

AG 
TEXAS
FARM CREDIT SERVICES
Quarterly Report

**The Second Quarter Ended
June 30, 2021**



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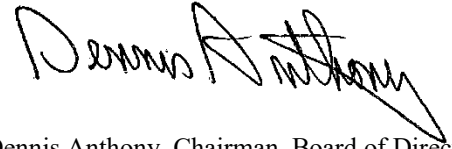
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The consolidated financial statements of *AgTexas Farm Credit Services* (“**Association**”) are prepared by management, who is responsible for the statements’ integrity and objectivity, including amounts that must necessarily be based on judgments and estimates. The consolidated financial statements have been prepared in conformity with accounting principles generally accepted in the United States of America appropriate in the circumstances. Other financial information included in the quarterly report is consistent with that in the consolidated financial statements and there are no significant changes in the association’s internal controls or in other factors that could significantly affects such controls during the quarter.

The undersigned certify that this quarterly report has been reviewed and prepared in accordance with all applicable statutory or regulatory requirements, and that the information contained herein is true, accurate and complete to the best of his knowledge and belief.



Tim McDonald, Chief Executive Officer
August 3, 2021



Dennis Anthony, Chairman, Board of Directors
August 3, 2021



Jeff Fairchild, Chief Financial Officer
August 3, 2021

Management’s Discussion & Analysis

The second quarter consolidated financial statements of AgTexas Farm Credit Services, including its wholly-owned subsidiaries AgTexas, PCA and AgTexas, FLCA (collectively referred to herein as the “**Association**”), is unaudited, but contains all adjustments necessary for a fair presentation of the interim financial condition and results of operations. The statements are prepared in conformity with generally accepted accounting principles and prevailing practices within the banking industry. In preparing these consolidated statements and meeting its responsibility for reliable financial information, management depends upon the Association’s accounting and internal control systems which have been designed to provide reasonable assurance that assets are safeguarded and transactions are properly authorized and recorded.

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

The following commentary explains management’s assessment of the principal aspects of the consolidated financial condition and results of operations of the Association for the three and six months ended June 30, 2021, and should be read in conjunction with the accompanying *consolidated financial statements* (“**CFS**”) and the *Association’s 2020 Annual Report to Stockholders* (“**2020 Annual Report**”). Management prepared the accompanying CFS under the oversight of the Association’s Audit Committee.

Significant Events.

The Association distributed patronage of approximately \$16.5 million in cash and an additional \$3.2 million in allocated equities in the first quarter of 2021. This represented the 2020 patronage declared by the Association.

Loan Portfolio.

Total loans outstanding at June 30, 2021, including nonaccrual loans, were \$2,352,909,751 compared to \$2,183,827,278 at December 31, 2020, reflecting an increase of 7.7 percent. Nonaccrual loans as a percentage of total loans outstanding were 0.2 percent at June 30, 2021, compared to 0.4 percent at December 31, 2020.

The Association recorded \$511,590 in recoveries and \$1,554 in charge-offs for the six months ended June 30, 2021, and \$958,559 in recoveries and \$625,125 in charge-offs for the same period in 2020. The Association’s allowance for credit losses, which consists of the allowance for loan losses and the reserve for unfunded credit commitments, was 0.34 percent and 0.37 percent of total loans outstanding as of June 30, 2021, and December 31, 2020, respectively.

The financial performance of the Association may be significantly impacted by the quality of loans within the loan portfolio. Internal policies and procedures, as well as third party credit reviews and examinations help to ensure asset quality is properly reflected. Additional detail on credit quality is illustrated in the following table.

	June 30, 2021	June 30, 2020	December 31, 2020
Acceptable	96.0%	93.9%	95.8%
OAEM	1.7%	3.1%	1.7%
Substandard/doubtful	2.3%	3.0%	2.5%
	100.0%	100.0%	100.0%

Management's Discussion & Analysis

Changes in the Association's loan portfolio from December 31, 2020 to June 30, 2021 follow:

Loan Type	June 30, 2021		December 31, 2020	
	Amount	%	Amount	%
Real estate mortgage	\$ 1,301,851,519	55.4%	\$ 1,173,139,059	53.7%
Production and intermediate term	743,785,711	31.6%	716,316,540	32.8%
Agribusiness:				
Loans to cooperatives	10,982,552	0.5%	8,629,186	0.4%
Processing and marketing	153,505,263	6.5%	143,266,511	6.5%
Farm-related business	30,826,176	1.3%	31,430,517	1.4%
Communication	20,833,597	0.9%	20,959,252	1.0%
Energy	5,993,044	0.3%	7,729,018	0.4%
Water and waste water	3,299,902	0.1%	4,167,976	0.2%
Rural residential real estate	8,066,259	0.3%	8,495,248	0.4%
International	11,288,657	0.5%	-	0.0%
Lease receivables	7,841,060	0.3%	4,993,460	0.2%
Mission-related investments	54,636,011	2.3%	64,700,511	3.0%
Total	<u>\$ 2,352,909,751</u>	<u>100.0%</u>	<u>\$ 2,183,827,278</u>	<u>100.0%</u>

The Association's portfolio includes significant mission-related investments authorized under the FCA approved *Rural America Bond Pilot Program* ("RAB"). The RAB program was designed to meet the growing and changing needs of agricultural enterprises, agribusinesses, and various infrastructure needs in rural communities through investment in these areas. The RAB pilot program ended as of December 31, 2014. FCA approved new investment regulations that became effective January 1, 2019. Effective February 25, 2019, the Association began purchasing USDA 100% unconditional guaranteed loans that are considered mission-related investments included in the above table.

Effective January 1, 2019, new FCA investment regulations provided authorization for the Association to invest in *Small Business Administration* ("SBA") pool securities. As a part of the conditions of the authorization, the investments are required to be 100% unconditionally guaranteed by the federal government or its agencies. For more information see Note 2 in the "Notes to Unaudited Consolidated Financial Statements".

Risk Exposure. High-risk assets include impaired loans and other property owned. Impaired loans are comprised of nonaccrual, past due ≥ 90 days and still accruing interest, and formally restructured loans. The following table illustrates the Association's components and trends of high-risk assets:

	June 30, 2021		December 31, 2020	
	Amount	%	Amount	%
Nonaccrual	\$ 5,181,846	40.2%	\$ 9,397,940	43.4%
90 days past due and still accruing interest	1,451,616	11.2%	461,912	2.1%
Formally restructured	6,273,072	48.6%	11,795,429	54.5%
Other property owned, net	-	0.0%	-	0.0%
Total	<u>\$ 12,906,534</u>	<u>100.0%</u>	<u>\$ 21,655,281</u>	<u>100.0%</u>

Management's Discussion & Analysis

Results of Operations. Changes in the Association's results of operations for the three and six months ended June 30, 2021 and June 30, 2020 follow:

	For the three months ended		For the six months ended	
	June 30, 2021	June 30, 2020	June 30, 2021	June 30, 2020
Interest income	\$ 22,344,644	\$ 21,277,380	\$ 43,232,033	\$ 44,973,497
Interest expense	(8,094,676)	(9,604,288)	(16,056,488)	(21,777,036)
(Provision for) reversal of loan losses	(29,647)	(556,830)	573,020	(422,257)
Net interest margin	14,220,321	11,116,262	27,748,565	22,774,204
Noninterest income	6,509,191	5,097,474	13,100,366	10,330,613
Noninterest expense	(8,741,610)	(7,140,705)	(17,581,953)	(15,388,639)
Net income	\$ 11,987,902	\$ 9,073,031	\$ 23,266,978	\$ 17,716,178

Net interest margin (interest income less interest expense) is the principal source of earnings and results from relative volumes of interest-earning assets and interest-bearing liabilities, yields on interest-earning assets, and rates on interest-bearing liabilities. The increase in interest income is primarily due to the growth in volume within the quarter but offset slightly year to date by lower interest rates. The changes in "(Provision for) reversal of loan losses" are due to changes in recoveries and charge-offs, as well as, a reduction in stresses. Noninterest income increases are due to increases in patronage income and higher than budgeted fee income. Noninterest expense increase is due to increase in salaries and FCS Insurance Premiums.

