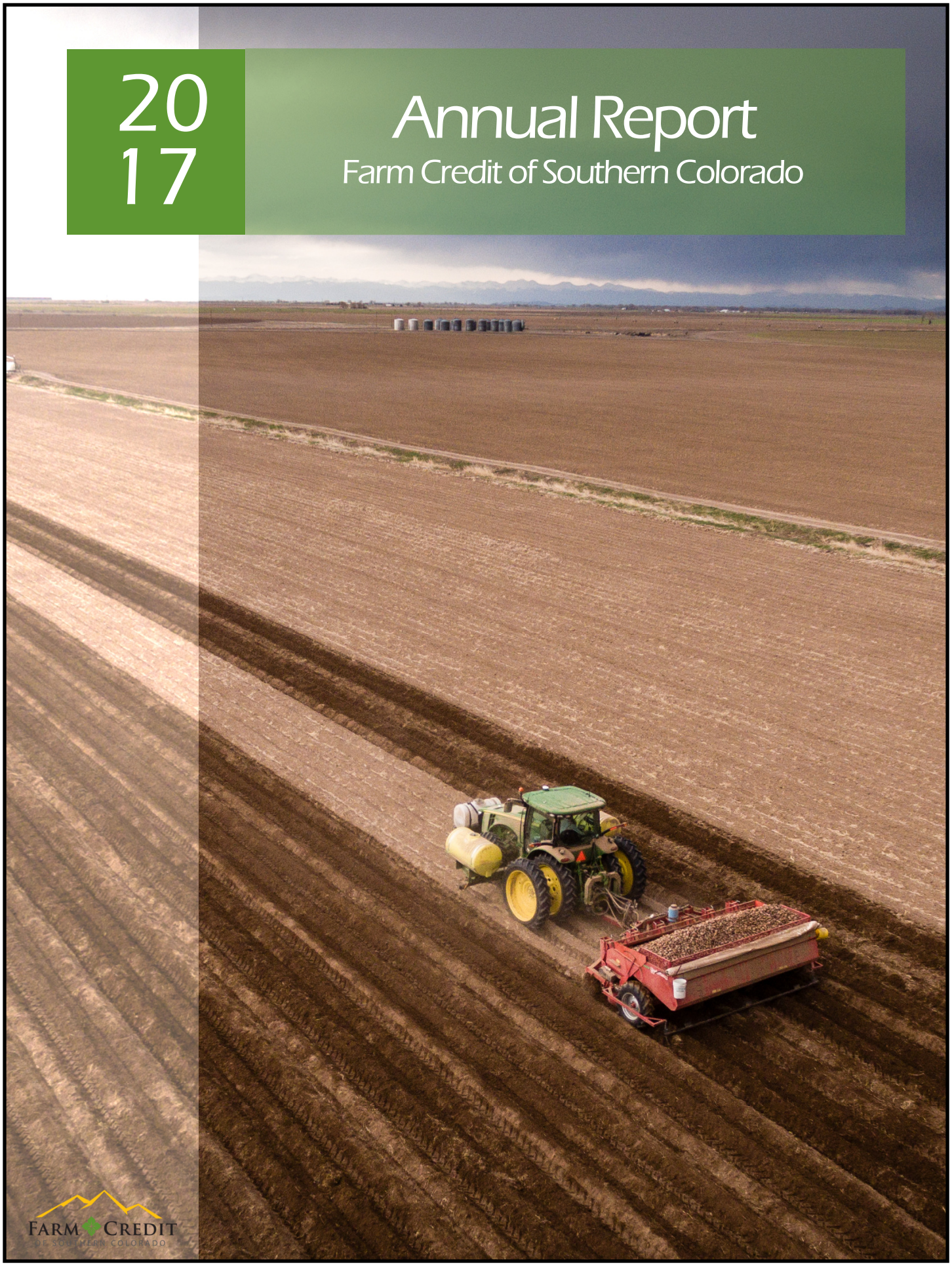
2017

Annual Report

Farm Credit of Southern Colorado



FARM CREDIT
OF SOUTHERN COLORADO

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OF SOUTHERN COLORADO

The Peak of AgLending

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Colorado Springs, CO 80915
(719) 570-1087
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We are pleased to present our 2017 Farm Credit of Southern Colorado Annual Report of Financial Condition. Farm Credit of Southern Colorado posted solid results in 2017, building upon the positive trends that your farmer/rancher owned cooperative has achieved over the years. These positive trends of sound operations are crucial in allowing us to fulfill our broader mission of serving farmers, ranchers, agriculture, and rural communities.

The Association had very strong operating results in 2017. Net earnings were in excess of $13.7 million which allows the Association to return $3.75 million in cash patronage in March 2018, to you our stockholders.

Additional Association highlights for 2017 included:

- Originated 47 new loans for $18.7 million to new young, beginning, or small farmers or ranchers customers.
- Continued an interest rate discount program for recently discharged military veterans.
- Made a significant sponsorship to Care and Share Food Bank of Southern Colorado to assist in battling rural hunger.
- Sponsored educational meetings within our lending territory.
- Added Rural Home loans and Leasing to our product offerings

At Farm Credit of Southern Colorado, we believe it is our duty to provide a relevant and dependable source of constructive credit and financial services that contribute to the long term success of our members and rural communities. We understand that as customers you expect competitively priced products and services, exceptional customer service, convenient credit delivery, knowledgeable staff, and a dedicated management team. As a member and owner of this cooperative, you also have the added benefit of playing a role in Association governance, earning back patronage, and building an organization to benefit current and future generations of farm and ranch families, all while working with a team of professionals devoted to your success.

The annual report provides detailed documentation supporting the financial results of the Association. We encourage you to read it carefully, and if you have concerns or questions, please feel free to contact us. Thank you for your continued support and for your business.

Sincerely,

Jeremy M. Anderson
President and CEO

Five-Year Summary of Selected Consolidated Financial Data

(Dollars in Thousands)

	December 31				
	2017	2016	2015	2014	2013
Statement of Condition Data					
Loans	**$ 981,997**	$ 943,326	$ 930,505	$ 899,667	$ 892,623
Less allowance for loan losses	**2,261**	1,535	1,474	1,413	1,555
Net loans	**979,736**	941,791	929,031	898,254	891,068
Investment in CoBank, ACB	**31,487**	30,876	29,954	29,423	27,717
Other property owned	**2,378**	2,575	1,752	5,398	4,355
Other assets	**41,236**	37,807	36,985	37,133	30,684
Total assets	**$ 1,054,837**	$ 1,013,049	$ 997,722	$ 970,208	$ 953,824
Obligations with maturities of one year or less	**$ 14,943**	$ 14,538	$ 13,571	$ 13,737	$ 8,910
Obligations with maturities longer than one year	**798,183**	766,778	762,847	744,959	729,197
Reserve for unfunded commitments	**382**	270	457	-	-
Total liabilities	**813,508**	781,586	776,875	758,696	738,107
Protected borrower stock	**-**	-	-	2	2
Preferred stock	**2,619**	1,879	1,761	2,863	19,004
Capital stock	**1,410**	1,407	1,375	1,328	1,306
Unallocated retained earnings	**238,141**	228,177	217,711	207,319	195,405
Accumulated other comprehensive income/(loss)	**(841)**	-	-	-	-
Total shareholders' equity	**241,329**	231,463	220,847	211,512	215,717
Total liabilities and shareholders' equity	**$ 1,054,837**	$ 1,013,049	$ 997,722	$ 970,208	$ 953,824

	For the Year Ended December 31				
	2017	2016	2015	2014	2013
Statement of Income Data					
Net interest income	**$ 26,678**	$ 25,648	$ 24,508	$ 23,769	$ 23,951
Patronage distribution from Farm Credit institutions	**3,541**	3,760	3,418	3,520	3,322
Provision for credit losses/(Credit loss reversal)	**822**	368	747	17	(765)
Noninterest expense, net	**15,662**	14,560	13,773	11,819	11,915
Provision for income taxes	**5**	5	5	5	5
Net income	**$ 13,730**	$ 14,475	$ 13,401	$ 15,448	$ 16,118
Comprehensive income	**$ 12,889**	$ 14,475	$ 13,401	$ 15,448	$ 16,118

Key Financial Ratios

For the Year					
Return on average assets	**1.33%**	1.44%	1.38%	1.61%	1.77%
Return on average shareholders' equity	**5.74%**	6.35%	6.19%	7.21%	7.56%
Net interest income as a percentage of average earning assets	**2.77%**	2.72%	2.70%	2.64%	2.80%
Net (recoveries)/charge-offs as a percentage of average net loans	**<(0.01%)**	0.05%	0.03%	0.02%	0.01%
At Year End					
Shareholders' equity as a percentage of total assets	**22.88%**	22.85%	22.14%	21.80%	22.62%
Debt as a ratio to shareholders' equity	**3.37:1**	3.38:1	3.52:1	3.59:1	3.42:1
Allowance for loan losses as a percentage of loans	**0.23%**	0.16%	0.16%	0.16%	0.17%
Common equity tier 1 (CET1) capital ratio	**19.52%**	N/A	N/A	N/A	N/A
Tier 1 capital ratio	**19.52%**	N/A	N/A	N/A	N/A
Total regulatory capital ratio	**19.74%**	N/A	N/A	N/A	N/A
Tier 1 leverage ratio	**20.35%**	N/A	N/A	N/A	N/A
Unallocated retained earnings and URE equivalents (UREE) leverage ratio	**20.94%**	N/A	N/A	N/A	N/A
Permanent capital ratio	**19.81%**	20.17%	19.16%	18.97%	20.00%
Total surplus ratio	**N/A**	19.85%	18.85%	18.54%	17.86%
Core surplus ratio	**N/A**	19.85%	18.85%	18.54%	17.57%
Net Income Distribution					
Cash patronage distributions paid	**$ 4,000**	$ 3,000	$ 3,500	$ 4,500	$ 3,000
Cash patronage declared	**$ 3,750**	$ 4,000	$ 3,000	$ 3,500	$ 4,500
Stock dividends paid	**$ 14**	$ 9	$ 10	$ 49	$ 52
Stock dividends declared	**$ 16**	$ 9	$ 9	$ 34	$ 69

MANAGEMENT'S DISCUSSION AND ANALYSIS

INTRODUCTION

The following discussion summarizes the financial position and results of operations of Farm Credit of Southern Colorado, ACA (Association) for the year ended December 31, 2017. Comparisons with prior years are included. We have emphasized material known trends, commitments, events, or uncertainties that have impacted, or are reasonably likely to impact our financial condition and results of operations. The discussion and analysis should be read in conjunction with the accompanying consolidated financial statements, footnotes and other sections of this report. The accompanying consolidated financial statements were prepared under the oversight of our Audit & Risk Committee. The Management's Discussion and Analysis includes the following sections:

- Business Overview
- Economic Overview
- Loan Portfolio
- Credit Risk Management
- Results of Operations
- Liquidity
- Capital Resources
- Regulatory Matters
- Governance
- Forward-Looking Information
- Critical Accounting Policies and Estimates
- Customer Privacy
- Other Matters
- Patron's Consent to Take Patronage Distribution into Income

Our quarterly reports to shareholders are available approximately 40 days after the calendar quarter end and annual reports are available approximately 75 days after the calendar year end. The reports may be obtained free of charge on our website, www.aglending.com, or upon request. We are located at 5110 Edison Avenue, Colorado Springs, Colorado 80915 or may be contacted by calling (800) 815-8559 or (719) 570-1087.

BUSINESS OVERVIEW

Farm Credit System Structure and Mission

We are one of 69 associations in the Farm Credit System (System), which was created by Congress in 1916 and has served agricultural producers for over 100 years. The System mission is to provide sound and dependable credit to American farmers, ranchers, and producers or harvesters of aquatic products and farm-related businesses through a member-owned cooperative system. This is done by making loans and providing financial services. Through its commitment and dedication to agriculture, the System continues to have the largest portfolio of agricultural loans of any lender in the United States. The Farm Credit Administration (FCA) is the System's independent safety and soundness federal regulator and was established to supervise, examine and regulate System institutions.

Our Structure and Focus

As a cooperative, we are owned by the members we serve. Our territory served extends across a diverse agricultural region of southern Colorado. The counties in our territory are listed in Note 1 of the accompanying consolidated financial statements. We make long-term real estate mortgage loans to farmers, ranchers, rural residents and agribusinesses and production and intermediate-term loans for agricultural production or operating purposes. Additionally, we provide other related services to our borrowers, such as credit life insurance, multi-peril crop and crop hail insurance, leasing, fee appraisals, advanced conditional payment accounts and an investment stock program. Our success begins with our extensive agricultural experience and knowledge of the market and is dependent on the level of satisfaction we provide to our borrowers.

As part of the System, we obtain the funding for our lending and operations from a Farm Credit Bank. Our funding bank, CoBank, ACB (CoBank), is a cooperative of which we are a member. CoBank, its related associations, and AgVantis, Inc. (AgVantis) are referred to as the District.

We, along with the borrower's investment in our Association, are materially affected by CoBank's financial condition and results of operations. The CoBank quarterly and annual reports are available free of charge by accessing CoBank's website, www.cobank.com, or may be obtained at no charge by contacting us at 5110 Edison Avenue, Colorado Springs, Colorado 80915 or by calling (800) 815-8559 or (719) 570-1087. Annual reports are available within 75 days after year end and quarterly reports are available within 40 days after the calendar quarter end.

We purchase technology and other operational services from AgVantis, which is a technology service corporation. Our current service agreement expires on September 29, 2018. We are a shareholder in AgVantis, along with other AgVantis customers. Farm Credit Foundations, a human resource shared service provider for a number of Farm Credit institutions, provides administration for our payroll and benefits and may provide related human resource offerings.

ECONOMIC OVERVIEW

Our territory experienced wet snows in April and May producing plenty of moisture and minimal freezing temperatures. This was followed by healthy summer rains, which resulted in bumper crop production throughout our lending territory. All of our branches were reporting good to excellent pasture and crop conditions at the end of November due to healthy precipitation over the spring and summer months. The strong yields helped to offset weaker commodity prices; although with continued price erosion, some borrowers may still have suffered losses in this current crop cycle.

Unfortunately, drought conditions deteriorated in our lending territory during December and resulted in a very dry month with no measurable precipitation. This has led to drought creeping into the eastern part of our territory. The January 2018 snow-pack map shows the overall state to be at 54% of the median for this time of year, and 49% compared to last year at this time. The snow-pack for the upper Rio Grande and Arkansas River regions is below 50% of the median.

The Federal Reserve raised the Fed Funds Rate 25 basis points in early March, again in June, and again in December. At the December meeting, the Federal Open Market Committee (FOMC) sited continued improvement in the labor market and rising economic activity. Thus, the FOMC decided to raise the Fed Funds Rate an additional 25 basis points to 1.25 – 1.50%. The Committee "will assess realized and expected economic conditions relative to its objectives of maximum employment and 2 percent inflation" in determining the size and timing of future adjustments to the Fed Funds Rate.

The export markets are seeing an upswing from 2016. This is driven by a drop in the value of the dollar in 2017. From January through September, the U.S. dollar depreciated roughly 8%. However, producers are still concerned about U.S. trade policy, as the agriculture sector remains anxious about the ongoing North American Free Trade Agreement talks.

According to the December 12, 2017 United States Department of Agriculture (USDA) report, the outlook for U.S. corn for 2017/2018 "is for increased corn used to produce ethanol and reduced ending stocks." Corn used for ethanol is projected to increase 50 million bushels. Many analysts believe corn prices have hit bottom. USDA's report confirms this by stating that "projected season-average farm price is unchanged this month at a midpoint of $3.20 per bushel," with a range of $2.85 to $3.55.

Wheat supplies are expected to continue to grow, with U.S. ending stocks (supplies) for 2017/2018 projected up another 25 million bushels due to reduced exports. The projected 2017/2018 "season-average farm price is unchanged at the midpoint of $4.60 per bushel," with a range of $4.50 to $4.70.

Fed cattle prices have rebounded from the lows hit in 2016 and are expected to average $110/cwt for 2017 with a range of $98 to $124/cwt. Feeder cattle prices are anticipated to be $150/cwt for 2017, with a range of $135 to $165/cwt. Longer-term prices are more questionable as USDA numbers indicate that 2.5 million cows have been added to the beef-breeding herd in the last three years. Those calves will hit the sale barns in 2018 and 2019, and could depress prices with the onslaught of supply.

Our customers endured several years of drought and weak yields. This resulted in multiple years of operating losses, thereby depleting working capital and owners' equity. With the forecast for continued low commodity prices and increasing interest rates, continued deterioration in the financials of our customers, especially our wheat and corn farmers, is possible. The saving grace was that we had timely precipitation in our territory during the summer, and our farmers experienced strong yields for their summer crops. This helped offset the lower prices and rising interest rates for a short time. With the drought conditions coming back into our territory, the 2017/2018 winter crop will likely be weak, and the summer 2018 crop may suffer as well.

The Agricultural Act of 2014 (Farm Bill) was signed into law on February 7, 2014. This Farm Bill governs an array of federal farm and food programs, including commodity price and support payments, farm credit, agricultural conservation, research, rural development, and foreign and domestic food programs for five years. The Farm Bill eliminates $23 billion in mandatory federal spending over a 10-year period, representing a reduction in the U.S. government farm policy support. The Farm Bill repeals direct payments and limits producers to risk management tools that offer protection when they suffer significant losses. The Farm Bill provides continued support for crop insurance programs, strengthens livestock disaster assistance and provides dairy producers with a voluntary margin protection program without imposing government-mandated supply controls.

During August 2017, CoBank management announced changes to their capital plans and patronage programs for eligible customer-owners designed to address a number of marketplace challenges. The changes are intended to strengthen CoBank's long-term capacity to serve customers' borrowing needs, enhance CoBank's ability to capitalize future customer growth, and ensure equitability among different customer segments. For cooperatives and other eligible direct borrowers as well as for loans purchased from other Farm Credit institutions, the new target patronage levels take effect in 2018 calendar year and will be reflected in patronage distributions made in March 2019. Affiliated Associations and non-affiliated Farm Credit and other financing institutions will transition to their new target patronage levels over a multi-year period ending in 2020.

New U.S. tax laws resulting from legislation commonly known as the Tax Cuts and Jobs Acts of 2017 (TCJA) were enacted in late 2017. Among other things, the TCJA changed the federal corporate tax rate from 35 percent to 21 percent. While the Association realized a net expense due to the revaluation of the net deferred tax asset from the decrease in the federal corporate tax rate in its 2017 financial results, the full impact of the TCJA is difficult to predict and may not be fully known for several years. Changes that could affect our business and customers include, but are not limited to, modifications to deductions surrounding interest expense and equipment purchases and the overall changes in the competitive environment impacting financial institutions.

LOAN PORTFOLIO

Total loans outstanding were $982.0 million at December 31, 2017, an increase of $38.7 million, or 4.1%, from loans at December 31, 2016 of $943.3 million, and an increase of $51.5 million, or 5.5%, from loans at December 31, 2015 of $930.5 million. The increase in loans was due to growth in both our core loan portfolio and participations purchased portfolio. The types of loans outstanding at December 31 are reflected in the following table.

	2017		2016		2015	
(dollars in thousands)	**Volume**	**Percent**	Volume	Percent	Volume	Percent
Real estate mortgage loans	**$573,590**	**58.4%**	$539,889	57.3%	$546,271	58.8%
Production and intermediate-term loans	**180,294**	**18.4%**	182,932	19.4%	166,406	17.9%
Agribusiness loans	**147,501**	**15.0%**	148,944	15.8%	137,009	14.7%
Rural infrastructure loans	**70,877**	**7.2%**	61,716	6.5%	70,895	7.6%
Agricultural export finance loans	**8,506**	**0.9%**	8,513	0.9%	8,528	0.9%
Rural residential real estate loans	**57**	**–**	107	–	121	–
Mission-related loans	**1,172**	**0.1%**	1,225	0.1%	1,275	0.1%
Total	**$981,997**	**100.0%**	$943,326	100.0%	$930,505	100.0%

Real estate mortgage loans outstanding increased 6.2% or $33.7 million to $573.6 million, compared with $539.9 million at year-end 2016, primarily due to a few large loans that were booked during 2017. Long-term mortgage loans are primarily used to purchase, refinance or improve real estate. These loans have maturities ranging from 5 to 40 years. Real estate mortgage loans are also made to rural homeowners. By federal regulation, a real estate mortgage loan must be secured by a first lien and may only be made in an amount up to 85% of the original appraised value of the property, or up to 97% of the appraised value, if the loan is guaranteed by certain state, federal, or other governmental agencies. Under our current underwriting standards, we loan less than the regulatory limit of 85% of the appraised value of the property.

The production and intermediate-term loans decreased 1.4% to $180.3 million compared with 2016 loans of $182.9 million, primarily due to a large pay-down by one of our largest customers along with pay-offs of other small loans. Production loans are used to finance the ongoing operating needs of agricultural producers. Production loans generally match the borrower's normal production and marketing cycle, which is typically 12 months. Intermediate-term loans are generally used to finance depreciable capital assets of a farm or ranch. Intermediate-term loans are written for a specific term, 1 to 15 years, with most loans being less than 10 years. Our production and intermediate-term loan portfolio shows some seasonality. Borrowings typically increase throughout the planting and growing seasons to meet farmers' operating and capital needs. These loans are normally at their lowest levels

following the harvest and then increase in the spring and throughout the rest of the year as borrowers fund operating needs.

Agribusiness loans were $147.5 million or 15.0% of the loan portfolio at the end of 2017, decreasing 1.0% from 2016. Agribusiness loans consist of loans to farm related businesses, cooperatives, and process and marketing businesses.

Increases were also noted in rural infrastructure loans where 100% of loan volume was due to loan participations in communication, energy and water/waste water. Additionally, at December 31, 2017, 100% of agricultural export finance volume was a result of loan participations.

Portfolio Diversification

While we make loans and provide financially related services to qualified borrowers in agricultural and rural sectors and to certain related entities, our loan portfolio is diversified by loan participations purchased and sold, geographic locations served, commodities financed and loan size as illustrated in the following four tables.

