# GREAT PLAINS AG CREDIT

# 2012 ANNUAL REPORT

December 31, 2012

Part of the Farm Credit System

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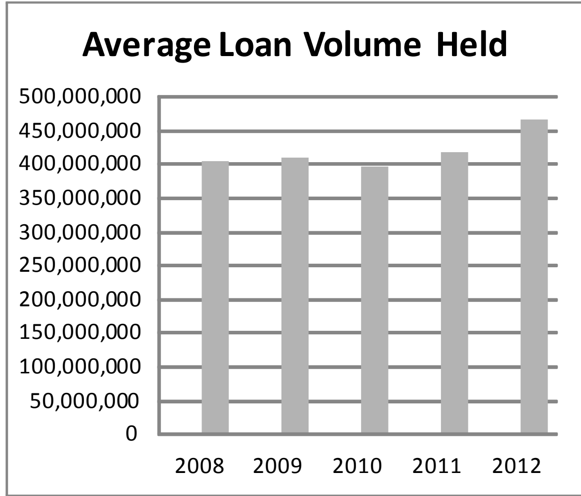
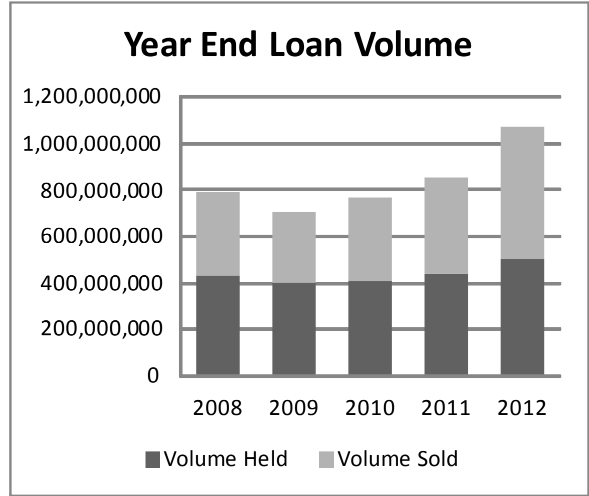
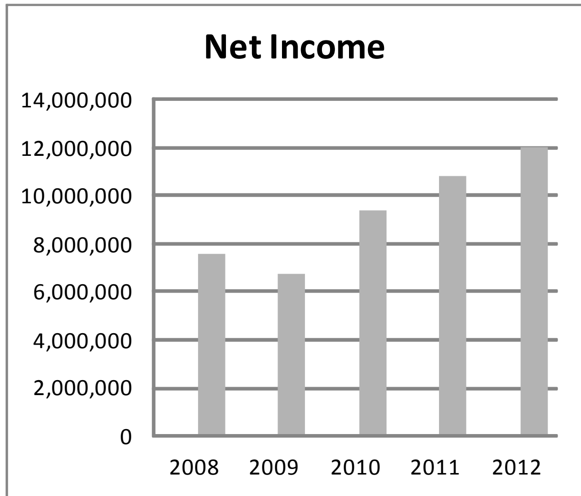
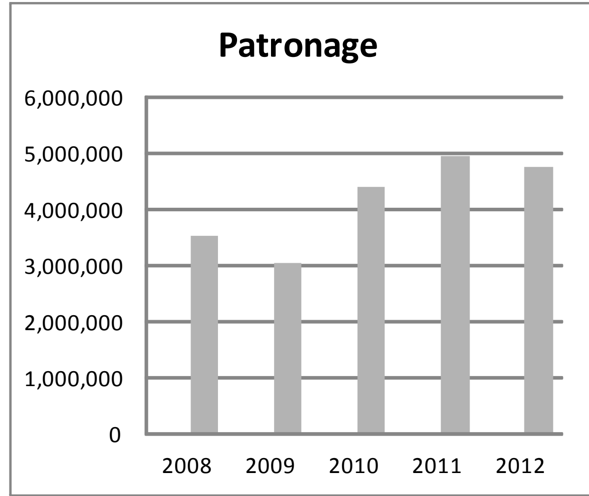
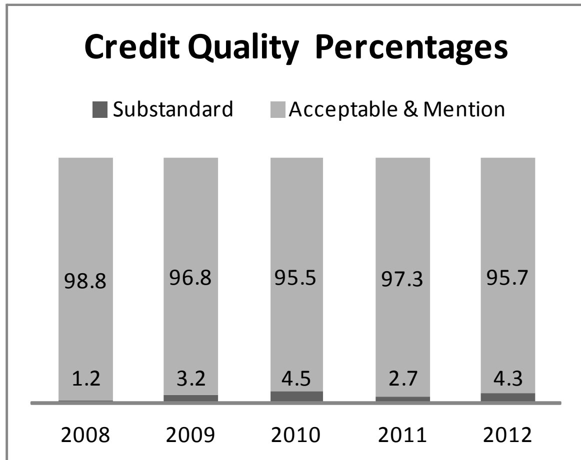
## FINANCIAL HIGHLIGHTS

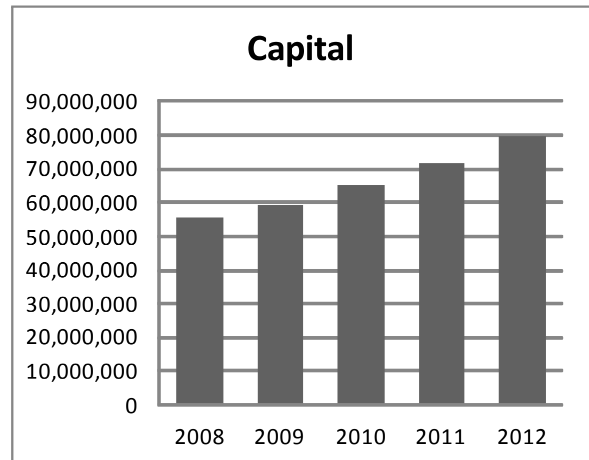


## REPORT OF MANAGEMENT

The consolidated financial statements of Great Plains Ag Credit, ACA (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 annual report is consistent with that in the consolidated financial statements.

To meet its responsibility for reliable financial information, management depends on the Farm Credit Bank of Texas' and the association's accounting and internal control systems, which have been designed to provide reasonable, but not absolute, assurance that assets are safeguarded and transactions are properly authorized and recorded. The systems have been designed to recognize that the cost of controls must be related to the benefits derived. The consolidated financial statements are audited by PricewaterhouseCoopers, LLP, independent accountants, who conduct a review of internal controls solely for the purpose of establishing a basis for reliance thereon in determining the nature, extent and timing of audit tests applied in the audit of the consolidated financial statements in accordance with auditing standards generally accepted in the United States of America. The association is also examined by the Farm Credit Administration.

The board of directors has overall responsibility for the association's systems of internal control and financial reporting. The board consults regularly with management and reviews the results of the audits and examinations referred to previously.

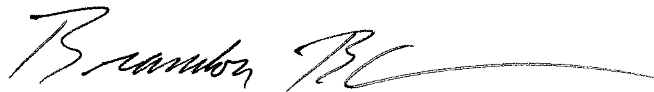
The undersigned certify that we have reviewed this annual report, that it has been prepared in accordance with all applicable statutory or regulatory requirements, and that the information contained herein is true, accurate and complete to the best of his or her knowledge or belief.

Tim McDonald, Chief Executive Officer

*February 28, 2013*

Dennis Anthony, Chairman, Board of Directors

*February 28, 2013*



Brandon Blaut, Chief Financial Officer

*February 28, 2013*

## REPORT OF AUDIT COMMITTEE

The Audit Committee (committee) is composed of four independent board members elected by the board of directors of Great Plains Ag Credit, ACA. In 2012, six committee meetings were held. The committee oversees the scope of Great Plains Ag Credit, ACA's testing of the system of internal controls and procedures, and the adequacy of management's action with respect to recommendations arising from those auditing activities. The committee's approved responsibilities are described more fully in the Audit Committee Charter, which is available on request or on Great Plains Ag Credit, ACA's website. The committee approved the appointment of PricewaterhouseCoopers LLP, for 2012.

Management is responsible for Great Plains Ag Credit, ACA's internal controls and the preparation of the consolidated financial statements in accordance with accounting principles generally accepted in the United States of America. The consolidated financial statements are prepared under the oversight of the committee. PricewaterhouseCoopers, LLP is responsible for performing an independent audit of the association's consolidated financial statements in accordance with auditing standards generally accepted in the United States of America and for issuing a report thereon. The committee's responsibilities include monitoring and overseeing the processes.

In this context, the committee reviewed and discussed Great Plains Ag Credit, ACA's audited consolidated financial statements for the year ended December 31, 2012 (audited consolidated financial statements) with management and PricewaterhouseCoopers, LLP. The committee also reviews with PricewaterhouseCoopers, LLP the matters required to be discussed by authoritative guidance "The Auditor's Communication With Those Charged With Governance," and both PricewaterhouseCoopers, LLP's and Great Plains Ag Credit, ACA's internal auditors directly provide reports on significant matters to the committee.

The committee discussed with PricewaterhouseCoopers, LLP its independence from Great Plains Ag Credit, ACA. The committee also reviewed the non-audit services provided by PricewaterhouseCoopers, LLP and concluded that these services were not incompatible with maintaining the independent accountant's independence. The committee has discussed with management and PricewaterhouseCoopers, LLP such other matters and received such assurances from them as the committee deemed appropriate.

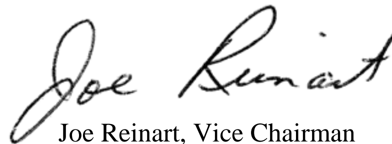
The committee also engaged FCC Services to conduct an external review of the loan portfolio based on criteria established by the committee. In addition, the committee engaged Lam Vinson & Company, LLP to perform agreed upon procedures to test key controls for operating effectiveness. The committee established the independence of both firms and each reported their findings directly to the audit committee.

Based on the foregoing review and discussions and relying thereon, the committee recommended that the board of directors include the audited consolidated financial statements in Great Plains Ag Credit, ACA's Annual Report to Stockholders for the year ended December 31, 2012.

Audit Committee Members

Terry Sherrill, Chairman

*February 28, 2013*

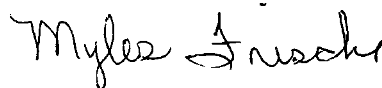


Joe Reinart, Vice Chairman

*February 28, 2013*

Danny Detten, Member

*February 28, 2013*



Myles Frische, Member

*February 28, 2013*

## DESCRIPTION OF BUSINESS

The description of the territory served, the persons eligible to borrow, the types of lending activities engaged in and the financial services offered, and related Farm Credit organizations required to be disclosed in this section is incorporated herein by reference from Note 1 to the consolidated financial statements, "Organization and Operations," included in this annual report.

The descriptions of significant developments that had or could have a material impact on earnings, interest rates to borrowers, patronage, or dividends and acquisitions or dispositions of material assets, changes in the reporting entity, changes in patronage policies or practices and financial assistance provided by or to the association through loss sharing or capital preservation agreements or from any other source, if any, required to be disclosed in this section are incorporated herein by reference from "Management's Discussion and Analysis of Financial Condition and Results of Operations," included in this annual report.

## DESCRIPTION OF PROPERTY

The association serves its 20-county territory through its main administrative and lending office at 5701 I-40 West, Amarillo, Texas. Additionally, there are four branch lending offices and two related services offices located throughout the territory. The association owns the office buildings in Amarillo, Dimmitt, Dumas, Friona, and Plainview, free of debt. The association leases office buildings in Amarillo and Muleshoe. The construction of the Dumas branch office was completed during 2007, and the construction of a branch in Plainview was completed during 2011. The association purchased land during 2012 for the future construction of a related services branch in Muleshoe to replace the current leased space.

## LEGAL PROCEEDINGS

In the ordinary course of business, the association is involved in various legal proceedings. In the opinion of legal counsel and management, there are no legal proceedings at this time that are likely to materially affect the consolidated financial statements of the association.

## DESCRIPTION OF CAPITAL STRUCTURE

The information required to be disclosed in this section is incorporated herein by reference from Note 9 to the consolidated financial statements, "Members' Equity," included in this annual report.

## DESCRIPTION OF LIABILITIES

The description of liabilities required to be disclosed in this section is incorporated herein by reference from Note 8 and in "Management's Discussion and Analysis of Financial Condition and Results of Operations," included in this annual report.

The description of contingent liabilities required to be disclosed in this section is incorporated herein by reference from Notes 2 and 14 to the consolidated financial statements, "Summary of Significant Accounting Policies" and "Commitments and Contingencies," respectively, included in this annual report.

## RELATIONSHIP WITH THE FARM CREDIT BANK OF TEXAS

The association's financial condition may be impacted by factors that affect the Farm Credit Bank of Texas (bank), as discussed in Note 1 to the consolidated financial statements, "Organization and Operations," included in this annual report. The financial condition and results of operations of the bank may materially affect the stockholders' investment in the association.

The Farm Credit Bank of Texas and District Associations' (district) 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, The Ag Agency, P.O. Box 202590, Austin, Texas 78720-2590 or calling (512) 483-9204. Copies of the district's annual and quarterly stockholder reports can also be requested by e-mailing *fcb@farmcreditbank.com*. The district's annual and quarterly stockholder reports are also available on its website at *www.farmcreditbank.com*.

The association's quarterly stockholder reports are also available free of charge, upon request. These reports will be available approximately 40 days after quarter end and can be obtained by writing to Great Plains Ag Credit, ACA P.O. Box 50060 Amarillo, TX 79159 or calling (806) 376-4669. Copies of the association's quarterly stockholder reports can also be requested by e-mailing *Carolyn.Brand@gpactx.com*. The association's annual stockholder report is available on its website at *www.gpactx.com* 75 days after the fiscal year end. Copies of the association's annual stockholder report can also be requested 90 days after the fiscal year end.

**GREAT PLAINS AG CREDIT, ACA**

**FIVE-YEAR SUMMARY OF SELECTED CONSOLIDATED FINANCIAL DATA**
**(unaudited)**
**(dollars in thousands)**

| | **2012** | 2011 | 2010 | 2009 | 2008 |
|---|---|---|---|---|---|
| **Balance Sheet Data** | | | | | |
| Assets | | | | | |
| Cash | **$ 35** | $ 33 | $ 26 | $ 38 | $ 421 |
| Investments | **3,304** | 5,425 | 7,404 | - | - |
| Loans | **500,213** | 432,167 | 404,272 | 399,125 | 430,050 |
| Less: allowance for credit losses | **(1,130)** | (692) | (1,189) | (1,353) | (705) |
| Net loans | **499,083** | 431,475 | 403,083 | 397,772 | 429,345 |
| Investment in and receivable from the Farm Credit Bank of Texas | **13,988** | 13,840 | 11,867 | 12,889 | 13,684 |
| Other assets | **10,408** | 9,379 | 8,599 | 8,496 | 10,848 |
| Total assets | **$ 526,818** | $ 460,152 | $ 430,979 | $ 419,195 | $ 454,298 |
| Liabilities | | | | | |
| Obligations with maturities of one year or less | **$ 18,847** | $ 386,139 | $ 13,123 | $ 12,836 | $ 397,098 |
| Obligations with maturities greater than one year | **428,452** | 2,107 | 352,587 | 346,879 | 1,701 |
| Total liabilities | **447,299** | 388,246 | 365,710 | 359,715 | 398,799 |
| Members' Equity | | | | | |
| Capital stock and participation certificates | **1,028** | 1,019 | 986 | 970 | 980 |
| Allocated retained earnings | **12,473** | 11,829 | 11,099 | 10,090 | 9,770 |
| Unallocated retained earnings | **66,116** | 58,901 | 53,027 | 48,053 | 44,305 |
| Accumulated other comprehensive income (loss) | **(98)** | 157 | 157 | 367 | 444 |
| Total members' equity | **79,519** | 71,906 | 65,269 | 59,480 | 55,499 |
| Total liabilities and members' equity | **$ 526,818** | $ 460,152 | $ 430,979 | $ 419,195 | $ 454,298 |
| **Statement of Income Data** | | | | | |
| Net interest income | **$ 13,805** | $ 12,137 | $ 11,201 | $ 10,341 | $ 9,625 |
| (Provision for loan losses) or loan loss reversal | **(1,462)** | 468 | (15) | (647) | (368) |
| Income from the Farm Credit Bank of Texas | **4,440** | 3,783 | 3,602 | 3,340 | 3,910 |
| Other noninterest income | **2,809** | 1,880 | 2,253 | 1,080 | 917 |
| Noninterest expense | **(7,562)** | (7,277) | (7,142) | (7,238) | (6,286) |
| Provision for income taxes | **(35)** | (153) | (501) | (86) | (215) |
| Net income (loss) | **$ 11,995** | $ 10,838 | $ 9,398 | $ 6,790 | $ 7,583 |
| **Key Financial Ratios for the Year** | | | | | |
| Return on average assets | **2.47%** | 2.48% | 2.26% | 1.58% | 1.79% |
| Return on average members' equity | **15.67%** | 15.77% | 14.97% | 11.78% | 14.07% |
| Net interest income as a percentage of average earning assets | **2.96%** | 2.90% | 2.82% | 2.51% | 2.38% |
| Net charge-offs (recoveries) as a percentage of average loans | **0.22%** | 0.00% | 0.00% | 0.00% | 0.00% |

## GREAT PLAINS AG CREDIT, ACA

## FIVE-YEAR SUMMARY OF SELECTED CONSOLIDATED FINANCIAL DATA

**(unaudited)**
**(dollars in thousands)**

| | **2012** | 2011 | 2010 | 2009 | 2008 |
|---|---|---|---|---|---|
| **Key Financial Ratios at Year End** | | | | | |
| Members' equity as a percentage of total assets | **15.09%** | 15.63% | 15.14% | 14.19% | 12.22% |
| Debt as a percentage of members' equity | **562.51%** | 539.94% | 560.31% | 604.77% | 718.58% |
| Allowance for loan losses as a percentage of loans | **0.23%** | 0.16% | 0.29% | 0.34% | 0.16% |
| Permanent capital ratio | **14.93%** | 14.95% | 14.66% | 13.74% | 11.59% |
| Core surplus ratio | **12.32%** | 12.21% | 11.67% | 11.02% | 9.29% |
| Total surplus ratio | **13.91%** | 13.85% | 13.27% | 13.48% | 11.36% |
| **Net Income Distribution** | | | | | |
| Patronage distribution declared | **$ 4,781** | $ 4,964 | $ 4,424 | $ 3,042 | $ 3,538 |
| Patronage dividends: | | | | | |
| Prior year's cash payment | **3,217** | 2,765 | 2,089 | 2,365 | 2,233 |
| Allocated surplus retirement | **720** | 1,015 | 652 | 633 | 1,194 |

## MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

The following commentary explains management's assessment of the principal aspects of the consolidated financial condition and results of operations of Great Plains Ag Credit, ACA, including its wholly-owned subsidiaries, Great Plains Ag Credit, PCA and Great Plains Ag Credit, FLCA (association) for the years ended December 31, 2012, 2011 and 2010, and should be read in conjunction with the accompanying consolidated financial statements. The accompanying financial statements were prepared under the oversight of the association's audit committee.

**Forward-Looking Information:**

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

- political, legal, regulatory and economic conditions and developments in the United States and abroad;
- economic fluctuations in the agricultural, rural utility, international and farm-related business sectors;
- weather-related, disease-related and other adverse climatic or biological conditions that periodically occur that impact agricultural productivity and income;
- changes in United States government support of the agricultural industry; and
- actions taken by the Federal Reserve System in implementing monetary policy.

**Significant Events:**

In December 2012, the association received a direct loan patronage of $1,693,621 from the bank, representing 43 basis points on the average daily balance of the association's direct loan with the bank. During 2012, the association received $96,959 in patronage payments from the bank, based on the association's stock investment in the bank. Also, the association received a capital markets patronage of $2,649,786 from the bank, representing 65 basis points on the association's average balance of participations in the bank's patronage pool program.

