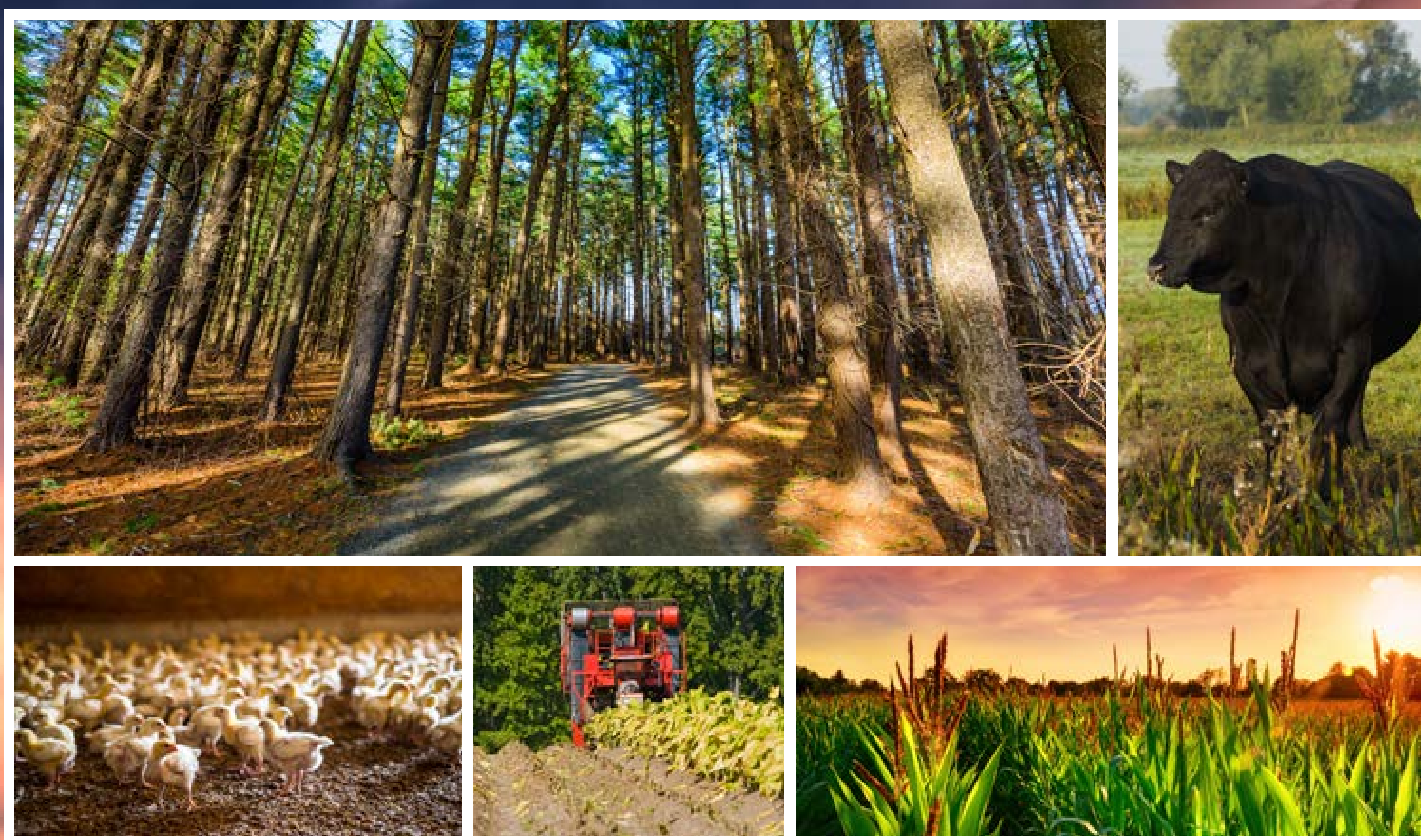
ANNUAL REPORT 2016



ArborOne
FARM CREDIT

ArborOne, ACA

2016 Annual Report

Contents

Management

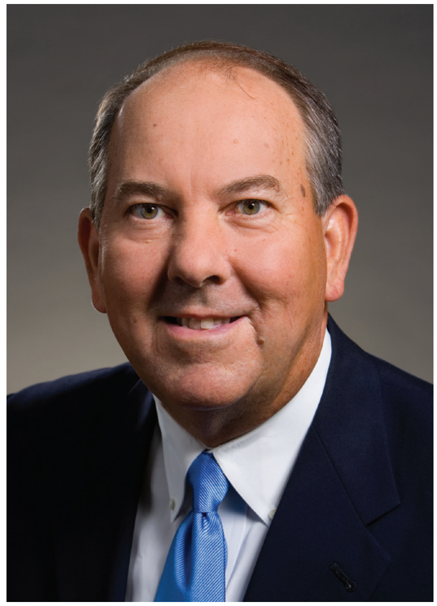
Kathy S. Heustess .... President and Chief Executive Officer
Tammy G. Smith .... Chief Financial Officer and Treasurer
Richard O. Pitts .... Chief Lending Officer
Sarah H. Jackson .... Director of Human Resources and Corporate Secretary

Board of Directors

James M. Ward .... Chairman
William DuPree Atkinson .... Vice Chairman
Harry B. DuRant .... Director
John E. Lay .... Director
John Lee Newman. .... Director
J. Whit Player .... Director
Jimmy Poston .... Director
Kelly O. Wiseman .... Director

THOMAS "TOM" S. WELSH, SR.

September 26, 1947 – August 15, 2016



Tom was a caring servant leader who was loved by all. He always looked for the good in everyone and as a leader looked for ways to grow not only the folks who reported to him directly, but everyone. Throughout his work life, he believed in listening to the input of those around him no matter their place on the organizational chart. Tom, a proud Clemson graduate, was born and reared in the Dog Island section of rural Lee County. Tom continued tilling the land and feeding the world through his work that began at the Production Credit Association in Orangeburg and later as Executive Vice President at AgFirst Farm Credit Bank in Columbia. Even after his retirement a few years back, his work continued with the Bank and Farm Credit Associations, including ArborOne, through the contract services he provided. One of his lifetime goals was to serve on an Association board, and he was appointed to the ArborOne Farm Credit board just months prior to his death.

Reflecting on a life that was so dear to many, one cannot fail to mention his belief in running daily despite the many obstacles of a busy executive. The emotional traits of a runner certainly are indicative of the Tom we all knew: Strong vision… Tom always made a way to build bridges with everyone and that vision always paid him future benefits on a project, meeting or personal endeavor. Focus and resilience… Tom always remained focused on the task at hand but quickly adapted to change. Capacity to Plan ahead… an attribute that served him well as he prepared planning sessions for as many as 16 Farm Credit Associations each year, including ArborOne prior to being appointed to our board. Calm demeanor… always calm unless, of course, changes were made without him knowing the details.

If you ever had the opportunity to ride with Tom or travel to a city where there was a jazz club, you may have gotten the opportunity to hear some of his favorite jazz tunes. Tom always had a story to share about someone he talked to on a plane ride or met in the lobby while waiting for an appointment. He never met a stranger and always took the time to listen. Tom was a great leader in his family as well. Whether he was teaching you how to shag dance or cook a "mean" low-country boil or simply placing a daily call to his sister, he modeled how to care for others. When he was relaxing on "his" Harbor Island, where he and his wife, Judy, had made their retirement home, he patrolled for sea turtles at sunrise and enjoyed a glass of red wine at sunset. He lived life fully.

He was quick to support charitable organizations as well as mission work with young adults. Tom often remarked that he never knew how poor he was growing up until he went to Clemson. He always wanted to give back. He believed that his success was from being persistent (another runner's trait) and remaining organized, a trait that dated back to his military experience. He also practiced that in his work life, working through some difficult situations while maintaining the course that paved the way for his success. He consistently reminded his employees that someone was always watching and that discipline should always be exercised. He preached the need to build advocates because we all need them.

Tom was a Clemson fan through and through. He rarely missed a home game. When Dabo Swinney took the head coaching position and later faced some opposition from his home team fans, Tom wrote Dabo a letter of encouragement as he did with many on a daily basis. A week never passed that Tom did not write at least one handwritten note with a blue medium point pen. Notes that left you feeling valued, important, remembered. Notes that many will cherish for years to come.

We will miss our friend, who left us suddenly and way too soon. We have renamed our scholarship the ArborOne Farm Credit Thomas S. Welsh Memorial Scholarship, in grateful memory of the life of a man who served agriculture and the Farm Credit System for over 40 years.

Message from the President

Dear Stockholder:

"2015 will go down in South Carolina history as the year of 'The Historic Flood.' From an overall economic standpoint, the impact will be felt for many years to come. For agriculture alone, immediate losses are estimated to be nearly $600 million; however, the long-term impact will likely be much more severe." This is a quote from my 2015 letter, and as anticipated, we spent much of 2016 assessing and working through the impact of 2015's weather events. Once again in 2016, weather events were still among our greatest concerns. In 2017, ArborOne will continue to work with each of you on an individual basis – as we always have – to advise you on the lending options that best fit your unique financial situation and needs because *your* success is *our* success. Our focus for 2017, much the same as it was in 2016, will be on growing the business, ensuring proper credit administration, maintaining a strong financial position, taking full advantage of our cooperative business model, and retaining a competent and engaged staff, while leveraging our good reputation locally and throughout the state.

Business Growth and Employee Engagement: ArborOne ended the year with earnings above projections! Keys to attaining our goals were loan growth of approximately 8 percent while also managing operating expenses. Each year we invest in planning, and this year was no exception. Our board and management team has a dedicated planning session and works throughout the year with the management team present in board and committee meetings. This helps us keep the focus on the key initiatives and measures that will sustain the Association for the next 100 years! Planning begins with the board but evolves into action when all employees provide the ideas for realistically reaching these objectives through our processes, events, marketing and service to our customers. Every organization must grow in order to survive. This year we will place special emphasis on how to reach our customers in new and innovative ways, and we want your input. In mid-January, we emailed almost 2,000 brief surveys to customers or potential customers. If you received a survey, it's my hope that you took the time to answer it. The goal of the survey was to determine how we can better serve your needs. Such information to be gathered includes: how you prefer to receive information; how you make key business decisions, such as land acquisitions or equipment purchases; who you turn to for information and expertise; and what creates customer loyalty. During 2017, we will provide more opportunities for interaction and feedback from you through educational seminars on topics of your choosing. We want to help you achieve your goals.

Credit Administration and Financial Strength: We are living in volatile times for agriculture, and it seems at times that we are on the cutting edge of that volatility given the severe weather events of the past several years. We want to always be your first-choice agricultural lender and financial expert. That is why our business model works; each of you has a relationship manager who works directly with you. They know you and your farming operations because they work with you at your place of business – not behind a desk – and many of them have farming operations themselves! We promised we would be here when times are bad just like we have been here through the good times. Like any industry, agriculture has cycles, but serving the needs of agriculture in the Pee Dee region is our mission and our passion! In 2016 Farm Credit celebrated its 100th year of supporting agriculture and rural communities. So it is with much confidence we say: We have been in it through each of those up and down cycles for the last 100 years and we plan to continue the course for the next hundred years – and beyond.

Reputation: We need your continued help to educate our representatives in Congress about agriculture. We believe it is important that they have a basic knowledge of what it means to be a farmer or to run an agribusiness. With few congressional members having an agricultural background, we believe it is imperative to remind them of the huge responsibility farmers have. As a member of the Farm Credit System, we participate in Capitol Hill visits and meet with legislators to promote the Farm Bill, emphasize the importance of crop insurance, and to educate our nation's leaders regarding agriculture and the role Farm Credit plays in financing rural communities and agriculture.

Cooperative Advantage: In a nutshell, patronage is your return for doing business with ArborOne; because as a cooperative, patronage is earned and distributed in a pro rata manner based upon how much business you do with your cooperative. Our cooperative structure, along with serving our mission and our vast knowledge of agriculture, sets us apart from commercial banks. In 2016, the board once again approved a revolvement of surplus capital amounting to approximately $2.5 million because we were financially sound and well capitalized. In about a month, you will receive a patronage check returning back a portion of the interest you paid on your borrowed funds during 2016. No other lending institution pays you back a portion of your interest expense like your Farm Credit cooperative.

We are ready for 2017! We want to help you to have a successful year! I hope I will get to see you at one of our annual customer events and at some of the educational events we are planning. We value your business, recognizing that it is a relationship that is built on trust and expertise.

Together, we are Farmer Strong!

Kathy S. Heustess

Kathy S. Heustess
President and Chief Executive Officer

March 13, 2017

Report of Management

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

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

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

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

James M. Ward

James M. Ward
Chairman of the Board

Kathy S. Heustess

Kathy S. Heustess
President and Chief Executive Officer

Tammy G. Smith

Tammy G. Smith
Chief Financial Officer and Treasurer

March 13, 2017

Report on Internal Control Over Financial Reporting

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

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

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

Kathy S. Heustess

Kathy S. Heustess
President and Chief Executive Officer

Tammy G. Smith

Tammy G. Smith
Chief Financial Officer and Treasurer

March 13, 2017

Consolidated Five - Year Summary of Selected Financial Data

(dollars in thousands)	December 31, 2016	2015	2014	2013	2012
Balance Sheet Data					
Cash	**$ 12**	$ 2	$ 2	$ 28	$ 432
Investment securities	**18,489**	22,171	29,767	41,286	53,492
Loans	**447,150**	383,427	340,945	306,199	298,785
Allowance for loan losses	**(8,676)**	(7,379)	(4,904)	(4,489)	(4,712)
Net loans	**438,474**	376,048	336,041	301,710	294,073
Investments in other Farm Credit institutions	**5,659**	9,316	10,497	12,395	13,267
Other property owned	**623**	1,553	3,807	6,223	7,441
Other assets	**20,421**	20,080	21,360	45,950	65,358
Total assets	**$ 483,678**	$ 429,170	$ 401,474	$ 407,592	$ 434,063
Notes payable to AgFirst Farm Credit Bank*	**$ 386,383**	$ 335,894	$ 309,286	$ 321,897	$ 342,261
Subordinated debt payable to other Farm Credit institutions	**—**	—	—	—	7,500
Accrued interest payable and other liabilities with maturities of less than one year	**12,777**	12,656	13,802	12,900	11,280
Total liabilities	**399,160**	348,550	323,088	334,797	361,041
Protected borrower stock	**62**	62	78	91	118
Capital stock and participation certificates	**1,351**	1,290	1,229	1,238	1,197
Retained earnings					
Allocated	**54,690**	52,625	51,516	49,893	43,392
Unallocated	**28,196**	25,945	24,578	22,574	22,686
Accumulated other comprehensive income (loss)	**219**	698	985	(1,001)	5,629
Total members' equity	**84,518**	80,620	78,386	72,795	73,022
Total liabilities and members' equity	**$ 483,678**	$ 429,170	$ 401,474	$ 407,592	$ 434,063
Statement of Income Data					
Net interest income	**$ 11,768**	$ 10,683	$ 9,959	$ 10,167	$ 9,029
Provision for (reversal of allowance for) loan losses	**1,711**	2,703	347	(444)	215
Noninterest income (expense), net	**(1,280)**	(380)	452	1,601	2,532
Net income	**$ 8,777**	$ 7,600	$ 10,064	$ 12,212	$ 11,346
Key Financial Ratios					
Rate of return on average:					
Total assets	**1.92%**	1.85%	2.57%	2.96%	2.77%
Total members' equity	**10.33%**	9.24%	12.71%	16.26%	15.69%
Net interest income as a percentage of average earning assets	**2.67%**	2.74%	2.74%	2.65%	2.42%
Net (chargeoffs) recoveries to average loans	**(0.099)%**	(0.063)%	0.021%	0.071%	0.462%
Total members' equity to total assets	**17.47%**	18.79%	19.52%	17.86%	16.82%
Debt to members' equity (:1)	**4.72**	4.32	4.12	4.60	4.94
Allowance for loan losses to loans	**1.94%**	1.92%	1.44%	1.47%	1.58%
Permanent capital ratio	**19.42%**	20.83%	21.11%	20.13%	20.22%
Total surplus ratio	**19.10%**	20.45%	20.71%	19.69%	19.80%
Core surplus ratio	**16.46%**	19.36%	18.38%	18.99%	17.19%
Net Income Distribution					
Estimated patronage refunds:					
Cash	**$ 1,992**	$ 1,636	$ 2,415	$ 3,544	$ 2,046
Qualified allocated retained earnings	**332**	1,091	—	591	2,046
Nonqualified allocated retained earnings	**4,317**	2,726	3,634	7,680	6,138
Nonqualified retained earnings	**—**	—	2,000	—	—

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

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

(dollars in thousands, except as noted)

GENERAL OVERVIEW

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

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

The Association is a cooperative, which is owned by the members (also referred to throughout this Annual Report as stockholders or shareholders) served. The territory of the Association extends across a diverse agricultural region of 12 counties located in northeastern South Carolina. Refer to Note 1, *Organization and Operations*, of the Notes to the Consolidated Financial Statements for counties in the Association's territory. The Association provides credit to farmers, ranchers, rural residents, and agribusinesses. Our success begins with our extensive agricultural experience and knowledge of the market.

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

Copies of the Association's Annual and Quarterly reports are also available upon request free of charge on the Association's website, ***www.arborone.com***, or by calling 1-800-741-7332, extension 2317, or writing Sarah Jackson, Corporate Secretary, ArborOne, ACA, P.O. Box 3699, Florence, S.C. 29502. The Association prepares an electronic version of the Annual Report, which is available on the website, within 75 days after the end of the fiscal year and distributes the Annual Reports to shareholders within 90 days after the end of the fiscal year. The Association prepares an electronic version of the Quarterly report, which is available on the internet, within 40 days after the end of each fiscal quarter, except that no report needs to be prepared for the fiscal quarter that coincides with the end of the fiscal year of the Association.