The effects of changes in average volumes, yields, and rates on interest margin follow:

	For the six months ended		For the six months ended	
	June 30, 2021		June 30, 2020	
	Average Balance	Interest	Average Balance	Interest
Total loans and investments	2,294,222,923	43,232,033	2,075,288,379	44,973,497
Interest-bearing liabilities	2,050,521,540	16,056,488	1,856,658,257	21,777,036
Impact of capital	\$ 243,701,383		\$ 218,630,122	
Net interest income		\$ 27,175,545		\$ 23,196,461

	2021	2020
	Average Yield	Average Yield
Yield on loans and investments	3.80%	4.35%
Cost of interest-bearing	1.58%	2.35%
Interest rate spread	2.22%	1.99%
Interest rate margin	2.39%	2.24%

	Six months ended June 30:		
	2021 vs. 2020		
	Increase (decrease) due to		
	Volume	Rate	Total
Interest income	\$ 4,722,688	\$ (6,464,152)	\$ (1,741,464)
Interest expense	2,259,171	(7,979,719)	(5,720,548)
Net interest income	\$ 2,463,517	\$ 1,515,567	\$ 3,979,084

Management's Discussion & Analysis

The Association's return on average assets was 1.99% and 1.66% for the quarters ended June 30, 2021 and 2020, respectively, and 1.97% and 1.64% for the six months ended June 30, 2021 and 2020, respectively. The increase in return on average assets for the three and six months ended June 30, 2021 is due to increased net income, which is explained above. The Association's return on average equity was 15.29% and 12.66% for the quarters ended June 30, 2021 and 2020, respectively, and 15.22% and 12.54% for the six months ended June 30, 2021 and 2020, respectively. The changes in return on average equity for the period mirrors the return on average assets above.

Liquidity and Funding Sources. *Interest rate risk* ("IRR") inherent in the loan portfolio is substantially mitigated through the funding relationship with the FCBT. FCBT manages IRR through direct loan pricing and asset/liability management. The Association's primary source of liquidity and funding is a direct note payable to FCBT. The following schedule summarizes the Association's borrowings:

	June 30, 2021	December 31, 2020
Note payable to the Bank	\$ 2,183,519,822	\$ 2,010,366,007
Accrued interest on note payable	2,724,426	2,790,897
Total	<u>\$ 2,186,244,248</u>	<u>\$ 2,013,156,904</u>

The Association operates under a *general financing agreement* ("GFA") with the bank. The current GFA is effective through September 30, 2023. The primary source of liquidity and funding for the Association is a direct loan from the bank. The outstanding balance of \$2,183,519,822 as of June 30, 2021, is recorded as a liability on the Association's balance sheet. The note carried a weighted average interest rate of 1.53 percent at June 30, 2021. The indebtedness is collateralized by a pledge of substantially all of the Association's assets to the bank and is governed by the GFA. The increase in note payable to the bank since December 31, 2020, is due to the Association's increase in loan volume. The Association's own funds, which represent the amount of the Association's loan portfolio funded by the Association's equity, were \$242,340,404 at June 30, 2021. The maximum amount the Association may borrow from the bank as of June 30, 2021, was \$2,424,095,405 as defined by the GFA. The indebtedness continues in effect until the expiration date of the GFA, unless sooner terminated by the bank upon the occurrence of an event of default, or by the Association, in the event of a breach of this agreement by the bank, upon giving the bank 30 calendar days' prior written notice, or in all other circumstances, upon giving the bank 120 days' prior written notice.

Capital Resources. The Association's members' equity was \$321,240,438 and \$298,034,229 at June 30, 2021 and December 31, 2020, respectively, a \$23,206,209 increase, which approximates current earnings. The Association's debt as a percentage of members' equity was 6.89:1 as of June 30, 2021, compared to 6.93:1 as of December 31, 2020. FCA regulations require associations to maintain minimums for various regulatory capital ratios. New regulations became effective January 1, 2017, which replaced the previously required core surplus and total surplus ratios with common equity tier 1, tier 1 capital and total capital risk-based capital ratios. The new regulations also added tier 1 leverage and *unallocated retained earnings and equivalents* ("UREE") ratios. The permanent capital ratio continues to remain in effect, with some modifications to align with the new regulations. See note 4 in the "Notes to Unaudited Consolidated Financial Statements". As of June 30, 2021, the Association exceeded all regulatory capital requirements.

Significant Recent Accounting Pronouncements. See Note 1 in CFS.

Relationship With FCBT. The Association has a statutory obligation to borrow only from FCBT, which is discussed in note 9, *Note Payable to FCBT*, in the Association's consolidated financial statements in the 2020 Annual Report.

FCBT's ability to access Association capital is discussed in note 2, *Summary of Significant Accounting Policies*, in the Association's consolidated financial statements in the 2020 Annual Report, within the *Farm Credit Bank of Texas Capital Stock* section.

FCBT's role to help mitigate Association exposure to IRR is described in the *Liquidity and Funding Sources* section of *Management's Discussion and Analysis of Financial Condition and Results of Operations* and note 9, *Note Payable to FCBT*, in the Association's consolidated financial statements in the 2020 Annual Report.

FCBT provides computer systems to support the critical operations of all *10th Farm Credit District* ("District") associations. In addition, each association has operating systems and facility-based systems that are not supported by FCBT. As disclosed in note 13, *Related Party Transactions*, in the Association's consolidated financial statements in the 2020 Annual Report, FCBT provides many services to the Association, which include administrative, marketing, accounting services and information systems.

Management's Discussion & Analysis

The Association's financial condition may be impacted by factors that affect FCBT. The financial condition and results of operations of FCBT may materially affect Association stockholders' investment in the Association.

Annual and Quarterly Stockholder Report Availability. FCBT's annual and quarterly stockholder reports are available free of charge, upon request. These reports can be obtained by writing to Farm Credit Bank of Texas, Corporate Communications, P.O. Box 202590, Austin, Texas 78720, or by calling (512) 483-9204. The annual and quarterly stockholder reports for FCBT are also available on its website at www.farmcreditbank.com.

Annual and quarterly stockholder reports for the Association are available free of charge on the Association's website www.agtexas.com or by *i*) writing to AgTexas Farm Credit Services, 5004 N. Loop 289, Lubbock, Texas 79416, *ii*) calling (806) 687-4068, or *iii*) e-mailing jeff.fairchild@agtexas.com.



Consolidated Balance Sheets

	June 30, 2021	December 31, 2020
	Unaudited	Audited
<u>Assets</u>		
Cash	\$ 3,727,779	\$ 8,594
Investments	88,328,567	80,838,236
Loans	2,352,909,751	2,183,827,278
Less: allowance for loan losses	6,522,520	6,504,599
Net loans	2,346,387,231	2,177,322,679
Accrued interest receivable	18,027,449	22,704,499
Investment in and receivable from the Farm Credit Bank of Texas:		
Capital stock	38,542,835	38,636,905
Other	11,185,007	18,008,816
Premises and equipment	25,473,028	24,903,330
Other assets	2,271,941	1,179,694
Total assets	\$ 2,533,943,837	\$ 2,363,602,753
<u>Liabilities</u>		
Note payable to the Farm Credit Bank of Texas	\$ 2,183,519,822	\$ 2,010,366,007
Advance conditional payments	10,820,443	17,754,206
Accrued interest payable	2,724,426	2,790,897
Accrued postretirement benefit liability	7,815,021	7,768,656
Patronage distributions payable	130	16,490,756
Other liabilities	7,823,557	10,398,002
Total liabilities	2,212,703,399	2,065,568,524
<u>Members' Equity</u>		
Capital stock and participation certificates	4,358,835	4,257,615
Preferred stock	20,000,000	20,000,000
Allocated retained earnings	22,229,695	22,230,993
Unallocated retained earnings	199,417,143	176,650,165
Additional paid-in capital	75,310,003	75,310,003
Accumulated other comprehensive income	(75,238)	(414,547)
Total members' equity	321,240,438	298,034,229
Total liabilities and members' equity	\$ 2,533,943,837	\$ 2,363,602,753