During 2012, the association received a payment totaling $407,735 which represented distributions from the Farm Credit System Insurance Corporation of excess reserves above the mandated Secure Base Amount. In addition, monies were also received which represented distributions from the Farm Credit Insurance Corporation to retire FAC stock totaling $326,040. These amounts were recorded in other noninterest income.

During 2010, the association received a payment totaling $387,915 which represented distributions from the Farm Credit System Insurance Corporation of excess reserves above the mandated Secure Base Amount. In addition, monies were also received which represented distributions from the Farm Credit Insurance Corporation to retire FAC stock totaling $302,486. These amounts were recorded in other noninterest income.

During 2009, the association modified its intended timeframe to retire allocated equities to reflect a period of no more than 20 years. This 10-year increase in the targeted revolvement period had the impact of reducing allocated equity retirements from previous years, thereby maintaining a greater level of association capital.

The association is party to various Long-Term Standby Purchase Commitments with the Farm Credit Bank of Texas and the Federal Agricultural Mortgage Corporation (Farmer Mac). The quality of the loan guarantees provided under these agreements, which the association utilizes to manage certain credit risk as well as regulatory capital requirements, could be significantly impacted by the financial results of the association's counterparties. Additional details relating to loan amounts guaranteed and fees paid under this arrangement are provided in Note 4 to the consolidated financial statements, "Loans and Allowance for Loan Losses," included in this annual report.

**Economic Outlook:**

In 2012, area farmers and ranchers benefited from high prices for most commodities they produce, but struggled through a second consecutive year of the drought. While moisture totals were better in 2012, we were still over 10 inches below normal.

Predictions are not favorable for the drought to end in 2013. Extended forecasts for the region include higher than normal temperatures and slightly better chances for moisture through the spring; drying out in May and throughout the growing season. Irrigated farmers will be able to produce good crops with proper water allocation, and dryland producers have crop insurance to generate revenue on land that would not otherwise produce. With the passage of time, however, the low yield history will affect the level of insurance available for those dryland farmers. Dry conditions in the territory and throughout the Midwest have negatively impacted cattle producers with reduced forage for grazing and much higher corn prices.

Native grass pastures are short and need a prolonged period of above-average moisture to return to pre-drought condition. The lack of outside grazing is limiting stocker cattle programs and driving up the cost of backgrounding feeder cattle, which pressures already thin feeder margins. Area feedlots have had difficulty projecting a profit from cattle on feed; most are relying on operating margins of the feedyard and enhancements from marketing programs to remain profitable overall.

The total U.S. cattle inventory, estimated at 89.3 million head at the end of 2012, has declined for six consecutive years, marking the lowest level since 1952. Today's beef cow herd is estimated at 29.3 million head and has declined 15 out of the past 17 years, making this the longest beef cow liquidation in history. Drought, high feed cost, opportunities for alternative land use and high cull cow prices are spurring on beef cow liquidation, despite record high calf prices. It is hard to predict when this trend will reverse, and once it does, it will take years to rebuild the herd.

In the meantime, competition for feeder cattle will remain tight. To maintain occupancy, feedlot owners will be forced to pay up for cattle while at times sacrificing operating margin from losses on cattle placed on feed. There are very few professional cattle feeders still active, causing custom feedlots to change their operating model to owning more cattle. Disciplined risk management is a must in this environment of thin margins and high volatility.

Beef demand remains relatively strong, although dependent on the general economy. Forecasters for 2013 have live cattle trading in a range from $115 on the low side to $130 on the high end.

The association also finances dairy operations, another protein sector struggling to maintain positive margins. The dairy cow herd decreased 10,000 head in 2012, totaling approximately 9.22 million head at year-end. Despite fewer milking cows, the market for class III milk has trended lower from its high of over $20/cwt. at the end of 3Q 2012 to around $18/cwt. at year-end. Looking forward, the futures market has milk trading in the $17-$18 range for all of 2013, which will be no better than a breakeven for most producers.

Feed costs are a major expense for dairies, so controlling that cost offers a strategic advantage. Farmland with good irrigation water is highly desirable for area dairy operations, and in turn supports land values in GPAC's 20-county territory. Over the past 5-10 years, values of good irrigated land increased by over 50 percent, driven by high commodity prices and feed needs for agribusinesses such as dairies and feedyards.

At its present price level, acres are shifting to corn production nationwide. Estimates are as high as 99 million acres in production; and an average yield of 158 bu./ac. would result in a crop 1.8 billion bu. larger than the prior record. This scenario requires rain in the Midwest during the critical months of the growing season, but if it happens, it is estimated the price of corn will drop to between $4 and $5/bu. On the other hand, carryover stocks are estimated at approximately 600 million bu., and if Midwest production is once again stifled by drought, it is believed prices for a bushel of corn could soar to $8 or more.

The cotton industry has been thriving throughout the territory for the past several years, with production advancing onto the north plains. Historically high prices of over $2/lb. two years ago resulted in production levels that outpaced demand and caused prices to retreat to levels around $0.60/lb., which is below breakeven for most producers. For 2013, the futures market has been advancing and is presently in the $0.80's. Many south plains operators are shifting acres away from cotton to grain sorghum. However, north plains farmers seem to be willing to maintain cotton in their rotation at these price levels.

A major issue for our area is water. Once an abundant resource from the Oglala aquifer, irrigation water districts are becoming more active in regulating water usage for agricultural purposes. While it is widely agreed that fundamentally sound regulation is needed, many are concerned that regulations may be overly restrictive or inconsistently administered, leading to disadvantages for some and possibly negatively impacting land values.

The region remains environmentally friendly to production agriculture; however, the environmental policy of this administration is not pro production agriculture and may result in more burdensome regulations and restrictions. All farms and agribusinesses are likely to be subject to higher cost of compliance in the future.

In summary, high commodity prices in general are providing good opportunities for profit; however, volatility is likely and must be managed with disciplined risk management programs. The challenging production scenario brought on by the continuing drought mitigates the benefit of high commodity prices. Those skilled operators who best position themselves for production while limiting their exposure to market and expense volatility should prosper in 2013.

**Loan Portfolio:**

The association makes and services loans to farmers, ranchers, rural homeowners and certain farm-related businesses. The association's loan volume consists of long-term farm mortgage loans, production and intermediate-term loans, and agribusiness loans. These loan products are available to eligible borrowers with competitive variable, fixed, adjustable and prime or LIBOR-based interest rates. Loan maturities range from one to 20 years, with annual operating loans comprising the majority of the commercial loans and five- to 20-year maturities comprising the majority of the mortgage loans. Loans serviced by the association offer several installment payment cycles, the timing of which usually coincides with the seasonal cash-flow capabilities of the borrower.

The association's portfolio consists of agricultural production and real estate loans focused in its 20-county chartered territory, which results in concentrations in the areas of beef cattle, crop production, and dairy. The profile of borrowers within the portfolio has evolved along with the agriculture industry, reflecting a more sophisticated customer base adept at managing the complexities of agribusiness operations. The quality of assets within the loan portfolio declined during 2012, reflecting deterioration in a small number of large credit relationships. The composition of the association's loan portfolio, including principal less funds held of $500,213,066, $432,166,853 and $404,272,031 as of December 31, 2012, 2011 and 2010, respectively, is described more fully in detailed tables in Note 4 to the consolidated financial statements, "Loans and Allowance for Loan Losses" included in this annual report.

**Purchase and Sales of Loans:**

During 2012, 2011 and 2010, the association was participating in loans with other lenders. As of December 31, 2012, 2011 and 2010, these participations totaled $59,731,520, $43,610,439 and $42,407,002, or 11.9 percent, 10.1 percent and 10.5 percent of loans, respectively. Included in these amounts are participations purchased from entities outside the district of $10,656,670, $10,160,674 and $2,842,745, or 2.1 percent, 2.4 percent and 0.7 percent of loans, respectively. The association has also sold participations of $565,742,934, $417,889,008 and $358,759,149 as of December 31, 2012, 2011 and 2010, respectively.

During 2010, the association exchanged loans totaling $7,635,135 for Federal Agricultural Mortgage Corporation (Farmer Mac) guaranteed mortgage-backed securities (AMBS). The loans were previously covered under the Long-Term Standby Commitment to Purchase Agreements with Farmer Mac. No gain or loss was recognized in the financial statements upon completion of the exchange transactions. These AMBS are included in the association's Consolidated Balance Sheet as held-to-maturity investments at an amortized cost balance of $3,304,296 at December 31, 2012. The association continues to service the loans included in those transactions.

**Risk Exposure:**

High-risk assets include nonaccrual loans, loans that are past due 90 days or more and still accruing interest, formally restructured loans, and other property owned, net. The following table illustrates the association's components and trends of high-risk assets serviced for the prior three years as of December 31:

| | **2012** | | 2011 | | 2010 | |
|---|---|---|---|---|---|---|
| | **Amount** | **%** | Amount | % | Amount | % |
| Nonaccrual | **$ 10,325,448** | **54.0%** | $ 19,306,723 | 100.0% | $ 19,720,290 | 100.0% |
| 90 days past due and still accruing interest | **-** | **0.0%** | - | 0.0% | - | 0.0% |
| Formally restructured | **8,554,491** | **46.0%** | - | 0.0% | - | 0.0% |
| Other property owned, net | **-** | **0.0%** | - | 0.0% | - | 0.0% |
| Total | **$ 18,879,939** | **100.0%** | $ 19,306,723 | 100.0% | $ 19,720,290 | 100.0% |

At December 31, 2012, 2011 and 2010, loans that were considered impaired were $18,879,939, $19,306,723 and $19,720,290, representing 3.8 percent, 4.5 percent and 4.9 percent of loan volume, respectively. Impaired loans consist of all high-risk assets except other property owned, net. The association maintains credit enhancements in the form of Farmer Mac Long-Term Standby agreements on a portion of these assets totaling $7,034,600. Furthermore, all relationships are well secured and the association anticipates full collection.

The changing composition of high-risk assets reflects positive performance on a loan relationship that was restructured as a result of the bankruptcy process, and formally discharged as of December 21, 2011. The relationship continues to perform under the terms of the restructure and was reinstated to accrual status during 2012.

At December 31, 2012, loan balances to the association's 10 largest credit exposures totaled $91,144,180, representing 18.2 percent of total loan volume. The association maintains credit enhancements in the form of Farmer Mac Long-Term Standby agreements on a portion of these assets totaling $32,892,764.

The short-term portion of the association's loan portfolio is seasonal in nature. Crop loans increase from the soil preparation through the harvest phases, then significantly decline as crops are sold.

The association regularly employs practices such as obtaining credit guarantees and engaging in loan participations to mitigate and diversify credit risk, to help manage commodity exposure, and to service the credit needs of certain borrowers.

**Allowance for Credit Losses:**

The following table provides relevant information regarding the allowance for loan losses as of, or for the year ended, December 31:

| | **2012** | 2011 | 2010 |
|---|---|---|---|
| Allowance for loan losses | **$1,129,817** | $691,893 | $1,188,958 |
| Reserve for unfunded credit commitments | **$217,686** | $208,493 | $178,628 |
| Allowance for credit losses | **$1,347,503** | $900,386 | $1,367,586 |
| | | | |
| Allowance for credit losses to total loans | **0.27%** | 0.21% | 0.34% |
| Allowance for loan losses to total loans | **0.23%** | 0.16% | 0.29% |
| Allowance for loan losses to nonaccrual loans | **10.9%** | 3.6% | 6.0% |
| Allowance for loan losses to impaired loans | **6.0%** | 3.6% | 6.0% |
| Net charge-offs to average loans | **0.22%** | 0.0% | 0.0% |

The allowance for credit losses is maintained based upon estimates that consider the general financial strength of the agricultural economy, loan portfolio composition, credit administration and the portfolio's prior loan loss experience. The association's process for determining the appropriate level of the allowance for credit losses is designed to account for credit deterioration as it occurs. Accordingly, the methodology is based upon internal loan level credit quality ratings and grade specific loss factors. Additionally, the association accounts for certain nonperforming loans through an individual impairment analysis utilizing the fair value of the underlying collateral in the loans. The association has recorded specific reserves on impaired assets totaling $110,145 for the period ended December 31, 2012, and did not require specific reserves to be booked for the periods ended December 31 2011, or 2010.

The current level of the allowance account maintained by the association is further supported by the association's continued focus on sound underwriting, loan structure and servicing. This includes the incorporation of loan agreements, borrowing bases, and guarantees to help mitigate credit risk. Based upon ongoing risk assessment and the allowance for credit losses procedures outlined above, the allowance for credit losses of $1,347,503, $900,386, and $1,367,586 at December 31, 2012, 2011 and 2010, respectively, is considered adequate by management to compensate for inherent losses in the loan portfolio at such dates.

**Results of Operations:**

The association's net income for the year ended December 31, 2012, was $11,995,473 as compared to $10,837,744 for the year ended December 31, 2011, reflecting an increase of $1,157,729, or 10.7 percent. The association's net income for the year ended December 31, 2010 was $9,398,043. Net income increased $1,439,701, or 15.3 percent, in 2011 versus 2010.

Net interest income for 2012, 2011 and 2010 was $13,805,416, $12,137,398 and $11,201,128, respectively, reflecting increases of $1,668,018, or 13.7 percent, for 2012 versus 2011 and $936,270, or 8.4 percent, for 2011 versus 2010. Net interest income is the principal source of earnings for the association and is impacted by volume, yields on assets and cost of debt. The effects of changes in average volume and interest rates on net interest income over the past three years are presented in the following tables:

| | **2012** | | 2011 | | 2010 | |
|---|---|---|---|---|---|---|
| | **Average Balance** | **Interest** | Average Balance | Interest | Average Balance | Interest |
| Loans | **$ 462,462,208** | **$ 20,445,143** | $ 413,094,610 | $ 18,795,554 | $ 392,411,685 | $ 18,242,724 |
| Investments | **4,407,415** | **273,330** | 6,140,619 | 365,602 | 5,116,691 | 289,268 |
| Total interest-earning assets | **466,869,623** | **20,718,473** | 419,235,229 | 19,161,156 | 397,528,376 | 18,531,992 |
| Interest-bearing liabilities | **403,326,701** | **6,913,057** | 362,188,254 | 7,023,758 | 346,811,553 | 7,330,864 |
| Impact of capital | **$ 63,542,922** | | $ 57,046,975 | | $ 50,716,823 | |
| Net interest income | | **$ 13,805,416** | | $ 12,137,398 | | $ 11,201,128 |

| | **2012 Average Yield** | 2011 Average Yield | 2010 Average Yield |
|---|---|---|---|
| Yield on loans | **4.42%** | 4.55% | 4.65% |
| Yield on investments | **6.20%** | 5.95% | 5.65% |
| Total yield on interest-earning assets | **4.44%** | 4.57% | 4.66% |
| Cost of interest-bearing liabilities | **1.71%** | 1.94% | 2.11% |
| Interest rate spread | **2.73%** | 2.63% | 2.55% |
| Interest rate margin | **2.96%** | 2.90% | 2.82% |

| | **2012 vs. 2011** | | | 2011 vs. 2010 | | |
|---|---|---|---|---|---|---|
| | **Increase (decrease) due to** | | | Increase (decrease) due to | | |
| | **Volume** | **Rate** | **Total** | Volume | Rate | Total |
| Interest income - loans | **$ 2,246,196** | **$ (596,607)** | **$ 1,649,589** | $ 961,523 | $ (408,693) | $ 552,830 |
| Interest income - investments | **(103,192)** | **10,920** | **(92,272)** | 57,887 | 18,447 | 76,334 |
| Total interest income | **2,143,004** | **(585,687)** | **1,557,317** | 1,019,410 | (390,246) | 629,164 |
| Interest expense | **797,780** | **(908,481)** | **(110,701)** | 325,031 | (632,137) | (307,106) |
| Net interest income | **$ 1,345,224** | **$ 322,794** | **$ 1,668,018** | $ 694,379 | $ 241,891 | $ 936,270 |

Interest income for 2012 increased by $1,557,317, or 8.1 percent, compared to 2011, as the impact of a higher volume of earning assets more than offset a decline in loan yields. Interest expense for 2012 decreased by $110,701, or 1.6 percent, compared to 2011 due to a continued low interest rate environment, which has allowed the association to fund debt at favorable rates. The association has benefitted from year-over-year interest rate spread increases of 10 basis points for the 2012 period and 8 basis points for the 2011 period, which in addition to the associations lower funding cost on debt, also reflects increases in income received on high-risk assets over the time periods.

The association's interest margin increased 6 basis points during the 2012 operating year, which compares to an 8 basis point increase in 2011. In addition to spread, margin is affected by interest rates' impact on the level of association capital funding the

loan portfolio. Margin was impacted during 2012 by a reduced yield on the association's loan portfolio, which was significantly offset by a higher level of capital funding the portfolio. This is contrasted by results realized during the 2010 reporting period during which margin was positively impacted by both a higher yielding portfolio as well as higher capital levels.

Loan products are available to eligible borrowers with competitive, differentially priced, variable or fixed rates which are uniformly determined by loan quality, loan size, reporting frequency and quality, frequency of interest payments, and servicing criteria. While the majority of loans contain provisions for variable interest rates, the fixed rate loan program is also available for all qualifying loans.

Variable rate loans may be priced, or indexed, based upon prime or LIBOR plus association spreads.

Fixed-rate terms on PCA loans range up to 10 years for most loan purposes, but may qualify for up to 15 years on certain facility-type loans. Fixed rate terms to 20 years are available on qualifying FLCA loans.

The association's spread is based on criteria as defined in the Interest Rate Policy and Procedures. An association Asset/Liability Committee reviews loan spreads and net interest margin regularly to assess interest rate margins and profitability, and is able to adjust as necessary. Loans are match funded in amount and maturity with the Farm Credit Bank of Texas, and rates are determined in accordance with pricing offered by the bank.

Noninterest income for 2012 increased by $1,585,635, or 28.0 percent, compared to 2011, due primarily to increased patronage income received from the bank relating to increases in both participation loans sold and direct note volume. Additionally, 2012 noninterest income benefitted from monies received from the Farm Credit System Insurance Corporation (FCSIC) relating to excess reserves in the insurance fund and the retirement of FAC stock which totaled $733,775. Authoritative accounting guidance requiring the capitalization and amortization of certain loan fees and costs was implemented during 2010. Fees totaling $561,091, $250,667 and $145,478 were capitalized during the 2012, 2011 and 2010 respective periods and will be amortized over the life of the loans as an adjustment to yield in net interest income. Noninterest income for 2011 totaled $5,662,565, a decrease of $192,826, or 3.3 percent, from the prior year primarily reflecting the receipt of a significant amount of nonrecurring revenue during 2010. Noninterest income was positively impacted in 2011 by related services revenue which increased $478,287 from the prior year, benefitting from both higher insurance premiums driven by commodity prices as well as a continued focus on expanding the insurance division's client base. Additionally, noninterest income benefitted from year-over-year gains in sold note patronage received from the Farm Credit Bank of Texas due to a higher volume of loan participations. Partially offsetting these gains were the impact of an 8 basis point decline in direct note patronage received from the bank as well as a lower level of fee income recorded as income.

The provision for credit losses reflects changes needed in the allowance accounts necessary to absorb probable losses within the association's loan portfolio and may be impacted by loan volume, loan quality and management estimates of loss. The provision for credit losses in 2012 was negatively influenced by deteriorating credit quality measures, resulting in a provision to the allowance account of $1,461,647 which included the impact of charge-offs totaling $1,014,616 and specific reserves of $110,145. This compared to a reversal to the allowance account totaling $467,577 during 2011 and a provision of $14,720 during 2010. There were no charge-offs or specific reserves which impacted the provision as of December 31, 2011 or 2010.