FORWARD LOOKING INFORMATION

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

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

AGRICULTURAL OUTLOOK

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

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

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

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

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

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

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

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

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

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

CRITICAL ACCOUNTING POLICIES

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

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

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

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

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

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

ECONOMIC CONDITIONS

During 2016, general economic conditions in our region were stable to improving when compared to 2015. Agricultural loan demand stabilized in 2016 due to lower commodity prices. Competition for agricultural loans continued strong in 2016 despite the stumbling agriculture economy. Unemployment in each of our 12 counties improved year over year but remains challenged in a few counties. South Carolina's unemployment rate was improved year over year ending 2016 at 4.3%. The overall U.S. unemployment rate ended the year at 4.7% showing improvement over the previous year's 5.0%. The housing and real estate markets in general continued to show improvement during 2016.

Much like 2015 our territory experienced more tumultuous weather albeit not as devastating from an agricultural perspective. The end of the summer turned out to be hot and dry with drought conditions and in the fall we experienced the remnants of tropical storm Hermine and a hurricane. Hurricane Matthew produced massive amounts of rain and devastating winds in the Pee Dee Region of our territory. For farmers located in our territory, those along the coast were impacted the hardest. However, agricultural economic impacts from the 2016 weather is expected to be minimal at best compared to the impacts from the flood and subsequent rains of 2015. The main difference in 2016 was that the rain stopped which allowed farmers to harvest their crops unlike 2015 where it continued to rain well into the new year thus killing any chances for farmers to salvage their crops. Throughout all of this the staff of ArborOne has been and continues to be dedicated to working diligently with our customers impacted by these two consecutive years of natural disasters. We do have tools in place to mitigate risks such as Farm Services Agency (FSA) guarantees, crop insurance and allowance for loan losses.

For the year ended December 31, 2016, the credit quality of the loan portfolio worsened in comparison to the previous year end. For the agricultural sector in 2016, continued high input prices coupled with continued lower commodity prices made profit margins slim for farm producers. Livestock producers saw the beginning of price declines in 2016, mainly for cattle. Swine and poultry industries profit margins were stable. Industries tied to housing such as forestry, sawmills, sod, and landscape nurseries saw increases in demand and profitability during 2016, but are still lagging behind numbers of the pre-recession era. Overall, we expect the credit quality of the Association's loan portfolio to remain stable to slightly decreasing in 2017 due to a continued weak agricultural economy coupled with two consecutive years of natural disasters impacting farmers right at harvest time.

During 2016, the Association continued to operate under tightened lending practices and policies in order to strengthen its capital and portfolio. By taking these actions beginning in 2010 and continuing thereafter, the Association has the tools necessary to weather any difficulties that may come to fruition during 2017. The Association continues efforts to expand services, increase public knowledge of our services, and streamline our current delivery of products to enhance our value to our customer owners.

LOAN PORTFOLIO

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

The gross loan volume of the Association as of December 31, 2016 was $447,150, an increase of $63,723 or 16.62 percent as compared to $383,427 at December 31, 2015, and an increase of $106,205 or 31.15 percent as compared to $340,945 at December 31, 2014. Net loans outstanding (gross loans net of the allowance for loan losses) on December 31, 2016 were $438,474, as compared to $376,048 at December 31, 2015, and $336,041 at December 31, 2014. Net loans accounted for 90.65 percent of total assets on December 31, 2016, as compared to 87.62 percent of total assets at December 31, 2015, and 83.70 percent of total assets at December 31, 2014.

The diversification of the Association's loan volume by type for each of the past three years at December 31 is shown in the below table.

	December 31,					
Loan Type	**2016**		**2015**		**2014**	
	(dollars in thousands)					
Real estate mortgage	$ 232,251	51.94 %	$ 187,971	49.02 %	$ 168,297	49.36 %
Production and intermediate term	185,439	41.47	162,608	42.41	150,899	44.26
Loans to cooperatives	1,866	0.42	436	0.11	455	0.13
Processing and marketing	16,385	3.67	21,591	5.63	12,144	3.56
Farm-related business	4,599	1.03	3,929	1.03	4,066	1.19
Power & Water/waste disposal	860	.19	2,391	0.63	753	0.22
Rural residential real estate	4,784	1.07	4,371	1.14	4,181	1.23
International	856	.19	–	–	–	–
Lease receivables	110	.02	130	0.03	150	0.05
Total	$ 447,150	100.00 %	$ 383,427	100.00 %	$ 340,945	100.00 %

While we make loans and provide financially related services to qualified borrowers in the agricultural and rural sectors and to certain related entities, our loan portfolio is diversified. The following tables reflect the geographic locations served and the commodities financed for both core and participation purchased loans.

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

	December 31,		
County	**2016**	**2015**	**2014**
Clarendon	14.6%	14.6%	12.8%
Horry*	11.7	10.7	9.6
Darlington	8.7	8.0	7.6
Sumter	7.9	7.6	7.6
Lee	7.1	6.5	6.4
Florence*	6.9	6.3	5.5
Williamsburg	5.4	5.5	4.6
Dillon	5.1	5.3	6.3
Chesterfield	4.6	5.1	5.9
Georgetown	3.6	2.9	3.5
Marion	2.6	2.6	3.2
Marlboro	1.2	1.4	1.6
Other**	20.6	23.5	25.4
Total	100.0%	100.0%	100.0%

**Branch Locations*
***The Other category above consists of loans originated and participated outside our territory.*

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

The major commodities in the Association loan portfolio are shown below. The predominant commodities are field crops, cash grains, forestry, and poultry which constitute 67 percent of the entire portfolio.

Commodity Group	December 31, 2016		2015		2014	
	(dollars in thousands)					
Field Crops	$ 94,440	21%	$ 82,755	21%	$ 77,395	23%
Cash Grains	84.856	19	73,568	19	56,859	16
Forestry & Logging	63,258	14	53,219	13	53,243	15
Poultry & Eggs	60,346	13	54,656	14	47,720	14
Miscellaneous	30,628	7	20,175	5	17,272	5
Livestock & Animal Specialties	30,373	7	27,408	7	24,750	7
General Farms	28,193	6	24,892	6	18,263	5
Agricultural Services	15,397	3	15,773	4	14,915	4
Food Preparations	12,775	3	8,095	2	7,122	2
Vegetables & Fruits	7,899	1	7,212	2	5,860	2
Horticultural Specialties	7,034	1	3,167	1	4,696	1
Mission Related Investments	6,602	1	7,524	2	7,683	2
Rural Home Loans	4,126	1	2,775	1	2,541	1
Rural Utilities	860	1	1,637	1	1,768	1
Tobacco Stem & Redry	217	1	503	1	608	1
Non-Farm Income	146	1	68	1	–	–
Energy	–	–	–	–	250	1
Total	$ 447,150	100%	$ 383,427	100%	$ 340,945	100%

Repayment ability is closely related to the commodities produced by our borrowers, and increasingly, the off-farm income of borrowers. The Association's largest concentrations based on risk volume are in cash grains, cotton, tobacco, contract poultry and forestry. Although a large percentage of the loan portfolio is concentrated in these industries, many of these operations are diversified within their enterprise and/or with crop production and additional sources of income, including non-farm businesses and salaried income, which reduces overall risk exposure. Demand for protein, prices of commodities, and international trade are some of the factors affecting these industries. The risk in the portfolio associated with commodity concentration and large loans is reduced by the range of diversity of enterprises in the Association's territory.

The increase in net loan volume for the twelve months ended December 31, 2016, was primarily attributed to an increase in originated loan volume within our twelve counties, the repurchase of our participations sold through the capitalized participation pools (CPPs) program, which was partially offset by the increase in participations sold within the district, a decrease in participations purchased, and an increase in allowance for loan losses. The general economy has improved but remains vulnerable. The agricultural economy has thrived the last few years; however, commodity price suppression began in 2014 and has worsened in 2016 with the negative trend expected to continue in 2017. Thus, the impact to association volume is expected to remain stable within its twelve counties.

Beginning in 2011 and continuing to present day, the Association has decreased purchased loan activity. However, as a means for the Association to spread credit concentration risk and realize non-patronage sourced interest and fee income, the strategy is to purchase accounts with acceptable credit risk to the Association.

During 2015, the Association had decreased activity in the selling of loans, primarily to the Bank, through the utilization of the CPPs program, which was used to strengthen both AgFirst and the Association's capital position. In 2016, given the Association's strong capital position, the Association canceled its participation in the CPPs program with the Bank. As a result, the Association repurchased $37,552 of participations previously sold to AgFirst. This decision was made effective October 1, 2016.

Loan Participations:	December 31, 2016	2015	2014
	(dollars in thousands)		
Participations Purchased – FCS Institutions	$ 39,654	$ 46,590	$ 46,757
Participations Purchased – Non-FCS Institutions	1,831	2,102	2,214
Participations Sold	(27,389)	(61,808)	(76,314)
Total	$ 14,096	$ (13,116)	$ (27,343)

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

The Association participates in the Farmer Mac Long Term Stand-By program. Farmer Mac was established by Congress to provide liquidity to agricultural lenders. At December 31, 2016, 2015, and 2014, the Association had loans amounting to $63, $306, and $395, respectively, which were 100 percent guaranteed by Farmer Mac. The Association had other federal guaranteed loans in the amount of $5,019 at December 31, 2016, compared to $5,141 at December 31, 2015, and $5,234 at December 31, 2014. In addition, the Association had $70,661 in FSA guaranteed loans at December 31, 2016, compared to $67,726 at December 31, 2015, and $70,048 at December 31, 2014.

MISSION RELATED INVESTMENTS

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

In October 2005, the FCA authorized AgFirst and the associations to make investments in Rural America Bonds under a three-year pilot period, and in October 2008 approved a continuation of the program. Effective December 31, 2014, the FCA concluded each pilot program approved as part of the Investment in Rural America program. Each institution participating in such programs may continue to hold its investment through the maturity dates for the investments, provided the institution continues to meet all approval conditions. Although the pilot programs are concluded, the FCA can consider future requests on a case-by-case basis. Rural America Bonds may include debt obligations issued by public and private enterprises, corporations, cooperatives, other financing institutions, or rural lenders where the proceeds would be used to support agriculture, agribusiness, rural housing, economic development, infrastructure, or community development and revitalization projects in rural areas. Examples would include investments in: value-added food and fiber processors/marketers, agribusiness, rural commercial enterprises, community services, schools, hospitals, and municipalities. These along with many other activities that sustain or revitalize rural communities and their economics would be a focus. The objective of this program was to help meet the growing and diverse financing needs of agricultural enterprises, agribusinesses, and rural communities by providing a flexible flow of money to rural areas through bond financing. These bonds may be classified as Loans or Investments on the Consolidated Balance Sheets depending on the nature of the investment. As of December 31, 2016, 2015, and 2014, the Association had $6,603, $7,525, and $7,683, respectively, in Rural America Bonds classified as Loans and $18,489, $21,171, and $29,767, respectively, in Rural American Bonds classified as Investments on the Consolidated Balance Sheets.

In September 2006, Meritus Ventures, L.P. (Meritus) received final approval and licensing as a Rural Business Investment Company (RBIC) that specifically targets investments in companies in rural areas in central and southern Appalachia and Arkansas. As of September 2011, the Association made a final capital call for a total investment of $250. Beginning in 2013, evaluations of the RBIC indicated that decreases in value of the investment had occurred that were other than temporary resulting in an initial credit impairment loss of $180. The Association recognized additional credit impairment losses of $40 and $30 for the years ended December 31, 2015 and 2014, respectively.

Refer to Note 4, *Investments,* of the Notes to the Consolidated Financial Statements for additional information regarding these Mission Related Investments.

INVESTMENT SECURITIES

As permitted under FCA regulations, the Association is authorized to hold eligible investments for the purposes of reducing interest rate risk and managing surplus short-term funds. The Bank is responsible for approving the investment policies of the Association. The Bank annually reviews the investment portfolio of every Association that it funds.

At the beginning of 2014, the Association's investment securities portfolio consisted of Mission Related Investments classified as available-for-sale. Because there have been no significant sales of available-for-sale securities for an extended period of time, and current management has the firm intent and ability to hold those securities to maturity, the Association judged that a held-to-maturity classification more closely reflects the way in which it expects to benefit from the cash flows from those assets. As a result, on October 1, 2014, the Association transferred $33,007 of its available-for-sale investments to a held-to-maturity classification while two of its ineligible bonds totaling $77 were settled with properties acquired.

For a debt security transferred into the held-to-maturity category, the use of fair value may create a premium or discount that, under amortized cost accounting, shall be amortized thereafter as an adjustment of yield. The investments were transferred to held-to-maturity at fair value with unrealized gains and losses recognized in Other Comprehensive Income (OCI) as a net unrealized gain in the amount of $1,189. These OCI amounts will be amortized or accreted to interest income ratably over the remaining life of each individual security in accordance with generally accepted accounting principles (GAAP). The amortization of an unrealized holding gain or loss reported in OCI will offset or mitigate the effect on interest income of the amortization of any premium or discount recorded on transfer to held-to-maturity for each security.

During 2016, investment securities decreased by $3,682. The decrease was mainly due to the payoff of one investment security in the amount of $2,778, normal payments in the amount of $945, and the amortization of the net unrealized gain from the transfer to HTM in the amount of $469. These decreases were offset by the partial accretion to interest income of the credit impairment on the substandard investment security in the amount of $510.

As of December 31, 2016, the majority of the Association's held-to-maturity Mission Related Investments are guaranteed; therefore the risk of credit loss to the Association is reduced. However, as of December 31, 2016, one security was rated as substandard and one security was rated other assets especially mentioned (OAEM), which made these securities ineligible investments under FCA regulation. FCA has been notified of these downgrades as required.

During 2014, an additional credit impairment of $114 was recognized on one of the two ineligible investments that were settled, bringing the total credit impairment on the two bonds to $406. Unrealized credit impairments on the remaining HTM investment portfolio as of December 31, 2014, totaled $2,757. No additional credit impairments were taken in 2015 or 2016; however, a partial accretion to interest income of the credit impairment on the substandard investment security during 2015 and 2016 were recognized in the amounts of $223 and $510, respectively. This reduced the total credit impairment to $2,024 as of December 31, 2016. No new bonds were added during 2016.

CREDIT RISK MANAGEMENT

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

- Character – borrower integrity and credit history
- Capacity – repayment capacity of the borrower based on cash flows from operations or other sources of income
- Collateral – protection for the lender in the event of default and a potential secondary source of repayment
- Capital – ability of the operation to survive unanticipated risks
- Conditions – intended use of the loan funds

The credit risk management process begins with an analysis of the borrower's credit history, repayment capacity, and financial position. Repayment capacity focuses on the borrower's ability to repay the loan based upon cash flows from operations or other sources of income, including non-farm income. Real estate loans must be collateralized by first liens on the real estate (collateral). As required by FCA regulations, each institution that makes loans on a collateralized basis must have collateral evaluation policies and procedures. Long term real estate mortgage loans may be made only in amounts up to 85 percent of the original purchase price or appraised value, the lesser of the two, of the property taken as collateral or up to 97 percent of the purchase price or appraised value, the lesser of the two, if guaranteed by a state, federal, or other governmental agency. The actual loan to appraised value when loans are made is generally lower than the statutory maximum percentage as outlined in the previous statement. Appraisals are required for loans of more than $250,000 and/or loans with an amortization of 10 years and greater. In addition, each loan is assigned a credit risk rating based upon the underwriting standards. This credit risk rating process incorporates objective and subjective criteria to identify inherent strengths, weaknesses, and risks in a particular relationship.

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

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

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

Credit Quality	2016	2015	2014
Acceptable & OAEM	97.64%	96.66%	95.60%
Substandard	2.36%	3.33%	4.38%
Doubtful	–%	0.01%	0.02%
Total	100.00%	100.00%	100.00%

Nonperforming Assets

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

	December 31,		
High-risk Assets	**2016**	**2015**	**2014**
	(dollars in thousands)		
Nonaccrual loans	$ 10,929	$ 9,469	$ 4,893
Restructured loans	9,432	7,377	6,789
Accruing loans 90 days past due	–	–	–
Total high-risk loans	20,361	16,846	11,682
Other property owned	623	1,553	3,807
Total high-risk assets	$ 20,984	$ 18,399	$ 15,489
Ratios			
Nonaccrual loans to total loans	2.44%	2.47%	1.44%
High-risk assets to total assets	4.34%	4.29%	3.86%

Nonaccrual loans represent all loans where there is a reasonable doubt as to the collection of principal and/or future interest accruals, under the contractual terms of the loan. In substance, nonaccrual loans reflect loans where the accrual of interest has been suspended. Nonaccrual loans increased $1,460 or 15.42% in 2016. This increase was mainly due to the transfer of several core loans to nonaccrual. The increase was partially offset by chargeoffs, normal payments, the reinstatement of two core loans to accruing status, and the transfer of two core loans to other property owned. Of the $10,929 in nonaccrual volume at December 31, 2016, $4,022 or 36.80% compared to 33.86% and 21.75% at December 31, 2015 and 2014, respectively, was current as to scheduled principal and interest payments, but did not meet all regulatory requirements to be transferred into accrual status.

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

Allowance for Loan Losses

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

The following table presents the activity in the allowance for loan losses for each of the past three years at December 31.

