance	**1,467**	1,078	920
Other	**1,145**	1,010	913
Total operating expenses	**$ 13,621**	$ 12,953	$ 11,821
Operating rate	**1.3%**	1.3%	1.3%

Salaries and employee benefits expense decreased primarily due to a reduction in incentive awards and pension expense. We expect pension expense to decrease in 2017 primarily driven by a plan amendment during 2016 and increased return on assets as a result of increased funding, partially offset by decreases in discount rate and expected return on plan assets assumptions.

We have been notified by our regulator, the FCA, that our examination fees are expected to increase in 2017.

FCSIC insurance expense increased in 2016 primarily due to an increase in the premium rate charged by FCSIC on accrual loans from 13 basis points in 2015 to 16 basis points for the first half and 18 basis points for the second half of 2016. The FCSIC has announced premiums will decrease to 15 basis points for 2017. The FCSIC Board meets periodically throughout the year to review premium rates and has the ability to change these rates at any time.

Provision for Income Taxes

The variance in provision for income taxes was related to our estimate of taxes based on taxable income. Patronage distributions to members reduced our tax liability in 2016, 2015 and 2014. Additional discussion is included in Note 8 to the accompanying Consolidated Financial Statements.

FUNDING AND LIQUIDITY

We borrow from AgriBank, under a note payable, in the form of a line of credit, as described in Note 6 to the accompanying Consolidated Financial Statements. This line of credit is our primary source of liquidity and is used to fund operations and meet current obligations. At December 31, 2016, we had $240.5 million available under our line of credit. We generally apply excess cash to this line of credit.

Note Payable Information

(dollars in thousands) For the year ended December 31	2016	2015	2014
Average balance	**$ 845,554**	$ 816,666	$ 769,244
Average interest rate	**1.9%**	1.6%	1.6%

The repricing attributes of our line of credit generally correspond to the repricing attributes of our loan portfolio which significantly reduces our market interest rate risk. Due to the cooperative structure of the Farm Credit System and as we are a stockholder of AgriBank, we expect this borrowing relationship to continue into the foreseeable future. Our other source of lendable funds is from unallocated surplus.

CAPITAL ADEQUACY

Total members' equity increased $17.8 million from December 31, 2015, primarily due to net income for the year partially offset by patronage distribution accruals**.**

Members' Equity Position Information

(dollars in thousands) As of December 31	2016	2015	2014	Regulatory Minimums
Members' equity	**$ 255,901**	$ 238,151	$ 219,558	
Surplus as a percentage of members' equity	**98.9%**	98.8%	98.7%	
Permanent capital ratio	**20.0%**	19.9%	18.9%	7.0%
Total surplus ratio	**19.8%**	19.6%	18.6%	7.0%
Core surplus ratio	**19.8%**	19.6%	18.6%	3.5%

Our capital plan is designed to maintain an adequate amount of surplus and allowance for loan losses which represents our reserve for adversity prior to impairment of stock. We manage our capital to allow us to meet member needs and protect member interests, both now and in the future.

Additional discussion of these regulatory ratios, along with discussion of new regulations and capital requirements which became effective January 1, 2017, are included in the Regulatory Matters section and in Note 7 to the accompanying Consolidated Financial Statements.

In addition to these regulatory requirements, we establish an optimum total capital target range. This target allows us to maintain a capital base adequate for future growth and investment in new products and services. The target is subject to revision as circumstances change. As of December 31, 2016, our optimum total capital target range was 14% to 20% as defined in our 2017 capital plan. We anticipate that we will exceed all regulatory requirements, including the capital conservation buffer. Further, we expect we will be within our targeted range for capital adequacy measures.

The changes in our capital ratios reflect changes in capital and assets. Refer to the Loan Portfolio and the Investment Securities sections for further discussion of the changes in assets. Additional members' equity information is included in Note 7 to the accompanying Consolidated Financial Statements.

RELATIONSHIP WITH AGRIBANK

Borrowing

We borrow from AgriBank to fund our lending operations in accordance with the Farm Credit Act. Approval from AgriBank is required for us to borrow elsewhere. A General Financing Agreement (GFA), as discussed in Note 6 to the accompanying Consolidated Financial Statements, governs this lending relationship.

The components of cost of funds under the GFA include:

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

In the periods presented, we were not subject to the risk premium component. Certain factors may impact our cost of funds, which primarily include market interest rate changes impacting marginal cost of debt as well as changes to pricing methodologies impacting the spread components described above.

The marginal cost of debt approach simulates matching the cost of underlying debt with similar terms as the anticipated terms of our loans to borrowers. This approach substantially protects us from market interest rate risk. We may occasionally engage in funding strategies that result in limited interest rate risk with approval by AgriBank's Asset Liability Committee.

Investment

We are required to invest in AgriBank capital stock as a condition of borrowing. This investment may be in the form of purchased stock or stock representing distributed AgriBank surplus. As of December 31, 2016, we were required by AgriBank to maintain an investment equal to 2.25% of the average quarterly balance of our note payable to AgriBank plus an additional 1.0% on growth that exceeded a targeted rate. AgriBank's current bylaws allow AgriBank to increase the required investment to 4.0%. In December 2016, AgriBank's Board approved the 2017 capital plan, which amended the required stock investments for affiliated Associations, effective January 1, 2017. The new required investment will be the lesser of 4.0% or a multiple component calculation based on a percentage of average quarterly balance of our note payable to AgriBank with a higher percentage on balances above a sustainable growth rate and includes a component for additional investments under the asset pool program. The 2017 component requirements are currently 2.25% on average note payable, with an additional 4.5% on growth in excess of a 5.5% sustainable growth rate and an 8.0% investment under the asset pool program.

As of December 31, 2016, we were required to hold AgriBank stock equal to 8.0% of the quarter end balance in the AgriBank Asset Pool program.

At December 31, 2016, $16.1 million of our investment in AgriBank consisted of stock representing distributed AgriBank surplus and $6.1 million consisted of purchased investment. For the periods presented in this report, we have received no dividend income on this stock investment and we do not anticipate any in future years.

Patronage

We receive different types of discretionary patronage from AgriBank, which is paid in cash. AgriBank's Board of Directors sets the level of:

- Patronage on our note payable with AgriBank
- Patronage based on the balance and net earnings of loans in the AgriBank Asset Pool program

Purchased Services

We purchase various services from AgriBank including certain financial and retail systems, financial reporting services, tax reporting services, technology services and insurance services.

The total cost of services we purchased from AgriBank was $547 thousand, $502 thousand and $521 thousand in 2016, 2015 and 2014, respectively. Costs of services purchased from AgriBank are partially dependent on the number of clients; if the number of clients decreases, the cost of services may increase.

Impact on Members' Investment

Due to the nature of our financial relationship with AgriBank, the financial condition and results of operations of AgriBank materially impact our members' investment.

OTHER RELATIONSHIPS AND PROGRAMS

Relationships with Other Farm Credit Institutions

FCS Commercial Finance Group: We participate in the FCS Commercial Finance Group (CFG) alliance with certain other associations in the AgriBank District to better meet the financial needs of agricultural producers and agribusiness operations. CFG is directed by representatives from participating associations. The income, expense and credit risks are allocated based on each association's participation interest of the CFG volume. Each association determines its commitment for new volume opportunities based on its capacity and preferences. We began participating in CFG effective January 1, 2016. We had $54.4 million of CFG volume at December 31, 2016. We also had $13.4 million of available commitment on CFG loans at December 31, 2016.

Insight Technology Unit: We participate in the Insight Technology Unit (Insight) with certain other AgriBank District associations to facilitate the development and maintenance of certain retail technology systems essential to providing credit to our borrowers. Insight is governed by representatives of each participating association. The expenses are shared pro rata based on the number of loans and leases of each participant.

CoBank, ACB: We have a relationship with CoBank, ACB (CoBank), a System bank, which involves purchasing and selling participation interests in loans. As part of this relationship, our equity investment in CoBank was $370 thousand at December 31, 2016, 2015 and 2014.

Farm Credit Foundations: We have a relationship with Farm Credit Foundations (Foundations) which involves purchasing human resource information systems and benefit, payroll and workforce management services. As of December 31, 2016, 2015 and 2014, our investment in Foundations was $13 thousand. The total cost of services we purchased from Foundations was $91 thousand, $74 thousand and $69 thousand in 2016, 2015 and 2014, respectively.

Unincorporated Business Entities (UBEs)

In certain circumstances we may establish separate entities to acquire and manage complex collateral, primarily for legal liability purposes.

RBF Acquisition VIII, LLC: We received an equity interest in RBF Acquisition VIII, LLC, which was formed to facilitate the acquisition, management and liquidation of assets acquired in 2009 from a troubled ethanol borrower. As of December 31, 2014, all assets of and subsequently our equity interest in RBF Acquisition VIII, LLC were liquidated and dissolved.

Programs

We are involved in a number of programs designed to improve our credit delivery, related services and marketplace presence.

Farm Cash Management: We offer Farm Cash Management to our members. Farm Cash Management links members' revolving lines of credit with an AgriBank investment bond to optimize members' use of funds.

REGULATORY MATTERS

Regulatory Capital Requirements

Effective January 1, 2017, the regulatory capital requirements for System banks and associations were modified. The stated objectives of the revised requirements are 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
- Meet the requirements of section 939A of the Dodd-Frank Wall Street Reform and Consumer Protection Act

The final rule replaced existing core surplus and total surplus ratios with common equity tier 1, tier 1 capital and total capital risk-based capital ratios. The final rule also added a tier 1 leverage ratio and an unallocated retained earnings equivalents leverage ratio. The permanent capital ratio continues to remain in effect with the final rule. Refer to Note 7 to the accompanying Consolidated Financial Statements for additional information regarding these ratios.

REPORT OF MANAGEMENT

AgHeritage Farm Credit Services, ACA

We prepare the Consolidated Financial Statements of AgHeritage Farm Credit Services, ACA (the Association) and are responsible for their integrity and objectivity, including amounts that must necessarily be based on judgments and estimates. The Consolidated Financial Statements have been prepared in conformity with accounting principles generally accepted in the United States of America. The Consolidated Financial Statements, in our opinion, fairly present the financial condition of the Association. Other financial information included in the Annual Report is consistent with that in the Consolidated Financial Statements.

To meet our responsibility for reliable financial information, we depend on accounting and internal control systems designed to provide reasonable, but not absolute, assurance that assets are safeguarded and transactions are properly authorized and recorded. Costs must be reasonable in relation to the benefits derived when designing accounting and internal control systems. Financial operations audits are performed to monitor compliance. PricewaterhouseCoopers LLP, our independent auditors, audit the Consolidated Financial Statements. They also conduct a review of internal controls to the extent necessary to comply with auditing standards generally accepted in the United States of America. The Farm Credit Administration also performs examinations for safety and soundness as well as compliance with applicable laws and regulations.

The Board of Directors has overall responsibility for our system of internal control and financial reporting. The Board of Directors and its Audit Committee consults regularly with us and meets periodically with the independent auditors and other auditors to review the scope and results of their work. The independent auditors have direct access to the Board of Directors, which is composed solely of directors who are not officers or employees of the Association.

The undersigned certify we have reviewed the Association's Annual Report, which has been prepared in accordance with all applicable statutory or regulatory requirements. The information contained herein is true, accurate and complete to the best of our knowledge and belief.

Michael D. Taylor
Chairperson of the Board
AgHeritage Farm Credit Services, ACA

Gregory W. Cole
President and Chief Executive Officer
AgHeritage Farm Credit Services, ACA

Kenneth L. Sumner
Senior Vice President and Chief Financial Officer
AgHeritage Farm Credit Services, ACA

March 14, 2017

REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING

AgHeritage Farm Credit Services, ACA

The AgHeritage Farm Credit Services, ACA (the Association) 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 2013 framework in Internal Control — Integrated Framework, 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 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.

Gregory W. Cole
President and Chief Executive Officer
AgHeritage Farm Credit Services, ACA

Kenneth L. Sumner
Senior Vice President and Chief Financial Officer
AgHeritage Farm Credit Services, ACA

March 14, 2017

REPORT OF AUDIT COMMITTEE

AgHeritage Farm Credit Services, ACA

The Consolidated Financial Statements were prepared under the oversight of the Audit Committee. The Audit Committee is composed of a subset of the Board of Directors of AgHeritage Farm Credit Services, ACA (the Association). The Audit Committee oversees the scope of the Association's internal audit program, the approval and independence of PricewaterhouseCoopers LLP (PwC) as independent auditors, the adequacy of the Association's system of internal controls and procedures and the adequacy of management's actions with respect to recommendations arising from those auditing activities. The Audit Committee's responsibilities are described more fully in the Internal Control Policy and the Audit Committee Charter.

Management is responsible for internal controls and the preparation of the Consolidated Financial Statements in accordance with accounting principles generally accepted in the United States of America. PwC is responsible for performing an independent audit of the Consolidated Financial Statements in accordance with auditing standards generally accepted in the United States of America and to issue their report based on their audit. The Audit Committee's responsibilities include monitoring and overseeing these processes.

In this context, the Audit Committee reviewed and discussed the audited Consolidated Financial Statements for the year ended December 31, 2016, with management. The Audit Committee also reviewed with PwC the matters required to be discussed by Statement on Auditing Standards AU-C 260, *The Auditor's Communication with Those Charged with Governance* and both PwC and the internal auditors directly provided reports on any significant matters to the Audit Committee.

The Audit Committee had discussions with and received written disclosures from PwC confirming its independence. The Audit Committee also reviewed the non-audit services provided by PwC, if any, and concluded these services were not incompatible with maintaining PwC's independence. The Audit Committee discussed with management and PwC any other matters and received any assurances from them as the Audit Committee deemed appropriate.

Based on the foregoing review and discussions and relying thereon, the Audit Committee recommended that the Board of Directors include the audited Consolidated Financial Statements in the Annual Report for the year ended December 31, 2016.

Sandra Morgan

Sandra Morgan
Chairperson of the Audit Committee
AgHeritage Farm Credit Services, ACA

Additional Audit Committee members:
Russell Bonner
Tracy Borgognoni
Jerry Burkett

March 14, 2017

Report of Independent Auditors

To the Board of Directors of AgHeritage Farm Credit Services, ACA,

We have audited the accompanying Consolidated Financial Statements of AgHeritage Farm Credit Services, ACA (the Association) and its subsidiaries, which comprise the consolidated statements of condition as of December 31, 2016, 2015 and 2014 and the related consolidated statements of 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.