We purchase loan participations from other System and non-System entities to generate additional earnings and diversify risk related to existing commodities financed and our geographic area served. In addition, we sell a portion of certain large loans to other System entities to reduce risk and comply with lending limits we have established.

To increase our market share of broadly syndicated participation loans, we are a party to a shared lending operation known as the Commercial Finance Group (CFG). The agreement includes our Association together with Premier Farm Credit, ACA; Oklahoma AgCredit, ACA; and several associations in the AgriBank District. Along with these associations, we pool our resources to coordinate and enhance the marketing, originating and servicing of large, complex commercial and mortgage loans, as well as diversify risk. This agreement essentially replaced the Agribusiness Finance Group (AFG), which was a similar agreement that terminated in 2011. The AFG agreement included our Association and three other District Associations. The remaining participations through AFG will terminate at maturity or renewal.

Our volume of participations purchased and sold as of December 31 follows.

(dollars in thousands)	**2017**	2016	2015
Participations purchased with AFG	**$ 17,583**	$ 18,381	$ 23,809
Participations purchased with CFG	**210,172**	189,360	174,292
Participations purchased with other Farm Credit institutions	**39,069**	47,376	49,875
Participations purchased with non-Farm Credit institutions	**4,105**	2,132	2,258
Total participations purchased	**$ 270,929**	$ 257,249	$ 250,234
Participations sold to other Farm Credit institutions	**$ 20,133**	$ 17,127	$ 17,897
Total participations sold	**$ 20,133**	$ 17,127	$ 17,897

We have no loans sold with recourse, retained subordinated participation interests in loans sold, or interests in pools of subordinated participation interests that are held in lieu of retaining a subordinated participation interest in the loans sold.

The geographic distribution of loans by county at December 31 follows. As previously mentioned we purchase loan participations outside our territory, which are included in Other - Colorado and Other in the following table.

	2017	2016	2015
Alamosa	**2.94%**	2.91%	2.29%
Arapahoe	**3.61%**	3.07%	2.49%
Baca	**2.91%**	3.16%	2.99%
Bent	**1.06%**	1.14%	1.15%
Cheyenne	**4.33%**	4.18%	4.19%
Conejos	**1.03%**	0.65%	0.75%
Douglas	**1.81%**	1.99%	1.89%
El Paso	**1.09%**	1.13%	1.15%
Elbert	**3.51%**	3.69%	4.19%
Jefferson	**1.30%**	1.18%	1.33%
Kiowa	**1.68%**	1.74%	1.55%
Kit Carson	**17.16%**	18.44%	20.03%
Las Animas	**0.90%**	0.97%	0.84%
Lincoln	**3.44%**	3.68%	4.43%
Otero	**2.00%**	1.92%	2.03%
Prowers	**2.17%**	2.35%	2.45%
Pueblo	**0.94%**	1.02%	1.07%
Rio Grande	**3.80%**	3.33%	2.81%
Saguache	**1.89%**	2.29%	2.35%
Other – Colorado	**12.72%**	10.98%	10.68%
Other	**29.71%**	30.18%	29.34%
Total	**100.00%**	100.00%	100.00%

We are party to a Territorial Approval Agreement (Agreement) with two other associations in the states of Colorado and Kansas. The Agreement eliminates territorial restrictions and allows associations that are a party to the Agreement to make loans in any other association's territory regardless of a borrower's place of residence, location of operations, location of loan security or location of headquarters. This Agreement can be terminated upon the earlier to occur of:

1) the time when all but one association has withdrawn as a party to the Agreement; or
2) when requested by FCA.

We are a party to an Agreement Providing Territorial Concurrence (Agreement) with Farm Credit Services of America. This Agreement eliminates territorial restrictions and allows either party to make loans through its dealer network in the other's territory.

The following table shows the primary agricultural commodities produced by our borrowers based on the Standard Industrial Classification System (SIC) published by the federal government. This system is used to assign commodity or industry categories based on the primary business of the customer. A primary business category is assigned when the commodity or industry accounts for 50% or more of the total value of sales for a business; however, a large percentage of agricultural operations typically include more than one commodity.

	December 31		
SIC Category	**2017**	2016	2015
Cattle	**22.05%**	22.10%	22.36%
Corn	**13.99%**	14.71%	15.97%
Wheat	**12.69%**	15.31%	18.59%
Potatoes	**6.59%**	6.47%	5.09%
Hay	**6.15%**	5.12%	4.81%
Landlords	**6.05%**	3.82%	2.73%
Power	**3.83%**	4.30%	4.00%
Timber	**3.08%**	3.82%	3.77%
Other	**25.57%**	24.35%	22.68%
Total	**100.00%**	100.00%	100.00%

Our loan portfolio contains a concentration of cattle, corn and wheat producers. The majority of our cattle producers fall into one of three categories: cow/calf producers, grazing stockers and fed cattle. Each has a distinct risk profile

which provides for additional diversity. As of December 31, 2017, borrowers with cow/calf producers as their primary product comprised 13.68% of the portfolio, fed cattle were 4.20% and stockers were 3.19%. Cattle producers that did not fall into one of these sub categories comprised 1.00% of the portfolio. Our concentration of corn producers decreased to 13.99%. Our concentration of wheat producers declined to 12.69%. The Other category reflects 25.57% of the volume and is comprised of more than 75 separate groups, the largest of these representing 2.57% of the total.

Repayment ability of our borrowers is closely related to the production and profitability of the commodities they raise. If a loan fails to perform, restructuring and/or other servicing alternatives are influenced by the underlying value of the collateral which is impacted by industry economics. Our future performance would be negatively impacted by adverse agricultural conditions. The degree of the adverse impact would be correlated to the commodities negatively affected and the magnitude and duration of the adverse agricultural conditions to our borrowers.

In addition to commodity diversification noted in the previous table, further diversification is also achieved from loans to rural residents and part-time farmers which typically derive most of their earnings from non-agricultural sources. These borrowers are less subject to agricultural cycles and would likely be more affected by weaknesses in the general economy. Of our outstanding loan volume at December 31, 2017, approximately 9.2% consists of borrowers that are non-farm income dependent, a decrease from 9.8% for 2016, and 10.6% for 2015.

The principal balance outstanding at December 31, 2017 for loans $250 thousand or less accounted for 18.9% of loan volume and 71.5% of the number of loans. Credit risk on small loans, in many instances, may be reduced by non-farm income sources. The following table details loan principal by dollar size at December 31 for the last three years.

	2017		2016		2015	
(dollars in thousands)	**Amount outstanding**	**Number of loans**	Amount outstanding	Number of loans	Amount outstanding	Number of loans
$1 - $250	**$ 185,249**	**2,325**	$ 185,462	2,391	$ 188,707	2,420
$251 - $500	**158,070**	**448**	159,697	452	150,605	426
$501 - $1,000	**193,837**	**273**	193,629	272	180,309	252
$1,001 - $5,000	**369,880**	**193**	348,698	179	342,035	179
$5,001 - $25,000	**74,961**	**11**	55,840	8	68,849	10
Total	**$ 981,997**	**3,250**	$ 943,326	3,302	$ 930,505	3,287

Approximately 12% of our loans outstanding are attributable to ten borrowers. Due to their size, the loss of any of these loans or the failure of any of these loans to perform would adversely affect the portfolio and our future operating results.

Credit guarantees with government agencies of $18.0 million at year-end 2017, $18.3 million at year-end 2016 and $15.8 million at year-end 2015 were outstanding.

Credit Commitments

We may participate in financial instruments with off-balance-sheet risk to satisfy the financing needs of our borrowers. These financial instruments include commitments to extend credit. The instruments involve, to varying degrees, elements of credit risk in excess of the amount recognized in our consolidated financial statements. Commitments to extend credit are agreements to lend to a borrower as long as there is not a violation of any condition established in the contract. Commitments generally have fixed expiration dates or other termination clauses and may require payment of a fee by the borrower. We may also participate in standby letters of credit to satisfy the financing needs of our borrowers. These standby letters of credit are irrevocable agreements to guarantee payments of specified financial obligations. The following table summarizes the maturity distribution of unfunded credit commitments on loans at December 31, 2017.

(dollars in thousands)	**Less than 1 year**	**1 – 3 years**	**3 – 5 years**	**Over 5 years**	**Total**
Commitments to extend credit	$ 59,950	$ 88,222	$ 75,399	$21,984	$ 245,555
Standby letters of credit	2,355	42	151	179	2,727
Total commitments	$ 62,305	$ 88,264	$ 75,550	$22,163	$ 248,282

Since many of these commitments are expected to expire without being drawn upon, the total commitments do not necessarily represent future cash requirements. However, these credit-related financial instruments have off-balance-sheet credit risk because their amounts are not reflected on the Consolidated Statement of Condition 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 we apply the same credit policies to these commitments. The amount of collateral obtained, if deemed necessary upon extension of credit, is based on our credit evaluation of the borrower. We consider potential losses related to unfunded commitments, and a reserve for unfunded commitments is included in the liabilities section of the Consolidated Statement of Condition. The related provision for the reserve for unfunded commitment is included as part of the provision for credit losses on the Consolidated Statement of Comprehensive Income.

High Risk Assets

Nonperforming loan volume is comprised of nonaccrual loans, restructured loans, and loans 90 days past due still accruing interest and are referred to as impaired loans. High risk assets consist of impaired loans and other property owned. Comparative information regarding high risk assets in the portfolio, including accrued interest, follows:

(dollars in thousands)	**2017**	2016	2015
Nonaccrual loans:			
Real estate mortgage	**$ 10,723**	$ 4,391	$ 4,503
Production and intermediate-term	**1,586**	1,420	1,907
Rural infrastructure	**–**	–	1,333
Total nonaccrual loans	**12,309**	5,811	7,743
Accruing restructured loans:			
Real estate mortgage	**519**	97	100
Production and intermediate-term	**717**	727	124
Rural infrastructure	**–**	1,279	–
Total accruing restructured loans	**1,236**	2,103	224
Accruing loans 90 days past due:			
Real estate mortgage	**–**	–	457
Total impaired loans	**13,545**	7,914	8,424
Other property owned	**2,378**	2,575	1,752
Total high risk assets	**$ 15,923**	$ 10,489	$ 10,176
Nonaccrual loans to total loans	**1.25%**	0.62%	0.83%
Impaired loans to total loans	**1.38%**	0.84%	0.91%
High risk assets to total loans	**1.62%**	1.11%	1.09%
High risk assets to total shareholders' equity	**6.60%**	4.53%	4.61%

Total high risk assets increased $5.4 million, or 51.8%, to $15.9 million at December 31, 2017 compared with year-end 2016. The increase in our high risk assets was due to an increase in nonaccrual loans.

Nonaccrual loans represent all loans where there is a reasonable doubt as to collection of all principal and/or interest. Nonaccrual volume increased $6.5 million compared with December 31, 2016 primarily due to one large loan complex being transferred to nonaccrual status, partially offset by the pay-off and the movement of several smaller loans to accrual status. At year-end, two loan complexes made up 100% of the nonaccrual loan volume. All of the nonaccrual loan volume is secured by real estate. The following table provides additional information on nonaccrual loans as of December 31 for the last three fiscal years.

(dollars in thousands)	**2017**	2016	2015
Nonaccrual loans current as to principal and interest	**$ 11,213**	$ 1,421	$ 5,594
Cash basis nonaccrual loans	**$ –**	$ –	$ 3,257
Restructured loans in nonaccrual status	**$ –**	$ 443	$ 2,649

Accruing restructured loans including related accrued interest decreased $867 thousand during 2017 primarily as a result of one loan complex being refinanced and transferred out of accruing restructured status. The accruing restructured loans include only the year-end balances of loans and related accrued interest on which monetary concessions have been granted to borrowers and that are in accrual status. Accruing restructured loans do not include loans on which monetary concessions have been granted but which remain in nonaccrual status.

At year-end 2017 and 2016, there were no loans 90 days past due and still accruing interest.

Other property owned is real or personal property that has been acquired through foreclosure, deed in lieu of foreclosure or other means. We had other property owned of $2.4 million at December 31, 2017, compared with $2.6 million at December 31, 2016 and $1.8 million at December 31, 2015. We are holding the same three real estate parcels at the end of 2017 as we held at the end of 2016. The chattels that we had at the end of 2016 were sold in 2017.

High risk asset volume is likely to increase through 2018 as we continue to see distress in the borrowers' operations due to commodity prices remaining low and the dry winter. We will continue to work with borrowers who are experiencing distress in their operations and will fully provide borrower rights to these borrowers. Our first direction is to restructure a borrower's loan(s) in an attempt to return them back to viability. We will explore and apply all feasible alternatives available to help these distressed borrowers shore up their operations without creating undue risk to the Association.

Credit Quality

We review the credit quality of the loan portfolio on an on-going basis as part of our risk management practices. Each loan is classified according to the Uniform Classification System (UCS), which is used by all System institutions. Following are the classification definitions.

- Acceptable – Assets are expected to be fully collectible and represent the highest quality.
- Other Assets Especially Mentioned (OAEM) – Assets are currently collectible but exhibit some potential weakness.
- Substandard – Assets exhibit some serious weakness in repayment capacity, equity, and/or collateral pledged on the loan.
- Doubtful – Assets exhibit similar weaknesses as substandard assets. However, doubtful assets have additional weaknesses in existing facts that make collection in full highly questionable.
- Loss – Assets are not considered collectible.

The following table presents statistics based on UCS related to the credit quality of the loan portfolio, including accrued interest at December 31 for the last three fiscal years.

	2017	2016	2015
Acceptable	**93.46%**	92.10%	94.93%
OAEM	**2.34%**	3.64%	3.28%
Substandard	**4.20%**	4.26%	1.79%
Total	**100.00%**	100.00%	100.00%

During 2017, overall credit quality improved. Loans classified as Acceptable and OAEM were 95.80% at December 31, 2017, 95.74% at December 31, 2016 and 98.21% at December 31, 2015. We had no loans classified as Doubtful or Loss for any of the three years presented. The financial position of most agricultural producers strengthened during the past decade, and most of our borrowers have maintained generally strong financial positions. As such, our credit quality is anticipated to remain sound, but may see a slight decrease in the near term. However, agriculture remains a cyclical business that is heavily influenced by production, operating costs and commodity prices. Each of these can be significantly impacted by uncontrollable events. If less favorable economic conditions continue, it will likely lead to weakening in the loan portfolio. Loan delinquencies (accruing loans 30 days or more past due) as a percentage of accruing loans decreased and remained at a low level of 0.17% at December 31, 2017, compared with 0.54% at December 31, 2016 and 0.60% at December 31, 2015.

Allowance for Loan Losses

We maintain an allowance for loan losses at a level consistent with the probable and estimable losses inherent in the loan portfolio identified by management. The allowance for loan losses at each period end was considered to be adequate to absorb probable losses existing in the loan portfolio. Because the allowance for loan losses considers factors such as current agricultural and economic conditions, loan loss experience, portfolio quality and loan portfolio

composition, there will be a direct impact to the allowance for loan losses and our income statement when there is a change in any of those factors. The following table provides relevant information regarding the allowance for loan losses as of December 31 for the last three fiscal years.

(dollars in thousands)	**2017**	2016	2015
Balance at beginning of year	**$ 1,535**	$ 1,474	$ 1,413
Charge-offs:			
Real estate mortgage	**–**	–	318
Production and intermediate-term	**22**	684	79
Total charge-offs	**22**	684	397
Recoveries:			
Real estate mortgage	**–**	50	–
Production and intermediate-term	**38**	140	168
Total recoveries	**38**	190	168
Net (recoveries)/charge-offs	**(16)**	494	229
Provision for loan losses	**710**	555	290
Balance at December 31	**$ 2,261**	$ 1,535	$ 1,474
Net (recoveries)/charge-offs to average net loans	**<(0.01%)**	0.05%	0.03%

The following table presents the allowance for loan losses by loan type as of December 31 for the last three fiscal years.

(dollars in thousands)	**2017**	2016	2015
Real estate mortgage	**$ 675**	$ 429	$ 446
Production and intermediate-term	**557**	388	335
Agribusiness	**693**	443	381
Rural infrastructure	**317**	265	301
Agricultural export finance	**6**	6	7
Mission-related	**13**	4	4
Total	**$ 2,261**	$ 1,535	$ 1,474

The allowance for loan losses increased $726 thousand from December 31, 2016, to $2.3 million at December 31, 2017. The increase in allowance for loan losses was primarily due to the provision for loan losses totaling $710 thousand that was recorded due to new (higher) PD factors utilized in the calculations based on the updated Combined System Risk Rating Guidance and the newly implemented 18-month default horizon. Net recoveries of $16 thousand were recorded during 2017. Overall, charge-off activity remains low relative to the size of our loan portfolio. During 2016, our allowance for loan losses increased $61 thousand from 2015 primarily due to the provision for loan losses totaling $555 thousand that was recorded as a result of an increase in our general reserves based on an increase in loan volume, an increase in the risk profile of our portfolio, and a change in our PD percent factors as a result of the Combined System Risk Rating Guidance. Comparative allowance for loan losses coverage as a percentage of loans and certain other credit quality indicators as of December 31 are presented in the following table.

	2017	2016	2015
Allowance as a percentage of:			
Loans	**0.23%**	0.16%	0.16%
Impaired loans	**16.69%**	19.39%	17.50%
Nonaccrual loans	**18.37%**	26.41%	19.04%

We maintain a separate reserve for unfunded commitment, which is included in Liabilities on our Consolidated Statement of Condition. The related provision for the reserve for unfunded commitments is included as part of the provision for credit losses on the Consolidated Statement of Comprehensive Income, along with the provision for loan losses.

A summary of changes in the reserve for unfunded commitment follows.

	Year Ended December 31		
(dollars in thousands)	**2017**	2016	2015
Balance at beginning of year	**$ 270**	$ 457	$ –
Provision for/(Reversal of) reserve for unfunded commitments	**112**	(187)	457
Total	**$ 382**	$ 270	$ 457

Young, Beginning and Small Farmers and Ranchers Program

As part of the Farm Credit System, we are committed to providing sound and dependable credit and related services to young, beginning and small (YBS) farmers and ranchers. We have a strong belief that the future of agriculture and the future of our organization are dependent upon the success of young, beginning and small farmers and ranchers. We provide lending products, financial services, training opportunities, sponsorships, and staff expertise to YBS farmers and ranchers. The following are FCA regulatory definitions for YBS farmers and ranchers.

- Young Farmer: A farmer, rancher, or producer or harvester of aquatic products who was age 35 or younger as of the date the loan was originally made.
- Beginning Farmer: A farmer, rancher, or producer or harvester of aquatic products who had 10 years or less farming or ranching experience as of the date the loan was originally made.
- Small Farmer: A farmer, rancher, or producer or harvester of aquatic products who normally generated less than $250 thousand in annual gross sales of agricultural or aquatic products at the date the loan was originally made.

The following table outlines our percentage of YBS loans as a percentage of the number of loans in our loan portfolio while the USDA column represents the percent of farmers and ranchers classified as YBS within our territory per the 2012 USDA Agricultural Census, which is the most current data available. Due to FCA regulatory definitions, a farmer/rancher may be included in multiple categories as they would be included in each category in which the definition was met.

	USDA	**2017**	2016	2015
Young	8.51%	**17.40%**	16.93%	16.15%
Beginning	37.32%	**20.88%**	20.34%	19.62%
Small	92.85%	**32.52%**	31.22%	29.31%

Note that several differences exist in definitions between USDA statistics and our data due to our use of FCA definitions. Young farmers are defined as 34 years old and younger by the USDA, while FCA definitions include farmers 35 years old and younger. Beginning farmers are defined by FCA as those with 10 years or less farming experience; however, the USDA identifies beginning farmers as on their current farm less than 10 years. This may include both beginning farmers and experienced farmers who have recently changed farmsteads. Our percentages are based on the number of loans in our portfolio, while the USDA percentages are based on the number of farmers and ranchers. While these definition differences do exist, the information is the best comparative information available.

We establish annual marketing goals to increase market share of loans to YBS farmers and ranchers. Our goals are as follows:

- Offer related services either directly or in coordination with others that are responsive to the needs of YBS farmers and ranchers in our territory;
- Take full advantage of opportunities for coordinating credit and services offered with other System institutions in the territory and other governmental and private sources of credit who offer credit and services to those who qualify as YBS farmers and ranchers in our territory; and,
- Implement effective outreach programs to attract YBS farmers and ranchers.

As a part of marketing strategy, we utilize USDA and other loan guarantee programs wherever it is advantageous to a YBS customer. During 2017, we sponsored several education programs that target YBS farmers and ranchers along with leadership development activities for agricultural organizations. In 2013, the Board approved a $50 thousand donation over five years to the Colorado FFA Foundation to assist with the building of a new Agricultural Education Building at Colorado State University (CSU). For 2018, we have established the following qualitative goals:

- Annually continue to provide surplus computers to FFA Chapters and Young Farmers organizations
- Continue to work with the Farm Services Agency offices in providing training for YBS customers

Quarterly reports are provided to our Board of Directors detailing the number, volume and credit quality of our YBS customers. We have developed quantitative targets to monitor our progress.

- Originate 42 or more new loans to new customers, for a total of $6.0 million or greater.
- Set aside $3.0 million of capital to fund loans to new Young and Beginning farmers and ranchers in our territory.
    - This capital allocation will fund over $15 million of loans, and
    - Allow for special priced rate of 0.50% below the normal qualifying rate for new young farmer and rancher loans.

For 2017, the goal was to originate 41 or more new YBS loans to new customers for a total of $5.75 million or greater. Actual results were 47 new loans for a total of $18.7 million to new customers meeting one of the three YBS criteria.