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



Unaudited Consolidated Statements of Comprehensive Income

	For the three months ended		For the six months ended	
	June 30, 2021	June 30, 2020	June 30, 2021	June 30, 2020
<u>Interest income</u>				
Loans	\$ 22,088,010	\$ 21,028,538	\$ 42,784,136	\$ 44,397,969
Investments	256,634	248,842	447,897	575,528
Total interest income	<u>22,344,644</u>	<u>21,277,380</u>	<u>43,232,033</u>	<u>44,973,497</u>
<u>Interest expense</u>				
Note payable to the Farm Credit Bank of Texas	8,093,778	9,600,308	16,054,584	21,760,233
Advance conditional payments	898	3,980	1,904	16,803
Total interest expense	<u>8,094,676</u>	<u>9,604,288</u>	<u>16,056,488</u>	<u>21,777,036</u>
Net interest income	<u>14,249,968</u>	<u>11,673,092</u>	<u>27,175,545</u>	<u>23,196,461</u>
Provision for (reversal of) loan losses	29,647	556,830	(573,020)	422,257
Net interest income after Provision for (reversal of) losses	<u>14,220,321</u>	<u>11,116,262</u>	<u>27,748,565</u>	<u>22,774,204</u>
<u>Noninterest income</u>				
Farm Credit Bank of Texas patronage income	5,183,136	4,048,568	10,177,668	7,965,206
Loan fees	190,614	236,517	527,268	424,937
Fees for financially related services	300,990	215,226	1,182,877	616,404
Other	834,451	597,163	1,212,553	1,324,066
Total noninterest income	<u>6,509,191</u>	<u>5,097,474</u>	<u>13,100,366</u>	<u>10,330,613</u>
<u>Noninterest expenses</u>				
Salaries and employee benefits	5,805,400	4,968,851	11,711,595	10,447,828
Directors' expense	62,291	56,482	129,475	154,500
Purchased services	333,912	366,024	1,003,197	952,909
Travel	340,480	212,674	581,247	503,220
Occupancy and equipment	406,671	386,333	866,302	871,763
Communication	85,805	98,420	179,127	181,034
Advertising	183,024	122,841	287,396	257,973
Public and member relations	275,575	113,842	469,628	389,512
Federally regulated examination fees	121,786	118,304	271,102	260,135
FCSIC insurance premiums	648,081	284,154	1,277,228	563,325
Other components of net periodic postretirement benefit cost	46,565	55,280	93,130	110,565
Other noninterest expense	432,020	357,500	712,526	695,875
Total noninterest expenses	<u>8,741,610</u>	<u>7,140,705</u>	<u>17,581,953</u>	<u>15,388,639</u>
Net income	<u>11,987,902</u>	<u>9,073,031</u>	<u>23,266,978</u>	<u>17,716,178</u>
Other comprehensive income (loss):				
Change in postretirement benefit plans	(7,020)	(8,658)	(14,040)	(17,316)
Change in fair value of available for sale investments	80,354	(121,343)	353,349	(52,469)
Total other comprehensive income (loss)	<u>73,334</u>	<u>(130,001)</u>	<u>339,309</u>	<u>(69,785)</u>
Comprehensive income	<u>\$ 12,061,236</u>	<u>\$ 8,943,030</u>	<u>\$ 23,606,287</u>	<u>\$ 17,646,393</u>

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



Unaudited Consolidated Statements of Changes in Members' Equity

	Capital Stock/ Participation Certificates	Preferred Stock	Retained Earnings		Additional Paid-In Capital	Accumulated Other Comprehensive Income (Loss)	Total Members' Equity
			Allocated	Unallocated			
Balance at December 31, 2019	\$ 4,160,515	\$20,000,000	\$ 21,422,837	\$ 155,179,391	\$ 75,310,003	\$ (502,425)	\$ 275,570,321
Comprehensive income	-	-	-	17,716,178	-	(69,785)	17,646,393
Capital stock/participation certificates issued	446,790	-	-	-	-	-	446,790
Capital stock/participation certificates retired	(422,295)	-	-	-	-	-	(422,295)
Preferred stock dividends: Paid	-	-	-	(500,000)	-	-	(500,000)
Patronage dividends: Paid or accrued	-	-	1	-	-	-	1
Balance at June 30, 2020	<u>\$ 4,185,010</u>	<u>\$20,000,000</u>	<u>\$ 21,422,838</u>	<u>\$ 172,395,569</u>	<u>\$ 75,310,003</u>	<u>\$ (572,210)</u>	<u>\$ 292,741,210</u>
Balance at December 31, 2020	\$ 4,257,615	\$20,000,000	\$ 22,230,993	\$ 176,650,165	\$ 75,310,003	\$ (414,547)	\$ 298,034,229
Comprehensive income	-	-	-	23,266,978	-	339,309	23,606,287
Capital stock/participation certificates issued	570,920	-	-	-	-	-	570,920
Capital stock/participation certificates retired	(469,700)	-	-	-	-	-	(469,700)
Preferred stock dividends: Paid	-	-	-	(500,000)	-	-	(500,000)
Patronage dividends: Paid or accrued	-	-	(1,298)	-	-	-	(1,298)
Balance at June 30, 2021	<u>\$ 4,358,835</u>	<u>\$20,000,000</u>	<u>\$ 22,229,695</u>	<u>\$ 199,417,143</u>	<u>\$ 75,310,003</u>	<u>\$ (75,238)</u>	<u>\$ 321,240,438</u>

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

Notes to Unaudited Consolidated Financial Statements

Note 1: Organization, Operations and Significant Accounting Policies

AgTexas Farm Credit Services and its wholly-owned subsidiaries, *AgTexas, PCA* (“PCA”) and *AgTexas, FLCA* (“FLCA”), are collectively referred to herein as the “Association.” The Association provides financing and related services through FLCA and PCA. FLCA makes secured long-term agricultural real estate and rural home mortgage loans. PCA makes short- and intermediate-term loans for agricultural production or operating purposes.

These notes and the encompassing consolidated financial statements for the Association (collectively referred to herein as “CFS”), include the accounts of PCA and FLCA. All significant intercompany balances and transactions are eliminated in consolidation. In management’s opinion, the CFS reflect all adjustments necessary to fairly state results for the interim periods presented, which are of a normal recurring nature.

The accompanying unaudited financial statements have been prepared in accordance with *accounting principles generally accepted in the U.S.* (“GAAP”) for interim financial information. Accordingly, they do not include all of the disclosures required by GAAP for annual financial statements and should be read in conjunction with the audited financial statements as of and for the year ended December 31, 2020, as contained in the 2020 Annual Report to Stockholders.

In the opinion of management, the CFS contain all adjustments necessary for a fair presentation of the interim financial condition and results of operations and conform with GAAP, except for the inclusion of a statement of cash flows. GAAP require a business enterprise that provides a set of financial statements reporting both financial position and results of operations to also provide a statement of cash flows for each period for which results of operations are provided. In regulations issued by *Farm Credit Administration* (“FCA”), Associations have the option to exclude statements of cash flows in interim financial statements. Therefore, the Association has elected not to include a statement of cash flows in these consolidated financial statements. These interim financial statements should be read in conjunction with the audited financial statements as of and for the year ended December 31, 2020 as contained in the 2020 Annual Report to Stockholders. The preparation of financial statements in accordance with GAAP requires management to make estimates and assumptions that affect the amounts reported in the financial statements and accompanying notes. Actual results could differ from those estimates. The results of operations for interim periods are not necessarily indicative of the results to be expected for the full year ending December 31, 2021. Descriptions of the significant accounting policies are included in the 2020 Annual Report to Stockholders. In the opinion of management, these policies and the presentation of the interim financial condition and results of operations conform with GAAP and prevailing practices within the banking industry.