Allowance for Loan Losses Activity:	2016	2015	2014
	Year Ended December 31, (dollars in thousands)		
Balance at beginning of year	$ 7,379	$ 4,904	$ 4,489
Charge-offs:			
Real estate mortgage	(300)	(268)	(70)
Production and intermediate-term	(342)	(188)	–
Total charge-offs	(642)	(456)	(70)
Recoveries:			
Real estate mortgage	70	125	130
Production and intermediate-term	158	103	8
Total recoveries	228	228	138
Net (charge-offs) recoveries	(414)	(228)	68
Provision for (reversal of allowance for) loan losses	1,711	2,703	347
Balance at end of year	$ 8,676	$ 7,379	$ 4,904
Ratio of net (charge-offs) recoveries during the period to average loans outstanding during the period	(0.099)%	(0.063)%	0.021%

The loan charge-offs were primarily associated with charge-offs on several core loans. The recoveries were mainly attributed to both core and participation loans.

Provision for loan loss was increased due to the growth in loan volume along with an additional special allowance for the significant rains and wind conditions experienced at the harvest peak in 2016.

The allowance for loan losses by loan type for each of the past three years at December 31 is shown in the below table.

	Year Ended December 31, 2016		2015	
	Amount	%	Amount	%
Real estate mortgage	$ 1,823	21.01%	$ 1,811	24.54%
Production and intermediate-term	6,410	73.88	4,872	66.03
Agribusiness	297	3.43	293	3.97
Power & Water/waste disposal	8	0.09	277	3.75
Rural residential real estate	18	0.21	9	0.12
International	7	0.08	–	–
Lease receivables	113	1.30	117	1.59
Total	$ 8,676	100.00%	$ 7,379	100.00%

	For Year Ended December 31, 2014	
	Amount	%
Real estate mortgage	$ 1,360	27.73%
Production and intermediate-term	2,314	47.19
Agribusiness	809	16.50
Power & Water/waste disposal	301	6.14
Rural residential real estate	7	0.14
International	–	–
Lease receivables	113	2.30
Total	$ 4,904	100.00%

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

Allowance for Loan Losses as a Percentage of:	December 31, 2016	2015	2014
Total loans	1.94%	1.92%	1.44%
Total high risk loans	42.61%	43.80%	41.98%
Nonaccrual loans	79.39%	77.93%	100.22%

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

RESULTS OF OPERATIONS

Net income for the year ended December 31, 2016 totaled $8,777, an increase of $1,177 or 15.49 percent as compared to $7,600 for the same period of 2015, and a decrease of $1,287 or 12.79 percent as compared to $10,064 for the same period of 2014.

Net Interest Income

Net interest income was $11,768, $10,683, and $9,959 in 2016, 2015, and 2014, respectively. Net interest income is the difference between interest income and interest expense. Net interest income is the principal source of earnings for the Association and is impacted by volume, yields on assets, and cost of debt. The effects of changes in average volume and interest rates on net interest income over the past three years are presented in the following table:

Change in Net Interest Income:

	Volume*	Rate	Nonaccrual Income	Total
	(dollars in thousands)			
12/31/16 - 12/31/15				
Interest income	$ 2,438	$ (84)	$ 96	$ 2,450
Interest expense	1,087	278		1,365
Change in net interest income	$ 1,351	$ (362)	$ 96	$ 1,085
12/31/15 - 12/31/14				
Interest income	$ 1,330	$ (747)	$ 30	$ 613
Interest expense	486	(597)		(111)
Change in net interest income	$ 844	$ (150)	$ 30	$ 724

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

Net interest income increased by $1,085 or 10.16 percent in 2016 compared to 2015 and increased by $1,809 or 18.16 percent compared to 2014. The key reason for the increase of $1,085 was due to an increase of new loan volume and the terming out of operating lines of credit due from the recent unforeseen weather conditions and lower commodity prices. Interest expense increased mainly due to the increase in loan volume.

The Association's net interest income as a percentage of average earning assets was 2.67 percent on December 31, 2016, compared to 2.74 percent on December 31, 2015, and 2.74 percent on December 31, 2014.

Noninterest Income

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

Noninterest Income	For the Year Ended December 31, 2016	2015	2014	Percentage Increase/(Decrease) 2016/2015	2015/2014
	(dollars in thousands)				
Loan fees	$ 1,693	$ 1,793	$ 1,909	(5.58)%	(6.08)%
Fees for financially related services	979	1,191	1,211	(17.80)	(1.65)
Patronage refund from other Farm Credit Institutions	6,792	7,043	9,279	(3.56)	(24.10)
Gains (losses) on sales of premises and equipment, net	32	61	–	(47.54)	100.00
Gains (losses) on sales of investment securities	–	–	96	–	(100.00)
Gains (losses) on other transactions	26	(1)	266	2,700.00	(100.38)
Net impairment losses on investments	–	(40)	(144)	100.00	(72.22)
Other noninterest income	4	6	21	(33.33)	(71.43)
Total noninterest income	$ 9,526	$ 10,053	$ 12,638	(5.24)%	(20.45)%

The decrease in loan fees of $100 for the 2016 year was attributed mainly to the reduction in Rural America Bond fees. Bond fees are typically based on volume, and volume has been reduced as a result of normal payments, one payoff, and the reduction in servicing fees on one investment.

The decrease in fees for financially related services was $212. This was primarily due to the farmers experiencing lower commodity prices along with higher input costs, which resulted in less crops planted in 2016 as well as a decrease in the loss ratio bonus due to the large quantity of claims from the 2015 flood.

Regarding patronage refunds received from other Farm Credit Institutions, the Association received $4,194 in a patronage refund and $2,486 in a special distribution from the Bank for the year ended December 31, 2016, compared to $4,445 and $2,496 for 2015, and $4,764 and $4,488 for 2014. Of the patronage refund, patronage paid on the CPP loans was $1,382, $1,998, and $2,449 for 2016, 2015, and 2014 respectively.

In 2014, the Association recorded a gain on sales of investment securities due to the disposal of one guaranteed callable investment security that resulted in a gain of $96; however, none were recorded in 2015 or 2016.

Gains on other transactions increased $27 for the year ended December 31, 2016. This increase is mainly the result of recorded gains on retirement plans as well as a gain from the distribution of surplus at net present value on one core loan liquidation.

In 2016, no impairment loss was recognized on the RBIC (Meritus), as well as no credit impairments were taken on the Rural America Bonds. During 2015, a final net impairment loss was recognized due to a credit impairment taken on the RBIC totaling $40, while no credit impairments were taken on the Rural American Bonds. During 2014, a net impairment loss was recognized due to a credit impairment taken on the RBIC totaling $30 and a credit impairment taken on one Rural America Bond totaling $114. Refer to the *Mission Related Investments* and *Investment Securities* section of this Management's Discussion and Analysis.

Noninterest Expense

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

Noninterest Expense	For the Year Ended December 31, 2016	2015	2014	Percentage Increase/(Decrease) 2016/2015	2015/2014
	(dollars in thousands)				
Salaries and employee benefits	$ 7,348	$ 7,204	$ 7,426	2.00%	(2.99)%
Occupancy and equipment	498	486	507	2.47	(4.14)
Insurance Fund premiums	495	319	265	55.17	20.38
(Gains) losses on other property owned, net	232	221	1,779	4.98	(87.58)
Other operating expenses	2,218	2,222	2,213	(0.18)	0.41
Total noninterest expense	$ 10,791	$ 10,452	$ 12,190	3.24%	(14.26)

Noninterest expense increased $339 or 3.24 percent for December 31, 2016 as compared to the same period for 2015 and decreased $1,399 or 11.48 percent compared to December 31, 2014. Salaries and employee benefits increased in 2016, when compared with 2015, primarily due to corporate bonuses and merit increases, which were partially offset by a decrease in the retirement healthcare plan costs. Corporate bonuses were recognized for 2016, 2015, and 2014.

Occupancy and equipment increased 2.47 percent for the twelve months ended December 31, 2016, compared to the same period of 2015. This increase was attributed to an increase in furniture and equipment depreciation and land improvement deprecation expenses, which was partially offset by a reduction in furniture and equipment maintenance and cost of space maintenance expenses.

Insurance Fund premiums expense increased 55.17 percent for the twelve months ended December 31, 2016, compared to the same period of 2015. This was primarily due to an increase in the rates from prior year on accruing volume, along with an increase in loan volume.

The Association had a net loss on other property owned of $232. This was mainly due to writedowns and expenses.

Other operating expenses decreased by 0.18 percent for the twelve months ended December 31, 2016, which was consistant with the same period in 2015.

Income Taxes

The Association recorded a provision of $15 for income taxes for the year ended December 31, 2016, as compared to a benefit of $19 for income taxes for 2015, and a benefit of $4 for 2014. Refer to Note 2, *Summary of Significant Accounting Policies, Income Taxes*, of the Notes to the Consolidated Financial Statements, for more information concerning Association income taxes.

Key Results of Operations Comparisons

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

Key Results of Operations Comparisons	For the 12 Months Ended 12/31/16	12/31/15	12/31/14
Return on average assets	1.92%	1.85%	2.57%
Return on average members' equity	10.33%	9.24%	12.71%
Net interest income as a percentage of average earning assets	2.67%	2.74%	2.74%
Net (charge-offs) recoveries to average loans	(0.099)%	(0.063)%	0.021%

A key factor in the growth of net income for future years will be continued improvement in net interest and noninterest income. Our goal is to generate earnings sufficient to fund operations, adequately capitalize the Association, and achieve an adequate rate of return for our members. To meet this goal, the agricultural economy must continue the improvement shown in recent years and the Association must meet certain objectives. These objectives are to attract and maintain high quality loan volume priced at competitive rates and to manage credit risk in our entire portfolio, while efficiently meeting the credit needs of our members.

LIQUIDITY AND FUNDING SOURCES

Liquidity and Funding

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

Total notes payable to the Bank at December 31, 2016 was $386,383, as compared to $335,894 at December 31, 2015, and $309,286 at December 31, 2014. The increases of 15.03 percent and 24.93 for December 31 2015 and 2014, respectively, were mainly attributed to an increase in originated loan volume, which was partially offset by a decrease in investment securities. The average volume of outstanding notes payable to the Bank was $365,988, $322,678, and $304,646 for the years ended December 31, 2016, 2015, and 2014, respectively. Refer to Note 6, *Debt - Notes Payable to AgFirst Farm Credit Bank*, of the Notes to the Consolidated Financial Statements, for weighted average interest rates and maturities, and additional information concerning the Association's notes payable.

Liquidity management is the process whereby funds are made available to meet all financial commitments including the extension of credit, payment of operating expenses, and payment of debt obligations. The Association receives access to funds through its borrowing relationship with the Bank and from income generated by operations. The liquidity policy of the Association is to manage cash balances to maximize debt reduction and to increase loan volume. As borrower payments are received, they are applied to the Association's note payable to the Bank. The Association's participation in the Farmer Mac, investments, and other secondary market programs provides additional liquidity. Sufficient liquid funds have been available to meet all financial obligations. There are no known trends likely to result in a liquidity deficiency for the Association. The Association did not have any lines of credit from third party financial institutions as of December 31, 2016.

Funds Management

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

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

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

Relationship with the Bank

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

The Bank's ability to access capital of the Association is discussed in Note 4, *Investments - Investments in Other Farm Credit Institutions*, of the Notes to the Consolidated Financial Statements.

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

CAPITAL RESOURCES

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

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

Total members' equity at December 31, 2016 increased 4.84 percent to $84,518 from the December 31, 2015 total of $80,620. At December 31, 2015, total members' equity increased 2.85 percent from the December 31, 2014 total of $78,386. The increase from prior year was primarily attributed to an increase in retained earnings as well as capital stock and was partially offset by a decrease in accumulated other comprehensive income.

Total capital stock and participation certificates were $1,413 on December 31, 2016, compared to $1,352 on December 31, 2015, and $1,307 on December 31, 2014. The increase from prior year was attributed to an increase of $61 in capital stock and participation certificates. The increase in capital stock was a result of growth in originated loan volume.

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

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

	2016	2015	2014	Regulatory Minimum
Permanent capital ratio	19.42%	20.83%	21.11%	7.00%
Total surplus ratio	19.10%	20.45%	20.71%	7.00%
Core surplus ratio	16.46%	19.36%	18.38%	3.50%

The slight decrease in the Association's permanent capital and total surplus for December 31, 2016 is mainly due to the increase in loan volume, which was partially offset by the increase in retained earnings and a decrease in the ineligible Rural America bonds. There are no trends, commitments, contingencies, or events that are likely to affect the Association's ability to meet regulatory minimum capital standards and capital adequacy requirements.

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

PATRONAGE PROGRAM

Prior to the beginning of any fiscal year, the Association's Board of Directors, by adoption of a resolution, may establish a Patronage Allocation Program to distribute its available consolidated net earnings. This resolution provides for the application of net earnings in the manner described in the Association's Bylaws. This includes the setting aside of funds to increase surplus to meet minimum capital adequacy standards established by FCA Regulations, to increase surplus to meet Association capital adequacy standards to a level necessary to support competitive pricing at targeted earnings levels, and for reasonable reserves for necessary purposes of the Association. After excluding net earnings attributable to (a) the portion of loans participated to another institution, and (b) non-patronage participation loans purchased, remaining consolidated net earnings are eligible for allocation to borrowers. Refer to Note 7, *Members' Equity*, of the Notes to the Consolidated Financial Statements, for more information concerning the patronage distributions. The Association declared patronage distributions of $6,641 in 2016, $5,453 in 2015, and $8,049 in 2014.

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

The Association's mission is to provide financial services to agriculture and the rural community, which includes providing credit to Young*, Beginning** and Small*** farmers. Because of the unique needs of these individuals, and their importance to the future growth of the Association, the Association has established annual marketing goals to increase our market share of loans to YBS farmers. Specific marketing plans have been developed to target these groups, and resources have been designated to help ensure YBS borrowers have access to a stable source of credit. At quarter end, the Association was meeting all of its YBS goals.

The following table outlines the loan volume and number of YBS loans in the loan portfolio for the Association.

	As of December 31, 2016	
	Number of Loans	Amount of Loans
Young	326	$45,446
Beginning	544	79,253
Small	773	95,818

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

The 2012 USDA Ag census data has been used as a benchmark to measure penetration of the Association's marketing efforts. Slight differences between the Census and the Association's YBS information are as follows:

- The Census shows young farmers in a group up to age 34, whereas the Association's YBS information shows young farmers up to age 35.
- The Census shows years on present farm up to nine years, whereas the Association's YBS information shows 10 years or less for a beginning farmer.
- The Census data is based on number of farms, whereas the Association's YBS information is based on number of loans.

The 2012 census data indicated that within the Association's chartered territory (counties) there were 5,610 reported farmers of which by definition 458 or 8.16 percent were Young, 1,438 or 25.63 percent were Beginning, and 4,977 or 88.72 percent were Small. Comparatively, as of December 31, 2016, the demographics of the Association's agricultural portfolio (by definition) are as follows: 326 or 11.60 percent were Young, 544 or 19.36 percent were Beginning, and 773 or 27.51 percent were Small.

The Association is committed to the future success of young, beginning, and small farmers.

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

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

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

REGULATORY MATTERS

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

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

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

The following sets forth the new regulatory capital ratios:

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

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

On November 30, 2015, the FCA, along with four other federal agencies, published in the Federal Register a final rule to establish capital and margin requirements for covered swap entities as required by the Dodd-Frank Act. See below for further information regarding the Dodd-Frank Act. This rule is not expected to have a material impact for District institutions.

On July 25, 2014, the FCA published a proposed rule in the Federal Register to revise the requirements governing the eligibility of investments for System banks and associations. The public comment period ended on October 23, 2014. The

FCA expects to issue a final regulation in 2017. The proposed investment regulations are expected to have a minimal impact for District institutions. The stated objectives of the proposed rule are as follows:

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

FINANCIAL REGULATORY REFORM

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

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

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

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

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

RECENTLY ISSUED ACCOUNTING PRONOUNCEMENTS

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

Disclosure Required by Farm Credit Administration Regulations

Description of Business

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

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

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

Each LLC held by the Association as of December 31, 2016, along with the entity type, the state in which it was established, and the ownership percentage is listed below.

Name	Entity Type	State	Entity Purpose	Ownership
A1 Ledges Wilder, LLC	LLC	South Carolina	Manage Acquired Property	27.28%
A1 Sequatchie Point, LLC	LLC	South Carolina	Manage Acquired Property	27.28%
CBF Holdings, LLC	LLC	North Carolina	Manage Acquired Property	2.17%
MB BP Properties Joint Venture, LLC	LLC	Texas	Manage Acquired Property	9.26%
Pickens County Properties, LLC	LLC	South Carolina	Manage Acquired Property	27.25%

Description of Property

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

Location	Description	Form of Ownership
800 Woody Jones Boulevard Florence	Administrative/ Branch	Owned
1720 Mill Pond Road Conway	Branch	Owned

Legal Proceedings

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

Description of Capital Structure

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

Description of Liabilities

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

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

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

Senior Officers

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

Name and Title	Term of Office	Prior Experience & Other Business Interest
Kathy S. Heustess, *President and Chief Executive Officer*	11/3/2011 – present	Started career with ArborOne in 1989 as Controller. Served as Chief Financial Officer and assumed the role of Chief Operating Officer in 2008. In 2011, assumed the role of President. As of January 2012, assumed the role of Chief Executive Officer. Additionally, serves on a local university foundation board and on the Farm Credit Council Services board, compensation committee (chair).
Tammy G. Smith, *Chief Financial Officer and Treasurer*	1/1/2009 – present	Started career with ArborOne in 1991 as an accountant. Served as Controller and assumed the role of Chief Financial Officer in 2009 and Treasurer in 2010.
Richard O. Pitts, *Chief Lending Officer*	11/1/2008 – present	Started career with ArborOne in 2002 as a credit analyst. Served as Credit Manager and assumed the role of Chief Lending Officer in 2008.
Sarah H. Jackson, *Director of Human Resources and Corporate Secretary*	1/1/2016 – present	Started career with ArborOne in 2006 as a financial analyst. Also, served as a Senior Credit Analyst and Senior Human Resources Administrator / Corporate Secretary prior to assuming the role of Director of Human Resources in 2016.