Operating expenses consist primarily of salaries, employee benefits and purchased services. Expenses for purchased services may include administrative services, marketing, information systems, accounting and loan processing, among others. Association operating expenses totaled $7,561,752 for 2012, an increase of $285,058, or 3.9 percent compared to the prior year. Factors contributing to the increase include a higher level of salary expense, increased support of area programs, and fees associated with increased utilization of Farmer Mac programs. Operating expenses for 2012 benefitted from year-over-year reductions in the areas of pension funding, which reduced expenses tied to benefits, and a reduction in allocated expenses passed through from the bank. Additionally, operating expenses are impacted by accounting guidance that requires the capitalization and amortization of certain loan fees and costs. Salary and benefits totaling $535,302, $235,637 and $141,381 have been capitalized during the 2012, 2011 and 2010 respective periods and will be amortized over the life of the loans as an adjustment to yield in net interest income. Operating expenses for 2011 totaled $7,276,694, an increase of $134,339, or 1.9 percent, compared to 2010. Factors contributing to this increase include a $194,947 increase in pension funding included in employee benefits, and repairs to the Amarillo office which impacted cost of space. Operating expenses for 2011 benefitted from reductions in the areas of purchased services and data processing, which reflects the recovery of legal expenses associated with collection efforts on impaired loans, as well as reduced costs for services provided by the bank.

For the year ended December 31, 2012, the association's return on average assets was 2.5 percent, as compared to 2.5 percent and 2.3 percent for the years ended December 31, 2011 and 2010, respectively. For the year ended December 31, 2012, the

association's return on average members' equity was 15.7 percent, as compared to 15.8 percent and 15.0 percent for the years ended December 31, 2011 and 2010, respectively.

Because the association depends on the bank for funding, any significant positive or negative factors affecting the operations of the bank would have a similar effect on the operations of the association.

**Liquidity and Funding Sources:**

The interest rate risk inherent in the association's loan portfolio is substantially mitigated through the funding relationship with the bank. The bank manages interest rate risk through its direct loan pricing and asset/liability management process; however, a portion of the association's own funds, which represents the amount of the association's loan portfolio funded by the association's equity, is impacted by rate movements.

The primary source of liquidity and funding for the association is a direct loan from the bank. The outstanding balance of $426,001,870, $370,853,835 and $350,486,462 as of December 31, 2012, 2011 and 2010, respectively, is recorded as a liability on the association's balance sheet. The note carried a weighted average interest rate of 1.58 percent, 2.21 percent and 1.89 percent at December 31, 2012, 2011 and 2010, respectively. The indebtedness is collateralized by a pledge of substantially all of the association's assets to the bank and is governed by a general financing agreement. The increase in note payable to the bank and related accrued interest payable since December 31, 2011, is due to growth in the association's loan portfolio. The association's own funds, which represent the amount of the association's loan portfolio funded by the association's equity, were $69,340,271, $60,154,580 and $53,512,227 at December 31, 2012, 2011 and 2010, respectively. The maximum amount the association may borrow from the bank as of December 31, 2012, was $494,928,071 as defined by the general financing agreement. The indebtedness continues in effect until the expiration date of the general financing agreement, which is September 30, 2015, unless sooner terminated by the bank upon the occurrence of an event of default, or by the association, in the event of a breach of this agreement by the bank, upon giving the bank 30 calendar days prior written notice, or in all other circumstances, upon giving the bank 120 days prior written notice.

The liquidity policy of the association is to manage cash balances to maximize debt reduction and to increase accrual loan volume. This policy will continue to be pursued during 2013. As borrower payments are received, they are applied to the association's note payable to the bank.

The association will continue to fund its operations through direct borrowings from the bank, capital surplus from prior years and borrower stock. It is management's opinion that funds available to the association are sufficient to fund its operations for the coming year.

**Capital Resources:**

The association's capital position remains strong, with total members' equity of $79,518,556, $71,905,980 and $65,269,140 at December 31, 2012, 2011 and 2010, respectively. Under regulations governing minimum permanent capital adequacy and other capitalization issues, the association is required to maintain a minimum adjusted permanent capital of 7.0 percent of risk-adjusted assets as defined by the FCA. The permanent capital ratio measures available at-risk capital relative to risk-adjusted assets and off-balance-sheet contingencies. The ratio is an indicator of the institution's financial capacity to absorb potential losses beyond that provided in the allowance for loss accounts. The association's permanent capital ratio at December 31, 2012, 2011 and 2010 was 14.9 percent, 15.0 percent and 14.7 percent, respectively. The core surplus ratio measures available core surplus capital relative to risk-adjusted assets and off-balance-sheet contingencies. The ratio is an indicator of the quality of capital that exists to maintain stable earnings and financial strength. The association's core surplus ratio at December 31, 2012, 2011 and 2010 was 12.3 percent, 12.2 percent and 11.7 percent, respectively, which is in compliance with the FCA's minimum ratio requirement of 3.5 percent. The total surplus ratio measures available surplus capital relative to risk-adjusted assets and off-balance-sheet contingencies. The ratio is an indicator of the reserves existing to protect borrowers' investments in the association. The association's total surplus ratio at December 31, 2012, 2011 and 2010 was 13.9 percent, 13.9 percent and 13.3 percent, respectively, which is in compliance with the FCA's minimum ratio requirement of 7.0 percent.

In 2012, 2011 and 2010, the association declared patronage distributions of $4,780,737, $4,963,544 and $4,424,121, respectively. Cash payments from the prior year's earnings were made of $3,217,184, $2,762,929 and $2,087,980; and additional payments to retire prior years' allocated surplus were made of $719,792, $1,015,746, and $652,258. See Note 9 to the consolidated financial statements, "Members' Equity," included in this annual report, for further information.

**Relationship With the Bank:**

The association's statutory obligation to borrow only from the bank is discussed in Note 8 to the consolidated financial statements, "Note Payable to the Bank," included in this annual report.

The bank's ability to access capital of the association is discussed in Note 2 to the consolidated financial statements, "Summary of Significant Accounting Policies," included in this annual report, within the section "Capital Stock Investment in the Bank."

The bank's role in mitigating the association's exposure to interest rate risk is described in the section "Liquidity and Funding Sources" of Management's Discussion and Analysis and in Note 8 to the consolidated financial statements, "Note Payable to the Bank," included in this annual report.

The bank provides computer systems to support the critical operations of all district associations. In addition, each association has operating systems and facility-based systems that are not supported by the bank. As disclosed in Note 12 to the consolidated financial statements, "Related Party Transactions," included in this annual report, the bank provides many services that the association can utilize, such as administrative, marketing, information systems and accounting services. Additionally, the bank bills district expenses to the associations, such as the Farm Credit System Insurance Corporation insurance premiums. As of April 2011, the bank only bills associations for direct pass-through expenses and no longer bills for allocated expenses.

**Summary:**

Over the past 79 years, regardless of the state of the agricultural economy, your association's board of directors and management, as well as the board of directors and management of the bank, have been committed to offering their borrowers a ready source of financing at a competitive price. Your continued support will be critical to the success of this association.

## DIRECTORS AND SENIOR OFFICERS

The association's member-elected and director-elected board of directors and senior officers are as follows:

| NAME | POSITION | DATE ELECTED/ EMPLOYED | TERM EXPIRES |
|---|---|---|---|
| Dennis Anthony | Chairman | 1993 | 2014 |
| Joe Reinart | Vice Chairman | 2006 | 2013 |
| Danny Detten | Director | 1999 | 2014 |
| Trent Finck | Director | 2006 | 2015 |
| Bryan Reinart | Director | 2007 | 2013 |
| Myles Frische | Director | 2012 | 2015 |
| Terry Sherrill | Director-elected | 2004 | 2013 |
| Dan McWhorter | Director | 2009 | expired in 2012 |
| Tim McDonald | President/CEO | 1989 | |
| Brandon Blaut | SVP/CFO | 2006 | |
| Doug Reinart | SVP/CCO | 1989 | |
| Eddie York | SVP/ CLO/Branch Manager | 1991 | |
| Debra Wilfong | VP/Treasurer/Asst. CFO/Asst. Sec. | 1981 | |

A brief statement of the business and employment background of each director and senior officer is provided for informational purposes.

**Dennis Anthony,** Chairman**,** age 60, was elected to the board in 1993 and serves on the Executive Committee. A graduate of Texas Tech University, he has been farming and a stockholder since 1975. He grows dryland milo and wheat, and some irrigated corn in Parmer and Deaf Smith counties, with his operation concentrated mostly toward livestock, including cattle feeding. He is also a stockholder in PACO Feedyard, Friona, Texas. Mr. Anthony is on the Human Resource Committee for GPAC. His term will expire in 2014.

**Joe Reinart,** Vice Chairman has served on the board since 2006. Mr. Reinart has been farming since 1973 in the Sherman/Dallam County area, focusing on irrigated corn, wheat, seed milo production and cotton in addition to stocker cattle. Mr. Reinart is 57 years old and has been a stockholder of GPAC since 1975. He also serves as chairman of the Sunray Co-op Board. He is the vice chairman of the Audit Committee and serves on the Executive and Marketing Committees. His term will expire in 2013.

**Danny Detten,** member of the Audit Committee and the Credit Review Committee, was elected to the board in 1999. He lives near Panhandle and farms, pastures and feeds cattle in Carson, Potter and Hutchinson counties, raises irrigated and dryland wheat, feed grains, corn and cotton in partnership with his son. Mr. Detten, age 68, has been a stockholder since 1980 and is a lifetime farmer and stockman. His term expires in 2014.

**Trent Finck** was elected to the board in May of 2006 and serves as chairman of the Human Resource Committee. He is also an alternate member on the Credit Review Committee. At age 52, he has been a farmer and rancher since his graduation in 1982 with a degree in ag economics from Texas Tech University. Trent has been a stockholder since 1983. His operation in Swisher and Briscoe counties includes a partnership with his father in which they jointly and individually operate a stocker cattle and cow-calf operation as well as irrigated and dryland wheat and milo, and irrigated cotton. His term expires in 2015.

**Bryan Reinart,** age 55, was elected to the board in 2007 and serves as vice chairman of the Human Resources Committee. Mr. Reinart is a lifelong farmer and resides in Dimmitt, Castro County, Texas. His operation consists of irrigated cotton, wheat, milo and corn, in addition to dryland cotton, wheat, milo and pasture. He also serves on the boards of the Hereford Grain Coop and Castro County Farm Bureau. Mr. Reinart became a Great Plains stockholder in 1980. His term will expire in 2013.

**Myles Frische** was elected to the board in April of 2012 and serves on the Audit Committee. A resident of Dumas, Mr. Frische farms and ranches in Hartley, Moore, Sherman, and Hutchinson counties. His operation consists of irrigated seed production, corn, wheat and cotton. He also farms dryland wheat and cotton, runs cattle on grass and wheat, and has a grow yard. Mr. Frische is also a partner in a full-service commercial fertilizer sale and application business. He has been a stockholder with Great Plains Ag Credit since 2004. He is 56 years of age and his term as director expires in 2015.

**Terry Sherrill** serves as chairman of the GPAC Audit Committee and was elected by the board of directors in January of 2004. He is 56 years old, a certified public accountant, and has owned and operated a public accounting firm in Gruver since 1999. Prior to that time, he was the chief financial officer for two large agribusinesses in the Panhandle and was also employed by the accounting firm Arthur Young and Company. He received a bachelor of business administration in accounting from West Texas State University. His term will expire in 2013.

**Dan McWhorter** was elected to the board in June of 2009. A resident of Canyon, Mr. McWhorter is president and owner/operator of Mc-6 Cattle Feeders near Hereford, Texas. His operation includes farmland in Deaf Smith County that grows feed for the yard, corn silage and wheat. He also operates acreage in Uvalde that yields corn, wheat, cotton and vegetables. He also runs cattle on ranchland in Nebraska. Mr. McWhorter is 65 years old and has been a member at Great Plains since 2005. He was a member of the Human Resource Committee. His term expired in 2012.

**Tim McDonald,** president and chief executive officer, age 45. Mr. McDonald was appointed chief executive officer in 2006 after serving in the capacity of regional credit officer for Great Plains and more recently as CCO. He was employed by the Amarillo PCA for 12 years and served as the Amarillo association's executive vice president from 1994 until October 1999. His prior service with the association was as loan officer in the Dumas office until 1992 and then transferred to the Amarillo office as loan officer and internal credit review coordinator. He completed his degree from West Texas State University.

**Brandon Blaut,** senior vice president, chief financial officer, age 36. Mr. Blaut joined the central office staff in June of 2006. He holds a B.B.A. degree in finance from West Texas A&M University and earned the Chartered Financial Analyst designation. Mr. Blaut had five years of experience in commercial lending prior to joining the association.

**Doug Reinart,** senior vice president, chief credit officer, age 54. He is a 23-year employee and supervises credit. He began his financial career as a loan officer trainee at the Central Texas PCA in 1985 and served as Central's vice president/branch manager from 1986 to 1989. Prior to that, he farmed and was employed by an agribusiness company in the Hereford, Texas, area. Mr. Reinart is a cum laude graduate of West Texas State University.

**Eddie York,** senior vice president, chief lending officer, age 48. He is a 22-year employee and served as vice president from 1998 through 2004. Mr. York was previously employed by the Clinton Production Credit Association in Oklahoma. He graduated from Southwestern Oklahoma State University with a master's degree in business.

**Debra Wilfong**, vice president, treasurer, assistant chief financial officer and assistant corporate secretary, age 49. She has been an employee for 31 years serving as branch office assistant, accounting department assistant and assistant treasurer. Ms. Wilfong was promoted to treasurer in 1999 and to vice president/treasurer in 2002. While employed by the association, Ms. Wilfong received a B.B.A. degree in finance from West Texas State University.

## COMPENSATION OF DIRECTORS

Directors were compensated for their service to the association in the form of an honorarium at the rate of $600 per day for director meetings and committee meetings, and they were reimbursed for certain expenses incurred while representing the association in an official capacity. The director-elected director was additionally compensated for his Audit Committee-related service to the association in the form of an honorarium at the rate of $1,875 per quarter. Mileage for attending official meetings during 2012 was paid at the IRS-approved rate of 55.5 cents per mile. A copy of the travel policy is available to stockholders of the association upon request.

| Director | Number of Days Served, Board Meetings | Number of Days Served, Other Official Activities | Total Compensation in 2012 |
|---|---|---|---|
| Dennis Anthony | 11 | 25 | 21,500 |
| Joe Reinart | 11 | 22 | 19,700 |
| Danny Detten | 10 | 2 | 7,100 |
| Trent Finck | 11 | 14 | 14,900 |
| Bryan Reinart | 11 | 9 | 11,900 |
| Myles Frische | 5 | 4.5 | 6,200 |
| Terry Sherrill | 11 | 13.5 | 22,700 |
| Dan McWhorter | 2 | 3 | 3,000 |
| | | | $ 107,000 |

The aggregate compensation paid to directors in 2012, 2011 and 2010 was $107,000, $91,825 and $93,850, respectively.

## BOARD COMMITTEES

The board of directors of Great Plains Ag Credit ACA, PCA, & FLCA has created a committee of directors to be known as the Audit Committee for the purpose of assisting the board in fulfilling its fiduciary and oversight responsibilities for the financial reporting process, the systems of internal control, the audit process, and the association's process for monitoring compliance with laws, regulations, policies, the standards of conduct and public responsibilities.

The board recognizes the complexities within personnel and compensation areas, and therefore has created a committee of directors known as the Human Resource Committee for the purpose of assisting the board in human resource due diligence and oversight responsibilities within the association. The HR Committee's sensitivity to current business environments and its prudent management of the association's financial resources are essential in protecting the association's reputation in the community and in the marketplace. The committee is to remain accountable and report only to the board.

The primary objective of the Executive Committee is providing oversight to the Loan Committee through periodic review of the association's loans. During this review, loans are presented in detail to the Executive Committee, enabling members to evaluate credit decisions and confirm that the Loan Committee is acting within prescribed guidelines. Loans presented are selected by management based on criteria such as loans to new stockholders, larger loans, loans financing commodities unfamiliar to the association, and lower quality loans. Additionally, the Executive Committee will review the minutes from all Loan Committee meetings, selecting any loan they wish to review in more detail.

The purpose of the Marketing Committee is to research and implement marketing and advertising efforts with the goal of creating positive consumer interest in the association while keeping in mind overall cost effectiveness.

Additional detail regarding director compensation paid for committee service (which is included in the table above) is as follows:

| Director | Committee Compensation<br>Audit | Human Resources | Executive | Marketing |
|---|---|---|---|---|
| Dennis Anthony | $ - | $ 600 | $ 1,500 | $ - |
| Joe Reinart | 1,200 | - | 1,500 | - |
| Danny Detten | 900 | - | 300 | - |
| Trent Finck | - | 600 | 1,500 | - |
| Bryan Reinart | - | 600 | 300 | - |
| Myles Frische | 600 | - | 900 | - |
| Terry Sherrill | 1,200 | - | 900 | - |
| Dan McWhorter | - | - | - | - |
| | $ 3,900 | $ 1,800 | 6,900 | $ - |

The aggregate amount of reimbursement for travel, subsistence and other related expenses paid to directors and on their behalf was $61,175, $36,567 and $43,205 in 2012, 2011 and 2010, respectively.

## COMPENSATION OF SENIOR OFFICERS

**Compensation Discussion and Analysis – Overview**

The objective of the association's salary administration program is to attract, retain and motivate staff in a fair and uniform manner so the association may accomplish its mission and achieve its strategic goals. The program ensures fair and equitable compensation opportunities for those who hold positions of comparable responsibility, and it meets legal requirements in all compensation practices. Objective methods are used to measure the relative value of jobs, and salary grades and ranges are used that will position the association to be competitive in the marketplace. The Human Resources Committee of the board of directors and management utilize the services of the Human Resources Compensation Team at the Farm Credit Bank of Texas to compile Compensation Market Data annually that is used by the board and management in establishing salary and incentive levels. Data sources used include the Federal Reserve Bank of Dallas 11th District survey, Texas Community Bank survey (Independent Bankers Association of Texas), Watson Wyatt Financial Institution surveys, Mercer Financial Services Commercial Lending survey and CompData surveys. The Compensation Market Data reveal salary and incentive levels for similar sized institutions operating in our geographic area.

Eligible employees may be furnished a company-owned automobile for use in accordance with the association's vehicle policy. Employees who used their personal automobile for business purposes were reimbursed during 2012 at the IRS-approved rate.

Eligible, full-time association employees participated in an incentive plan in accordance with the 2012 Employee Incentive Plan Policy. The incentive program is contingent upon minimum association performance for 2012 based on various criteria. In addition to exceeding minimum ROA standards, the association must also pay patronage to stockholders, exceed benchmarks established under the Financial Institution Rating System (FIRS), comply with all terms of the general financing agreement with the bank, and receive acceptable internal and external audits. Available gross incentive amounts are determined based pretax earnings adjusted for extraordinary and nonrecurring income or expenses. Individual incentive amounts for various job positions are based on factors such as office earnings, credit quality and administration, loan growth and fee income generation, and business referrals.

Additionally, employees involved with the sale, collection and administration of crop, livestock and life insurance who did not have any delegated lending authority were eligible to participate in the Insurance Incentive Plan according to the 2012 Insurance Incentive Plan Policy. Available gross incentive amounts were computed based on total sales commissions received and net income for the insurance division during 2012. Incentives were determined by branch based upon duties within each branch office and based upon criteria such as growth, retention and business referrals. No incentive amount exceeded the 5 percent salary cap imposed by FCA regulations for any employee who is subject to the FCA salary cap.

Neither the CEO nor any other senior officer received noncash compensation exceeding $5,000 in 2012.

The board of directors and senior officers, including the CEO, are reimbursed for reasonable travel, subsistence and other related expenses while conducting association business. A copy of the association's travel policy is available to shareholders upon request but in general allows reimbursement for the following: Travel includes airplanes, buses, taxicabs, rental vehicles and personal vehicle use. Subsistence includes lodging, meals and incidentals which may include communication, valet, laundry and entertainment. All claims for reimbursement must be submitted on approved forms and approved by the CEO. Expenses reimbursed to the CEO are submitted to an executive committee member of the board of directors for approval.