New Loans	Number Goal	Number Results	Volume Goal	Volume Results
Young	165	137	$ 38,480	$ 32,137
Beginning	218	170	$ 54,080	$ 63,330
Small	255	219	$ 41,600	$ 46,794
Existing Loans				
Young	695	634	$ 140,000	$ 145,726
Beginning	840	761	$ 192,400	$ 209,930
Small	1,260	1,185	$ 174,500	$ 179,851

Our 2018 YBS quantitative objectives are as follows:

New Loans	Number Goal	Volume Goal
Young	171	$ 40,000
Beginning	266	$ 56,200
Small	265	$ 43,200
Existing Loans		
Young	722	$ 145,000
Beginning	870	$ 200,000
Small	1,310	$ 181,500

To ensure that credit and services offered to our YBS farmers and ranchers are provided in a safe and sound manner and within our risk-bearing capacity, we utilize customized loan underwriting standards, loan guarantee programs, and other credit enhancement programs. Additionally, we are actively involved in developing and sponsoring educational opportunities, leadership training, business financial training and insurance services for YBS farmers and ranchers.

CREDIT RISK MANAGEMENT

Credit risk arises from the potential failure of a borrower to meet repayment obligations that result in a financial loss to the lender. Credit risk exists in our loan portfolio and also in our unfunded loan commitments and standby letters of credit. Credit risk is actively managed on an individual and portfolio basis through application of sound lending and underwriting standards, policies and procedures.

Underwriting standards are utilized to determine an applicant's operational, financial, and managerial resources available for repaying debt within the terms of the note and loan agreement. Underwriting standards include among other things, an evaluation of:

- character – borrower integrity and credit history;
- capacity – repayment capacity of the borrower based on cash flows from operations or other sources of income;
- collateral – to protect the lender in the event of default and also serve as a secondary source of loan repayment;
- capital – ability of the operation to survive unanticipated risks; and,
- conditions – intended use of the loan funds, terms, restrictions, etc.

Processes for information gathering, balance sheet and income statement verification, loan analysis, credit approvals, disbursements of proceeds and subsequent loan servicing actions are established and followed. Underwriting standards vary by industry and are updated periodically to reflect market and industry conditions.

By regulation, we cannot have loan commitments to one borrower for more than 15% of our lending limit base. The lending limit base is defined as permanent capital with any applicable adjustments related to preferred stock and any investment held in connection with the sale of loan participation interest. Additionally, we set our own lending limits to manage loan concentration risk. Lending limits have been established on a loan by loan basis for all customer complexes that exceed 5% of our lending limit base. We utilize a tool that considers factors such as financial position, enterprise concentrations and collateral.

We have established internal lending delegations to properly control the loan approval process. Delegations to staff are based on our risk-bearing capacity, loan size, complexity, type and risk, as well as the expertise and position of the credit staff member. Larger and more complex loans or loans perceived to have higher risk are typically approved by a loan committee of our most experienced and knowledgeable credit staff.

The majority of our lending is first mortgage real estate loans which must be secured by a first lien on real estate. Production and intermediate-term lending accounts for most of the remaining volume and is typically secured by livestock, crops and equipment. Collateral evaluations are completed in compliance with FCA and Uniform Standards of Professional Appraisal Practices requirements. All property is appraised at market value. All collateral evaluations must be performed by a qualified appraiser. Certain appraisals must be performed by individuals with a state certification or license.

We use a two-dimensional risk rating model (Model) based on the Farm Credit System's Combined System Risk Rating Guidance. The Model estimates each loan's probability of default (PD) and loss given default (LGD). PD estimates the probability that a borrower will experience a default within twelve months from the date of determination. We adjust the PD factors in the Combined System Risk Rating Guidance to account for our loss emergence period which has been determined to be 18 months. LGD provides an estimation of the anticipated loss with respect to a specific financial obligation of a borrower assuming a default has occurred or will occur within the next twelve months. The Model uses objective and subjective criteria to identify inherent strengths, weaknesses, and risks in each loan. PDs and LGDs are utilized in loan and portfolio management processes and are utilized for the allowance for loan losses estimate.

The Model's 14-point probability of default scale provides for nine acceptable categories, one OAEM category, two substandard categories, one doubtful category and one loss category; each carrying a distinct percentage of default probability. The Model's LGD scale provides six categories, A through F, that have the following anticipated principal loss and range of economic loss expectations:

- A 0% anticipated principal loss; 0% to 5% range of economic loss
- B 0% to 3% anticipated principal loss; >5% to 15% range of economic loss
- C > 3% to 7% anticipated principal loss; >15% to 20% range of economic loss
- D > 7% to 15% anticipated principal loss; >20% to 25% range of economic loss
- E > 15% to 40% anticipated principal loss; >25% to 50% range of economic loss
- F above 40% anticipated loss; above 50% range of economic loss

In regards to our purchased participation loans, there are a few differences in the credit risk management practices of this segment of our portfolio. Like core credit, underwriting standards are utilized to determine an applicant's operational, financial, and managerial resources available for repayment of debt; however, due to the unique industries financed in the capital markets arena, this segment of our portfolio has a different set of underwriting standards that apply to the specific industries in which we lend. Also, like core credit, we cannot have commitments to one borrower for more than 15% of our lending limit base. Within the purchased participations portfolio, specific hold limits have been established based on PD and industry. Additionally, the participations purchased portfolio contains loans to borrowers that are considered similar entities, and by regulation must be in compliance with specific limits outlined in our Association policy.

RESULTS OF OPERATIONS

Earnings Summary

In 2017, we recorded net income of $13.7 million, compared with $14.5 million in 2016, and $13.4 million in 2015. The decrease in 2017 was primarily due to higher noninterest expense and increased provision for credit losses,

partially offset by higher net interest income. The increase in 2016 was primarily due to higher net interest income. The following table presents the changes in the significant components of net income from the previous year.

(dollars in thousands)	**2017 vs. 2016**	2016 vs. 2015
Net income, prior year	**$ 14,475**	$ 13,401
Increase/(Decrease) from changes in:		
Interest income	**2,923**	1,714
Interest expense	**(1,893)**	(574)
Net interest income	**1,030**	1,140
Provision for credit losses	**(454)**	380
Noninterest income	**(304)**	(222)
Noninterest expense	**(1,017)**	(224)
Total (decrease)/increase in net income	**(745)**	1,074
Net income, current year	**$ 13,730**	$ 14,475

Return on average assets decreased to 1.33% from 1.44% in 2016, and return on average shareholders' equity decreased to 5.74% from 6.35% in 2016, primarily as a result of a decrease in net income.

Net Interest Income

Net interest income for 2017 was $26.7 million compared with $25.6 million for 2016 and $24.5 million for 2015. Net interest income is our principal source of earnings and is impacted by interest earning asset volume, yields on assets and cost of debt. The increase in net interest income was largely due to an increase in our average accrual loan volume coupled with an increase in the return on our own capital. The following table provides an analysis of the individual components of the change in net interest income during 2017 and 2016.

(dollars in thousands)	**2017 vs. 2016**	2016 vs. 2015
Net interest income, prior year	**$ 25,648**	$ 24,508
Increase/(Decrease) in net interest income from changes in:		
Interest rates earned	**1,894**	836
Interest rates paid	**(1,580)**	(150)
Volume of interest-bearing assets and liabilities	**704**	1,036
Interest income on nonaccrual loans	**12**	(582)
Increase in net interest income	**1,030**	1,140
Net interest income, current year	**$ 26,678**	$ 25,648

The following table illustrates net interest margin and the average interest rates on loans and debt cost and interest rate spread.

	Year Ended December 31		
	2017	2016	2015
Net interest margin	**2.77%**	2.72%	2.70%
Interest rate on:			
Average loan volume	**4.57%**	4.36%	4.33%
Average debt	**2.21%**	2.00%	1.98%
Interest rate spread	**2.36%**	2.36%	2.35%

The interest rate spread was unchanged due to a 21 basis point increase in interest rates on average loan volume and a 21 basis point increase in interest rates on average debt. The increase in net interest margin was due to higher earnings on our own capital.

Provision for Credit Losses/(Credit Loss Reversals)

We monitor our loan portfolio and unfunded commitments on a regular basis to determine if any increase through provision for credit losses or decrease through a credit loss reversal in our allowance for loan losses or reserve for unfunded commitment is warranted based on our assessment of the probable and estimable losses inherent in our loan portfolio and unfunded commitments. We recorded net provision for credit losses of $822 thousand in 2017, compared with $368 thousand in 2016 and $747 thousand in 2015. The provision for loan losses of $710 thousand recorded during 2017 was primarily due to higher PD factors utilized in the calculation based on the updated Combined System Risk Rating Guidance along with a newly implemented 18-month default horizon. The provision for loan losses of $555 thousand in 2016 was primarily due to an increase in our general reserves stemming from an increase in loan volume, an increase in the risk profile of our portfolio and a change in our PD percent factors as a

result of the Combined System Risk Rating Guidance. The provision for loan losses recorded in 2015 was primarily due to stress testing in the portfolio which helped management assess the impact of various factors, resulting in an increase in management reserves.

The provision for reserve for unfunded commitments of $112 thousand was recorded during 2017 due to the change in the PD factors utilized in the calculation of the reserve for unfunded commitments as a result of the newly implemented 18-month default horizon. The reversal of provision for reserve for unfunded commitments of $187 thousand in 2016 was due to the elimination of management reserves on unfunded commitments. The provision for reserve for unfunded commitments of $457 thousand in 2015 was the first year this activity was separated from the provision for loan losses.

Noninterest Income

During 2017, we recorded noninterest income of $4.8 million, compared with $5.1 million in 2016 and $5.4 million in 2015. Patronage distributions from CoBank are our primary source of noninterest income. Patronage is accrued in the year earned and then received from CoBank in the following year. CoBank patronage is distributed in cash and stock. Patronage earned from CoBank was $3.5 million in 2017, $3.5 million in 2016 and $3.4 million in 2015.

During August 2017, CoBank management announced changes to their patronage program. The new plan includes a reduction to our patronage income in 2019 of five basis points on loans with CoBank and an additional reduction of four basis points in 2020. Patronage on participation sold loans will reduce by five basis points in 2018. In 2017, we received 45 basis points related to our direct note with CoBank for other loans and 100 basis points on participation loans.

In 2016 and 2015, we received a patronage distribution from AgVantis, based on our services purchased from AgVantis during the respective fiscal year. During 2017, no patronage distribution was issued. We received a Notice of Allocation with our total patronage of $283 thousand in 2016 and $48 thousand in 2015, which includes cash patronage of $57 thousand for 2016 and $10 thousand for 2015. The balance of the allocation is recorded in other assets. Additionally, we recorded a cash patronage of $12 thousand from Farm Credit Foundations, the organization that provides our payroll and human resource services. This compares with $11 thousand recorded in 2016 and $7 thousand in 2015. Patronage from these two entities and CoBank is included in patronage distribution from Farm Credit institutions on the Consolidated Statement of Comprehensive Income.

We received mineral income of $657 thousand during 2017, which is distributed to us quarterly by CoBank. Mineral income increased from $642 thousand in 2016 and decreased from $1.2 million in 2015. The reduction is primarily attributed to lower mineral prices resulting in reduced production and lease related income.

Noninterest income also includes loan fees, financially related services income and other noninterest income. Loan fees in 2017 were $387 thousand, a decrease of $137 thousand, from 2016, primarily due to less fee based loan activity in our participations purchased portfolio.

Noninterest Expense

Noninterest expense for 2017 increased $1.0 million, or 6.4%, to $17.0 million compared with 2016 and increased $1.2 million, or 7.9% compared with 2015. Noninterest expense for each of the three years ended December 31 is summarized as follows:

				Percent of Change	
(dollars in thousands)	**2017**	2016	2015	**2017/2016**	2016/2015
Salaries & employee benefits	**$ 9,577**	$ 8,754	$ 8,517	**9.40%**	2.78%
Occupancy & equipment	**1,313**	1,219	1,227	**7.71%**	(0.65%)
Purchased services from AgVantis	**1,593**	1,710	1,270	**(6.84%)**	34.65%
Supervisory & examination costs	**362**	349	302	**3.72%**	15.56%
Other	**2,753**	2,574	2,458	**6.95%**	4.72%
Total operating expense	**15,598**	14,606	13,774	**6.79%**	6.04%
Losses on other property owned	**265**	109	1,020	**143.12%**	(89.31%)
Farm Credit Insurance Fund premium	**1,089**	1,220	918	**(10.74%)**	32.90%
Total noninterest expense	**$ 16,952**	$ 15,935	$ 15,712	**6.38%**	1.42%

For the year ended December 31, 2017, total operating expense increased $992 thousand, or 6.8%, compared with the year ended December 31, 2016, primarily due to an increase in salaries and employee benefits. Salaries and employee benefits costs are higher due to an increase in the number of employees for part of the year, annual raises, hiring bonus, relocation expenses, separation pay and qualified pension expense. Occupancy and equipment costs are higher due to increased property taxes, higher utilities and software licenses. Other costs are

higher due to increased purchased services and travel. Losses on other property owned include higher expenses on the three properties in 2017 compared with one property in 2016, in addition to a valuation write-down in 2017. Insurance Fund premium decreased $131 thousand to $1.1 million due to a decrease in the premium rate offset by an increase in average net loan payable to CoBank.

Provision for income taxes

We recorded $5 thousand in provision for income taxes during 2017, 2016 and 2015. The tax expense was impacted by $1.1 million in expense resulting from the enactment of federal tax legislation in late December 2017 which, among other things, lowered the federal corporate tax rate from 35 percent to 21 percent beginning in 2018. In accordance with accounting principles generally accepted in the United State (GAAP), the change to the lower corporate tax rate led to a revaluation of our deferred tax assets and deferred tax liabilities in the period of enactment (2017). We operate as a Subchapter T cooperative for tax purposes and thus may deduct from taxable income certain amounts that are distributed from net earnings to borrowers. See Note 10 for additional details.

LIQUIDITY

Liquidity is necessary to meet our financial obligations. Liquidity is needed to pay our note with CoBank, fund loans and other commitments, and fund business operations in a cost-effective manner. Our liquidity policy is intended to manage short-term cash flow, maximize debt reduction and liquidate nonearning assets. Our direct loan with CoBank, cash on hand and borrower loan repayments provide adequate liquidity to fund our on-going operations and other commitments.

Funding Sources

Our primary source of liquidity is the ability to obtain funds for our operations through a borrowing relationship with CoBank. Our note payable to CoBank is collateralized by a pledge to CoBank of substantially all of our assets. Substantially all cash received is applied to the note payable and all cash disbursements are drawn on the note payable. The indebtedness is governed by a General Financing Agreement (GFA) with CoBank. The GFA in effect at December 31, 2017 was scheduled to mature on May 31, 2018; however, a new GFA entered into on January 1, 2018 will mature on December 31, 2022. The annual average principal balance of the note payable to CoBank was $781.0 million in 2017, $766.3 million in 2016 and $743.7 million in 2015.

We plan to continue to fund lending operations through the utilization of our funding arrangement with CoBank, retained earnings from current and prior years and from borrower stock investments. CoBank's primary source of funds is the ability to issue Systemwide Debt Securities to investors through the Federal Farm Credit Bank Funding Corporation. This access has traditionally provided a dependable source of competitively priced debt that is critical for supporting our mission of providing credit to agriculture and rural America. Although financial markets experienced significant volatility in the last few years, we were able to obtain sufficient funding to meet the needs of our customers.

Interest Rate Risk

The interest rate risk inherent in our loan portfolio is substantially mitigated through our funding relationship with CoBank which allows for loans to be match-funded. Borrowings from CoBank match the pricing, maturity, and option characteristics of our loans to borrowers. CoBank manages interest rate risk through the direct loan pricing and its asset/liability management processes. Although CoBank incurs and manages the primary sources of interest rate risk, we may still be exposed to interest rate risk through the impact of interest rate changes on earnings generated from our loanable funds. To stabilize earnings from loanable funds, we have committed excess loanable funds with CoBank at a fixed rate for a specified term as a part of CoBank's Association Equity Positioning Program (AEPP). This enables us to reduce our overall cost of funds with CoBank without significantly increasing our overall interest rate risk position.

Funds Management

We offer variable, fixed, adjustable prime-based and LIBOR-based rate loans to borrowers. Our Asset Liability Committee with oversight from our Board of Directors determines the interest rate charged based on the following factors: 1) the interest rate charged by CoBank; 2) our existing rates and spreads; 3) the competitive rate environment; and 4) our profitability objectives.

We have a relationship with CoBank, and First Tennessee Bank to offer a purchase card program to commercial customers. The purchase cards are similar to credit cards and allow customers to make agricultural-related purchases which are then automatically posted to the customer's loan on a monthly basis. We remit payment to First Tennessee Bank on behalf of the borrowers each month for purchases made with the card.

CAPITAL RESOURCES

Capital supports asset growth and provides protection for unexpected credit and operating losses. Capital is also needed for investments in new products and services. We believe a sound capital position is critical to our long-term financial success due to the volatility and cycles in agriculture. Over the past several years, we have been able to build capital primarily through net income retained after patronage. Shareholders' equity at December 31, 2017 totaled $241.3 million, compared with $231.5 million at December 31, 2016 and $220.8 million at December 31, 2015. The increase of $9.8 million in shareholders' equity reflects net income and net stock issuances, partially offset by patronage refunds, dividends paid and an increase in accumulated other comprehensive loss. Our capital position is reflected in the following ratio comparisons.

	2017	2016	2015
Debt to shareholders' equity	**3.37:1**	3.38:1	3.52:1
Shareholders' equity as a percent of net loans	**24.63%**	24.58%	23.77%
Shareholders' equity as a percent of total assets	**22.88%**	22.85%	22.14%

Debt to shareholders' equity decreased and shareholders' equity as a percent of net loans and of total assets increased from 2016 primarily due to an increase in unallocated retained earnings.

Retained Earnings

Our retained earnings increased $9.9 million to $238.1 million at December 31, 2017 from $228.2 million at December 31, 2016 and increased $20.4 million from $217.7 million at December 31, 2015. The increase in 2017 was a result of net income of $13.7 million, partially offset by $3.8 million of patronage distributions declared.

Patronage Program

We have a Patronage Program that allows us to distribute our available net earnings to our shareholders. This program provides for the application of net earnings in the manner described in our Bylaws. In addition to determining the amount and method of patronage to be distributed, the Bylaws address increasing surplus to meet capital adequacy standards established by Regulations; increasing surplus to a level necessary to support competitive pricing at targeted earnings levels; and increasing surplus for reasonable reserves. Patronage distributions are based on business done with us during the year. We paid cash patronage of $4.0 million in 2017, $3.0 million in 2016 and $3.5 million in 2015. During 2017, we declared patronage distributions of $3.8 million to be paid in March 2018.

Stock

Our total stock increased $743 thousand to $4.0 million at December 31, 2017, from $3.3 million at December 31, 2016 and increased from $3.1 million at December 31, 2015. The increase during 2017 was due to $976 thousand of stock issuances and $14 thousand preferred stock dividends paid, partially offset by $247 thousand of stock retirements. We have a Borrower Level Stock Program which allows stock to be assigned to each borrower instead of each loan. This reduces the stock requirements for borrowers with multiple loans. The current stock requirement for each borrower is the lesser of one thousand dollars or 2.00% of the collective total balance of each borrower's loan(s).

Preferred stock is a one cent, at risk, investment stock that can only be purchased by owners of any class of common stock. Dividends are declared and paid at the discretion of the Board of Directors. Dividends accrue daily at a set investment rate and are declared and paid quarterly by purchase of additional preferred stock in the owner's name.

Accumulated Other Comprehensive Income or Loss

Accumulated other comprehensive loss totaled $841 thousand at December 31, 2017, compared with no accumulated other comprehensive income/loss at year-end 2016 and year-end 2015. Certain employees participate in a non-qualified Defined Benefit Pension Restoration Plan (Plan). Accounting guidance requires recognition of the Plan's underfunded status and unamortized actuarial gains and losses and prior service costs or credits as a liability with an offsetting adjustment to accumulated other comprehensive loss.

Capital Plan and Regulatory Requirements

Our Board of Directors establishes a formal capital adequacy plan that addresses capital goals in relation to risks. The capital adequacy plan assesses the capital level necessary for financial viability and to provide for growth. Our

plan is updated annually and approved by our Board of Directors. FCA regulations require the plan consider the following factors in determining optimal capital levels, including:

- Regulatory capital requirements;
- Asset quality;
- Needs of our customer base; and,
- Other risk-oriented activities, such as funding and interest rate risks, contingent and off-balance sheet liabilities and other conditions warranting additional capital.

In 2016, the FCA adopted final rules (the New Capital Regulations) relating to regulatory capital requirements for System banks and Associations. The New Capital Regulations took effect January 1, 2017. The stated objectives of the New Capital Regulations are as follows:

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

The New Capital Regulations, among other things, replaced existing core surplus and total surplus requirements with common equity tier 1 (CET1), tier 1 and total capital (tier 1 plus tier 2) risk-based capital ratio requirements. The New Capital Regulations also added a tier 1 leverage ratio for all System institutions, which replaced the existing net collateral ratio for System banks. In addition, the New Capital Regulations established a capital conservation buffer and a leverage buffer and enhanced the sensitivity of risk weightings. The revisions to the risk-weightings included alternatives to the use of credit ratings, as required by the Dodd-Frank Act.

The New Capital Regulations set the following minimum risk-based requirements:

- A CET1 capital ratio of 4.5 percent;
- A tier 1 capital ratio (CET1 capital plus additional tier 1 capital) of 6 percent; and
- A total capital ratio (tier 1 capital plus tier 2) of 8 percent.

The New Capital Regulations also set a minimum tier 1 leverage ratio (tier 1 capital divided by total assets) of 4 percent, of which at least 1.5 percent must consist of unallocated retained earnings (URE) and URE equivalents, which are nonqualified allocated equities with certain characteristics of URE.

The New Capital Regulations established a capital cushion (capital conservation buffer) of 2.5 percent above the risk-based CET1, tier 1 and total capital requirements. In addition, the New Capital Regulations established a leverage capital cushion (leverage buffer) of 1 percent above the tier 1 leverage ratio requirement. If capital ratios fall below the regulatory minimum plus buffer amounts, capital distributions (equity redemptions, cash dividend payments, and cash patronage payments) and discretionary senior executive bonuses are restricted or prohibited without prior FCA approval. The New Capital Regulations established a three-year phase-in of the capital conservation buffer beginning January 1, 2017. There is no phase-in of the leverage buffer.