The total amount of compensation earned by the CEO and the highest paid officers as a group during the years ended December 31, 2016, 2015, and 2014, is as follows:

		Annual					
Name of Individual or Number in Group	Year	Salary	Bonus	Deferred Comp.	Changes in Pension Value **(a)	Perq./-Other *	Total
Kathy S. Heustess	2016	$ 300,011	$ 143,800	$ 33,894	$ 404,344	$ 9,940	$ 891,989
Kathy S. Heustess	2015	$ 282,461	$ 110,139	$ 34,880	$ 230,240	$ 7,392	$ 665,112
Kathy S. Heustess	2014	$ 269,010	$ 174,850	$ 49,933	$ 590,498	$ 6,037	$ 1,090,328
6	2016	$ 750,471	$ 281,868	$ 48,147	$ 409,211	$ 19,986	$ 1,509,683
5	2015	$ 676,521	$ 200,472	$ 32,716	$ 224,670	$ 16,809	$ 1,151,188
5	2014	$ 662,568	$ 277,791	$ 47,050	$ 1,010,355	$ 11,415	$ 2,009,179

* *Amounts in the above table classified as Perquisites include group life insurance and automobile compensation.*

** *On February 4, 2015, the FCA Board approved the final rule, "Disclosure to Shareholders; Pension Benefit Disclosures." The rule amends FCA regulations to exclude employee compensation from being reported in the Summary Compensation Table if the employee would be considered a "highly compensated employee" solely because of payments related to or change(s) in value of the employee's qualified pension plan provided that the plan was available to all similarly situated employees on the same basis at the time the employee joined the plan. System banks and associations were required to comply with the rule for compensation reported in the table for the fiscal year ending 2015, and could implement the rule retroactively for the fiscal year ended 2014. The Association did not apply this rule retroactively.*

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

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

The Association participates in District and multi-District sponsored benefit plans. Change in pension value is considered a part of compensation. The Pension Benefits table below reflects number of years credited service, actuarial present value of accumulated benefits, along with any payments made during 2016.

Pension Benefits Table
As of December 31, 2016

Name of Individual or Number in Group	Year	Plan Name	Number of Years Credited Service	Actuarial Present Value of Accumulated Benefits	Payments During 2016
CEO:					
Kathy S. Heustess	2016	AgFirst Retirement Plan	28.67	$ 2,573,184	$ –
				$ 2,573,184	$ –
Senior Officers and Highly Compensated Employees:					
6 Officers, excluding the CEO	2016	AgFirst Retirement Plan	*14.20	$ 2,104,727	$ –
				$ 2,104,727	–

* *Represents the average years of credited service for the group*

In addition to a base salary, all employees are eligible for additional compensation utilizing incentive plans. Specified employees are eligible for individual incentive plans. The executive management is eligible for a long-term incentive plan.

The incentive plans are designed to maximize financial performance while improving the Association's financial position and shareholder wealth providing employees with a competitive total compensation package. The plans' criteria include a balance of credit and financial results. The board of directors reviews and approves all the plans and authorizes all incentive payouts. At the discretion of the board of directors, an incentive was paid to all eligible staff based on financial results in 2016.

No participation in any plan is allowed for persons terminating employment prior to the fiscal year end or persons having unsatisfactory performance evaluations or on probation without prior approval from the CEO. New employees receive a pro rata share. The plans are paid based on percentage of salary, and will be paid from the Association's earnings. Bonuses are shown on the financial statements as an expense in the year earned, which may be different than the year of payment.

The 2016 Association plan for all employees included four tiers based on job functionality and four percentage levels of payout based upon incremental income, with increments of one million dollars per level, in excess of budget which resulted in a cap on incentive paid as a percentage of salary. The 2016 plan has "on/off" switches on payout to include Credit Quality, Return on Assets, and Permanent Capital ratio requirements to align the plan with the Association's business plan objectives and focus.

The individual incentive plans are specifically for relationship managers, financial related services (FRS) managers, and credit analysts to reward based on level of accomplishments and provide variable pay to maintain competitive compensation practices in the financial services industry. The Relationship Managers Plan includes criteria for average daily balance of loan volume outstanding, spreads, fee income, gains/ (losses) on loans and other property owned, and delinquency rate. The FRS Managers Plan includes criteria for commissions collected and any loss/recovery on claims. The Credit Analyst Plan includes criteria for average daily balance of loan volume outstanding, spreads, fee income, gains/ (losses) on loans and other property owned, and credit administration of B's and C's by volume.

The long-term plan is based on long-range financial results achieved over a three-year period. The objective of the plan is to reward and retain key decision makers as well as establish long-range goals to protect the Association's viability. Long-term incentive awards are earned over a three year performance period. The 2016 plan is subject to forfeiture based upon the Association's performance during the two-year performance period immediately following the plan year. Specifically, the long-term award will be reduced by an amount equal to one-half of the original award for each subsequent year during the two-year performance period in which any one of the performance thresholds are not achieved.

Disclosure of information on the total compensation paid during 2016 to any senior officer, or to any other individual included in the total, is available to shareholders upon request.

Directors

The following chart details the year the director began serving on the board, the current term of expiration, and total cash compensation paid for 2016:

DIRECTOR	ORIGINAL YEAR OF ELECTION OR APPOINTMENT	CURRENT TERM EXPIRATION	TOTAL COMPENSATION PAID DURING 2016
James M. Ward, ***Chairman***	1998	2018	$42,000
William DuPree Atkinson, ***Vice-Chairman***	1999	2019	32,300
Harry B. Durant	1997	2022	28,000
John Lee Newman	2008	2020	31,200
J. Whit Player	2011	2017	29,500
Jimmy Poston	1994	2021	34,000
Harold C. Stowe	2003	2016	6,200
Thomas S. Welsh, Sr.	2016	2022*	11,600
Kelly O. Wiseman	2007	2019	35,600
			$250,400

*Thomas Welsh's term ended in August 2016 prior to the term expiration.

The following represents certain information regarding the directors of the Association, including their principal occupation and employment for the past five years. Committee assignments can change during the year; therefore, service rendered may not cover the full 12 months of 2016.

James M. Ward, Chairman of the Board, is a self-employed farmer and partner of Mickey Ward Farms. He served on the audit and compensation committees during 2016.

William DuPree Atkinson, Vice Chairman of the Board and Chairman of the Compensation Committee, is a self-employed farmer and owner of Atkinson Farms, LLC. He served on the board of Pee Dee Peanut, LLC (peanut purchasing) in which he is an officer and has part ownership interest. He served on the audit committee during 2016.

Harry B. DuRant, is a self-employed farmer and part owner of Double D Farms and Alcolu Peanut, LLC (peanut purchasing). He served on the compensation and credit committees during 2016.

John E. Lay, retired from AgFirst Farm Credit Bank in February 2016 as Vice President and Treasurer after approximately 34 years of service. He serves on the board of AgFirst Federal Credit Union (credit union) in which he is the Treasurer. His term will begin in February 2017.

John Lee Newman, Interim Chairman of the Credit Committee, is a self-employed farmer and owner of Lee Newman Farms, JLN Services, LLC (planting services), and A & L Farms (poultry). He served on the board of Sumter County Farm Bureau (insurance). He served on the governance committee during 2016.

J. Whit Player, is a self-employed farmer and owner of J. Whit Player Farm and Player's Stoney Run Farm. He is also a forestry technician with SC Forestry Commission. He served on the board of St. Charles Gin Co. (cotton ginning) in which he is an officer and has part ownership interest. He served on the board of the South Carolina Boll Weevil Eradication Program (agriculture), Pork Chop Welsh Scholarship Board (education), and the Carolina Cotton Growers Board (agriculture). He also served on the audit and governance committees during 2016.

Jimmy Poston, Chairman of the Governance Committee, is a self-employed farmer and part owner of Triple P Farms. He served on the board of Florence County Soil and Water Conservation District (agriculture), and the South Carolina Tobacco Grower Association (agriculture). He also served on the compensation and credit committees during 2016.

Harold C. Stowe, is an investment manager and part owner of Stowe-Monier Management, LLC. He is also part owner of Willow Oak Quarry, LLC (rock quarry), American Timberlands Company (land management), and Basic6, Inc. (computer application). He served on the boards of the following businesses: The Jackson Companies (campground, land development), SeaMist, Inc. (hotel), Smith Medical Clinic (free medical clinic), Baskerville Outreach, Inc. (low income housing), Canal Holdings, LLC (real estate holding), SCANA Corp. (utilities), Hollins Cancer Center (hospital), Wall School of Business at Coastal Carolina University (education), and Wall Fellows Board at Coastal Carolina University (education). He served as the Chairman of the Credit Committee until his term expired in April of 2016.

Thomas S. Welsh Sr., was a consultant and owner of Sea Oats Business, LLC. He worked with Farm Credit for 38 years and retired as Executive Vice President of AgFirst Farm Credit Bank in January of 2011. He was a member of the credit committee in April of 2016 and the Chairman of the Credit Committee from May until August of 2016.

Kelly O. Wiseman, Chairman of the Audit Committee, is a certified public accountant with approximately 15 years experience with a major accounting firm.

Subject to approval by the Board, the Association may allow directors honoraria of $1,000 for attendance at meetings or special assignments, except for the Chairman of the Board who receives $1,250. Directors are paid honoraria $500 for committee meetings and $600 if chairman of the committee. Outside directors are paid a $750 quarterly retainer. The directors are paid honoraria on a quarterly basis and includes a payment for each month within the quarter that does not have a scheduled board or special meeting as well. Total compensation paid to directors as a group was $250,400 for 2016. No director received more than $5,000 in non-cash compensation during the year.

The following chart details the number of meetings, other activities, and additional compensation paid for other activities (if applicable) for each director:

	Days Served			
Name of Director	**Regular Board Meetings**	**Other Official Activities***	**Committee Assignments****	**Comp. Paid for other Activities***
James M. Ward, ***Chairman***	5	30	Audit Committee and Compensation Committee	$ 27,000
William Dupree Atkinson, ***Vice-Chairman and Chairman of Compensation Committee***	5	25	Audit Committee, Chairman of Compensation Committee	20,300
Harry B. Durant	5	20	Credit Committee and Compensation Committee	16,000
John Lee Newman, ***Interim Chairman of the Credit Committee***	5	24	Credit Committee (January – August 2016), Interim Chairman of the Credit Committee (September – December 2016), and Governance Committee	19,200
J. Whit Player	4	22	Audit Committee and Governance Committee	17,500
Jimmy Poston, ***Chairman of Governance Committee***	5	28	Compensation Committee, Chairman of the Governance Committee, and member of the Credit Committee	22,000
Harold C. Stowe	2	2	Chairman of the Credit Committee (January – April 2016)	2,200
Thomas S. Welsh, Sr.	2	5	Credit Committee (April 2016) and Chairman of the Credit Committee (May – August 2016)	5,600
Kelly O. Wiseman, ***Chairman of Audit Committee***	5	23	Chairman of the Audit Committee	23,600
				$ 153,400

** Includes board committee meetings and other board activities other than regular board meetings.*
*** Assignments are for the full 12 months of 2016 unless otherwise noted.*

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

The aggregate amount of reimbursement for travel, subsistence and other related expenses for all directors as a group was $82,477 for 2016, $79,648 for 2015, and $80,950 for 2014.

Transactions with Senior Officers and Directors

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

Transactions Other Than Loans

There have been no transactions that occurred at any time during the year ended December 31, 2016, between the Association and senior officers or directors, their immediate family members or any organizations with which they are affiliated, which require reporting per FCA regulations. Some directors have transacted business with borrowers of the Association. These transactions were performed at market prices, at an arm's length, and in the normal course of business. There were no transactions with any senior officer or director related to the purchase or retirement of preferred stock of the Association for the year ended December 31, 2016.

Involvement in Certain Legal Proceedings

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

Relationship with Independent Certified Public Accountants

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

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

	2016
Independent Certified Public Accountant	
PricewaterhouseCoopers LLP	
Audit services	$ 65,720
Total	$ 65,720

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

Consolidated Financial Statements

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

Copies of the Association's Annual and Quarterly reports are available upon request free of charge by calling 1-800-741-7332, or writing Sarah Jackson, Corporate Secretary, ArborOne, ACA, P.O. Box 3699, Florence, SC 29502, or accessing the website, ***www.arborone.com***. The Association prepares an electronic version of the Annual Report which is available on the Association's website within 75 days after the end of the fiscal year and distributes the Annual Reports to shareholders within 90 days after the end of the fiscal year. The Association prepares an electronic version of the quarterly report within 40 days after the end of each fiscal quarter, except that no report need be prepared for the fiscal quarter that coincides with the end of the fiscal year of the institution.

Borrower Information Regulations

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

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

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

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

Shareholder Investment

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

Report of the Audit Committee

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

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

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

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

Kelly O. Wiseman

Kelly O. Wiseman
Chairman of the Audit Committee

Members of Audit Committee

William Dupree Atkinson
J. Whit Player
James M. Ward

March 13, 2017

pwc

Report of Independent Certified Public Accountants

To the Board of Directors and Members of
ArborOne, ACA

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

Management's Responsibility for the Consolidated Financial Statements

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

Certified Public Accountants' Responsibility

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

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

Opinion

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

PricewaterhouseCoopers LLP

March 13, 2017

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

Consolidated Balance Sheets

(dollars in thousands)	December 31, 2016	2015	2014
Assets			
Cash	**$ 12**	$ 2	$ 2
Investment securities:			
Held to maturity (fair value of $18,449, $22,466, and $30,313, respectively)	**18,489**	22,171	29,767
Loans	**447,150**	383,427	340,945
Allowance for loan losses	**(8,676)**	(7,379)	(4,904)
Net loans	**438,474**	376,048	336,041
Other investments	**—**	—	40
Accrued interest receivable	**6,692**	5,313	4,517
Investments in other Farm Credit institutions	**5,659**	9,316	10,497
Premises and equipment, net	**3,940**	3,972	3,933
Other property owned	**623**	1,553	3,807
Accounts receivable	**7,040**	7,428	9,796
Other assets	**2,749**	3,367	3,074
Total assets	**$ 483,678**	$429,170	$ 401,474
Liabilities			
Notes payable to AgFirst Farm Credit Bank	**$ 386,383**	$335,894	$ 309,286
Accrued interest payable	**868**	714	645
Patronage refunds payable	**2,896**	2,345	2,996
Accounts payable	**602**	466	312
Other liabilities	**8,411**	9,131	9,849
Total liabilities	**399,160**	348,550	323,088
Commitments and contingencies (Note 11)			
Members' Equity			
Protected borrower stock	**62**	62	78
Capital stock and participation certificates	**1,351**	1,290	1,229
Retained earnings			
Allocated	**54,690**	52,625	51,516
Unallocated	**28,196**	25,945	24,578
Accumulated other comprehensive income	**219**	698	985
Total members' equity	**84,518**	80,620	78,386
Total liabilities and members' equity	**$ 483,678**	$429,170	$ 401,474

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

Consolidated Statements of Income

(dollars in thousands)	For the year ended December 31, 2016	2015	2014
Interest Income			
Loans	**$ 19,454**	$ 17,022	$ 15,809
Investments	**1,779**	1,761	2,361
Total interest income	**21,233**	18,783	18,170
Interest Expense			
Notes payable to AgFirst Farm Credit Bank	**9,465**	8,100	8,211
Net interest income	**11,768**	10,683	9,959
Provision for (reversal of allowance for) loan losses	**1,711**	2,703	347
Net interest income after provision for (reversal of allowance for) loan losses	**10,057**	7,980	9,612
Noninterest Income			
Loan fees	**1,693**	1,793	1,909
Fees for financially related services	**979**	1,191	1,211
Patronage refunds from other Farm Credit institutions	**6,792**	7,043	9,279
Gains (losses) on sales of premises and equipment, net	**32**	61	—
Gains (losses) on sales of investment securities	**—**	—	96
Gains (losses) on other transactions	**26**	(1)	266
Total other-than-temporary impairment losses on investments	**—**	(40)	(90)
Portion of loss recognized in other comprehensive income (loss)	**—**	—	(54)
Net impairment losses on investments	**—**	(40)	(144)
Other noninterest income	**4**	6	21
Total noninterest income	**9,526**	10,053	12,638
Noninterest Expense			
Salaries and employee benefits	**7,348**	7,204	7,426
Occupancy and equipment	**498**	486	507
Insurance Fund premiums	**495**	319	265
(Gains) losses on other property owned, net	**232**	221	1,779
Other operating expenses	**2,218**	2,222	2,213
Total noninterest expense	**10,791**	10,452	12,190
Income before income taxes	**8,792**	7,581	10,060
Provision (benefit) for income taxes	**15**	(19)	(4)
Net income	**$ 8,777**	$ 7,600	$ 10,064

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

Consolidated Statements of Comprehensive Income

(dollars in thousands)	For the year ended December 31, 2016	2015	2014
Net income	**$ 8,777**	$ 7,600	$ 10,064
Other comprehensive income net of tax			
Unrealized gains (losses) on investments:			
Other-than-temporarily impaired	**6**	6	240
Not other-than-temporarily impaired	**(475)**	(324)	1,832
Employee benefit plans adjustments	**(10)**	31	(86)
Other comprehensive income (loss) (Note 7)	**(479)**	(287)	1,986
Comprehensive income	**$ 8,298**	$ 7,313	$ 12,050