**Chief Executive Officer (CEO) Compensation Table and Policy**

The CEO's salary is set by the board using the Compensation Market Data as a guideline to arrive at a fair and competitive salary. Annual incentive amounts awarded to the CEO are determined at the sole discretion of the board of directors using the Compensation Market Data as a guideline. Factors considered by the board in determining final incentive amounts for the CEO include personal performance evaluation, association performance related to the business plan, profitability, return on assets, credit quality, credit administration, capital adequacy, ability to pay patronage to members and overall management exhibited by the CEO. The association offers a nonqualified supplemental 401(k) plan to all employees who qualify. Through the plan the association may offer restored employer contributions, discretionary contributions or an eligible employee may make elective deferrals. In 2012, the association did not make any restored employer contributions or discretionary contribution to the CEO. The CEO is not working under a written employment agreement.

| Name of Individual | Year | Salary | Bonus | Change in Pension Value | Deferred/ Perquisite | Other* | Total |
|---|---|---|---|---|---|---|---|
| Tim McDonald, CEO | 2012 | $ 225,009 | $ 50,716 | $ 57,497 | $ - | $ 29,541 | $ 362,763 |
| Tim McDonald, CEO | 2011 | 199,508 | 95,000 | 76,510 | 10,500 | 31,926 | 413,444 |
| Tim McDonald, CEO | 2010 | 180,507 | 42,750 | 61,073 | 11,750 | 24,866 | 320,946 |

*Amounts in the "Other" column include contributions to 401(k), automobile benefits, life insurance and medical/dental premiums paid by the association.

**Pension Benefits Table for the CEO**

The following table presents the total annual benefit provided from the defined benefit pension plan applicable to the CEO for the year ended December 31, 2012:

| Name | Plan Name | Number of Years Credited Service | Present Value of Accumulated Benefit | Payments During 2012 |
|---|---|---|---|---|
| Tim McDonald | Farm Credit Bank of Texas Pension Plan | 24.302 | $ 688,130 | $ - |

Assumptions Used to Determine the Present Value of Accumulated Benefits

1. The present value of accumulated benefits is based on immediate retirement; otherwise, present value is based on a benefit payable at age 65.
2. The following ASC715 assumptions as of 12/31/2012 were used to determine the above present value:
    a. Discount rate of 4.15%
    b. Payment shown in the normal form (Qualified Joint and 50% Survivor Annuity assuming a spouse 2 years younger)
    c. Mortality based on the RP2000 combined healthy table with mortality improvements projected to 2024.
3. No termination, withdrawal, or disability is assumed before retirement age.

**Pension Benefits Table Narrative Disclosure for the CEO**

The CEO of the association participates in the Farm Credit of Texas Pension Plan (the "Pension Plan"), which is a qualified defined benefit retirement plan. Compensation, as defined in the Pension Plan, includes wages, incentive compensation, and deferrals to the 401(k) and flexible spending account plans, but excludes annual leave or sick leave that may be paid in cash at the time of termination, retirement, or transfer of employment, severance payments, retention bonuses, taxable fringe benefits, and any other payments. Pension Plan benefits are based on the average of monthly eligible compensation over the 60 consecutive months that produce the highest average after 1996 ("FAC60"). The Pension Plan's benefit formula for a Normal Retirement Pension is the sum of (a) 1.65 percent of FAC60 times "Years of Benefit Service" and (b) 0.50 percent of (i) FAC60 in excess of Social Security covered compensation items (ii) "Years of Benefit Service" (not to exceed 35). The present value of the CEO's accumulated Pension Plan is calculated assuming retirement had occurred at the measurement date used for financial reporting purposes with the retirement at age 65. The Pension Plan's benefit formula for the Normal Retirement Pension assumes that the CEO is married on the date the annuity begins, that the spouse is exactly two years younger than the CEO, and that the benefit is payable in the form of a 50 percent joint and survivor annuity. If any of those assumptions are incorrect, the benefit is recalculated to be the actuarial equivalent benefit.

**Compensation of Other Senior Officers**

Senior officer salaries are set by the CEO working in conjunction with the Human Resources Committee and utilizing Compensation Market Data. Annual incentive amounts awarded to senior officers are determined by the CEO working in conjunction with the Human Resources Committee and utilizing Compensation Market Data as a guideline. Factors considered in determining final incentive amounts for the senior officers varies according to their job but generally include personal performance evaluation, overall performance of their department, association financial performance, profitability, credit quality, credit administration, loan growth, fee income generation and the ability to pay patronage to members. The association offers a nonqualified supplemental 401(k) plan to all employees who qualify. Through the plan the association may offer restored employer contributions, discretionary contributions or an eligible employee may make elective deferrals. In 2012, the association did not make any restored employer contributions or discretionary contribution to any senior officer, and no senior officer elected to defer any of his/her salary or incentive. No senior officer is working under a written employment agreement.

The following table summarizes the compensation paid to senior officers of the association during 2012, 2011 and 2010. Amounts reflected in the table are presented in the year the compensation was earned.

| Name of Group | Year | Salary | Bonus | Change in Pension Value | Deferred/ Perquisite | Other* | Total |
|---|---|---|---|---|---|---|---|
| Aggregate No. of Senior Officers Excluding CEO | | | | | | | |
| (3) | 2012 | $ 426,566 | $ 121,877 | $ 41,006 | $ - | $ 75,263 | $ 664,712 |
| (3) | 2011 | 382,868 | 112,439 | 57,185 | - | 69,447 | 621,939 |
| (4) | 2010 | 469,833 | 92,356 | 80,220 | - | 86,310 | 728,719 |

*Amounts in the "Other" column include contributions to 401(k), defined contribution plans, automobile benefits, life insurance and medical/dental premiums paid by the association.

Disclosure of information on the total compensation paid and the arrangements of the compensation plans during the last fiscal year to any senior officer or to any other officer included in the aggregate are available and will be disclosed to shareholders of the institution upon request. Additionally, the Farm Credit Administration amended regulations during 2012, which impacted advisory votes on senior officer compensation. The new regulations require the association to hold an advisory vote on senior officer compensation when 5 percent of the voting stockholders petition for a vote. Stockholders may petition for an advisory vote on the compensation of the chief executive officer, the aggregate senior officer group, or both.

Total compensation earned by the five most highly paid officers (excluding the CEO) of the association, including incentives, was $1,028,989, $982,139 and $878,808 in 2012, 2011 and 2010, respectively. Incentives earned by such officers for 2012, 2011 and 2010 were $202,097, $202,524 and $120,956, respectively.

## TRANSACTIONS WITH DIRECTORS AND SENIOR OFFICERS

The association's policies on loans to and transactions with its officers and directors, required to be disclosed in this section, are incorporated herein by reference from Note 12 to the consolidated financial statements, "Related Party Transactions," included in this annual report.

## DIRECTORS' AND SENIOR OFFICERS' INVOLVEMENT IN CERTAIN LEGAL PROCEEDINGS

The association has no directors or senior officers with any involvement in certain legal proceedings as described in FCA regulation 620.5(k).

## RELATIONSHIP WITH INDEPENDENT AUDITOR

During 2012 the association's audit committee approved the engagement of a new financial auditor, PricewaterhouseCoopers, LLP. This was not the result of disagreement with the previous auditor; it aligns the association's financial auditor with the firm engaged by the bank and the Farm Credit System. Previously, the Audit Committee had engaged Simonton & Kutac, LLP located at 1010 Lamar Suite 850, Houston, TX 77002 to audit the association's consolidated financial statements. All financial audit, tax and SOX 404 testing services were approved by the association's audit committee. The total fees, by the category of services provided, paid during the reporting period to qualified public accountants were as follows.

| Simonton & Kutac, LLP | | PricewaterhouseCoopers, LLP | | Lam Vinson | |
|---|---|---|---|---|---|
| Financial Audit | $22,189 | Financial Audit | $45,500 | SOX 404 Testing | $11,763 |
| Tax | $12,475 | | | | |
| Other | $336 | | | | |

## FINANCIAL STATEMENTS

The financial statements, together with the report thereon of PricewaterhouseCoopers, LLP dated March 7, 2013, and the report of management in this annual report to stockholders are incorporated herein by reference.

## MEMBER/SHAREHOLDER PRIVACY

Members' nonpublic personal financial information is protected by Farm Credit Administration regulation. Our directors and employees are restricted from disclosing information not normally contained in published reports or press releases about the association or its members.

## CREDIT AND SERVICES TO YOUNG, BEGINNING AND SMALL FARMERS AND RANCHERS, AND PRODUCERS OR HARVESTERS OF AQUATIC PRODUCTS

The association is active in providing credit and other services to YBS operators throughout its 20-county territory, and its objective is to increase, in a sound and constructive way, services and penetration to this segment of producers by 5 percent of number and volume of loans. YBS operators are defined as farmers, ranchers, or producers or harvesters of aquatic products of which a "young" borrower is one who is 35 years or younger, a "beginning" borrower is one who has 10 years or less experience, and a "small" borrower is one who normally generates less than $250,000 in annual gross sales of agricultural or aquatic products.

At the end of 2012, 17.7 percent of all association loans (by number) were to "young" operators, 22.9 percent were to "beginning" borrowers and 25.3 percent were to "small" operators. On a combined basis, 56.3 percent of all loans were to "young," "beginning" or "small" borrowers.

Utilizing USDA-NASS 2007 ag census data and Farm Credit Bank of Texas Data Warehouse information as of June 30, 2012, the Farm Credit Bank of Texas has produced a report summarizing YBS demographic and penetration data for the association in its territory. Out of the 9,604 farmers within our 20-county territory, 500 (5.2 percent) are under age 35; 2,340 (24.4 percent) have been farming less than 10 years and 7,340 (76.4 percent) have gross sales of less than $250,000 annually. Within the same 20-county territory, the association has 577 customers, 94 (16.3 percent) of which are under age 35; 137 (23.7 percent) have been farming less than 10 years and 186 (32.2 percent) have gross sales of less than $250,000 annually.

Loan programs and procedures in place include the reduction of certain minimum lending (underwriting) standards for an applicant to qualify for a "young," "beginning" or "small" loan; utilization of governmental and Farmer Mac guarantees and loan programs; utilization of individual guarantees; and coordination with other lenders. In assessing operating plans of YBS operators and potential operators, association loan officers provide financial education and counseling inclusive of risk management practices. The association participates in outreach, educational and sponsorship programs to potentially attract new YBS borrowers and for the benefit of existing borrowers. They include contributions and participation in extension service education-oriented programs and organizations, and various youth group sponsorships.

## Independent Auditor's Report

To the Board of Directors and Members of
Great Plains Ag Credit, ACA:

We have audited the accompanying consolidated financial statements of Great Plains Ag Credit, ACA and its subsidiaries (the Association), which comprise the consolidated balance sheets as of December 31, 2012, 2011 and 2010, and the related consolidated statements of comprehensive income, of changes in members' equity and of 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.

### *Auditor's 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 Great Plains Ag Credit, ACA and its subsidiaries at December 31, 2012, 2011 and 2010, 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.

### *Other Matter*

The consolidated financial statements of the Association as of December 31, 2011 and 2010 and for the years then ended were audited by other auditors whose report dated February 23, 2012, and February 22, 2011 expressed an unqualified opinion on those statements.

PricewaterhouseCoopers LLP

March 7, 2013

*PricewaterhouseCoopers LLP, 300 West 6th Street, Suite 1800, Austin, Texas 78701*
*T: (512) 477-1300, F: (512) 477-8681, www.pwc.com/us*

## GREAT PLAINS AG CREDIT, ACA

## CONSOLIDATED BALANCE SHEETS

| | December 31, | | |
|---|---|---|---|
| | **2012** | 2011 | 2010 |
| **Assets** | | | |
| Cash | **$ 35,415** | $ 33,385 | $ 26,499 |
| Investments | **3,304,296** | 5,424,993 | 7,403,693 |
| Loans | **500,213,066** | 432,166,853 | 404,272,031 |
| Less: allowance for loan losses | **(1,129,817)** | (691,893) | (1,188,958) |
| Net loans | **499,083,249** | 431,474,960 | 403,083,073 |
| Accrued interest receivable | **5,314,976** | 4,581,465 | 4,493,742 |
| Investment in the Farm Credit Bank of Texas | **7,792,945** | 7,010,000 | 6,777,870 |
| Receivables from the Farm Credit Bank of Texas | **6,194,863** | 6,829,530 | 5,089,514 |
| Premises and equipment | **2,957,082** | 2,933,966 | 2,286,799 |
| Deferred taxes, net | **900,692** | 698,054 | 806,051 |
| Other assets | **1,234,036** | 1,165,376 | 1,012,185 |
| Total assets | **$ 526,817,554** | $ 460,151,729 | $ 430,979,426 |
| **Liabilities** | | | |
| Note payable to the Farm Credit Bank of Texas | **$ 426,001,870** | $ 370,853,835 | $ 350,486,462 |
| Advance conditional payments | **8,419,143** | 7,294,100 | 7,517,294 |
| Accrued interest payable | **591,228** | 610,926 | 595,330 |
| Accrued postretirement benefit liability | **2,450,613** | 2,106,501 | 2,100,269 |
| Patronage distributions payable | **3,418,139** | 3,217,340 | 2,763,106 |
| Other liabilities | **6,418,005** | 4,163,047 | 2,247,825 |
| Total liabilities | **447,298,998** | 388,245,749 | 365,710,286 |
| **Members' Equity** | | | |
| Capital stock and participation certificates | **1,027,810** | 1,018,495 | 985,565 |
| Allocated retained earnings | **12,472,438** | 11,829,485 | 11,098,871 |
| Unallocated retained earnings | **66,116,080** | 58,901,344 | 53,027,144 |
| Accumulated other comprehensive income (loss) | **(97,772)** | 156,656 | 157,560 |
| Total members' equity | **79,518,556** | 71,905,980 | 65,269,140 |
| Total liabilities and members' equity | **$ 526,817,554** | $ 460,151,729 | $ 430,979,426 |

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

**GREAT PLAINS AG CREDIT, ACA**

**CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME**

| | Year Ended December 31, | | |
|---|---|---|---|
| | **2012** | 2011 | 2010 |
| **Interest Income** | | | |
| Loans | **$ 20,445,143** | $ 18,795,554 | $ 18,242,724 |
| Investments | **273,330** | 365,602 | 289,268 |
| Total interest income | **20,718,473** | 19,161,156 | 18,531,992 |
| **Interest Expense** | | | |
| Note payable to the Farm Credit Bank of Texas | **6,897,987** | 7,006,626 | 7,307,547 |
| Advance conditional payments | **12,536** | 10,956 | 13,477 |
| Other | **2,534** | 6,176 | 9,840 |
| Total interest expense | **6,913,057** | 7,023,758 | 7,330,864 |
| Net interest income | **13,805,416** | 12,137,398 | 11,201,128 |
| (Provision for) reversal of Loan Losses | **(1,461,647)** | 467,577 | (14,720) |
| Net interest income after provision for losses | **12,343,769** | 12,604,975 | 11,186,408 |
| **Noninterest Income** | | | |
| Patronage Income | **4,764,995** | 3,992,214 | 3,801,269 |
| Fees for financially related services | **1,367,033** | 1,322,861 | 844,574 |
| Other | **1,116,172** | 347,490 | 1,209,548 |
| Total noninterest income | **7,248,200** | 5,662,565 | 5,855,391 |
| **Noninterest Expenses** | | | |
| Salaries and employee benefits | **4,871,049** | 5,041,879 | 4,851,736 |
| Directors' expense | **168,176** | 128,392 | 137,459 |
| Purchased services | **308,707** | 170,297 | 260,917 |
| Travel | **364,160** | 285,335 | 266,593 |
| Cost of space occupied | **241,390** | 264,832 | 195,838 |
| Office | **206,100** | 192,497 | 173,671 |
| Data Processing | **165,283** | 146,206 | 240,930 |
| Advertising | **119,346** | 123,990 | 139,048 |
| FCSIC insurance premiums | **202,502** | 219,242 | 173,694 |
| Farmer Mac Fees | **296,584** | 205,513 | 251,935 |
| Public and member relations | **242,772** | 131,800 | 148,252 |
| Federally regulated examination fees | **153,955** | 149,841 | 146,882 |
| Other noninterest expense | **221,728** | 216,870 | 155,400 |
| Total noninterest expenses | **7,561,752** | 7,276,694 | 7,142,355 |
| Income before income taxes | **12,030,217** | 10,990,846 | 9,899,444 |
| Provision for income taxes | **34,744** | 153,102 | 501,401 |
| **NET INCOME** | **11,995,473** | 10,837,744 | 9,398,043 |
| Other comprehensive income/(loss): | | | |
| Change in postretirement benefit plans | **(254,428)** | (904) | (208,908) |
| **COMPREHENSIVE INCOME/(LOSS)** | **$ 11,741,045** | $ 10,836,840 | $ 9,189,135 |

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

**GREAT PLAINS AG CREDIT, ACA**

**CONSOLIDATED STATEMENTS OF CHANGES IN MEMBERS' EQUITY**

| | Capital Stock/ Participation Certificates | Additional Paid-in-Capital | Retained Earnings | | Accumulated Other Comprehensive Income (Loss) | Total Members' Equity |
|---|---|---|---|---|---|---|
| | | | Allocated | Unallocated | | |
| Balance at December 31, 2009 | $ 970,315 | $ - | $ 10,089,937 | $ 48,053,222 | $ 366,468 | $ 59,479,942 |
| Comprehensive income | - | - | - | 9,398,043 | (208,908) | 9,189,135 |
| Capital stock/participation certificates issued | 158,385 | - | - | - | - | 158,385 |
| Capital stock/participation certificates and allocated retained earnings retired | (143,135) | - | - | - | - | (143,135) |
| Patronage refnds: | | | | | | |
| Allocatee retained ernings | - | - | 1,661,192 | (1,661,192) | - | - |
| Paid/declared payable | - | - | (652,258) | (2,762,929) | - | (3,415,187) |
| Balance at December 31, 2010 | 985,565 | - | 11,098,871 | 53,027,144 | 157,560 | 65,269,140 |
| Comprehensive income | - | - | - | 10,837,744 | (904) | 10,836,840 |
| Capital stock/participation certificates issued | 134,690 | - | - | - | - | 134,690 |
| Capital stock/participation certificates and allocated retained earnings retired | (101,760) | - | - | - | - | (101,760) |
| Patronage dividends: | | | | | | |
| Allocatee retained ernings | - | - | 1,746,360 | (1,746,360) | - | - |
| Paid/declared payable | - | - | (1,015,746) | (3,217,184) | - | (4,232,930) |
| Balance at December 31, 2011 | 1,018,495 | - | 11,829,485 | 58,901,344 | 156,656 | 71,905,980 |
| Comprehensive income/(loss) | - | - | - | 11,995,473 | (254,428) | 11,741,045 |
| Capital stock/participation certificates issued | 196,345 | - | - | - | - | 196,345 |
| Capital stock/participation certificates and allocated retained earnings retired | (187,030) | - | - | - | - | (187,030) |
| Patronage dividends: | | | | | | |
| Allocated retained earnings | - | - | 1,362,745 | (1,362,745) | - | - |
| Paid/declared payable | - | - | (719,792) | (3,417,992) | - | (4,137,784) |
| **Balance at December 31, 2012** | **$ 1,027,810** | **$ -** | **$ 12,472,438** | **$ 66,116,080** | **$ (97,772)** | **$ 79,518,556** |