Auditors' 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 AgHeritage Farm Credit Services, ACA and its subsidiaries as of December 31, 2016, 2015 and 2014 and the results of its operations and its cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

PricewaterhouseCoopers LLP

March 14, 2017

PricewaterhouseCoopers LLP, 45 South Seventh Street, Suite 3400, Minneapolis, MN 55402
T: (612) 596 6000, www.pwc.com/us

CONSOLIDATED STATEMENTS OF CONDITION

AgHeritage Farm Credit Services, ACA

(in thousands)

As of December 31	**2016**	2015	2014
ASSETS			
Loans	**$ 1,073,202**	$ 977,289	$ 965,083
Allowance for loan losses	**5,307**	1,520	981
Net loans	**1,067,895**	975,769	964,102
Investment in AgriBank, FCB	**22,219**	21,439	21,493
Investment securities	**6,004**	8,610	11,663
Accrued interest receivable	**19,070**	18,424	16,440
Deferred tax assets, net	**1,302**	230	--
Other assets	**6,138**	4,820	5,259
Total assets	**$ 1,122,628**	$ 1,029,292	$ 1,018,957
LIABILITIES			
Note payable to AgriBank, FCB	**$ 855,257**	$ 780,798	$ 789,775
Accrued interest payable	**4,171**	3,496	3,205
Deferred tax liabilities, net	**--**	--	51
Patronage distribution payable	**3,600**	3,500	3,400
Other liabilities	**3,699**	3,347	2,968
Total liabilities	**866,727**	791,141	799,399
Contingencies and commitments (Note 11)			
MEMBERS' EQUITY			
Protected members' equity	**1**	1	1
Capital stock and participation certificates	**2,875**	2,877	2,909
Unallocated surplus	**253,025**	235,273	216,648
Total members' equity	**255,901**	238,151	219,558
Total liabilities and members' equity	**$ 1,122,628**	$ 1,029,292	$ 1,018,957

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

CONSOLIDATED STATEMENTS OF INCOME

AgHeritage Farm Credit Services, ACA

(in thousands)

For the year ended December 31	**2016**	2015	2014
Interest income	**$ 48,200**	$ 45,354	$ 42,121
Interest expense	**15,941**	13,389	12,088
Net interest income	**32,259**	31,965	30,033
Provision for loan losses	**3,764**	1,360	--
Net interest income after provision for loan losses	**28,495**	30,605	30,033
Other income			
Patronage income	**3,900**	3,205	3,900
Financially related services income	**326**	382	521
Fee income	**2,254**	1,612	1,667
Miscellaneous income, net	**171**	97	146
Total other income	**6,651**	5,296	6,234
Operating expenses			
Salaries and employee benefits	**7,978**	8,186	7,358
Other operating expenses	**5,643**	4,767	4,463
Total operating expenses	**13,621**	12,953	11,821
Income before income taxes	**21,525**	22,948	24,446
Provision for income taxes	**218**	847	1,473
Net income	**$ 21,307**	$ 22,101	$ 22,973

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

CONSOLIDATED STATEMENTS OF CHANGES IN MEMBERS' EQUITY

AgHeritage Farm Credit Services, ACA

(in thousands)

	Protected Members' Equity	Capital Stock and Participation Certificates	Unallocated Surplus	Total Members' Equity
Balance as of December 31, 2013	$ 4	$ 2,896	$ 197,064	$ 199,964
Net income	--	--	22,973	22,973
Unallocated surplus designated for patronage distributions	--	--	(3,389)	(3,389)
Capital stock and participation certificates issued	--	206	--	206
Capital stock and participation certificates retired	(3)	(193)	--	(196)
Balance as of December 31, 2014	1	2,909	216,648	219,558
Net income	--	--	22,101	22,101
Unallocated surplus designated for patronage distributions	--	--	(3,476)	(3,476)
Capital stock and participation certificates issued	--	183	--	183
Capital stock and participation certificates retired	--	(215)	--	(215)
Balance as of December 31, 2015	1	2,877	235,273	238,151
Net income	**--**	**--**	**21,307**	**21,307**
Unallocated surplus designated for patronage distributions	**--**	**--**	**(3,555)**	**(3,555)**
Capital stock and participation certificates issued	**--**	**206**	**--**	**206**
Capital stock and participation certificates retired	**--**	**(208)**	**--**	**(208)**
Balance as of December 31, 2016	**$ 1**	**$ 2,875**	**$ 253,025**	**$ 255,901**

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

CONSOLIDATED STATEMENTS OF CASH FLOWS

AgHeritage Farm Credit Services, ACA

(in thousands)

For the year ended December 31		**2016**		2015		2014
Cash flows from operating activities						
Net income	**$**	**21,307**	$	22,101	$	22,973
Depreciation on premises and equipment		**305**		287		263
Gain on sale of premises and equipment, net		**(108)**		(39)		(70)
Amortization of premiums on loans and investment securities		**84**		149		182
Provision for loan losses		**3,764**		1,360		--
Stock patronage received from AgriBank, FCB		**--**		--		(1,276)
Loss (gain) on other property owned, net		**18**		(2)		(21)
Changes in operating assets and liabilities:						
Increase in accrued interest receivable		**(745)**		(1,998)		(1,854)
(Increase) decrease in other assets		**(2,238)**		164		200
Increase in accrued interest payable		**675**		291		313
Increase in other liabilities		**352**		328		357
Net cash provided by operating activities		**23,414**		22,641		21,067
Cash flows from investing activities						
Increase in loans, net		**(96,067)**		(12,937)		(72,787)
(Purchases) redemptions of investment in AgriBank, FCB, net		**(780)**		54		2,521
Decrease in investment securities, net		**2,491**		2,904		2,961
Proceeds from sales of other property owned		**409**		23		21
Purchases of premises and equipment, net		**(349)**		(203)		(416)
Net cash used in investing activities		**(94,296)**		(10,159)		(67,700)
Cash flows from financing activities						
Increase (decrease) in note payable to AgriBank, FCB, net		**74,459**		(8,977)		50,055
Patronage distributions paid		**(3,455)**		(3,376)		(3,289)
Capital stock and participation certificates retired, net		**(122)**		(129)		(133)
Net cash provided by (used in) financing activities		**70,882**		(12,482)		46,633
Net change in cash		**--**		--		--
Cash at beginning of year		**--**		--		--
Cash at end of year	**$**	**--**	$	--	$	--
Supplemental schedule of non-cash activities						
Stock financed by loan activities	**$**	**186**	$	168	$	194
Stock applied against loan principal		**66**		70		50
Stock applied against interest		**--**		1		1
Interest transferred to loans		**99**		13		10
Loans transferred to other property owned		**427**		77		--
Patronage distributions payable to members		**3,600**		3,500		3,400
Financed sales of other property owned		**--**		56		--
Supplemental information						
Interest paid	**$**	**15,266**	$	13,098	$	11,775
Taxes paid		**1,444**		1,193		1,456

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

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

AgHeritage Farm Credit Services, ACA

NOTE 1: ORGANIZATION AND OPERATIONS

Farm Credit System and District

The Farm Credit System (System) is a nationwide system of cooperatively owned banks and associations established by Congress to meet the credit needs of American agriculture. As of January 1, 2017, the System consisted of three Farm Credit Banks (FCB), one Agricultural Credit Bank (ACB) and 73 customer-owned cooperative lending institutions (associations). AgriBank, FCB (AgriBank), a System bank and its affiliated Associations are collectively referred to as the AgriBank Farm Credit District (AgriBank District or the District). At January 1, 2017, the District consisted of 17 Agricultural Credit Associations (ACA) that each have wholly-owned Federal Land Credit Association (FLCA) and Production Credit Association (PCA) subsidiaries.

FLCAs are authorized to originate long-term real estate mortgage loans. PCAs are authorized to originate short-term and intermediate-term loans. ACAs are authorized to originate long-term real estate mortgage loans and short-term and intermediate-term loans either directly or through their subsidiaries. Associations are authorized to provide lease financing options for agricultural purposes and are also authorized to purchase and hold certain types of investments. AgriBank provides funding to all associations chartered within the District.

Associations are authorized to provide, either directly or in participation with other lenders, credit and related services to eligible borrowers. Eligible borrowers may include farmers, ranchers, producers or harvesters of aquatic products, rural residents and farm-related service businesses. In addition, associations can participate with other lenders in loans to similar entities. Similar entities are parties that are not eligible for a loan from a System lending institution, but have operations that are functionally similar to the activities of eligible borrowers.

The Farm Credit Administration (FCA) is authorized by Congress to regulate the System banks and associations. We are examined by the FCA and certain association actions are subject to the prior approval of the FCA and/or AgriBank.

The Farm Credit Act established the Farm Credit System Insurance Corporation (FCSIC) to administer the Farm Credit Insurance Fund (Insurance Fund). The Insurance Fund is used to ensure the timely payment of principal and interest on Farm Credit Systemwide debt obligations, to ensure the retirement of protected borrower capital at par or stated value and for other specified purposes.

At the discretion of the FCSIC, the Insurance Fund is also available to provide assistance to certain troubled System institutions and for the operating expenses of the FCSIC. Each System bank is required to pay premiums into the Insurance Fund until the assets in the Insurance Fund equal 2.0% of the aggregated insured obligations adjusted to reflect the reduced risk on loans or investments guaranteed by federal or state governments. This percentage of aggregate obligations can be changed by the FCSIC, at its sole discretion, to a percentage it determines to be actuarially sound. The basis for assessing premiums is debt outstanding with adjustments made for nonaccrual loans and impaired investment securities which are assessed a surcharge while guaranteed loans and investment securities are deductions from the premium base. AgriBank, in turn, assesses premiums to District associations each year based on similar factors.

Association

AgHeritage Farm Credit Services, ACA (the Association) and its subsidiaries, AgHeritage Farm Credit Services, FLCA and AgHeritage Farm Credit Services, PCA (subsidiaries) are lending institutions of the System. We are a customer-owned cooperative providing credit and credit-related services to, or for the benefit of, eligible members for qualified agricultural purposes in the counties of Arkansas, Ashley, Bradley, Chicot, Cleburne, Cleveland, Desha, Drew, Fulton, Independence, Izard, Jackson, Jefferson, Lawrence, Lincoln, Lonoke, Monroe, Prairie, Pulaski, Randolph, Sharp, Stone, White and Woodruff in the state of Arkansas.

We borrow from AgriBank and provide financing and related services to our members. Our ACA holds all the stock of the FLCA and PCA subsidiaries.

We offer credit life, term life, credit disability, crop hail and multi-peril crop insurance to borrowers and those eligible to borrow. We also offer fee appraisals to our members.

NOTE 2: SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Accounting Principles and Reporting Policies

Our accounting and reporting policies conform to accounting principles generally accepted in the United States of America (GAAP) and the prevailing practices within the financial services industry. Preparing financial statements in conformity with GAAP requires us to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the Consolidated Financial Statements and the reported amounts of revenues and expenses during the period. Actual results could differ from those estimates.

Principles of Consolidation

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

Significant Accounting Policies

Loans: Loans are carried at their principal amount outstanding net of any unearned income, cumulative charge-offs, unamortized deferred fees and costs on originated loans and unamortized premiums or discounts on purchased loans. Loan interest is accrued and credited to interest income based upon the daily principal amount outstanding. Origination fees, net of related costs, are deferred and recognized over the life of the loan as an adjustment to net interest income. The net amount of loan fees and related origination costs are not material to the Consolidated Financial Statements taken as a whole.

Generally we place loans in nonaccrual status when principal or interest is delinquent for 90 days or more (unless the loan is well secured and in the process of collection) or circumstances indicate that full collection is not expected.

When a loan is placed in nonaccrual status, we reverse current year accrued interest to the extent principal plus accrued interest before the transfer exceeds the net realizable value of the collateral. Any unpaid interest accrued in a prior year is capitalized to the recorded investment of the loan, unless the net realizable value is less than the recorded investment in the loan, then it is charged-off against the allowance for loan losses. Any cash received on nonaccrual loans is applied to reduce the recorded investment in the loan, except in those cases where the collection of the recorded investment is fully expected and the loan does not have any unrecovered prior charge-offs. In these circumstances interest is credited to income when cash is received. Loans are charged-off at the time they are determined to be uncollectible. 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, the borrower has demonstrated payment performance and the loan is not classified as doubtful or loss.

In situations where, for economic or legal reasons related to the borrower's financial difficulties, we grant a concession for other than an insignificant period of time to the borrower that we would not otherwise consider, the related loan is classified as a troubled debt restructuring, also known as a formally restructured loan for regulatory purposes. A concession is generally granted in order to minimize economic loss and avoid foreclosure. Concessions vary by program and borrower and may include interest rate reductions, term extensions, payment deferrals, or an acceptance of additional collateral in lieu of payments. In limited circumstances, principal may be forgiven. Loans classified as troubled debt restructurings are considered risk loans (as defined below).

Loans that are sold as participations are transferred as entire financial assets, groups of entire financial assets or participating interests in the loans. The transfers of such assets or participating interests are structured such that control over the transferred assets, or participating interests have been surrendered and that all of the conditions have been met to be accounted for as a sale.

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

Loans in our portfolio that are considered impaired are analyzed individually to establish a specific allowance. A loan is impaired when it is probable that all amounts due will not be collected according to the contractual terms of the loan agreement. We generally measure impairment based on the net realizable value of the collateral. Risk loans include nonaccrual loans, accruing restructured loans and accruing loans 90 days or more past due. All risk loans are considered to be impaired loans.

We record a specific allowance to reduce the carrying amount of the risk loan by the amount the recorded investment exceeds the net realizable value of collateral. When we deem a loan to be uncollectible, we charge the loan principal and prior year(s) accrued interest against the allowance for loan losses. Subsequent recoveries, if any, are added to the allowance for loan losses.

An allowance is recorded for probable and estimable credit losses as of the financial statement date for loans that are not individually assessed as impaired. We use a two-dimensional loan risk rating model that incorporates a 14-point rating scale to identify and track the probability of borrower default and a separate 6-point scale addressing the loss severity. The combination of estimated default probability and loss severity is the primary basis for recognition and measurement of loan collectability of these pools of loans. These estimated losses may be adjusted for relevant current environmental factors.

Changes in the allowance for loan losses consist of provision activity, recorded in "Provision for loan losses" in the Consolidated Statements of Income, recoveries and charge-offs.

Investment in AgriBank: Our stock investment in AgriBank is on a cost plus allocated equities basis.