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

Consolidated Statements of Changes in Members' Equity

(dollars in thousands)	Protected Borrower Stock	Capital Stock and Participation Certificates	Retained Earnings Allocated	Retained Earnings Unallocated	Accumulated Other Comprehensive Income (Loss)	Total Members' Equity
Balance at December 31, 2013	$ 91	$ 1,238	$ 49,893	$ 22,574	$ (1,001)	$ 72,795
Comprehensive income				10,064	1,986	12,050
Protected borrower stock issued/(retired), net	(13)					(13)
Capital stock/participation certificates issued/(retired), net		(9)				(9)
Patronage distribution						
Cash				(2,415)		(2,415)
Nonqualified allocated retained earnings			3,634	(3,634)		—
Nonqualified retained earnings			2,000	(2,000)		—
Retained earnings retired			(4,019)			(4,019)
Patronage distribution adjustment			8	(11)		(3)
Balance at December 31, 2014	$ 78	$ 1,229	$ 51,516	$ 24,578	$ 985	$ 78,386
Comprehensive income				7,600	(287)	7,313
Protected borrower stock issued/(retired), net	(16)					(16)
Capital stock/participation certificates issued/(retired), net		61				61
Patronage distribution						
Cash				(1,636)		(1,636)
Qualified allocated retained earnings			1,091	(1,091)		—
Nonqualified allocated retained earnings			2,726	(2,726)		—
Retained earnings retired			(3,852)			(3,852)
Patronage distribution adjustment			1,144	(780)		364
Balance at December 31, 2015	$ 62	$ 1,290	$ 52,625	$ 25,945	$ 698	$ 80,620
Comprehensive income				**8,777**	**(479)**	**8,298**
Capital stock/participation certificates issued/(retired), net		**61**				**61**
Patronage distribution						
Cash				**(1,992)**		**(1,992)**
Qualified allocated retained earnings			**332**	**(332)**		**—**
Nonqualified allocated retained earnings			**4,317**	**(4,317)**		**—**
Retained earnings retired			**(2,502)**			**(2,502)**
Patronage distribution adjustment			**(82)**	**115**		**33**
Balance at December 31, 2016	**$ 62**	**$ 1,351**	**$ 54,690**	**$ 28,196**	**$ 219**	**$ 84,518**

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

Consolidated Statements of Cash Flows

(dollars in thousands)	For the year ended December 31, 2016	2015	2014
Cash flows from operating activities:			
Net income	$ **8,777**	$ 7,600	$ 10,064
Adjustments to reconcile net income to net cash provided by (used in) operating activities:			
Depreciation on premises and equipment	**383**	339	343
Amortization (accretion) of net deferred loan costs (fees)	**(43)**	(32)	(17)
Premium amortization (discount accretion) on investments	**(510)**	(224)	(49)
Provision for (reversal of allowance for) loan losses	**1,711**	2,703	347
(Gains) losses on other property owned	**145**	77	1,591
Net impairment losses on investments	**—**	40	144
(Gains) losses on sales of investment securities	**—**	—	(96)
(Gains) losses on sales of premises and equipment, net	**(32)**	(61)	—
(Gains) losses on other transactions	**(26)**	1	(266)
Changes in operating assets and liabilities:			
(Increase) decrease in accrued interest receivable	**(1,379)**	(796)	(109)
(Increase) decrease in accounts receivable	**388**	2,368	1,131
(Increase) decrease in other assets	**618**	(293)	349
Increase (decrease) in accrued interest payable	**154**	69	(146)
Increase (decrease) in accounts payable	**136**	154	(148)
Increase (decrease) in other liabilities	**(704)**	(688)	2,198
Total adjustments	**841**	3,657	5,272
Net cash provided by (used in) operating activities	**9,618**	11,257	15,336
Cash flows from investing activities:			
Proceeds from maturities of or principal payments received on investment securities, held to maturity	**3,723**	7,502	3,292
Proceeds from sales/maturities of or principal payments received on investment securities, available for sale	**—**	—	10,213
Net (increase) decrease in loans	**(64,223)**	(42,853)	(34,990)
(Increase) decrease in investment in other Farm Credit institutions	**3,657**	1,181	1,898
Proceeds from payments received on other investments	**—**	—	23,444
Purchases of premises and equipment	**(355)**	(380)	(558)
Proceeds from sales of premises and equipment	**36**	63	—
Proceeds from sales of other property owned	**914**	2,352	1,231
Net cash provided by (used in) investing activities	**(56,248)**	(32,135)	4,530
Cash flows from financing activities:			
Advances on (repayment of) notes payable to AgFirst Farm Credit Bank, net	**50,489**	26,608	(12,611)
Protected borrower stock retired	**—**	(16)	(13)
Capital stock and participation certificates issued/(retired), net	**61**	61	(9)
Patronage refunds and dividends paid	**(1,408)**	(1,923)	(3,240)
Retained earnings retired	**(2,502)**	(3,852)	(4,019)
Net cash provided by (used in) financing activities	**46,640**	20,878	(19,892)
Net increase (decrease) in cash	**10**	—	(26)
Cash, beginning of period	**2**	2	28
Cash, end of period	$ **12**	$ 2	$ 2
Supplemental schedule of non-cash activities:			
Financed sales of other property owned	$ **6**	$ 659	$ 69
Receipt of property in settlement of loans	**135**	834	475
Estimated cash dividends or patronage distributions declared or payable	**1,992**	1,636	2,415
Investment securities transferred from held to maturity to available for sale	**—**	—	33,007
Change in unrealized gains (losses) on investments	**(469)**	(318)	2,072
Employee benefit plans adjustments (Note 9)	**10**	(31)	86
Supplemental information:			
Interest paid	**9,311**	8,031	8,357
Taxes (refunded) paid, net	**—**	—	5

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

Notes to the Consolidated Financial Statements

(dollars in thousands, except as noted)

Note 1 — Organization and Operations

A. **Organization:** ArborOne, ACA (Association) is a member-owned cooperative that provides credit and credit-related services to qualified borrowers. The territory of the Association extends across a diverse agricultural region of the following 12 counties in northeastern South Carolina: *Chesterfield, Clarendon, Darlington, Dillon, Florence, Georgetown, Horry, Lee, Marion, Marlboro, Sumter, and Williamsburg.*

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

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

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

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

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

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

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

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

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

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

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

Note 2 — Summary of Significant Accounting Policies

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

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

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

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

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

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

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

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

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

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

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

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

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

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

A specific allowance may be established for impaired loans under Financial Accounting Standards Board (FASB) guidance on accounting by creditors for impairment of a loan. Impairment of these loans is measured based on the present value of expected future cash flows discounted at the loan's effective interest rate or, as practically expedient, at the loan's observable market price or fair value of the collateral if the loan is collateral dependent.

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

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

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

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

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

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

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

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

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

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

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

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

At acquisition, and at each reporting date thereafter, the appropriateness of the classification of the Association's investment securities is reassessed. If an entity does not have the intent and ability to hold securities to maturity, their classification as HTM would not be appropriate. Likewise, if securities are reclassified from AFS in one period, judgment is required in determining when circumstances have changed such that management can assert with a greater degree of credibility that it now has the intent and ability to hold securities to maturity. These determinations are made by management on a case by case basis. The transfer of a security between categories of investments is accounted for at fair value.

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

Other Investments
As discussed in Note 8, certain investments, consisting primarily of mutual funds, are held in trust and investment accounts and are reported at fair value. Holding period gains and losses are included within other noninterest income on the Consolidated Statements of Income and the balance of these investments, totaling $499, is included in Other Assets on the accompanying Consolidated Balance Sheet as of December 31, 2016.

The Association holds minority equity interests in a Rural Business Investment Company (RBIC). This investment is accounted for under the cost method and is carried at the lower of cost or fair value.

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

Please see further discussion in Note 8.

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

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

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

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

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

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

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

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

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

In June, 2016, the FASB issued ASU 2016-13 Financial Instruments—Credit Losses (Topic 326): Measurement of Credit Losses on Financial Instruments. The Update improves financial reporting by requiring timelier recording of credit losses on financial instruments. It requires an organization to measure all expected credit losses for financial assets held at the reporting date. Financial institutions and other organizations will use forward-looking information to better estimate their credit losses. Many of the loss estimation techniques applied today will still be permitted, although the inputs to those techniques will change to reflect the full amount of expected credit losses. Organizations will continue to use judgment to determine which loss estimation method is appropriate for their circumstances. The ASU requires enhanced disclosures to help investors and other financial statement users better understand significant estimates and judgments used in estimating credit losses, as well as the credit quality and underwriting standards of an organization's portfolio. Additionally, the ASU amends the accounting for credit losses on available-for-sale debt securities and purchased financial assets with credit deterioration. The Update will take effect for U.S. Securities and Exchange Commission (SEC) filers for fiscal years, and interim periods within those fiscal years, beginning after December 15, 2019. For public business entities that are not SEC filers, it will take effect for fiscal years beginning after December 15, 2020, and interim periods within those fiscal years. For all other organizations, the ASU will take effect for fiscal years beginning after December 15, 2020, and for interim periods within fiscal years beginning after December 15, 2021. Early application will be permitted for all organizations for fiscal years, and interim periods within those fiscal years, beginning after December 15, 2018. The Association will apply the ASU guidance as a public business entity that is not a SEC filer. The Association is in the process of evaluating what effects the guidance may have on the statements of financial condition and results of operations.

In March, 2016, the FASB issued ASU 2016-07 Investments ¬ Equity Method and Joint Ventures (Topic 323): Simplifying the Transition to the Equity Method of Accounting. To simplify the accounting for equity method investments, the amendments in the Update eliminate the requirement that an entity retroactively adopt the equity method of accounting if an investment qualifies for use of the equity method as a result of an increase in the level of ownership or degree of influence. The amendments require that the equity method investor add the cost of acquiring the additional interest in the investee to the current basis of the investor's previously held interest and adopt the equity method of accounting as of the date the investment becomes qualified for equity method accounting. The guidance is effective for fiscal years, and interim periods within those fiscal years, beginning after December 15, 2016. Earlier application is permitted. The amendments should be applied prospectively upon their effective date to increases in the level of ownership interest or degree of influence that result in the adoption of the equity method. Application of this guidance is not expected to have a material impact on the Association's financial condition or results of operations.

In March, 2016, the FASB issued ASU 2016-06 Derivatives and Hedging (Topic 815): Contingent Put and Call Options in Debt Instruments. Topic 815 requires that embedded derivatives be separated from the host contract and accounted for separately as derivatives if certain criteria are met, including the "clearly and closely related" criterion. The amendments in this Update clarify the requirements for assessing whether contingent call (put) options that can accelerate the payment of principal on debt instruments are clearly and closely related to their debt hosts. An entity performing the assessment under the amendments is required to assess the embedded call (put) options solely in accordance with the four-step decision sequence. The amendments apply to all entities that are issuers of or investors in debt instruments (or hybrid financial instruments that are determined to have a debt host) with embedded call (put) options. For public business entities, the amendments are effective for financial statements issued for fiscal years beginning after December 15, 2016, and interim periods within those fiscal years. The amendments are to be applied on a modified retrospective basis to existing debt instruments as of the beginning of the fiscal year for which the amendments are effective. Early adoption is permitted, including adoption in an interim period. If an entity early adopts the amendments in an interim period, any adjustments should be reflected as of the beginning of the fiscal year that includes that interim period. Application of this guidance is not expected to have a material impact on the Association's financial condition or results of operations.

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

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

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

In May, 2015, the FASB issued ASU 2015-07, Fair Value Measurement (Topic 820): Disclosures for Investments in Certain Entities That Calculate Net Asset Value per Share (or Its Equivalent). Topic 820 permits a reporting entity, as a practical expedient, to measure the fair value of certain investments using the net asset value per share of the investment. Investments valued using the practical expedient were categorized within the fair value hierarchy on the basis of whether the investment was redeemable with the investee at net asset value on the measurement date, never redeemable with the investee at net asset value, or redeemable with the investee at net asset value at a future date. To address diversity in practice related to how certain investments measured at net asset value with future redemption dates were categorized, the amendments in this Update removed the requirement to categorize investments for which fair values are measured using the net asset value per share practical expedient. It also limited disclosures to investments for which the entity has elected to measure the fair value using the practical expedient. For public business entities, the guidance was effective for fiscal years beginning after December 15, 2015, and interim periods within those fiscal years. Adoption of this guidance was applied retrospectively to all periods presented and did not have an impact on the Association's financial condition or results of operations.

In February, 2015, the FASB issued ASU 2015-02, Consolidation (Topic 810): Amendments to the Consolidation Analysis. The amendments affect reporting entities that are required to evaluate whether they should consolidate certain legal entities. All legal entities are subject to reevaluation under the revised consolidation model. Specifically, the amendments modify the evaluation of whether limited partnerships and similar legal entities are VIEs or voting interest entities, eliminate the presumption that a general partner should consolidate a limited partnership, affect the consolidation analysis of reporting entities that are involved with VIEs, particularly those that have fee arrangements and related party relationships, and provide a scope exception from consolidation guidance for reporting entities with interests in legal entities that are required to comply with or operate in accordance with requirements that are similar to those in Rule 2a-7 of the Investment Company Act of 1940 for registered money market funds. The amendments in this Update were effective for public business entities for fiscal years, and for interim periods within those fiscal years, beginning after December 15, 2015. Adoption of this guidance was applied on a modified retrospective basis and did not have an impact on the Association's financial condition or results of operations.

In November, 2014, the FASB issued ASU 2014-16, Derivatives and Hedging (Topic 815): Determining Whether the Host Contract in a Hybrid Financial Instrument Issued in the Form of a Share Is More Akin to Debt or to Equity. Under GAAP, features such as conversion rights, redemption rights, dividend payment preferences, and others that are included in instruments issued in the form of shares may qualify as derivatives. If so, the shares issued are considered hybrid financial instruments. To determine the proper accounting for hybrid financial instruments, investors and issuers in the instruments must determine whether the nature of the host contract containing the feature is more akin to debt or equity as well as whether the economic characteristics and risks of the embedded derivative feature are clearly and closely related to the host contract. The purpose of the Update is to eliminate diversity in accounting for hybrid financial instruments by both issuers and investors. When evaluating the host contract to determine whether it is more akin to debt or equity, the reporting entity should consider all relevant terms and features of the contract, including the embedded derivative feature that is being evaluated for separation. The amendments in this Update were effective for public business entities for fiscal years, and interim periods within those fiscal years, beginning after December 15, 2015. Adoption of this guidance was applied on a modified retrospective basis and did not have a material impact on the Association's financial condition or results of operations.

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

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

Note 3 — Loans and Allowance for Loan Losses

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

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

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

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

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

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

- Production and intermediate-term loans — loans to full-time or part-time farmers that are not real estate mortgage loans. These loans fund eligible financing needs including operating inputs (such as labor, feed, fertilizer, and repairs), livestock, living expenses, income taxes, machinery or equipment, farm buildings, and other business-related expenses. Production loans may be made on a secured or unsecured basis and are most often made for a period of time that matches the borrower's normal production and marketing cycle, which is typically one year or less. Intermediate-term loans are made for a specific term, generally greater than one year and less than or equal to ten years.

- Loans to cooperatives — loans for any cooperative purpose other than for communication, power, and water and waste disposal.

- Processing and marketing loans — loans for operations to process or market the products produced by a farmer, rancher, or producer or harvester of aquatic products, or by a cooperative.

- Farm-related business loans — loans to eligible borrowers that furnish certain farm-related business services to farmers or ranchers that are directly related to their agricultural production.

- Rural residential real estate loans — loans made to individuals, who are not farmers, to purchase a single-family dwelling that will be the primary residence in open country, which may include a town or village that has a population of not more than 2,500 persons. In addition, the loan may be to remodel, improve, or repair a rural home, or to refinance existing debt. These loans are generally secured by a first lien on the property.

- Communication loans — loans primarily to finance rural communication providers.

- Power loans — loans primarily to finance electric generation, transmission and distribution systems serving rural areas.

- Water and waste disposal loans — loans primarily to finance water and waste disposal systems serving rural areas.

- International loans — primarily loans or credit enhancements to other banks to support the export of U.S. agricultural commodities or supplies. The federal government guarantees a substantial portion of these loans.

- Lease receivables — the net investment for all finance leases such as direct financing leases, leveraged leases, and sales-type leases.

- Other (including Mission Related) — additional investments in rural America approved by the FCA on a program or a case-by-case basis. Examples of such investments include partnerships with agricultural and rural community lenders, investments in rural economic development and infrastructure, and investments in obligations and mortgage securities that increase the availability of affordable housing in rural America.