Significant Recent Accounting Pronouncements. In January 2021, the Financial Accounting Standards Board (“FASB”) issued an update whereby certain derivative instruments may be modified to change the rate used for margining, discounting, or contract price alignment. An entity may elect to apply the new amendments on a full retrospective basis as of any date from the beginning of an interim period that includes or is subsequent to March 12, 2020, or on a prospective basis to new modifications from any date within an interim period that includes or is subsequent to the date of the update, up to the date that financial statements are available to be issued. These amendments do not apply to contract modifications made or new hedging relationships entered into after December 31, 2022, and existing hedging relationships evaluated for effectiveness in periods after December 31, 2022. The association adopted the guidance in the first quarter of 2021 and the impact was not material to the association’s financial condition or results of operations.

In March 2020, the FASB issued guidance entitled “Facilitation of the Effects of Reference Rate Reform on Financial Reporting.” The guidance provides optional expedients and exceptions for applying GAAP to contracts, hedging relationships and other transactions affected by reference rate reform. The guidance simplifies the accounting evaluation of contract modifications that replace a reference rate affected by reference rate reform and contemporaneous modifications of other contracts related to the replacement of the reference rate. With respect to hedge accounting, the guidance allows amendment of formal designation and documentation of hedging relationships in certain circumstances as a result of reference rate reform and provides additional expedients for different types of hedges, if certain criteria are met. The optional amendments are effective as of March 12, 2020, through December 31, 2022. The association applied the optional accounting expedients available under the guidance to derivative contract modifications related to the LIBOR transition in the fourth quarter of 2020. The impact of adoption was not material to the association’s financial condition or its results of operations. In addition, the association applied the optional expedients as it relates to loans in the first quarter of 2021. The impact of adoption was not material to the association’s financial condition or its results of operations.

Notes to Unaudited Consolidated Financial Statements

In June 2016, the FASB issued guidance entitled “Measurement of Credit Losses on Financial Instruments.” The guidance replaces the current incurred loss impairment methodology with a methodology that reflects expected credit losses and requires consideration of a broader range of reasonable and supportable information to inform credit loss estimates. Credit losses relating to available-for-sale securities would also be recorded through an allowance for credit losses. For public business entities that are not U.S. Securities and Exchange Commission filers this guidance was to become effective for interim and annual periods beginning after December 15, 2020, with early application permitted. In November 2019, the FASB issued an update that amends the mandatory effective date for this guidance for certain institutions. The change resulted from a change in the effective date philosophy that extends and simplifies the adoption by staggering the dates between large public entities and other entities. As a result of the change, the new credit loss standard, for those institutions qualifying for the delay, becomes effective for interim and annual reporting periods beginning after December 15, 2022, with early adoption permitted. The Association qualifies for the delay in the adoption date. The Association continues to evaluate the impact of adoption on the Association’s financial condition and its results of operations.

The consolidated financial statements comprise the operations of the ACA and its wholly-owned subsidiaries. The preparation of these consolidated financial statements requires the use of management’s estimates. The results for the quarter ended June 30, 2021, are not necessarily indicative of the results to be expected for the year ended December 31, 2021.

Note 2: Investment Securities

Held to Maturity (“HTM”)

Federal Agricultural Mortgage Corporation (“Farmer Mac”) guaranteed *agricultural mortgage-backed securities (“AMBS”)* comprise the Association’s investment portfolio, and the Association services the underlying loans. Additional information follows:

	AMBS				
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value	Weighted Average Yield
June 30, 2021	\$ 986,228	\$ 22,797	\$ -	\$ 1,009,025	4.90%
December 31, 2020	1,117,246	41,195	-	1,158,441	5.73%

The Association has not experienced impairments of these securities. Farmer Mac guarantees the underlying mortgages, and the Association has the ability and intent to hold these securities to maturity or pay-off and it is unlikely the Association would be required to sell these securities. These AMBS have contractual weighted average maturities of 3.04 years as of June 30, 2021, however, expected maturities differ from contractual maturities because borrowers may have the right to call or prepay obligations with or without call or prepayment penalties.

Notes to Unaudited Consolidated Financial Statements

Available for sale (“AFS”)

The Association’s AFS investment securities consists entirely of *Small Business Administration* (“SBA”) pool securities. A summary of the amortized cost and fair value of AFS investment securities is as follows:

	SBA pool securities				
	Amortized	Gross	Gross	Fair Value	Weighted
	Cost	Unrealized	Unrealized		Average
		Gains	Losses		Yield
June 30, 2021	\$86,662,462	\$ 679,877	\$ -	\$ 87,342,339	3.17%
December 31, 2020	79,394,462	326,528	-	79,720,990	3.21%

The following table is a summary of the contractual maturity, fair value, amortized cost and weighted average yield of AFS investments securities at **June 30, 2021**:

	SBA pool securities				
	Due in	Due After 1	Due After 5	Due	Total
	1 Year	Year Through	Years Through	After	
or Less	5 Years	10 Years	10 Years		
Fair value	\$ -	\$ -	\$ 32,101,709	\$ 55,240,630	\$ 87,342,339
Amortized cost	-	-	31,914,532	54,747,930	86,662,462
Weighted average yield	0.00%	0.00%	3.73%	2.84%	3.17%

Note 3: Loans and Allowance for Loan Losses (“ALL”)

Loans. Loan carrying amounts (outstanding principal adjusted as applicable for capitalized accrued interest, direct partial charge-offs, deferred fees or costs on originated loans, and unamortized purchase premiums and discounts; excludes uncapitalized accrued interest) by portfolio segment follows:

Loan Type	June 30, 2021		December 31, 2020	
	Amount	%	Amount	%
Real estate mortgage	\$ 1,301,851,519	55.4%	\$ 1,173,139,059	53.7%
Production and intermediate term	743,785,711	31.6%	716,316,540	32.8%
Agribusiness:				
Loans to cooperatives	10,982,552	0.5%	8,629,186	0.4%
Processing and marketing	153,505,263	6.5%	143,266,511	6.5%
Farm-related business	30,826,176	1.3%	31,430,517	1.4%
Communication	20,833,597	0.9%	20,959,252	1.0%
Energy	5,993,044	0.3%	7,729,018	0.4%
Water and waste water	3,299,902	0.1%	4,167,976	0.2%
Rural residential real estate	8,066,259	0.3%	8,495,248	0.4%
International	11,288,657	0.5%	-	0.0%
Lease receivables	7,841,060	0.3%	4,993,460	0.2%
Mission-related investments	54,636,011	2.3%	64,700,511	3.0%
Total	\$ 2,352,909,751	100.0%	\$ 2,183,827,278	100.0%

Notes to Unaudited Consolidated Financial Statements

Mission-related investment and real estate mortgage loans purchased with 100% U.S. government agency or government sponsored enterprise guarantees present essentially no credit risk other than purchase premiums, which are forfeited when borrowers prepay or refinance their loans before the premiums are fully amortized. Management anticipates and considers potential prepayments to estimate an appropriate amortization period. Net purchased premiums included in the mission-related investment and real estate mortgage loan balances above as of June 30, 2021 and December 31, 2020, follow:

	June 30, 2021	December 31, 2020
Real estate mortgage	\$ 3,826,509	\$ 4,595,659
Mission-related investments	909,443	1,259,670
Total premium	\$ 4,735,952	\$ 5,855,329

The Association may purchase or sell participations in loans to diversify risk, manage loan volume, and comply with FCA regulations. Participation carrying amount details as of June 30, 2021 follow:

	Other Farm Credit Institutions		Non-Farm Credit Institutions		Total	
	Participations Purchased	Participations Sold	Participations Purchased	Participations Sold	Participations Purchased	Participations Sold
	Real estate mortgage	\$ 107,172,088	\$ 332,220,756	\$ 204,107,551	\$ 2,363,725	\$ 311,279,639
Production and intermediate term	70,519,859	482,076,058	-	-	70,519,859	482,076,058
Agribusiness	110,968,411	38,578,630	-	-	110,968,411	38,578,630
Communication	20,833,597	-	-	-	20,833,597	-
Energy	5,993,044	-	-	-	5,993,044	-
Water and waste water	3,299,902	-	-	-	3,299,902	-
International	11,288,656	-	-	-	11,288,656	-
Lease receivables	7,841,060	-	-	-	7,841,060	-
Total	\$ 337,916,616	\$ 852,875,444	\$ 204,107,551	\$ 2,363,725	\$ 542,024,167	\$ 855,239,170

The Association is authorized under the Farm Credit Act to accept *advance conditional payments* (“ACPs”) from borrowers. To the extent the borrower’s access to such ACPs is restricted and the legal right of setoff exists, the ACPs are netted against the borrower’s related loan balance. Unrestricted advance conditional payments are included in other liabilities. ACPs are not insured, and interest is generally paid by the Association on such balances. Balances of ACPs were \$23,649,470 and \$45,851,481 at June 30, 2021 and December 31, 2020, respectively.

Notes to Unaudited Consolidated Financial Statements

Credit Quality. Loans are the Association’s primary asset. Collectability of these assets is critical to the Association’s financial position and results of operations. Collectability is primarily a function of credit quality.

Loans that have not performed in accordance with terms demonstrate heightened credit risk, and the level and trends in non-performing loans is a strong indicator of credit quality. Non-performing loans and *other property owned* (“**OPO**”) comprise non-performing assets.

The recorded investment in a loan, as defined by GAAP, includes the outstanding principal adjusted, as applicable, for accrued interest, direct partial charge-offs, deferred fees or costs on originated loans, and unamortized purchase premiums and discounts; the recorded investment in a loan does not include an allocation of the ALL or any specific valuation adjustments. The recorded investment in non-performing asset balances by loan portfolio segment and OPO follow:

	June 30, 2021	December 31, 2020
Nonaccrual loans:		
Real estate mortgage	\$ 4,130,029	\$ 6,483,899
Production and intermediate term	895,774	1,847,490
Rural residential real estate	156,043	166,145
Mission-related investments	-	900,406
Total nonaccrual loans	5,181,846	9,397,940
Accruing restructured loans:		
Real estate mortgage	6,170,711	11,022,057
Production and intermediate term	102,361	773,372
Total accruing restructured loans	6,273,072	11,795,429
Accruing loans 90 days or more past due:		
Real estate mortgage	875,740	461,912
Production and intermediate term	575,876	-
Total accruing loans 90 days or more past due	1,451,616	461,912
Total non-performing loans	12,906,534	21,655,281
Other property owned	-	-
Total non-performing assets	\$ 12,906,534	\$ 21,655,281

Notes to Unaudited Consolidated Financial Statements

Age analysis of the recorded investment (including accrued interest) in past due loans by loan segment follows:

June 30, 2021	30-89 Days Past Due	90 Days or More Past Due	Total Past Due	Not Past Due or less than 30 Days Past Due	Total Loans	Recorded Investment >90 days and Accruing
Real estate mortgage	\$ 7,286,111	\$ 4,558,406	\$ 11,844,517	\$ 1,301,009,278	\$ 1,312,853,795	\$ 875,740
Production and intermediate-term	1,025,195	575,881	1,601,076	747,583,231	749,184,307	575,876
Loans to cooperatives	-	-	-	10,991,219	10,991,219	-
Processing and marketing	1,184,929	-	1,184,929	152,757,894	153,942,823	-
Farm-related business	-	1	1	30,975,532	30,975,533	-
Communication	-	-	-	20,834,878	20,834,878	-
Energy	-	-	-	6,003,313	6,003,313	-
Water and waste water	-	-	-	3,300,462	3,300,462	-
Rural residential real estate	-	-	-	8,098,502	8,098,502	-
International	-	-	-	11,312,055	11,312,055	-
Lease receivables	17,070	-	17,070	7,855,158	7,872,228	-
Mission-related investments	-	-	-	55,123,377	55,123,377	-
Total	<u>\$ 9,513,305</u>	<u>\$ 5,134,288</u>	<u>\$ 14,647,593</u>	<u>\$ 2,355,844,899</u>	<u>\$ 2,370,492,492</u>	<u>\$ 1,451,616</u>
December 31, 2020	30-89 Days Past Due	90 Days or More Past Due	Total Past Due	Not Past Due or less than 30 Days Past Due	Total Loans	Recorded Investment >90 days and Accruing
Real estate mortgage	\$ 4,171,090	\$ 4,489,103	\$ 8,660,193	\$ 1,178,638,875	\$ 1,187,299,068	\$ 461,912
Production and intermediate-term	4,578,533	10	4,578,543	718,375,947	722,954,490	-
Loans to cooperatives	-	-	-	8,635,985	8,635,985	-
Processing and marketing	-	-	-	143,948,102	143,948,102	-
Farm-related business	-	-	-	31,497,365	31,497,365	-
Communication	-	-	-	20,960,364	20,960,364	-
Energy	-	-	-	7,742,965	7,742,965	-
Water and waste water	-	-	-	4,168,225	4,168,225	-
Rural residential real estate	166,145	-	166,145	8,367,733	8,533,878	-
Lease receivables	-	-	-	5,005,207	5,005,207	-
Mission-related investments	1,889,359	900,406	2,789,765	62,568,542	65,358,307	-
Total	<u>\$ 10,805,127</u>	<u>\$ 5,389,519</u>	<u>\$ 16,194,646</u>	<u>\$ 2,189,909,310</u>	<u>\$ 2,206,103,956</u>	<u>\$ 461,912</u>

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

Management has rated each loan in the portfolio using the System's 14-point rating system. These aggregated classifications are a significant indicator of credit quality. The classification categories are defined as follows:

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

Notes to Unaudited Consolidated Financial Statements

The following table presents the Association's loan portfolio segment balances, including accrued interest thereon, as a percentage of the total category, as classified by management and aggregated under the FCA's Uniform Loan Classification System:

	June 30, 2021	December 31, 2020
Real estate mortgage		
Acceptable	97.0%	96.1%
OAEM	0.6%	1.0%
Substandard/doubtful	2.4%	2.9%
	<u>100.0%</u>	<u>100.0%</u>
Production and intermediate term		
Acceptable	95.1%	95.9%
OAEM	2.1%	1.1%
Substandard/doubtful	2.8%	3.0%
	<u>100.0%</u>	<u>100.0%</u>
Loans to cooperatives		
Acceptable	100.0%	100.0%
OAEM	0.0%	0.0%
Substandard/doubtful	0.0%	0.0%
	<u>100.0%</u>	<u>100.0%</u>
Processing and marketing		
Acceptable	88.5%	88.6%
OAEM	10.4%	11.4%
Substandard/doubtful	1.2%	0.0%
	<u>100.0%</u>	<u>100.0%</u>
Farm-related business		
Acceptable	100.0%	100.0%
OAEM	0.0%	0.0%
Substandard/doubtful	0.0%	0.0%
	<u>100.0%</u>	<u>100.0%</u>
Communication		
Acceptable	100.0%	100.0%
OAEM	0.0%	0.0%
Substandard/doubtful	0.0%	0.0%
	<u>100.0%</u>	<u>100.0%</u>
Energy		
Acceptable	100.0%	100.0%
OAEM	0.0%	0.0%
Substandard/doubtful	0.0%	0.0%
	<u>100.0%</u>	<u>100.0%</u>
Water and waste water		
Acceptable	100.0%	100.0%
OAEM	0.0%	0.0%
Substandard/doubtful	0.0%	0.0%
	<u>100.0%</u>	<u>100.0%</u>
Rural residential real estate		
Acceptable	98.1%	98.1%
OAEM	0.0%	0.0%
Substandard/doubtful	1.9%	1.9%
	<u>100.0%</u>	<u>100.0%</u>
International		
Acceptable	100.0%	0.0%
OAEM	0.0%	0.0%
Substandard/doubtful	0.0%	0.0%
	<u>100.0%</u>	<u>0.0%</u>
Lease receivables		
Acceptable	100.0%	100.0%
OAEM	0.0%	0.0%
Substandard/doubtful	0.0%	0.0%
	<u>100.0%</u>	<u>100.0%</u>
Mission-related investments		
Acceptable	100.0%	98.6%
OAEM	0.0%	0.0%
Substandard/doubtful	0.0%	1.4%
	<u>100.0%</u>	<u>100.0%</u>
Total Loans		
Acceptable	96.0%	95.8%
OAEM	1.7%	1.7%
Substandard/doubtful	2.3%	2.5%
	<u>100.0%</u>	<u>100.0%</u>