Investment Securities: We are authorized to purchase and hold certain types of investments. As we have the positive intent and ability to hold these investments to maturity, they have been classified as held-to-maturity and are carried at cost adjusted for the amortization of premiums and accretion of discounts. If an investment is determined to be other-than-temporarily impaired, the carrying value of the security is written down to fair value. The impairment loss is separated into credit related and non-credit related components. The credit related component is expensed through "Miscellaneous income, net" in the Consolidated Statements of Income in the period of impairment. The non-credit related component is recognized in other comprehensive income. Purchased premiums and discounts are amortized or accreted using the straight-line method, which approximates the interest method, over the terms of the respective securities. Realized gains and losses are determined using specific identification method and are recognized in current operations.

Other Property Owned: Other property owned, consisting of real and personal property acquired through foreclosure or deed in lieu of foreclosure, is recorded at the fair value less estimated selling costs upon acquisition and is included in "Other assets" in the Consolidated Statements of Condition. 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 costs 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. Related income, expenses and gains or losses from operations and carrying value adjustments are included in "Miscellaneous income, net" in the Consolidated Statements of Income. We had no other property owned at December 31, 2016, 2015 or 2014.

Premises and Equipment: The carrying amount of premises and equipment is at cost, less accumulated depreciation and is included in "Other assets" in the Consolidated Statements of Condition. Calculation of depreciation is generally on the straight-line method over the estimated useful lives of the assets.

Gains or losses on disposition are included in “Miscellaneous income, net” in the Consolidated Statements of Income. Depreciation and maintenance and repair expenses are included in “Other operating expenses” in the Consolidated Statements of Income, and improvements are capitalized.

Post-Employment Benefit Plans: The District has various post-employment benefit plans in which our employees participate. Expenses related to these plans are included in “Salaries and employee benefits” in the Consolidated Statements of Income.

Certain employees participate in the AgriBank District Retirement Plan. The plan is comprised of two benefit formulas. At their option, employees hired prior to October 1, 2001, are on the cash balance formula or on the final average pay formula. Benefits eligible employees hired between October 1, 2001, and December 31, 2006, are on the cash balance formula. Effective January 1, 2007, the AgriBank District Retirement Plan was closed to new employees. The AgriBank District Retirement Plan utilizes the "Projected Unit Credit" actuarial method for financial reporting and funding purposes.

Certain employees also participate in the AgriBank District Pension Restoration Plan. This plan restores retirement benefits to certain highly compensated eligible employees that would have been provided under the qualified plan if such benefits were not above certain Internal Revenue Code limits.

We also provide certain health insurance benefits to eligible retired employees according to the terms of those benefit plans. The anticipated cost of these benefits is accrued during the employees’ active service period.

The defined contribution plan allows eligible employees to save for their retirement either pre-tax, post-tax, or both, with an employer match on a percentage of the employee’s contributions. We provide benefits under this plan for those employees that do not participate in the AgriBank District Retirement Plan in the form of a fixed percentage of salary contribution in addition to the employer match. Employer contributions are expensed when incurred.

Income Taxes: The ACA and PCA accrue federal and state income taxes. Deferred tax assets and liabilities are recognized for future tax consequences of temporary differences between the carrying amounts and tax basis of assets and liabilities. Deferred tax assets are recorded if the deferred tax asset is more likely than not to be realized. If the realization test cannot be met, the deferred tax asset is reduced by a valuation allowance. The expected future tax consequences of uncertain income tax positions are accrued.

The FLCA is exempt from federal and other taxes to the extent provided in the Farm Credit Act.

Patronage Program: We accrue patronage distributions according to a prescribed formula approved by the Board of Directors. Generally, we pay the accrued patronage during the first quarter after year end.

Off-Balance Sheet Credit Exposures: Commitments to extend credit are agreements to lend to customers, generally having fixed expiration dates or other termination clauses. Standby letters of credit are agreements to pay a beneficiary if there is a default on a contractual arrangement. Commercial letters of credit are agreements to pay a beneficiary under specific conditions. Any reserve for unfunded lending commitments and unexercised letters of credit is based on management’s best estimate of losses inherent in these instruments, but the commitments have not yet disbursed. Factors such as likelihood of disbursal and likelihood of losses given disbursement are utilized in determining a reserve, if needed. Based on our assessment, any reserve is recorded in “Other liabilities” in the Consolidated Statements of Condition and a corresponding loss is recorded in “Provision for credit losses” in the Consolidated Statements of Income. However, no such reserve was necessary as of December 31, 2016, 2015 or 2014.

Cash: For purposes of reporting cash flow, cash includes cash on hand.

Fair Value Measurement: The accounting guidance describes three levels of inputs that may be used to measure fair value.

Level 1 — Unadjusted quoted prices in active markets for identical assets or liabilities that the reporting entity has the ability to access at the measurement date.

Level 2 — Observable inputs other than quoted prices included within Level 1 that are observable for the asset or liability either directly or indirectly. Level 2 inputs include:

- Quoted prices for similar assets or liabilities in active markets
- Quoted prices for identical or similar assets or liabilities in markets that are not active so that they are traded less frequently than exchange-traded instruments, quoted prices that are not current, or principal market information that is not released publicly
- Inputs that are observable such as interest rates and yield curves, prepayment speeds, credit risks and default rates
- Inputs derived principally from or corroborated by observable market data by correlation or other means

Level 3 — Unobservable inputs that are supported by little or no market activity and that are significant to the fair value of the assets or liabilities. These unobservable inputs reflect the reporting entity’s own judgments about assumptions that market participants would use in pricing the asset or liability. Level 3 assets and liabilities include financial instruments whose value is determined using pricing models, discounted cash flow methodologies, or similar techniques, as well as instruments for which the determination of fair value requires significant management judgment or estimation.

Recently Issued or Adopted Accounting Pronouncements

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

Standard	Description	Effective date and financial statement impact
In June 2016, the FASB issued ASU 2016-13 “Financial Instruments – Credit Losses.”	The guidance replaces the current incurred loss impairment methodology with a methodology that reflects expected credit losses and requires consideration of a broader range of reasonable and supportable information to determine credit loss estimates. Credit losses relating to available-for-sale securities would also be recorded through an allowance for credit losses.	The guidance is effective for nonpublic entities for annual reporting periods beginning after December 15, 2020, and interim periods within annual periods beginning after December 15, 2021. Early adoption is permitted as of annual reporting periods beginning after December 15, 2018, including interim periods within those annual periods. We are currently evaluating the impact of the guidance on our financial condition, results of operations, cash flows and financial statement disclosures.
In February 2016, the FASB issued ASU 2016-02 “Leases.”	The guidance modifies the recognition and accounting for lessees and lessors and requires expanded disclosures regarding assumptions used to recognize revenue and expenses related to leases.	The guidance is effective for nonpublic entities for annual reporting periods beginning after December 15, 2019, and interim periods the subsequent year. Early adoption is permitted and modified retrospective adoption is required. We are currently evaluating the impact of the guidance on our financial condition, results of operations, cash flows and financial statement disclosures.
In January 2016, the FASB issued ASU 2016-01 “Recognition and Measurement of Financial Assets and Financial Liabilities.”	The guidance is intended to enhance the reporting model for financial instruments to provide users of financial statements with more decision-useful information. The amendments address certain aspects of recognition, measurement, presentation and disclosure of financial statements.	The guidance is effective for nonpublic entities for annual reporting periods beginning after December 15, 2018, and interim periods with annual periods beginning after December 15, 2019. Certain disclosure changes are permitted to be immediately adopted for annual reporting periods that have not yet been made available for issuance. Nonpublic entities are no longer required to include certain fair value of financial instruments disclosures as part of these disclosure changes. We have immediately adopted this guidance and have excluded such disclosures from our Notes to Consolidated Financial Statements. Early adoption is permitted for interim and annual reporting periods beginning after December 15, 2017, for other applicable sections of the guidance. We are currently evaluating the impact of the remaining guidance on our financial condition, results of operations, cash flows and financial statement disclosures.
In February 2015, the FASB issued ASU 2015-02 “Consolidation-Amendments to the Consolidation Analysis.”	The guidance modifies the assessment of Variable Interest Entity (VIE) characteristics as well as the assessment of related parties. Additional clarifying guidance was issued in October 2016 under ASU 2016-17 “Consolidation-Interests Held through Related Parties That are under Common Control.”	The guidance is effective for nonpublic entities for annual reporting after December 15, 2016, and interim periods within annual periods beginning after December 15, 2017. Early adoption is allowed, including in any interim period. The adoption of this guidance did not have a material impact on our financial condition, results of operations, cash flows and financial statement disclosures.
In August 2014, the FASB issued ASU 2014-15 “Presentation of Financial Statements-Going Concern.”	The guidance requires management to perform interim and annual assessments of an entity’s ability to continue as a going concern within one year after the date the Financial Statements are issued or within one year after the Financial Statements are available to be issued, when applicable. Substantial doubt to continue as a going concern exists if it is probable that the entity will be unable to meet its obligations for the assessed period.	This guidance became effective for all entities for interim and annual periods ending after December 15, 2016. The adoption of this guidance did not have a material impact on our financial condition, results of operations, cash flows or financial statement disclosures.

Standard	Description	Effective date and financial statement impact
In May 2014, the FASB issued ASU 2014-09 "Revenue from Contracts with Customers."	The guidance governs revenue recognition from contracts with customers and requires an entity to recognize revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. Financial instruments and other contractual rights within the scope of other guidance issued by the FASB are excluded from the scope of this new revenue recognition guidance. In this regard, a majority of our contracts would be excluded from the scope of this new guidance.	The guidance is effective for nonpublic entities for annual reporting periods beginning after December 15, 2017, and interim periods within annual periods beginning after December 15, 2018. In March 2016, the FASB issued ASUs 2016-08 and 2016-10 which provided further clarifying guidance on the previously issued standard. We are in the process of reviewing contracts to determine the effect, if any, on our financial condition and results of operations.

NOTE 3: LOANS AND ALLOWANCE FOR LOAN LOSSES

Loans by Type

(dollars in thousands)	**2016**		2015		2014	
As of December 31	Amount	**%**	Amount	%	Amount	%
Real estate mortgage	**$ 556,800**	**51.9%**	$ 515,525	52.8%	$ 506,437	52.5%
Production and intermediate term	**372,673**	**34.7%**	364,804	37.3%	368,580	38.2%
Agribusiness	**98,428**	**9.2%**	59,994	6.1%	52,677	5.5%
Other	**45,301**	**4.2%**	36,966	3.8%	37,389	3.8%
Total	**$ 1,073,202**	**100.0%**	$ 977,289	100.0%	$ 965,083	100.0%

The other category is primarily comprised of rural residential real estate loans and certain assets originated under the Mission Related Investment authority.

Portfolio Concentrations

Concentrations exist when there are amounts loaned to multiple borrowers engaged in similar activities, which could cause them to be similarly impacted by economic conditions. We lend primarily within agricultural industries.

As of December 31, 2016, volume plus commitments to our ten largest borrowers totaled an amount equal to 9.3% of total loans and commitments.

While these concentrations represent our maximum potential credit risk, as it relates to recorded loan principal, a substantial portion of our lending activities are collateralized. This reduces our exposure to credit loss associated with our lending activities. 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. Long-term real estate loans are secured by the first liens on the underlying real property. FCA regulations state that long-term real estate loans are not to exceed 85% (97% if guaranteed by a government agency) of the property's appraised value at origination, and our underwriting standards generally limit lending to no more than 65% at origination. 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 lender in the collateral, may result in loan-to-value ratios in excess of the regulatory maximum. The District has an internally maintained database which uses market data to estimate market values of collateral for a significant portion of the real estate mortgage portfolio. We consider credit risk exposure in establishing the allowance for loan losses.

Participations

We may purchase or sell participation interests with other parties in order to diversify risk, manage loan volume or comply with the FCA Regulations or General Financing Agreement (GFA) limitations.

Participations Purchased and Sold

	AgriBank		Other Farm Credit Institutions		Total	
(in thousands)	Participations		Participations		Participations	
As of December 31, 2016	Purchased	Sold	Purchased	Sold	Purchased	Sold
Real estate mortgage	**$ --**	**$ (30,793)**	**$ 38,174**	**$ (28,278)**	**$ 38,174**	**$ (59,071)**
Production and intermediate term	**--**	**--**	**24,043**	**(11,645)**	**24,043**	**(11,645)**
Agribusiness	**--**	**(12,671)**	**84,779**	**(34,468)**	**84,779**	**(47,139)**
Other	**--**	**(324)**	**16,443**	**--**	**16,443**	**(324)**
Total	**$ --**	**$ (43,788)**	**$ 163,439**	**$ (74,391)**	**$ 163,439**	**$ (118,179)**

As of December 31, 2015	AgriBank Participations Purchased	AgriBank Participations Sold	Other Farm Credit Institutions Participations Purchased	Other Farm Credit Institutions Participations Sold	Total Participations Purchased	Total Participations Sold
Real estate mortgage	$ --	$ (36,122)	$ 30,222	$ (30,241)	$ 30,222	$ (66,363)
Production and intermediate term	--	--	18,450	(12,614)	18,450	(12,614)
Agribusiness	--	(15,604)	46,790	(41,263)	46,790	(56,867)
Other	--	(574)	6,789	--	6,789	(574)
Total	$ --	$ (52,300)	$ 102,251	$ (84,118)	$ 102,251	$ (136,418)

As of December 31, 2014	AgriBank Participations Purchased	AgriBank Participations Sold	Other Farm Credit Institutions Participations Purchased	Other Farm Credit Institutions Participations Sold	Total Participations Purchased	Total Participations Sold
Real estate mortgage	$ --	$ (40,771)	$ 32,569	$ (19,419)	$ 32,569	$ (60,190)
Production and intermediate term	--	--	12,022	(10,853)	12,022	(10,853)
Agribusiness	--	(4,777)	46,260	(16,465)	46,260	(21,242)
Other	--	(621)	4,301	--	4,301	(621)
Total	$ --	$ (46,169)	$ 95,152	$ (46,737)	$ 95,152	$ (92,906)

Information in the preceding chart excludes loans entered into under our Mission Related Investment authority.

Credit Quality and Delinquency

We utilize the FCA Uniform Classification System to categorize loans into five credit quality categories. The categories are:

- Acceptable – loans are non-criticized loans representing the highest quality. They are expected to be fully collectible. This category is further differentiated into various probabilities of default.
- Other assets especially mentioned (Special Mention) – are currently collectible but exhibit some potential weakness. These loans involve increased credit risk, but not to the point of justifying a substandard classification.
- Substandard – loans exhibit some serious weakness in repayment capacity, equity and/or collateral pledged on the loan.
- Doubtful – loans exhibit similar weaknesses as substandard loans. Doubtful loans have additional weaknesses in existing factors, conditions and values that make collection in full highly questionable.
- Loss – loans are considered uncollectible.