A summary of loans follows:

	December 31,		
	2016	2015	2014
Real estate mortgage	$ 232,251	$ 187,971	$ 168,297
Production and intermediate-term	185,439	162,608	150,899
Loans to cooperatives	1,866	436	455
Processing and marketing	16,385	21,591	12,144
Farm-related business	4,599	3,929	4,066
Power and water/waste disposal	860	2,391	753
Rural residential real estate	4,784	4,371	4,181
International	856	–	–
Lease receivables	110	130	150
Total Loans	$ 447,150	$ 383,427	$ 340,945

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

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

The Association may purchase or sell participation interests with other parties in order to diversify risk, manage loan volume, and comply with FCA regulations. During 2016, the Association canceled its participation in the Capitalized Participation Pool program with the Bank. As a result, the Association repurchased $37,552 of participations previously sold to AgFirst. The following tables present the principal balance of participation loans at periods ended:

	December 31, 2016							
	Within AgFirst District		Within Farm Credit System		Outside Farm Credit System		Total	
	Participations Purchased	Participations Sold	Participations Purchased	Participations Sold	Participations Purchased	Participations Sold	Participations Purchased	Participations Sold
Real estate mortgage	$ 5,638	$ 15,270	$ –	$ –	$ –	$ –	$ 5,638	$ 15,270
Production and intermediate-term	19,784	4,244	–	–	–	–	19,784	4,244
Loans to cooperatives	1,453	–	–	–	–	–	1,453	–
Processing and marketing	8,626	7,875	–	–	–	–	8,626	7,875
Farm-related business	2,429	–	–	–	–	–	2,429	–
Power and water/waste disposal	867	–	–	–	–	–	867	–
Rural residential real estate	–	–	–	–	1,831	–	1,831	–
International	857	–	–	–	–	–	857	–
Total	$ 39,654	$ 27,389	$ –	$ –	$ 1,831	$ –	$ 41,485	$ 27,389

	December 31, 2015							
	Within AgFirst District		Within Farm Credit System		Outside Farm Credit System		Total	
	Participations Purchased	Participations Sold	Participations Purchased	Participations Sold	Participations Purchased	Participations Sold	Participations Purchased	Participations Sold
Real estate mortgage	$ 5,805	$ 44,839	$ –	$ –	$ –	$ –	$ 5,805	$ 44,839
Production and intermediate-term	21,613	15,357	–	–	–	–	21,613	15,357
Processing and marketing	14,836	1,529	–	–	–	–	14,836	1,529
Farm-related business	2,689	83	–	–	–	–	2,689	83
Power and water/waste disposal	1,647	–	–	–	–	–	1,647	–
Rural residential real estate	–	–	–	–	2,102	–	2,102	–
Total	$ 46,590	$ 61,808	$ –	$ –	$ 2,102	$ –	$ 48,692	$ 61,808

	December 31, 2014							
	Within AgFirst District		Within Farm Credit System		Outside Farm Credit System		Total	
	Participations Purchased	Participations Sold	Participations Purchased	Participations Sold	Participations Purchased	Participations Sold	Participations Purchased	Participations Sold
Real estate mortgage	$ 7,328	$ 57,433	$ 3,270	$ –	$ –	$ –	$ 10,598	$ 57,433
Production and intermediate-term	21,793	18,730	600	–	–	–	22,393	18,730
Loans to cooperatives	–	–	–	–	–	–	–	–
Processing and marketing	11,914	58	250	–	–	–	12,164	58
Farm-related business	1,602	93	–	–	–	–	1,602	93
Rural residential real estate	–	–	–	–	2,214	–	2,214	–
Total	$ 42,637	$ 76,314	$ 4,120	$ –	$ 2,214	$ –	$ 48,971	$ 76,314

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

	December 31, 2016			
	Due less than 1 year	Due 1 Through 5 years	Due after 5 years	Total
Real estate mortgage	$ 10,139	$ 31,323	$ 190,789	$ 232,251
Production and intermediate-term	72,542	71,257	41,640	185,439
Loans to cooperatives	–	152	1,714	1,866
Processing and marketing	29	9,851	6,505	16,385
Farm-related business	1,940	1,149	1,510	4,599
Power and water/waste disposal	–	–	860	860
Rural residential real estate	10	125	4,649	4,784
International	–	346	510	856
Lease receivables	–	110	–	110
Total Loans	$ 84,660	$ 114,313	$ 248,177	$ 447,150
Percentages	18.93%	25.57%	55.50%	100.00%

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

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

	December 31, 2016	2015	2014
Real estate mortgage:			
Acceptable	92.45%	92.65%	93.00%
OAEM	4.26	2.70	3.25
Substandard/doubtful/loss	3.29	4.65	3.75
	100.00%	100.00%	100.00%
Production and intermediate-term:			
Acceptable	87.68%	93.09%	93.01%
OAEM	10.78	4.91	2.88
Substandard/doubtful/loss	1.54	2.00	4.11
	100.00%	100.00%	100.00%
Loans to cooperatives:			
Acceptable	100.00%	100.00%	100.00%
OAEM	–	–	–
Substandard/doubtful/loss	–	–	–
	100.00%	100.00%	100.00%
Processing and marketing:			
Acceptable	100.00%	100.00%	86.79%
OAEM	–	–	–
Substandard/doubtful/loss	–	–	13.21
	100.00%	100.00%	100.00%
Farm-related business:			
Acceptable	96.99%	100.00%	100.00%
OAEM	3.01	–	–
Substandard/doubtful/loss	–	–	–
	100.00%	100.00%	100.00%
Power and water/waste disposal:			
Acceptable	100.00%	68.49%	–%
OAEM	–	–	–
Substandard/doubtful/loss	–	31.51	100.00
	100.00%	100.00%	100.00%
Rural residential real estate:			
Acceptable	99.26%	98.07%	97.05%
OAEM	–	–	–
Substandard/doubtful/loss	0.74	1.93	2.95
	100.00%	100.00%	100.00%
International:			
Acceptable	100.00%	–%	–%
OAEM	–	–	–
Substandard/doubtful/loss	–	–	–
	100.00%	–%	–%
Lease receivables:			
Acceptable	100.00%	100.00%	100.00%
OAEM	–	–	–
Substandard/doubtful/loss	–	–	–
	100.00%	100.00%	100.00%
Total Loans:			
Acceptable	90.92%	93.24%	92.72%
OAEM	6.72	3.41	2.88
Substandard/doubtful/loss	2.36	3.35	4.40
	100.00%	100.00%	100.00%

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

December 31, 2016	30 Through 89 Days Past Due	90 Days or More Past Due	Total Past Due	Not Past Due or Less Than 30 Days Past Due	Total Loans	Recorded Investment 90 Days or More Past Due and Accruing Interest
Real estate mortgage	$ 223	$ 3,604	$ 3,827	$ 231,682	$ 235,509	$ –
Production and intermediate-term	1,665	2,256	3,921	184,590	188,511	–
Loans to cooperatives	–	–	–	1,872	1,872	–
Processing and marketing	–	–	–	16,543	16,543	–
Farm-related business	–	–	–	4,617	4,617	–
Power and water/waste disposal	–	–	–	862	862	–
Rural residential real estate	–	–	–	4,817	4,817	–
International	–	–	–	857	857	–
Lease receivables	–	–	–	111	111	–
Total	$ 1,888	$ 5,860	$ 7,748	$ 445,951	$ 453,699	$ –

December 31, 2015	30 Through 89 Days Past Due	90 Days or More Past Due	Total Past Due	Not Past Due or Less Than 30 Days Past Due	Total Loans	Recorded Investment 90 Days or More Past Due and Accruing Interest
Real estate mortgage	$ 2,013	$ 3,187	$ 5,200	$ 185,223	$ 190,423	$ –
Production and intermediate-term	132	2,103	2,235	162,866	165,101	–
Loans to cooperatives	–	–	–	436	436	–
Processing and marketing	–	–	–	21,701	21,701	–
Farm-related business	–	–	–	3,953	3,953	–
Power and water/waste disposal	–	–	–	2,390	2,390	–
Rural residential real estate	–	–	–	4,405	4,405	–
Lease receivables	–	–	–	131	131	–
Total	$ 2,145	$ 5,290	$ 7,435	$ 381,105	$ 388,540	$ –

	December 31, 2014					
	30 Through 89 Days Past Due	90 Days or More Past Due	Total Past Due	Not Past Due or Less Than 30 Days Past Due	Total Loans	Recorded Investment 90 Days or More Past Due and Accruing Interest
Real estate mortgage	$ 1,176	$ 2,867	$ 4,043	$ 166,161	$ 170,204	$ –
Production and intermediate-term	916	777	1,693	151,418	153,111	–
Loans to cooperatives	–	–	–	457	457	–
Processing and marketing	–	–	–	12,165	12,165	–
Farm-related business	–	–	–	4,085	4,085	–
Power and water/waste disposal	779	–	779	–	779	–
Rural residential real estate	83	–	83	4,133	4,216	–
Lease receivables	–	–	–	151	151	–
Total	$ 2,954	$ 3,644	$ 6,598	$ 338,570	$ 345,168	$ –

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

	December 31,		
	2016	2015	2014
Nonaccrual loans:			
Real estate mortgage	$ 5,915	$ 6,003	$ 3,373
Production and intermediate-term	5,014	3,420	1,437
Rural residential real estate	–	46	83
Total	$ 10,929	$ 9,469	$ 4,893
Accruing restructured loans:			
Real estate mortgage	$ 7,346	$ 6,612	$ 5,438
Production and intermediate-term	1,975	634	1,200
Lease receivables	111	131	151
Total	$ 9,432	$ 7,377	$ 6,789
Accruing loans 90 days or more past due:			
Total	$ –	$ –	$ –
Total nonperforming loans	$ 20,361	$ 16,846	$ 11,682
Other property owned	623	1,553	3,807
Total nonperforming assets	$ 20,984	$ 18,399	$ 15,489
Nonaccrual loans as a percentage of total loans	2.44%	2.47%	1.44%
Nonperforming assets as a percentage of total loans and other property owned	4.69%	4.78%	4.49%
Nonperforming assets as a percentage of capital	24.83%	22.82%	19.76%

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

	December 31,		
	2016	2015	2014
Impaired nonaccrual loans:			
Current as to principal and interest	$ 4,022	$ 3,206	$ 1,064
Past due	6,907	6,263	3,829
Total	10,929	9,469	4,893
Impaired accrual loans:			
Restructured	9,432	7,377	6,789
90 days or more past due	–	–	–
Total	9,432	7,377	6,789
Total impaired loans	$ 20,361	$ 16,846	$ 11,682
Additional commitments to lend	$ 10	$ 7	$ –

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

	December 31, 2016			Year Ended December 31, 2016	
Impaired Loans	Recorded Investment	Unpaid Principal Balance	Related Allowance	Average Impaired Loans	Interest Income Recognized on Impaired Loans
With a related allowance for credit losses:					
Real estate mortgage	$ 3,506	$ 3,488	$ 335	$ 3,311	$ 119
Production and intermediate-term	1,428	1,474	138	1,349	48
Lease receivables	111	111	113	105	4
Total	$ 5,045	$ 5,073	$ 586	$ 4,765	$ 171
With no related allowance for credit losses:					
Real estate mortgage	$ 9,755	$ 10,603	$ –	$ 9,214	$ 330
Production and intermediate-term	5,561	6,348	–	5,251	189
Rural residential real estate	–	29	–	–	–
Total	$ 15,316	$ 16,980	$ –	$ 14,465	$ 519
Total:					
Real estate mortgage	$ 13,261	$ 14,091	$ 335	$ 12,525	$ 449
Production and intermediate-term	6,989	7,822	138	6,600	237
Rural residential real estate	–	29	–	–	–
Lease receivables	111	111	113	105	4
Total	$ 20,361	$ 22,053	$ 586	$ 19,230	$ 690

	December 31, 2015			Year Ended December 31, 2015	
Impaired Loans	Recorded Investment	Unpaid Principal Balance	Related Allowance	Average Impaired Loans	Interest Income Recognized on Impaired Loans
With a related allowance for credit losses:					
Real estate mortgage	$ 4,240	$ 4,213	$ 435	$ 3,719	$ 138
Production and intermediate-term	1,707	1,692	143	1,496	56
Lease receivables	131	131	117	115	4
Total	$ 6,078	$ 6,036	$ 695	5,330	198
With no related allowance for credit losses:					
Real estate mortgage	$ 8,375	$ 8,738	$ –	$ 7,342	$ 273
Production and intermediate-term	2,347	3,441	–	2,059	76
Rural residential real estate	46	107	–	40	2
Total	$ 10,768	$ 12,286	$ –	9,441	351
Total:					
Real estate mortgage	$ 12,615	$ 12,951	$ 435	$ 11,061	$ 411
Production and intermediate-term	4,054	5,133	143	3,555	132
Rural residential real estate	46	107	–	40	2
Lease receivables	131	131	117	115	4
Total	$ 16,846	$ 18,322	$ 695	14,771	549

	December 31, 2014			Year Ended December 31, 2014	
Impaired Loans	Recorded Investment	Unpaid Principal Balance	Related Allowance	Average Impaired Loans	Interest Income Recognized on Impaired Loans
With a related allowance for credit losses:					
Real estate mortgage	$ 5,278	$ 5,228	$ 502	$ 4,717	$ 228
Production and intermediate-term	305	320	123	273	13
Lease receivables	151	150	113	135	6
Total	$ 5,734	$ 5,698	$ 738	$ 5,125	$ 247
With no related allowance for credit losses:					
Real estate mortgage	$ 3,533	$ 3,767	$ –	$ 3,157	$ 152
Production and intermediate-term	2,332	3,134	–	2,084	101
Rural residential real estate	83	153	–	74	4
Total	$ 5,948	$ 7,054	$ –	$ 5,315	$ 257
Total:					
Real estate mortgage	$ 8,811	$ 8,995	$ 502	$ 7,874	$ 380
Production and intermediate-term	2,637	3,454	123	2,357	114
Rural residential real estate	83	153	–	74	4
Lease receivables	151	150	113	135	6
Total	$ 11,682	$ 12,752	$ 738	$ 10,440	$ 504

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

	Year Ended December 31, 2016	2015	2014
Interest income which would have been recognized under the original loan terms	$ 1,312	$ 1,017	$ 821
Less: interest income recognized	690	549	504
Foregone interest income	$ 622	$ 468	$ 317

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

	Real Estate Mortgage	Production and Intermediate-term	Agribusiness*	Power and Water/Waste Disposal	Rural Residential Real Estate	International	Lease Receivables	Total
Activity related to the allowance for credit losses:								
Balance at December 31, 2015	$ 1,811	$ 4,872	$ 293	$ 277	$ 9	$ –	$ 117	$ 7,379
Charge-offs	(300)	(342)	–	–	–	–	–	(642)
Recoveries	70	158	–	–	–	–	–	228
Provision for loan losses	242	1,722	4	(269)	9	7	(4)	1,711
Balance at December 31, 2016	$ 1,823	$ 6,410	$ 297	$ 8	$ 18	$ 7	$ 113	$ 8,676
Balance at December 31, 2014	$ 1,360	$ 2,314	$ 809	$ 301	$ 7	$ –	$ 113	$ 4,904
Charge-offs	(268)	(188)	–	–	–	–	–	(456)
Recoveries	125	103	–	–	–	–	–	228
Provision for loan losses	594	2,643	(516)	(24)	2	–	4	2,703
Balance at December 31, 2015	$ 1,811	$ 4,872	$ 293	$ 277	$ 9	$ –	$ 117	$ 7,379
Balance at December 31, 2013	$ 1,884	$ 1,900	$ 286	$ 302	$ 3	$ –	$ 114	$ 4,489
Charge-offs	(70)	–	–	–	–	–	–	(70)
Recoveries	130	8	–	–	–	–	–	138
Provision for loan losses	(584)	406	523	(1)	4	–	(1)	347
Balance at December 31, 2014	$ 1,360	$ 2,314	$ 809	$ 301	$ 7	$ –	$ 113	$ 4,904
Allowance on loans evaluated for impairment:								
Individually	$ 335	$ 138	$ –	$ –	$ –	$ –	$ 113	$ 586
Collectively	1,488	6,272	297	8	18	7	–	8,090
Balance at December 31, 2016	$ 1,823	$ 6,410	$ 297	$ 8	$ 18	$ 7	$ 113	$ 8,676
Individually	$ 435	$ 143	$ –	$ –	$ –	$ –	$ 117	$ 695
Collectively	1,376	4,729	293	277	9	–	–	6,684
Balance at December 31, 2015	$ 1,811	$ 4,872	$ 293	$ 277	$ 9	$ –	$ 117	$ 7,379
Individually	$ 502	$ 123	$ –	$ –	$ –	$ –	$ 113	$ 738
Collectively	858	2,191	809	301	7	–	–	4,166
Balance at December 31, 2014	$ 1,360	$ 2,314	$ 809	$ 301	$ 7	$ –	$ 113	$ 4,904
Recorded investment in loans evaluated for impairment:								
Individually	$ 13,261	$ 6,989	$ –	$ –	$ –	$ –	$ 111	$ 20,361
Collectively	222,248	181,522	23,032	862	4,817	857	–	433,338
Balance at December 31, 2016	$ 235,509	$ 188,511	$ 23,032	$ 862	$ 4,817	$ 857	$ 111	$ 453,699
Individually	$ 12,615	$ 4,348	$ –	$ –	$ 46	$ –	$ 131	$ 17,140
Collectively	177,808	160,753	26,090	2,390	4,359	–	–	371,400
Balance at December 31, 2015	$ 190,423	$ 165,101	$ 26,090	$ 2,390	$ 4,405	$ –	$ 131	$ 388,540
Individually	$ 8,811	$ 2,638	$ –	$ –	$ 82	$ –	$ 151	$ 11,682
Collectively	161,393	150,473	16,707	779	4,134	–	–	333,486
Balance at December 31, 2014	$ 170,204	$ 153,111	$ 16,707	$ 779	$ 4,216	$ –	$ 151	$ 345,168

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

To mitigate risk of loan losses, the Association may enter into guarantee arrangements with certain GSEs, including the Federal Agricultural Mortgage Corporation (Farmer Mac), and state or federal agencies. These guarantees generally remain in place until the loans are paid in full or expire and give the Association the right to be reimbursed for losses incurred or to sell designated loans to the guarantor in the event of default (typically four months past due), subject to certain conditions. The guaranteed balance of designated loans under these agreements was $75,743, $73,173, and $68,693 at December 31, 2016, 2015, and 2014, respectively. Fees paid for such guarantee commitments totaled $1, $2, and $2 for 2016, 2015, and 2014, respectively. These amounts are classified as noninterest expense.