As shown in the following table, at December 31, 2017, our capital and leverage ratios exceeded regulatory minimums. If these capital standards are not met, the FCA can impose restrictions, including limiting our ability to pay patronage distributions, retire equities and pay preferred stock dividends.

	2017	Minimum Requirement with Buffer
Common Equity Tier 1 Capital ratio	**19.52%**	7.00%
Tier 1 Capital ratio	**19.52%**	8.50%
Total Capital ratio	**19.74%**	10.50%
Tier 1 Leverage ratio	**20.35%**	5.00%
Unallocated Retained Earnings and URE Equivalents (UREE) Leverage ratio	**20.94%**	1.50%
Permanent capital ratio	**19.81%**	7.00%

The minimum ratios established were not meant to be adopted as the optimum capital level, so we have established goals in excess of the regulatory minimum. As of December 31, 2017, we have exceeded our goals. Due to our strong capital position, we will continue to be able to retire at-risk stock.

As displayed in the following table, we exceeded the minimum regulatory capital requirements in effect through December 31, 2016.

	2016	2015	2014	2013	2012	Regulatory Minimum
Permanent capital ratio	20.17%	19.16%	18.97%	20.00%	21.38%	7.00%
Total surplus ratio	19.85%	18.85%	18.54%	17.86%	19.01%	7.00%
Core surplus ratio	19.85%	18.85%	18.54%	17.57%	18.53%	3.50%

Refer to Note 8, Shareholders' Equity, in this report for additional information on our capital and related requirements and restrictions.

REGULATORY MATTERS

As of December 31, 2017, we had no enforcement actions in effect and FCA took no enforcement actions on us during the year.

GOVERNANCE

Board of Directors

We are governed by a twelve-member board that provides direction and oversees our management. Of these directors, ten are elected by the shareholders and two are appointed by the elected directors. Our Board of Directors represents the interests of our shareholders. The Board of Directors meets regularly to perform the following functions, among others:

- selects, evaluates and compensates the chief executive officer;
- approves the strategic plan, capital plan, financial plan and the annual operating budget;
- oversees the lending operations;
- directs management on significant issues; and,
- oversees the financial reporting process, communications with shareholders and our legal and regulatory compliance.

Director Independence

All directors must exercise sound judgment in deciding matters in our interest. All our directors are independent from the perspective that none of our management or staff serves as Board members. However, we are a financial services cooperative, and the Farm Credit Act and FCA Regulations require our elected directors to have a loan relationship with us.

The elected directors, as borrowers, have a vested interest in ensuring our Association remains strong and successful. However, our borrowing relationship could be viewed as having the potential to compromise the independence of an elected director. For this reason, the Board has established independence criteria to ensure that a loan relationship does not compromise the independence of our Board. Annually, in conjunction with our independence analysis and reporting on our loans to directors, each director provides financial information and any other documentation and/or assertions needed for the Board to determine the independence of each Board member.

Audit & Risk Committee

The Audit & Risk Committee reports to the Board of Directors. The Audit & Risk Committee is composed of six members of the Board of Directors. During 2017, eleven meetings were held. The Audit & Risk Committee responsibilities generally include, but are not limited to:

- oversight of the financial reporting risk and the accuracy of the quarterly and annual shareholder reports;
- the oversight of the system of internal controls related to the preparation of quarterly and annual shareholder reports;
- the review and assessment of the impact of accounting and auditing developments on the consolidated financial statements; and,

- the establishment and maintenance of procedures for the receipt, retention and treatment of confidential and anonymous submission of concerns, regarding accounting, internal accounting controls or auditing matters.

The Audit & Risk Committee is responsible for the oversight of credit risk, including lending and underwriting standards and assesses the conditions that may materially impact the loan portfolio.

Human Resource Committee

The Human Resource Committee is responsible for the oversight of employee and director compensation. The Human Resource Committee is composed of seven members of the Board of Directors. The Committee annually reviews, evaluates and recommends to the full Board for approval the compensation policies, programs and plans for senior officers and employees including benefits programs.

Other Governance

The Board has monitored the requirements of public companies under the Sarbanes-Oxley Act. While we are not subject to the requirements of this law, we are striving to implement steps to strengthen governance and financial reporting. We strive to maintain strong governance and financial reporting through the following actions:

- a system for the receipt and treatment of whistleblower complaints;
- a code of ethics for our President/CEO, Chief Financial Officer, Chief Credit Officer; Chief Operating Officer, Chief Banking Officer and Chief Appraisal Officer;
- open lines of communication between the independent auditors, management, and the Audit Committee;
- “plain English” disclosures;
- officer certification of accuracy and completeness of the consolidated financial statements; and,
- information disclosure through our website.

Code of Ethics

Our directors and employees are responsible for maintaining the highest of standards in conducting our business. In that regard, we established a Code of Ethics for the Board of Directors and all employees, including those who are involved, directly or indirectly, with the preparation of our financial statements and the maintenance of financial records supporting the financial statements. This Codes of Ethics supplements our Standards of Conduct Policies for Directors and Employees. Bi-annually, each employee and director acknowledges and agrees to comply with the Code of Ethics.

Whistleblower Program

We maintain a program for anyone to report complaints related to accounting, financial reporting, internal accounting controls, or auditing matters and all other incidents of misconduct such as theft, harassment, discrimination or collusion. This program allows for the submission of confidential, anonymous concerns regarding accounting, financial reporting, internal accounting controls, fraud or auditing matters and all other incidents of misconduct such as theft, harassment, discrimination or collusion without the fear of reprisal, retaliation or adverse action being taken against any employee who, in good faith, reports or assists in the investigation of a violation or suspected violation, or who makes an inquiry about the appropriateness of an anticipated or actual course of action.

FORWARD-LOOKING INFORMATION

Our discussion 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,” and “will,” or other variations of these terms are intended to identify 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, disease, and other adverse climatic or biological conditions that periodically occur that impact agricultural productivity and income;
- changes in United States government support of the agricultural industry and/or the Farm Credit System; and,
- actions taken by the Federal Reserve System in implementing monetary policy.

CRITICAL ACCOUNTING POLICIES AND ESTIMATES

Our consolidated financial statements are based on accounting principles generally accepted in the United States of America. Our significant accounting policies are critical to the understanding of our results of operations and financial position because some accounting policies require us to make complex or subjective judgments and estimates that may affect the value of certain assets or liabilities. We consider these policies critical because we have to make judgments about matters that are inherently uncertain. For a complete discussion of significant accounting policies, see Note 2 of the accompanying consolidated financial statements. The development and selection of critical accounting policies, and the related disclosures, have been reviewed by our Audit Committee. A summary of critical policies relating to the determination of the allowance for loan losses follows.

Allowance for Loan Losses/Reserve for Unfunded Commitment

The allowance for loan losses is our best estimate of the amount of probable loan losses existing in and inherent in our loan portfolio as of the balance sheet date. The allowance for loan losses is increased through provisions for loan losses and loan recoveries and is decreased through loan loss reversals and loan charge-offs. Additionally, we provide line of credit financing to our customers. We have established a reserve for unfunded commitment to cover probable losses. This reserve is reported as a liability in our consolidated balance sheet. The reserve for unfunded commitment is increased through provision for the reserve for unfunded commitments and is decreased through reversals of the reserve for unfunded commitments. Provision for loan losses and provision for reserve for unfunded commitments are referred to as a provision for credit losses on the Consolidated Statement of Comprehensive Income. We determine the allowance for loan losses and the reserve for unfunded commitment based on a regular evaluation of the loan and commitment portfolios, which generally considers recent historical charge-off experience adjusted for relevant factors.

Loans are evaluated based on the borrower's overall financial condition, resources, and payment record; the prospects for support from any financially responsible guarantor; and, if appropriate, the estimated net realizable value of any collateral. The allowance for loan losses attributable to these loans is established by a process that estimates the probable loss inherent in the loans, taking into account various historical factors, internal risk ratings, regulatory oversight, and geographic, industry and other factors.

Changes in the factors we consider in the evaluation of losses in the loan portfolio could occur for various credit related reasons and could result in a change in the allowance for loan losses, which would have a direct impact on the provision for loan losses and results of operations. See Notes 2 and 3 to the accompanying consolidated financial statements for detailed information regarding the allowance for loan losses.

CUSTOMER PRIVACY

FCA regulations require that borrower information be held in confidence by Farm Credit institutions, their directors, officers and employees. FCA regulations and our Standards of Conduct Policies specifically restrict Farm Credit institution directors and employees from disclosing information not normally contained in published reports or press releases about the institution or its borrowers or members. These regulations also provide Farm Credit institutions clear guidelines for protecting their borrowers' nonpublic information.

OTHER MATTERS

In October 2017, the Association learned that a web portal it used to share documents internally could be accessed through internet search engines without having to enter user credentials. After discovering the incident, the Association's information security team launched a comprehensive investigation to secure, and remove documents from, that portal. The Association also retained third-party forensic investigators who worked with its information security team to determine the nature and scope of the issue. The Association has implemented additional security measures to strengthen its network against similar incidents in the future and has discontinued the use of the web portal. The Association provided written notice of this incident to its shareholders.

PATRON'S CONSENT TO TAKE PATRONAGE DISTRIBUTION INTO INCOME

Our Bylaws under Section 735.6 states that each holder of our stock consent to take into account, as income, at its stated dollar amount as provided in 26 U.S.C. Section 1385, the amount of his or her respective distribution paid as qualified written notice of allocation, which may include stock, allocated surplus, and/or the amount of any distribution that has been applied to the patron's indebtedness as provided in Section 735.4 and 735.5 of our Bylaws.

Consent under this section shall be continuing in effect, provided that consent pursuant to the first paragraph of this section shall cease to be effective with respect to patronage of a distributee occurring after the distributee has ceased to hold stock in us. Consent obtained under this section may be revoked in writing, provided that such revocation shall become effective only with respect to patronage occurring on or after the first day of our first fiscal year beginning after the revocation is filed with us.

FARM CREDIT
OF SOUTHERN COLORADO
The Peak of AgLending

5110 Edison Avenue
Colorado Springs, CO 80915
(719) 570-1087
www.aglending.com

REPORT OF MANAGEMENT

The consolidated financial statements of Farm Credit of Southern Colorado, ACA (Association) are prepared by management, who is responsible for their integrity and objectivity, including amounts that must necessarily be based on judgments and estimates. The consolidated financial statements have been prepared in conformity with generally accepted accounting principles appropriate in the circumstances, and in the opinion of management, fairly present the financial condition of the Association. Other financial information included in the 2017 annual report is consistent with that in the financial statements.

To meet its responsibility for reliable financial information, management depends on 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. To monitor compliance, management engaged Ann Wagner to perform audits of the accounting records, review accounting systems and internal controls, and recommend improvements as appropriate. The Association is also examined by the Farm Credit Administration.

The Audit Committee of the Board of Directors has overall responsibility for the Association's system of internal control and financial reporting. The Audit Committee consults regularly with management and reviews the results of the examinations by the various entities named above. The independent auditors have direct access to the Audit Committee.

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

Gary Pautler
Chairman of the Board

Jeremy M. Anderson
President and Chief Executive Officer

Shawna R. Neppl
Chief Financial Officer

March 16, 2018

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REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING

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

The Association's management has completed an assessment of the effectiveness of internal control over financial reporting as of December 31, 2017. In making the assessment, management used the framework in *Internal Control — Integrated Framework (2013)*, promulgated by the Committee of Sponsoring Organizations of the Treadway Commission, commonly referred to as the "COSO" criteria.

Based on the assessment performed, the Association concluded that as of December 31, 2017, the internal control over financial reporting was effective based upon the COSO criteria. Additionally, based on this assessment, the Association determined that there were no material weaknesses in the internal control over financial reporting as of December 31, 2017.

Jeremy M. Anderson
President and Chief Executive Officer

Shawna R. Neppl
Chief Financial Officer

March 16, 2018

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AUDIT & RISK COMMITTEE REPORT

The Audit & Risk Committee (Committee) includes five (5) members from the Board of Directors of Farm Credit of Southern Colorado, ACA (Association). In 2017, eleven (11) Committee meetings were held. The Committee oversees the scope of the Association's internal audit program, the independence of the outside auditors, the adequacy of the Association's 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 responsibilities are described more fully in the Internal Control Policy and the Audit & Risk Committee Charter. The Committee approved the appointment of PricewaterhouseCoopers, LLP (PwC) as the Association's independent auditors for 2017.

The fees for professional services rendered for the Association by its independent auditor, PwC, during 2017 were $49,200 for audit services and $7,700 for tax services.

Management is responsible for the Association's internal controls and the preparation of the consolidated financial statements in accordance with accounting principles generally accepted in the United States of America. PwC is responsible for performing an independent audit of the Association's consolidated financial statements in accordance with auditing standards generally accepted in the United States of America and to issue a report thereon. The Committee's responsibilities include monitoring and overseeing these processes.

In this context, the Committee reviewed and discussed the Association's Quarterly Reports and the Association's audited financial statements for the year ended December 31, 2017 (the "Financial Statements") with management. The Committee also reviews with PwC the matters required to be discussed by Statements on Auditing Standards. Both PwC and the Association's internal auditors directly provide reports on significant matters to the Committee.

Based on the foregoing review and discussions and relying thereon, the Committee recommended that the Board of Directors include the Financial Statements in the Association's Annual Report to Shareholders for the year ended December 31, 2017 and for filing with the Farm Credit Administration.

Mark Peterson, Chairman of the Audit & Risk Committee

Audit & Risk Committee Members
Colin Durham Rosalie Martinez Gary Pautler
Mark Peterson Paul Prentice

March 16, 2018

Report of Independent Auditors

To the Board of Directors of
Farm Credit of Southern Colorado, ACA

We have audited the accompanying consolidated financial statements of Farm Credit of Southern Colorado, ACA and its subsidiaries (the Association), which comprise the consolidated statements of condition as of December 31, 2017, 2016 and 2015, and the related consolidated statements of comprehensive income, of changes in shareholders' 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.

Auditors' Responsibility

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

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

Opinion

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of Farm Credit of Southern Colorado, ACA and its subsidiaries as of December 31, 2017, 2016, and 2015, and the results of their operations and their cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

PricewaterhouseCoopers LLP

March 16, 2018

PricewaterhouseCoopers LLP, 1100 Walnut St. Kansas City, MO 64106
T: (816) 472 7921, F: (816) 218 1890, *www.pwc.com/us*

Consolidated Statement of Condition

(Dollars in Thousands)

	December 31		
	2017	2016	2015
ASSETS			
Loans	**$ 981,997**	$ 943,326	$ 930,505
Less allowance for loan losses	**2,261**	1,535	1,474
Net loans	**979,736**	941,791	929,031
Cash	**6,886**	5,035	5,691
Accrued interest receivable	**15,796**	14,337	13,309
Investment in CoBank, ACB	**31,487**	30,876	29,954
Premises and equipment, net	**12,172**	12,642	13,254
Other property owned	**2,378**	2,575	1,752
Prepaid benefit expense	**1,645**	1,105	433
Other assets	**4,737**	4,688	4,298
Total assets	**$ 1,054,837**	$ 1,013,049	$ 997,722
LIABILITIES			
Note payable to CoBank, ACB	**$ 796,825**	$ 765,542	$ 761,665
Advance conditional payments	**5,923**	7,248	7,108
Accrued interest payable	**1,358**	1,236	1,182
Patronage distributions payable	**3,750**	4,000	3,000
Accrued benefits liability	**1,018**	189	202
Reserve for unfunded commitments	**382**	270	457
Other liabilities	**4,252**	3,101	3,261
Total liabilities	**813,508**	781,586	776,875
Commitments and Contingencies (See Note 14)			
SHAREHOLDERS' EQUITY			
Preferred stock	**2,619**	1,879	1,761
Capital stock	**1,410**	1,407	1,375
Unallocated retained earnings	**238,141**	228,177	217,711
Accumulated other comprehensive income/(loss)	**(841)**	-	-
Total shareholders' equity	**241,329**	231,463	220,847
Total liabilities and shareholders' equity	**$ 1,054,837**	$ 1,013,049	$ 997,722

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

Consolidated Statement of Comprehensive Income

(Dollars in Thousands)

	For the Year Ended December 31		
	2017	2016	2015
INTEREST INCOME			
Loans	**$ 44,031**	$ 41,108	$ 39,394
Total interest income	**44,031**	41,108	39,394
INTEREST EXPENSE			
Note payable to CoBank, ACB	**17,338**	15,453	14,881
Other	**15**	7	5
Total interest expense	**17,353**	15,460	14,886
Net interest income	**26,678**	25,648	24,508
Provision for credit losses	**822**	368	747
Net interest income after provision for credit losses	**25,856**	25,280	23,761
NONINTEREST INCOME			
Financially related services income	**179**	122	137
Loan fees	**387**	524	505
Patronage distribution from Farm Credit institutions	**3,541**	3,760	3,418
Mineral income	**657**	642	1,196
Other noninterest income	**67**	87	101
Total noninterest income	**4,831**	5,135	5,357
NONINTEREST EXPENSE			
Salaries and employee benefits	**9,577**	8,754	8,517
Occupancy and equipment	**1,313**	1,219	1,227
Purchased services from AgVantis, Inc.	**1,593**	1,710	1,270
Losses on other property owned, net	**265**	109	1,020
Farm Credit Insurance Fund premium	**1,089**	1,220	918
Supervisory and examination costs	**362**	349	302
Other noninterest expense	**2,753**	2,574	2,458
Total noninterest expense	**16,952**	15,935	15,712
Income before income taxes	**13,735**	14,480	13,406
Provision for income taxes	**5**	5	5
Net income	**13,730**	14,475	13,401
COMPREHENSIVE INCOME			
Actuarial loss in retirement obligation	**(841)**	-	-
Comprehensive income	**$ 12,889**	$ 14,475	$ 13,401

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

Consolidated Statement of Changes in Shareholders' Equity

(Dollars in Thousands)

	Protected Borrower Stock	Preferred Stock	Capital Stock	Unallocated Retained Earnings	Accumulated Other Comprehensive Income/(Loss)	Total Shareholders' Equity
Balance at December 31, 2014	$ 2	$ 2,863	$ 1,328	$ 207,319	$ -	$ 211,512
Comprehensive income				13,401	-	13,401
Stock issued	-	525	197			722
Stock retired	(2)	(1,637)	(150)			(1,789)
Preferred stock dividends		10		(9)		1
Patronage distributions: Cash				(3,000)		(3,000)
Balance at December 31, 2015	-	1,761	1,375	217,711	-	220,847
Comprehensive income				14,475	-	14,475
Stock issued	-	225	168			393
Stock retired	-	(116)	(136)			(252)
Preferred stock dividends		9		(9)		-
Patronage distributions: Cash				(4,000)		(4,000)
Balance at December 31, 2016	-	1,879	1,407	228,177	-	231,463
Comprehensive income				13,730	(841)	12,889
Stock issued	-	842	134			976
Stock retired	-	(116)	(131)			(247)
Preferred stock dividends		14		(16)		(2)
Patronage distributions: Cash				(3,750)		(3,750)
Balance at December 31, 2017	**$ -**	**$ 2,619**	**$ 1,410**	**$ 238,141**	**$ (841)**	**$ 241,329**

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

Consolidated Statement of Cash Flows

(Dollars in Thousands)

	2017	2016	2015
CASH FLOWS FROM OPERATING ACTIVITIES:			
Net income	**$ 13,730**	$ 14,475	$ 13,401
Adjustments to reconcile net income to net cash provided by/(used in) operating activities:			
Depreciation	**712**	708	704
Provision for credit losses	**822**	368	747
Patronage stock from CoBank, ACB	**(13)**	(18)	(17)
Allocated patronage from AgVantis	**-**	(226)	(38)
Losses/(Gains) on sales of premises and equipment	**19**	5	(13)
Losses on sale of other property owned	**-**	-	757
Carrying value adjustment for other property owned	**172**	109	-
Change in assets and liabilities:			
Increase in accrued interest receivable	**(1,459)**	(1,028)	(1,483)
(Increase)/Decrease in prepaid benefit expense	**(540)**	(672)	169
Increase in other assets	**(36)**	(146)	(61)
Increase/(Decrease) in accrued interest payable	**122**	54	(3,443)
Decrease in accrued benefits liability	**(12)**	(13)	(2)
Increase/(Decrease) in other liabilities	**1,149**	(160)	373
Total adjustments	**936**	(1,019)	(2,307)
Net cash provided by operating activities	**14,666**	13,456	11,094
CASH FLOWS FROM INVESTING ACTIVITIES:			
Increase in loans, net	**(38,655)**	(14,247)	(31,067)
Increase in investment in CoBank, ACB	**(611)**	(922)	(531)
Expenditures for premises and equipment, net	**(261)**	(101)	(811)
Proceeds from sales of other property owned	**25**	-	2,889
Net cash used in investing activities	**(39,502)**	(15,270)	(29,520)
CASH FLOWS FROM FINANCING ACTIVITIES:			
Net draw on note payable to CoBank, ACB	**31,283**	3,877	21,331
(Decrease)/Increase in advance conditional payments	**(1,325)**	140	(36)
Protected borrower stock retired	**-**	-	(2)
Preferred stock retired	**(116)**	(116)	(1,637)
Preferred stock issued	**842**	225	525
Capital stock retired	**(131)**	(136)	(150)
Capital stock issued	**134**	168	197
Cash patronage distributions paid	**(4,000)**	(3,000)	(3,500)
Net cash provided by financing activities	**26,687**	1,158	16,728
Net increase/(decrease) in cash	**1,851**	(656)	(1,698)
Cash at beginning of year	**5,035**	5,691	7,389
Cash at end of year	**$ 6,886**	$ 5,035	$ 5,691
SUPPLEMENTAL CASH INFORMATION:			
Cash paid during the year for:			
Interest	**$ 17,231**	$ 15,406	$ 18,329
Income taxes	**$ 5**	$ 7	$ 5
SUPPLEMENTAL SCHEDULE OF NON-CASH INVESTING AND FINANCING ACTIVITIES:			
Patronage stock from CoBank, ACB	**$ 13**	$ 18	$ 17
Allocated patronage from AgVantis	**$ -**	$ 226	$ 38
Loans transferred to other property owned	**$ -**	$ 932	$ -
Net (recoveries)/charge-offs	**$ (16)**	$ 494	$ 229
Patronage distributions payable	**$ 3,750**	$ 4,000	$ 3,000
Stock dividends paid	**$ 14**	$ 9	$ 10
Stock dividends declared	**$ 16**	$ 9	$ 9
Change in accumulated other comprehensive (loss)/income	**$ (841)**	$ -	$ -

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

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(Dollars in Thousands, Except as Noted)

NOTE 1 – ORGANIZATION AND OPERATIONS

A. Organization: Farm Credit of Southern Colorado, ACA and its subsidiaries, Farm Credit of Southern Colorado, FLCA, (Federal Land Credit Association (FLCA)) and Farm Credit of Southern Colorado, PCA, (Production Credit Association (PCA)), (collectively called "the Association") are member-owned cooperatives which provide credit and credit-related services to or for the benefit of eligible borrowers/shareholders for qualified agricultural purposes in the counties of Alamosa, Arapahoe, Archuleta, Baca, Bent, Chaffee, Cheyenne, Conejos, Costilla, Crowley, Custer, Douglas, El Paso, Elbert, Fremont, Hinsdale, Huerfano, Kiowa, Kit Carson, Lake, Las Animas, Lincoln, Mineral, Otero, Park, Prowers, Pueblo, Rio Grande, Saguache, Teller, and the southern half of Jefferson in the state of Colorado.