We had no loans categorized as loss at December 31, 2016, 2015 or 2014.

Credit Quality of Loans

(dollars in thousands) **As of December 31, 2016**	Acceptable Amount	Acceptable %	Special Mention Amount	Special Mention %	Substandard/ Doubtful Amount	Substandard/ Doubtful %	Total Amount	Total %
Real estate mortgage	**$ 542,893**	**95.8%**	**$ 11,252**	**2.0%**	**$ 12,324**	**2.2%**	**$ 566,469**	**100.0%**
Production and intermediate term	**346,885**	**91.0%**	**21,115**	**5.5%**	**13,232**	**3.5%**	**381,232**	**100.0%**
Agribusiness	**98,865**	**100.0%**	**--**	**--**	**--**	**--**	**98,865**	**100.0%**
Other	**44,583**	**98.0%**	**603**	**1.3%**	**301**	**0.7%**	**45,487**	**100.0%**
Total	**$ 1,033,226**	**94.6%**	**$ 32,970**	**3.0%**	**$ 25,857**	**2.4%**	**$ 1,092,053**	**100.0%**

As of December 31, 2015	Acceptable Amount	Acceptable %	Special Mention Amount	Special Mention %	Substandard/ Doubtful Amount	Substandard/ Doubtful %	Total Amount	Total %
Real estate mortgage	$ 511,319	97.5%	$ 10,488	2.0%	$ 2,858	0.5%	$ 524,665	100.0%
Production and intermediate term	362,738	97.2%	7,646	2.0%	3,086	0.8%	373,470	100.0%
Agribusiness	55,086	91.5%	5,134	8.5%	--	--	60,220	100.0%
Other	35,680	96.2%	861	2.3%	560	1.5%	37,101	100.0%
Total	$ 964,823	96.9%	$ 24,129	2.4%	$ 6,504	0.7%	$ 995,456	100.0%

As of December 31, 2014	Acceptable Amount	Acceptable %	Special Mention Amount	Special Mention %	Substandard/ Doubtful Amount	Substandard/ Doubtful %	Total Amount	Total %
Real estate mortgage	$ 502,972	97.8%	$ 2,608	0.5%	$ 8,490	1.7%	$ 514,070	100.0%
Production and intermediate term	361,718	96.0%	6,389	1.7%	8,654	2.3%	376,761	100.0%
Agribusiness	50,868	96.2%	2,006	3.8%	--	--	52,874	100.0%
Other	35,982	95.8%	973	2.6%	604	1.6%	37,559	100.0%
Total	$ 951,540	97.0%	$ 11,976	1.2%	$ 17,748	1.8%	$ 981,264	100.0%

Note: Accruing loans include accrued interest receivable.

Aging Analysis of Loans

(in thousands) **As of December 31, 2016**	30-89 Days Past Due	90 Days or More Past Due	Total Past Due	Not Past Due or Less than 30 Days Past Due	Total	90 Days Past Due and Accruing
Real estate mortgage	**$ 988**	**$ 1,062**	**$ 2,050**	**$ 564,419**	**$ 566,469**	**$ --**
Production and intermediate term	**515**	**2,865**	**3,380**	**377,852**	**381,232**	**--**
Agribusiness	**--**	**--**	**--**	**98,865**	**98,865**	**--**
Other	**1,079**	**19**	**1,098**	**44,389**	**45,487**	**--**
Total	**$ 2,582**	**$ 3,946**	**$ 6,528**	**$ 1,085,525**	**$ 1,092,053**	**$ --**

As of December 31, 2015	30-89 Days Past Due	90 Days or More Past Due	Total Past Due	Not Past Due or Less than 30 Days Past Due	Total	90 Days Past Due and Accruing
Real estate mortgage	$ 6,056	$ 952	$ 7,008	$ 517,657	$ 524,665	$ --
Production and intermediate term	904	335	1,239	372,231	373,470	--
Agribusiness	--	--	--	60,220	60,220	--
Other	297	156	453	36,648	37,101	130
Total	$ 7,257	$ 1,443	$ 8,700	$ 986,756	$ 995,456	$ 130

As of December 31, 2014	30-89 Days Past Due	90 Days or More Past Due	Total Past Due	Not Past Due or Less than 30 Days Past Due	Total	90 Days Past Due and Accruing
Real estate mortgage	$ 4,175	$ 457	$ 4,632	$ 509,438	$ 514,070	$ --
Production and intermediate term	2,106	73	2,179	374,582	376,761	--
Agribusiness	--	--	--	52,874	52,874	--
Other	1,283	680	1,963	35,596	37,559	645
Total	$ 7,564	$ 1,210	$ 8,774	$ 972,490	$ 981,264	$ 645

Note: Accruing loans include accrued interest receivable.

All loans 90 days or more past due and still accruing interest were adequately secured and in the process of collection and, as such, were eligible to remain in accruing status.

Risk Loans

Risk loans are loans for which it is probable that all principal and interest will not be collected according to the contractual terms. Interest income recognized and cash payments received on nonaccrual risk loans are applied as described in Note 2.

Risk Loan Information

(in thousands) As of December 31		2016		2015		2014
Nonaccrual loans:						
Current as to principal and interest	**$**	**6,637**	$	1,122	$	1,113
Past due		**4,146**		1,332		3,463
Total nonaccrual loans		**10,783**		2,454		4,576
Accruing restructured loans		**--**		--		--
Accruing loans 90 days or more past due		**--**		130		645
Total risk loans	**$**	**10,783**	$	2,584	$	5,221
Volume with specific reserves	**$**	**3,727**	$	352	$	113
Volume without specific reserves		**7,056**		2,232		5,108
Total risk loans	**$**	**10,783**	$	2,584	$	5,221
Total specific reserves	**$**	**2,755**	$	223	$	113
For the year ended December 31		**2016**		2015		2014
Income on accrual risk loans	**$**	**5**	$	9	$	15
Income on nonaccrual loans		**379**		577		152
Total income on risk loans	**$**	**384**	$	586	$	167
Average recorded risk loans	**$**	**7,490**	$	4,655	$	2,952

Note: Accruing loans include accrued interest receivable.

The increase in nonaccrual loans was primarily due to several real estate mortgage and production and intermediate term loans transferred to nonaccrual status during the year ended December 31, 2016.

Nonaccrual Loans by Loan Type

(in thousands) As of December 31		2016		2015		2014
Real estate mortgage	**$**	**6,506**	$	1,450	$	2,134
Production and intermediate term		**4,155**		632		2,123
Other		**122**		372		319
Total	**$**	**10,783**	$	2,454	$	4,576

Additional Impaired Loan Information by Loan Type

(in thousands)	As of December 31, 2016 Recorded Investment	Unpaid Principal Balance	Related Allowance	For the year ended December 31, 2016 Average Impaired Loans	Interest Income Recognized
Impaired loans with a related allowance for loan losses:					
Real estate mortgage	$ 805	$ 807	$ 22	$ 549	$ --
Production and intermediate term	2,922	3,077	2,733	1,922	--
Agribusiness	--	--	--	--	--
Other	--	--	--	--	--
Total	$ 3,727	$ 3,884	$ 2,755	$ 2,471	$ --
Impaired loans with no related allowance for loan losses:					
Real estate mortgage	$ 5,702	$ 5,905	$ --	$ 3,886	$ 194
Production and intermediate term	1,232	1,596	--	811	131
Agribusiness	--	--	--	--	--
Other	122	198	--	322	59
Total	$ 7,056	$ 7,699	$ --	$ 5,019	$ 384
Total impaired loans:					
Real estate mortgage	$ 6,507	$ 6,712	$ 22	$ 4,435	$ 194
Production and intermediate term	4,154	4,673	2,733	2,733	131
Agribusiness	--	--	--	--	--
Other	122	198	--	322	59
Total	$ 10,783	$ 11,583	$ 2,755	$ 7,490	$ 384

	As of December 31, 2015 Recorded Investment	Unpaid Principal Balance	Related Allowance	For the year ended December 31, 2015 Average Impaired Loans	Interest Income Recognized
Impaired loans with a related allowance for loan losses:					
Real estate mortgage	$ 3	$ 24	$ 2	$ 4	$ --
Production and intermediate term	349	358	221	1,239	--
Agribusiness	--	--	--	--	--
Other	--	1	--	--	--
Total	$ 352	$ 383	$ 223	$ 1,243	$ --
Impaired loans with no related allowance for loan losses:					
Real estate mortgage	$ 1,447	$ 1,713	$ --	$ 1,870	$ 266
Production and intermediate term	284	1,094	--	1,009	278
Agribusiness	--	--	--	--	5
Other	501	603	--	533	37
Total	$ 2,232	$ 3,410	$ --	$ 3,412	$ 586
Total impaired loans:					
Real estate mortgage	$ 1,450	$ 1,737	$ 2	$ 1,874	$ 266
Production and intermediate term	633	1,452	221	2,248	278
Agribusiness	--	--	--	--	5
Other	501	604	--	533	37
Total	$ 2,584	$ 3,793	$ 223	$ 4,655	$ 586

	As of December 31, 2014			For the year ended December 31, 2014	
	Recorded Investment	Unpaid Principal Balance	Related Allowance	Average Impaired Loans	Interest Income Recognized
Impaired loans with a related allowance for loan losses:					
Real estate mortgage	$ --	$ --	$ --	$ --	$ --
Production and intermediate term	113	139	113	65	--
Agribusiness	--	--	--	--	--
Other	--	--	--	--	--
Total	$ 113	$ 139	$ 113	$ 65	$ --
Impaired loans with no related allowance for loan losses:					
Real estate mortgage	$ 2,134	$ 2,370	$ --	$ 1,218	$ 89
Production and intermediate term	2,011	2,351	--	1,164	42
Agribusiness	--	--	--	--	5
Other	963	1,047	--	505	31
Total	$ 5,108	$ 5,768	$ --	$ 2,887	$ 167
Total impaired loans:					
Real estate mortgage	$ 2,134	$ 2,370	$ --	$ 1,218	$ 89
Production and intermediate term	2,124	2,490	113	1,229	42
Agribusiness	--	--	--	--	5
Other	963	1,047	--	505	31
Total	$ 5,221	$ 5,907	$ 113	$ 2,952	$ 167

The recorded investment in the loan is the unpaid principal amount increased or decreased by applicable accrued interest and unamortized premium, discount, finance charges and acquisition costs and may also reflect a previous direct charge-off of the investment.

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

We did not have any material commitments to lend additional money to borrowers whose loans were at risk at December 31, 2016.

Troubled Debt Restructurings (TDRs)

Included within our loans are troubled debt restructurings (TDRs). These loans have been modified by granting a concession in order to maximize the collection of amounts due when a borrower is experiencing financial difficulties. All risk loans, including TDRs, are analyzed within our allowance for loan losses.

TDR Activity

(in thousands) For the year ended December 31	**2016**		2015		2014	
	Pre-modification	Post-modification	Pre-modification	Post-modification	Pre-modification	Post-modification
Production and intermediate term	**$ 6**	**$ 6**	$ 303	$ 299	$ 117	$ 117
Other	**--**	**--**	--	--	45	45
Total	**$ 6**	**$ 6**	$ 303	$ 299	$ 162	$ 162

Pre-modification represents the outstanding recorded investment of the loan just prior to restructuring and post-modification represents the outstanding recorded investment of the loan immediately following the restructuring. The recorded investment of the loan is the unpaid principal amount of the receivable increased or decreased by applicable accrued interest and unamortized premium, discount, finance charges and acquisition costs and may also reflect a previous direct charge-off.

The primary types of modification included interest rate reduction below market and extension of maturity.

TDRs that Occurred Within the Previous 12 Months that Subsequently Defaulted

(in thousands)	**2016**	2015	2014
Production and intermediate term	**6**	--	32
Other	**--**	--	45
Total	**$ 6**	$ --	$ 77

TDRs Outstanding

(in thousands) As of December 31		2016		2015		2014
Production and intermediate term		**8**		44		5
Other		**19**		26		35
Total TDRs in nonaccrual status	**$**	**27**	$	70	$	40

There were no commitments to lend to borrowers whose loans have been modified in a TDR at December 31, 2016.

Allowance for Loan Losses

Changes in Allowance for Loan Losses

(in thousands) For the year ended December 31		2016		2015		2014
Balance at beginning of year	**$**	**1,520**	$	981	$	1,002
Provision for loan losses		**3,764**		1,360		--
Loan recoveries		**114**		312		19
Loan charge-offs		**(91)**		(1,133)		(40)
Balance at end of year	**$**	**5,307**	$	1,520	$	981

The increase in allowance for loan losses was related to $3.8 million provision for loan losses recorded in 2016 due to the recognition of specific reserves and changes in loss estimates.