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

	Year Ended December 31, 2016				
Outstanding Recorded Investment	**Interest Concessions**	**Principal Concessions**	**Other Concessions**	**Total**	**Charge-offs**
Pre-modification:					
Real estate mortgage	$ –	$ 1,480	$ 252	$ 1,732	
Production and intermediate-term	–	1,846	–	1,846	
Total	$ –	$ 3,326	$ 252	$ 3,578	
Post-modification:					
Real estate mortgage	$ –	$ 1,553	$ 253	$ 1,806	$ –
Production and intermediate-term	–	1,860	–	1,860	–
Total	$ –	$ 3,413	$ 253	$ 3,666	$ –

	Year Ended December 31, 2015				
Outstanding Recorded Investment	**Interest Concessions**	**Principal Concessions**	**Other Concessions**	**Total**	**Charge-offs**
Pre-modification:					
Real estate mortgage	$ –	$ 843	$ –	$ 843	
Production and intermediate-term	–	947	–	947	
Total	$ –	$ 1,790	$ –	$ 1,790	
Post-modification:					
Real estate mortgage	$ –	$ 1,392	$ –	$ 1,392	$ –
Production and intermediate-term	–	961	–	961	(52)
Total	$ –	$ 2,353	$ –	$ 2,353	$ (52)

	Year Ended December 31, 2014				
Outstanding Recorded Investment	**Interest Concessions**	**Principal Concessions**	**Other Concessions**	**Total**	**Charge-offs**
Pre-modification:					
Real estate mortgage	$ 114	$ 1,789	$ –	$ 1,903	
Production and intermediate-term	885	1,605	–	2,490	
Total	$ 999	$ 3,394	$ –	$ 4,393	
Post-modification:					
Real estate mortgage	$ 114	$ 1,789	$ –	$ 1,903	$ –
Production and intermediate-term	885	1,390	–	2,275	–
Total	$ 999	$ 3,179	$ –	$ 4,178	$ –

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

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

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

	Total TDRs			**Nonaccrual TDRs**		
	December 31,			**December 31,**		
	2016	**2015**	**2014**	**2016**	**2015**	**2014**
Real estate mortgage	$ 8,162	$ 6,612	$ 5,584	$ 816	$ –	$ 146
Production and intermediate-term	2,811	2,249	2,121	836	1,615	921
Lease receivables	111	131	151	–	–	–
Total Loans	$ 11,084	$ 8,992	$ 7,856	$ 1,652	$ 1,615	$ 1,067
Additional commitments to lend	$ –	$ –	$ –			

The following table presents information as of period end:

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

Note 4 — Investments

Investment Securities

The Association's investments consist primarily of Rural America Bonds (RABs), which are private placement securities purchased under the Mission Related Investment program approved by the FCA. In its Conditions of Approval for the program, the FCA considers a RAB ineligible if its investment rating, based on the internal 14-point risk rating scale used to also grade loans, falls below 9 and requires System institutions to provide notification to FCA when a security becomes ineligible. At December 31, 2016, the Association held two RABs whose credit quality has deteriorated beyond the program limits.

A summary of the amortized cost and fair value of HTM investment securities follows:

	December 31, 2016				
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value	Yield
RABs (a)	$ 18,489	$ 434	$ (474)	$ 18,449	5.87%

	December 31, 2015				
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value	Yield
RABs (b)	$ 22,171	$ 569	$ (274)	$ 22,466	6.09%

	December 31, 2014				
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value	Yield
RABs (c)	$ 29,767	$ 547	$ (1)	$ 30,313	6.03 %

(a) Gross unrealized losses include non-credit related other-than-temporary impairment recognized in AOCI of $95.
(b) Gross unrealized losses include non-credit related other-than-temporary impairment recognized in AOCI of $101.
(c) Gross unrealized losses include non-credit related other-than-temporary impairment recognized in AOCI of $107.

On October 1, 2014, the Association transferred its AFS investments to a HTM classification. The following table summarizes the transaction:

AFS Investments Reclassified to HTM	Amortized Cost	Fair Value	Unrealized Gains/(Losses) Recognized in OCI
RABs	$31,818	$33,007	$1,189

Because there had been no significant sales of AFS securities for an extended period of time, and current management has the firm intent and ability to hold those securities to maturity, the Association judged that a HTM classification more closely reflects the way in which it expects to benefit from the cash flows from those assets.

For a debt security transferred into the HTM category, the use of fair value may create a premium or discount that, under amortized cost accounting, shall be amortized or accreted thereafter as an adjustment of yield. The investments were transferred to HTM at fair value with an unrealized net gain (premiums and discounts) recognized in OCI in the amount of $1,189. These OCI amounts will be amortized or accreted to interest income ratably over the remaining life of each individual security in accordance with GAAP. The amortization of an unrealized holding gain or loss reported in OCI will offset or mitigate the effect on interest income of the amortization of any premium or discount recorded on transfer to HTM for each security.

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

	December 31, 2016		
	Amortized Cost	Fair Value	Weighted Average Yield
In one year or less	$ 888	$ 889	5.00%
After one year through five years	–	–	–
After five years through ten years	–	–	–
After ten years	17,601	17,560	5.92
Total	$ 18,489	$ 18,449	5.87%

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

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

	December 31, 2016			
	Less than 12 Months		12 Months or Greater	
	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
RABs	$ 941	$ (30)	$ 3,027	$ (444)

	December 31, 2015			
	Less than 12 Months		12 Months or Greater	
	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
RABs	$ 10,831	$ (237)	$ 348	$ (37)

	December 31, 2014			
	Less than 12 Months		12 Months or Greater	
	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
RABs	$ 389	$ (1)	$ –	$ –

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

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

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

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

Based on the results of all analyses, the Association has recognized credit-related other-than-temporary impairment of $0, $0, and $114 for 2016, 2015, and 2014, respectively, which is included in Impairment Losses on Investments in the Statements of Income. During 2016, a partial accretion to interest income of previously recognized credit impairment of $510 was recorded compared to $223 for 2015 and none for 2014. Since the Association does not intend to sell these other-than-temporarily impaired debt securities and is not more likely than not to be required to sell before recovery, the total other-than temporary impairment is reflected in the Statements of Income with: (1) a net other-than-temporary impairment amount related to estimated credit loss, and (2) an amount relating to all other factors, recognized as a reclassification to or from Other Comprehensive Income.

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

The following schedule details the activity related to cumulative credit losses on investments recognized in earnings:

	For the Year Ended December 31,		
	2016	2015	2014
Amount related to credit loss-beginning balance	$ 2,534	$ 2,757	$ 3,049
Additions for initial credit impairments	–	–	–
Additions for subsequent credit impairments	–	–	114
Reductions for increases in expected cash flows	(510)	(223)	–
Reductions for securities sold, settled, or matured	–	–	(406)
Amount related to credit loss-ending balance	2,024	2,534	2,757
Life to date incurred credit losses	–	–	–
Remaining unrealized credit losses	$ 2,024	$ 2,534	$ 2,757

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

The Association's investment in the Bank totaled $4,844 for 2016, $8,432 for 2015 and $9,591 for 2014. The Association owns 1.91 percent of the issued stock of the Bank as of December 31, 2016 net of any reciprocal investment. As of that date, the Bank's assets totaled $32.1 billion and shareholders' equity totaled $2.2 billion. The Bank's earnings were $342 million for 2016. In addition, the Association had an investment of $815 related to other Farm Credit institutions at December 31, 2016.

Other Investments
In 2006, the Association agreed to become one of several investors in a USDA approved Rural Business Investment Company (RBIC). This investment was made under the USDA's Rural Business Investment Program, which is authorized by the Farm Security and Rural Investment Act (FSRIA). It permits USDA to license RBICs and provide guarantees and grants to promote rural economic development and job opportunities and meet equity capital investment needs of small rural enterprises. FSRIA authorizes FCS institutions to establish and invest in RBICs, provided that such investments are not greater than 5 percent of the capital and surplus of the FCS institution.

Over the years, the Association purchased total equity investments in the RBIC of $250. There are no outstanding commitments to make additional equity purchases beyond this amount. Beginning in 2013, analyses indicated that decreases in value of the investment had occurred that were other than temporary, due to a series of losses and other factors. As a result, the Association recognized other-than-temporary impairment of $0, $40, and $30 for the years ended December 31, 2016, 2015, and 2014 respectively, which is included in Impairment Losses on Investments in the Statements of Income. As of December 31, 2016, there were no holdings of RBIC investments.

Note 5 — Real Estate and Other Property

Premises and Equipment
Premises and equipment consists of the following:

	December 31, 2016	2015	2014
Land	$ 1,189	$ 1,189	$ 1,075
Buildings and improvements	2,828	2,824	2,815
Furniture and equipment	1,895	1,819	1,703
	5,912	5,832	5,593
Less: accumulated depreciation	1,972	1,860	1,660
Total	$ 3,940	$ 3,972	$ 3,933

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

	December 31, 2016	2015	2014
(Gains) losses on sale, net	$ (1)	$ –	$ 1
Carrying value unrealized (gains) losses	146	77	1,590
Operating (income) expense, net	87	144	188
(Gains) losses on other property owned, net	$ 232	$ 221	$ 1,779

Gains on sales of other property owned were deferred if the sales involved financing from the Association and did not meet the criteria for immediate recognition. There were no deferred gains at December 31, 2016, 2015, and 2014.

Note 6 — Debt

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

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

The weighted average interest rates on the variable rate advances were 1.87 percent for LIBOR-based loans and 1.98 percent for Prime-based loans, and the weighted average remaining maturities were 3.3 years and 1.1 years, respectively, at December 31, 2016. The weighted-average interest rate on the fixed rate and adjustable rate mortgage (ARM) loans which are match funded by the Bank was 2.85 percent, and the weighted average remaining maturity was 9.4 years at December 31, 2016. The weighted-average interest rate on all interest-bearing notes payable was 2.59 percent and the weighted-average remaining maturity was 7.6 years at December 31, 2016. Variable rate and fixed rate notes payable represent approximately 9.95 percent and 90.05 percent, respectively, of total notes payable at December 31, 2016. The weighted average maturities described above are related to matched-funded loans. The direct note itself has an annual maturity as prescribed in the GFA.

Note 7 — Members' Equity

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

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

B. **Capital Stock and Participation Certificates:** In accordance with the Farm Credit Act and the Association's capitalization bylaws, each borrower is required to invest in Class C stock for agricultural loans, or participation certificates in the case of rural home and farm related business loans, as a condition of borrowing. The initial borrower investment, through either purchase or transfer, must be in an amount equal to the lesser of $1 thousand or 2 percent of the amount of the loan. The Board of Directors may increase the amount of investment if necessary to meet the Association's capital needs. Loans designated for sale or sold into the Secondary Market on or after April 16, 1996 will have no voting stock or participation certificate purchase requirement if sold within 180 days following the date of designation.

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

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

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

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

	2016	2015	2014	Regulatory Minimum
Permanent capital ratio	19.42%	20.83%	21.11%	7.00%
Total surplus ratio	19.10%	20.45%	20.71%	7.00%
Core surplus ratio	16.46%	19.36%	18.38%	3.50%

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

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

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

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

		Shares Outstanding	
Class	Protected	Number	Aggregate Par Value
A Common/Nonvoting	Yes	11,924	$ 60
B Common/Nonvoting	Yes	501	2
C Common/Voting	No	256,793	1,284
B Participation Certificates/Nonvoting	Yes	18	–
C Participation Certificates/Nonvoting	No	13,352	67
Total Capital Stock and Participation Certificates		282,588	$ 1,413

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

   Retained Earnings

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

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

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

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

At December 31, 2016, allocated members' equity consisted of $7,486 of qualified surplus, $35,103 of nonqualified allocated surplus, and $12,101 of nonqualified retained surplus.

Dividends

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

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

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

Patronage Distributions

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

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

Transfer

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

Impairment

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

1. Class C Common Stock and Class C Participation Certificates
2. Classes A and B Common Stock and Class B Participation Certificates
3. Classes A and D Preferred Stock

Liquidation

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

1. Holders of Classes A and D Preferred Stock
2. Holders of Classes A and B Common Stock and Class B Participation Certificates
3. Holders of Class C Common Stock and Class C Participation Certificates
4. Holders of allocated surplus evidenced by qualified written notices of allocation, in the order of year of issuance and pro rata by year of issuance, until the total amount of such allocated surplus has been distributed
5. Holders of allocated surplus evidenced by nonqualified written notices of allocation, in the order of year of issuance and pro rata by year of issuance, until the total amount of such allocated surplus has been distributed
6. Any remaining assets of the Association after such distributions shall be distributed to past and present patrons on a patronage basis, to the extent practicable.

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

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

	For the years ended December 31,		
	2016	**2015**	**2014**
Unrealized Gains (Losses) on Investments:			
Balance at beginning of period	$ 922	$ 1,240	$ (832)
Other comprehensive income before reclassifications	–	–	2,003
Amounts reclassified from AOCI	(469)	(318)	69
Net current period OCI	(469)	(318)	2,072
Balance at end of period	453	922	1,240
Employee Benefit Plans:			
Balance at beginning of period	(224)	(255)	(169)
Other comprehensive income before reclassifications	(17)	23	(91)
Amounts reclassified from AOCI	7	8	5
Net current period OCI	(10)	31	(86)
Balance at end of period	(234)	(224)	(255)
Accumulated Other Comprehensive Income:			
Balance at beginning of period	698	985	(1,001)
Other comprehensive income before reclassifications	(17)	23	1,912
Amounts reclassified from AOCI	(462)	(310)	74
Net current period OCI	(479)	(287)	1,986
	$ 219	$ 698	$ 985

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

	2016	**2015**	**2014**	**Income Statement Line Item**
Investment Securities:				
Sales gains and losses	$ –	$ –	$ 96	Gains (losses) on investments, net
Holding gains and losses	–	–	(114)	Net other-than-temporary impairment
Amortization	469	318	(51)	Interest income on investments
Amounts reclassified	469	318	(69)	
Defined Benefit Pension Plans:				
Periodic pension costs	(7)	(8)	(5)	See Note 9.
Amounts reclassified	(7)	(8)	(5)	
Total reclassifications for the period	$ 462	$ 310	$ (74)	

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

Note 8 — Fair Value Measurement

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

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

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

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

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

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

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

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

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

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

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

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

The fair value of investment securities is estimated by discounting expected future cash flows using prevailing rates for similar instruments at the measurement date.

There are no observable market values for the Association's RBIC investments. Management must estimate the fair value based on an assessment of the operating performance of the company and available capital to operate the venture. This analysis requires significant judgment and actual sales values could differ materially from those estimated.

The Association had no transfers of assets or liabilities measured on a recurring basis into or out of Level 1 or Level 2 during the reporting periods presented. For Level 3 assets and liabilities measured at fair value on a recurring basis, the tables below present a reconciliation from the opening balances to the closing balances, and any transfers into or out of Level 3. Due to the transfer of investment securities from AFS to HTM on October 1, 2014, there were no Level 3 assets measured at fair value on a recurring basis during 2016 and 2015.