The Association is a lending institution of the Farm Credit System (System), a nationwide system of cooperatively owned banks and associations, which 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 (the Farm Credit Act). The System is comprised of three Farm Credit Banks, one Agricultural Credit Bank and 69 associations.

CoBank, ACB (funding bank or the "Bank") its related associations and AgVantis, Inc. (AgVantis) are collectively referred to as the District. CoBank provides the funding to associations within the District and is responsible for supervising certain activities of the District Associations. AgVantis, which is owned by the entities it serves, provides technology and other operational services to certain associations and to CoBank. The CoBank District consists of CoBank, 22 Agricultural Credit Associations (ACA), which each have two wholly owned subsidiaries, (a FLCA and a PCA) and AgVantis.

ACA parent companies provide financing and related services through their FLCA and PCA subsidiaries. Generally, the FLCA makes secured long-term agricultural real estate and rural home mortgage loans and 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 institutions to ensure their compliance with the Farm Credit Act, FCA regulations and safe and sound banking practices.

The Farm Credit Act established the Farm Credit System Insurance Corporation (Insurance Corporation) to administer the Farm Credit Insurance Fund (Insurance Fund). By law, the Insurance Fund is required to be used (1) to ensure the timely payment of principal and interest on Systemwide debt obligations (Insured Debt), (2) to ensure the retirement of protected stock at par or stated value, and (3) for other specified purposes. The Insurance Fund is also available for discretionary use by the Insurance Corporation in providing assistance to certain troubled System institutions and to cover the operating expenses of the Insurance Corporation. Each System Bank is required to pay premiums, which may be passed on to the Associations, into the Insurance Fund based on its annual average outstanding insured debt adjusted to reflect the reduced risk on loans or investments guaranteed by federal or state governments until the assets 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 Debt or such other percentage of the Insured Debt 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 Insurance Corporation is required to reduce premiums, as necessary to maintain the Insurance Fund at the 2.0 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. The Bank passes this premium expense and the return of excess funds as applicable through to each Association based on the Association's average adjusted note payable with the Bank.

B. Operations: The Farm Credit Act sets forth the types of authorized lending activity, persons eligible to borrow, and financial services which can be provided 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, their cooperatives, rural residents and farm-related businesses.

The Association also offers credit life insurance, multi-peril crop and crop hail insurance, advance conditional payment accounts, leasing and provides additional services to borrowers such as fee appraisals and an investment stock program.

The Association's financial condition may be impacted by factors affecting CoBank. The CoBank Annual Report is available free of charge on CoBank's website, www.cobank.com; or may be obtained at no charge by contacting the Association at 5110 Edison Avenue, Colorado Springs, Colorado 80915, or at PO Box 75640, Colorado Springs, Colorado 80970-5640 or by calling (800) 815-8559 or (719) 570-1087. Upon request, Association shareholders will be provided with a copy of the CoBank Annual Report. The CoBank Annual Report discusses the material aspects of CoBank's and District's financial condition, changes in financial condition, and results of operations.

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 financial statements in conformity with GAAP requires Association management to make estimates and assumptions that affect the amounts reported in the consolidated financial statements and accompanying notes. Actual results may differ from these estimates. Significant estimates are discussed in these footnotes as applicable. Certain amounts in prior years' consolidated financial statements have been reclassified to conform to the current year's financial statement presentation.

The consolidated financial statements include the accounts of Farm Credit of Southern Colorado, FLCA and Farm Credit of Southern Colorado, PCA. All significant inter-company transactions have been eliminated in consolidation. Recently issued accounting pronouncements follow.

In March 2017, the Financial Accounting Standards Board (FASB) issued guidance entitled "Improving the Presentation of Net Periodic Pension Cost and Net Periodic Postretirement Cost." The guidance requires that an employer report the service cost component in the same line item or items as other compensation costs arising from services rendered by the pertinent employees during the period. Other components are required to be presented in the income statement separately from the service cost component and outside a subtotal of income from operations, if one is presented. This guidance becomes effective for interim and annual periods beginning after December 15, 2017. The adoption of this guidance is not expected to impact the Association's financial condition but could change the classification of certain items in the results of operations.

In August 2016, the FASB issued guidance entitled "Classification of Certain Cash Receipts and Cash Payments." The guidance addresses specific cash flow issues with the objective of reducing the diversity in the classification of these cash flows. Included in the cash flow issues are debt prepayment or debt extinguishment costs and settlement of zero-coupon debt instruments or other debt instruments with coupon interest rates that are insignificant in relation to the effective interest rate of the borrowing. This guidance becomes effective for interim and annual periods beginning after December 15, 2017. The adoption of this guidance is not expected to impact the Association's financial condition or its results of operations but could change the classification of certain items in the statement of cash flows.

In June 2016, the FASB issued guidance entitled "Measurement of Credit Losses on Financial Instruments." The guidance replaces the current incurred loss impairment methodology with a methodology that reflects expected credit losses and requires consideration of a broader range of reasonable and supportable information to inform credit loss estimates. Credit losses relating to available-for-sale securities would also be recorded through an allowance for credit losses. For public business entities that are not U.S. Securities and Exchange commission filers this guidance becomes effective for interim and annual periods beginning after December 15, 2020, with early application permitted. The Association is evaluating the impact of adoption on its financial condition and its results of operations.

In February 2016, the FASB issued guidance entitled "Leases." The guidance requires the recognition by lessees of lease assets and lease liabilities on the balance sheet for the rights and obligations created by those leases. Leases with lease terms of more than 12 months are impacted by this guidance. This guidance becomes effective for interim and annual periods beginning after December 15, 2018, with early application permitted. The Association is evaluating the impact of adoption on its financial condition and results of operations.

In January 2016, the FASB issued guidance entitled "Recognition and Measurement of Financial Assets and Liabilities." The guidance affects, among other things, the presentation and disclosure requirements for financial instruments. For public entities, the guidance eliminates the requirement to disclose the methods and significant assumptions used to estimate the fair value of financial instruments carried at amortized cost. This guidance

becomes effective for interim and annual periods beginning after December 15, 2017. The adoption of this guidance did not impact the Association's financial condition or its results of operations.

In May 2014, the FASB issued guidance entitled, "Revenue from Contracts with Customers." The guidance governs revenue recognition from contracts with customers and requires an entity to recognize revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. Financial instruments and other contractual rights within the scope of other guidance issued by the FASB are excluded from the scope of this new revenue recognition guidance. In this regard, a majority of our contracts would be excluded from the scope of this new guidance. In August 2015, the FASB issued an update that defers this guidance by one year, which results in the new revenue standard becoming effective for interim and annual reporting periods beginning after December 15, 2017. The Association determined the effect was not material to its financial condition or results of operations.

Below is a summary of our significant accounting policies.

A. Loans and Allowance for Loan Losses: Long-term real estate mortgage loans generally have original maturities ranging from five to 40 years. Substantially all short- and intermediate-term loans made for agricultural production or operating purposes have maturities of ten 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. Loan origination fees and direct loan origination costs are capitalized and the net fee or cost is amortized over the life of the related loan as an adjustment to yield.

   Impaired loans are loans for which it is probable that principal and interest will not 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 contract 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 is collected in full or otherwise discharged.

   Impaired loans are generally placed in nonaccrual status when principal or interest is delinquent for 90 days or more (unless adequately collateralized and in the process of collection) or when 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 reversed (if accrued in the current year) and/or included in the recorded nonaccrual balance (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.

   When loans are in nonaccrual status, loan payments are generally applied against the recorded nonaccrual balance. A nonaccrual loan may, at times, be maintained on a cash basis. As a cash basis nonaccrual loan, the recognition of interest income from cash payments received is allowed when the collectability of the recorded investment in the loan is no longer in doubt and the loan does not have a remaining unrecovered charge-off associated with it. Nonaccrual loans may be returned to accrual status when all contractual principal and interest is 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.

   In cases where a borrower experiences financial difficulties and the Association makes certain monetary concessions to the borrower through modifications to the contractual term of the loan, the loan is classified as a restructured loan. If the borrower's ability to meet the revised payment schedule is uncertain, the loan is classified as a nonaccrual loan.

   The Association purchases loan participations from other System and non-System entities to generate additional earnings and diversify risk. Additionally, the Association sells a portion of certain large loans to other System entities to reduce risk and comply with established lending limits. Loans are accounted for following the accounting requirements for sale treatment.

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

Each of the 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 and grows significantly as a loan moves to a substandard (viable) level. A substandard (non-viable) rating indicates that the probability of default is almost certain.

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 and estimable losses inherent in the loan portfolio. The allowance is increased through provision for loan losses and loan recoveries and is decreased through loan loss reversals and loan charge-offs. The allowance is based on a periodic evaluation of the loan portfolio by management in which numerous factors are considered, including economic conditions, environmental conditions, loan portfolio composition, collateral value, portfolio quality, current production 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 collateral that, by their nature, contain elements of uncertainty, imprecision and variability. Changes in the agricultural economy and environment and their impact on borrower repayment capacity will cause various judgments, evaluations and appraisals to change over time. Accordingly, actual circumstances could vary significantly from the Association's expectations and predictions of those circumstances. Management considers the following macro-economic factors in determining and supporting the level of allowance for loan losses: the concentration of lending in agriculture, combined with uncertainties associated with farmland values, commodity prices, exports, government assistance programs, regional economic effects and weather-related influences.

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, 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 as previously discussed.

B. Cash: Cash, as included in the consolidated financial statements, represents cash on hand and on deposit at financial institutions. At times, cash deposits may be in excess of federally insured limits.

C. Investment in CoBank: The Association's required investment in CoBank is in the form of Class A Stock. The minimum required investment is 4.00 percent of the prior year's average direct loan volume. The investment in CoBank is comprised of patronage based stock and purchased stock. The requirement for capitalizing patronage-based participation loans sold to CoBank is 8.00 percent of the prior ten-year average of such participations sold to CoBank.

D. Premises and Equipment: Land is carried at cost. Premises and equipment are carried at cost less accumulated depreciation. Depreciation is provided on the straight-line method over the estimated useful lives of the assets. Estimated useful life ranges from 20 to 40 years for buildings, 1 to 10 years for furniture and equipment and 1 to 5 years for automobiles. Gains and losses on dispositions are reflected in current operating results. Maintenance and repairs are expensed and improvements above certain thresholds are capitalized.

E. Other Property Owned: Other property owned, consisting of real and personal property acquired through foreclosure or deed in lieu of foreclosure, is recorded at fair value less estimated selling costs upon acquisition. Any initial reduction in the carrying amount of a loan to the fair value of the collateral received is charged to the allowance for loan losses. On at least an annual basis, revised estimates to the fair value are

reported as adjustments to the carrying amount of the asset, provided that such adjusted value is not in excess of the carrying amount at acquisition. Income and expenses from operations and carrying value adjustments are included in net gains/(losses) on other property owned in the Consolidated Statement of Comprehensive Income.

F. Other Assets and Other Liabilities: Other assets are comprised primarily of accounts receivable, prepaid expenses, and investment in Farm Credit institutions. Significant components of other liabilities primarily include accounts payable and employee benefits.

G. Advance Conditional Payments: The Association is authorized under the Farm Credit Act to accept advance payments from borrowers. To the extent the borrower's access to such advance payments is restricted, the advance conditional payments are netted against the borrower's related loan balance. Unrestricted advance conditional payments are included in liabilities. Restricted advance conditional payments are primarily associated with mortgage loans, while non-restricted are primarily related to production and intermediate-term loans and insurance proceeds on mortgage loans. Advance conditional payments are not insured. Interest is generally paid by the Association on advance conditional payments.

H. Employee Benefit Plans: Substantially all employees of the Association participate in the Ninth Farm Credit District Pension Plan (Pension Plan) and/or the Farm Credit Foundations Defined Contribution/401(k) Plan (401(k) Plan). The Pension Plan is a non-contributory defined benefit plan. Benefits are based on compensation and years of service. The Association recognizes its proportional share of expense and contributes its proportional share of funding. The Pension Plan was closed to employees beginning January 1, 2007.

The 401(k) Plan has two components. Employees who do not participate in the Pension Plan may receive benefits through the Employer Contribution portion of the Defined Contribution Plan. In this plan, the Association provides a monthly contribution based on a defined percentage of the employee's salary. Employees may also participate in a Salary Deferral Plan governed by Section 401(k) of the Internal Revenue code. The Association matches a certain percentage of employee contributions. All defined contribution costs are expensed in the same period that participants earn employer contributions.

The Association also participates in the Farm Credit Foundations Retiree Medical Plan. These postretirement benefits (other than pensions) are provided to eligible retired employees of the Association. The anticipated costs of these benefits were accrued during the period of the employee's active service. The authoritative accounting guidance requires the accrual of the expected cost of providing postretirement benefits during the years that the employee renders service necessary to become eligible for these benefits.

The Association also participates in the Ninth District nonqualified defined benefit Pension Restoration Plan. This plan provides retirement benefits above the Internal Revenue Code compensation limit to certain highly compensated eligible employees. Benefits payable under this plan are offset by the benefits payable from the pension plan.

I. Patronage Distribution from CoBank: Patronage distributions from CoBank are accrued by the Association in the year earned.

J. Income Taxes: As previously described, the ACA holding company conducts its business activities through two wholly owned subsidiaries. Long-term mortgage lending activities are operated through a wholly owned FLCA subsidiary which is exempt from federal and state income tax. Short- and intermediate-term lending activities are operated through a 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 taxes. The Association accounts for income taxes under the liability method. Accordingly, deferred taxes are recognized for estimated taxes ultimately payable or recoverable based on federal, state or local laws.

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 distributions. Deferred taxes are recorded on the tax effect of all temporary differences based on the assumption that such temporary differences are retained by the Association and will therefore impact future tax payments. A valuation allowance is provided against deferred tax assets to

the extent that it is more likely than not (over 50 percent probability), based on management's estimate, the deferred tax assets 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.

Deferred income taxes have not been recorded by the Association on stock patronage distributions received from the Bank prior to January 1, 1993, the adoption date of accounting guidance on income taxes. Association management's intent is to permanently invest these and other undistributed earnings in CoBank, or if converted to cash, to pass through any such earnings to Association borrowers through qualified patronage allocations.

The Association has not provided deferred income taxes on amounts allocated to the Association which relate to the Bank's post-1992 earnings to the extent that such earnings will be passed through to Association borrowers through qualified patronage allocations. Additionally, deferred income taxes have not been provided on the Bank's post-1992 unallocated earnings.

K. Other Comprehensive Income/Loss: Other comprehensive income refers to revenue, expenses, gains and losses that under GAAP are recorded as an element of shareholders' equity and comprehensive income but are excluded from net income. Accumulated other comprehensive income/loss refers to the balance of these transactions. The Association records other comprehensive income/loss associated with the liability under the Pension Restoration Plan.

L. Fair Value Measurement: Accounting 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 include assets held in trust funds which relate to the Association's deferred compensation plan and supplemental retirement plan. The trust funds include investments that are actively traded and have quoted net asset values that are observable in the marketplace.

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.

Level 3 — Unobservable inputs are those that are supported by little or no market activity and that are significant to the determination of the fair value of the assets or liabilities. These unobservable inputs reflect the reporting entity's own assumptions about factors that market participants would use in pricing the asset or liability. Level 3 assets and liabilities include financial instruments whose values are 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. Level 3 assets include other property owned.

The fair value disclosures are presented in Note 15.

M. 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 – LOANS AND ALLOWANCE FOR LOAN LOSSES

A summary of loans follows.

	December 31		
	2017	2016	2015
Real estate mortgage	**$ 573,590**	$ 539,889	$ 546,271
Production and intermediate-term	**180,294**	182,932	166,406
Agribusiness	**147,501**	148,944	137,009
Rural infrastructure	**70,877**	61,716	70,895
Agricultural export finance	**8,506**	8,513	8,528
Rural residential real estate	**57**	107	121
Mission-related	**1,172**	1,225	1,275
Total loans	**$ 981,997**	$ 943,326	$ 930,505

The Association purchases or sells loan participations with other parties in order to diversify risk, manage loan volume and comply with FCA regulations. The following table presents information regarding participations purchased and sold as of December 31, 2017:

	Other Farm Credit Institutions		Non-Farm Credit Institutions		Total	
	Purchased	Sold	Purchased	Sold	Purchased	Sold
Real estate mortgage	$ 26,769	$ 19,899	$ 4,105	$ –	$ 30,874	$ 19,899
Production and intermediate-term	21,153	234	–	–	21,153	234
Agribusiness	139,519	–	–	–	139,519	–
Rural infrastructure	70,877	–	–	–	70,877	–
Agricultural export finance	8,506	–	–	–	8,506	–
Total	$ 266,824	$ 20,133	$ 4,105	$ –	$ 270,929	$ 20,133

A substantial portion of the Association's loans are collateralized. 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 first liens on the underlying real property. Federal regulations state that long-term real estate loans are not to exceed 85 percent (97 percent if guaranteed or enhanced by a government agency) of the property's appraised value. However, a decline in a property's market value subsequent to loan origination or advances, or other actions necessary to protect the financial interest of the Association in the collateral, may result in loan to value ratios in excess of the regulatory maximum.

Credit enhancements with federal government agencies of $18,036 at year-end 2017, $18,349 at year-end 2016 and $15,789 at year-end 2015 were outstanding. These credit enhancements consist primarily of loans in the USDA FSA Guaranteed Loan Program. To incent the Association to make certain loans we could not normally underwrite, the USDA typically will guarantee 90% of the loss on the debt. This program is a valuable tool used to manage credit to young/beginning/small borrowers, as well as high risk credit groups. Using the program creates constructive credit for both the borrower and the lender.

One credit quality indicator utilized by the Association is the Farm Credit Administration 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 FCA Uniform Loan Classification system as a percentage of total loans and related accrued interest receivable by loan type as of December 31.

	2017	2016	2015
Real estate mortgage			
Acceptable	**91.90%**	91.83%	94.36%
OAEM	**2.55%**	3.17%	3.60%
Substandard	**5.55%**	5.00%	2.04%
Total	**100.00%**	100.00%	100.00%
Production and intermediate-term			
Acceptable	**91.01%**	86.42%	96.13%
OAEM	**4.31%**	7.29%	2.57%
Substandard	**4.68%**	6.29%	1.30%
Total	**100.00%**	100.00%	100.00%
Agribusiness			
Acceptable	**99.10%**	97.81%	95.96%
OAEM	**0.32%**	1.14%	2.56%
Substandard	**0.58%**	1.05%	1.48%
Total	**100.00%**	100.00%	100.00%
Rural infrastructure			
Acceptable	**100.00%**	96.56%	93.77%
OAEM	**–**	3.44%	4.35%
Substandard	**–**	–	1.88%
Total	**100.00%**	100.00%	100.00%
Agricultural export finance			
Acceptable	**100.00%**	100.00%	100.00%
Total	**100.00%**	100.00%	100.00%
Rural residential real estate			
Acceptable	**100.00%**	100.00%	100.00%
Total	**100.00%**	100.00%	100.00%
Mission related			
Acceptable	**100.00%**	100.00%	100.00%
Total	**100.00%**	100.00%	100.00%
Total Loans			
Acceptable	**93.46%**	92.10%	94.93%
OAEM	**2.34%**	3.64%	3.28%
Substandard	**4.20%**	4.26%	1.79%
Total	**100.00%**	100.00%	100.00%

Impaired loans are loans for which it is probable that all principal and interest will not be collected according to the contractual terms. The following presents information relating to impaired loans including accrued interest.

	December 31		
	2017	2016	2015
Nonaccrual loans:			
Current as to principal and interest	**$ 11,213**	$ 1,420	$ 5,594
Past due	**1,096**	4,391	2,149
Total nonaccrual loans	**12,309**	5,811	7,743
Impaired accrual loans:			
Restructured	**1,236**	2,103	224
Accrual loans 90 days or more past due	**–**	–	457
Total impaired accrual loans	**1,236**	2,103	681
Total impaired loans	**$ 13,545**	$ 7,914	$ 8,424

Commitments to lend additional funds to debtors whose loans were classified as impaired at December 31, 2017 totaled $791. These commitments were considered when establishing the reserve for unfunded commitments which is recorded in liabilities.