Changes in Allowance for Loan Losses and Year End Recorded Investments by Loan Type

(in thousands)		Real Estate Mortgage		Production and Intermediate Term		Agribusiness		Other		Total
Allowance for loan losses:										
Balance as of December 31, 2015	**$**	**354**	**$**	**1,076**	**$**	**57**	**$**	**33**	**$**	**1,520**
Provision for loan losses		**170**		**3,407**		**84**		**103**		**3,764**
Loan recoveries		**18**		**95**		**--**		**1**		**114**
Loan charge-offs		**(10)**		**(81)**		**--**		**--**		**(91)**
Balance as of December 31, 2016	**$**	**532**	**$**	**4,497**	**$**	**141**	**$**	**137**	**$**	**5,307**
Ending balance: individually evaluated for impairment	**$**	**22**	**$**	**2,733**	**$**	**--**	**$**	**--**	**$**	**2,755**
Ending balance: collectively evaluated for impairment	**$**	**510**	**$**	**1,764**	**$**	**141**	**$**	**137**	**$**	**2,552**
Recorded investment in loans outstanding:										
Ending balance as of December 31, 2016	**$**	**566,469**	**$**	**381,232**	**$**	**98,865**	**$**	**45,487**	**$**	**1,092,053**
Ending balance: individually evaluated for impairment	**$**	**6,507**	**$**	**4,154**	**$**	**--**	**$**	**122**	**$**	**10,783**
Ending balance: collectively evaluated for impairment	**$**	**559,962**	**$**	**377,078**	**$**	**98,865**	**$**	**45,365**	**$**	**1,081,270**

		Real Estate Mortgage		Production and Intermediate Term		Agribusiness		Other		Total
Allowance for loan losses:										
Balance as of December 31, 2014	$	215	$	703	$	44	$	19	$	981
Provision for loan losses		450		891		13		6		1,360
Loan recoveries		11		293		--		8		312
Loan charge-offs		(322)		(811)		--		--		(1,133)
Balance as of December 31, 2015	$	354	$	1,076	$	57	$	33	$	1,520
Ending balance: individually evaluated for impairment	$	2	$	221	$	--	$	--	$	223
Ending balance: collectively evaluated for impairment	$	352	$	855	$	57	$	33	$	1,297
Recorded investment in loans outstanding:										
Ending balance as of December 31, 2015	$	524,665	$	373,470	$	60,220	$	37,101	$	995,456
Ending balance: individually evaluated for impairment	$	1,450	$	633	$	--	$	501	$	2,584
Ending balance: collectively evaluated for impairment	$	523,215	$	372,837	$	60,220	$	36,600	$	992,872

	Real Estate Mortgage	Production and Intermediate Term	Agribusiness	Other	Total
Allowance for loan losses:					
Balance as of December 31, 2013	$ 116	$ 814	$ 61	$ 11	$ 1,002
Provision for (reversal of) loan losses	98	(79)	(17)	(2)	--
Loan recoveries	5	4	--	10	19
Loan charge-offs	(4)	(36)	--	--	(40)
Balance as of December 31, 2014	$ 215	$ 703	$ 44	$ 19	$ 981
Ending balance: individually evaluated for impairment	$ --	$ 113	$ --	$ --	$ 113
Ending balance: collectively evaluated for impairment	$ 215	$ 590	$ 44	$ 19	$ 868
Recorded investment in loans outstanding:					
Ending balance as of December 31, 2014	$ 514,070	$ 376,761	$ 52,874	$ 37,559	$ 981,264
Ending balance: individually evaluated for impairment	$ 2,134	$ 2,124	$ --	$ 963	$ 5,221
Ending balance: collectively evaluated for impairment	$ 511,936	$ 374,637	$ 52,874	$ 36,596	$ 976,043

The recorded investment in the loan is the unpaid principal amount increased or decreased by applicable accrued interest and unamortized premium, discount, finance charges and acquisition costs and may also reflect a previous direct charge-off of the investment.

NOTE 4: INVESTMENT IN AGRIBANK

As of December 31, 2016, we were required by AgriBank to maintain an investment equal to 2.25% of the average quarterly balance of our note payable to AgriBank plus an additional 1.0% on growth that exceeded a targeted rate. In December 2016, AgriBank's Board approved the 2017 capital plan, which amended the required stock investments for affiliated Associations, effective January 1, 2017. The new required investment will be the lesser of 4.0% or a multiple component calculation based on a percentage of our average quarterly balance of our note payable to AgriBank with a higher percentage on balances above a sustainable growth rate and includes a component for additional investments under the asset pool program. The 2017 component requirements are currently 2.25% on average note payable, with an additional 4.5% on growth in excess of a 5.5% sustainable growth rate and an 8.0% investment under the asset pool program.

As of December 31, 2016, we were also required by AgriBank to maintain an investment equal to 8.0% of the quarter end balance of the participation interests in real estate loans sold to AgriBank under the AgriBank Asset Pool program.

The balance of our investment in AgriBank, all required stock, was $22.2 million, $21.4 million and $21.5 million at December 31, 2016, 2015 and 2014, respectively.

NOTE 5: INVESTMENT SECURITIES

We held investment securities of $6.0 million, $8.6 million and $11.7 million at December 31, 2016, 2015 and 2014, respectively. Our investment securities consisted of securities containing loans guaranteed by the Small Business Administration (SBA).

The investment securities have been classified as held-to-maturity. The investment portfolio is evaluated for other-than-temporary impairment. To date, we have not recognized any impairment on our investment portfolio.

Additional Investment Securities Information

(dollars in thousands)

As of December 31	**2016**	2015	2014
Amortized cost	**$ 6,004**	$ 8,610	$ 11,663
Unrealized gains	**270**	332	504
Unrealized losses	**--**	--	(1)
Fair value	**$ 6,274**	$ 8,942	$ 12,166
Weighted average yield	**2.3%**	2.3%	2.4%

Investment income is recorded in “Interest income” in the Consolidated Statements of Income and totaled $149 thousand, $238 thousand and $320 thousand in 2016, 2015 and 2014, respectively.

NOTE 6: NOTE PAYABLE TO AGRIBANK

Our note payable to AgriBank represents borrowings, in the form of a line of credit, to fund our loan portfolio. The line of credit is governed by a GFA and our assets serve as collateral.

Note Payable Information

(dollars in thousands) As of December 31	**2016**	2015	2014
Line of credit	**$ 1,100,000**	$ 1,037,000	$ 953,000
Outstanding principal under the line of credit	**855,257**	780,798	789,775
Interest rate	**2.0%**	1.7%	1.6%

Our note payable matures May 31, 2017, at which time the note will be renegotiated.

The GFA provides for limitations on our ability to borrow funds based on specified factors or formulas relating primarily to outstanding balances, credit quality and financial condition. At December 31, 2016, and throughout the year, we materially complied with the GFA terms and were not declared in default under any GFA covenants or provisions.

NOTE 7: MEMBERS' EQUITY

Capitalization Requirements

In accordance with the Farm Credit Act, each borrower is required to invest in us as a condition of obtaining a loan. As authorized by the Agricultural Credit Act and our capital bylaws, the Board of Directors has adopted a capital plan that establishes a stock purchase requirement for obtaining a loan of 2.0% of the customer's total loan(s) or one thousand dollars, whichever is less. The purchase of one participation certificate is required of all customers and of all non-stockholder customers who purchase financial services. The Board of Directors may increase the amount of required investment to the extent authorized in the capital bylaws. The borrower acquires ownership of the capital stock at the time the loan or lease is made. The aggregate par value of the stock is added to the principal amount of the related obligation. We retain a first lien on the stock or participation certificates owned by customers.

Protection Mechanisms

Under the Farm Credit Act, certain borrower equity is protected. We are required to retire protected borrower equity at par or stated value regardless of its book value. Protected borrower equity includes capital stock and participation certificates that were outstanding as of January 6, 1988 or were issued prior to October 6, 1988 as a requirement for obtaining a loan. If we were to be unable to retire protected borrower equity at par value or stated value, the FCSIC would provide the amounts needed to retire this equity.

Regulatory Capitalization Requirements

Select Capital Ratios

As of December 31	**2016**	2015	2014	Regulatory Minimums
Permanent capital ratio	**20.0%**	19.9%	18.9%	7.0%
Total surplus ratio	**19.8%**	19.6%	18.6%	7.0%
Core surplus ratio	**19.8%**	19.6%	18.6%	3.5%

These ratios are calculated in accordance with FCA Regulations and are discussed below:

- The permanent capital ratio is average at-risk capital plus any allocated excess stock divided by average risk-adjusted assets.
- The total surplus ratio is average unallocated surplus less any deductions made in the computation of permanent capital divided by average risk-adjusted assets.
- The core surplus ratio is average unallocated surplus less any deductions made in the computation of total surplus and less any allocated excess stock investment in AgriBank divided by average risk-adjusted assets.

Risk-adjusted assets have been defined by FCA Regulations as the Statement of Condition assets and off-balance-sheet commitments adjusted by various percentages, depending on the level of risk inherent in the various types of assets.

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

FCA Revised Capital Requirements

	Regulatory Minimums	Capital Conservation Buffer	Total
Risk-adjusted:			
Common equity tier 1 ratio	4.5%	2.5%	7.0%
Tier 1 capital ratio	6.0%	2.5%	8.5%
Total capital ratio	8.0%	2.5%	10.5%
Non-risk-adjusted:			
Tier 1 leverage ratio	4.0%	1.0%	5.0%
UREE leverage ratio	1.5%	0.0%	1.5%

If the capital ratios fall below the total requirements, including the buffer amounts, capital distributions (equity redemptions, dividends and patronage) and discretionary senior executive bonuses are restricted or prohibited without prior FCA approval.

Regulatory capital included any allocated investment in AgriBank that is in excess of the required investment under an allotment agreement with AgriBank. We had no allocated excess stock at December 31, 2016, 2015 or 2014. Effective January 1, 2017, the regulatory capital requirements allow for allotment agreements for only the permanent capital ratio and as such any stock in excess of our AgriBank required investment will not be included in the common equity tier 1, tier 1 capital, total capital or leverage ratios.

Description of Equities

The following represents information regarding classes and number of shares of stock and participation certificates outstanding. All shares and participation certificates are stated at a $5.00 par value.

	Number of Shares		
As of December 31	**2016**	2015	2014
Class A common stock (protected)	**199**	199	199
Class C common stock (at-risk)	**554,998**	552,460	558,167
Participation certificates (at-risk)	**19,938**	22,906	23,571

Under our bylaws, we are also authorized to issue Class B common stock and Class D common stock. Each of these classes of stock is at-risk and nonvoting. The Class B common stock has a $5.00 par value per share and the Class D common stock has a $1,000 par value per share. Currently, no stock of these classes has been issued.

Only holders of Class C common stock have voting rights. Our bylaws do not prohibit us from paying dividends on any classes of stock. However, no dividends have been declared to date.

Our bylaws generally permit stock and participation certificates to be retired at the discretion of our Board of Directors and in accordance with our capitalization plans, provided prescribed capital standards have been met. At December 31, 2016, we exceeded the prescribed standards. We do not anticipate any significant changes in capital that would affect the normal retirement of stock.

In the event of our liquidation or dissolution, according to our bylaws, any remaining assets after payment or retirement of all liabilities will be distributed in the following order of priority:

- first, pro rata to holders of common stock and participation certificates
- second, any remaining assets of the Association after such distribution shall be distributed to present and former patrons on a patronage basis, to the extent practicable

Any impairment of capital stock shall be treated as impairing all shares of common stock and participations certificates pro rata; however, protected stock will be retired at par value regardless of impairment.

All classes of stock are transferable to other customers who are eligible to hold such classes of stock. Transfers of stock are only allowed when we meet minimum regulatory capital requirements.

Patronage Distributions

We accrued patronage distributions of $3.6 million, $3.5 million and $3.4 million at December 31, 2016, 2015 and 2014, respectively. Generally, the patronage distributions are paid in cash during the first quarter after year end. The Board of Directors may authorize a distribution of earnings provided we meet all statutory and regulatory requirements.

The FCA Regulations prohibit patronage distributions to the extent they would reduce our permanent capital ratio below the minimum permanent capital adequacy standards. Additionally, effective January 1, 2017, patronage distributions may be restricted or prohibited without prior FCA approval if capital ratios fall below the total requirements, including the buffer amounts. We do not foresee any events that would result in this prohibition in 2017.

NOTE 8: INCOME TAXES

Provision for Income Taxes

Provision for Income Taxes

(dollars in thousands) For the year ended December 31	2016	2015	2014
Current:			
Federal	**$ 1,078**	$ 934	$ 1,220
State	**212**	194	249
Total current	**$ 1,290**	$ 1,128	$ 1,469
Deferred:			
Federal	**$ (890)**	$ (234)	$ 4
State	**(182)**	(47)	--
Total deferred	**(1,072)**	(281)	4
Provision for income taxes	**$ 218**	$ 847	$ 1,473
Effective tax rate	**1.0%**	3.7%	6.0%

Reconciliation of Taxes at Federal Statutory Rate to Provision for Income Taxes

(in thousands) For the year ended December 31	2016	2015	2014
Federal tax at statutory rates	**$ 7,318**	$ 7,802	$ 8,312
State tax, net	**20**	93	162
Patronage distributions	**(1,224)**	(1,190)	(1,156)
Effect of non-taxable entity	**(5,939)**	(5,877)	(5,869)
Other	**43**	19	24
Provision for income taxes	**$ 218**	$ 847	$ 1,473

Deferred Income Taxes

Tax laws require certain items to be included in our tax returns at different times than the items are reflected on our Consolidated Statements of Income. Some of these items are temporary differences that will reverse over time. We record the tax effect of temporary differences as deferred tax assets and liabilities netted on our Consolidated Statements of Condition.

Deferred Tax Assets and Liabilities

(in thousands) As of December 31	2016	2015	2014
Allowance for loan losses	**$ 1,814**	$ 509	$ 295
Postretirement benefit accrual	**202**	201	191
Accrued incentive	**178**	187	169
Accrued patronage income not received	**(179)**	(97)	(158)
AgriBank 2002 allocated stock	**(243)**	(243)	(243)
Accrued pension asset	**(184)**	(102)	(113)
Depreciation	**(79)**	(80)	(57)
Other liabilities	**(207)**	(145)	(135)
Deferred tax assets (liabilities), net	**$ 1,302**	$ 230	$ (51)
Gross deferred tax assets	**$ 2,194**	$ 897	$ 655
Gross deferred tax liabilities	**$ (892)**	$ (667)	$ (706)

A valuation allowance for the deferred tax assets was not necessary at December 31, 2016, 2015 or 2014.

We have not provided for deferred income taxes on patronage allocations received from AgriBank prior to 1993. Such allocations, distributed in the form of stock, are subject to tax only upon conversion to cash. Our intent is to permanently maintain this investment in AgriBank. Our total permanent investment in AgriBank is $9.6 million. Additionally, we have not provided deferred income taxes on accumulated FLCA earnings of $201.1 million as it is our intent to permanently maintain this equity in the FLCA or to distribute the earnings to members in a manner that results in no additional tax liability to us.

Our income tax returns are subject to review by various United States taxing authorities. We record accruals for items that we believe may be challenged by these taxing authorities. However, we had no uncertain income tax positions at December 31, 2016. In addition, we believe we are no longer subject to income tax examinations for years prior to 2013.

NOTE 9: EMPLOYEE BENEFIT PLANS

Pension and Post-Employment Benefit Plans

Complete financial information for the pension and post-employment benefit plans may be found in the Combined AgriBank and affiliated Associations 2016 Annual Report (District financial statements).

The Farm Credit Foundations Plan Sponsor and Trust Committees provide oversight of the benefit plans. These governance committees are comprised of elected or appointed representatives (senior leadership and/or Board of Director members) from the participating organizations. The Coordinating Committee (a subset of the Plan Sponsor Committee comprised of AgriBank District representatives) is responsible for decisions regarding retirement benefits at the direction of the AgriBank District participating employers. The Trust Committee is responsible for fiduciary and plan administrative functions.