Notes to Unaudited Consolidated Financial Statements

Based on current information and events, management has determined it is probable that scheduled payments of principal or interest on the following loans may not be collected when due according to the contractual terms of the loan agreements and has classified these loans as impaired. Once classified as impaired, management then determines the amount of impairment, if any, on each individual impaired loan; aggregated impairment on individual impaired loans is included in management's estimate of an appropriate ALL at each reporting date.

Impaired loan information, by loan portfolio segment, follows:

	June 30, 2021			December 31, 2020		
	Recorded Investment	Unpaid Principal Balance ^a	Related Allowance	Recorded Investment	Unpaid Principal Balance ^a	Related Allowance
Impaired loans with a related allowance for credit losses:						
Real estate mortgage	\$ 947,276	\$ 1,195,567	\$ 92,000	\$ 999,152	\$ 1,247,443	\$ 92,000
Production and intermediate term	-	-	-	-	-	-
Farm-related business	-	-	-	-	-	-
Rural residential real estate	-	-	-	-	-	-
Mission-related investments	-	-	-	-	-	-
Total	<u>\$ 947,276</u>	<u>\$ 1,195,567</u>	<u>\$ 92,000</u>	<u>\$ 999,152</u>	<u>\$ 1,247,443</u>	<u>\$ 92,000</u>
Impaired loans with no related allowance for credit losses:						
Real estate mortgage	\$ 10,229,204	\$ 10,884,692	\$ -	\$ 16,968,716	\$ 18,432,824	\$ -
Production and intermediate term	1,574,011	5,481,242	-	2,620,862	8,026,594	-
Farm-related business	1	1,555	-	-	-	-
Rural residential real estate	156,043	156,042	-	166,145	166,145	-
Mission-related investments	-	-	-	900,406	900,406	-
Total	<u>\$ 11,959,259</u>	<u>\$ 16,523,531</u>	<u>\$ -</u>	<u>\$ 20,656,129</u>	<u>\$ 27,525,969</u>	<u>\$ -</u>
Total impaired loans:						
Real estate mortgage	\$ 11,176,480	\$ 12,080,259	\$ 92,000	\$ 17,967,868	\$ 19,680,267	\$ 92,000
Production and intermediate term	1,574,011	5,481,242	-	2,620,862	8,026,594	-
Farm-related business	-	1,555	-	-	-	-
Rural residential real estate	156,043	156,042	-	166,145	166,145	-
Mission-related investments	-	-	-	900,406	900,406	-
Total	<u><u>\$ 12,906,534</u></u>	<u><u>\$ 17,719,098</u></u>	<u><u>\$ 92,000</u></u>	<u><u>\$ 21,655,281</u></u>	<u><u>\$ 28,773,412</u></u>	<u><u>\$ 92,000</u></u>

Notes to Unaudited Consolidated Financial Statements

	For the six months ended June 30, 2021		For the six months ended June 30, 2020		For the Year Ended December 31, 2020	
	Average Impaired Loans	Interest Income Recognized	Average Impaired Loans	Interest Income Recognized	Average Impaired Loans	Interest Income Recognized
	Impaired loans with a related allowance for credit losses:					
Real estate mortgage	\$ 967,193	\$ -	\$ 1,080,142	\$ -	\$ 1,062,298	\$ -
Production and intermediate term	-	-	1,043,862	-	-	-
Farm-related business	-	-	-	-	-	-
Rural residential real estate	-	-	-	-	-	-
Mission-related investments	-	-	-	-	-	-
Total	<u>\$ 967,193</u>	<u>\$ -</u>	<u>\$ 2,124,004</u>	<u>\$ -</u>	<u>\$ 1,062,298</u>	<u>\$ -</u>
Impaired loans with no related allowance for credit losses:						
Real estate mortgage	\$10,256,667	\$ 189,245	\$19,372,494	\$ 478,237	\$15,031,381	\$ 747,037
Production and intermediate term	1,588,064	16,339	4,613,370	102,258	2,981,890	68,441
Farm-related business	701	9,725	32,763	-	22,968	8,026
Rural residential real estate	162,262	-	118,875	-	144,244	-
Mission-related investments	792,378	484,310	1,305,464	4,571	970,117	-
Total	<u>\$12,800,072</u>	<u>\$ 699,619</u>	<u>\$25,442,966</u>	<u>\$ 585,066</u>	<u>\$19,150,600</u>	<u>\$ 823,504</u>
Total impaired loans:						
Real estate mortgage	\$11,223,860	\$ 189,245	\$20,452,636	\$ 478,237	\$16,093,679	\$ 747,037
Production and intermediate term	1,588,064	16,339	5,657,232	102,258	2,981,890	68,441
Farm-related business	701	9,725	32,763	-	22,968	8,026
Rural residential real estate	162,262	-	118,875	-	144,244	-
Mission-related investments	792,378	484,310	1,305,464	4,571	970,117	-
Total	<u>\$13,767,265</u>	<u>\$ 699,619</u>	<u>\$27,566,970</u>	<u>\$ 585,066</u>	<u>\$20,212,898</u>	<u>\$ 823,504</u>

^a Unpaid principal balance represents the recorded principal balance of the loan.

A restructuring of a debt constitutes a troubled debt restructuring if the creditor for economic or legal reasons related to the debtor's financial difficulties grants a concession to the debtor that it would not otherwise consider. Troubled debt restructurings are undertaken in order to improve the likelihood of recovery on the loan and may include, but are not limited to, forgiveness of principal or interest, interest rate reductions that are lower than the current market rate for new debt with similar risk, or significant term or payment extensions.

The following table provides additional information on troubled debt restructurings that occurred in the six months ended June 30, 2020.

For the six months ended June 30, 2020	Premodification	Postmodification
	Outstanding Recorded Investment	Outstanding Recorded Investment
Troubled debt restructurings:		
Production and intermediate term	<u>\$ 955,501</u>	<u>\$ 1,003,918</u>

Notes to Unaudited Consolidated Financial Statements

The following table provides additional information on troubled debt restructurings that occurred in the six months ended June 30, 2021.

For the six months ended June 30, 2021	Premodification Outstanding Recorded Investment	Postmodification Outstanding Recorded Investment
Troubled debt restructurings:		
Production and intermediate term	\$ 56,048	\$ 57,573

The premodification outstanding recorded investment represents the recorded investment of the loans as of the quarter end prior to the restructuring. The postmodification outstanding recorded investment represents the recorded investment of the loans as of the quarter end the restructuring occurred.

As of June 30, 2021, the total recorded investment of troubled debt restructured loans was \$7,226,414, of which \$953,342 was classified as nonaccrual, with specific allowance for loan losses of \$0. Commitments to lend funds to borrowers whose loan terms have been modified in a troubled debt restructuring were \$0 at June 30, 2021 and \$0 at December 31, 2020.