High risk assets consist of impaired loans and other property owned. The following table presents these in a more detailed manner than the previous table. These nonperforming assets (including related accrued interest) are as follows:

	December 31		
	2017	2016	2015
Nonaccrual loans			
Real estate mortgage	**$ 10,723**	$ 4,391	$ 4,503
Production and intermediate-term	**1,586**	1,420	1,907
Rural infrastructure	**–**	–	1,333
Total nonaccrual loans	**12,309**	5,811	7,743
Accruing restructured loans			
Real estate mortgage	**519**	97	100
Production and intermediate-term	**717**	727	124
Rural infrastructure	–	1,279	–
Total accruing restructured loans	**1,236**	2,103	224
Accruing loans 90 days past due			
Real estate mortgage	**–**	–	457
Total impaired loans	**13,545**	7,914	8,424
Other property owned	**2,378**	2,575	1,752
Total high risk assets	**$ 15,923**	$ 10,489	$ 10,176

Additional impaired loan information is as follows:

	Recorded Investment at 12/31/17	Unpaid Principal Balance*	Related Allowance	Average Impaired Loans	Interest Income Recognized
Impaired loans with no related allowance for credit losses:					
Real estate mortgage	$ 11,242	$ 15,274		$ 5,433	$ 147
Production and intermediate-term	2,303	6,894		1,712	76
Total	$ 13,545	$ 22,168	$ –	$ 7,145	$ 223

The Association had no impaired loans with a related allowance at December 31, 2017.

	Recorded Investment at 12/31/16	Unpaid Principal Balance*	Related Allowance	Average Impaired Loans	Interest Income Recognized
Impaired loans with a related allowance for credit losses:					
Real estate mortgage	$ –	$ –	$ –	$ 168	$ –
Production and intermediate-term	–	–	–	1,435	–
Total	$ –	$ –	$ –	$ 1,603	$ –
Impaired loans with no related allowance for credit losses:					
Real estate mortgage	$ 4,488	$ 4,525		$ 9,458	$ 176
Production and intermediate-term	2,147	6,518		1,730	23
Agribusiness	–	–		96	–
Rural infrastructure	1,279	1,601		1,390	67
Total	$ 7,914	$ 12,644		$ 12,674	$ 266
Total impaired loans:					
Real estate mortgage	$ 4,488	$ 4,525	$ –	$ 9,626	$ 176
Production and intermediate-term	2,147	6,518	–	3,165	23
Agribusiness	–	–	–	96	–
Rural infrastructure	1,279	1,601	–	1,390	67
Total	$ 7,914	$ 12,644	$ –	$ 14,277	$ 266

	Recorded Investment at 12/31/15	Unpaid Principal Balance*	Related Allowance	Average Impaired Loans	Interest Income Recognized
Impaired loans with a related allowance for credit losses:					
Real estate mortgage	$ 254	$ 592	$ 76	$ 173	$ –
Production and intermediate-term	10	11	–	2,214	–
Total	$ 264	$ 603	$ 76	$ 2,387	$ –
Impaired loans with no related allowance for credit losses:					
Real estate mortgage	$ 4,806	$ 4,776		$ 10,748	$ 651
Production and intermediate-term	2,021	6,582		674	61
Agribusiness	–	–		32	12
Rural infrastructure	1,333	1,666		1,376	–
Total	$ 8,160	$ 13,024		$ 12,830	$ 724
Total impaired loans:					
Real estate mortgage	$ 5,060	$ 5,368	$ 76	$ 10,921	$ 651
Production and intermediate-term	2,031	6,593	–	2,888	61
Agribusiness	–	–	–	32	12
Rural infrastructure	1,333	1,666	–	1,376	–
Total	$ 8,424	$ 13,627	$ 76	$ 15,217	$ 724

* Unpaid principal balance represents the recorded principal balance of the loan

Interest income is recognized and cash payments are applied on nonaccrual impaired loans as described in Note 2. The following table presents interest income recognized on impaired loans.

	Year Ended December 31		
	2017	2016	2015
Interest income recognized on:			
Nonaccrual loans	**$ 112**	$ 101	$ 682
Restructured accrual loans	**55**	83	12
Accrual loans 90 days or more past due	**56**	82	30
Interest income recognized on impaired loans	**$ 223**	$ 266	$ 724

Interest income on nonaccrual and accruing restructured loans that would have been recognized under the original terms of the loans follows.

	Year Ended December 31		
	2017	2016	2015
Interest income which would have been recognized under the original loan terms	**$1,225**	$1,001	$1,111
Less: interest income recognized	**167**	184	694
Interest income not recognized	**$1,058**	$ 817	$ 417

The following table provides an age analysis of past due loans (including accrued interest).

December 31, 2017	30-89 Days Past Due	90 Days or More Past Due	Total Past Due	Not Past Due or less than 30 Days Past Due	Recorded Investment in Loans Outstanding	Recorded Investment > 90 Days and Accruing
Real estate mortgage	$ 778	$ –	$ 778	$ 583,492	$ 584,270	$ –
Production and intermediate-term	1,815	212	2,027	182,285	184,312	–
Agribusiness	–	–	–	148,278	148,278	–
Rural infrastructure	1	–	1	71,173	71,174	–
Rural residential real estate	–	–	–	58	58	–
Mission-related	–	–	–	1,174	1,174	–
Agricultural export finance	–	–	–	8,527	8,527	–
Total	$ 2,594	$ 212	$ 2,806	$ 994,987	$ 997,793	$ –

December 31, 2016	30-89 Days Past Due	90 Days or More Past Due	Total Past Due	Not Past Due or less than 30 Days Past Due	Recorded Investment in Loans Outstanding	Recorded Investment > 90 Days and Accruing
Real estate mortgage	$ 1,301	$ 3,423	$ 4,724	$ 544,757	$ 549,481	$ –
Production and intermediate-term	4,732	118	4,850	181,759	186,609	–
Agribusiness	–	–	–	149,673	149,673	–
Rural infrastructure	–	–	–	62,005	62,005	–
Rural residential real estate	–	–	–	109	109	–
Mission-related	–	–	–	1,228	1,228	–
Agricultural export finance	–	–	–	8,558	8,558	–
Total	$ 6,033	$ 3,541	$ 9,574	$ 948,089	$ 957,663	$ –

December 31, 2015	30-89 Days Past Due	90 Days or More Past Due	Total Past Due	Not Past Due or less than 30 Days Past Due	Recorded Investment in Loans Outstanding	Recorded Investment > 90 Days and Accruing
Real estate mortgage	$ 3,773	$ 991	$ 4,764	$ 550,760	$ 555,524	$ 457
Production and intermediate-term	2,728	46	2,774	166,783	169,557	–
Agribusiness	267	–	267	137,466	137,733	–
Rural infrastructure	–	–	–	71,026	71,026	–
Rural residential real estate	–	–	–	122	122	–
Mission-related	–	–	–	1,278	1,278	–
Agricultural export finance	–	–	–	8,574	8,574	–
Total	$ 6,768	$ 1,037	$ 7,805	$ 936,009	$ 943,814	$ 457

Note: The recorded investment in the loan 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 loan receivable.

A restructuring of a debt constitutes a troubled debt restructuring (TDR) if the creditor for economic or legal reasons related to the debtor's financial difficulties grants a concession to the debtor that it would not otherwise consider.

The following table presents additional information regarding troubled debt restructurings (whether accrual or nonaccrual) that occurred during the year.

	Year Ended December 31					
	2017		2016		2015	
	Outstanding Recorded Investment					
	Pre-modification	Post-modification	Pre-modification	Post-modification	Pre-modification	Post-modification
Real estate mortgage	$ –	$ –	$ 443	$ 443	$ –	$ –
Production and intermediate-term	891	891	716	716	–	–
Rural infrastructure	–	–	–	–	–	–
Total	$ 891	$ 891	$ 1,159	$ 1,159	$ –	$ –

Note: Pre-modification represents the recorded investment in the loan receivable just prior to restructuring and post-modification represents the recorded investment in the loan receivable immediately following the restructuring. The recorded investment is the face amount of the loan receivable 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 loan receivable.

Additional commitments to lend to borrowers whose loans have been modified in TDRs were $463 at December 31, 2017, $76 at December 31, 2016 and $82 at December 31, 2015. There were no TDRs that occurred within the previous 12 months of the year for which there was a payment default during the period.

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 at December 31.

	Loans modified as TDRs			TDRs in Nonaccrual Status*		
	2017	2016	2015	**2017**	2016	2015
Real estate mortgage	**$ –**	$ 540	$ 100	**$ –**	$ 443	$ –
Production and intermediate-term	**519**	727	1,439	**–**	–	1,316
Rural infrastructure	**717**	1,279	1,333	**–**	–	1,333
Total	**$ 1,236**	$ 2,546	$ 2,872	**$ –**	$ 443	$ 2,649

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

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

	Balance at December 31, 2016	Charge-offs	Recoveries	Provision for Loan Losses/(Loan Loss Reversals)	Balance at December 31, 2017
Real estate mortgage	$ 429	$ –	$ –	$ 246	$ 675
Production and intermediate-term	388	22	38	153	557
Agribusiness	443	–	–	250	693
Rural infrastructure	265	–	–	52	317
Mission-related	4	–	–	9	13
Agricultural export finance	6	–	–	–	6
Total	$ 1,535	$ 22	$ 38	$ 710	$ 2,261

	Balance at December 31, 2015	Charge-offs	Recoveries	Provision for Loan Losses/(Loan Loss Reversals)	Balance at December 31, 2016
Real estate mortgage	$ 446	$ –	$ 50	$ (67)	$ 429
Production and intermediate-term	335	684	140	597	388
Agribusiness	381	–	–	62	443
Rural infrastructure	301	–	–	(36)	265
Mission-related	4	–	–	–	4
Agricultural export finance	7	–	–	(1)	6
Total	$ 1,474	$ 684	$ 190	$ 555	$ 1,535

	Balance at December 31, 2014	Charge-offs	Recoveries	Provision for Loan Losses/(Loan Loss Reversals)	Balance at December 31, 2015
Real estate mortgage	$ 252	$ 318	$ –	$ 512	$ 446
Production and intermediate-term	421	79	168	(175)	335
Agribusiness	449	–	–	(68)	381
Rural infrastructure	283	–	–	18	301
Mission-related	3	–	–	1	4
Agricultural export finance	5	–	–	2	7
Total	$ 1,413	$ 397	$ 168	$ 290	$ 1,474

The Association maintains a separate reserve for unfunded commitments, which is included in Liabilities on our Consolidated Statement of Condition. The related provision for the reserve for unfunded commitments is included as part of the provision for credit losses on the Consolidated Statement of Comprehensive Income, along with the provision for loan losses.

A summary of changes in the reserve for unfunded commitments follows:

	Year Ended December 31		
	2017	2016	2015
Balance at beginning of period	**$ 270**	$ 457	$ –
Provision for unfunded commitments	**112**	(187)	457
Total	**$ 382**	$ 270	$ 457

Additional information on the allowance for loan losses follows.

	Allowance for Credit Losses Ending Balance at December 31, 2017		Recorded Investment in Loans Outstanding Ending Balance at December 31, 2017	
	Individually evaluated for impairment	Collectively evaluated for impairment	Individually evaluated for impairment	Collectively evaluated for impairment
Real estate mortgage	$ –	$ 675	$ 11,242	$ 573,028
Production and intermediate-term	–	557	2,303	182,009
Agribusiness	–	693	–	148,278
Rural infrastructure	–	317	–	71,174
Rural residential real estate	–	–	–	58
Mission-related	–	13	–	1,174
Agricultural export finance	–	6	–	8,527
Total	$ –	$ 2,261	$ 13,545	$ 984,248

	Allowance for Credit Losses Ending Balance at December 31, 2016		Recorded Investment in Loans Outstanding Ending Balance at December 31, 2016	
	Individually evaluated for impairment	Collectively evaluated for impairment	Individually evaluated for impairment	Collectively evaluated for impairment
Real estate mortgage	$ –	$ 429	$ 4,754	$ 544,727
Production and intermediate-term	–	388	2,147	184,462
Agribusiness	–	443	–	149,673
Rural infrastructure	–	265	–	62,005
Rural residential real estate	–	–	–	109
Mission-related	–	4	–	1,228
Agricultural export finance	–	6	–	8,558
Total	$ –	$ 1,535	$ 6,901	$ 950,762

	Allowance for Credit Losses Ending Balance at December 31, 2015		Recorded Investment in Loans Outstanding Ending Balance at December 31, 2015	
	Individually evaluated for impairment	Collectively evaluated for impairment	Individually evaluated for impairment	Collectively evaluated for impairment
Real estate mortgage	$ 76	$ 370	$ 5,060	$ 550,464
Production and intermediate-term	–	335	2,031	167,526
Agribusiness	–	381	–	137,733
Rural infrastructure	–	301	1,333	69,693
Rural residential real estate	–	–	–	122
Mission-related	–	4	–	1,278
Agricultural export finance	–	7	–	8,574
Total	$ 76	$ 1,398	$ 8,424	$ 935,390

NOTE 4 – INVESTMENT IN COBANK

At December 31, 2017, the Association's investment in CoBank is in the form of Class A stock with a par value of $100.00 per share. The Association is required to own stock in CoBank to capitalize its direct loan balance and participation loans sold to CoBank. The current requirement for capitalizing its direct loan from CoBank is 4.00 percent of the Association's prior year average direct loan balance. The current requirement for capitalizing patronage-based participation loans sold to CoBank is 8.00 percent of the Association's prior ten-year average balance of such participations sold to CoBank. Under the current CoBank capital plan applicable to such participations sold, patronage from CoBank related to these participations sold is paid 75 percent cash and 25 percent Class A stock. The capital plan is evaluated annually by CoBank's board of directors and management and is subject to change.

CoBank may require the holders of its equities to subscribe for such additional capital as may be needed to meet its capital requirements for its joint and several liability under the Farm Credit Act and regulations. In making such a capital call, CoBank shall take into account the financial condition of each such holder and such other considerations, as it deems appropriate.

The Association owned approximately 0.97 percent of the outstanding common stock of CoBank at December 31, 2017.

NOTE 5 – PREMISES AND EQUIPMENT

Premises and equipment consisted of the following.

	December 31		
	2017	2016	2015
Land	**$ 916**	$ 916	$ 916
Buildings and leasehold improvements	**12,402**	12,371	12,350
Furniture, equipment and automobiles	**3,058**	2,988	2,922
Construction in progress	**–**	9	38
	16,376	16,284	16,226
Less: accumulated depreciation	**4,204**	3,642	2,972
Total	**$ 12,172**	$ 12,642	$ 13,254

NOTE 6 – OTHER PROPERTY OWNED

Losses on other property owned, net as reflected on the Consolidated Statement of Comprehensive Income consisted of the following.

	December 31		
	2017	2016	2015
Losses on sale, net	**$ –**	$ –	$ 757
Carrying value adjustments	**172**	109	–
Operating expense, net	**93**	–	263
Losses on other property owned, net	**$ 265**	$ 109	$ 1,020

NOTE 7 – NOTE PAYABLE TO COBANK

The Association's indebtedness to CoBank represents borrowings by the Association to fund its loan portfolio. This indebtedness is collateralized by a pledge of substantially all of the Association's assets and is governed by a General Financing Agreement (GFA). According to the agreement, the aggregate outstanding amount of principal and accrued interest shall not at any time exceed the line of credit. The GFA is subject to periodic renewals in the normal course of business. The GFA in effect at December 31, 2017 was scheduled to mature on May 31, 2018; however, a new GFA entered into effective January 1, 2018 will mature on December 31, 2022. The Association was in compliance with the terms and conditions of the GFA as of December 31, 2017. Substantially all borrower loans are match-funded with CoBank. Payments and disbursements are made on the note payable to CoBank on the same basis the Association collects payments from and disburses on borrower loans. The interest rate may periodically be adjusted by CoBank based on the terms and conditions of the borrowing.

	December 31		
	2017	2016	2015
Line of credit	**$ 925,000**	$ 908,749	$ 900,068
Outstanding principal and accrued interest balance	**$ 798,183**	$ 766,777	$ 762,847
Average outstanding principal balance under the line of credit	**$ 781,017**	$ 766,282	$ 743,709
Weighted average interest rate	**2.22%**	2.02%	2.00%

Under the Farm Credit Act, the Association is obligated to borrow only from CoBank, unless CoBank gives approval to borrow elsewhere. Other than our funding relationship with the Bank, and our advanced conditional payments, we have no other uninsured or insured debt. See Note 2 for additional information. CoBank, consistent with FCA regulations, has established limitations on the Association's ability to borrow funds based on specified factors or

formulas relating primarily to credit quality and financial condition. At December 31, 2017, the Association's notes payable was within the specified limitations.

The Association has the opportunity to commit loanable funds with CoBank under a variety of programs at either fixed or variable rates for specified timeframes. Participants in the program receive a credit on the committed loanable funds balance classified as a reduction of interest expense. These committed funds are netted against the note payable to the Bank. The average committed funds as of December 31 are as follows:

	2017	2016	2015
Average committed funds	**$ 190,094**	$ 183,301	$ 173,424
Average rates	**0.99%**	0.55%	0.30%

NOTE 8 – SHAREHOLDERS' EQUITY

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

A. Protected Borrower Stock

Protection of certain stock is provided under the Farm Credit Act which requires the Association, when retiring protected stock, to retire it at par or stated value regardless of its book value. Protected stock includes stock and allocated equities which were outstanding as of January 6, 1988, or were issued or allocated prior to October 6, 1988.

B. Capital Stock

In accordance with the Farm Credit Act, each borrower is required to invest in the Association as a condition of borrowing. The borrower normally acquires ownership of the stock at the time the loan is made, but usually does not make a cash investment. Generally, the aggregate par value of the stock is added to the principal amount of the related loan obligation. The Association has a first lien on the stock owned by its borrowers. Retirement of such equities will generally be at the lower of par or book value, and repayment of a loan does not automatically result in retirement of the corresponding stock. Our bylaws generally permit stock to be retired at the discretion of the Board of Directors and in compliance with our capitalization plans, provided prescribed capital standards have been met. At December 31, 2017, we exceeded the prescribed standards. We do not anticipate any significant changes in capital that would affect the normal retirement of stock.

Capitalization bylaws allow stock requirements to range from the lesser of one thousand dollars or 2.00 percent of the amount of the loan to 10.00 percent of the loan. The Board of Directors has the authority to change the minimum required stock level of a shareholder as long as the change is within this range. Currently, the Association has a stock requirement of the lesser of one thousand dollars or 2.00 percent of the amount of the borrower's combined loan volume.

C. Regulatory Capitalization Requirements and Restrictions

The Farm Credit Administration sets minimum regulatory capital requirements for Banks and Associations. Effective January 1, 2017, new regulatory capital surplus requirements for Banks and Associations were adopted. These new requirements replaced the core surplus and total surplus requirements with Common Equity Tier 1, Tier 1 Capital and Total Capital risk-based capital ratio requirements. The new requirements also replaced the existing net collateral ratio for System Banks with a Tier 1 Leverage ratio and an Unallocated Retained Earnings (URE) and URE Equivalents Leverage ratio that are applicable to both the Banks and Associations. The Permanent Capital Ratio continues to remain in effect; however, the risk-adjusted assets are calculated differently than in the past.

The following sets forth the regulatory capital ratio requirements and ratios at December 31, 2017:

Ratio	Primary Components of Numerator	Denominator	Ratios as of December 31, 2017	Minimum with Buffer*	Minimum Requirement
Common Equity Tier 1 (CET1) Capital	Unallocated retained earnings (URE), common cooperative equities (qualifying capital stock and allocated equity)[1]	Risk-adjusted assets	19.52%	7.0%	4.5%
Tier 1 Capital	CET1 Capital, non-cumulative perpetual preferred stock	Risk-adjusted assets	19.52%	8.5%	6.0%
Total Capital	Tier 1 Capital, allowance for loan losses[2], common cooperative equities[3], and term preferred stock and subordinated debt[4]	Risk-adjusted assets	19.74%	10.5%	8.0%
Tier 1 Leverage**	Tier 1 Capital	Total assets	20.35%	5.0%	4.0%
Unallocated Retained Earnings and URE Equivalents (UREE) Leverage	URE and URE Equivalents	Total assets	20.94%	—	1.5%
Permanent Capital	Retained earnings, common stock, non-cumulative perpetual preferred stock and subordinated debt, subject to certain limits	Risk-adjusted assets	19.81%	—	7.0%

* The new capital requirements have a three-year phase-in of the capital conservation buffer applied to the risk-adjusted capital ratios. There is no phase-in of the leverage buffer. Amounts shown reflect the full capital conservation buffer.

** Must include the regulatory minimum requirement for the URE and UREE Leverage ratio.
[1] Equities outstanding 7 or more years
[2] Capped at 1.25% of risk-adjusted assets
[3] Outstanding 5 or more years, but less than 7 years
[4] Outstanding 5 or more years

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

The Board of Directors has established, adopted and will maintain formal written Capital Adequacy Plan to ensure the Association maintains compliance with capital adequacy regulations. The objectives in the plan are:

- Maintain Association capital at a level sufficient to meet all regulatory and System requirements;
- Provide protection against risk inherent in the Association's operation;
- Provide protection against unknown or unexpected risk;
- Provide sufficient capital for future asset growth;
- Allow the Association to operate profitably over the long-term;
- Maintain a competitive market positon; and,
- Increase Association surplus, thereby reducing reliance on borrower stock for capitalization needs.

Additionally, the Capital Adequacy Plan includes the capital targets necessary to achieve the Association's capital adequacy goals, as well as the minimum regulatory capital requirements.

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

D. Description of Equities

The following paragraphs describe the attributes of each class of stock authorized by the Association bylaws and indicates the number of shares outstanding at December 31, 2017. Unless otherwise indicated all classes of stock have a par value of $5.00. All classes of stock are transferrable to other customers who are eligible to hold such class of stock. Transfers of stock are only allowed as long as the Association meets the regulatory minimum capital requirements.

Class A Common Stock (Nonvoting, at-risk, no shares outstanding) – Issued in exchange for Class B Common Stock or Class C Common Stock; as a patronage refund; as a dividend; or in exchange for allocated surplus. Retirement is at the sole discretion of the Board of Directors.