Pension Plan: Certain employees participate in the AgriBank District Retirement Plan, a District-wide multi-employer defined benefit retirement plan. The Department of Labor has determined the plan to be a governmental plan; therefore, the plan is not subject to the provisions of the Employee Retirement Income Security Act of 1974, as amended (ERISA). As the plan is not subject to ERISA, the plan's benefits are not insured by the Pension Benefit Guaranty Corporation. Accordingly, the amount of accumulated benefits that participants would receive in the event of the plan's termination is contingent on the sufficiency of the plan's net assets to provide benefits at that time. This Plan is noncontributory and covers certain eligible District employees. The assets, liabilities and costs of the plan are not segregated by participating entities. As such, plan assets are available for any of the participating employers' retirees at any point in time. Additionally, if a participating employer stops contributing to the plan, the unfunded obligations of the plan may be borne by the remaining participating employers. Further, if we choose to stop participating in the plan, we may be required to pay an amount based on the underfunded status of the plan. Because of the nature of the plan, any individual employer is not able to unilaterally change the provisions of the plan. If an employee transfers to another employer within the same plan, the employee benefits under the plan transfer. Benefits are based on salary and years of service. There is no collective bargaining agreement in place as part of this plan.

AgriBank District Retirement Plan Information

(in thousands)

As of December 31	2016	2015	2014
Unfunded liability	**$ 374,305**	$ 453,825	$ 423,881
Projected benefit obligation	**1,269,625**	1,255,259	1,234,960
Fair value of plan assets	**895,320**	801,434	811,079
Accumulated benefit obligation	**1,096,913**	1,064,133	1,051,801

For the year ended December 31	2016	2015	2014
Total plan expense	**$ 53,139**	$ 63,800	$ 45,827
Our allocated share of plan expenses	**772**	904	647
Contributions by participating employers	**90,000**	62,722	52,032
Our allocated share of contributions	**1,258**	890	728

The unfunded liability reflects the net of the fair value of the plan assets and the projected benefit obligation at the date of these Consolidated Financial Statements. The projected benefit obligation is the actuarial present value of all benefits attributed by the pension benefit formula to employee service rendered prior to the measurement date based on assumed future compensation levels. The accumulated benefit obligation is the actuarial present value of the benefits attributed to employee service rendered before the measurement date and based on current employee service and compensation. The funding status is subject to many variables including performance of plan assets and interest rate levels. Therefore, changes in assumptions could significantly affect these estimates.

Costs are determined for each individual employer based on costs directly related to their current employees as well as an allocation of the remaining costs based proportionately on the estimated projected liability of the employer under this plan. We recognize our proportional share of expense and contribute a proportional share of funding. Our allocated share of plan expenses is included in "Salaries and employee benefits" in the Consolidated Statements of Income.

Benefits paid to participants in the District were $56.4 million in 2016. While the plan is a governmental plan and is not subject to minimum funding requirements, the employers contribute amounts necessary on an actuarial basis to provide the plan with sufficient assets to meet the benefits to be paid to participants. The amount of the total District employer contributions expected to be paid into the pension plan during 2017 is $90.0 million. Our allocated share of these pension contributions is expected to be $1.3 million. The amount ultimately to be contributed and the amount ultimately recognized as expense as well as the timing of those contributions and expenses, are subject to many variables including performance of plan assets and interest rate levels. These variables could result in actual contributions and expenses being greater than or less than the amounts reflected in the District financial statements.

Nonqualified Retirement Plan: We also participate in the District-wide nonqualified defined benefit Pension Restoration Plan. This plan restores retirement benefits to certain highly compensated eligible employees that would have been provided under the qualified plan if such benefits were not above certain Internal Revenue Code limits.

Pension Restoration Plan Information

(in thousands) As of December 31		2016		2015		2014
Unfunded liability	$	**28,514**	$	31,650	$	27,695
Projected benefit obligation		**28,514**		31,650		27,695
Accumulated benefit obligation		**22,778**		26,323		22,959

For the year ended December 31		2016		2015		2014
Total plan expense	$	**5,767**	$	3,776	$	3,652
Our allocated share of plan expenses		**73**		45		29
Our cash contributions		**73**		--		--

The nonqualified plan is funded as the benefits are paid; therefore, there are no assets in the plan and the unfunded liability is equal to the projected benefit obligation. The amount of the pension benefits funding status is subject to many variables including interest rate levels. Therefore, changes in assumptions could significantly affect these estimates.

Costs are determined for each individual employer based on costs directly related to their participants in the plan. Our allocated share of plan expenses is included in “Salaries and employee benefits” in the Consolidated Statements of Income. The Pension Restoration Plan is unfunded; however, we contributed $34 thousand to a Rabbi Trust in 2012 to fund our future liability under this plan. A Rabbi Trust is a trust created for the purpose of supporting the nonqualified benefit obligation of employers to their employees. There were no benefits paid under the Pension Restoration Plan to our senior officers who were actively employed during the year.

Retiree Medical Plans: District employers also provide certain health insurance benefits to eligible retired employees according to the terms of the benefit plans. The anticipated costs of these benefits are accrued during the period of the employee’s active status.

Retiree Medical Plan Information

(in thousands) For the year ended December 31		2016		2015		2014
Postretirement benefit expense	$	**41**	$	84	$	61
Our cash contributions		**39**		37		38

Postretirement benefit costs are included in “Salaries and employee benefits” in the Consolidated Statements of Income. Our cash contributions are equal to the benefits paid.

Defined Contribution Plans

We participate in a District-wide defined contribution plan. For employees hired before January 1, 2007, employee contributions are matched dollar for dollar up to 2.0% and 50 cents on the dollar on the next 4.0% on both pre-tax and post-tax contributions. The maximum employer match is 4.0%. For employees hired after December 31, 2006, we contribute 3.0% of the employee’s compensation and will match employee contributions dollar for dollar up to a maximum of 6.0% on both pre-tax and post-tax contributions. The maximum employer contribution is 9.0%.

We also participate in a District-wide Nonqualified Deferred Compensation Plan. Eligible participants must meet one of the following criteria: certain salary thresholds as determined by the IRS, are either a Chief Executive Officer or President of a participating employer, or have previously elected pre-tax deferrals in 2006 under predecessor nonqualified deferred compensation plans. Under this plan the employee may defer a portion of his/her salary, bonus and other compensation. Additionally, the plan provides for supplemental employer matching contributions related to any compensation deferred by the employee that would have been eligible for a matching contribution under the defined contribution plan if it were not for certain IRS limitations.

Employer contribution expenses for the defined contribution plan, included in “Salaries and employee benefits” in the Consolidated Statements of Income, were $248 thousand, $241 thousand and $210 thousand in 2016, 2015 and 2014, respectively. These expenses were equal to our cash contributions for each year.

NOTE 10: RELATED PARTY TRANSACTIONS

In the ordinary course of business, we may enter into loan transactions with our officers, directors, their immediate family members and other organizations with which such persons may be associated. Such transactions may be subject to special approval requirements contained in the FCA Regulations and are made on the same terms, including interest rates, amortization schedules and collateral, as those prevailing at the time for comparable transactions with other persons. In our opinion, none of these loans outstanding at December 31, 2016, involved more than a normal risk of collectability.

Related Party Loans Information

(in thousands)		2016		2015		2014
As of December 31:						
Total related party loans	**$**	**14,707**	$	14,731	$	12,548
For the year ended December 31:						
Advances to related parties	**$**	**16,669**	$	19,599	$	13,565
Repayments by related parties		**16,741**		17,372		10,542

The related parties can be different each year end primarily due to changes in the composition of the Board of Directors and the mix of organizations with which such persons may be associated. Advances and repayments on loans in the preceding chart are related to those considered related parties at year end.

As discussed in Note 6, we borrow from AgriBank, in the form of a line of credit, to fund our loan portfolio.

We purchase various services from AgriBank including certain financial and retail systems, financial reporting services, tax reporting services, technology services and insurance services. The total cost of services we purchased from AgriBank was $547 thousand, $502 thousand and $521 thousand in 2016, 2015 and 2014, respectively.

We also purchase human resource information systems, benefit, payroll and workforce management services from Farm Credit Foundations (Foundations). As of December 31, 2016, 2015 and 2014, our investment in Foundations was $13 thousand. The total cost of services purchased from Foundations was $91 thousand, $74 thousand and $69 thousand in 2016, 2015 and 2014, respectively.

NOTE 11: CONTINGENCIES AND COMMITMENTS

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

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

We have commitments to extend credit and letters of credit to satisfy the financing needs of our borrowers. These financial instruments involve, to varying degrees, elements of credit risk that may be recognized in the 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 loan contract. Standby letters of credit are agreements to pay a beneficiary if there is a default on a contractual arrangement. At December 31, 2016, we had commitments to extend credit and unexercised commitments related to standby letters of credit of $280.9 million. Additionally, we had $1.2 million of issued standby letters of credit as of December 31, 2016.

Commitments to extend credit and letters of credit generally have fixed expiration dates or other termination clauses and we may require payment of a fee. If commitments to extend credit and letters of credit remain unfulfilled or have not expired, they may have credit risk not recognized in the financial statements. Many of the commitments to extend credit and letters of credit will expire without being fully drawn upon. Therefore, the total commitments do not necessarily represent future cash requirements. Certain letters of credit may have recourse provisions that would enable us to recover from third parties amounts paid under guarantees, thereby limiting our maximum potential exposure. The credit risk involved in issuing these financial instruments is essentially the same as that involved in extending loans to borrowers and we apply the same credit policies. The amount of collateral obtained, if deemed necessary by us upon extension of credit, is based on management’s credit evaluation of the borrower.

NOTE 12: FAIR VALUE MEASUREMENTS

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

We did not have any assets or liabilities measured at fair value on a recurring basis at December 31, 2016, 2015 or 2014.

Non-Recurring

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

Assets Measured at Fair Value on a Non-recurring Basis

(in thousands)

As of December 31, 2016	Fair Value Measurement Using				
	Level 1	Level 2	Level 3	Total Fair Value	Total (Losses)
Impaired loans	**$ --**	**$ 1,021**	**$ --**	**$ 1,021**	**$ (2,623)**
Other property owned	**--**	**--**	**--**	**--**	**(18)**

As of December 31, 2015	Fair Value Measurement Using				Total (Losses)
	Level 1	Level 2	Level 3	Total Fair Value	Gains
Impaired loans	$ --	$ 135	$ --	$ 135	$ (1,243)
Other property owned	--	--	--	--	2

As of December 31, 2014	Fair Value Measurement Using				Total (Losses)
	Level 1	Level 2	Level 3	Total Fair Value	Gains
Impaired loans	$ --	$ --	$ --	$ --	$ (14)
Other property owned	--	--	--	--	21

Valuation Techniques

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

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

NOTE 13: SUBSEQUENT EVENTS

We have evaluated subsequent events through March 14, 2017, which is the date the Consolidated Financial Statements were available to be issued. There have been no material subsequent events that would require recognition in our 2016 Consolidated Financial Statements or disclosures in the Notes to Consolidated Financial Statements.

DISCLOSURE INFORMATION REQUIRED BY REGULATIONS

AgHeritage Farm Credit Services, ACA

(Unaudited)

Description of Business

General information regarding the business is incorporated herein by reference from Note 1 to the accompanying Consolidated Financial Statements.

The description of significant business developments, if any, is incorporated herein by reference from the “Management's Discussion and Analysis" section of the accompanying Consolidated Financial Statements.

Description of Property

Property Information

Location	Description	Usage
Little Rock, AR	Leased	Headquarters
Batesville, AR	Leased	Branch
Brinkley, AR	Owned	Branch
Dermott, AR	Owned	Branch
Lonoke, AR	Owned	Branch
Newport, AR	Owned	Branch
Pocahontas, AR	Owned	Branch
Searcy, AR	Owned	Branch
Star City, AR	Owned	Branch
Stuttgart, AR	Owned	Branch

Legal Proceedings

Information regarding legal proceedings is discussed in Note 11 to the accompanying Consolidated Financial Statements. We were not subject to any enforcement actions as of December 31, 2016.

Description of Capital Structure

Information regarding our capital structure is discussed in Note 7 to the accompanying Consolidated Financial Statements.

Description of Liabilities

Information regarding liabilities is discussed in Notes 6, 7, 8, 9 and 11 to the accompanying Consolidated Financial Statements.

Selected Financial Data

The "Consolidated Five-Year Summary of Selected Financial Data” is presented at the beginning of the accompanying Consolidated Financial Statements.

Management’s Discussion and Analysis

Information regarding any material aspects of our financial condition, changes in financial condition and results of operations are discussed in the "Management's Discussion and Analysis” section of the accompanying Consolidated Financial Statements.

Board of Directors

Our Board of Directors is organized into the following committees to carry out Board responsibilities:

The **Audit Committee** oversees financial reporting, the adequacy of our internal control systems, the scope of the Association’s internal audit program, the independence of the outside auditors and the processes for monitoring compliance with laws and regulations. The Audit Committee also oversees the adequacy of management’s actions with respect to recommendations arising from auditing activities;

The **Finance Committee** monitors our financial and capital planning, asset/liability management and funding and investment activities. Committee members serve as a resource to the Board by maintaining a more in-depth knowledge of our financial activities;

The **Executive Committee** addresses issues of Board governance and the Board’s continuing efforts to strengthen and renew the Board, administers a process for maintaining and periodically reviewing board policies and administers a planning process focused upon achieving our mission and maintaining a viable, competitive institution. The committee is authorized to take action on behalf of the Board on matters requiring board approval between normally scheduled board meetings when necessary. Such authorization is to be reviewed and acted upon at the next board meeting;

The **Human Resources Committee** oversees and provides overall direction and/or recommendations for compensation, benefits and human resource performance management programs; and

The **Member Relations Committee** provides direction on the Association's agriculture public policy position at the local, state and national level. Committee members serve as a resource for maintaining high quality member relations/involvement programs, board involvement of market and customer needs and in developing programs to attract young and beginning and next generation farmers.