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

**GREAT PLAINS AG CREDIT, ACA**

**CONSOLIDATED STATEMENTS OF CASH FLOWS**

| | Year Ended December 31, | | |
|---|---|---|---|
| | **2012** | 2011 | 2010 |
| **Cash flows from operating activities:** | | | |
| Net income | **$ 11,995,473** | $ 10,837,744 | $ 9,398,043 |
| Adjustments to reconcile net income to net cash provided by operating activities: | | | |
| Provision for loan losses or (loan loss reversal) | **447,031** | (467,577) | 14,720 |
| Depreciation | **250,715** | 193,462 | 183,182 |
| Gain on sale of premises and equipment, net | **(33,566)** | (29,665) | (85,030) |
| (Increase) decrease in accrued interest receivable | **(733,511)** | (87,723) | 724,831 |
| Decrease in other receivables from the Farm Credit Bank of Texas | **634,667** | - | - |
| (Increase) decrease in deferred tax assets | **(202,638)** | 100,429 | 195,670 |
| Increase in other assets | **(68,660)** | (1,893,207) | (11,406) |
| (Decrease) increase in accrued interest payable | **(19,698)** | 15,596 | (63,913) |
| Increase in other liabilities | **2,335,448** | 1,898,254 | 381,442 |
| Net cash provided by operating activities | **14,605,261** | 10,567,313 | 10,737,539 |
| **Cash flows from investing activities:** | | | |
| Increase in loans, net | **(68,046,213)** | (27,894,822) | (12,782,505) |
| Cash recoveries of loans previously charged off | **87** | 377 | 147 |
| Proceeds from redemtion (purchase) of investment in the Farm Credit Bank of Texas | **(782,945)** | (232,130) | 433,250 |
| Decrease in Investments, net | **2,120,697** | 1,978,700 | 231,472 |
| Purchases of premises and equipment | **(296,679)** | (845,964) | (536,979) |
| Proceeds from sales of premises and equipment | **56,414** | 35,000 | 88,966 |
| Net cash used in investing activities | **(66,948,639)** | (26,958,839) | (12,565,649) |

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

## CONSOLIDATED STATEMENTS OF CASH FLOWS

| | Year Ended December 31, | | |
|---|---|---|---|
| | **2012** | 2011 | 2010 |
| **Cash flows from financing activities:** | | | |
| Net draws on note payable to the Farm Credit Bank of Texas | **55,148,035** | 20,367,373 | 5,421,705 |
| Increase (decrease) in advance conditional payments | **1,125,043** | (223,194) | (880,255) |
| Issuance of capital stock and participation certificates | **196,345** | 134,690 | 158,385 |
| Retirement of capital stock and participation certificates | **(187,030)** | (101,760) | (143,135) |
| Cash dividends paid | **(3,936,985)** | - | - |
| Patronage distributions paid | **-** | (3,778,697) | (2,740,246) |
| Net cash provided by financing activities | **52,345,408** | 16,398,412 | 1,816,454 |
| Net increase (decrease) in cash | **2,030** | 6,886 | (11,656) |
| Cash at the beginning of the year | **33,385** | 26,499 | 38,155 |
| Cash at the end of the year | **$ 35,415** | $ 33,385 | $ 26,499 |
| | | | |
| **Supplemental schedule of noncash investing and financing activities:** | | | |
| Loans exchanged for agricultural mortgage-backed securities | **-** | - | 7,635,165 |
| Loans charged off | **1,014,616** | - | - |
| Patronage distributions declared | **3,417,992** | 3,217,184 | 2,762,929 |
| Transfer of allowance for loan losses from (into) reserve for unfunded commitments | **(9,195)** | (29,865) | (178,628) |
| | | | |
| **Supplemental cash information:** | | | |
| Cash paid during the year for: | | | |
| Interest | **$ 6,932,755** | $ 7,008,162 | $ 7,394,777 |
| Income taxes | **-** | 230,000 | 331,000 |

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

## NOTE 1 — ORGANIZATION AND OPERATIONS:

**Organization:** Great Plains Ag Credit, ACA, including its wholly-owned subsidiaries, Great Plains Ag Credit, PCA and Great Plains Ag Credit, FLCA (collectively called "the association"), is a member-owned cooperative which provides credit and credit-related services to, or for the benefit of, eligible borrowers/stockholders for qualified agricultural purposes in the west 20 counties in the Panhandle and South Plains of the state of Texas.

The association is a lending institution of the Farm Credit System (System), a nationwide system of cooperatively owned banks and associations that was established by Acts of Congress to meet the credit needs of American agriculture and is subject to the provisions of the Farm Credit Act of 1971, as amended (Act). At December 31, 2012, the System consisted of three Farm Credit Banks (FCBs) and their affiliated associations, one Agricultural Credit Bank (ACB) and its affiliated associations, the Federal Farm Credit Banks Funding Corporation (Funding Corporation), and various service and other organizations.

The Farm Credit Bank of Texas (bank) and its related associations are collectively referred to as the "district." The bank provides funding to all associations within the district and is responsible for supervising certain activities of the district associations. At December 31, 2012, the district consisted of the bank, one FLCA and 16 ACA parent companies, which have two wholly-owned subsidiaries, an FLCA and a PCA, operating in or servicing the states of Alabama, Louisiana, Mississippi, New Mexico and Texas. ACA parent companies provide financing and related services through their FLCA and PCA subsidiaries. The FLCA makes secured long-term agricultural real estate and rural home mortgage loans. The PCA makes short- and intermediate-term loans for agricultural production or operating purposes.

The Farm Credit Administration (FCA) is delegated authority by Congress to regulate the System banks and associations. The FCA examines the activities of System associations to ensure their compliance with the Farm Credit Act, FCA regulations, and safe and sound banking practices.

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

FCA regulations require borrower information to be held in strict confidence by Farm Credit institutions, their directors, officers and employees. Directors and employees of the Farm Credit institutions are prohibited, except under specified circumstances, from disclosing nonpublic personal information about members.

**Operations:** The Act sets forth the types of authorized lending activity, persons eligible to borrow and financial services that can be offered by the association. The association is authorized to provide, either directly or in participation with other lenders, credit, credit commitments and related services to eligible borrowers. Eligible borrowers include farmers, ranchers, producers or harvesters of aquatic products, rural residents and farm-related businesses. The association makes and services short- and intermediate-term loans for agricultural production or operating purposes, and secured long-term real estate mortgage loans, with funding from the bank.

The association also serves as an intermediary in offering credit life insurance, multiperil crop insurance, crop hail insurance and livestock insurance to members.

The association's financial condition may be affected by factors that affect the bank. The financial condition and results of operations of the bank may materially affect stockholders' investments in the association. Upon request, stockholders of the association will be provided with the Farm Credit Bank of Texas and District Associations' Annual Report to Stockholders, which

includes the combined financial statements of the bank and all of the district associations. The district's annual report discusses the material aspects of the financial condition, changes in financial condition, and results of operations for the bank and the district. In addition, the district's annual report identifies favorable and unfavorable trends, significant events, uncertainties and the impact of activities of the Insurance Fund.

The lending and financial services offered by the bank are described in Note 1, "Organization and Operations," of the district's annual report to stockholders.

**NOTE 2 — SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES:**

The accounting and reporting policies of the association conform to accounting principles generally accepted in the United States of America (GAAP) and prevailing practices within the banking industry. The preparation of consolidated financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the amounts reported in the consolidated financial statements and accompanying notes. Significant estimates are discussed in these footnotes, as applicable. Actual results could differ from those estimates. Certain amounts in prior years' consolidated financial statements have been reclassified to conform to current financial statement presentation. The consolidated financial statements include the accounts of Great Plains Ag Credit, PCA and Great Plains Ag Credit, FLCA. All significant intercompany transactions have been eliminated in consolidation.

A. Recently Issued or Adopted Accounting Pronouncements:

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

   In September 2011, the FASB issued guidance titled "Compensation – Retirement Benefits – Multiemployer Plans." The guidance is intended to provide more information about an employer's financial obligations to a multiemployer pension plan, which should help financial statement users better understand the financial health of significant plans in which the employer participates. The additional disclosures include: a) a description of the nature of plan benefits, b) a qualitative description of the extent to which the employer could be responsible for the obligations of the plan, including benefits earned by employees during employment with another employer, and c) other quantitative information to help users understand the financial information about the plan. The amendments are effective for annual periods for fiscal years ending after December 15, 2012, for nonpublic entities. The amendments should be applied retrospectively for all prior periods presented. The adoption did not impact the association's financial condition or results of operations.

   In June and December 2011, the FASB issued guidance titled "Comprehensive Income – Presentation of Comprehensive Income." This guidance is intended to increase the prominence of other comprehensive income in financial statements. The main provisions of the guidance provide that an entity that reports items of other comprehensive income has the option to present comprehensive income in either one or two consecutive financial statements. This guidance did not change the items that must be reported in other comprehensive income. With either approach, an entity is required to present reclassification adjustments for items reclassified from other comprehensive income to net income in the statement(s). The December 2011 guidance deferred the effective date for the presentation of reclassification adjustments.

   This guidance is applied retrospectively and is effective for fiscal years, and interim periods within those years, beginning after December 15, 2011. The adoption of this guidance did not impact financial condition or results of operations, but resulted in changes to the presentation of comprehensive income.

B. Cash and Cash Equivalents: Cash and cash equivalents, as included in the statement of cash flows, represent cash on hand and on deposit at local banks.

C. Investment Securities: The association's investments include mortgage-backed securities issued by Federal Agricultural Mortgage Corporation (Farmer Mac) for which the association has the intent and ability to hold to maturity and which are

consequently classified as held-to-maturity. Held-to-maturity investments are carried at cost, adjusted for the amortization of premiums and accretion of discounts. Changes in the fair value of these investments are not recorded unless the investment is deemed to be other-than-temporarily impaired. Impairment is considered to be other-than-temporary if the present value of cash flows expected to be collected from the debt security is less than the amortized cost basis of the security (any such shortfall is referred to as a "credit loss"). If an entity intends to sell an impaired debt security or is more likely than not to be required to sell the security before recovery of its amortized cost basis less any current-period credit loss, the impairment is other-than-temporary and should be recognized currently in earnings in an amount equal to the entire difference between fair value and amortized cost. If a credit loss exists, but an entity does not intend to sell the impaired debt security and is not more likely than not to be required to sell before recovery, the impairment is other-than-temporary and should be separated into (i) the estimated amount relating to credit loss and (ii) the amount relating to all other factors. Only the estimated credit loss amount is recognized currently in earnings, with the remainder of the loss amount recognized in other comprehensive income.

D. Loans and Allowance for Loan Losses: Long-term real estate mortgage loans generally have original maturities ranging from five to 20 years. Substantially all short- and intermediate-term loans for agricultural production or operating purposes have maturities of 10 years or less. Loans are carried at their principal amount outstanding adjusted for charge-offs and deferred loan fees or costs. Interest on loans is accrued and credited to interest income based upon the daily principal amount outstanding. Authoritative accounting guidance requires loan origination fees and direct loan origination costs, if material, to be capitalized and the net fee or cost to be amortized over the life of the related loan as an adjustment to yield.

Impaired loans are loans for which it is probable that not all principal and interest will be collected according to the contractual terms of the loan and are generally considered substandard or doubtful, which is in accordance with the loan rating model, as described below. Impaired loans include nonaccrual loans, restructured loans, and loans past due 90 days or more and still accruing interest. A loan is considered contractually past due when any principal repayment or interest payment required by the loan instrument is not received on or before the due date. A loan shall remain contractually past due until it is formally restructured or until the entire amount past due, including principal, accrued interest and penalty interest incurred as a result of past-due status, is collected or otherwise discharged in full.

Impaired loans are generally placed in nonaccrual status when principal or interest is delinquent for 90 days (unless adequately secured and in the process of collection) or circumstances indicate that collection of principal and/or interest is in doubt. Additionally, all loans over 180 days past due are placed in nonaccrual status. When a loan is placed in nonaccrual status, accrued interest deemed uncollectible is either reversed (if accrued in the current year) or charged against the allowance for loan losses (if accrued in prior years). Loans are charged off at the time they are determined to be uncollectible.

A restructured loan constitutes a troubled debt restructuring if for economic or legal reasons related to the debtor's financial difficulties the association grants a concession to the debtor that it would not otherwise consider. A concession is generally granted in order to minimize the association's economic loss and avoid foreclosure. Concessions vary by program and are borrower-specific and may include interest rate reductions, term extensions, payment deferrals or the acceptance of additional collateral in lieu of payments. In limited circumstances, principal may be forgiven. A loan restricted in a troubled debt restructuring is an impaired loan.

Payments received on nonaccrual loans are generally applied to the recorded investment in the loan asset. If collection of the recorded investment in the loan is fully expected and the loan does not have a remaining unrecovered prior charge-off associated with it, the interest portion of payments is recognized as current interest income. Nonaccrual loans may be returned to accrual status when principal and interest are current, the borrower has demonstrated payment performance, there are no unrecovered prior charge-offs, and collection of future payments is no longer in doubt. If previously unrecognized interest income exists at the time the loan is transferred to accrual status, cash received at the time of or subsequent to the transfer is first recorded as interest income until such time as the recorded balance equals the contractual indebtedness of the borrower.

The bank and related associations use a two-dimensional loan rating model based on an internally generated combined system risk-rating guidance that incorporates a 14-point risk-rating scale to identify and track the probability of borrower default and a separate scale addressing loss given default over a period of time. Probability of default is the probability that a borrower will experience a default within 12 months from the date of the determination of the risk rating. A default is considered to have occurred if the lender believes the borrower will not be able to pay its obligation in full or the borrower is past due more than 90 days. The loss given default is management's estimate as to the anticipated economic loss on a specific loan, assuming default has occurred or is expected to occur within the next 12 months.

Each of the probability of default categories carries a distinct percentage of default probability. The 14-point risk-rating scale provides for granularity of the probability of default, especially in the acceptable ratings. There are nine acceptable categories

that range from a borrower of the highest quality to a borrower of minimally acceptable quality. The probability of default between 1 and 9 is very narrow and would reflect almost no default to a minimal default percentage. The probability of default grows more rapidly as a loan moves from a "9" to other assets especially mentioned (OAEM) and grows significantly as a loan moves to a substandard (viable) level. A substandard (nonviable) rating indicates that the probability of default is almost certain.

The credit risk-rating methodology is a key component of the association's allowance for loan losses evaluation, and is generally incorporated into its loan underwriting standards and internal lending limit. The allowance for loan losses is maintained at a level considered adequate by management to provide for probable losses inherent in the loan portfolio. The allowance is based on a periodic evaluation of the loan portfolio by management in which numerous factors are considered, including economic conditions, loan portfolio composition, collateral value, portfolio quality, current production conditions and economic conditions, and prior loan loss experience. The allowance for loan losses encompasses various judgments, evaluations and appraisals with respect to the loans and their underlying security that, by their nature, contain elements of uncertainty and imprecision. Changes in the agricultural economy and their impact on borrower repayment capacity will cause these various judgments, evaluations and appraisals to change over time. Accordingly, actual circumstances could vary significantly from the institutions' expectations and predictions of those circumstances.

The allowance for loan losses includes components for loans individually evaluated for impairment and loans collectively evaluated for impairment. Generally, for loans individually evaluated the allowance for loan losses represents the difference between the recorded investment in the loan and the present value of the cash flows expected to be collected discounted at the loan's effective interest rate, or at the fair value of the collateral, less estimated costs to sell, if the loan is collateral-dependent. For those loans collectively evaluated for impairment, the allowance for loan losses is determined using the risk-rating model.

E. Capital Stock Investment in the Farm Credit Bank of Texas: The association's investment in the bank is in the form of Class A voting capital stock and allocated retained earnings. This investment is adjusted periodically based on the association's proportional utilization of the bank compared to other district associations. The bank requires a minimum stock investment of 2 percent of the association's average borrowing from the bank. This investment is carried at cost plus allocated equities in the accompanying consolidated balance sheet.

   If needed to meet regulatory capital adequacy requirements, the board of directors of the bank may increase the percentage of stock held by an association from 2 percent of the average outstanding balance of borrowings from the bank to a maximum of 5 percent of the average outstanding balance of borrowings from the bank.

F. Premises and Equipment: Premises and equipment are carried at cost less accumulated depreciation. Land is carried at cost. Depreciation is provided on the straight-line method using estimated useful lives of the assets. Gains and losses on dispositions are reflected in current operations. Maintenance and repairs are charged to operating expense, and improvements are capitalized.

G. Advance Conditional Payments: The association is authorized under the Act to accept advance payments from borrowers. To the extent that the borrower's access to such funds is restricted, the advance conditional payments are netted against the borrower's related loan balance. Amounts in excess of the related loan balance and amounts to which the borrower has unrestricted access are presented as liabilities in the accompanying consolidated balance sheet. Advance conditional payments are not insured. Interest is generally paid by the association on such accounts at rates established by the board of directors.

H. Employee Benefit Plans: Employees of the association participate in either the district defined benefit retirement plan (DB Plan) or the defined contribution plan (DC Plan). All eligible employees may participate in the Farm Credit Benefits Alliance 401(k) Plan. Also, the association sponsors a nonqualified defined contribution 401(k) plan. The DB Plan is closed to new participants. Participants generally include employees hired prior to January 1, 1996. The DB Plan is noncontributory and provides benefits based on salary and years of service. The "projected unit credit" actuarial method is used for financial reporting and funding purposes for the DB Plan.

   Participants in the DC Plan generally include employees who elected to transfer from the DB Plan prior to January 1, 1996, and employees hired on or after January 1, 1996. Participants in the DC Plan direct the placement of their employers' contributions, 5.0 percent of eligible pay for the year ended December 31, 2012, made on their behalf into various investment alternatives.

   The structure of the district's DB Plan is characterized as multiemployer, since neither the assets, liabilities nor costs of the plan are segregated or separately accounted for by the associations. No portion of any surplus assets is available to the

associations, nor are the associations required to pay for plan liabilities upon withdrawal from the plans. As a result, the associations recognize as pension cost the required contribution to the plans for the year. Contributions due and unpaid are recognized as a liability. The association recognized pension costs for the DC Plan of $140,989, $120,439 and $103,763 for the years ended December 31, 2012, 2011 and 2010, respectively. For the DB Plan, the association recognized pension costs of $430,776, $795,513 and $600,566 for the years ended December 31, 2012, 2011 and 2010, respectively.

The association also participates in the Farm Credit Benefits Alliance 401(k) Plan, which requires the associations to match 100 percent of employee contributions up to 3.0 percent of eligible earnings and to match 50 percent of employee contributions for the next 2.0 percent of employee contributions, up to a maximum employer contribution of 4.0 percent of eligible earnings. Association 401(k) plan costs are expensed as incurred. The association's contributions to the 401(k) plan were $138,927, $125,956 and $120,079 for the years ended December 31, 2012, 2011 and 2010, respectively.

In addition to pension benefits, the association provides certain health care and life insurance benefits to qualifying retired employees (other postretirement benefits). These benefits are not characterized as multiemployer and, consequently, the liability for these benefits is included in other liabilities.

I. Income Taxes: The ACA holding company conducts its business activities through two wholly-owned subsidiaries. Long-term mortgage lending activities are operated through the wholly-owned FLCA subsidiary, which is exempt from federal and state income tax. Short- and intermediate-term lending activities are operated through the wholly-owned PCA subsidiary. Operating expenses are allocated to each subsidiary based on estimated relative service. All significant transactions between the subsidiaries and the parent company have been eliminated in consolidation. The ACA, along with the PCA subsidiary, is subject to income tax. The association is eligible to operate as a cooperative that qualifies for tax treatment under Subchapter T of the Internal Revenue Code. Accordingly, under specified conditions, the association can exclude from taxable income amounts distributed as qualified patronage refunds in the form of cash, stock or allocated retained earnings. Provisions for income taxes are made only on those earnings that will not be distributed as qualified patronage refunds. Deferred taxes are provided on the association's taxable income on the basis of a proportionate share of the tax effect of temporary differences not allocated in patronage form. A valuation allowance is provided against deferred tax assets to the extent that it is more likely than not (over 50 percent probability), based on management's estimate, that they will not be realized. The consideration of valuation allowances involves various estimates and assumptions as to future taxable earnings, including the effects of the association's expected patronage program, which reduces taxable earnings.