Class B Common Stock (Voting, at-risk, 278,728 shares outstanding) – Issued solely to, and shall be acquired by, borrowers and other applicants who are farmers, ranchers, or producers or harvesters of aquatic products and who are eligible to vote. Class B Common Stock may also be held by those borrowers who exchanged one share of Class F Common Stock for one share of Class B Common Stock. Each Class B Common shareholder shall hold at least one share as long as the holder continues business with the Association. Within two years after the holder terminates its relationship with the Association, any outstanding Class B Common Stock shall be converted to Class A Common Stock. Retirement is at the sole discretion of the Board of Directors.

Class C Common Stock (Nonvoting, at-risk, 3,220 shares outstanding) – Class C Common Stock may be issued to borrowers or applicants who are: (a) rural residents, including persons eligible to hold voting stock, to capitalize rural housing loans; (b) persons or organizations furnishing farm-related services; (c) other persons or organizations who are eligible to borrow from or participate with the Association but who are not eligible to hold voting stock. Class C Common Stock may be issued to any person who is not a shareholder but who is eligible to borrow from the Association for the purpose of qualifying such person for technical assistance, financially related services and leasing services offered by the Association. Within two years after the holder terminates its relationship with the Association, any outstanding Class C Common Stock shall be converted to Class A Common Stock. Retirement is at the sole discretion of the Board of Directors.

Class D Common Stock (Nonvoting, at-risk, no shares outstanding, par value of one thousand dollars) – Issued to CoBank or to any person through direct sale.

Class E Preferred Stock (Nonvoting, at-risk, no shares outstanding, par value as may be determined by any agreement of financial assistance between the Association and CoBank) - Issued only to CoBank in consideration of financial assistance to the Association from CoBank. Retirement is at the sole discretion of the Board of Directors.

Class F Common Stock (Voting, protected, no shares outstanding) – Shall be issued to those individuals and entities who held the same class of stock in a predecessor to the Association. The Association shall not issue any additional Class F Common Stock. Each Class F Common shareholder shall hold at least one share as long as the holder continues business with the Association. Within two years after the holder terminates its relationship with the Association, any outstanding Class F Common Stock shall be converted to Class G Common Stock. Retirement is at the sole discretion of the Board of Directors.

Class G Common Stock (Nonvoting, protected, no shares outstanding) – Issued only to those individuals and entities who held the same class of stock in a predecessor to the Association and as necessary for conversions from Class F Common Stock. No further shares of Class G Common Stock will be issued. It must be retired upon repayment of the loan.

Class H Preferred Stock (Nonvoting, at-risk, 261,880,195 shares outstanding, par value of one cent) – Issued to and may be acquired only by owners of any class of Common Stock and who have an outstanding loan with the Association.

The changes in the number of shares of protected and capital stock outstanding during 2017 are summarized in the following table.

Shares in whole numbers	Preferred	Capital
Balance outstanding at January 1, 2017	187,907,655	281,484
Issuances	85,595,559	26,729
Retirements	(11,623,019)	(26,265)
Balance outstanding at December 31, 2017	261,880,195	281,948

E. Patronage and/or Dividends

Dividends may be declared and paid to holders of Class H Stock on a quarterly basis based on a dividend rate determined by the Board of Directors. Dividends paid on the stock will be applied towards the purchase of additional shares of the stock at par value.

Dividends may be declared or patronage distributions allocated to holders of Class B, C, F and G Stock out of the whole or any part of net earnings which remain at the end of the fiscal year, as the Board of Directors may determine, in accordance with the regulations for banks and associations of the System. Additionally, patronage distributions may be allocated to System institutions, with or for whom the Association conducts specified business transactions. However, distributions and retirements are precluded by regulation until the minimum capital adequacy standards have been attained. Amounts not distributed are retained as unallocated retained earnings. The Association made a cash patronage distribution of $4,000 in 2017, $3,000 in 2016 and $3,500 in 2015. The Association declared a $3,750 cash patronage to be distributed in 2018.

In the event of liquidation or dissolution of the Association, any assets of the Association remaining after payment or retirement of all liabilities shall be distributed to retire stock in the following order of priority: First, to the holders of all classes of Class E Preferred Stock (if any) until an amount equal to the aggregate par value of all such shares then issued and outstanding has been distributed to such holders; second, to the holders of all classes of Class H Preferred Stock until an amount equal to the aggregate par value of all such shares then issued and outstanding has been distributed to such holders; third, to the holders, pro rata, of all classes of common stock, until an amount equal to the aggregate par value of all such shares then issued and outstanding has been distributed to such holders; fourth, any remaining assets of the Association after such distributions shall be distributed to present and former members and other patrons on a patronage basis, to the extent practicable.

At each year end, the Board of Directors evaluates whether to retain the Association's net income to strengthen its capital position or to distribute a portion of the net income to customers by declaring a qualified/cash patronage refund. For 2017, the Association allocated 27.35 percent of its patronage-sourced net income to its patrons.

F. Accumulated Other Comprehensive Income/Loss

The Association reports accumulated other comprehensive loss in its Consolidated Statement of Changes in Shareholders' Equity. As more fully described in Note 2, accumulated other comprehensive income/loss results from the recognition of the Pension Restoration Plan's net unamortized gains and losses and prior service costs or credits. The Association has accumulated other comprehensive loss of $841 in 2017. There was no accumulated other comprehensive income or loss in 2016 and 2015. There were no other items affecting comprehensive income or loss.

The following table presents activity in the accumulated other comprehensive income/(loss), net of tax by component:

	2017
Pension and other benefit plans:	
Beginning balance	**$ –**
Other comprehensive loss before reclassifications	**(841)**
Amounts reclassified from accumulated other comprehensive income/(loss)	**–**
Net current period other comprehensive income/(loss)	**(841)**
Year-end balance	**$ (841)**

NOTE 9 – PATRONAGE DISTRIBUTION FROM FARM CREDIT INSTITUTIONS

Patronage income recognized from Farm Credit institutions to the Association follows.

	2017	2016	2015
CoBank	**$ 3,529**	$ 3,466	$ 3,363
AgVantis	**–**	283	48
Farm Credit Foundations	**12**	11	7
Total	**$ 3,541**	$ 3,760	$ 3,418

Patronage distributed from CoBank was in cash and stock. The amount earned in 2017 was accrued and will be paid by CoBank in March 2018. The amount earned and accrued in 2016 and 2015 was paid by CoBank in March of the following year.

Patronage distribution from AgVantis was in the form of a Notice of Allocation; 20 percent was distributed in cash with the balance of the allocation recorded as an investment in AgVantis which is recorded in other assets in the year received.

Patronage distributed by Farm Credit Foundations was accrued at the end of the year and will be paid in March 2018. Farm Credit Foundations, a human resource service provider for a number of Farm Credit institutions, provides our payroll and human resource services.

NOTE 10 – INCOME TAXES

The provision for income taxes follows.

	Year Ended December 31		
	2017	2016	2015
Current:			
Federal	**$ 4**	$ 4	$ 4
State	**1**	1	1
Provision for income taxes	**$ 5**	$ 5	$ 5

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.

	Year Ended December 31		
	2017	2016	2015
Federal tax at statutory rate	**$ 4,670**	$ 4,923	$ 4,558
State tax, net	**1**	1	1
Effect of non-taxable FLCA subsidiary	**(5,212)**	(5,090)	(4,490)
Change in valuation allowance	**(601)**	159	51
Qualified patronage refunds to borrowers	**–**	–	(110)
Change in tax rates	**1,143**	–	–
Other	**4**	12	(5)
Provision for income taxes	**$ 5**	$ 5	$ 5

Deferred tax assets and liabilities are comprised of the following.

	December 31		
	2017	2016	2015
Deferred income tax assets:			
Allowance for loan losses	**$ 156**	$ 160	$ 170
Nonaccrual loan interest	**634**	799	724
Gain on other property owned	**221**	269	229
Net operating loss carryforward	**1,451**	1,890	1,808
Charitable contribution carryover	**2**	4	4
Gross deferred tax assets	**2,464**	3,122	2,935
Deferred tax asset valuation allowance	**(2,272)**	(2,824)	(2,651)
Deferred income tax liabilities:			
Depreciation	**(10)**	(18)	(17)
Bank patronage allocation	**(180)**	(277)	(264)
Sale of fixed assets	**(1)**	(1)	(1)
Gain on installment sales	**(1)**	(2)	(2)
Gross deferred tax liability	**(192)**	(298)	(284)
Net deferred tax asset	**$ –**	$ –	$ –

The calculation of deferred tax assets and liabilities involves various management estimates and assumptions as to future taxable earnings, including the amount of non-patronage income and patronage income retained. The expected future tax rates are based upon enacted tax laws.

The tax expense in 2017 was impacted by the enactment of federal tax legislation in late December 2017 which, among other things, lowered the federal corporate tax rate from 35 percent to 21 percent beginning in 2018. In accordance with GAAP, the change to the lower corporate tax rate led to a revaluation of the Association's deferred tax assets and deferred tax liabilities in the period of enactment (2017).

The Association recorded a valuation allowance of $2,272 in 2017, $2,824 in 2016 and $2,651 in 2015. The Association will continue to evaluate the realizability of the deferred tax assets and adjust the valuation allowance accordingly. At December 31, 2017, the net tax effect of the Association's federal and state net operating loss carryforward was $1,451. The carryforward will expire from 2032 to 2037.

The Association has no uncertain tax positions as of December 31, 2017, 2016 or 2015. The Association recognizes interest and penalties related to unrecognized tax positions as an adjustment to income tax expense. The tax years that remain open for federal and major state income tax jurisdictions are 2014 and forward.

NOTE 11 – EMPLOYEE BENEFIT PLANS

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

The defined benefit pension plan reflects an unfunded liability totaling $84.6 million at December 31, 2017. The pension benefits funding status reflects the net of the fair value of the plan assets and the projected benefit obligation at the date of these consolidated financial statements. The projected benefit obligation is the actuarial present value of all benefits attributed by the pension benefit formula to employee service rendered prior to the measurement date based on assumed future compensation levels. The projected benefit obligation of the plan was $292.6 million at

December 31, 2017, $270.6 million at December 31, 2016 and $244.3 million at December 31, 2015. The fair value of the plan assets was $208.0 million at December 31, 2017, $175.6 million at December 31, 2016 and $155.1 million at December 31, 2015. The amount of the pension benefits funding status is subject to many variables including performance of plan assets and interest rate levels. Therefore, changes in assumptions could significantly affect these estimates.

Costs are determined for each individual employer based on costs directly related to its current employees as well as an allocation of the remaining costs based proportionately on the estimated projected liability of the employer under this plan. The Association recognizes its proportional share of expense and contributes a proportional share of funding. Total plan expense for participating employers was $12.7 million in 2017, $11.3 million in 2016 and $16.1 million in 2015. The Association's allocated share of plan expenses included in salaries and employee benefits was $946 in 2017, $832 in 2016, and $1.1 million in 2015. Participating employers contributed $20.0 million in 2017, $20.4 million in 2016 and $13.6 million in 2015 to the plan. The Association's allocated share of these pension contributions was $1.5 million in 2017, $1.5 million in 2016, and $944 in 2015. While the plan is a governmental plan and is not subject to minimum funding requirements, the employers contribute amounts necessary on an actuarial basis to provide the plan with sufficient assets to meet the benefits to be paid to participants. The amount of the total employer contributions expected to be paid into the pension plans during 2018 is $20.0 million. The Association's allocated share of these pension contributions is expected to be $1.7 million. The amount ultimately to be contributed and the amount ultimately recognized as expense as well as the timing of those contributions and expenses, are subject to many variables including performance of plan assets and interest rate levels. These variables could result in actual contributions and expenses being greater than or less than anticipated.

Postretirement benefits other than pensions are provided through the Farm Credit Foundations Retiree Medical Plan to retired employees of the Association. Benefits provided are determined on a graduated scale based on years of service. The anticipated costs of these benefits were accrued during the period of the employee's active service. Postretirement benefits (primarily health care benefits) included in salaries and employee benefits were income of $3 in 2017 and $1 in 2016, and expense of $9 in 2015. The Association made cash contributions of $9 in 2017, $12 in 2016 and $12 in 2016.

Beginning in 2017, the Association participates in a non-qualified defined benefit Pension Restoration Plan that is unfunded. The plan provides retirement benefits above the Internal Revenue Code compensation limit to certain highly compensated eligible employees. Benefits payable under the Pension Restoration Plan are offset by the benefits payable from the Pension Plan. For 2017, there were no Pension Restoration Plan expenses included in salaries and employee benefits.

The funding status and the amounts recognized in the Consolidated Statement of Condition for the Association's Pension Restoration Plan follows:

	2017
Change in benefit obligation:	
Benefit obligation at the beginning of the period	**$ –**
Actuarial loss/(gain)	**841**
Benefit obligation at the end of the period	**$ 841**
Change in plan assets:	
Company contributions	**$ –**
Benefits paid	**–**
Fair value of plan assets at the end of the period	**$ –**
Funded status of the plan	**$ (841)**
Amounts recognized in the Consolidated Statement of Condition consist of:	
Liabilities	**$ 841**
Net amount recognized	**$ 841**

The following table represents the amounts included in accumulated other comprehensive income/loss for the Pension Restoration Plan at December 31:

	2017
Net actuarial loss	**$ (841)**
Total amount recognized in AOCI/loss	**$ (841)**

An estimated net actuarial loss of $265 for the Pension Restoration Plan will be amortized into income over the next year.

The projected and accumulated benefit obligation for the Pension Restoration Plan at December 31 was:

	2017
Projected benefit obligation	**$ 841**
Accumulated benefit obligation	**$ 841**

Changes in benefit obligation recognized in accumulated other comprehensive income are included in the following table.

	2017
Current year net actuarial loss	**$ (841)**
Total recognized in other comprehensive income	**$ (841)**

Weighted average assumptions used to determine benefit obligation at December 31:

	2017
Discount rate	**3.35%**
Rate of compensation increase	**5.00%**

Weighted average assumptions used to determine net periodic benefit cost for the years ended December 31:

	2017
Discount rate	
Projected benefit obligation	**3.51%**
Service Cost	**3.58%**
Interest Cost	**3.04%**
Rate of compensation increase	**5.00%**

The Association expects to contribute $290 to the Pension Restoration Plan in 2018.

Estimated Future Benefit Payments

The following benefit payments, which reflect expected future service, as appropriate, are expected to be paid:

	Pension Restoration Benefits
2018	$ 290
2019	$ 290
2020	$ 290
2021	$ –
2022	$ –
2023 – 2027	$ –

The Association also participates in the Farm Credit Foundations Defined Contribution/401(k) Plan. Employees who do not participate in the Pension Plan may receive benefits through the Employer Contribution portion of the Contribution Plan. In this plan, the Association provides a monthly contribution based on a defined percentage of the employee's salary. Employees may also participate in a Salary Deferral Plan governed by Section 401(k) of the Internal Revenue Code. The Association matches a certain percentage of employee contributions to the plan. Employer contributions to the Contribution Plan were $486 in 2017, $432 in 2016 and $391 in 2015.

NOTE 12 – RELATED PARTY TRANSACTIONS

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

The Association has a policy that loans to directors and senior officers must be maintained at an Acceptable or Other Assets Especially Mentioned (OAEM) credit classification. If the loan falls below the OAEM credit classification, corrective action must be taken and the loan brought back to either Acceptable or OAEM within a year. If not, the director or senior officer must resign from the Board of Directors or employment.

Loan information to related parties for the years ended December 31 is shown below.

	2017	2016	2015
Beginning balance	**$16,450**	$15,448	$16,538
New loans and advances	**11,226**	11,733	9,901
Repayments	**(10,041)**	(10,881)	(10,611)
Reclassifications*	**360**	150	(380)
Ending balance	**$17,995**	$16,450	$15,448

∗ Represents loans that were once considered related party, but are no longer considered related party, or loans that were not related party that subsequently became related party loans.

In the opinion of management, none of the loans outstanding to officers and directors at December 31, 2017 involved more than a normal risk of collectibility.

The Association also has business relationships with certain other System entities. The Association paid $1.6 million in 2017, $1.7 million in 2016 and $1.3 million in 2015 to AgVantis for technology services and $2 in 2017 and none in 2016 and 2015 to CoBank for operational services. The Association paid $167 in 2017, $145 in 2016, and $128 in 2015 to Foundations for human resource services.

NOTE 13 – REGULATORY ENFORCEMENT MATTERS

There are no regulatory enforcement actions in effect for the Association.

NOTE 14 – COMMITMENTS AND CONTINGENCIES

The Association has various commitments outstanding and contingent liabilities. With regard to contingent liabilities, there are no actions pending against the Association in which claims for monetary damages are asserted.

The Association may participate in financial instruments with off-balance sheet risk to satisfy the financing needs of its borrowers and to manage their exposure to interest-rate risk. These financial instruments include commitments to extend credit. The instruments involve, to varying degrees, elements of credit risk in excess of the amount recognized in the consolidated financial statements. Commitments to extend credit are agreements to lend to a borrower as long as there is not a violation of any condition established in the contract. Commitments generally have fixed expiration dates or other termination clauses and may require payment of a fee by the borrower. At December 31, 2017, $245.6 million of commitments to extend 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 Consolidated Statement of Condition until funded or drawn upon. The credit risk associated with issuing commitments 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.

The Association also participates in standby letters of credits to satisfy the financing needs of its borrowers. These letters of credit are irrevocable agreements to guarantee payments of specified financial obligations. At December 31, 2017, $2.7 million of standby letters of credit were outstanding with a nominal fair value. Outstanding standby

letters of credit have expiration dates ranging from 2018 to 2025. The maximum potential amount of future payments the Association is required to make under the guarantees is $2.7 million.

NOTE 15 – 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. The fair value measurement is not an indication of liquidity. See Note 2 for additional information.

The Association has no assets or liabilities measured at fair value on a recurring basis for the periods presented. During the three years presented, the Association recorded no transfers in or out of Levels 1, 2, or 3. Assets measured at fair value on a non-recurring basis at December 31 for each of the fair value hierarchy values are summarized as follows:

	Fair Value Measurement Using			**Total Fair Value**
	Level 1	**Level 2**	**Level 3**	
2017				
Loans	**$ –**	**$ –**	**$ –**	**$ –**
Other property owned	**$ –**	**$ –**	**$ 2,565**	**$ 2,565**
2016				
Loans	$ –	$ –	$ 356	$ 356
Other property owned	$ –	$ –	$ 2,870	$ 2,870
2015				
Loans	$ –	$ –	$ 3,387	$ 3,387
Other property owned	$ –	$ –	$ 2,071	$ 2,071

The Association has no liabilities measured at fair value on a non-recurring basis for any of the periods presented.

Valuation Techniques

As more fully discussed in Note 2, 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. Fair values of financial instruments represent the estimated amount to be received to sell an asset or paid to transfer or extinguish a liability in active markets among willing participants at the reporting date. Due to the uncertainty of expected cash flows resulting from financial instruments, the use of different assumptions and valuation methodologies could significantly affect the estimated fair value amounts. Accordingly, certain of the estimated fair values may not be indicative of the amounts for which the financial instruments could be exchanged in a current or future market transaction. The following presents a brief summary of the valuation techniques used by the Association for assets and liabilities subject to fair value measurement:

Loans

For impaired loans measured on a non-recurring basis, 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 and the net loan is reported at its fair value.

Other Property Owned

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

NOTE 16 – QUARTERLY FINANCIAL INFORMATION (UNAUDITED)

Quarterly results of operations for the years ended December 31, 2017, 2016 and 2015, follow.

	2017				
	First	**Second**	**Third**	**Fourth**	**Total**
Net interest income	**$ 6,494**	**$ 6,711**	**$ 6,803**	**$ 6,670**	**$ 26,678**
Provision for credit losses/(Credit loss reversal)	**613**	**(178)**	**71**	**316**	**822**
Noninterest expense, net	**3,079**	**2,910**	**3,029**	**3,108**	**12,126**
Net income	**$ 2,802**	**$ 3,979**	**$ 3,703**	**$ 3,246**	**$ 13,730**

	2016				
	First	Second	Third	Fourth	Total
Net interest income	$ 6,219	$ 6,300	$ 6,495	$ 6,634	$ 25,648
Provision for credit losses/(Credit loss reversal)	234	323	236	(425)	368
Noninterest expense, net	2,733	2,651	2,520	2,901	10,805
Net income	$ 3,252	$ 3,326	$ 3,739	$ 4,158	$ 14,475

	2015				
	First	Second	Third	Fourth	Total
Net interest income	$ 5,868	$ 5,816	$ 6,110	$ 6,714	$ 24,508
Provision for credit losses/(Credit loss reversal)	481	692	31	(457)	747
Noninterest expense, net	2,649	2,245	3,108	2,358	10,360
Net income	$ 2,738	$ 2,879	$ 2,971	$ 4,813	$ 13,401

NOTE 17 – SUBSEQUENT EVENTS

The Association has evaluated subsequent events through March 16, 2018 which is the date the financial statements were issued, and no material subsequent events were identified.

Disclosure Information Required By Farm Credit Administration Regulations

(Amounts in Whole Dollars)

Description of Business

The description of the territory served, persons eligible to borrow, types of lending activities engaged in and 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 financial statements, "Organization and Operations," included in this annual report to shareholders.

The description of significant developments that had or could have a material impact on earnings or interest rates to borrowers, acquisitions or dispositions of material assets, material changes in the manner of conducting the business, seasonal characteristics, and concentrations of assets, if any, required to be disclosed in this section, is incorporated herein by reference from "Management's Discussion and Analysis" (MD&A) included in this annual report to shareholders.

Description of Property

The following table sets forth certain information regarding the properties of the Association:

Location	Description	Form of Ownership
5110 Edison Avenue Colorado Springs, Colorado	Administrative Office and Lending Office	Owned
549 South Lincoln Burlington, Colorado	Lending Office	Owned
1302 East Third Street La Junta, Colorado	Lending Office	Owned
201 South Fifth Street Lamar, Colorado	Lending Office	Owned
100 East Main Street Limon, Colorado	Lending Office	Owned
159 Washington Street Monte Vista, Colorado	Lending Office	Owned

Legal Proceedings and Enforcement Actions

Information required to be disclosed in this section is incorporated herein by reference from Note 13 to the financial statements, "Regulatory Enforcement Matters," and Note 14 to the financial statements, "Commitments and Contingencies," included in this annual report to shareholders.