Board of Directors as of December 31, 2016, including business experience during the last five years

Name	Term	Principal Occupation and Other Affiliations
Michael D. Taylor Chairperson Service Began: 2001	2016-2020	**Principal Occupation:** Self-employed grain farmer and natural gas development **Other Affiliations:** Manager: Wood Family Mineral Development, LLC, involved in natural gas Board member of White County Farm Bureau
Dwain Morris Vice Chairperson Service Began: 1991	2014-2018	**Principal Occupation:** Self-employed grain farmer **Other Affiliations:** President: 4-D Farms Board member of Randolph County Farm Bureau
Russell Bonner Service Began: 2006	2014-2018	**Principal Occupation:** Self-employed grain farmer **Other Affiliations:** Board member of Monroe County Farm Bureau Board member of New Peoples Gin, cotton ginning
Tracy Borgognoni Service Began: 2012	2016-2020	**Principal Occupation:** Self-employed grain and cotton farmer
Jerry Burkett Service Began: 2002	2013-2017	**Principal Occupation:** Self-employed grain farmer **Other Affiliations:** Board member of Arkansas County Farm Bureau
Mike Burkett Service Began: 2006	2013-2017	**Principal Occupation:** Self-employed grain farmer **Other Affiliations:** Board member of Woodruff County Farm Bureau
Ray C. "Chuck" Culver III Outside Director Service Began: 1992	2016-2020	**Principal Occupation:** Director of External Relations, Division of Agriculture at the University of Arkansas System
Mike Ellis Service Began: 2007	2015-2019	**Principal Occupation:** Self-employed grain and livestock farmer
Sandra Morgan Outside Director Service Began: 2015	2015-2018	**Principal Occupation:** Vice President & Chief Financial Officer at Riceland Foods, Inc.
Clay Schaefer Service Began: 2011	2015-2019	**Principal Occupation:** Self-employed grain farmer **Other Affiliations:** Board member of Riceland Foods, Inc. Board member of Tri-County Farmers Association
Keith Watkins Service Began: 2008	2016-2020	**Principal Occupation:** Self-employed grain and cattle farmer **Other Affiliations:** Board member of Riceland Foods, Inc. Board member of White County Farm Bureau
Scott Young Service Began: 2013	2013-2017	**Principal Occupation:** Self-employed grain and timber farmer Partner in Dogwood Farms President and shareholder in Jim Young Farms, Inc. **Other Affiliations:** Board member of Ashley County Farm Bureau

Pursuant to our bylaws, directors are paid a reasonable amount for attendance at board meetings, committee meetings or other special assignments. Directors are also reimbursed for reasonable expenses incurred in connection with such meetings or assignments. Our Board of Directors has adopted a rate of $500 per day. Board members also receive a $3,500 annual retainer fee, except for the Board Chairperson and Vice Chairperson, who receive a retainer fee of $5,000 and $4,250, respectively, for their additional duties as Board Chairperson and Vice Chairperson.

Information regarding compensation paid to each director who served during 2016 follows:

	Number of Days Served		Compensation Paid for Service on a Board Committee		Total Compensation Paid in 2016
Name	Board Meetings	Other Official Activities		Name of Committee	
Michael D. Taylor	9.0	26.5	$ 600	Audit ($250), HR ($100), Finance ($250)	$ 23,300
Dwain Morris	9.0	31.5	100	HR ($100)	24,800
Russell Bonner	8.0	6.5	500	Audit ($250), Finance ($250)	10,850
Tracy Borgognoni	9.0	2.0	250	Audit ($250)	9,100
Jerry Burkett	9.0	11.5	500	Audit ($250), Finance ($250)	13,850
Mike Burkett	9.0	5.5	100	HR ($100)	10,950
Ray C. "Chuck" III Culver	9.0	4.5	-		10,350
Mike Ellis	8.0	2.0	250	Finance ($250)	8,600
Sandra Morgan	9.0	6.0	350	Audit ($250), HR ($100)	11,400
Clay Schaefer	9.0	12.0	100	HR ($100)	14,400
Keith Watkins	8.0	6.0	250	Finance ($250)	10,600
Scott Young	9.0	6.5	100	HR ($100)	11,450
					$ 159,650

Senior Officers

Senior Officers as of December 31, 2016, including business experience during the last five years

Name and Position	Business experience and other business interests
Gregory W. Cole President/Chief Executive Officer	**Business experience:** President/Chief Executive Officer since April 2008 **Other business interests:** Board Member of Arkansas Agriculture Foundation, an organization that promotes awareness of agriculture in Arkansas
Kenneth L. Sumner SVP/Chief Financial Officer	**Business experience:** SVP/Chief Financial Officer since August 2009 **Other business interests:** Board Treasurer of Wade Knox Child Advocacy Center, a local charity President of Arkansas Waterfowl Association, a not-for-profit organization that raises funds to support local charities and to provide outdoor opportunities for children who would not have the opportunity otherwise
Drue Ford SVP/Chief Credit Officer	**Business experience:** SVP/Chief Credit Officer since October 2006
Leslie J. Brown VP/Human Resources	**Business experience:** VP/Human Resources since February 2015 Administrator of Benefits and Compensation at major insurance company prior to February 2015 **Other business interests:** Treasurer of Arkansas Compensation Association, which provides information and leadership to compensation professionals

Senior Officer Compensation

We believe the design and governance of our senior officer compensation program is consistent with the highest standards of risk management and provides total compensation that promotes our mission to ensure a safe, sound and dependable source of credit and related services for agriculture and rural America. Our compensation philosophy aims to provide a competitive total rewards package that will enable us to attract and retain highly qualified officers with the requisite expertise and skills while achieving desired business results aligned with the best interests of our members. The design of our senior officer compensation program supports our risk management goals through a set of checks and balances, including (1) a balanced mix of base and variable pay, (2) a balanced use of performance measures that are risk-adjusted where appropriate, and (3) a pay-for-performance process that allocates individual awards based on both results and how those results were achieved.

Elements of Compensation:

Base Salary: The CEO, senior officer and highly compensated individuals base salaries reflect the employee's experience and level of responsibility. Compensation plans for all employees, except the CEO, are subject to review and approval by the Human Resources Committee of our Board of Directors. Information is accumulated regarding competitive market conditions and used in assessing adequate compensation for all employees. CEO salary is reviewed and approved by the Board of Directors.

Short-term Incentives: The short-term incentive plan available only to the CEO and senior officers is paid annually based on performance criteria approved by our Human Resources Committee of the Board of Directors. The criteria related to the overall association performance include return on assets, loan volume, capital ratios, surplus, operating rate, credit quality, credit administration, adverse assets to risk funds, borrower concentration and customer satisfaction. Additional criteria related to personal performance include attainment of personal objectives and overall performance rating. We calculate the incentives after the end of the plan year (the plan year is the calendar year) and pay out the incentives within 60 days of year-end. There were no material amendments to the plan during the last fiscal year.

Highly compensated employees' short-term incentive plan is based on an adjusted pre-tax net income and the employee's individual performance. Individual performance includes a variety of objectives including credit quality, fees, growth and job competencies. There were no material changes to the plan during the last fiscal year.

Other incentives: We have a retention incentive available to all employees, including the CEO, senior officers and highly compensated individuals. The incentive is paid with an annual component and a long-term component, subject to the participant's employment after three years. Eligibility to participate in this incentive program includes the employee's most recent performance as well as specialized knowledge and strategic role of his/her position. Due to the retention nature of this incentive, it is reported in the Compensation Table in the period paid. In addition, we have a sales incentive plan that is available to all full-time branch employees. The incentives are paid for sales of insurance and leasing products, are paid monthly and are subject to the cap set by FCA.

Retirement Plans: We have various post-employment benefit plans which are generally available to all association employees, including the CEO, senior officers and highly compensated individuals, based on dates of service to the association and are not otherwise differentiated by position, unless specifically stated. Information regarding the post-employment benefit plans is included in Notes 2 and 9 to the accompanying Consolidated Financial Statements.

Other Components of Compensation: Additionally, compensation associated with any company-paid vehicles, group term life insurance premiums, disability insurance premiums or other on-the-spot incentives such as gift cards, may be made available to the CEO, senior officers and highly compensated individuals based on job criteria or similar plans available to all employees.

Compensation to the CEO, Senior Officers, and Highly Compensated Individuals

(in thousands) Name	Year	Salary	Bonus	Deferred/ Perquisites	Other	Total
Gregory W. Cole, CEO	**2016**	**$ 312**	**$ 156**	**$ 4**	**$ 294**	**$ 766**
Gregory W. Cole, CEO	2015	300	151	4	287	742
Gregory W. Cole, CEO	2014	270	135	3	517	925
Aggregate Number of Senior Officers and Highly Compensated Individuals, excluding CEO						
Five*	**2016**	**$ 650**	**$ 190**	**$ 18**	**$ 408**	**$ 1,266**
Six**	2015	735	266	18	380	1,399
Four	2014	548	231	16	449	1,244

*Includes compensation for a departure of a senior officer in September 2016.
**Includes compensation for a senior officer who retired during 2015 as well as the individual hired into this position during 2015.

The amount in the "Other" category in the preceding table primarily includes:

- Employer match on defined contribution plans available to all employees.
- Changes in the value of pension benefits. The change in value of the pension benefits is defined as the change in the vested portion of the present value of the accumulated benefit obligation from December 31 of the prior year to December 31 of the most recent year for the District-wide Pension Plan and the Pension Restoration Plan, as applicable, as disclosed in Note 9 to the accompanying Consolidated Financial Statements. This change in value does not represent cash payments made by the Association during the year, but rather is an estimate of the change in the Association's future obligations under the pension plans. The change in the value of the pension benefits is highly sensitive to discount rates used to value the plan liabilities to participants.
- Amounts related to the resignation of a senior officer in September 2016, and for 2015, amounts related to the retirement of a senior officer.

No tax reimbursements are made to the CEO, senior officer and highly compensated individuals.

The value of the pension benefits from December 31, 2015, to December 31, 2016, changed primarily due to interest cost, accumulation of an additional year of credited service by plan participants and changes in actuarial assumptions.

Members may request information on the compensation to the individuals included in the preceding table during 2016.

Effective April 29, 2015, the Farm Credit Administration Board adopted a final rule changing the determination of employees that could be considered highly compensated employees. While not final as of December 31, 2014, employees disclosed for 2014 in the above chart were determined based on the final rule.

Pension Benefits Attributable to the CEO, Senior Officers and Highly Compensated Individuals

(dollars in thousands) 2016 Name	Plan	Years of Credited Service	Present Value of Accumulated Benefits	Payments Made During the Reporting Period
Gregory W. Cole, CEO	AgriBank District Retirement Plan	**33.6**	**$ 2,081**	**$ --**
	AgriBank District Pension Restoration Plan	**33.6**	**168**	**--**
Aggregate Number of Senior Officers/Highly Compensated Individuals, excluding CEO				
Three	AgriBank District Retirement Plan	**25.1**	**$ 1,971**	**$ --**

The change in composition of the aggregate senior officer and highly compensated individuals can have a significant impact on the calculation of the accumulated pension benefits.

Effective January 1, 2007, the AgriBank District Retirement Plan was closed to new employees. Therefore, any employee starting employment with the AgriBank District after that date is not eligible to be in the plan.

The AgriBank District Pension Restoration Plan restores retirement benefits to certain highly compensated employees that would have been provided under the qualified plan if such benefits were not above certain Internal Revenue Code limits. Not all senior officers or highly compensated employees are eligible to participate in this plan.

Transactions with Senior Officers and Directors

Information regarding related party transactions is discussed in Note 10 to the accompanying Consolidated Financial Statements.

Travel, Subsistence and Other Related Expenses

Directors and senior officers are reimbursed for reasonable travel, subsistence and other related expenses associated with business functions. A copy of our policy for reimbursing these costs is available by contacting us at:

119 East Third Street, Suite 200
Little Rock, AR 72201
(800) 299-2290
www.agheritagefcs.com

The total directors' travel, subsistence and other related expenses were $99 thousand, $98 thousand and $90 thousand in 2016, 2015 and 2014, respectively.

Involvement in Certain Legal Proceedings

No events occurred during the past five years that are material to evaluating the ability or integrity of any person who served as a director or senior officer on January 1, 2017, or at any time during 2016.

Member Privacy

The FCA Regulations protect members' nonpublic personal financial information. Our directors and employees are restricted from disclosing information about our association or our members not normally contained in published reports or press releases.

Relationship with Qualified Public Accountant

There were no changes in independent auditors since the last Annual Report to members and we are in agreement with the opinion expressed by the independent auditors. The total fees paid during 2016 were $27 thousand. The fees paid were for audit services.

Financial Statements

The "Report of Management", "Report on Internal Control Over Financial Reporting", "Report of Audit Committee", "Report of Independent Auditors", "Consolidated Financial Statements" and "Notes to Consolidated Financial Statements" are presented prior to this portion of the accompanying Consolidated Financial Statements.

Young, Beginning and Small Farmers and Ranchers

Information regarding credit and services to young, beginning and small farmers and ranchers and producers or harvesters of aquatic products is discussed in an addendum to this Annual Report.

YOUNG, BEGINNING AND SMALL FARMERS AND RANCHERS

AgHeritage Farm Credit Services, ACA

(Unaudited)

We have specific programs in place to serve the credit and related needs of young, beginning and small farmers and ranchers (YBS) in our territory. The definitions of YBS as developed by the Farm Credit Administration (FCA) follow:

- Young: A farmer, rancher, or producer or harvester of aquatic products who is age 35 or younger as of the loan transaction date.
- Beginning: A farmer, rancher, or producer or harvester of aquatic products who has 10 years or less farming or ranching experience as of the loan transaction date.
- Small: A farmer, rancher, or producer or harvester of aquatic products who normally generates less than $250 thousand in annual gross sales of agricultural or aquatic products.

Demographics

We have compared counts of our YBS borrowers against the 2012 Ag Census data. The census reports at a county level the age, years on farm and gross receipts. Some of the census categories are not perfect comparisons for our YBS reporting methodology. The Census' Small comparison is most similar as the census counts the population of farms with sales less than $250 thousand. The Young category is the next best comparison by reporting operations with primary operator less than 35 years of age while YBS parameters include those 35 years of age or less. Finally, the Beginning category is least similar. The census does not quantify years of experience, but it does report Principal Operator with Years on Present Farm into a category of Less than 10 Years. While not an exact comparison for YBS Beginning category, it is used as the best comparison available. Finally, the two disparate populations pose another analysis challenge. The census measures the total population regardless of borrowing characteristics; while we operate within a sub-group of the census based on farmers who both finance their operation and who finance with AgHeritage Farm Credit Services, ACA.

The following chart compares our 2016 YBS customers to the 2012 Ag Census:

Total Farms	Census < 10 yrs	AgHeritage Beginning	% of Census Category
12,882	2,592	1,889	72.9%
	Census <35 Yrs Old	AgHeritage Young	--
	834	979	117.4%
	Census Sales <$250k	AgHeritage Small	--
	10,949	1,818	16.6%

The 2012 Ag Census trend shows a decline from the 2007 Ag Census in the number of Young, Beginning and Small farms in the AgHeritage LSA. The 1997-2012 trend showed small annual increases over the previous Ag Census for Small Farms in 2002 and 2007 (7% and 3%) but a 13% decline in 2012. Beginning had increases over the previous Ag Census in 2002 and 2007 (7% and 8%) but a large decline (75%) in 2012. For Small farms, there were also increases from the prior Ag Census in 2002 and 2007 (7% and 3%) with a drop in the 2012 Ag Census (13%).