J. Patronage Refunds From the Farm Credit Bank of Texas: The association records patronage refunds from the bank on an accrual basis.

K. Fair Value Measurement: The FASB guidance defines fair value, establishes a framework for measuring fair value and expands disclosures about fair value measurements. It describes three levels of inputs that may be used to measure fair value:

Level 1 — Quoted prices in active markets for identical assets or liabilities that the reporting entity has the ability to access at the measurement date. Level 1 assets and liabilities include debt and equity securities and derivative contracts that are traded in an active exchange market, as well as certain U.S. Treasury, other U.S. government and agency mortgage-backed debt securities that are highly liquid and are actively traded in over-the-counter markets. Also included in Level 1 are assets held in trust funds, which relate to deferred compensation and our supplemental retirement plan. The trust funds include investments that are actively traded and have quoted net asset values that are observable in the marketplace. Pension plan assets that are invested in equity securities, including mutual funds and fixed-income securities that are actively traded, are also included in Level 1.

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 the following: (a) quoted prices for similar assets or liabilities in active markets; (b) 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, the prices are not current or principal market information is not released publicly; (c) inputs other than quoted prices that are observable such as interest rates and yield curves, prepayment speeds, credit risks and default rates; and (d) inputs derived principally from or corroborated by observable market data by correlation or other means. This category generally includes certain U.S. government and agency mortgage-backed debt securities, corporate debt securities, and derivative contracts. Pension plan assets that are derived from observable inputs, including corporate bonds and mortgage-backed securities, are reported in Level 2.

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 are considered Level 3. These unobservable inputs reflect the reporting entity's own assumptions 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. This category generally includes certain private equity investments, retained residual interests in securitizations, asset-backed securities, highly structured or long-term derivative contracts, certain loans and other property owned. Pension plan assets such as certain mortgage-backed securities that are supported by little or no market data in determining the fair value are included in Level 3.

The fair value disclosures are presented in Note 13, "Fair Value Measurements."

L. Off-balance-sheet credit exposures: Commitments to extend credit are agreements to lend to customers, generally having fixed expiration dates or other termination clauses that may require payment of a fee. Commercial letters of credit are conditional commitments issued to guarantee the performance of a customer to a third party. These letters of credit are issued to facilitate commerce and typically result in the commitment being funded when the underlying transaction is consummated between the customer and third party. The credit risk associated with commitments to extend credit and commercial letters of credit is essentially the same as that involved with extending loans to customers and is subject to normal credit policies. Collateral may be obtained based on management's assessment of the customer's creditworthiness.

## NOTE 3 — INVESTMENT SECURITIES:

Effective April 1, 2010, $7,635,135 of agricultural mortgage loans previously covered under a Long-Term Standby Commitment to Purchase agreement with the Federal Agricultural Mortgage Corporation (Farmer Mac) were securitized. No gain or loss was recognized in the financial statements upon completion of the securitization. Terms of the agreement call for a guarantee fee of 20-50 basis points to be paid to Farmer Mac, and for the association to receive a 30-basis-point fee for servicing the underlying loans.

The following is a summary of Farmer Mac agricultural mortgage-backed securities:

| | **December 31, 2012** | | | | |
|---|---|---|---|---|---|
| | **Amortized Cost** | **Gross Unrealized Gains** | **Gross Unrealized Losses** | **Fair Value** | **Weighted Average Yield** |
| Agricultural mortgage-backed securities | **$ 3,304,296** | **$ 69,600** | **$ -** | **$ 3,373,896** | **5.94 %** |

| | December 31, 2011 | | | | |
|---|---|---|---|---|---|
| | Amortized Cost | Gross Unrealized Gains | Gross Unrealized Losses | Fair Value | Weighted Average Yield |
| Agricultural mortgage-backed securities | $ 5,424,993 | $ 130,055 | $ - | $ 5,555,348 | 6.15 % |

| | December 31, 2010 | | | | |
|---|---|---|---|---|---|
| | Amortized Cost | Gross Unrealized Gains | Gross Unrealized Losses | Fair Value | Weighted Average Yield |
| Agricultural mortgage-backed securities | $ 7,403,693 | $ 3,739 | $ - | $ 7,407,432 | 5.56 % |

**NOTE 4 — LOANS AND ALLOWANCE FOR LOAN LOSSES:**

A summary of loans as of December 31 follows:

| Loan Type | 2012 Amount | 2012 % | 2011 Amount | 2011 % | 2010 Amount | 2010 % |
|---|---|---|---|---|---|---|
| Real estate mortgage | **$ 258,748,010** | **51.7%** | $ 212,993,729 | 49.3% | $ 181,769,172 | 45.0% |
| Production and intermediate term | **218,132,582** | **43.6%** | 197,088,324 | 45.6% | 193,422,892 | 47.8% |
| Agribusiness: | | | | | | |
| Loans to cooperatives | **637,341** | **0.1%** | 560,400 | 0.1% | 2,786,780 | 0.7% |
| Processing and marketing | **11,070,240** | **2.2%** | 14,580,077 | 3.4% | 15,516,988 | 3.8% |
| Farm-related business | **10,799,955** | **2.2%** | 5,958,337 | 1.4% | 9,740,720 | 2.4% |
| Rural residential real estate | **702,769** | **0.2%** | 768,021 | 0.2% | 1,035,479 | 0.3% |
| Lease receivables | **122,169** | **0.0%** | 217,965 | 0.0% | - | 0.0% |
| Total | **$ 500,213,066** | **100%** | $ 432,166,853 | 100% | $ 404,272,031 | 100% |

The association may purchase or sell participation interests with other parties in order to diversify risk, manage loan volume and comply with Farm Credit Administration regulations. The following table presents information regarding participations purchased and sold as of December 31, 2012:

| | Other Farm Credit Institutions | | Non-Farm Credit Institutions | | Total | |
|---|---|---|---|---|---|---|
| | Participations Purchased | Participations Sold | Participations Purchased | Participations Sold | Participations Purchased | Participations Sold |
| Real estate mortgage | $ 26,484,643 | $ 68,159,288 | $ - | $ - | $ 26,484,643 | $ 68,159,288 |
| Production and intermediate term | 12,539,849 | 496,778,298 | 10,656,670 | - | 23,196,519 | 496,778,298 |
| Agribusiness | 10,050,358 | 805,348 | - | - | 10,050,358 | 805,348 |
| Total | $ 49,074,850 | $ 565,742,934 | $ 10,656,670 | $ - | $ 59,731,520 | $565,742,934 |

Geographic Distribution

| County | **2012** | 2011 | 2010 |
|---|---|---|---|
| Armstrong | **0.6%** | 0.3% | 0.4% |
| Bailey | **0.8%** | 0.9% | 1.1% |
| Briscoe | **0.3%** | 0.3% | 0.2% |
| Carson | **1.0%** | 0.5% | 0.6% |
| Castro | **12.5%** | 10.1% | 7.9% |
| Dallam | **10.7%** | 10.1% | 11.0% |
| Deaf Smith | **5.0%** | 5.6% | 6.9% |
| Floyd | **2.7%** | 1.2% | 1.4% |
| Hale | **4.3%** | 4.2% | 4.4% |
| Hansford | **3.4%** | 3.9% | 5.2% |
| Hartley | **5.2%** | 6.0% | 2.5% |
| Hutchinson | **1.4%** | 0.8% | 1.1% |
| Lamb | **4.3%** | 3.2% | 3.3% |
| Moore | **6.4%** | 10.5% | 8.3% |
| Oldham | **0.6%** | 0.4% | 0.6% |
| Parmer | **6.9%** | 7.1% | 8.6% |
| Potter | **2.4%** | 3.1% | 3.0% |
| Randall | **2.9%** | 3.9% | 4.8% |
| Sherman | **3.7%** | 4.2% | 4.6% |
| Swisher | **1.7%** | 1.4% | 1.2% |
| Other Counties | **7.0%** | 6.6% | 10.7% |
| Other States | **16.2%** | 15.7% | 12.2% |
| Total | **100.0%** | **100.0%** | **100.0%** |

The association's concentration of credit risk in various agricultural commodities is shown in the following table. While the amounts represent the association's maximum potential credit risk as it relates to recorded loan principal, a substantial portion of

the association's lending activities is collateralized, and the association's exposure to credit loss associated with lending activities is reduced accordingly. An estimate of the association's credit risk exposure is considered in the determination of the allowance for loan losses.

| Operation/Commodity | **2012** Amount | **2012** % | 2011 Amount | 2011 % | 2010 Amount | 2010 % |
|---|---|---|---|---|---|---|
| Livestock, except dairy and poultry | **$ 172,962,335** | **34.6%** | $ 159,308,498 | 36.9% | $ 148,446,076 | 36.7% |
| Cash grains | **100,583,092** | **20.1%** | 63,771,888 | 14.8% | 50,171,576 | 12.4% |
| General farms, primarily crops | **86,837,076** | **17.4%** | 83,131,654 | 19.2% | 71,354,543 | 17.7% |
| Dairy farms | **68,706,223** | **13.7%** | 59,680,532 | 13.8% | 57,646,055 | 14.3% |
| General farms, primarily livestock | **22,242,370** | **4.5%** | 19,922,207 | 4.6% | 22,393,381 | 5.5% |
| Field crops except cash grains | **18,793,780** | **3.8%** | 14,255,433 | 3.3% | 11,463,815 | 2.8% |
| Crop Services | **7,133,129** | **1.4%** | 11,752,832 | 2.7% | 6,544,665 | 1.6% |
| Timber tracts | **6,052,042** | **1.2%** | 6,192,042 | 1.4% | 6,332,042 | 1.6% |
| Meat products | **5,845,911** | **1.2%** | 3,872,495 | 0.9% | 8,216,798 | 2.0% |
| Lessors of real property | **4,163,936** | **0.8%** | 3,140,779 | 0.7% | 4,205,271 | 1.0% |
| Farm product warehousing & storage | **699,430** | **0.1%** | 698,713 | 0.2% | 6,767,799 | 1.7% |
| All other commodities | **6,193,742** | **1.2%** | 6,439,780 | 1.5% | 10,730,010 | 2.7% |
| Total | **$ 500,213,066** | **100.0%** | $ 432,166,853 | 100.0% | $ 404,272,031 | 100.0% |

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

To mitigate the risk of loan losses, the association has obtained loan guarantees in the form of standby commitments to purchase qualifying loans from Farmer Mac through an arrangement with the bank. The agreements, which will remain in place until the loans are paid in full, give the association the right to sell the loans identified in the agreements to Farmer Mac in the event of defaults (typically four months past due), subject to certain conditions. At December 31, 2012, 2011 and 2010, loans totaling $55,193,940, $51,051,858 and $32,371,220, respectively, were guaranteed by these commitments. Fees paid for these guarantees totaled $296,584, $205,513 and $251,935 in 2012, 2011 and 2010, respectively, and are included in noninterest expense.

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

| | **December 31, 2012** | December 31, 2011 | December 31, 2010 |
|---|---|---|---|
| **Nonaccrual loans:** | | | |
| Real estate mortgage | **$ 7,964,886** | $ 15,736,377 | $ 15,864,454 |
| Production and intermediate term | **2,360,562** | 3,570,346 | 3,855,836 |
| Total nonaccrual loans | **10,325,448** | 19,306,723 | 19,720,290 |
| **Accruing restructured loans:** | | | |
| Real estate mortgage | **7,182,452** | - | - |
| Production and intermediate term | **1,372,039** | - | - |
| Total accruing restructured loans | **8,554,491** | - | - |
| Total nonperforming loans | **18,879,939** | 19,306,723 | 19,720,290 |

One credit quality indicator utilized by the bank and association is the Farm Credit Administration's Uniform Loan Classification System that categorizes loans into five categories. The 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.

The following table shows loans and related accrued interest classified under the Farm Credit Administration's Uniform Loan Classification System as a percentage of total loans and related accrued interest receivable by loan type as of December 31:

| | **2012** | 2011 | 2010 |
|---|---|---|---|
| Real estate mortgage | | | |
| Acceptable | **93.7%** | 96.2% | 86.9% |
| OAEM | **3.2%** | 0.0% | 8.4% |
| Substandard/doubtful | **3.1%** | 3.8% | 4.7% |
| | **100.0%** | 100.0% | 100.0% |
| Production and intermediate term | | | |
| Acceptable | **92.8%** | 98.2% | 88.7% |
| OAEM | **1.1%** | 0.0% | 6.3% |
| Substandard/doubtful | **6.1%** | 1.8% | 5.0% |
| | **100.0%** | 100.0% | 100.0% |
| Loans to cooperatives | | | |
| Acceptable | **100.0%** | 100.0% | 100.0% |
| OAEM | **0.0%** | 0.0% | 0.0% |
| Substandard/doubtful | **0.0%** | 0.0% | 0.0% |
| | **100.0%** | 100.0% | 100.0% |
| Processing and marketing | | | |
| Acceptable | **87.3%** | 87.1% | 79.4% |
| OAEM | **12.7%** | 12.9% | 20.6% |
| Substandard/doubtful | **0.0%** | 0.0% | 0.0% |
| | **100.0%** | 100.0% | 100.0% |
| Farm-related business | | | |
| Acceptable | **100.0%** | 100.0% | 100.0% |
| OAEM | **0.0%** | 0.0% | 0.0% |
| Substandard/doubtful | **0.0%** | 0.0% | 0.0% |
| | **100.0%** | 100.0% | 100.0% |
| Rural residential real estate | | | |
| Acceptable | **100.0%** | 100.0% | 71.8% |
| OAEM | **0.0%** | 0.0% | 28.2% |
| Substandard/doubtful | **0.0%** | 0.0% | 0.0% |
| | **100.0%** | 100.0% | 100.0% |
| Lease receivables | | | |
| Acceptable | **100.0%** | 100.0% | 100.0% |
| OAEM | **0.0%** | 0.0% | 0.0% |
| Substandard/doubtful | **0.0%** | 0.0% | 0.0% |
| | **100.0%** | 100.0% | 100.0% |
| Total Loans | | | |
| Acceptable | **93.3%** | 96.9% | 87.8% |
| OAEM | **2.4%** | 0.4% | 7.7% |
| Substandard/doubtful | **4.3%** | 2.7% | 4.5% |
| | **100.0%** | 100.0% | 100.0% |

The following tables provide an age analysis of past due loans (including accrued interest) as of December 31, 2012 and 2011:

| December 31, 2012: | 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 | $ - | $ 7,964,886 | $ 7,964,886 | $ 254,462,148 | $ 262,427,034 | $ - |
| Production and intermediate-term | 740,301 | 2,277,166 | 3,017,467 | 216,589,314 | 219,606,781 | - |
| Loans to cooperatives | - | - | - | 662,727 | 662,727 | - |
| Processing and marketing | - | - | - | 11,069,167 | 11,069,167 | - |
| Farm-related business | - | - | - | 10,860,261 | 10,860,261 | - |
| Rural residential real estate | - | - | - | 705,671 | 705,671 | - |
| Lease receivables | - | - | - | 122,366 | 122,366 | - |
| Total | $ 740,301 | $ 10,242,052 | $ 10,982,353 | $ 494,471,654 | $ 505,454,007 | $ - |

| December 31, 2011: | 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 | $ - | $ 7,708,905 | $ 7,708,905 | $ 208,170,168 | $ 215,879,073 | $ - |
| Production and intermediate-term | 275,851 | 2,103,645 | 2,379,496 | 196,051,837 | 198,431,333 | - |
| Loans to cooperatives | - | - | - | 588,972 | 588,972 | - |
| Processing and marketing | - | - | - | 14,628,258 | 14,628,258 | - |
| Farm-related business | - | - | - | 6,022,658 | 6,022,658 | - |
| Rural residential real estate | 87,343 | - | 87,343 | 690,496 | 777,839 | - |
| Lease receivables | - | - | - | 222,160 | 222,160 | - |
| Total | $ 363,194 | $ 9,812,550 | $ 10,175,744 | $ 426,374,549 | $ 436,550,293 | $ - |

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 the investment.

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.

As of December 31, 2012, the total recorded investment of troubled debt restructured loans was $18,246,882, including $9,692,391 classified as nonaccrual and $8,554,491 classified as accrual, with no related specific allowance for loan losses. As of December 31, 2012, there were no commitments to lend additional funds to borrowers whose loan terms have been modified in a troubled debt restructuring.

The following tables present additional information regarding troubled debt restructurings, which includes both accrual and nonaccrual loans with troubled debt restructuring designation, that occurred during the years ended December 31, 2012, and December 31, 2011. The pre-modification outstanding recorded investment represents the recorded investment of the loans as of the quarter end prior to the restructuring. The post-modification outstanding recorded investment represents the recorded investment of the loans as of the quarter end the restructuring occurred.

| December 31, 2012: | Pre-modification Outstanding Recorded Investment | Post-modification Outstanding Recorded Investment |
|---|---|---|
| Troubled debt restructurings: | | |
| Real estate mortgage | $ 7,708,905 | $ 7,708,905 |
| Production and intermediate term | 2,054,338 | 2,054,338 |
| Total | $ 9,763,243 | $ 9,763,243 |

| December 31, 2011: | Pre-modification Outstanding Recorded Investment | Post-modification Outstanding Recorded Investment |
|---|---|---|
| Troubled debt restructurings: | | |
| Real estate mortgage | $ 7,725,588 | $ 7,725,588 |
| Production and intermediate term | 1,466,701 | 1,466,701 |
| Total | $ 9,192,289 | $ 9,192,289 |

In restructurings where principal is forgiven, the amount of the forgiveness is immediately charged off. In restructurings where accrued interest is forgiven, the interest is reversed (if current year interest) or charged off (if prior year interest). There have been no charge-offs or interest reversals recorded associated with modifications on troubled debt restructurings.

The predominate 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 the association assesses all of the modified terms to determine whether the overall modification qualifies as a troubled debt restructuring.

The following table presents information regarding loans that met the accounting criteria as a troubled debt restructuring and that occurred within the previous 12 months of that year and for which there was a 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.

| Troubled debt restructurings that subsequently defaulted: | **Recorded Investment at December 31, 2012** | Recorded Investment at December 31, 2011 |
|---|---|---|
| Real estate mortgage | **$ 7,638,886** | $ - |
| Production and intermediate term | **2,053,505** | - |
| Total | **$ 9,692,391** | $ - |

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 on Nonaccrual Status* | |
|---|---|---|---|---|
| | December 31, 2012 | December 31, 2011 | December 31, 2012 | December 31, 2011 |
| Troubled debt restructurings: | | | | |
| Real estate mortgage | $ 14,821,338 | $ 7,725,588 | $ 7,638,886 | $ 7,725,588 |
| Production and intermediate term | 3,425,544 | 1,466,701 | 2,053,505 | 1,466,701 |
| Total | $ 18,246,882 | $ 9,192,289 | $ 9,692,391 | $ 9,192,289 |

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

Additional impaired loan information is as follows:

| | Recorded Investment at 12/31/2012 | Unpaid Principal Balance[a] | Related Allowance | Average Impaired Loans | Interest Income Recognized |
|---|---|---|---|---|---|
| Impaired loans with a related allowance for credit losses: | | | | | |
| Real estate mortgage | $ 326,000 | $ 363,378 | $ 47,962 | $ 94,699 | $ 15,046 |
| Production and intermediate term | 223,661 | 1,192,226 | 62,183 | 252,712 | 56,842 |
| Total | $ 549,661 | $ 1,555,604 | $ 110,145 | $ 347,411 | $ 71,888 |
| Impaired loans with no related allowance for credit losses: | | | | | |
| Real estate mortgage | $ 14,821,337 | $ 14,821,337 | $ - | $ 15,010,310 | $ 480,787 |
| Production and intermediate term | 3,508,941 | 3,517,614 | - | 3,449,479 | 96,793 |
| Total | $ 18,330,278 | $ 18,338,951 | $ - | $ 18,459,789 | $ 577,580 |
| Total impaired loans: | | | | | |
| Real estate mortgage | $ 15,147,337 | $ 15,184,715 | $ 47,962 | $ 15,105,009 | $ 495,833 |
| Production and intermediate term | 3,732,602 | 4,709,840 | 62,183 | 3,702,191 | 153,635 |
| Total | $ 18,879,939 | $ 19,894,555 | $ 110,145 | $ 18,807,200 | $ 649,468 |

[a] Unpaid principal balance represents the recorded principal balance of the loan.