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

	Loans Modified as TDRs		TDRs in Nonaccrual Status*	
	June 30, 2021	December 31, 2020	June 30, 2021	December 31, 2020
Real estate mortgage	\$ 6,228,284	\$ 11,022,057	\$ 57,573	\$ -
Production and intermediate term	998,129	1,707,564	895,768	934,193
Farm-related business	1	-	1	
Mission-related investments		900,406		900,406
Total	\$ 7,226,414	\$ 13,630,027	\$ 953,342	\$ 1,834,599

*represents the portion of loans modified as TDRs that are in nonaccrual status

The predominant form of concession granted for troubled debt restructuring includes modifications to extend the term and delay payments. At times, these terms might be offset with incremental payments, collateral or new borrower guarantees, in which case management assesses all of the modified terms to determine if the overall modification qualifies as a troubled debt restructuring.

There were no loans that met the accounting criteria as a troubled debt restructuring and that occurred within the previous 12 months for which there was a subsequent payment default during the period. A payment default is defined as a payment that is 30 days past due after the date the loan was restructured.

Notes to Unaudited Consolidated Financial Statements

Allowance for Loan Losses (“ALL”). A summary of changes in ALL and period end recorded investment in loans is as follows:

	Real Estate Mortgage	Production and Intermediate Term	Agri- business	Communi- cation	Energy, water and waste water	Rural Residential Real Estate	Inter- national	Lease Receivable	Mission- Related Investments	Total
Allowance for Loan Losses:										
Balance at										
December 31, 2020	\$ 1,772,530	\$ 3,283,744	\$ 1,341,326	\$ 39,017	\$ 34,500	\$ 12,037		\$ 20,172	\$ 1,273	\$ 6,504,599
Charge-offs	-	-	(1,554)	-	-	-	-	-	-	(1,554)
Recoveries	-	511,590	-	-	-	-	-	-	-	511,590
Provision for loan losses	95,174	(516,311)	(162,117)	(3,764)	717	(3,643)	21,188	(4,044)	(221)	(573,020)
Other	(4,711)	35,557	53,300	730	(4,144)	171	-	-	-	80,905
Balance at										
June 30, 2021	\$ 1,862,992	\$ 3,314,581	\$ 1,230,955	\$ 35,983	\$ 31,073	\$ 8,566	\$ 21,188	\$ 16,129	\$ 1,052	\$ 6,522,520
Ending Balance:										
Individually evaluated for impairment	\$ 92,000	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ 92,000
Collectively evaluated for impairment	\$ 1,770,992	\$ 3,314,581	\$ 1,230,955	\$ 35,983	\$ 31,073	\$ 8,566	\$ 21,188	\$ 16,129	\$ 1,052	\$ 6,430,520
Acquired with deteriorated credit quality	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -
Recorded Investment in Loans Outstanding:										
Ending Balance at										
June 30, 2021	\$1,312,853,795	\$ 749,184,307	\$195,909,575	\$ 20,834,878	\$ 9,303,775	\$ 8,098,502	\$11,312,055	\$7,872,228	\$ 55,123,377	\$ 2,370,492,492
Individually evaluated for impairment	\$ 11,176,480	\$ 1,574,011	\$ -	\$ -	\$ -	\$ 156,043	\$ -	\$ -	\$ -	\$ 12,906,534
Collectively evaluated for impairment	\$1,301,677,315	\$ 747,610,296	\$195,909,575	\$ 20,834,878	\$ 9,303,775	\$ 7,942,459	\$11,312,055	\$7,872,228	\$ 55,123,377	\$ 2,357,585,958
Acquired with deteriorated credit quality	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -
Allowance for Loan Losses:										
Balance at										
December 31, 2019	\$ 1,525,554	\$ 3,748,407	\$ 730,161	\$ 38,983	\$ 18,383	\$ 7,676	\$ -	\$ 4,170	\$ 954	\$ 6,074,288
Charge-offs	(125)	(625,000)	-	-	-	-	-	-	-	(625,125)
Recoveries	-	958,559	-	-	-	-	-	-	-	958,559
Provision for loan losses	139,612	291,396	(32,272)	1,942	19,106	352	-	2,149	(28)	422,257
Other	1,098	(594,822)	3,699	95	2,801	(576)	-	-	-	(587,705)
Balance at										
June 30, 2020	\$ 1,666,139	\$ 3,778,540	\$ 701,588	\$ 41,020	\$ 40,290	\$ 7,452	\$ -	\$ 6,319	\$ 926	\$ 6,242,274
Ending Balance:										
Individually evaluated for impairment	\$ 172,000	\$ 536,200	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ 708,200
Collectively evaluated for impairment	\$ 1,494,139	\$ 3,242,340	\$ 701,588	\$ 41,020	\$ 40,290	\$ 7,452	\$ -	\$ 6,319	\$ 926	\$ 5,534,074
Acquired with deteriorated credit quality	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -
Recorded Investment in Loans Outstanding:										
Ending Balance at										
June 30, 2020	\$1,134,125,429	\$ 652,045,842	\$176,526,781	\$ 20,646,092	\$12,492,101	\$ 8,318,066	\$ -	\$1,515,235	\$ 66,649,941	\$ 2,072,319,487
Individually evaluated for impairment	\$ 20,293,972	\$ 12,083,874	\$ 30,649	\$ -	\$ -	\$ 171,884	\$ -	\$ -	\$ 1,262,867	\$ 33,843,246
Collectively evaluated for impairment	\$1,113,831,457	\$ 639,961,968	\$176,496,132	\$ 20,646,092	\$12,492,101	\$ 8,146,182	\$ -	\$1,515,235	\$ 65,387,074	\$ 2,038,476,241
Acquired with deteriorated credit quality	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -

Notes to Unaudited Consolidated Financial Statements

Note 4: Capital

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

Regulatory Capitalization Requirements.

	Capital			As of June 30, 2021	As of December 31, 2020
	Regulatory Minimums	Conservation Buffer	Total		
Risk-adjusted:					
Common equity tier 1 ratio	4.50%	2.50%	7.00%	11.36%	11.57%
Tier 1 capital ratio	6.00%	2.50%	8.50%	11.36%	11.57%
Total capital ratio	8.00%	2.50%	10.50%	12.63%	12.96%
Permanent capital ratio	7.00%	0.00%	7.00%	12.31%	12.58%
Non-risk-adjusted:					
Tier 1 leverage ratio	4.00%	1.00%	5.00%	10.56%	10.57%
UREE leverage ratio	1.50%	0.00%	1.50%	10.61%	10.64%

Following are the amounts included in the calculation of the capital ratios as of June 30, 2021:

	Regulatory Capital		Risk weighted assets/ Adjusted average total assets	
	6/30/2021	12/31/2020	6/30/2021	12/31/2020
Risk-adjusted capital ratios				
Common equity tier 1 ratio	\$ 250,791,722	\$ 239,563,607	\$ 2,206,718,387	\$ 2,069,735,381
Tier 1 capital ratio	250,791,722	239,563,607	2,206,718,387	2,069,735,381
Total capital ratio	278,712,426	268,279,789	2,206,718,387	2,069,735,381
Permanent capital ratio	270,791,422	259,563,607	2,200,286,401	2,062,561,942
Non-risk-adjusted capital ratios				
Tier 1 leverage ratio	250,791,722	239,563,607	2,374,527,797	2,265,402,932
UREE leverage ratio	252,021,895	240,930,272	2,374,527,797	2,265,402,932

Preferred stock issuance. In January 2017, the Association received clearance from FCA and the board approved the issuance of 20 million shares of a series of preferred stock, par value of \$1.00 per share. The stock was issued March 24, 2017. The stock is designated as *Fixed-to-Floating Rate Perpetual Cumulative Preferred Stock, Series A* ("**Series A Preferred Stock**"). The Series A Preferred stock has a fixed rate dividend of 5% for ten years, payable semi-annually. After ten years, the dividend rate becomes a floating rate at 5.00% above 6-month LIBOR. On or after 5 years, the Association may, at its option, redeem all or part of the Series A Preferred Stock. The Series A Preferred Stock is non-voting, except: (i) to materially change the Association's Charter or Bylaws that would materially adversely affect the holder of Series A Preferred Stock, (ii) to create, issue or authorize any class of stock ranking senior to the Series A Preferred Stock as to dividends or liquidation.