Description of Capital Structure

Information required to be disclosed in this section is incorporated herein by reference from Note 8 to the financial statements, "Shareholders' Equity," included in this annual report to shareholders.

Description of Liabilities

The description of debt outstanding required to be disclosed in this section is incorporated herein by reference from Note 7 to the financial statements, "Note Payable to CoBank," included in this annual report to shareholders.

The description of advance conditional payments is incorporated herein by reference to Note 2 to the financial statements, "Summary of Significant Accounting Policies," to the financial statements, included in this annual report to shareholders.

The description of contingent liabilities required to be disclosed in this section is incorporated herein by reference from Note 14 included in this annual report to shareholders.

SELECTED FINANCIAL DATA

The selected financial data for the five years ended December 31, 2017, required to be disclosed in this section is incorporated herein by reference from the "Five-Year Summary of Selected Consolidated Financial Data," included in this annual report to shareholders.

MANAGEMENT'S DISCUSSION AND ANALYSIS

"Management's Discussion and Analysis," which appears within this annual report to shareholders and is required to be disclosed in this section, is incorporated herein by reference.

DIRECTORS AND SENIOR OFFICERS

The following represents certain information regarding the directors and senior officers of the Association.

DIRECTORS

Gary Pautler: Chairman of the Board serving a three-year term which expires in 2020 and a member of the Association's Audit & Risk Committee and Human Resources Committee. Mr. Pautler has been farming since 1967. He is a partner in Pautler Brothers, a family owned irrigated and dryland corn and wheat operation. Mr. Pautler serves as Chairman on the Kit Carson County Planning Commission and is Treasurer of the Stratton Fire Protection District.

Kent Price: Vice Chairman of the Board and Director currently serving a three-year term which expires in 2020 and Chairman of the Association's Human Resource Committee. Mr. Price is a partner in Price Farms LLC, Price Farms Certified Seed Company LLC, Price Heritage LLC and Expo LLC. He is also part owner in San Acio Seed and San Acio Lands LLC. His operations include seed and market potatoes, and produce malt barley for Coors. He graduated from Adams State University and has been farming for over 35 years. He is currently secretary/treasurer for the Colorado Certified Potato Growers Association, serves on the San Luis Valley Colorado State University Research Committee, and the San Luis Valley Well Owner's Association. He is an alternate on the Colorado Potato Administration Committee (CPAC) for Saguache County.

Colin Durham: Director currently serving a three-year term which expires in 2019 and a member of the Association's Audit & Risk Committee. Dr. Durham is a 2013 graduate of Colorado State University's College of Veterinary Medicine. Dr. Durham is a partner at Colorado Veterinary Clinic, P.C. in La Junta, Colorado. He is also a veterinarian at La Junta Livestock Commission, Inc. He and his brother run a commercial cow-calf and stocker operation. Additionally, they take in cattle on a custom grazing/partnership basis. They lease pasture in Crowley, El Paso, Lincoln and Otero counties.

Carl Keith James: Director currently serving a three-year term which expires in 2019 and a member of the Association's Human Resource Committee. He is the Association representative to the CoBank, ACB District Farm Credit Council. Mr. James has been farming since 1973. He has a cow/calf, stocker and wheat operation. Mr. James is Chairman of both the Eastern Slope Rural Telephone Association and Lincoln Community Hospital Boards.

Scott Maranville: Director currently serving a three-year term which expires in 2018 and a member of the Association's Human Resources Committee. Mr. Maranville is a partner in Maranville Farms Partnership, a family owned dryland farming operation. He has been there since graduating college 21 years ago. He and his wife also have a cow/calf operation. Mr. Maranville also has an interest in Maranville, LLC and S&B Farms, Inc., both farm and ag related businesses run by the family.

Rosalie Martinez: Director, currently serving a three-year term which expires in 2018 and a member of the Association's Audit & Risk Committee. Mrs. Martinez has been engaged in farming and ranching for over 38 years. She is a partner in Rio Vega Ranch, LLC, a cow/calf operation, and a partner in Esperanza Farms, LLC, a farming enterprise which raises potatoes, barley and alfalfa. She is a partner in Ace Hardware of Alamosa and Sierra Vista Lumber Company, LLC, which includes retail sales in hardware, building supplies and steel. She is a partner with her husband, LeRoy, in the family businesses: L&M Auto, which includes car sales, body shop and salvage yard; Valley Finance, a finance company used to finance vehicles sold by L&M Auto; and Martinez Farm, the family farm which raises mostly alfalfa. She is retired from Adams State College where she taught in the School of Business and later held the position Associate Vice President for Administration. Ms. Martinez is currently serving on the San Luis Valley Health Board of Trustees and the San Luis Health Foundation Board. She is also serving on the Board for Amarah's Children's Foundation Hope for Kids Like Me.

John Negley: Director currently serving a three-year term which expires in 2020 and a member of the Association's Human Resource Committee. Mr. Negley has farmed and ranched since 1970. He is a partner in J & L Farms, a family partnership conducting a wheat and cow/calf operation. He serves as Secretary on the Board of Directors for the Kiowa Soil Conservation Board and Director for the Eads Hospital Board.

Mark Peterson: Director currently serving a three-year term which expires in 2019 and Chairman of the Association's Audit & Risk Committee. Mr. Peterson is a partner in a family run farm, Peterson Farms, LLC, farming potatoes and malting barley for Coors. Mr. Peterson is currently serving as Chairman of the Colorado Potato Administrative Committee. He is a Director on the National Potato Council, which is the governmental oversight committee for the potato industry in the US. He serves on the Trade Affairs committee, the US-Mexico Trade affairs sub-committee, and the Legislative and Governmental Affairs Committee.

Paul Prentice: Appointed Director currently serving a three-year term which expires in 2020 and Vice Chairman of the Association's Audit & Risk Committee. Dr. Prentice is the founder, President and Chief Economist of Farm Sector Economics, Inc., a consulting firm specializing in macroeconomic linkages to agriculture. After a 30-year run, Dr. Prentice closed Farm Sector Economics to focus on his teaching and Board work. He serves on the Board of Advisors for Bio-Economic Research Associates and also the Board of Advisors for the Bastiat Society of Colorado Springs. Dr. Prentice teaches as a Professor of Economics and Business at Colorado Technical University. He is an Adjunct Scholar at the Ludwig von Mises Institute, a Senior Fellow at the Independence Institute, and a Fellow of the Centennial Institute at Colorado Christian University.

Ronald Rehfeld: Director currently serving a three-year term which expires in 2018 and a member of the Association's Human Resources Committee. Mr. Rehfeld has farmed and ranched since 1980. He currently operates a cow/calf and dryland wheat, feed and millet operation. He also backgrounds, feeds and direct markets his beef. Mr. Rehfeld is a Board Member of the Cheyenne County Farm Service Agency County Committee.

Jeffrey Uhland: Director currently serving a three-year term which expires in 2018 and Vice Chairman of the Association's Human Resources Committee. Mr. Uhland is a partner with his brothers in Tri-County Farms GP, which has a dryland crop operation raising wheat, milo, corn, sunflowers and millet. He is also partner in TC Equipment LLC which owns and leases equipment and U-Land LLC which owns and leases land. He is a partner in Colorado Mills LLC, a sunflower oil and feed processing plant in Lamar, Colorado. He is partner in JAG, Inc. a farming corporation and partner in Kiowa County Investment Group, LLC. He serves on the Kiowa County Weed Board and is an alternate on the Sunflower Administrative Committee.

Christopher Bledsoe: Appointed Director, resigned from the Board in June 2017. His term was due to expire in 2018. Mr. Bledsoe served as a Vice-Chairman of the Board and Chairman of the Association's Audit & Risk Committee prior to his resignation.

SENIOR OFFICERS

Jeremy Anderson: President and Chief Executive Officer (CEO) since November 2017. Previously, he served as Regional President, Board Member and part owner of a community bank in south central Nebraska. Mr. Anderson has over 16 years of commercial banking experience with National and Regional commercial banks. He has also been an active farmer. He and his wife have operated a working row-crop farming operation with his grandparents and parents near Clay Center, Nebraska for 24 years.

William A. Barnes: Chief Appraisal Officer since January 2015. He was Senior Vice President – Appraisal Services January 2011 to December 2014. Prior to that he was the Vice President – Appraisals for 17 years. Mr. Barnes is a Colorado Certified General Appraiser and holds the Accredited Rural Appraiser, (ARA), designation which is awarded by the American Society of Farm Managers and Rural Appraisers, (ASFMRA), to those members who have had years of experience, are technically trained, have passed a rigid examination and subscribe to a high code of ethics. He has held this designation since 1989. He has been with the Farm Credit System for 38 years.

Shawna R. Neppl: Chief Financial Officer since February 2007. Ms. Neppl served as Interim CEO from June 2017 to November 2017. She also served as Vice President/Branch Manager of the Colorado Springs Branch from February 2001 to February 2007 and as Assistant Vice President – Risk Management from January 2000 to February 2001. She has been with the Farm Credit System for 25 years.

David L. Self: Chief Credit Officer beginning in December 2014, previously Executive Vice President Lending from July 2014 to December 2014; Senior Vice President Lending from November 2009 to July 2014. Mr. Self served as the Vice President – Credit from July 2000 to November 2009. Mr. Self started as a field representative in 1981 and has worked for five different Associations, one Farm Credit Bank and three different Farm Credit Districts. Mr. Self has been employed within the Farm Credit System for 37 years.

Ricky Sellers: Interim Chief Operating Officer since July 2017; Standards of Conduct Officer since July 2017; Compliance Officer from January 2011 to present. Previously he served as Vice President/Branch Manager for the Colorado Springs Branch from 2007 to 2010 and Limon Branch from 2008 to 2011 and was a loan officer for the Colorado Springs Branch from June 2001 to 2007. In total, Mr. Sellers has been with Farm Credit of Southern Colorado for over 16 years. Prior to coming to Farm Credit he was the Career and Technical Education Student Organization Specialist/State FFA Advisor for Colorado in the Colorado Community College System and previously taught agricultural education at the high school level.

Kenneth P. West: Chief Banking Officer since March 2016. Previously, Mr. West served as Vice President – Capital Markets from May 2015 to March 2016. Mr. West began his career with CoBank as a credit analyst, then moved to Farm Credit of Southern Colorado from 2004 to 2007 reaching the position of Vice President – Credit. He then served at American AgCredit as Vice President – Relationship Manager for eight years, returning to Farm Credit of Southern Colorado in 2015. Mr. West has been with the Farm Credit System for 16 years and in the banking industry 25 years.

Alan Woodard: President and Chief Executive Officer (CEO) from October 2016 to June 2017.

Linda Iverson: Chief Operating Officer from January 2005 to June 2017.

COMPENSATION OF DIRECTORS AND SENIOR OFFICERS

Directors of the Association were compensated for services on a per diem basis at the rate of $500 per day and an additional $250 preparation time for each Board Meeting (excluding conferences, tours, etc.). The Chairman of the Board and Committee Chairs received an additional $100 per official meeting. When Human Resource (HR) and Audit & Risk committee meetings were held in conjunction with the regular board meetings, no additional compensation was paid to the directors for those meetings. The two Board appointed financial experts received an additional $100 per official meeting. The Directors were compensated at the rate of $100 per hour for conference calls. Mileage was compensated at the rate of $0.535 per mile while on official business.

Additional information for each director is provided below:

	Number of Days Served at		Compensation for			
Name	Board Meetings	Other Official Activities	Board Meetings And Official Duties	Audit and Risk Committee	HR Committee	Compensation Paid During 2017
Gary Paulter	12.0	35.5	$ 25,400	$ 3,500	$ 3,200	$ 32,100
Kent Price	11.0	21.5	18,150	–	4,550	22,700
Colin Durham	11.5	6.5	10,450	2,150	–	12,600
Carl Keith James	12.0	16.5	14,700	–	2,750	17,450
Scott Maranville	11.0	13.0	13,100	–	1,750	14,850
Rosalie Martinez	12.0	18.5	19,000	2,900	–	21,900
John Negley	12.0	18.0	15,350	–	2,750	18,100
Mark Peterson	10.0	17.0	13,900	3,850	–	17,750
Paul Prentice	12.0	17.5	18,400	3,600	–	22,000
Ronald Rehfeld	12.0	19.5	15,750	–	3,000	18,750
Jeffrey Uhland	10.0	13.0	12,100	–	2,000	14,100
Christopher Bledsoe	6.0	15.0	10,000	4,400	–	14,400
Total Compensation			$ 186,300	$ 20,400	$ 20,000	$ 226,700

Directors and senior officers are reimbursed for travel, subsistence and other expenses related to Association business according to Association policy. A copy of this policy is available to shareholders upon request. Aggregate reimbursements to directors for travel, subsistence and other related expenses were $104,287 in 2017, $102,995 in 2016 and $70,623 in 2015. Noncash compensation paid to directors as a group was $582 during 2017.

Information on senior officers and directors who hold Preferred H-Stock follows. The average dividend rate during 2017 on all balances was 0.50%.

Name of the Account	Director or Officer	Title	December 31, 2017 Balance	Purchases during 2017	Retirements during 2017
Gary Pautler	Director	Chairman	$ 50,516	$ 278	$ –

Information on Chief Executive Officer (CEO), senior officers and other highly compensated individuals follows.

CEO Name[1]	Year	Salary	Incentive Compensation	Deferred/Perq	Other[2]	Total
Alan Woodard	2017	$ 124,205	$ –	$ 13,692	$ 10,932	$ 148,829
Shawna Neppl	2017	$ 117,303	$ 16,326	$ 5,128	$ –	$ 138,757
Jeremy Anderson	2017	$ 47,788	$ 6,539	$ 188,342	$ –	$ 242,669
Alan Woodard	2016[3]	$ 70,000	$ 10,466	$ 13,010	$ 210	$ 93,686
Russell Tomky	2016[3]	$ 260,560	$ 39,121	$ 13,540	$ 194,221	$ 507,442
Russell Tomky	2015[3]	$ 317,784	$ 35,946	$ 49,898	$ 236,978	$ 640,606

[1] CEO Compensation for 2017 includes Alan Woodard from January 1 through June 9, 2017, Shawna Neppl as Interim CEO from June 12 through November 10, 2017, and Jeremy Anderson from November 13 through December 31, 2017. CEO compensation for 2016 includes Russell Tomky from January 1 through September 30, 2016, and Alan Woodard from October 1 through December 31, 2016.

Aggregate Number Of Officers/Highly Compensated Individuals (excluding CEO)	Year	Salary	Incentive Compensation	Deferred/Perq	Other[2]	Total
6	2017[1]	$ 1,056,476	$ 96,122	$ 72,464	$ 2,073,936	$ 3,298,999
5	2016[3]	$ 813,291	$ 121,374	$ 56,630	$ 438,973	$ 1,430,268
5	2015[3]	$ 759,497	$ 84,456	$ 43,361	$ 623,028	$ 1,510,342

Disclosure of information on the total compensation paid during the last fiscal year to any senior officer, or to any other officer included in the aggregate, is available to shareholders upon request. The senior officers and highly compensated employees included above are those defined by FCA regulations section 619.9310 and section 620.6.

[1] Aggregate Number includes 5 senior officers and 1 highly compensated employee for 2017. CFO served as Interim CEO for the period June 12, 2017 through November 10, 2017. Compensation earned during this time period is included in CEO information; remaining time is included in senior officer information.

[2] "Other" includes changes in the value of pension benefits, vacation payouts, separation pay and service awards. The change in value of the pension benefits is defined as the vested portion of the present value of the accumulated benefit obligation from December 31 of the prior year, disclosed in Note 11 of the Financial Statements. No tax reimbursements are made to senior officers/highly compensated individuals.

[3] For 2015 and 2016, we reclassified employer match on the deferred contribution plan available to all employees from "Other" to "Deferred/Perq". We also reclassified vacation pay from "Deferred/Perq" to "Other".

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

Senior officers are compensated with a mix of direct cash as well as retirement plans generally available to all employees. Our Board of Directors determines the appropriate balance of short-term compensation while keeping in mind their responsibilities to our shareholders. Base salary and short-term incentive are intended to be competitive with annual compensation for comparable positions at peer organizations. The Association has one Incentive Plan. The Pay for Performance Incentive Program is available to all employees and payable once a year. This Pay for Performance Incentive Program is designed and intended to promote and reward positive business results in several key performance areas. These typically include credit quality, loan volume growth, return on assets and other key

ratios. It is also intended to build and enhance teamwork among all employees and groups of employees for the ultimate benefit of our customers and their Association. Annual Incentive Compensation reflects the amount in the year earned.

Senior officer base salaries reflect the officer's experience and level of responsibility. Base salaries are subject to review and approval by the Human Resource Committee of our Board of Directors and are subject to adjustment based on changes in responsibilities or competitive market conditions.

Information on pension benefits attributable to senior officers and other highly compensated individuals follows. As of December 31, 2017, the CEO did not participate in the Ninth Farm Credit District Pension Plan or the Ninth District Pension Restoration Plan.

Aggregate Number of Senior Officers/ Highly Compensated Individuals Participating in Plan	Plan	Average Years of Credited Service	Present Value of Accumulated Benefits	Payments Made During the Reporting Period
5	Ninth Pension Plan	34.72	$8,714,459	$ 105,338
	Nonqualified Pension Restoration Plan	34.72	$ 843,251	$ –

For the Ninth Pension Plan and the Ninth District Pension Restoration Plan, the average years of service represents an average for the aggregate senior officers and highly compensated employee group included in the Plan.

Retirement Plan Overview – Certain Senior Officers participate in two defined benefit retirement plans: (a) the Ninth Farm Credit District Pension Plan (the Pension Plan), which is a qualified defined benefit plan and (b) the Ninth District Pension Restoration Plan, which is a nonqualified retirement plan. Additionally, substantially all employees participate in the 401(k) Plan, which has an employer matching contribution.

Qualified Pension Plan – In general, the Pension Plan provides participants with a 50% joint-and-survivor annuity benefit at normal retirement that is equal to 1.50% of average monthly compensation during the 60 consecutive months in which an individual receives his highest compensation (High 60) multiplied by his years of benefit service, plus 0.25% of the amount by which the High 60 exceeds covered compensation multiplied by years of benefit service. The benefit is actuarially adjusted if the individual chooses a different form of distribution than a 50% joint-and-survivor annuity, such as a lump sum distribution. The pension valuation was determined using a blended approach assuming half of the benefits would be paid as a lump sum and half as an annuity at the participants earliest unreduced retirement age. The Pension Plan pays benefits up to the applicable limits under the Internal Revenue Code.

Nonqualified Pension Restoration Plan – The Pension Restoration Plan is unfunded and not qualified for tax purposes. Benefits payable under this plan are equal to the excess of the amount that would be payable under the terms of the Qualified Pension Plan disregarding the limitations imposed under Internal Revenue Code Sections 401(a)(17) and 415, over the pension actually payable under the Qualified Pension Plan. The plan also restores any benefits attributable to nonqualified deferred compensation excluded from the benefit determined under the Qualified Pension Plan. The nonqualified pension restoration valuation was determined using an assumption that benefits would be paid as a lump sum at the participants earliest unreduced retirement age.

TRANSACTIONS WITH SENIOR OFFICERS AND DIRECTORS

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 financial statements, "Related Party Transactions," included in this annual report to shareholders.

INVOLVEMENT OF SENIOR OFFICERS AND DIRECTORS IN CERTAIN LEGAL PROCEEDINGS

There were no matters which came to the attention of management or the Board of Directors regarding involvement of senior officers or current directors in specified legal proceedings which are required to be disclosed in this section.

BORROWER PRIVACY STATEMENT

Since 1972, Farm Credit Administration (FCA) regulations have forbidden the directors and employees of Farm Credit institutions from disclosing personal borrower information to others without borrower consent. The Association does not sell or trade customers' personal information to marketing companies or information brokers. Additional information regarding FCA rules governing the disclosure of customer information can be obtained by contacting the Association.

RELATIONSHIP WITH INDEPENDENT AUDITORS

There were no changes in independent auditors since the prior annual report to shareholders and there were no material disagreements with our independent auditors on any matter of accounting principles or financial statement disclosure during this period.

RELATIONSHIP WITH COBANK, ACB (COBANK)

The Association is materially affected by CoBank's financial condition and results of operations.

The Association's statutory obligation to borrow from CoBank is discussed in Note 7. Financial assistance agreements between the Association and CoBank are discussed in Note 8. Association requirement to invest in CoBank and CoBank's ability to access capital of the Association is discussed in Note 4 to the financial statements, "Investment in CoBank," included in this annual report to shareholders. CoBank's role in mitigating the Association's exposure to interest rate risk is discussed in the MD&A section – Liquidity.

CoBank is required to distribute its Annual Report to shareholders of the Association if the bank experiences a significant event that has a material effect on the Association as defined by FCA regulations.

FINANCIAL STATEMENTS

The financial statements, together with the report thereon of PricewaterhouseCoopers LLP dated March 16, 2018, and the Report of Management, appearing as part of this annual report to shareholders, are incorporated herein by reference.

COBANK ANNUAL AND QUARTERLY REPORTS TO SHAREHOLDERS

The shareholders' investment in the Association is materially affected by the financial condition and results of operations of CoBank. Consequently, the Association's annual and quarterly reports should be read in conjunction with CoBank's 2016 Annual and Quarterly Reports to Shareholders. Quarterly reports are available approximately 40 days after the calendar quarter end and annual reports are available approximately 75 days after the calendar year end. A copy of these reports may be obtained free upon request from the Association. The Association is located at 5110 Edison Avenue, Colorado Springs, Colorado 80915, or may be contacted at PO Box 75640, Colorado Springs, Colorado 80970-5640 or by calling (800) 815-8559 or (719) 570-1087. The reports may also be obtained free of charge by visiting CoBank's website at www.cobank.com.