There were no material commitments to lend additional funds to debtors whose loans were classified as impaired at December 31, 2012.

Interest income on nonaccrual and accruing restructured loans that would have been recognized under the original terms of the loans at December 31:

| | **2012** | 2011 | 2010 |
|---|---|---|---|
| Interest income which would have been recognized under the original terms | **$ 1,164,436** | $ 1,352,078 | $ 826,741 |
| Less: interest income recognized | **(649,468)** | (365,944) | - |
| Foregone interest income | **$ 514,968** | $ 986,134 | $ 826,741 |

A summary of the changes in the allowance for credit losses and the ending balance of loans outstanding are as follows:

| | Real Estate Mortgage | Production and Intermediate Term | Agribusiness | Rural Residential Real Estate | Lease Receivable | Total |
|---|---|---|---|---|---|---|
| **Allowance for Credit Losses:** | | | | | | |
| Balance at December 31, 2011 | $ 210,528 | $ 432,267 | $ 45,247 | $ 1,100 | $ 2,751 | $ 691,893 |
| Charge-offs | (37,378) | (977,238) | - | - | - | (1,014,616) |
| Recoveries | - | 87 | - | - | - | 87 |
| Provision for loan losses | 194,014 | 1,256,411 | 12,198 | (100) | (876) | 1,461,647 |
| Other | 2,161 | (10,811) | (544) | - | - | (9,194) |
| Balance at December 31, 2012 | $ 369,325 | $ 700,716 | $ 56,901 | $ 1,000 | $ 1,875 | $ 1,129,817 |
| Ending Balance: individually evaluated for impairment | $ 47,962 | $ 62,183 | $ - | $ - | $ - | $ 110,145 |
| Ending Balance: collectively evaluated for impairment | $ 321,363 | $ 638,535 | $ 56,901 | $ 1,000 | $ 1,874 | $ 1,019,673 |
| Ending Balance: loans acquired with deteriorated credit quality | $ - | $ - | $ - | $ - | $ - | $ - |
| **Recorded Investment in Loans Outstanding:** | | | | | | |
| Ending Balance at December 31, 2012 | $ 262,331,492 | $219,606,781 | $ 22,624,196 | $ 705,671 | $122,366 | $505,390,506 |
| Ending balance for loans individually evaluated for impairment | $ 15,285,331 | $ 3,758,647 | $ - | $ - | $ - | $ 19,043,978 |
| Ending balance for loans collectively evaluated for impairment | $ 247,046,161 | $215,848,134 | $ 22,624,196 | $ 705,671 | $122,366 | $486,346,528 |
| Ending balance for loans acquired with deteriorated credit quality | $ - | $ - | $ - | $ - | $ - | $ - |

A summary of the allowance for loan losses as of December 31 follows:

| | 2012 | 2011 |
|---|---|---|
| Beginning balance | $ 691,893 | $ 1,188,958 |
| Provision for loan losses | 1,461,647 | (467,577) |
| Loans charged off | (1,014,616) | - |
| Recoveries | 87 | 377 |
| Other | (9,194) | (29,865) |
| Allowance for loan losses | $ 1,129,817 | $ 691,893 |

**NOTE 5 — INVESTMENT IN THE FARM CREDIT BANK OF TEXAS**

The investment in the Farm Credit Bank of Texas is a requirement of borrowing from the bank and is carried at cost plus allocated equities, not fair value, in the accompanying balance sheet. Estimating the fair value of the association's investment in the Farm Credit Bank of Texas is not practicable because the stock is not traded. The association owns 3.64 percent of the issued stock of the

bank as of December 31, 2012. As of that date, the bank's assets totaled $15.4 billion and members' equity totaled $1.274 billion. The bank's earnings were $174.6 million during 2012.

**NOTE 6 — PREMISES AND EQUIPMENT:**

Premises and equipment consisted of the following at December 31:

| | **2012** | 2011 | 2010 |
|---|---|---|---|
| Land and improvements | **$ 665,806** | $ 647,582 | $ 392,582 |
| Building and improvements | **2,271,350** | 2,271,350 | 1,912,176 |
| Furniture and equipment | **377,774** | 357,393 | 311,574 |
| Computer equipment and software | **208,412** | 197,914 | 176,222 |
| Automobiles | **629,761** | 540,776 | 519,062 |
| Construction in progress | **-** | - | - |
| | **4,153,103** | 4,015,015 | 3,311,616 |
| Accumulated depreciation | **(1,196,021)** | (1,081,049) | (1,024,817) |
| Total | **$ 2,957,082** | $ 2,933,966 | $ 2,286,799 |

The association leases office space in Amarillo and Muleshoe. Lease expense was $29,558, $30,800 and $16,100 for 2012, 2011 and 2010, respectively. Minimum annual lease payments for the next five years are as follows:

| | Operating |
|---|---|
| 2013 | $ 32,812 |
| 2014 | 13,500 |
| 2015 | 6,750 |
| 2016 | 0 |
| 2017 | 0 |
| Thereafter | 0 |
| Total | $ 53,062 |

**NOTE 7 — OTHER ASSETS AND OTHER LIABILITIES:**

Other assets comprised the following at December 31:

| | **2012** | 2011 | 2010 |
|---|---|---|---|
| Intangible | **$ 594,721** | $ 528,250 | $ 540,750 |
| Accounts receivable | **228,114** | 190,868 | 189,882 |
| Equity investments in other Farm Credit entities | **216,376** | 102,361 | 95,504 |
| Other assets | **194,825** | 343,897 | 186,049 |
| Total | **$ 1,234,036** | $ 1,165,376 | $ 1,012,185 |

Other liabilities comprised the following at December 31:

| | **2012** | 2011 | 2010 |
|---|---|---|---|
| Loan drafts outstanding | **$ 5,513,815** | $ 3,027,459 | $ 645,368 |
| Reserve for unfunded credit commitments | **217,686** | 208,492 | 178,627 |
| Accrued annual leave | **208,638** | 208,527 | 212,797 |
| Other liabilities | **477,866** | 718,569 | 1,211,033 |
| Total | **$ 6,418,005** | $ 4,163,047 | $ 2,247,825 |

**NOTE 8 — NOTE PAYABLE TO THE BANK:**

The interest rate risk inherent in the association's loan portfolio is substantially mitigated through the funding relationship with the bank. The bank manages interest rate risk through its direct loan pricing and asset/liability management process. The association's indebtedness to the bank represents borrowings by the association to fund the majority of its loan portfolio. The indebtedness is collateralized by a pledge of substantially all of the association's assets, and is governed by a general financing agreement. The

interest rate on the direct loan is based upon the bank's cost of funding the loans the association has outstanding to its borrowers. The indebtedness continues in effect until the expiration date of the general financing agreement, which is September 30, 2015, unless sooner terminated by the bank upon the occurrence of an event of default, or by the association, in the event of a breach of this agreement by the bank, upon giving the bank 30 calendar days prior written notice, or in all other circumstances, upon giving the bank 120 days prior written notice.

The total amount and the weighted average interest rate of the association's direct loan from the bank at December 31, 2012, 2011 and 2010, was $426,001,870 at 1.58 percent, $370,853,835 at 2.21 percent and $350,486,462 at 1.89 percent, respectively.

Under the Act, the association is obligated to borrow only from the bank unless the bank approves borrowing from other funding sources. The bank and FCA regulations have established limitations on the association's ability to borrow funds based on specified factors or formulas relating primarily to credit quality and financial condition. At December 31, 2012, 2011 and 2010, the association's note payable was within the specified limitations. The maximum amount the association may borrow from the bank as of December 31, 2012, was $494,928,071, as defined by the general financing agreement.

In addition to borrowing limits, the financing agreement establishes certain covenants including limits on leases, investments, other debt, and dividend and patronage distributions; minimum standards for return on assets and for liquidity; and provisions for conducting business, maintaining records, reporting financial information, and establishing policies and procedures. Remedies specified in the general financing agreement associated with the covenants include additional reporting requirements, development of action plans, increases in interest rates on indebtedness, reduction of lending limits or repayment of indebtedness. As of and for the years ended December 31, 2012, 2011 and 2010, the association was not subject to remedies associated with the covenants in the general financing agreement.

**NOTE 9 — MEMBERS' EQUITY:**

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

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

In accordance with the Act and the association's capitalization bylaws, each borrower is required to invest in the association as a condition of borrowing. The investment in Class B capital stock (for agricultural loans), or participation certificates (for rural home and farm related business loans) is equal to 2 percent of the loan amount, up to a maximum amount of $1,000. The borrower acquires ownership of the capital stock or participation certificates at the time the loan is made, usually by adding the aggregate par value of the capital stock or participation certificates to the principal amount of the related loan obligation. The capital stock or participation certificates are subject to a first lien by the association. Retirement of such equities will generally be at the lower of par or book value, and repayment of a loan does not automatically result in retirement of the corresponding capital stock or participation certificates.

If needed to meet regulatory capital adequacy requirements, the board of directors of the association may increase the percentage of stock requirement for each borrower up to a maximum of 10 percent of the loan amount.

Each owner of Class B capital stock is entitled to a single vote, while class A capital stock and participation certificates provide no voting rights to their owners.

Within two years of repayment of a loan, the association capital bylaws require the conversion of any borrower's outstanding Class B capital stock to Class A stock. Class A stock has no voting rights except in a case where a new issuance of preferred stock has been submitted to stockholders affected by the preference. Redemption of all stock and participation certificates is made solely at the discretion of the association's board of directors.

All borrower stock is at-risk. As such, losses that result in impairment of capital stock or participation certificates shall be borne on a pro rata basis by all holders of Class B and Class A capital stock and participation certificates. In the event of liquidation of the association, capital stock and participation certificates would be utilized as necessary to satisfy any remaining obligations in excess of the amounts realized on the sale or liquidation of assets. Any excess of the amounts realized on the sale or liquidation of assets over the association's obligations to external parties and to the bank would be distributed to the association's stockholders.

Dividends and patronage distributions may be paid on the capital stock and participation certificates of the association, as the board of directors may determine by resolution, subject to capitalization requirements as defined by the FCA. Amounts not distributed are retained as unallocated retained earnings. In 2012, 2011 and 2010, the association declared patronage distributions of $4,780,737, $4,963,544 and $4,424,121, respectively. Cash payments from the prior years' earnings were made of $3,217,184, $2,762,929 and $2,087,980; and additional payments to retire prior years' allocated surplus were made of $719,792, $1,015,746, and $652,258.

The FCA's capital adequacy regulations require the association to achieve permanent capital and total surplus of at least 7.0 percent and core surplus of at least 3.5 percent of risk-adjusted assets and off-balance-sheet commitments. Failure to meet the ratio requirements can initiate certain mandatory and possibly additional discretionary actions by the FCA that, if undertaken, could have a direct material effect on the association's financial statements. The association is prohibited from reducing permanent capital by retiring stock or making certain other distributions to stockholders unless prescribed capital standards are met. As of December 31, 2012, the association is not prohibited from retiring stock or distributing earnings; furthermore, neither the board nor senior management knows of any such prohibitions that may apply during the subsequent fiscal year. The association's permanent capital ratio, core surplus ratio and total surplus ratio at December 31, 2012, were 14.9 percent, 12.3 percent and 13.9 percent, respectively.

As part of the association's financial planning process, the association maintains a written capital adequacy plan. In conjunction with this plan, the association's board and management are charged with managing the association's capital position to provide for long-term profitability and concurrence with regulatory requirements. The association's capital planning process incorporates a number of financial performance objectives, and takes into consideration factors such as fluctuations in the rate environment, capital calls by the bank on the association, sharing of bank equities and fluctuations in volume growth. For 2012, the association established its total surplus ratio objective of 12 to 13 percent.

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

At December 31, the association had the following shares of Class A capital stock, Class B stock and participation certificates outstanding at a par value of $5 per share:

| | **2012** | 2011 | 2010 |
|---|---|---|---|
| Class A stock | **222** | 224 | 224 |
| Class B stock | **202,546** | 200,151 | 192,283 |
| Participation certificates | **2,794** | 3,324 | 4,606 |
| Total | **205,562** | 203,699 | 197,113 |

An additional component of equity is accumulated other comprehensive income (loss), which is reported net of taxes totaling ($97,772), $156,656, and $157,560 as of December 2012, 2011 and 2010, respectively.

**NOTE 10 — INCOME TAXES:**

The provision for (benefit from) income taxes follows for the years ended December 31:

| | **2012** | 2011 | 2010 |
|---|---|---|---|
| Current | **$ 159,207** | $ 52,673 | $ 305,731 |
| Deferred | **(124,463)** | 100,429 | 195,670 |
| Total provision for (benefit from) income taxes | **34,744** | 153,102 | 501,401 |

The provision for (benefit from) income tax differs from the amount of income tax determined by applying the applicable U.S. statutory federal income tax rate to pretax income as follows for the years ended December 31:

| | **2012** | 2011 | 2010 |
|---|---|---|---|
| Federal tax at statutory rate | **$ 4,090,274** | $ 3,736,888 | $ 3,365,811 |
| Effect of nontaxable FLCA subsidiary | **(2,410,977)** | (1,989,210) | (1,442,680) |
| Patronage distributions | **(1,625,451)** | (1,687,605) | (1,504,201) |
| Other | **(19,102)** | 93,029 | 82,471 |
| Provision for (benefit from) income taxes | **$ 34,744** | $ 153,102 | $ 501,401 |

Deferred tax assets and liabilities in accordance with accounting guidance, "Accounting for Income Taxes," are comprised of the following at December 31:

| | **2012** | 2011 | 2010 |
|---|---|---|---|
| Deferred Tax Assets | | | |
| Allowance for credit losses | **$ 305,352** | $ 186,472 | $ 207,332 |
| Postretirement benefits, other | **580,567** | 543,759 | 582,612 |
| Enhanced retirement program | **44,370** | 46,580 | 48,790 |
| Gross deferred tax assets | **930,290** | 776,811 | 838,734 |
| Deferred tax asset valuation allowance | **-** | - | - |
| Deferred Tax Liabilities | | | |
| Capitalization of net loan origination expenses | **(29,598)** | (78,757) | (32,683) |
| Gross deferred tax liabilities | **(29,598)** | (78,757) | (32,683) |
| Net deferred tax asset (liability) | **$ 900,691** | $ 698,054 | $ 806,051 |

The calculation of tax assets and liabilities involves various management estimates and assumptions as to the future taxable earnings. At December 31, 2012, nonpatronage income is expected to be approximately 20.5 percent of total taxable income (before patronage), and patronage income retained is expected to be 50 percent of total patronage income on a tax basis. The expected future tax rates are based upon enacted tax laws.

## NOTE 11 — EMPLOYEE BENEFIT PLANS:

**Employee Retirement Plans:** Employees of the association participate in either the defined benefit retirement plan (DB Plan) or the defined contributions plan (DC Plan) and are eligible to participate in the Farm Credit Benefits Alliance 401(k) Plan. Also, the association sponsors a nonqualified defined contribution 401(k) plan. These plans are described more fully in section H of Note 2, "Summary of Significant Accounting Policies." The structure of the district's DB Plan is characterized as multiemployer, since neither the assets, liabilities nor cost of any plan is segregated or separately accounted for by participating employers (bank and associations). No portion of any surplus assets is available to any participating employer. As a result, participating employers of the plan only recognize as cost the required contributions for the period and a liability for any unpaid contributions required for the period of their financial statements. Plan obligations, assets and the components of annual benefit expenses are recorded and reported upon district combination only. The association records current contributions to the DB Plan as an expense in the current year.

The DB Plan is noncontributory and benefits are based on salary and years of service. The legal name of the plan is Farm Credit Bank of Texas Pension Plan; its employer identification number is 74-1110170. The DB Plan is not subject to any contractual expiration dates. The DB Plan's funding policy is to fund current year benefits expected to be earned by covered employees plus an amount to improve the accumulated benefit obligation funded status by a percentage approved by the plan sponsor. The plan sponsor is the board of the Farm Credit Bank of Texas. The "projected unit credit" actuarial method is used for both financial reporting and funding purposes. District employers have the option of providing enhanced retirement benefits, under certain conditions, within the DB Plan, to facilitate reorganization and/or restructuring. Actuarial information regarding the DB pension plan accumulated benefit obligation and plan asset is calculated for the district as a whole and is presented in the district's Annual Report to Stockholders. The actuarial present value of vested and nonvested accumulated benefit obligation exceeded the net assets of the DB Plan as of December 31, 2012.

The risks of participating in these multiemployer plans are different from single-employer plans in the following aspects:

a. Assets contributed to the multiemployer plan by one employer may be used to provide benefits to employees of other participating employers.
b. If a participating employer stops contributing to the plan, the unfunded obligations of the plan may be borne by the remaining participating employers.
c. If the association chooses to stop participating in some of its multiemployer plans, it may be required to pay the plan an amount based on the underfunded status of the plan, referred to as a withdrawal liability.

The following table includes additional information regarding the funded status of the plan, the association's contributions, and the percentage of association contribution to total plan contributions for the years ended December 31, 2012, 2011 and 2010:

| | **2012** | 2011 | 2010 |
|---|---|---|---|
| Funded status of plan | **65.0%** | 64.9% | 71.6% |
| Association's contribution | **$ 430,776** | $ 795,513 | $ 600,566 |
| Percentage of association's contribution to total contributions | **2.7%** | 3.5% | 3.0% |

The funded status presented above is based on the percentage of plan assets to projected benefit obligations. DB Plan funding is based on the percentage of plan assets to the accumulated benefit obligation, which was 72.7 percent, 72.6 percent and 78.8 percent at December 31, 2012, 2011 and 2010, respectively.

**Other Postretirement Benefits:** In addition to pension benefits, the association provides certain health care benefits to qualifying retired employees (other postretirement benefits). These benefits are not characterized as multiemployer and, consequently, the liability for these benefits is included in other liabilities.

In September 2006, the FASB issued guidance, which required the recognition of the overfunded or underfunded status of pension and other postretirement benefit plans on the balance sheet. The balance sheet recognition provisions of this guidance were adopted at December 31, 2007. The guidance also required that employers measure the benefit obligation and plan assets as of the fiscal year end for fiscal years ending after December 15, 2008. In fiscal 2007 and earlier, the System used a September 30 measurement date for pension and other postretirement benefit plans. The guidance provided two approaches for an employer to transition to a fiscal year-end measurement date. The System has applied the second approach, which allows for the use of the measurements determined for the prior year end.

Under this alternative, pension and postretirement benefit income measured for the three-month period October 1, 2007, to December 31, 2007, (determined using the September 2007 measurement date) was recorded as an adjustment to beginning 2008 retained earnings. As a result, the association decreased retained earnings by $9,261, net of taxes, and increased the pension and other postretirement benefit liabilities by $14,032.