Notes to Unaudited Consolidated Financial Statements

Note 5: Income taxes

The Association is subject to federal and certain other income taxes. The Association is eligible to operate as a cooperative that qualifies for tax treatment under Subchapter T of the Internal Revenue code. Under specified conditions, the Association can exclude from taxable income amounts distributed as qualified patronage refunds in the form of cash, stock or allocated surplus. Provisions for income taxes are made only on those earnings that will not be distributed as qualified patronage refunds. During 2021, the Association is participating in a patronage program. Deferred taxes are recorded at the tax effect of all temporary differences based on the assumption that such temporary differences are retained by the institution and will therefore impact future tax payments. A valuation allowance is provided against deferred tax assets to the extent that it is more likely than not (more than 50 percent probability), based on management's estimate, that they will not be realized. The subsidiary, AgTexas, FLCA, is exempt from federal and other income taxes as provided in the Farm Credit Act of 1971.

Note 6: Fair Value Measurements

FASB guidance defines fair value as the exchange price that would be received for an asset or paid to transfer a liability in the principal or most advantageous market for the asset or liability. See note 14 to the 2020 Annual Report to Stockholders for a more complete description.

Assets and liabilities measured at fair value on a recurring basis are summarized below:

June 30, 2021	Fair Value Measurement Using			Total Fair Value
	Level 1	Level 2	Level 3	
Assets:				
Assets held in nonqualified benefit trusts	\$ 225,207	\$ -	\$ -	\$ 225,207
SBA pool securities	-	87,342,339	-	87,342,339
December 31, 2020	Fair Value Measurement Using			Total Fair Value
	Level 1	Level 2	Level 3	
Assets:				
Assets held in nonqualified benefit trusts	\$ 195,554	\$ -	\$ -	\$ 195,554
SBA pool securities	-	79,720,990	-	79,720,990

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

June 30, 2021	Fair Value Measurement Using			Total Fair Value
	Level 1	Level 2	Level 3	
Assets:				
Loans*	\$ -	\$ -	\$ 855,276	\$ 855,276
December 31, 2020	Fair Value Measurement Using			Total Fair Value
	Level 1	Level 2	Level 3	
Assets:				
Loans*	\$ -	\$ -	\$ 907,152	\$ 907,152

*Represents the fair value of certain loans that were evaluated for impairment under authoritative guidance "Accounting by Creditors for Impairment of a Loan." The fair value was based upon the underlying collateral since these were collateral-dependent loans for which real estate is the collateral.

Notes to Unaudited Consolidated Financial Statements

Information About Recurring and Nonrecurring Level 3 Fair Value Measurements

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

Information About Recurring and Nonrecurring Level 2 Fair Value Measurements

SBA pool securities are valued using a third-party pricing vendor. The Association's vendor utilizes major pricing services including Reuters and Intercontinental Exchange. The market values are based on inputs other than quoted prices, including:

- Quoted prices for similar assets in active markets.
- Quoted prices for identical or similar assets in markets that are not active.
- Inputs other than quoted prices, which provide a reasonable basis for fair value determination. Such inputs may include interest rates and yield curves, volatilities, prepayment speeds, credit risks and default rates.
- Inputs derived principally from observable market data.

Valuation Techniques

As more fully discussed in note 2 to the 2020 Annual Report, authoritative guidance establishes a fair value hierarchy, which requires an entity to maximize the use of observable inputs and minimize the use of unobservable inputs when measuring fair value. The following represent a brief summary of the valuation techniques used for the Association's assets and liabilities. For a more complete description, see notes to the 2020 Annual Report.

Assets Held in Nonqualified Benefits Trusts. Assets held in trust funds related to deferred compensation and supplemental retirement plans are classified within Level 1. The trust funds include investments that are actively traded and have quoted net asset values that are observable in the marketplace.

Loans Evaluated for Impairment. For certain loans evaluated for impairment under FASB impairment guidance, the fair value is based upon the underlying real estate collateral since the loans were collateral-dependent. The fair value measurement process uses independent appraisals and other market-based information, but in many cases it also requires significant input based on management's knowledge of and judgment about current market conditions, specific issues relating to the collateral and other matters. As a result, a majority of these loans have fair value measurements that fall within Level 3 of the fair value hierarchy. When the value of the real estate, less estimated costs to sell, is less than the principal balance of the loan, a specific reserve is established. The fair value of these loans would fall under Level 2 of the hierarchy if the process uses independent appraisals and other market-based information.

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

Note 7: Employee Benefit Plans

Employee Retirement Benefits. The following table summarizes the components of net periodic benefit costs of nonpension other postretirement employee benefits for the six months ended June 30:

	2021	2020
Service cost	\$ 53,980	\$ 59,347
Interest cost	107,170	127,881
Amortization of prior service credits	(23,936)	(23,936)
Amortization of net actuarial loss	9,896	6,620
Net periodic benefit cost	<u>\$ 147,110</u>	<u>\$ 169,912</u>

Notes to Unaudited Consolidated Financial Statements

The Association's liability for the unfunded accumulated obligation for these benefits at June 30, 2021, was \$7,815,021 and is included in "Accrued postretirement benefit liability" in the balance sheet. The components of net periodic benefit cost other than the service cost component are included in the line item "Other components of net periodic postretirement benefit cost" in the income statement.

The structure of the Association's defined benefit pension plan is characterized as multiemployer since the assets, liabilities and cost of the plan are not segregated or separately accounted for by participating employers (bank and associations). The Association recognizes its amortized annual contributions to the plan as an expense. The Association contributed \$2,236,998 to the District's defined benefit pension plan in 2021. Pension plan funding expense was \$1,118,499 and \$557,729 for the six months ended June 30, 2021 and 2020.

Note 8: Commitments and Contingent Liabilities

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

Note 9: Accumulated Other Comprehensive Income (Loss) ("AOCI")

AOCI includes the accumulated balance of certain gains, losses or costs for which values are included in assets or liabilities on the balance sheets, but which have not yet been recognized in earnings. For the Association, these elements include unrealized gains or losses on the AFS investment securities and amortization of retirement benefit elements. The following table summarizes the changes in the components of AOCI for the six months ended June 30, 2021 and 2020.

	Total	Unrealized gain on SBA pool securities	Retirement benefit plans
AOCI at			
December 31, 2020	\$ (414,547)	\$ 326,528	\$ (741,075)
SBA pool securities:			
Net change in unrealized gains	353,349	353,349	-
Retirement benefit plans:			
Amortization of prior service credits	(23,936)	-	(23,936)
Amortization of net actuarial loss	9,896	-	9,896
AOCI at			
June 30, 2021	<u>\$ (75,238)</u>	<u>\$ 679,877</u>	<u>\$ (755,115)</u>
	Total	Unrealized gain on SBA pool securities	Retirement benefit plans
AOCI at			
December 31, 2019	\$ (502,425)	\$ 121,558	\$ (623,983)
SBA pool securities:			
Net change in unrealized gains	(52,469)	(52,469)	-
Retirement benefit plans:			
Amortization of prior service credits and net actuarial loss	(17,316)	-	(17,316)
AOCI at			
June 30, 2020	<u>\$ (572,210)</u>	<u>\$ 69,089</u>	<u>\$ (641,299)</u>

Note 10: Subsequent Events

Association management has evaluated subsequent events through August 3, 2021, which is the date the CFS were issued or available to be issued, with no significant events to report.