The AgHeritage trend in Young borrowers for 2003 – 2016 was steady annual increases of 1- 20% through 2012. Starting in 2013 the number of Young borrowers began to decrease between 4-9% per year with an 8% decrease in 2016. Beginning borrowers also increased in most years from 2003 – 2014 with increases ranging from 1-19% annually. In 2015 and 2016 Beginning borrowers decreased 5% and 7% respectively. Small borrowers have been more volatile ranging from slight decreases (≤ 3%) in most early years except for a 13% decrease in 2006 but followed by a 15% increase in 2009. The most recent 2013-2016 have seen decreases ranging from 1% to 10%.

Mission Statement

Management and the Board of Directors feel that it is strategically important to support and develop YBS programs. Our YBS Farmer Program mission is to develop and implement programs to attract Young, Beginning and Small and next generation farmers and to strive to reach numeric goals for YBS customers.

Quantitative Goals

	2017		2018		2019		2020		2021	
	# Loans	in 000's	# Loans	in 000's	# Loans	in 000's	# Loans	in 000's	# Loans	in 000's
Young	1,000	$ 205,000	1,020	$ 210,000	1,040	$ 210,000	1,060	$ 220,000	1,080	$ 225,000
Beginning	2,000	$ 440,000	2,050	$ 450,000	2,100	$ 495,000	2,150	$ 470,000	2,200	$ 480,000
Small	1,825	$ 165,000	1,775	$ 175,000	1,750	$ 195,000	1,725	$ 195,000	1,700	$ 205,000

Qualitative Goals

The following related services were offered to YBS farmers during 2016:

- Crop insurance, both hail and multi-peril,
- Life insurance,
- Fee real estate appraisal services and
- Equipment and facility leasing.

We made use of federal loan guarantee programs in providing loans and leases to YBS farmers. We maintain a Preferred Lender Program designation with Farm Service Agency.

Outreach Programs

We encourage the use of Young and Beginning farmer programs like those offered by the Farm Service Agency and the Cooperative Extension Service.

We continue to sponsor an annual scholarship program for college bound or current college students with one winner from each branch office.

We sponsor the Arkansas Farm Bureau Young Farm Family program. This annual program recognizes and rewards Young Farm Families who take an active role in agriculture at the state and local levels. This program also provides educational opportunities for the Young Farm Family participants.

We continue to sponsor and participate in the annual Arkansas State University Ag Business Conference and the University of Arkansas – Division of Agriculture's Women in Ag conference.

We support the Arkansas Farm Family of the Year program. We have enjoyed having members each year who are honored at the local and state level by the Farm Family of the Year program. Implicit in the Farm Family of the Year is the next generation of farming. The honored families are typically multi-generational and include members who frequently fit within our YBS and Next Generation Farmer parameters.

In 2016 AgHeritage began co-hosting a biennial Arkansas State Young Beginning Farmer Conference. This is a joint effort among all Arkansas Farm Credit associations. The conference was designed to provide attendees the opportunity to network with their peers and experienced professionals in finance, credit and economics. State and national expert speakers covered topics that impact young producers including the current economic outlook, strategic business planning and financial and risk management.

We sponsor and/or participate in a variety of other Young, Beginning and Small outreach activities including:

- AgHeritage and other Arkansas Farm Credit Associations sponsor, support and participate in various Arkansas Grown activities which is an initiative of the Arkansas Department of Agriculture
  - Garden Program contest for Arkansas school gardens
  - Local Conversations brings together stakeholders to improve the quality of food reaching consumers
  - Arkansas Grown Magazine
  - Farmers Market Promotion Program
  - Farm2Home
- ASU Student Leadership Conference
- Cooperative Extension Farm Safety Day
- Arkansas Women in Agriculture– sponsorship and attendance of conference and Annie's Project
- AgHeritage continued its Youth Loan Program for FFA and 4-H members to borrow funds for their crop or livestock projects
- University Agriculture Department Scholarship Fundraisers – UA & ASU
- National Black Growers Council – speaker at National Black Growers Council Annual Meeting and sponsorship/participation at the local National Black Growers Council Model Field Day
- Arkansas Farm Family of the Year Program
- Yearly contributions to FFA and 4-H
- FFA/4-H AgHeritage Dealer Financing Program Donations
- AgHeritage Next Generation Farmer Program
- AgHeritage Farm Credit Services Customer Scholarship Program / University Scholarship
- Junior Livestock Auction: State Fair Belt Buckle Sponsorship and Sale of Champions Sponsorship; Local Fair Livestock Sponsorships

- County Extension Meeting Sponsorships: Crop Production, Marketing, Beef, etc.
- Exhibit/Sponsorships/Attendance:
    - Arkansas Foundation for Agriculture
    - Agricultural Council of Arkansas
    - Midsouth Gin Show
    - Arkansas Cattlemen's Conference; Local Conference
    - Arkansas Agricultural Aviation Association
    - Poultry Festival
    - USA Rice Outlook Conference
    - Crowley's Ridge Classic Show-Scholarship Awards
    - Crossett Rodeo Arena Sponsorship
    - Black Rock Technical College Foundation Scholarship Golf Tournament
    - Arkansas Soybean Association Annual Meeting
    - Arkansas Rice Council/Producers Annual Meeting
    - Mid-South Chapter of the American Society of Farm Managers and Rural Appraisers
    - Various local county fair associations: Belt Buckle Award sponsor
    - Various rural community sports league sponsorships

Safety and Soundness of the Program

We will limit the amount of risk classified loans that meet the Next Generation Farmer and/or YBS qualifications. The amount of volume for either will not exceed 25% of the Association's risk funds. This limit is cumulative and not to be exceeded at any point.

The credit quality guidelines and quarterly monitoring ensure that credit offered to the YBS and Next Generation Farmer groups is provided in a safe and sound manner within our risk-bearing capacity.

FUNDS HELD PROGRAM

AgHeritage Farm Credit Services, ACA

(Unaudited)

AgHeritage Farm Credit Services, ACA (the Association), offers a Funds Held Program ("Funds Held") that provides for customers to make advance payments on designated real estate and intermediate-term loans. The following terms and conditions apply to all Funds Held unless the loan agreement, or related documents, between the Association and customer provide for other limitations.

Payment Application: Loan payments received by the Association before the loan has been billed will be placed into Funds Held upon request and applied against the next installment due. Loan payments received after the loan has been billed will be directly applied to the installment due on the loan and related charges, if any. Any Funds Held deposit greater than 10% of the original commitment amount is considered to be a prepayment of the loan.

When a loan installment becomes due, amounts in Funds Held for the loan will be automatically applied toward the installment on the due date. Any accrued interest on Funds Held will be applied first. If the balance in Funds Held does not fully satisfy the entire installment, the customer must pay the difference by the installment due date.

Account Maximum: The amount in Funds Held may not exceed 50% of the unpaid principal balance of the customer's eligible loans or 50% of each eligible loan. However, the amount in Funds Held may not exceed 10% of the term loan's original commitment if the loan contains a prepayment penalty.

Interest Rate: Interest will accrue on Funds Held at a simple rate of interest that may be changed by the Association from time to time based upon the current interest rate environment. The interest rate may never exceed the interest rate charged on the related loan. Interest rates are currently reported on each customer's loan statement.

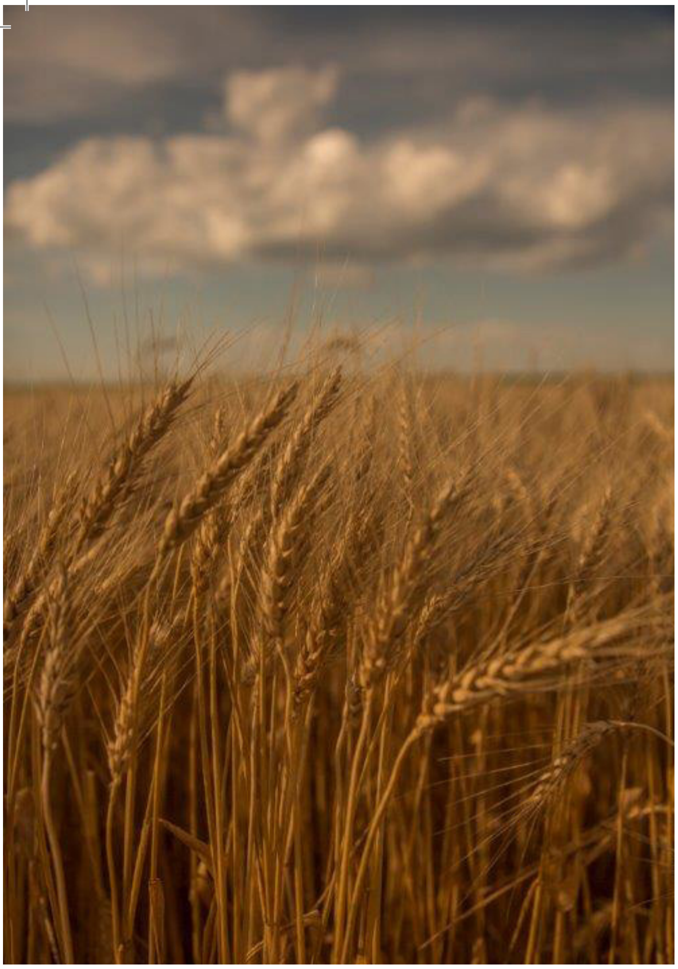
Withdrawals: Amounts in Funds Held may be withdrawn under the following conditions, depending on the customer's loan program:

- Customers can withdraw funds up to three times per month upon the approval of the loan officer after receipt of a written customer request. Withdrawals must be for an eligible purpose under the Funds Held program.
- Customers required to assign income to their loan, such as poultry and dairy assignments, may withdraw amounts in excess of their next installment.

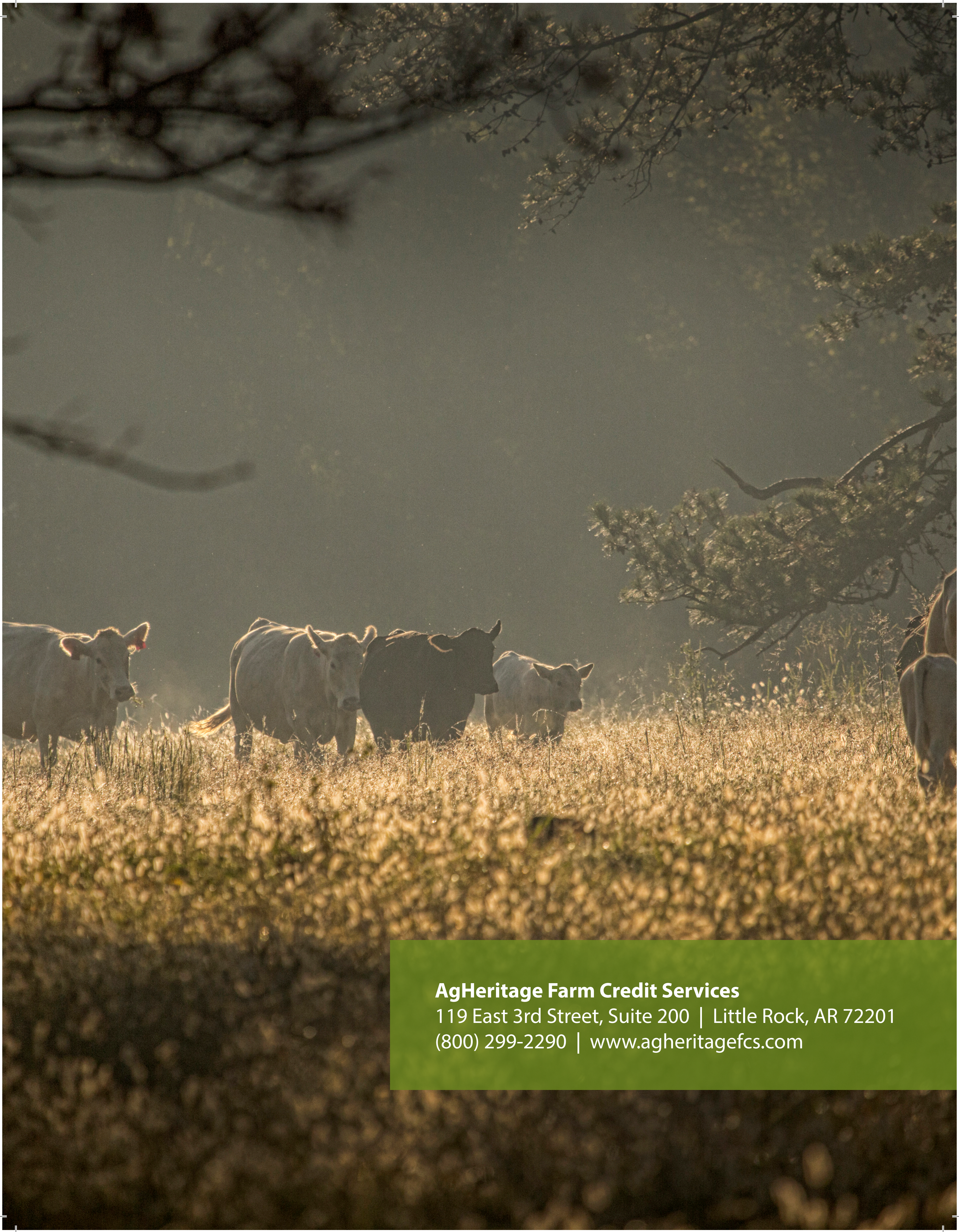
Association Options: In the event of default on any loan, or if Funds Held exceeds the maximum limit as established above, or if the Association discontinues the Funds Held program, the Association may apply funds in the account to the unpaid loan balance and other amounts due and shall return any excess funds to the customer.

Uninsured Account: Funds Held is not a depository account and is not insured. In the event of Association liquidation, customers having balances in Funds Held shall be notified according to FCA Regulations.

Questions: Please direct any questions regarding Funds Held to AgHeritage Farm Credit Services, ACA.




Trusted Lender for Over 100 Years



AgHeritage Farm Credit Services
119 East 3rd Street, Suite 200 | Little Rock, AR 72201
(800) 299-2290 | www.agheritagefcs.com