The following table reflects the benefit obligation, cost and actuarial assumptions for the association's other postretirement benefits:

**Retiree Welfare Benefit Plans**

| **Disclosure Information Related to Retirement Benefits** | **2012** | 2011 | 2010 |
|---|---|---|---|
| **Change in Accumulated Postretirement Benefit Obligation** | | | |
| Accumulated postretirement benefit obligation, beginning of year | **$ 2,106,502** | $ 2,100,269 | $ 1,813,535 |
| Service cost | **58,108** | 59,063 | 46,984 |
| Interest cost | **105,410** | 117,687 | 107,546 |
| Plan participants' contributions | **15,827** | 20,500 | 6,797 |
| Plan amendments | **-** | - | - |
| Special termination benefits | **-** | - | - |
| Actuarial loss (gain) | **256,690** | (87,446) | 193,760 |
| Benefits paid | **(91,924)** | (103,572) | (68,353) |
| Accumulated postretirement benefit obligation, end of year | **$ 2,450,613** | $ 2,106,501 | $ 2,100,269 |
| **Change in Plan Assets** | | | |
| Plan assets at fair value, beginning of year | **$ -** | $ - | $ - |
| Actual return on plan assets | **-** | - | - |
| Company contributions | **76,097** | 83,072 | 61,556 |
| Plan participants' contributions | **15,827** | 20,500 | 6,797 |
| Benefits paid | **(91,924)** | (103,572) | (68,353) |
| Plan assets at fair value, end of year | **$ -** | $ - | $ - |
| Funded status of the plan | **$ (2,450,613)** | $ (2,106,501) | $ (2,100,269) |
| **Amounts Recognized in the Balance Sheet** | | | |
| Other liabilities | **$ (2,450,613)** | $ (2,106,501) | $ (2,100,269) |
| **Amounts Recognized in Accumulated Other Comprehensive Income** | | | |
| Net actuarial loss (gain) | **$ 412,212** | $ 155,522 | $ 246,569 |
| Prior service cost (credit) | **(288,323)** | (362,028) | (448,829) |
| Net transition obligation (asset) | **-** | - | - |
| Total | **$ 123,889** | $ (206,506) | $ (202,260) |
| **Weighted-Average Assumptions Used to Determine Obligations at Year End** | | | |
| Measurement date | **12/31/2012** | 12/31/2011 | 12/31/2010 |
| Discount rate | **4.40%** | 5.10% | 5.70% |
| Health care cost trend rate assumed for next year (pre-/post-65) - medical | **7.25%/6.50%** | 8.50%/6.75% | 7.50%/6.50% |
| Health care cost trend rate assumed for next year - Rx | **7.25%** | 8.00% | 10.00% |
| Ultimate health care cost trend rate | **5.00%** | 5.00% | 5.00% |
| Year that the rate reaches the ultimate trend rate | **2023** | 2018 | 2017 |

| **Total Cost** | | **2012** | | 2011 | | 2010 |
|---|---|---|---|---|---|---|
| Service cost | **$** | **58,108** | $ | 59,063 | $ | 46,984 |
| Interest cost | | **105,410** | | 117,688 | | 107,546 |
| Expected return on plan assets | | **-** | | - | | - |
| Amortization of: | | | | | | |
| Unrecognized net transition obligation (asset) | | **-** | | - | | - |
| Unrecognized prior service cost | | **(73,705)** | | (86,801) | | (89,239) |
| Unrecognized net loss (gain) | | **-** | | 3,601 | | - |
| Net postretirement benefit cost | **$** | **89,813** | $ | 93,551 | $ | 65,291 |
| Accounting for settlements/curtailments/special termination benefits | **$** | **-** | $ | - | $ | - |
| **Other Changes in Plan Assets and Projected Benefit Obligation Recognized in Other Comprehensive Income** | | | | | | |
| Net actuarial loss (gain) | **$** | **256,690** | $ | (87,446) | $ | 193,760 |
| Amortization of net actuarial loss (gain) | | **-** | | (3,601) | | - |
| Prior service cost (credit) | | **-** | | - | | - |
| Amortization of prior service cost | | **73,705** | | 86,801 | | 89,239 |
| Recognition of prior service cost | | **-** | | - | | - |
| Amortization of transition liability (asset) | | **-** | | - | | - |
| Total recognized in other comprehensive income | **$** | **330,395** | $ | (4,246) | $ | 282,999 |
| **AOCI Amounts Expected to be Amortized Into Expense in 2013** | | | | | | |
| Unrecognized net transition obligation (asset) | **$** | **-** | $ | - | $ | - |
| Unrecognized prior service cost | | **(51,061)** | | (73,705) | | - |
| Unrecognized net loss (gain) | | **17,006** | | - | | - |
| Total | **$** | **(34,055)** | $ | (73,705) | $ | - |
| **Weighted-Average Assumptions Used to Determine Benefit Cost** | | | | | | |
| Measurement date | | **12/31/2011** | | 12/31/2010 | | 12/31/2009 |
| Discount rate | | **5.10%** | | 5.70% | | 6.05% |
| Health care cost trend rate assumed for next year (pre-/post-65) - medical | | **8.5%/6.75%** | | 7.50%/6.50% | | 8.0%/7.00% |
| Health care cost trend rate assumed for next year - Rx | | **8.00%** | | 10.00% | | 10.50% |
| Ultimate health care cost trend rate | | **5.00%** | | 5.00% | | 5.00% |
| Year that the rate reaches the ultimate trend rate | | **2018** | | 2017 | | 2017 |

**Expected Future Cash Flows**

| **Expected Benefit Payments (net of employee contributions)** | | |
|---|---|---|
| Fiscal 2013 | **$** | **89,074** |
| Fiscal 2014 | | **94,073** |
| Fiscal 2015 | | **98,352** |
| Fiscal 2016 | | **94,596** |
| Fiscal 2017 | | **103,902** |
| Fiscal 2018–2022 | | **701,189** |
| **Expected Contributions** | | |
| Fiscal 2013 | **$** | **89,074** |

## NOTE 12 — RELATED PARTY TRANSACTIONS:

Directors of the association, except for any director-elected directors, are required to be borrowers/stockholders of the association. Also, in the ordinary course of business, the association may enter into loan origination or servicing transactions with its officers, relatives of officers and directors or with organizations with which such persons are associated. Such loans are subject to special approval requirements contained in FCA regulations and are made on the same terms, including interest rates, amortization schedule and collateral, as those prevailing at the time for comparable transactions with unrelated borrowers.

Total loans to such persons for the association amounted to $11,987,952, $7,450,157 and $9,268,674 at December 31, 2012, 2011 and 2010, respectively. During 2012, $18,780,863 of advances were made, and repayments totaled $15,017,066. In the opinion of management, no such loans outstanding at December 31, 2012, 2011 and 2010 involved more than a normal risk of collectability.

Expenses incurred from the bank may include such purchased services as marketing, information systems, accounting services and allocations of expenses incurred by the bank passed through to the associations, such as FCSIC expenses. The bank charges the individual associations directly for these services based on each association's proportionate usage. These expenses totaled $342,119, $409,811 and $462,029 in 2012, 2011 and 2010, respectively. As of April 2011, the bank only bills associations for direct pass-through expenses and no longer bills for allocated expenses.

The association accrued patronage payments from related parties totaling $4,668,036, $3,890,392 and $3,678,437 during 2012, 2011 and 2010, respectively.

## NOTE 13 — FAIR VALUE MEASUREMENTS:

Accounting guidance defines fair value as the exchange price that would be received for an asset or paid to transfer a liability in an orderly transaction between market participants in the principal or most advantageous market for the asset or liability. See Note 2, "Summary of Significant Accounting Policies," for additional information.

With regard to impaired loans and other property owned, it is not practicable to provide specific information on inputs because 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 Other Financial Instrument Fair Value Measurements:

| | Valuation Technique(s) | Input |
|---|---|---|
| Cash | Carrying value | Par/principal and appropriate interest yield |
| Mission-related and other investments held-to-maturity | Discounted cash flow | Prepayment rates<br>Probability of default<br>Loss severity |
| Loans | Discounted cash flow | Prepayment forecasts<br>Probability of default<br>Loss severity |
| Systemwide debt securities, subordinated debt and other bonds | Discounted cash flow | Benchmark yield curve<br>Derived yield spread<br>Own credit risk |
| Other interest bearing liabilities | Carrying value | Par/principal and appropriate interest yield |

Assets and liabilities measured at fair value on a recurring basis at December 31, 2012, 2011 and 2010 for each of the fair value hierarchy values are summarized below:

| **December 31, 2012** | **Fair Value Measurement Using** | | | **Total Fair** |
|---|---|---|---|---|
| | **Level 1** | **Level 2** | **Level 3** | **Value** |
| Assets: | | | | |
| Investments available-for-sale* | **$ -** | **$ -** | **$ -** | **$ -** |
| Assets held in nonqualified benefit trusts | **61,858** | **-** | **-** | **61,858** |
| Total assets | **$ 61,858** | **$ -** | **$ -** | **$ 61,858** |
| Liabilities: | | | | |
| Standby letters of credit | **-** | **-** | **-** | **-** |
| Total liabilities | **$ -** | **$ -** | **$ -** | **$ -** |

| December 31, 2011 | Fair Value Measurement Using | | | Total Fair |
|---|---|---|---|---|
| | Level 1 | Level 2 | Level 3 | Value |
| Assets: | | | | |
| Investments available-for-sale* | $ - | $ - | $ - | $ - |
| Assets held in nonqualified benefit trusts | 53,526 | - | - | 53,526 |
| Total assets | $ 53,526 | **$ -** | **$ -** | $ 53,526 |
| Liabilities: | | | | |
| Standby letters of credit | - | - | - | - |
| Total liabilities | $ - | $ - | $ - | $ - |

| December 31, 2010 | Fair Value Measurement Using | | | Total Fair |
|---|---|---|---|---|
| | Level 1 | Level 2 | Level 3 | Value |
| Assets: | | | | |
| Investments available-for-sale* | $ - | $ - | $ - | $ - |
| Assets held in nonqualified benefit trusts | 40,286 | - | - | 40,286 |
| Total assets | $ 40,286 | **$ -** | **$ -** | $ 40,286 |
| Liabilities: | | | | |
| Standby letters of credit | - | - | - | - |
| Total liabilities | $ - | $ - | $ - | $ - |

*Accounting guidance requires that the fair value measurement for investments be broken out by the different types of investments held.

Assets and liabilities measured at fair value on a nonrecurring basis at December 31, 2012, 2011 and 2010 for each of the fair value hierarchy values are summarized below:

| **December 31, 2012** | **Fair Value Measurement Using** | | | **Total Fair** |
|---|---|---|---|---|
| | **Level 1** | **Level 2** | **Level 3** | **Value** |
| Assets: | | | | |
| Loans | **$ -** | **$ -** | **$ 439,516** | **$ 439,516** |
| Other property owned | **-** | **-** | **-** | **-** |

| December 31, 2011 | Fair Value Measurement Using | | | Total Fair |
|---|---|---|---|---|
| | Level 1 | Level 2 | Level 3 | Value |
| Assets: | | | | |
| Loans | $ - | $ - | $ - | $ - |
| Other property owned | - | - | - | - |

| December 31, 2010 | Fair Value Measurement Using | | | Total Fair |
|---|---|---|---|---|
| | Level 1 | Level 2 | Level 3 | Value |
| Assets: | | | | |
| Loans | $ - | $ - | $ - | $ - |
| Other property owned | - | - | - | - |

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

| | December 31, 2012 Fair Value Measurement Using | | | | | December 31, 2011 | | December 31, 2010 | |
|---|---|---|---|---|---|---|---|---|---|
| | Total Carrying Amount | Level 1 | Level 2 | Level 3 | Total Fair Value | Total Carrying Amount | Total Fair Value | Total Carrying Amount | Total Fair Value |
| Assets: | | | | | | | | | |
| Cash | $ 35,415 | $ 35,415 | $ - | $ - | $ 35,415 | $ 33,385 | $ 33,385 | $ 26,499 | $ 26,499 |
| Mission-related and other investments held-to-maturity | 3,304,296 | - | - | 3,373,896 | 3,373,896 | 5,424,993 | 5,555,348 | 7,403,693 | 7,407,432 |
| Net loans | 498,643,733 | - | - | 498,424,472 | 498,424,472 | 431,474,960 | 430,334,890 | 403,083,073 | 399,891,971 |
| Total Assets | $501,983,444 | $ 35,415 | $ - | $501,798,368 | $501,833,783 | $436,933,338 | $435,923,623 | $410,513,265 | $407,325,902 |
| Liabilities: | | | | | | | | | |
| Note payable to Farm Credit Bank of Texas | $426,001,870 | $ - | $ - | $425,815,139 | $425,815,139 | $370,853,835 | $369,870,844 | $350,486,462 | $347,439,668 |
| Total Liabilities | $426,001,870 | $ - | $ - | $425,815,139 | $425,815,139 | $370,853,835 | $369,870,844 | $350,486,462 | $347,439,668 |

## Valuation Techniques

As more fully discussed in Note 2, “Summary of Significant Accounting Policies,” accounting guidance establishes a fair value hierarchy, which requires an entity to maximize the use of observable inputs and minimize the use of unobservable inputs when measuring fair value. The following represent a brief summary of the valuation techniques used by the bank and associations for assets and liabilities:

*Investment Securities*

Where quoted prices are available in an active market, available-for-sale securities would be classified as Level 1. If quoted prices are not available in an active market, the fair value of securities is estimated using pricing models that utilize observable inputs, quoted prices for similar securities received from pricing services or discounted cash flows. Generally, these securities would be classified as Level 2. This would include certain mortgage-backed and asset-backed securities. Where there is limited activity or less transparency around inputs to the valuation, the securities are classified as Level 3. Securities classified within Level 3 include asset-based securities and certain mortgage-backed securities, including private label-FHA/VA securities and those issued by Farmer Mac.

*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*

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

## NOTE 14 — COMMITMENTS AND CONTINGENCIES

In addition to those commitments and contingencies discussed in Note 2, "Summary of Significant Accounting Policies," the association is involved in various legal proceedings in the ordinary 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.

The association may participate in financial instruments with off-balance-sheet risk to satisfy the financing needs of its borrowers in the form of commitments to extend credit and commercial letters of credit. These financial instruments involve, to varying degrees, elements of credit risk in excess of the amount 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 contract. Commercial letters of credit are agreements to pay a beneficiary under conditions specified in the letter of credit. Commitments and letters of credit generally have fixed expiration dates or other termination clauses and may require payment of a fee. At December 31, 2012, $217,600,388 of commitments and $5,474,660 of letters of credit were outstanding.

Since many of these commitments are expected to expire without being drawn upon, the total commitments do not necessarily represent future cash requirements. However, these credit-related financial instruments have off-balance-sheet credit risk because their amounts are not reflected on the balance sheet until funded or drawn upon. The credit risk associated with issuing commitments and letters of credit is substantially the same as that involved in extending loans to borrowers, and management applies the same credit policies to these commitments. Upon fully funding a commitment, the credit risk amounts are equal to the contract amounts, assuming that borrowers fail completely to meet their obligations and the collateral or other security is of no value. The amount of collateral obtained, if deemed necessary upon extension of credit, is based on management's credit evaluation of the borrower.

**NOTE 15 — QUARTERLY FINANCIAL INFORMATION (UNAUDITED):**

Quarterly results of operations for the years ended December 31 (in thousands) follow:

| | 2012 | | | | |
|---|---|---|---|---|---|
| | **First** | **Second** | **Third** | **Fourth** | **Total** |
| **Net interest income** | **$ 3,074** | **$ 3,238** | **$ 3,701** | **$ 3,792** | **$ 13,805** |
| **(Provision for) reversal of loan losses** | **(20)** | **(30)** | **(754)** | **(658)** | **(1,462)** |
| **Noninterest income (expense), net** | **(216)** | **537** | **360** | **(1,029)** | **(348)** |
| **Net income** | **$ 2,838** | **$ 3,745** | **$ 3,307** | **$ 2,105** | **$ 11,995** |

| | 2011 | | | | |
|---|---|---|---|---|---|
| | First | Second | Third | Fourth | Total |
| Net interest income | $ 2,698 | $ 2,832 | $ 3,294 | $ 3,313 | $ 12,137 |
| (Provision for) reversal of loan losses | (297) | 392 | 301 | 72 | 468 |
| Noninterest income (expense), net | (527) | (397) | 17 | (860) | (1,767) |
| Net income | $ 1,874 | $ 2,827 | $ 3,612 | $ 2,525 | $ 10,838 |

| | 2010 | | | | |
|---|---|---|---|---|---|
| | First | Second | Third | Fourth | Total |
| Net interest income | $ 2,528 | $ 2,667 | $ 3,120 | $ 2,886 | $ 11,201 |
| (Provision for) reversal of loan losses | 144 | (11) | (163) | 15 | (15) |
| Noninterest income (expense), net | (776) | 344 | (213) | (1,143) | (1,788) |
| Net income | $ 1,896 | $ 3,000 | $ 2,744 | $ 1,758 | $ 9,398 |

**NOTE 16 — SUBSEQUENT EVENTS:**

The association has evaluated subsequent events through March 7, 2013, which is the date the financial statements were issued or available to be issued.

## Directors and Employees

**Board of Directors**
Dennis Anthony, Chairman
Joe Reinart, Vice Chairman
Terry Sherrill, Outside Director
Danny Detten
Trent Finck
Bryan Reinart
Myles Frische

**Amarillo Branch Office**
**5701 West Interstate 40 806.376.4669**
Heath Wilson, Vice President/Branch Manager
Casey Cook, VP Lending
Matt Cox, VP Commercial Lending
Brad Thacker, Assistant Vice President
Kendall Wallin, VP Lending
Sabra Snyder, Loan Administrator
Brittany Borden, Loan Administrator
Jill Graves, Customer Service Representative

**Friona Branch Office**
**1602 West Highway 60 806.250.2758**
Robert Jones, Vice President/Branch Manager
Tommy St. Clair, Assistant Vice President
Tamara Garcia, Loan Administrator

**Dumas Branch Office**
**1315 East First Street 806.935.6851**
Casey Johnson, Vice President/Branch Manager
Mike Reemtsma, Assistant Vice President
LaKrisha Williamson, Sr Loan Administrator
Kay Hale, Loan Administrator
Kylie Pope, Loan Administrator

**Plainview Insurance Office**
**104 Interstate 27 North 806.296.2782**
Don Dixon, Manager of Insurance Services
Sarah Medley, Insurance Administrative Assistant

**Amarillo Central Office**
**5701 West Interstate 40 806.376.4669**
Tim McDonald, President/CEO
Brandon Blaut, Sr Vice President/ CFO
Doug Reinart, Sr Vice President/CCO
Eddie York, Sr Vice President/ CLO
Debra Wilfong, VP/Treasurer/Asst CFO/Asst Sec.
Rebecca Huey, IT Operations Manager
Erin Morgan, Credit and Oversite Manager
Carolyn Brand, Executive Assistant/Secretary
Ramona Seago, Assistant Treasurer
Missy Howell, Business Analyst
Charlee Gilliam, Accountant I
Misty Caperton, Sr. Credit Analyst
Jason Stroud, Sr. Credit Analyst
Lauren Winkelman, Credit Analyst Associate
Taos Weldon, Credit Analyst
Geary Mortimer, Chief Collateral Evaluator

**Plainview Branch Office**
**104 North Interstate 27 806.296.2782**
Cliff Daniel, Vice President/Branch Manager
Harriett Burleson, Assistant Vice President
Tammy Fields, Loan Administrator
Daleyn Schwartz, Loan Administrator

**Dimmitt Branch Office**
**112 East Jones 806.647.3169**
Mark Kleman, Vice President/Branch Manager
Gerrod Salyer, Assistant Vice President
Kay Conyers, Loan Administrator

**Amarillo Insurance Office**
**5801 I-40 West, Suite 107 806.418.2641**
Rachel Myers, Director of Insurance Services
Haley Shelton, Insurance Administrative Assistant
Janell Turner, Insurance Administrative Assistant

**Muleshoe Insurance Office**
**218 South Main Street 806.272.4271**
Dustin Cleavinger, Insurance Specialist
Lynnie Meeves, Insurance Administrative Assistant
Jaimie Saylor, Insurance Administrative Assistant