	Mission Related Investments		
	For the years ended December 31,		
	2016	2015	2014
Beginning balance	$ –	$ –	$ 41,286
Gains (losses) included in earnings	–	–	(18)
Gains (losses) included in OCI	–	–	2,030
Purchases	–	–	–
Sales	–	–	(4,886)
Settlements	–	–	(5,405)
Transfer to held to maturity (See Note 4)	–	–	(33,007)
Transfers in and/or out of Level 3	–	–	–
Ending balance	$ –	$ –	$ –

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

	At or for the Year ended December 31, 2016					
	Total Carrying Amount	Level 1	Level 2	Level 3	Total Fair Value	Fair Value Effects On Earnings
Recurring Measurements						
Assets:						
Assets held in Trust funds	$ 499	$ 499	$ –	$ –	$ 499	
Recurring Assets	$ 499	$ 499	$ –	$ –	$ 499	
Liabilities:						
Recurring Liabilities	$ –	$ –	$ –	$ –	$ –	
Nonrecurring Measurements						
Assets:						
Impaired loans	$ 19,775	$ –	$ –	$ 19,775	$ 19,775	$ (305)
Other property owned	623	–	–	718	718	(145)
Nonrecurring Assets	$ 20,398	$ –	$ –	$ 20,493	$ 20,493	$ (450)
Other Financial Instruments						
Assets:						
Cash	$ 12	$ 12	$ –	$ –	$ 12	
Investment securities, held-to-maturity	18,489	–	–	18,449	18,449	
Loans	418,699	–	–	412,865	412,865	
Other Financial Assets	$ 437,200	$ 12	$ –	$ 431,314	$ 431,326	
Liabilities:						
Notes payable to AgFirst Farm Credit Bank	$ 386,383	$ –	$ –	$ 383,443	$ 383,443	
Other Financial Liabilities	$ 386,383	$ –	$ –	$ 383,443	$ 383,443	

	At or for the Year ended December 31, 2015					
	Total Carrying Amount	Level 1	Level 2	Level 3	Total Fair Value	Fair Value Effects On Earnings
Recurring Measurements						
Assets:						
Assets held in Trust funds	$ 506	$ 506	$ –	$ –	$ 506	
Recurring Assets	$ 506	$ 506	$ –	$ –	$ 506	
Liabilities:						
Recurring Liabilities	$ –	$ –	$ –	$ –	$ –	
Nonrecurring Measurements						
Assets:						
Impaired loans	$ 16,151	$ –	$ –	$ 16,151	$ 16,151	$ (184)
Other property owned	1,553	–	–	1,700	1,700	(77)
Other investments	–	–	–	–	–	(40)
Nonrecurring Assets	$ 17,704	$ –	$ –	$ 17,851	$ 17,851	$ (301)
Other Financial Instruments						
Assets:						
Cash	$ 2	$ 2	$ –	$ –	$ 2	
Investment securities, held-to-maturity	22,171	–	–	22,466	22,466	
Loans	359,897	–	–	360,853	360,853	
Other Financial Assets	$ 382,070	$ 2	$ –	$ 383,319	$ 383,321	
Liabilities:						
Notes payable to AgFirst Farm Credit Bank	$ 335,894	$ –	$ –	$ 336,063	$ 336,063	
Other Financial Liabilities	$ 335,894	$ –	$ –	$ 336,063	$ 336,063	

	At or for the Year ended December 31, 2014					
	Total Carrying Amount	Level 1	Level 2	Level 3	Total Fair Value	Fair Value Effects On Earnings
Recurring Measurements						
Assets:						
Assets held in Trust funds	$ 532	$ 532	$ –	$ –	$ 532	
Recurring Assets	$ 532	$ 532	$ –	$ –	$ 532	
Liabilities:						
Recurring Liabilities	$ –	$ –	$ –	$ –	$ –	
Nonrecurring Measurements						
Assets:						
Impaired loans	$ 10,944	$ –	$ –	$ 10,944	$ 10,944	$ (2)
Other property owned	3,807	–	–	4,149	4,149	(1,591)
Other investments	40	–	–	40	40	(30)
Nonrecurring Assets	$ 14,791	$ –	$ –	$ 15,133	$ 15,133	$ (1,623)
Other Financial Instruments						
Assets:						
Cash	$ 2	$ 2	$ –	$ –	$ 2	
Investment securities, held-to-maturity	29,767	–	–	30,313	30,313	
Loans	325,097	–	–	323,977	323,977	
Other Financial Assets	$ 354,866	$ 2	$ –	$ 354,290	$ 354,292	
Liabilities:						
Notes payable to AgFirst Farm Credit Bank	$ 309,286	$ –	$ –	$ 307,802	$ 307,802	
Other Financial Liabilities	$ 309,286	$ –	$ –	$ 307,802	$ 307,802	

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

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

INVESTMENT SECURITIES

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

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

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

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

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

Quantitative Information about Recurring and Nonrecurring Level 3 Fair Value Measurements

	Fair Value	Valuation Technique(s)	Unobservable Input	Range
Impaired loans and other property owned	$ 20,493	Appraisal	Income and expense	*
			Comparable sales	*
			Replacement costs	*
			Comparability adjustments	*
Other investments-RBIC	$ –	Third party evaluation	Income, expense, capital	Not applicable

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

Information about Other Financial Instrument Fair Value Measurements

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

Note 9 — Employee Benefit Plans

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

1. Assets contributed to multiemployer plans by one employer may be used to provide benefits to employees of other participating employers.
2. If a participating employer stops contributing to the plan, the unfunded obligations of the plan may be borne by the remaining participating employers.
3. If the Association chooses to stop participating in some of its multiemployer plans, the Association may be required to contribute to eliminate the underfunded status of the plan.

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

1. The CB Plan was closed to new participants effective as of December 31, 2014. Based on the plan's eligibility provisions, this change affected employees hired on or after November 4, 2014.
2. Employer contributions were discontinued effective as of January 1, 2015.
3. All participants who were not already fully vested in the CB Plan became fully vested as of December 31, 2014.
4. The CB Plan was terminated effective as of December 31, 2015.

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

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

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

The Association's participation in the multiemployer defined benefit plans for the annual periods ended December 31, 2016, 2015 and 2014 is outlined in the table below. The "Percentage Funded to Projected Benefit Obligation" or "Percentage Funded to Accumulated Postretirement Benefit Obligation" represents the funded amount for the entire plan and the "Contributions" and "Percentage of Total Contributions" columns represent the Association's respective amounts.

Pension Plan	Percentage Funded to Projected Benefit Obligation			Contributions			Percentage of Total Contributions		
	2016	2015	2014	2016	2015	2014	2016	2015	2014
AgFirst Farm Credit Retirement Plan	86.96%	85.73%	84.56%	$734	$1,657	$1,018	2.58%	2.87%	2.68%
AgFirst Farm Credit Cash Balance Retirement Plan	100.21%	102.72%	100.07%	$–	$–	$135	0.00%	0.00%	2.72%

Other Postretirement Benefit Plan	Percentage Funded to Accumulated Postretirement Benefit Obligation			Contributions			Percentage of Total Contribution		
	2016	2015	2014	2016	2015	2014	2016	2015	2014
Farm Credit Benefits Alliance Retiree and Disabled Medical and Dental Plans	0.00%	0.00%	0.00%	$187	$181	$191	2.61%	2.66%	2.47%

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

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

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

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

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

Substantially all employees of the Association hired before November 4, 2014 are eligible to participate in either the FAP Plan or the CB Plan. These two plans are noncontributory and include eligible Association and other District employees. For participants hired prior to January 1, 2003, benefits are provided under the FAP Plan and are based on eligible compensation and years of service. For participants hired on or after January 1, 2003 through November 3, 2014, benefits are provided under the CB Plan and are determined using a percent of eligible compensation formula. Prior to January 1, 2015, when employer contributions were discontinued as discussed above, the employer contribution into the CB Plan was based on a formula of 3.00-5.00 percent of eligible compensation (depending on years of service) and interest credits as allocated to an employee's theoretical account balance. The actuarially-determined costs of these plans are allocated to each participating entity, including the Association, by multiplying the plans' net pension expense by each institution's eligible service cost and accumulated benefit obligation as a percentage of the total eligible service cost and total accumulated benefit obligation for all plan participants. Plan expenses included in employee benefit costs were $1,364 for 2016, $1,338 for 2015, and $1,481 for 2014. The cumulative excess of amounts funded by the Association over the cost allocated to the Association is reflected as prepaid retirement expense, a component of Other Assets in the Consolidated Balance Sheets.

In addition to providing pension benefits, the Association provides certain medical and dental benefits for eligible retired employees through the OPEB Plan. Substantially all of the Association employees may become eligible for the benefits if they reach early retirement age while working for the Association. Early retirement age is defined as a minimum of age 55 and 10 years of service. Employees hired after December 31, 2002, and employees who separate from service between age 50 and age 55, are required to pay the full cost of their retiree health insurance coverage. Employees who retire subsequent to December 1, 2007 are no longer provided retiree life insurance benefits. Certain Association charges related to this plan are an allocation of District charges based on the Association's proportional share of the plan liability. This plan is unfunded with expenses paid as incurred. Postretirement benefits other than pensions included in employee benefit costs were $247 for 2016, $318 for 2015, and $188 for 2014. The cumulative excess of cost allocated to the Association over the amounts funded by the Association is reflected as postretirement benefits other than pensions, a component of Other Liabilities in the Association's Consolidated Balance Sheets.

The Association also participates in a defined contribution Farm Credit Benefits Alliance (FCBA) 401(k) Plan (401(k) Plan), which qualifies as a 401(k) plan as defined by the Internal Revenue Code. For employees hired on or prior to December 31, 2002, the Association contributes $0.50 for each $1.00 of the employee's first 6.00 percent of contribution (based on total compensation) up to the maximum employer contribution of 3.00 percent of total compensation. For employees hired on or after January 1, 2003, the Association contributes $1.00 for each $1.00 of the employee's first 6.00 percent of contribution up to the maximum employer contribution of 6.00 percent of total compensation. Employee deferrals are not to exceed the maximum deferral as determined and adjusted by the Internal Revenue Service. The 401(k) Plan costs are expensed as funded. Employer contributions to this plan included in salaries and employee benefit costs were $282, $259, and $200 for the years ended December 31, 2016, 2015, and 2014, respectively. Beginning in 2015, contributions include additional amounts related to the discontinuation of the CB Plan as discussed above.

FASB guidance further requires the determination of the fair value of plan assets and recognition of actuarial gains and losses, prior service costs or credits, and transition assets or obligations as a component of AOCI. Under the guidance, these amounts are subsequently recognized as components of net periodic benefit costs over time. For 2016, 2015, and 2014,

$(10), $31 and $(86) has been recognized as a net debit, net credit and net debit to AOCI to reflect these elements.

In addition to the multi-employer plans described above, the Association sponsors nonqualified supplemental retirement and 401(k) plans. The supplemental retirement plan is unfunded and had a projected benefit obligation of $663 and a net under-funded status of $663 at December 31, 2016. Assumptions used to determine the projected benefit obligation as of December 31, 2016 included a discount rate of 4.35 percent. The expenses of these nonqualified plans included in employee benefit costs were $37, $39, and $36 for 2016, 2015, and 2014, respectively.

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

Note 10 — Related Party Transactions

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

Total loans to such persons at December 31, 2016 amounted to $9,703. During 2016, $3,451 of new loans and advances were made and repayments totaled $2,264. In the opinion of management, none of these loans outstanding at December 31, 2016 involved more than a normal risk of collectibility.

Note 11 — Commitments and Contingencies

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

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

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

Since many of these commitments are expected to expire without being drawn upon, the total commitments do not necessarily represent future cash requirements. However, these credit-related financial instruments have off-balance-sheet credit risk because their amounts are not reflected on the Consolidated Balance Sheets until funded or drawn upon. The credit risk associated with issuing commitments and letters of credit is substantially the same as that involved in extending loans to borrowers and management applies the same credit policies to these commitments. Upon fully funding a commitment, the credit risk amounts are equal to the contract amounts, assuming that borrowers fail completely to meet their obligations and the collateral or other security is of no value. The amount of collateral obtained, if deemed necessary upon extension of credit, is based on management's credit evaluation of the borrower. At December 31, 2016, $90,938 of commitments to extend credit and no commercial letters of credit were outstanding. There was no reserve for unfunded commitments included in Other Liabilities on the Consolidated Balance Sheets at December 31, 2016.

The Association also participates in standby letters of credit to satisfy the financing needs of its borrowers. These letters of credit are irrevocable agreements to guarantee payments of specified financial obligations. At December 31, 2016, standby letters of credit outstanding totaled $548 with expiration dates ranging from January 1, 2017 to May 9, 2019. The maximum potential amount of future payments that may be required under these guarantees was $548.

Note 12 — Income Taxes

The provision (benefit) for income taxes follows:

	Year Ended December 31,		
	2016	2015	2014
Current:			
Federal	$ 15	$ (20)	$ (3)
State	–	1	(1)
	15	(19)	(4)
Deferred:			
Federal	–	–	–
State	–	–	–
	–	–	–
Total provision (benefit) for income taxes	$ 15	$ (19)	$ (4)

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

	December 31,		
	2016	2015	2014
Federal tax at statutory rate	$ 3,077	$ 2,653	$ 3,521
State tax, net	(2)	(3)	1
Patronage distributions	(814)	(954)	(845)
Tax-exempt FLCA earnings	(2,604)	(2,552)	(3,287)
Change in valuation allowance	352	898	676
Change due to graduated rate on nonpat income	10	10	(4)
Other	(4)	(71)	(66)
Provision (benefit) for income taxes	$ 15	$ (19)	$ (4)

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

	December 31,		
	2016	2015	2014
Deferred income tax assets:			
Allowance for loan losses	$ 2,520	$ 2,260	$ 1,019
Nonaccrual loan interest	406	317	226
Other property owned writedown	–	–	434
Loan origination fees	3	–	–
Gross deferred tax assets	2,929	2,577	1,679
Less: valuation allowance	(2,929)	(2,577)	(1,679)
Gross deferred tax assets, net of valuation allowance	–	–	–
Deferred income tax liabilities:	–	–	–
Net deferred tax asset (liability)	$ –	$ –	$ –

At December 31, 2016, deferred income taxes have not been provided by the Association on approximately $50 of patronage refunds received from the Bank prior to January 1, 1993. Such refunds, distributed in the form of stock, are subject to tax only upon conversion to cash. The tax liability related to future conversions is not expected to be material.

The Association recorded a valuation allowance of $2,929, $2,577 and $1,679 as of December 31, 2016, 2015 and 2014, respectively. The Association will continue to evaluate the realizability of these deferred tax assets and adjust the valuation allowance accordingly.

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

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

Note 13 — Additional Financial Information

Quarterly Financial Information (Unaudited)

	2016				
	First	Second	Third	Fourth	Total
Net interest income	$ 2,712	$ 2,863	$ 3,018	$ 3,175	$ 11,768
Provision for (reversal of allowance for) loan losses	57	206	403	1,045	1,711
Noninterest income (expense), net	(938)	(547)	(891)	1,096	(1,280)
Net income	$ 1,717	$ 2,110	$ 1,724	$ 3,226	$ 8,777

	2015				
	First	Second	Third	Fourth	Total
Net interest income	$ 2,415	$ 2,602	$ 2,793	$ 2,873	$ 10,683
Provision for (reversal of allowance for) loan losses	603	289	161	1,650	2,703
Noninterest income (expense), net	(1,000)	(194)	(124)	938	(380)
Net income	$ 812	$ 2,119	$ 2,508	$ 2,161	$ 7,600

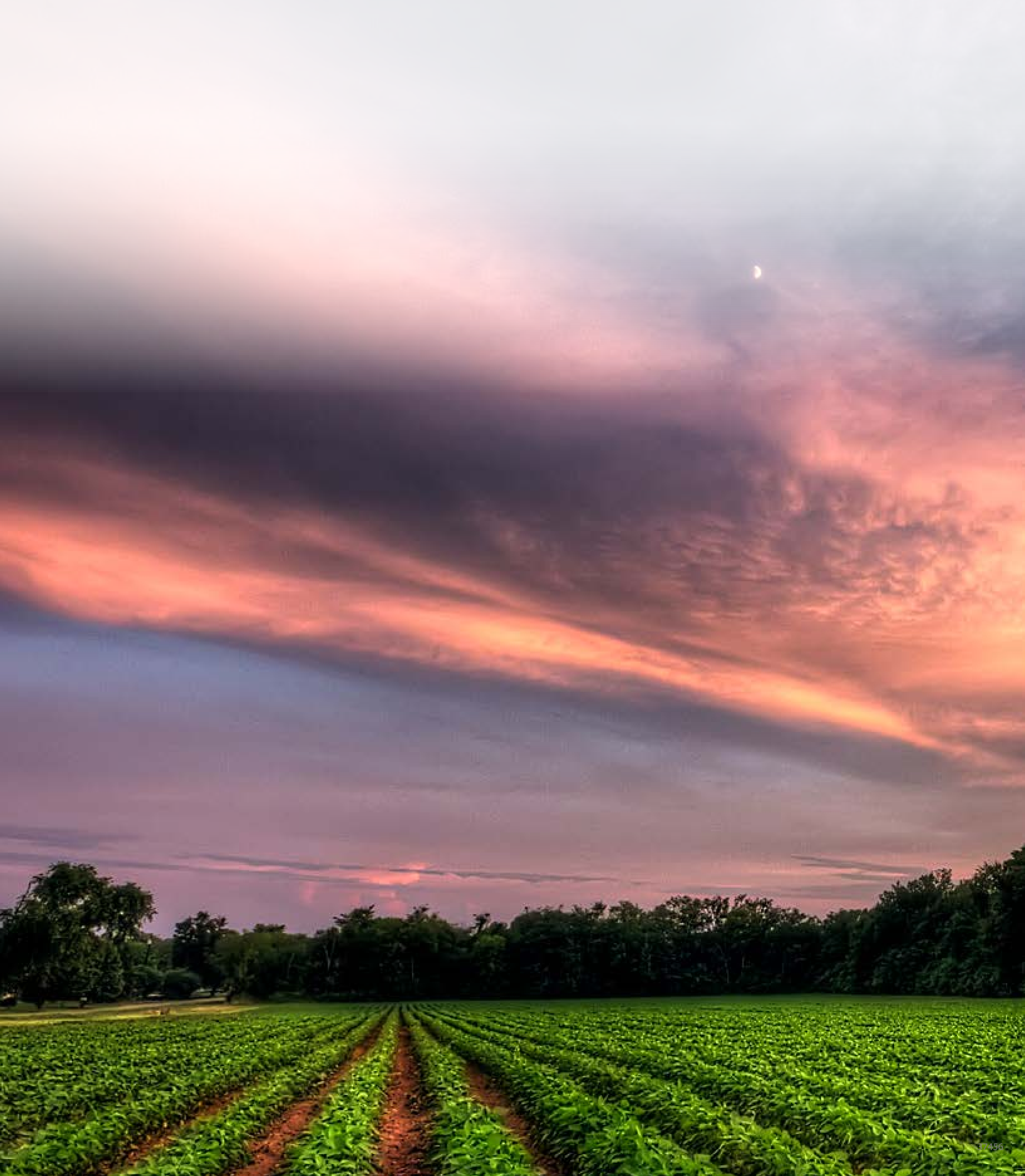
	2014				
	First	Second	Third	Fourth	Total
Net interest income	$ 2,448	$ 2,506	$ 2,183	$ 2,822	$ 9,959
Provision for (reversal of allowance for) loan losses	(139)	260	607	(381)	347
Noninterest income (expense), net	(199)	(486)	(412)	1,549	452
Net income	$ 2,388	$ 1,760	$ 1,164	$ 4,752	$ 10,064

Note 14 — Subsequent Events

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

ArborOne
FARM CREDIT

800 Woody Jones Boulevard • Florence, SC 29501



37456